

# MAKING RECORDS

CALIFORNIA WATER SERVICE GROUP  
2017 10-K AND PROXY STATEMENT







**California Water Service Group**  
**California Water Service Company, Hawaii Water Service Company,**  
**New Mexico Water Service Company, Washington Water Service**  
**Company, CWS Utility Services, and HWS Utility Services**

**1720 North First Street**  
**San Jose, CA 95112-4598**  
**(408) 367-8200**

April 18, 2018

**Dear Fellow Stockholder:**

You are cordially invited to attend our Annual Meeting of Stockholders at 9:30 a.m. on May 30, 2018, at the executive offices of California Water Service Group, located at 1720 North First Street in San Jose, California.

Enclosed are a notice of matters to be voted on at the meeting, our Proxy Statement, a proxy card, and our 2017 Annual Report.

Whether or not you plan to attend, your vote is important. Please vote your shares, as soon as possible, in one of three ways: by Internet, by telephone, or by mail. Instructions regarding Internet and telephone voting are included on the proxy card or voting instruction card. If you choose to vote by mail, please follow the instructions on the proxy card or voting instruction card.

In a continuing effort to conserve natural resources and reduce costs, we produced a summary annual report again this year, opting not to duplicate the financial information that continues to be provided in our Form 10-K filed with the Securities and Exchange Commission. Your perspectives on the annual report are valuable to us. Please send your feedback to [annualreport@calwater.com](mailto:annualreport@calwater.com).

Thank you for your investment in the California Water Service Group.

Sincerely,

/s/ PETER C. NELSON

**Peter C. Nelson**  
Chairman of the Board

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For directions to the Annual Meeting, please refer to page 64 of this Proxy Statement.

# California Water Service Group

## Notice of Annual Meeting of Stockholders

The 2018 Annual Meeting of Stockholders (Annual Meeting) of California Water Service Group (Group) will be held on Wednesday, May 30, 2018, at 9:30 a.m., at the executive offices of California Water Service Group, located at 1720 North First Street in San Jose, California. At the meeting, stockholders will consider and vote on the following matters:

1. Election of the nine directors named in the Proxy Statement;
2. An advisory vote to approve executive compensation;
3. Ratification of the selection of Deloitte & Touche LLP as the Group's independent registered public accounting firm for 2018;
4. Approval of the Group's 2018 Employee Stock Purchase Plan; and
5. Such other business as may properly come before the meeting.

The Board of Directors has fixed the close of business on April 3, 2018 as the record date for the determination of holders of common stock entitled to notice of, and to vote at, the Annual Meeting.

Please submit a proxy as soon as possible so that your shares can be voted at the meeting in accordance with your instructions. You may submit your proxy: (a) by Internet, (b) by telephone, or (c) by U.S. Postal Service mail. You may revoke your proxy at any time prior to the vote at the Annual Meeting. Of course, in lieu of submitting a proxy, you may vote in person at the Annual Meeting; provided, however, that if you hold your shares in street name, you must request a legal proxy from your stockbroker in order to do so. For specific instructions, please refer to "Questions and Answers about the Proxy Materials and the Annual Meeting" in this Proxy Statement and the instructions on the proxy card.

**Important Notice Regarding the Availability of Proxy Materials for the Stockholders Meeting to be Held on May 30, 2018:** Electronic copies of the Group's Form 10-K, including exhibits, and this Proxy Statement will be available at [www.proxyvote.com](http://www.proxyvote.com).

### By Order of the Board of Directors

/s/ MICHELLE R. MORTENSEN

**MICHELLE R. MORTENSEN**  
Corporate Secretary



## PROXY STATEMENT

This Proxy Statement, dated April 18, 2018, relates to the solicitation of proxies by the Board of Directors of California Water Service Group (Group) for use at our 2018 Annual Meeting of Stockholders, which is scheduled to be held on May 30, 2018. We expect to begin mailing this Proxy Statement to stockholders on or about April 18, 2018.

### QUESTIONS AND ANSWERS ABOUT THE PROXY MATERIALS AND THE ANNUAL MEETING

#### What am I voting on?

- Election of the nine directors named in the Proxy Statement to serve until the 2019 Annual Meeting;
- An advisory vote to approve executive compensation;
- Ratification of the selection of Deloitte & Touche LLP as the Group's independent registered public accounting firm for 2018; and
- Approval of the Group's 2018 Employee Stock Purchase Plan.

#### Who may attend the Annual Meeting?

Any stockholders of the Group may attend.

#### Who is entitled to vote?

Stockholders of record on the record date are entitled to vote. The Board has fixed the close of business on April 3, 2018 as the record date (Record Date) for the determination of stockholders entitled to notice of, and to vote at, the Annual Meeting.

#### How many votes do I get?

Each share of common stock is entitled to one vote.

#### What constitutes a quorum?

A majority of the outstanding shares – present at the Annual Meeting or represented by persons holding valid proxies – constitutes a quorum. If you submit a valid proxy card, your shares will be considered in determining whether a quorum is present.

Without a quorum, no business may be transacted at the Annual Meeting. However, whether or not a quorum exists, a majority of the voting power of those present at the Annual Meeting may adjourn the Annual Meeting to another date, time, and place.

At the Record Date, there were 1,934 stockholders of record. There were 48,073,847 shares of our common stock outstanding and entitled to vote at the Annual Meeting.

## **How are the directors elected?**

Our bylaws provide for a majority voting standard for the election of directors in uncontested elections. Under this majority voting standard, each director must be elected by the affirmative vote of a majority of the votes cast with respect to the director. A majority of the votes cast means that the number of votes cast "FOR" a nominee for director exceeds the number of votes cast "AGAINST" that nominee for director. As a result, abstentions will not be counted in determining which nominees receive a majority of votes cast since abstentions do not represent votes cast for or against a nominee. If you hold your shares through a stockbroker (or other nominee), the stockbroker does not have authority to vote your shares in the election of directors without instructions from you. Shares that your stockbroker does not vote ("broker non-votes") are not considered votes cast for or against a nominee, and they will not be counted in determining which nominees receive a majority of votes cast. In accordance with our director resignation policy, the Nominating/Corporate Governance Committee has established procedures that require an incumbent nominee for director who does not receive the required votes for re-election to tender his or her resignation offer to the Nominating/Corporate Governance Committee. The Nominating/Corporate Governance Committee will recommend to the Board whether to accept or reject the offer, or whether other action should be taken. The Board will act on the Nominating/Corporate Governance Committee's recommendation within 90 days after certification of the election results. We will promptly publicly disclose the Board's decision regarding the resignation offer, including the rationale for rejecting the resignation offer, if applicable.

## **Who are the Board's nominees?**

The nominees are Gregory E. Aliff, Terry P. Bayer, Edwin A. Guiles, Martin A. Kropelnicki, Thomas M. Krummel, M.D., Richard P. Magnuson, Peter C. Nelson, Carol M. Pottenger, and Lester A. Snow. All of the nominees are current Board members. See "Proposal No. 1 – Election of Directors" for biographical information and qualifications. George A. Vera is retiring from the Board as of the Annual Meeting and will not stand for re-election in accordance with the Board's retirement policy.

## **What are the Board's voting recommendations?**

"FOR" each of the nominees to the Board (Proposal No. 1);

"FOR" the proposal regarding an advisory vote to approve executive compensation (Proposal No. 2);

"FOR" the ratification of the selection of Deloitte & Touche LLP as the Group's independent registered public accounting firm for 2018 (Proposal No. 3); and

"FOR" the approval of the Group's 2018 Employee Stock Purchase Plan (Proposal No. 4).

## **How do I vote?**

If you are a stockholder of record (that is, you hold your shares in your own name), you may vote on the Internet, by telephone, by mail, or in person at the meeting. Different rules apply if your stockbroker or another nominee holds your shares for you (see below).



### ***You may vote on the Internet.***

You do this by following the "Vote by Internet" instructions on the proxy card. If you vote by Internet, you do not have to mail in your proxy card.

 **You may vote by telephone.**

You do this by following the “Vote by Phone” instructions on the proxy card. If you vote by telephone, you do not have to mail in your proxy card. You must have a touch-tone phone to vote by telephone.

 **You may vote by mail.**

You do this by signing the proxy card and mailing it in the enclosed, prepaid, and addressed envelope. If you mark your voting instructions on the proxy card, your shares will be voted as you instruct.

If you return a signed card but do not provide voting instructions, your shares will be voted:

- For the nine named director nominees;
- For the advisory vote to approve executive compensation;
- For the ratification of the selection of Deloitte & Touche LLP as the Group’s independent registered public accounting firm for 2018; and
- For the approval of the Group’s 2018 Employee Stock Purchase Plan.

**You may vote in person at the meeting.**

We will distribute written ballots to anyone who wants to vote at the Annual Meeting. If you hold your shares in street name, you must request a legal proxy from your stockbroker in order to vote at the meeting.

**What if I change my mind after I return my proxy?**

You may revoke your proxy and/or change your vote at any time before the polls close at the Annual Meeting. You may do this by:

- Signing another proxy with a later date;
- Voting by Internet or by telephone (your latest Internet or telephone proxy is counted);
- Voting again at the meeting; or
- Notifying the Corporate Secretary, in writing, that you wish to revoke your previous proxy. We must receive your notice prior to the vote at the Annual Meeting.

**Will my shares be voted if I do not return my proxy?**

If you are a stockholder of record, and you do not return your proxy, your shares will not be voted unless you attend the meeting and vote in person.

**What happens if my shares are held by my stockbroker (or other nominee)?**

If your shares are held by a stockbroker (or other nominee), you will receive a voting instruction card so that you can instruct your stockbroker on how to vote your shares. If you do not return your voting instruction card, then your stockbroker, under certain circumstances, may vote your shares.

Specifically, stockbrokers have authority under exchange regulations to vote your uninstructed shares on certain “routine” matters. For “non-routine” matters, no votes will be cast on your behalf if you do not instruct your stockbroker on how to vote. If you wish to change the



voting instructions that you gave to your stockbroker, you must ask your stockbroker how to do so.

If you do not give your stockbroker voting instructions, your stockbroker may either:

- Proceed to vote your shares on routine matters and refrain from voting on non-routine matters; or
- Leave your shares entirely unvoted.

Shares that your stockbroker does not vote (“broker non-votes”) will count towards the quorum only. We encourage you to provide your voting instructions to your stockbroker. This ensures that your shares will be voted at the meeting.

### **As to my stockbroker voting, which proposals are considered “routine” or “non-routine”?**

The ratification of the selection of Deloitte & Touche LLP as the Group’s independent registered public accounting firm for 2018 (Proposal No. 3) is routine. A stockbroker may generally vote on routine matters if the stockbroker has not received voting instructions from you with respect to such matters.

The election of directors (Proposal No. 1), the advisory vote to approve executive compensation (Proposal No. 2), and the approval of the Group’s 2018 Employee Stock Purchase Plan (Proposal No. 4) are matters considered “non-routine” under applicable rules. A stockbroker cannot vote without your instructions on non-routine matters.

### **What is the voting requirement to approve each of the proposals?**

<u>Proposal</u>	<u>Vote Required</u>
Proposal No. 1 – Election of nine directors	Majority of Votes Cast
Proposal No. 2 – Advisory vote to approve executive compensation	Majority of Shares Present in Person or Represented by Proxy and Entitled to Vote
Proposal No. 3 – Ratify the selection of Deloitte & Touche LLP as the Group’s independent registered public accounting firm for 2018	Majority of Shares Present in Person or Represented by Proxy and Entitled to Vote
Proposal No. 4 – Approve the Group’s 2018 Employee Stock Purchase Plan	Majority of Shares Present in Person or Represented by Proxy and Entitled to Vote

### **How are broker non-votes and abstentions treated?**

Broker non-votes and abstentions are counted for purposes of determining whether a quorum is present. Only “FOR” and “AGAINST” votes are counted for purposes of determining the votes received in connection with the proposal relating to the election of directors (Proposal No. 1), and therefore broker non-votes and abstentions have no effect on that proposal. Stockbrokers may not vote your shares on Proposal No. 1 without instructions from you. The affirmative vote of the majority of the shares present in person or represented by proxy and entitled to vote at the Annual Meeting is required to approve Proposal No. 2, Proposal No. 3, and Proposal No. 4. In addition, the New York Stock Exchange listing standards contain separate approval requirements with respect to the Group’s 2018 Employee Stock Purchase Plan (Proposal No. 4). Under the New York Stock Exchange listing standards, approval of Proposal No. 4 requires the

affirmative vote of the majority of votes cast. Proposal No. 2 is advisory, meaning that they are not binding on the Board, although the Board will consider the outcome of the votes on these proposals. Abstentions have the effect of a vote "AGAINST" Proposal No. 2, Proposal No. 3, and Proposal No. 4. Stockbrokers may vote your shares on Proposal No. 3 (but not on Proposal No. 2 or Proposal No. 4) without instructions from you. Shares resulting in broker non-votes, if any, are not entitled to vote and will have no effect on the outcome of these proposals.

### **Who will count the vote?**

Representatives of Broadridge Financial Services, Proxy Services, will serve as the inspector of elections and count the votes.

### **What does it mean if I get more than one proxy card?**

It means that you have multiple accounts at the transfer agent and/or with stockbrokers. Please sign and return all proxy cards to ensure that all your shares are voted.

### **What percentage of stock do the directors and executive officers own?**

Together, directors and executive officers own approximately 1.0% of our common stock. See "Stock Ownership of Management and Certain Beneficial Owners" for more details elsewhere in this Proxy Statement.

### **Who are the largest common stockholders?**

As of December 31, 2017, the largest stockholders were:

- BlackRock, Inc. beneficially owned 6,368,283 shares of common stock, representing 13.3% of our aggregate outstanding stock as of such date;
- The Vanguard Group, Inc. beneficially owned 5,135,812 shares of common stock, representing 10.69% of our aggregate outstanding stock as of such date; and
- T. Rowe Price Associates, Inc. beneficially owned 3,243,606 shares of common stock, representing 6.7% of our aggregate outstanding stock as of such date.

- \* To the best of our knowledge, no other stockholders held more than 5% of our common shares as of such date.

### **What is the deadline for submitting stockholder proposals for the Group's proxy materials for next year's Annual Meeting?**

Any proposals that stockholders intend to submit for inclusion in next year's Group proxy materials must be received by the Corporate Secretary of the Group by December 19, 2018. A proposal, together with any supporting statement, may not exceed 500 words and must comply with other requirements of Rule 14a-8 under the Securities Exchange Act of 1934. Please submit the proposal to the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, California 95112-4598.

### **How can a stockholder propose a nominee for the Board or other business for consideration at a stockholders' meeting?**

Stockholders who are entitled to vote at a stockholders' meeting may propose a nominee for the Board or other business for consideration at a meeting without seeking to have the matter included in the proxy materials for the meeting pursuant to Rule 14a-8. The bylaws contain the requirements for doing so. The bylaws are posted on the Group's website at

<http://www.calwatergroup.com>. Physical copies of these documents are also available upon request to the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, CA 95112-4598. Briefly, a stockholder must give timely prior notice of the matter to the Group. The notice must be received by the Corporate Secretary at the Group's principal place of business by the 150th day before the first anniversary of the prior year's Annual Meeting. For the 2019 Annual Meeting, to be timely, notice must be received by the Corporate Secretary not later than the close of business on December 31, 2018. If we change the date of the meeting by more than thirty days before or more than sixty days after the date of the previous meeting, notice is due not later than the close of business on the later of the 150th day before the Annual Meeting or the 10th day after we publicly announce the holding of the meeting. If the Group's Corporate Secretary receives notice of a matter after the applicable deadline, the notice will be considered untimely. In that case, or where notice is timely but the stockholder fails to satisfy the requirements of Rule 14a-4 under the Securities Exchange of 1934, the persons named as proxies may exercise their discretion in voting with respect to the matter when and if it is raised at the meeting.

The bylaws specify what the notice must contain. Stockholders must comply with applicable law with respect to matters submitted in accordance with the bylaws. The bylaws do not affect any stockholder's right to request inclusion of proposals in the Group's Proxy Statement under Rule 14a-8.

**How can a stockholder or other interested parties contact the independent directors, the director who chairs the Board's executive sessions, or the full Board?**

Stockholders or other interested parties may address inquiries to any of the Group's directors, to the lead director (who chairs the Board's executive sessions), or to the full Board, by email to [stockholdercommunication@calwater.com](mailto:stockholdercommunication@calwater.com) or by writing to them in care of the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, California 95112-4598. All such communications are sent directly to the intended recipient(s).

**Can I make comments and/or ask questions during the Annual Meeting?**

Yes. Stockholders wishing to address the meeting are welcome to do so by adhering to the following guidelines:

1. Stockholders may address the meeting when recognized by the Chairman or President & Chief Executive Officer (CEO);
2. Each stockholder, when recognized, should stand and identify himself or herself; and
3. Stockholder remarks must be limited to matters before the meeting and may not exceed two minutes in duration per speaker.

No cameras, video, or recording equipment will be permitted at the meeting. Many cellular phones have built-in digital cameras, and while these phones may be brought into the meeting, the camera function may not be used at any time.

**Where and when will I be able to find the results of the voting?**

Preliminary results will be announced at the Annual Meeting. We will publish the final results in a current report on Form 8-K to be filed with the Securities and Exchange Commission ("SEC") within four business days of the Annual Meeting.

## BOARD STRUCTURE

This section briefly describes the structure of the Board and the functions of the principal committees of the Board. The Board has adopted Corporate Governance Guidelines that, along with the charters of the Board committees, provide a framework for the governance of the Group. The Corporate Governance Guidelines and the current charters for the Audit, Organization and Compensation, Finance and Risk Management, and Nominating/Corporate Governance committees are posted on the Group's website at <http://www.calwatergroup.com>. Physical copies of these documents are also available upon request to the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, California 95112-4598.

The Group's policy is that all directors must be able to devote the required time to carry out director responsibilities and should attend all meetings of the Board and of committees on which they sit.

### Leadership Structure

Peter C. Nelson has served as Chairman of the Board since 2012. The roles of Chairman of the Board and CEO are separate. The Board believes that separating these roles is the most appropriate leadership structure for the Group, based on numerous factors, including the Board's historical practice (which has predominantly been to separate the roles), its assessment of the Group's leadership, and the Group's current and anticipated needs. The Board attributes a portion of the historical success of its leadership model to the Chairman of the Board's 17-plus years of service as the former President & CEO of the Group. The Board believes that Mr. Nelson, who retired from the Group in 2013, brings significant experience in the water and public utility industries making him best positioned to lead the Board as it oversees and monitors implementation of the Group's business strategy, considers risks related to strategy and business decisions, and performs its oversight function with respect to the Group's operations.

The Board also has established the position of lead director because it supports having an independent director in a Board leadership position at all times. The lead director is an independent director who is elected by the independent directors to serve for a period of at least one year. Richard P. Magnuson currently serves as lead director. As set forth in the Corporate Governance Guidelines, the lead director's responsibilities and authority include:

- Presiding over executive sessions of the non-management and independent directors and having the authority to call executive sessions;
- Presiding at meetings of the Board in the absence of the Chairman of the Board;
- Recommending to the Chairman of the Board items for consideration on the Board meeting agendas and schedules;
- Serving as liaison between the Chairman of the Board and the independent directors; and
- Being available for consultation and communication with major stockholders upon request.

### Risk Oversight

Under the Corporate Governance Guidelines, the full Board oversees the Group's processes for assessing and managing risk. The Board does not view risk in isolation, but considers risk as part of its regular consideration of business decisions and business strategy. The Board exercises its risk oversight function through the Board as a whole and through its committees. Each of the Board committees considers the risks within its areas of responsibility and identified in its charter. The Finance and Risk Management Committee reviews the Group's major risk

exposures and the steps management has taken and proposes to take to monitor and control such exposures. The Audit Committee reviews with management risks related to financial reporting and internal controls. At least annually, the Finance and Risk Management Committee discusses the Group's risk assessment and risk management with the Audit Committee. The Organization and Compensation Committee reviews enterprise risks to see that our compensation plans and programs do not encourage management to take unreasonable risks relating to our business. The Nominating/Corporate Governance Committee oversees risks related to matters of corporate governance, including director independence and Board performance.

The Group has a Management Committee (MC) that reports to the Finance and Risk Management Committee and meets at least semi-monthly. The MC is chaired by the Group's President & CEO and membership is comprised of the Group's executive officers. Among other functions, the MC identifies and prioritizes key risks and recommends the implementation of appropriate mitigation measures, as needed. The MC reports to the Audit Committee no less frequently than annually. Further review or reporting on risks is conducted as needed or as requested by the Board or committee.

In addition, the Audit Committee oversees the Company's cyber risk management program. The Audit Committee regularly briefs the full Board on issues related to the cyber risk management program and related cyber issues.

## Committees

There are four committees within our Board of Directors: (1) Audit; (2) Organization and Compensation; (3) Finance and Risk Management; and (4) Nominating/Corporate Governance. The membership and the function of each of these committees are described below.

Name	Audit	Organization and Compensation	Finance and Risk Management	Nominating/Corporate Governance
Gregory E. Aliff	✓		✓	
Terry P. Bayer		✓		✓
Edwin A. Guiles	✓	✓	Chair	
Martin A. Kropelnicki				
Thomas M. Krummel, M.D.		Chair		✓
Richard P. Magnuson	✓		✓	Chair
Peter C. Nelson				
Carol M. Pottenger				
Lester A. Snow		✓	✓	
George A. Vera	Chair		✓	✓
<b>Number of meetings held during 2017</b>	<b>5</b>	<b>4</b>	<b>2</b>	<b>3</b>

**AUDIT:** Reviews the Group's auditing, accounting, financial reporting, and internal audit functions. The Audit Committee is also directly responsible for the appointment, compensation, and oversight of the independent registered public accounting firm, although stockholders are asked to ratify the Audit Committee's selection of this firm. All members are independent as defined in the listing standards of the New York Stock Exchange and meet the additional independence requirements for audit committee members imposed by the Sarbanes-Oxley Act and the rules of the SEC thereunder.

The Board has determined that George A. Vera, chair of the Audit Committee, Gregory E. Aliff, and Edwin A. Guiles are audit committee financial experts and are independent under the standards applicable to audit committee members. Designation as an audit committee financial expert means that the Board believes Mr. Vera, Mr. Aliff, and Mr. Guiles have:

- (i) An understanding of generally accepted accounting principles and financial statements;
- (ii) The ability to assess the general application of such principles in connection with the accounting for estimates, accruals, and reserves;
- (iii) Experience preparing, auditing, analyzing, or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the Group's financial statements, or experience actively supervising one or more persons engaged in such activities;
- (iv) An understanding of internal controls over financial reporting; and
- (v) An understanding of audit committee functions.

Designation of a person as an audit committee financial expert does not result in the person being deemed an expert for any purpose, including under Section 11 of the Securities Act of 1933. The designation does not impose on the person any duties, obligations, or liability greater than those imposed on any other audit committee member or any other director and does not affect the duties, obligations, or liability of any other member of the Audit Committee or Board of Directors.

**ORGANIZATION AND COMPENSATION:** Reviews the Group's executive compensation programs, including their establishment, modification, and administration. All members are independent as defined in the listing standards of the New York Stock Exchange, and meet additional independence requirements for compensation committee members applicable under the New York Stock Exchange listing standards. The Organization and Compensation Committee has taken steps to analyze the current risk profile of the Group's executive compensation programs. In its evaluation, the Organization and Compensation Committee review took into account that the Group operates in a highly regulated environment and thus maintains strong internal controls, which factors tend to mitigate against undue risk.

As a result of this evaluation, the Committee does not believe that the Group's compensation practices and programs create risks that are reasonably likely to have a material adverse effect on the Group, nor does it believe that the Group's executive compensation practices and programs are designed to promote risk taking.

**Compensation Consultant:** The Organization and Compensation Committee retained Veritas Executive Compensation Consultants (Veritas) to advise it on marketplace trends in executive compensation, management proposals for the 2017 compensation program, and executive officer compensation decisions. Additionally, Veritas generally evaluated the Group's equity compensation programs. Veritas also consulted with the Nominating/Corporate Governance Committee about its recommendations to the Board on director compensation. Veritas has been retained for advice on 2018 executive officer compensation.

Veritas was directly accountable to the Organization and Compensation Committee. To maintain the independence of their advice, Veritas did not provide any services for the Group other than those described above. In addition, the Organization and Compensation Committee conducted a conflict of interest assessment, considering the following six factors with respect to Veritas: (i) the provision of other services to the Group by Veritas; (ii) the amount of fees received from the Group by Veritas, as a percentage of total revenue of Veritas; (iii) the policies

and procedures of Veritas that are designed to prevent conflicts of interest; (iv) any business or personal relationship between the consultants at Veritas with whom the Group work and any members of the Organization and Compensation Committee; (v) any of our stock owned by the Veritas consultants; and (vi) any business or personal relationship of Veritas or the Veritas consultants with any of the Group's executive officers, and no conflict of interest was identified.

For a description of the processes and procedures used by the Organization and Compensation Committee for the consideration and determination of executive compensation, see "Compensation Discussion & Analysis" elsewhere in this Proxy Statement.

**FINANCE AND RISK MANAGEMENT:** Assists the Board in reviewing the Group's financial policies, risk management strategies, and capital structure. All members are independent as defined in the listing standards of the New York Stock Exchange.

**NOMINATING/CORPORATE GOVERNANCE:** Reviews the Group's director compensation and assists the Board by (i) overseeing director succession planning and recruitment of individuals qualified to become Board members; (ii) overseeing the Group's corporate governance practices; and (iii) reviewing the Group's Corporate Governance Guidelines annually and recommending changes to the Board. All members are independent as defined in the listing standards of the New York Stock Exchange.

During 2017, there were nine meetings of the Board, five meetings of the Audit Committee, four meetings of the Organization and Compensation Committee, two meetings of the Finance and Risk Management Committee, and three meetings of the Nominating/Corporate Governance Committee. The incumbent directors attended at least 75% of all Board and applicable committee meetings in 2017 (held during the period each director served).

### **Independence of Directors**

As discussed in the Group's Corporate Governance Guidelines, a substantial majority of the Board is comprised of independent directors. Currently, the Group's independent directors are Gregory E. Aliff, Terry P. Bayer, Edwin A. Guiles, Thomas M. Krummel, M.D., Richard P. Magnuson, Carol M. Pottenger, Lester A. Snow, and George A. Vera (who will retire from the Board as of the Annual Meeting in accordance with our director retirement policy). Under the listing standards of the New York Stock Exchange, a director is independent if he or she has no material relationship, whether commercial, industrial, banking, consulting, accounting, legal, charitable, familial, or otherwise, with the Group, either directly or indirectly as a partner, stockholder, or executive officer of an entity that has a material relationship with the Group. The Board makes an affirmative determination regarding the independence of each director annually, based on the recommendation of the Nominating/Corporate Governance Committee. The Board has adopted standards to assist it in assessing the independence of directors, which are set forth in the Corporate Governance Guidelines, which are posted on the Group's website at <http://www.calwatergroup.com>. Under these standards, the Board has determined that a director is not independent if:

- The director is, or has been within the last three years, an employee of any company that comprises the Group or an immediate family member is, or has been within the last three years, an executive officer of any company that comprises the Group;
- The director has received, or has an immediate family member who has received, during any twelve-month period during the last three years, more than \$120,000 in direct compensation from companies that comprise the Group, other than director or committee fees and pension or other forms of deferred compensation for prior service (compensation

received by an immediate family member for service as an employee, other than an executive officer, of the Group is not considered for purposes of this standard);

- The director, or an immediate family member, is a current partner of the Group's internal or external auditor; the director is a current employee of such a firm; the director's immediate family member is a current employee of such a firm who personally works on the Group's audit, or the director or an immediate family member was within the last three years a partner or employee of such a firm and personally worked on the Group's audit within that time;
- The director, or an immediate family member, is, or has been within the last three years, employed as an executive officer of another company where any of the Group's present executive officers serves or served at the same time on that company's compensation committee;
- The director is a current employee, or has an immediate family member who is a current executive officer, of a customer or vendor or other party that has made payments to or received payments from companies that comprise the Group for property or services in an amount that, in any of the last three fiscal years, exceeded the greater of \$1 million or 2% of the party's consolidated gross revenues; or
- The director, or the director's spouse, is an executive officer of a non-profit organization to which the Group makes, or in the past three years has made, payments that, in any single fiscal year, exceeded the greater of \$1 million or 2% of the non-profit organization's consolidated gross revenues.

In addition, the Board has determined that none of the following relationships, by itself, is a material relationship that would impair a director's independence:

- Being a residential customer of any subsidiary of the Group;
- Being a current executive officer or employee of, or being otherwise affiliated with, a commercial customer from which the Group has received payments that, in any of the last three fiscal years, did not exceed the greater of (i) 1% of the Group's consolidated gross revenues for the year; or (ii) \$500,000;
- Being a current executive officer or employee of, or having a 5% or greater ownership or similar financial interest in, a supplier or vendor that has received payments from the Group that, in any of the last three fiscal years, did not exceed the lesser of (i) 1% of the Group's consolidated gross revenues for the year; or (ii) \$500,000; or
- Being a director of any of the Group's subsidiaries.

Directors inform the Board as to their relationships with the Group and provide other pertinent information pursuant to questionnaires that they complete, sign, and certify on an annual basis. The Board reviews such relationships to identify possible impairments to director independence and in connection with disclosure obligations. In assessing Mr. Aliff's independence, the Board previously considered that he is a retired former partner of Deloitte LLP, which is the parent entity of Deloitte & Touche LLP, the Group's independent registered public accounting firm. While at Deloitte, Mr. Aliff did not work on the Group's audit or otherwise have any involvement in providing services to the Group. For those directors who reside in a service territory of California Water Service Company and are customers, the Board has determined that it is not a material relationship that would impair their independence under the above standards.



## **Director Qualifications and Diversity**

The Board believes that the Board of Directors, as a whole, should possess a combination of skills, professional experience, and diversity of backgrounds necessary to oversee the Group's business. In addition, the Board believes that there are certain attributes that every director should possess, as reflected in the Board's membership criteria. Accordingly, the Board and the Nominating/Corporate Governance Committee consider the qualifications of directors and director nominees individually and in the broader context of the Board's overall composition as well as in the Group's current and future business and operations.

The Nominating/Corporate Governance Committee is responsible for developing and recommending Board membership criteria to the Board for approval. The Board and the Nominating/Corporate Governance Committee seek a variety of occupational and personal backgrounds on the Board in order to obtain a range of viewpoints and perspectives and to enhance the diversity of the Board. An annual evaluation of the Board's composition enables the Board and Nominating/Corporate Governance Committee to update the skills and experience they seek in the Board as a whole, and in individual directors, as the Group's needs evolve and change over time and to assess diversity. In identifying director nominees from time to time, the Board and the Nominating/Corporate Governance Committee may identify specific skills and experience that it believes the Group should seek in order to constitute a balanced and effective board.

The Group seeks directors having the following specific qualifications:

- Evidence of leadership in his or her particular field;
- Broad experience and sound business judgment;
- Expertise in an area of importance to the Group and its subsidiaries;
- The ability to work in a collegial Board environment;
- High personal and professional ethics and integrity;
- The ability to devote the required time to carry out director responsibilities;
- The ability and willingness to contribute special competencies to Board activities, including appointment to Board committees;
- Freedom from conflicts of interest that would interfere with serving and acting in the best interests of the Group and its stockholders; and
- Evidence of being a high caliber individual who has achieved a level of prominence in his or her career; for example, a CEO or highest level financial officer of a sizeable organization, a director of a major corporation, or a prominent civic or academic leader.

Additionally, Section 2.9 of the Group's bylaws contains requirements that a person must meet to avoid conflicts of interest that would disqualify that person from serving as a director.

Board membership should reflect diversity in its broadest sense. The Group seeks directors who represent a diversity of backgrounds and experiences that will enhance the quality of the Board's deliberations and decisions. The Board, as a whole, should possess a combination of skills, professional experience, and backgrounds necessary to oversee the Group's business. The Board assesses the diversity of skills, experience, and backgrounds represented on the Board as part of the annual Board self-evaluation process.

## **Identification of Director Nominees**

The Group identifies new director nominees through a variety of sources. The Nominating/Corporate Governance Committee will consider director nominees recommended by stockholders in the same manner it considers other nominees, as described in “Board Structure – Director Qualifications and Diversity” elsewhere in this Proxy Statement. Stockholders seeking to recommend nominees for consideration by the Nominating/Corporate Governance Committee should submit a recommendation in writing describing the nominee’s qualifications and other relevant biographical information and provide confirmation of the nominee’s consent to serve as director. Please submit this information to the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, California 95112-4598.

Stockholders may also propose director nominees by adhering to the advance notice procedure described under “Questions and Answers About the Proxy Materials and the Annual Meeting – How can a stockholder propose a nominee for the Board or other business for consideration at a stockholders’ meeting?” elsewhere in this Proxy Statement.

## **Executive Sessions of the Board**

Under the Group’s Corporate Governance Guidelines, the non-management directors meet at least four times each year in executive session without management present, and the independent directors meet in executive session at least once a year. The lead director, Richard P. Magnuson, chairs these sessions.

## **Retirement Age of Directors**

The Group has established a mandatory retirement age for directors. A director must retire no later than the Annual Meeting that follows the date of the director’s 75th birthday. An employee director must retire as an employee no later than the Annual Meeting that follows the date of his or her 70th birthday, but may remain on the Board at the discretion of the Board of Directors.

## **Annual Meeting Attendance**

All directors are expected to attend each Annual Meeting of the Group’s stockholders, unless attendance is prevented by an emergency. All of the Group’s directors who were directors as of the date of the Group’s 2017 Annual Meeting attended the Group’s 2017 Annual Meeting.

## **Other Governance Best Practices**

The Group has adopted other practices that we believe reflect our commitment to good corporate governance including:

### ***No Hedging and Pledging Policies***

In accordance with our Insider Trading Policy, our directors and executive officers are prohibited from (i) hedging their ownership of Group stock, including trading in options, puts, calls, or other derivative instruments related to Group stock or debt; and (ii) pledging their ownership of Group stock.

### ***Executive Compensation Recovery (“Clawback”) Policy***

The Board has adopted an executive compensation recovery, or “clawback,” policy requiring the reimbursement of excess incentive-based compensation provided to the Group’s executive

officers in the event of certain restatements of the company's financial statements. A more detailed description of the Executive Compensation Recovery Policy appears in the "Compensation Discussion and Analysis" section of this Proxy Statement.

### **Stock Ownership Requirements**

Our Board has adopted stock ownership requirements for directors and executive officers. These stock ownership requirements were adopted to promote a long-term perspective in managing the Group and to help align the interests of our stockholders, directors, and executive officers. As of April 3, 2018, 16 of our non-employee directors and executive officers already met or exceeded their ownership requirements. New directors have five years to meet the requirements and executive officers must retain 50% of the net after-tax shares from equity awards until the relevant ownership requirement is achieved. A complete description of the stock ownership requirements for directors and executive officers appears in the "Compensation Discussion and Analysis" section of this Proxy Statement.

Our directors as of April 18, 2018, are as follows:

<b>Name</b>	<b>Age</b>	<b>Position</b>	<b>Current Term Expires</b>	<b>Director Since</b>	<b>Independent</b>	<b>Occupation</b>	<b>Other Board Experience</b>	<b>Public Utilities or Public Health Experience</b>
Gregory E. Aliff	64	Director	2018	2015	Yes	Former Vice Chairman and Senior Partner of U.S. Energy & Resources, Deloitte LLP	Yes	Yes
Terry P. Bayer	67	Director	2018	2014	Yes	Former COO of Molina Healthcare, Inc.	Yes	Yes
Edwin A. Guiles	68	Director	2018	2008	Yes	Former Executive Vice President of Corporate Development, Sempra Energy	Yes	Yes
Martin A. Kropelnicki	51	President & CEO and Director	2018	2013	No	President & CEO of California Water Service Group	Yes	Yes
Thomas M. Krummel, M.D.	66	Director	2018	2010	Yes	Emile Holman and Chair Emeritus of the Department of Surgery at Stanford University School of Medicine	Yes	Yes
Richard P. Magnuson	62	Lead Director & Chair of the Board's Executive Sessions	2018	1996	Yes	Venture Capitalist	Yes	
Peter C. Nelson	70	Chairman of the Board	2018	1996	No	Chairman of the Board of California Water Service Group	Yes	Yes
Carol M. Pottenger	62	Director	2018	2017	Yes	Principal and Owner of CMP Global, LLC	Yes	
Lester A. Snow	66	Director	2018	2011	Yes	Executive Director of the Klamath River Renewal Corporation	Yes	Yes
George A. Vera	74	Director	2018	1998	Yes	Principal Executive Officer of the Carroll Investment Company	Yes	

## PROPOSAL NO. 1 – ELECTION OF DIRECTORS

Upon the recommendation of the Nominating/Corporate Governance Committee, the Board has nominated for election at the 2018 Annual Meeting of Stockholders a slate of nine director nominees. All of the nominees, except Ms. Pottenger, have served as directors since the last Annual Meeting. Ms. Pottenger has served as a director since September 2017, and was recommended to the Nominating/Corporate Governance Committee by the President & CEO of the Group. All directors are elected annually to serve until the next Annual Meeting or until their respective successors are elected. Mr. Vera is retiring from the Board as of the 2018 Annual Meeting and will not stand for re-election, in accordance with the Board's director retirement policy. Accordingly, the Board had reduced the number of directors to nine, effective as of the Annual Meeting.

### **Nominee Qualifications**

When an incumbent director is up for re-election, the Nominating/Corporate Governance Committee reviews the performance, skills, and characteristics of such incumbent director before making a determination to recommend that the Board nominate him or her for re-election.

The Nominating/Corporate Governance Committee believes that all of the following nine director nominees listed are highly qualified and have the skills and experience required for membership on our Board. A description of the specific experience, qualifications, attributes and skills that led our Board to conclude that each of the nominees should serve as a director follows the biographical information of each nominee.

### **Vote Required**

Each director must be elected by the affirmative vote of a majority of the votes cast. A majority of the votes cast means that the number of votes cast "FOR" a director nominee exceeds the number of votes cast "AGAINST" that nominee for director.

## Recommendation of the Board

Our Board of Directors unanimously recommends that you vote “FOR” the election of each of the following nominees:

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### Gregory E. Aliff

Age 64

Director since 2015

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*Mr. Aliff* is the former Vice Chairman and Senior Partner of U.S. Energy & Resources at Deloitte LLP, a global provider of professional services, where he began his distinguished career nearly four decades ago. From 2012 until his retirement in 2014, Mr. Aliff led Deloitte’s Sustainability Services practice, which focused on water and energy management. Prior to that, he led the firm’s U.S. Energy & Resources practice for ten years. Mr. Aliff also previously served as a member of the Board of Directors of the United States Energy Association. He currently serves as a director on the board of SCANA Corporation and as a director for Grid Alternatives, a non-profit organization. Mr. Aliff earned his Bachelor of Science in Accounting and his Masters of Business Administration from Virginia Tech. He is a Certified Public Accountant.

Mr. Aliff brings extensive accounting, auditing, and financial reporting experience to the Board, with specific expertise in both the public utility and energy and resources industries. He also has in-depth experience in strategy, enterprise risk management, and regulatory affairs from his many years providing professional services to numerous major utilities. His deep understanding of public utility markets and the breadth of experience he has gained from working with public companies make him a valuable resource to the Group.

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### Terry P. Bayer

Age 67

Director since 2014

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*Ms. Bayer* is the former Chief Operating Officer (COO) for Molina Healthcare, Inc., a managed care company that provides solutions to meet the healthcare needs of low-income individuals and families who participate in government programs, including Medicaid, Medicare, and Marketplace. She held that position from 2005 until her retirement in February 2018. She was previously Executive Vice President of Health Plan Operations and also held management positions at Family Health Plan (FHP), Maxicare, Matria Healthcare, and AccentCare, Inc. Ms. Bayer previously served on the Board of Directors of Apria Healthcare

Group, Inc. from 2006 to 2008 where she served as the chair of the compliance committee and served as a member of the compensation committee. She holds a Juris Doctor Degree from Stanford University, a Master’s Degree in Public Health from the University of California, Berkeley, and a Bachelor’s Degree in Communication from Northwestern University.

Ms. Bayer brings senior leadership, financial, operational, and public health expertise to the Board from her service as the COO of Molina Healthcare, Inc., a public company. She has many years of experience as an operating executive with a strong focus on government program compliance, public health and administration, as well as customer service. Her significant background and experience in healthcare supports the Board’s efforts in overseeing and advising on employee health matters. Her previous experience as a director of Apria Healthcare Group, Inc. and a committee member also allows her to contribute to the Group.

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**Edwin A. Guiles****Age 68****Director since 2008**

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*Mr. Guiles* has been a director of Cubic Corporation since 2008. He was formerly Executive Vice President of Corporate Development at Sempra Energy. From 2000 to 2006, he was Chairman and CEO of San Diego Gas & Electric (SDG&E) and Southern California Gas Company (SoCal Gas), Sempra Energy's California regulated utilities. He held a variety of management positions at SDG&E since joining that company in 1972. Mr. Guiles is also past chairman of the California Chamber of Commerce. He has a Mechanical Engineering Degree from the University of Arizona.

Mr. Guiles is a former chairman & CEO with a strong public utility background. He has corporate governance experience through his service on the boards of SDG&E, SoCal Gas, and Cubic Corporation, a public company. He brings to the Board valuable senior management and operational expertise from his 37 years at Sempra Energy, SDG&E, and SoCal Gas. Additionally, Mr. Guiles' in depth knowledge of public utility regulation provides the Board with crucial insight.

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**Martin A. Kropelnicki****Age 51****Director since 2013**

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*Mr. Kropelnicki* is President & CEO of the Group. Mr. Kropelnicki joined the Group as Vice President, Chief Financial Officer (CFO) and Treasurer in 2006 and was named the President and COO in 2012. He then was appointed President & CEO of the Group effective September 1, 2013. He has over 29 years of experience in finance and operations, including 15-plus years as CFO at public listed companies and has held executive positions at PowerLight Corporation, Hall Kinion & Associates, Deloitte & Touche Consulting Group, and Pacific Gas & Electric Company. He serves as a director for the Bay Area Council, and the California Foundation on

the Environment & Economy, and is a member of the Silicon Valley Leadership Group. Mr. Kropelnicki is the past President of the National Association of Water Companies and currently serves on their Executive Committee and Board of Directors. He holds a Bachelor of Arts Degree and Master of Arts Degree in Business Economics from San Jose State University. In 2016, Mr. Kropelnicki was awarded the United States Navy Memorial Fund's Naval Heritage Award. He is the 12th recipient of this award since its inauguration.

Mr. Kropelnicki is well positioned to lead the Group's management team and give guidance and perspective to the Board. His experience as the former CFO of the Group provides expertise in both corporate leadership and financial management. His 15-plus years as a CFO of publicly listed companies and operations management experience enables him to offer valuable perspectives on the Group's corporate planning, rate making, and budgeting along with operational and financial reporting.

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**Thomas M. Krummel, M.D.**

**Age 66**

**Director since 2010**

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*Dr. Krummel* is the Emile Holman and Chair Emeritus of the Department of Surgery at Stanford University School of Medicine. A leader in his field, he has been honored with the Henry J. Kaiser Family Foundation Award for Excellence in Clinical Teaching; the John Austin Collins, M.D. Memorial Award for Outstanding Teaching and Dedication to Resident Training; and the Lucile Packard Children's Hospital Recognition of Service Excellence. He is currently Chair of the Board of Directors at The Fogarty Institute for Innovation and serves as a Director of The Morgridge Institute for Research – University of Wisconsin.

Dr. Krummel brings to the Board experience with professional training and development as well as expertise with medical, public health, and science issues. He offers the Board unique insight on public health matters, including healthcare policy and legislation, drinking water quality, and employee health.

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**Richard P. Magnuson**

**Age 62**

**Director since 1996**

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*Mr. Magnuson* is a private venture capitalist and is lead director. Mr. Magnuson holds an undergraduate degree in economics, a law degree and a master's degree in business administration from Stanford University. From 1984 to 1996, he was a general partner of Menlo Ventures, a venture capital firm. He has served on the boards of the following public companies: Rogue Wave Software (acquired by Quovadx), IKOS Systems, Inc. (acquired by Mentor Graphics), and OrCAD, Inc. (acquired by Cadence Design Systems). He has also served on the boards of several other privately held companies in the past.

With his legal and venture capital backgrounds, Mr. Magnuson brings valuable financial and business strategy expertise to the Board. His past experience on the boards of other public companies, and his insight on financial and operational matters, adds value to the Board. His past and current Board service also provides insight on corporate governance practices.

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**Peter C. Nelson**

**Age 70**

**Director since 1996**

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*Mr. Nelson* is Chairman of the Board of the Group and its subsidiaries. He is a director of the California Chamber of Commerce and a past president of the National Association of Water Companies (NAWC).

Mr. Nelson has a strong record of operational and strategic leadership in the public utility business, including his 17-plus years of experience as the former President & CEO of the Group. An engineer by training with a graduate degree in business administration, he gained extensive senior executive experience at Pacific Gas & Electric Company. He has a vast understanding of the water industry from his role as the former

President & CEO of the Group and from his leadership roles representing the water profession nationally at NAWC as well as in California at the State Chamber of Commerce.

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**Carol M. Pottenger**

**Age 62**

**Director since 2017**

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*Ms. Pottenger is principal and owner of CMP Global LLC, which provides consulting services in business development, process improvement, corporate governance, strategic planning, and cyber and information systems, which she founded and has owned since 2014. The first female three-star Admiral in American history to lead in a combat branch, Ms. Pottenger commanded two ships, a logistic force of 30 ships, a Japan-based strike-group of 8 ships, and the Expeditionary Force of 40,000 sailors during her 36 years in the U.S. Navy before retiring in 2013. She was also the senior U.S. Flag Officer responsible for military*

*transformation and sensitive military topics such as counterterrorism and cyber security while on assignment with NATO.*

Ms. Pottenger brings unique experience to the board, ranging from operations to technology to risk management. A graduate of Purdue University in Lafayette, Ind., she also serves on various private, defense, and non-profit boards, including the U.S. Navy Memorial Foundation in Washington, D.C. and PricewaterhouseCoopers LLP Board of Partners and Principals.

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**Lester A. Snow**

**Age 66**

**Director since 2011**

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*Mr. Snow has served as Secretary of the California Natural Resources Agency, Director of the California Department of Water Resources, Regional Director of the U.S. Bureau of Reclamation, Executive Director of the CALFED Bay Delta Program, and General Manager of the San Diego County Water Authority. He served as Executive Director of the California Water Foundation, an initiative of the Resources Legacy Fund, and currently serves on the board of the Klamath River Renewal Corporation. He holds a Master of Science Degree in Water Resources Administration from the University of Arizona and a Bachelor of Science*

*Degree in Earth Sciences from Pennsylvania State University.*

Mr. Snow brings more than 30 years of water and natural resource management experience to the Board. His distinguished public service career enables him to assist the Board in addressing water and environmental issues as well as regulatory and public policy matters.

Additionally, his executive experience in the public sector provides the Board with critical insight on a variety of operational and financial matters.



## STOCK OWNERSHIP OF MANAGEMENT AND CERTAIN BENEFICIAL OWNERS

### **Ownership of Directors and Executive Officers**

The Group's Corporate Governance Guidelines, available on the Group's website at <http://www.calwatergroup.com>, include the stock ownership requirements for non-employee directors and executive officers. The requirements were adopted to promote a long-term perspective in managing the Group and to help align the interests of our stockholders, directors, and executive officers. A more complete description of the stock ownership requirements appears in the "Compensation Discussion and Analysis" section of this Proxy Statement.

Directors are required to achieve the relevant ownership threshold within five years following adoption of the requirements or five years after commencing service, whichever is later. Executive officers must retain 50% of the net after-tax shares from equity awards until the relevant ownership requirement is achieved.

The following table shows the common stock ownership of our directors and executive officers as of April 3, 2018. All directors and executive officers have sole voting and investment power over their shares (or share such powers with their spouses).

Name	Common Stock Beneficially Owned(*)
Gregory E. Aliff Director	7,905
Terry P. Bayer Director	11,315
Shannon C. Dean Executive Officer	9,240
Edwin A. Guiles Director	31,606
David B. Healey Executive Officer	15,949
Martin A. Kropelnicki Director and Executive Officer	76,129
Thomas M. Krummel, M.D. Director	23,507
Robert J. Kuta Executive Officer	8,399
Michael B. Luu Executive Officer	10,836
Richard P. Magnuson Director	69,790
Lynne P. McGhee Executive Officer	20,179
Michelle R. Mortensen Executive Officer	5,046
Peter C. Nelson Director and Retired Executive Officer	42,977
Elissa Y. Ouyang Executive Officer	3,297
Carol M. Pottenger Director	2,657
Gerald A. Simon Executive Officer	3,171
Thomas F. Smegal III Executive Officer	36,548
Lester A. Snow Director	17,375
Paul G. Townsley Executive Officer	17,290
Timothy D. Treloar Executive Officer	13,648
George A. Vera Director	41,511
Ronald D. Webb Executive Officer	12,783
All directors and executive officers as a group	481,158

\* To the knowledge of the Group, as of April 3, 2018, all directors and executive officers together beneficially owned an aggregate of approximately 1.0% of the Group's outstanding common shares. No one director or executive officer beneficially owns more than 1.0% of the Group's outstanding common shares.

## Ownership of Largest Stockholders

As of December 31, 2017, the Group's records and other information available from outside sources indicated that the following stockholders were the beneficial owner of more than five percent of the outstanding shares of our common stock.

The information below is as reported in filings made by third parties with the SEC. Based solely on the review of our stockholder records and public filings made by the third parties with the SEC, the Group is not aware of any other beneficial owners of more than five percent of the common stock.

Class	Beneficial Owner	Number of Shares of Common Stock	Percent of Class
Common	BlackRock, Inc. <sup>(1)</sup> 55 East 52 <sup>nd</sup> Street New York, NY 10055	6,368,283	13.3%
Common	The Vanguard Group, Inc. <sup>(2)</sup> 100 Vanguard Blvd. Malvern, PA 19355	5,135,812	10.69%
Common	T. Rowe Price Associates, Inc. <sup>(3)</sup> 100 E. Pratt Street Baltimore, MD 21202	3,243,606	6.7%

(1) BlackRock, Inc. has sole voting power over 6,261,476 shares and sole investment power over 6,368,283 shares as of December 31, 2017, as filed on SEC Schedule 13G/A.

(2) The Vanguard Group, Inc. has sole voting power over 85,143 shares; sole investment power over 5,043,093 shares; shared voting power over 18,992 shares; and shared investment power over 92,719 shares as of December 31, 2017, as filed on SEC Schedule 13G/A.

(3) T. Rowe Price Associates, Inc. has sole voting power over 710,700 shares and sole investment power over 3,243,606 shares as of December 31, 2017, as filed on SEC Schedule 13G/A.

## Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, requires our directors, executive officers, and holders of more than 10% of our common stock to file with the SEC reports regarding their ownership, and changes in ownership of our securities. Based solely on its review of the copies of forms furnished to the Group, or written representations that no annual forms (SEC Form 5) were required, the Group believes that for fiscal year ended December 31, 2017, our directors and executive officers filed all reports on a timely basis.

## COMPENSATION DISCUSSION AND ANALYSIS

This Compensation Discussion and Analysis (CD&A) describes the material elements of the Group's executive compensation program for 2017. This section focuses on the compensation of the Group's principal executive officer, principal financial officer, and the three other most highly compensated executive officers for 2017 referred to herein as "named executive officers" (NEOs) or "executives."

### **Role of the Organization and Compensation Committee**

The Organization and Compensation Committee (Committee), which is comprised entirely of independent outside directors, is responsible for overseeing the Group's compensation programs for executives and executive succession. After a review of compensation levels, the Committee recommends to the Board compensation levels and incentive performance objectives for executives for the 12-month period beginning January 1st of each year. These objectives align with stockholder and customer interests and support the long-term growth and health of the Group. The Committee starts its planning and review process in February of each preceding year and typically concludes its process in November. After year-end results are final, the Committee reviews the achieved results for the prior year, certifies the achievement of each goal, approves payment of incentive compensation as certified, and approves the incentive compensation targets for the current year.

The following is a summary of the key features of Group’s executive compensation program:

<b>WHAT WE DO</b>	<b>WHAT WE DON'T DO</b>
<ul style="list-style-type: none"> <li>✓ We pay for performance with compensation in the form of annual short-term performance-based incentives as well as awarding 50% of long-term equity incentive compensation in the form of restricted stock units (RSUs) subject to performance-based vesting criteria over a three-year period.</li> <li>✓ We require stock ownership for all directors and executives to promote a long-term perspective in managing the Group and to help align the interests of our stockholders, directors, and executives.</li> <li>✓ We have implemented an executive compensation recovery (“clawback”) policy requiring the reimbursement of excess incentive-based compensation provided to the Group’s executives in the event of certain restatements of the Company’s financial statements.</li> <li>✓ We have retained an independent compensation consultant who reports to the Organization and Compensation Committee.</li> </ul>	<ul style="list-style-type: none"> <li>✗ We do not provide employment agreements. Other than participation in the Executive Severance Plan, none of the executives are party to individual employment or severance agreements.</li> <li>✗ We do not provide single-trigger change in control benefits. The Group’s Executive Severance Plan provides for change in control severance benefits upon a termination of employment following a change in control. In addition, the Group’s equity incentive plan does not require single-trigger vesting acceleration upon a change in control.</li> <li>✗ We do not provide tax gross-ups on perquisites or other personal benefits.</li> <li>✗ We limit perquisites. As detailed below, the Group provides executives with only limited perquisites consisting of a company car with related excess liability insurance and an employee relocation program.</li> <li>✗ We do not allow hedging and pledging with respect to Group stock. Group’s directors and executives are prohibited from hedging their ownership of Group stock, including trading in options, puts, calls, or other derivative instruments related to Group stock or debt, in accordance with an anti-hedging prohibition in our insider trading policy. Our directors and executives are also prohibited from pledging their ownership of Group stock in accordance with an anti-pledging provision in our insider trading policy.</li> </ul>

### **Pay for Performance**

The Group’s executive compensation program is designed to link executive compensation to the Group’s performance (as measured by key operational and financial objectives incorporated in both long-term and short-term performance-based compensation programs), including:

- Use of a short-term performance-based compensation program in the form of an annual short-term performance-based incentive (STI) that supports the long-term growth objectives of the Group;
- Awarding 50% of long-term equity incentive compensation in the form of restricted stock units (RSUs) subject to performance-based vesting criteria, with the remaining 50% awarded in the form of time-based restricted stock awards (RSAs); and

- Using a three-year performance period for the performance-based RSUs with vesting based upon achievement of performance targets related to each of the following: water quality, customer service, utility plant investment, return on equity, and safety.

### **2017 Say-on-Pay Vote**

The Group's executive compensation program (Say-on-Pay Vote) received approximately 93% of the votes cast on the advisory vote in its for fiscal year 2016, taken at the 2017 Annual Meeting of Stockholders. The Committee believes the high level of support was the result of the Committee's commitment to maintaining an executive compensation program focused on pay for performance. These principles continue to be applied, as described more fully below, although the Committee did not make any changes to the executive compensation program in response to the 2017 Say-on-Pay Vote.

We strongly believe in soliciting feedback from stockholders to better understand their views. We continued to solicit feedback from stockholders in 2017. The Committee believes that a mix of short-term and long-term incentive compensation will reward and motivate near-term performance, while at the same time providing significant incentives to keep executives focused on longer-term corporate goals that support both stockholders and customers.

The Committee recognizes that best practices in executive compensation continue to evolve and will continue to monitor developments in this area. The Committee plans to continue regular solicitation of stockholder feedback on our executive compensation program.

### **Recap of 2017 Group Performance**

Our executive team's 2017 performance demonstrates our commitment to delivering value to our stockholders and customers.

#### **Financial Results**

- Achieved net income of \$67.2 million and diluted earnings per share of \$1.40 (each determined in accordance with GAAP);
- Achieved the majority of its operational goals while keeping controllable costs within budget;
- Invested a record \$256.0 million of capital, inclusive of developer contributions, an increase of 16% over 2016;
- Increased the Group's annual dividend by three cents, which represents our 52<sup>nd</sup> consecutive annual dividend increase;
- Maintained the Company's strong credit rating of A+ stable and AA – for first mortgage bonds and "exceptional" liquidity rating from Standard & Poor's (one of the only North American utilities to do so); and
- Achieved consolidated Group earnings per share in 2017 representing a return on equity (determined in accordance with GAAP) of 9.93% as reported in item 7 of the Group's Form 10-K for the year ended December 31, 2017 as filed with the SEC.

On December 15, 2016, the California Public Utilities Commission (CPUC) approved the Group's largest subsidiary's, California Water Service Company (Cal Water), 2015 General Rate Case (GRC) application. The decision authorizes Cal Water to request annual escalation rate increases for 2018 for those districts that passed the earnings test. In November of 2017, Cal Water requested escalation rate increase in all of its regulated districts in California. The annual

adopted gross revenue associated with the November 2017 filing was \$15.9 million (93% of the authorized escalation rate increase), effective January 1, 2018.

On December 20, 2017, Cal Water entered into an \$85 million settlement agreement and release of claims with the manufacturers and distributors of products containing 1,2,3-Trichloropropane (TCP) in *California Water Service Company and City of Bakersfield v. The Dow Chemical Company, et al., Civil Case No. CIV-470999* (TCP Action). The TCP Action sought damages and other relief related to the alleged contamination of drinking water supply and water wells with the chemical TCP. The proceeds from the settlement, after payment of Cal Water's legal fees, will be used to reimburse a portion of the costs associated with Cal Water's remediation efforts related to such alleged TCP contamination.

### **Water Quality and Customer Service Accomplishments**

- Met all state and federal water quality standards in all 221 water systems Group operates;
- Met the new limit of five parts per trillion for 1,2,3-Trichloropropane set by the California State Water Resources Control Board in July 2017 by the initial compliance deadline of January 2018;
- Met or exceeded all customer service standards as set by the CPUC;
- Implemented a Leading Customer Loyalty training program to "win the heart of every customer"; and
- Recognized with the National Association of Water Companies Management Innovation Award for drought management.

### **Safety Achievement**

- Conducted Emergency Operations Center (EOC) training in all subsidiaries, including four with local police, fire, and city authorities;
- Initiated Supervisor Safety Leadership Program;
- Updated and launched Injury and Illness Prevention Program;
- Trained and configured the Critical Incident Response Management Team throughout Cal Water;
- Reduced Lost Time accident rates by 71% over 2016 rates;
- Received the American Water Works Association's (AWWA) Larry C. Larson Safety Award for 2016-2017.

### **CEO Pay Overview**

Martin A. Kropelnicki, the Group's CEO since September 1, 2013, made significant contributions managing the Group's performance in 2017. Based on the 2017 performance objectives, the Committee granted Mr. Kropelnicki an equity incentive award with a total value of \$575,000 for 2017, consisting of \$287,500 in the form of time-based RSAs vesting over three years and \$287,500 in the form of performance-based RSUs with a three-year performance period and the opportunity to earn up to 200% of the target performance-based RSU award based on achievement with respect to Committee approved objectives. With a 2017 base salary of \$925,000 and \$1,297,313 annual performance-based short-term incentive compensation (representing a payout of 165% of target for 2017 and reflecting superior performance during the year as described in more detail below), Mr. Kropelnicki's total direct compensation for 2017 was \$2,809,469 (comprised of salary, annual performance based short-term incentive

compensation bonus, performance-based restricted stock units, and time-based restricted stock awards).

The main difference between Mr. Kropelnicki's total direct compensation and the amount reported in the 2017 Summary Compensation Table later in this proxy statement is the change in value of his pension from 2016 to 2017, a \$5.0 million increase in the actuarial estimate of his future potential pension benefits. Changes in actuarial assumptions for the pension and Supplemental Executive Retirement Plan (SERP) costs are included in customer rates through a rate recovery mechanism. The net present value of the pension benefit ultimately received by Mr. Kropelnicki will change based on a number of factors, including changes in interest rates, changes in mortality tables, current age of the participant, years of service, and age at retirement. No pension benefit is paid to Mr. Kropelnicki until after his retirement from the Group.

### **Compensation Philosophy for Executives**

The Group's overall philosophy is to provide compensation that attracts, retains, and motivates talented executives, rewards excellent job performance, overall leadership, and provides for fair, reasonable, and competitive total compensation that aligns executives' interests with the long-term interests of our stockholders and customers.

The Committee believes that a balance of fixed and variable compensation, with short-term and long-term compensation elements, maintains a strong link between the NEOs' compensation and the overall Group's performance, as well as promotes the interests of both customers and stockholders. The Committee annually re-evaluates the mix of fixed and variable compensation, including the proportions of incentive compensation awarded as short-term cash-based and long-term equity-based awards. Additionally, the Committee continues to monitor the Group's program on an annual basis to ensure that the structure will not incentivize excessive risk-taking.

Overall, we believe our executive compensation program is achieving the intended results. We believe our compensation is competitive in the industry and has resulted in the attraction and retention of executives who contribute to the long-term success of the Group. In addition, the program creates a strong linkage between pay and performance through our long-term equity and annual performance-based short-term incentive compensation without encouraging imprudent risk taking by the Group's executives.

### **Elements of Compensation**

The material elements of the Group's executive compensation program for 2017 included:

- Base Salary;
- Annual Performance-Based Short-Term Incentive Compensation;
- Performance and Time-Based Long-Term Equity Compensation;
- Basic and Supplemental Pension Plan Benefits;
- Deferred Compensation Plan Benefits; and
- Limited Perquisites.



In determining compensation, the Committee is mindful that as a holding company for a California regulated utility, the Group's financial performance is substantially dependent upon CPUC regulation plus other factors, which to a large extent are beyond the control of executives. Therefore, the Committee's decisions regarding overall compensation are determined largely by evaluation of factors that are within the executives' control and its comparisons with companies in its peer group. As discussed below, the metrics used to determine the executives' annual short-term performance-based incentive compensation and the vesting of long-term performance-based equity compensation awards are appropriate metrics that will align executive performance in a manner beneficial to both stockholders and customers and not encourage imprudent risk-taking.

### **Base Salary**

The Group provides the largest portion of executive total compensation in the form of base salaries that compensate the executives for performance of primary roles and responsibilities. The Committee reviews base salaries for executives annually and determines whether or not to recommend adjustments to salaries. To assist the Committee in this review, the Group's President & CEO provides an assessment of each executive's performance and contribution towards the key corporate goals and makes recommendations regarding base salary adjustments to the Committee for each of the executives other than himself based on the competitive data and the other factors described below under "Determining Executive Compensation."

The Committee has and continues to target base salaries for each executive that are appropriate for the performance, skills, capabilities, and individual contributions in his/her position. The base salary levels are established by reference to the competitive data described below.

Consistent with last year's practice, when determining 2017 base salaries and total target cash compensation, the Group compared both the base salaries for its executives to the base salaries for similar positions within the competitive data as well as the target total cash compensation for its executives (taking into account annual short-term incentive compensation targets) to the competitive market target total cash compensation. Each executive's base salary for 2017 was within the competitive range (defined as plus or minus 20% from the median compensation level, based upon available survey data) of target total cash compensation.

Each year, executives of the Group, including the NEOs, establish a number of corporate goals and objectives that promote the long-term growth and align the interests of stockholders, customers, and employees. The objectives are communicated internally and monitored quarterly. Changes in base salary levels for our President & CEO and other NEOs are generally based on progress against certain of these key corporate goals and individual executive performance. For 2017, the following corporate goals were used to evaluate 2017 compensation for our current President & CEO and NEOs:

1. **Group Operations Goal** – Achieve planned operating results as defined in the 2017 Corporate Goals and Objectives. Our overall goal was to manage the controllable elements of administrative and general, other operations, and maintenance expenses within budget.

**Achieved Results for Group Operations** – For 2017, the Group achieved the majority of its operational goals while keeping controllable costs within budget. The Group completed key strategic objectives in the year including:

- Continued enhancement of Group's safety organization and programs making safety a top priority;

- Updated all vulnerability/security assessments in all districts and customer centers;
- Completed companywide office facilities strategic master plan; and
- Co-hosted Emergency Operation Center exercises with four communities.

2. **Stockholder Value Goal** – Achieve budgeted earnings per share of \$1.20, return on equity on invested capital of 9.43%, and company-funded capital expenditures of \$210 million.

**Achieved Results for Stockholder Value** – For 2017, the Group achieved the following result for the major objective in this category:

- Earnings per share of \$1.40 or 117% of target, which represents a return on equity (as determined in accordance with GAAP) of 9.93% as reported in item 7 of the Group's Form 10-K for the year ended December 31, 2017 as filed with the SEC.
- Company-funded capital expenditures were \$256.0 million, exceeding the 2017 Capital program by \$46 million or 22%. The Group's 2017 achieved capital expenditures was \$259.2 million as reported in item 7 of the Group's Form 10-K for the year ended December 31, 2017 as filed with the SEC. Excluding developer funded expenditures of \$17.0 million and including accounts payable accruals of \$13.8 million for capital project spend, the Group spent \$256.0 million on company-funded capital expenditures for the 2017 performance period.

3. **Regulatory Goal** – Earn authorized annual escalation rate increases for 2018, conclude the Hawaii Water Service Company (Pukalani) GRC; file the Hawaii Water Service Company (Waikoloa) GRC.

**Achieved Results for Regulatory** – On December 15, 2016, the CPUC voted to approve Cal Water's 2015 GRC settlement agreement. As a part of the decision Cal Water was authorized to request annual escalation rate increases for 2018 for those districts that passed the earnings test. In November of 2017, Cal Water requested escalation rate increases in all of its regulated districts increasing adopted gross revenue by \$15.9 million. The new rates became effective on January 1, 2018.

In December of 2016, Hawaii Water Service Company filed a GRC for its Pukalani wastewater system requesting an additional \$1.3 million in revenues annually. On September 15, 2017, the Hawaii Public Utilities Commission (HPUC) issued a proposed decision authorizing a \$0.8 million increase in revenues annually to be phased in over four years (\$0.2 million per year). The first phase of the increase was effective on October 18, 2017.

In December of 2017, Hawaii Water filed GRC applications requesting and additional \$3.8 million in revenues on an annual basis for its Waikoloa Village and Resort Systems with the HPUC.

4. **Customer Service and Water Quality Goal** – Complete key strategic projects in the areas of customer service and water quality including:

- Meet or exceed all customer service standards as set by the CPUC;
- Meet or exceed all water quality standards in every state, every day, with no water quality violations in 2017; and
- Meet or exceed all wastewater discharge standards in every system, every day, in 2017.

**Achieved Results for Customer Service and Water Quality** – During 2017, the Group completed key strategic objectives in the areas of customer service and water quality. Cal Water successfully exceeded the nine CPUC standards which encompass key measurements for telephone responsiveness, service responsiveness, billing accuracy, and general levels of

customer complaints. The nine CPUC customer service standards are found in the CPUC's General Order 103-A.

Additional key objectives include:

- Planned, designed, and constructed treatment to meet the new limit of five parts per trillion for 1,2,3-Trichloropropane set by the California State Water Resources Control Board in July 2017 by the compliance deadline of January 2018;
- Developed and implemented response to new Environmental Protection Agency (EPA)/State of California guidance on the revised Lead and Copper Rule; and
- Company maintained an excellent environmental standards record throughout 2017.

5. **Employee Retention and Development Goal** – Implement key strategic projects in the area of employee retention and development.

**Achieved Results for Employee Retention and Development** – During 2017, the Group completed key strategic objectives in the area of employee retention and development, including:

- Successfully updated and enhanced the Group's Continuous Improvement program, piloting it in two districts;
- Completed the 2017 succession and employee development plan, including leadership development program and executive development program;
- Implemented a Critical Incident Response Management (CIRM) process to support the well-being of those members either directly or indirectly exposed to a critical incident;
- Continued focus on developing partnerships with local schools and other entities to build interest in individuals wanting a career in the water industry at Cal Water;
- Introduced and implement Lost Time Accidents rates to track the return to work program, reducing rates to 0.4 in 2017 from 1.4 in 2016, a 71% reduction;
- Recipient of the American Water Works Association's (AWWA) Larry C. Larson Safety Award for 2016-2017;
- Named a "Top 100 Workplace" in the San Francisco Bay Area for the sixth consecutive year; and
- Received certification as a Great Place to Work® by the Great Place to Work® Institute for the second consecutive year.

Once the Committee assesses the business results for each goal as described above, the Committee then reviews and discusses the overall performance of each executive and the competitive data provided by the independent consultant retained by the Committee. Once reviewed and agreed upon, the Committee recommends to the Board the base salaries for the

executives (including the President & CEO). The following table shows the 2016, 2017, and 2018 base salaries for the NEOs:

<b>Name</b>	<b>2016 Base Salary</b>	<b>2017 Base Salary</b>	<b>2018 Base Salary</b>
Martin A. Kropelnicki	\$825,000	\$925,000	\$958,000
Thomas F. Smegal	405,600	427,000	442,000
Lynne P. McGhee	275,600	293,000	304,000
Paul G. Townsley	345,050	368,000	391,000
Robert J. Kuta	306,000	322,000	334,000

The increases to salaries are intended to compensate the individuals for job performance and overall leadership while being within the “competitive range” of the market data for target total cash compensation for similar positions (“competitive range” is described in more detail above and below) when taking into account the short-term incentive compensation described below.

### ***Performance-Based Short-Term Incentive Compensation***

The Company maintains an annual performance-based short-term incentive compensation program for executives that aligns long-term goals with payouts dependent upon achievement of certain performance objectives over a one-year performance period.

For 2017, the performance criteria for the annual short-term incentive awards were tied to the same performance metrics used for the long-term performance-based RSUs that were eligible to be earned for 2017 performance, which are listed in the table that follows under “Performance and Time-Based Equity Compensation.” The same metrics were utilized for two reasons. First, the Committee believes aligning incentives between short-term and long-term incentive compensation discourages short-term risk taking at the expense of the long-term health of the Group’s regulated utilities, customers, and operations. Second, the metrics previously underwent regulatory review in our last general rate case, and as such, compensation payable based upon these metrics is currently included in customer rates through a rate recovery mechanism.

For 2017, the Committee granted the opportunity for executives (other than our President & CEO) to receive short-term performance incentive awards with a target payout equal to 20% of base salary (up from 15% in 2016) with an actual payout range of 0% to 200% of target, based on performance. For our President & CEO, the Committee granted the opportunity to receive a short-term performance based incentive award in 2017 with a target payout equal to 85% of base salary (up from 75% in 2016), with an actual payout range of 0% to 200% of target, based on performance.

Payment of the short-term performance incentive awards is typically made in March, following the Group’s receipt of audited financial statements and the subsequent certification of the Group’s performance by the Committee. However, due to the enactment of the Tax Cuts and Jobs Act (H.R.1), and the resulting changes to Section 162(m) of the Code (as discussed in more detail below), the Committee reviewed and certified preliminary achievement of the performance criteria for the annual short-term incentive awards and authorized payment of the award based upon preliminary achievement results in December 2017 to enable the Group to preserve the deductibility of those payments at the higher corporate tax rates in effect in 2017 (as compared to 2018 when the new law went into effect). In February 2018, following review of the audited financial statements, the Committee certified final achievement of the performance criteria (which was at a level greater than the preliminary performance results

certified in December 2017) and payment of the remaining balance of the earned annual short-term incentive awards in early March 2018. See below for additional information regarding the performance goals and resulting payouts under the annual short-term incentive program for 2017.

### **Performance and Time-Based Equity Compensation**

The purpose of the Group's long-term equity incentive compensation is to better align executive compensation with the interests of both stockholders and customers, to create incentives for executive recruiting and retention, to encourage long-term performance by the Group's executives, and to promote stock ownership. Risk is taken into account in determining the aggregate amount of incentive compensation and performance criteria, including assessment of risk management and risk mitigation.

As with target short-term incentive compensation, the Committee reviewed the competitive range of long-term equity compensation and total direct compensation for similar positions within the competitive market in making decisions regarding long-term equity compensation awards for 2017. However, the Committee also believes that, in the interest of fostering the Group's "One-Team" approach for the executive team, which strengthens and rewards teamwork and collaboration within the executive team, the annual equity incentive awards granted to each of the Group's executives (other than the President & CEO) should be based on the same objectives and methodology. The Committee recommended awarding the President & CEO a greater value of equity awards in 2017 than the other executives because of his substantially greater level of responsibility and ability to influence the Group's operational results.

Based on the methodology described above, the grant values for 2017 were unchanged from 2016's grant values. For 2017, the Committee set the total value for the equity compensation awards at \$575,000 for our President & CEO, \$150,000 for vice presidents, and \$90,000 for all other executives, assuming a target level of performance. All equity awards for executives were granted 50% in the form of time-based RSAs vesting over three years and 50% in the form of performance-based RSUs with a three-year performance period and the opportunity to earn up to 200% of the target performance-based RSU award based on achievement with respect to Committee-approved objectives.

The performance-based RSUs awarded to our President & CEO and other executives provide for a three-year performance period with vesting based solely upon the achievement of objective performance criteria. Each year of the performance period, the performance of each metric is certified and approved by the Committee. At completion of the three-year performance period, the annual performance is aggregated to attain the three-year performance period's final achievement. The number of shares awarded at the end of the three-year performance period is based on the extent the performance criteria is met over such time and subject to the executive's continued employment through such date. Each year following the performance period, the Committee establishes performance metrics with respect to each of the performance criteria described below. As noted above, for 2017, the performance criteria for our annual short-term incentive program are the same metrics applicable to the performance-based RSUs for 2017.

The following section provides a more detailed look at each performance metric, along with the maximum, target, and threshold levels for each:

- **Water Quality:** This metric is based only upon performance of the Group's largest subsidiary, Cal Water. The CPUC has authority to set drinking water standards. It has adopted the California State Water Resources Control Board, Division of Drinking Water

(DDW) standards, which also incorporate U.S. Environmental Protection Agency (EPA) drinking water standards.

- A primary drinking water standard violation is related to public health, either acute or long-term.
- A secondary drinking water standard violation is related to taste or aesthetics, such as excessive iron and manganese, and can generate customer complaints.
- A procedural violation is a missed sample or other non-compliance item that is not a violation of a primary or secondary standard.

Performance is evaluated based on number of procedural violations and violations of primary and secondary drinking water standards. Cal Water makes it a priority to meet all water quality standards, every day, in every service area. For this reason, the target performance level was set for no primary water standard violations, two or fewer secondary water standard violations, and no more than four procedural violations.

Performance Level*	Primary Water Standards Violations	Secondary Water Standards Violations	Procedural Violations	Goal Achieved
Maximum	0	0	0	200%
Target	0	2 or fewer	Up to 4	100%
Threshold	1 or fewer	4 or fewer	Up to 8	50%

\* An additional tier applies between the target and maximum level.

- **Customer Service:** A combination of nine CPUC standards and one internal Cal Water performance indicator which encompass key measurements for telephone responsiveness, service responsiveness, billing accuracy, and general levels of customer complaints comprises this metric. The nine CPUC customer service standards are found in the CPUC's General Order 103-A. This metric is evaluated each quarter for 10 measurements in 20 California service areas for an annual target of 760-767 and a maximum annual metric measurement of 800.

Performance Level*	Criteria	Goal Achieved
Maximum	99% of maximum annual metric	200%
Target	95% of maximum annual metric	100%
Threshold	92% of maximum annual metric	25%

\* Multiple tiers apply between the threshold and target level and between the target and maximum level.

- **Utility Plant Investment:** The annual Board-approved capital expenditures budget is the target for this metric. Investment in utility plant, property, and equipment is a driver of stockholder return and a key component of providing reliable, high-quality water service to customers. This metric is updated each year to reflect the annual approved capital program and budget for the Group and its subsidiaries. For 2017, the annual Board-approved capital expenditure budget and target performance level was set at

\$210 million, an increase of \$20 million over 2016's Board-approved capital expenditure budget.

Performance Level*	2017 (In Millions)	Goal Achieved
Maximum	\$230	200%
Target	\$210	100%
Threshold	\$195	25%

\* Multiple tiers apply between the threshold and target level and between the target and maximum level

- Return on Equity (ROE):** The return on equity of 9.43% on invested capital is the target for this metric. Return on equity is defined using net income divided by average common stockholders' equity. This metric measures the effectiveness of the Group's financial management and regulatory strategy. It provides for a substantial increase in the award for performance above the authorized ROE (20% increase for a 5 basis points [bps] increase in ROE) and a more graduated downside measure (20% decrease in award for a 50 bps decrease in ROE) due to the regulatory mechanisms in place which limit the possibility of achieving high returns on equity. For 2017, the ROE authorized by the CPUC was 9.43%.

Performance Level*	Each Annual Period	Goal Achieved
Maximum	9.96%	200%
Target	9.43%	100%
Threshold	7.46%	20%

\* Multiple tiers apply between the threshold and target level and between the target and maximum level.

- SAFETY:** This metric is measured annually for Cal Water and is the sum of two broadly used indices of a company's workplace safety. Those indices are the federal Occupational Safety and Health Administration Reportable Incident Rate (ORIR) and lost productivity measured in employee days away, restricted, or transferred (DART). The Group's executive team has been focused on improving its management of the safety program and has set this metric to improve performance from the 2016 achieved results. The two measures are aggregated, so performance at the 50% level for each metric would be the equivalent of a 100% performance on this metric as a whole.

Performance Level*	ORIR Measure Performance Target	Numeric Equivalent	Goal Achieved
Maximum	40% improvement over 2016 achieved results	3.4	100%
Target	25% improvement over 2016 achieved results	4.2	50%
Threshold	10% improvement over 2016 achieved results	5.1	25%

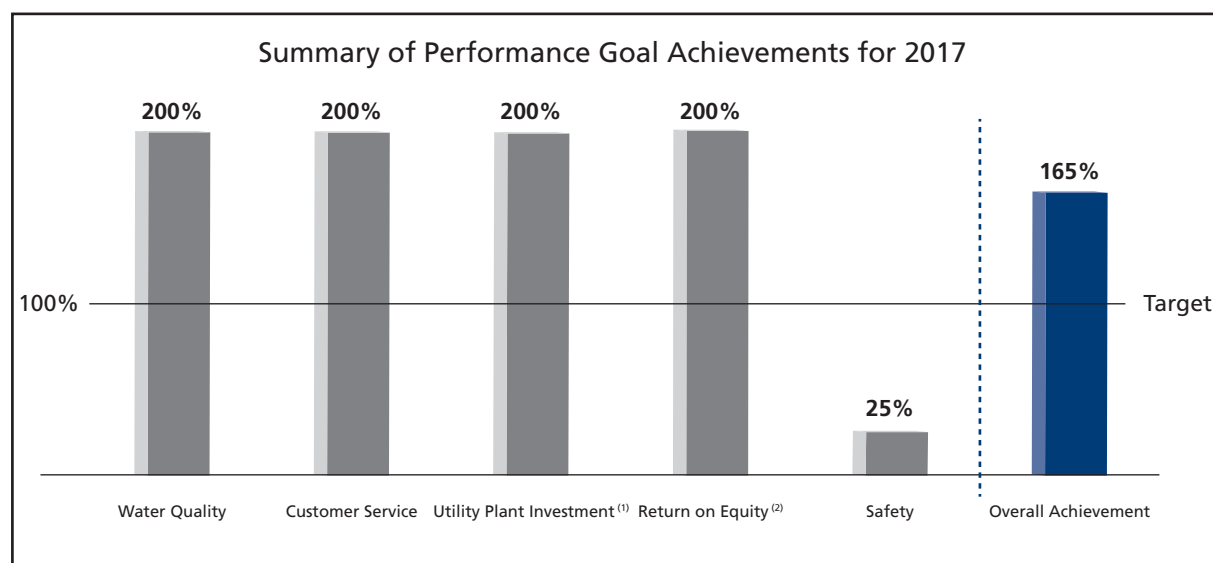
\* An additional tier applies between the target and maximum level.

Performance Level*	DART Measure Performance Target	Numeric Equivalent	Goal Achieved
Maximum	40% improvement over 2016 achieved results	2.0	100%
Target	25% improvement over 2016 achieved results	2.6	50%
Threshold	10% improvement over 2016 achieved results	3.0	25%

\* An additional tier applies between the target and maximum level.

### Summary of Performance Goal Achievements for 2017

The following chart sets forth the performance goals used for short-term and long-term compensation for 2017, and the achievement of each goal as certified by the committee for 2017. The RSU/cash award component weighting is 20% for each of the five performance goals as follows:



- Water Quality was above target with no primary, secondary, or procedural violations.
- Customer Service was above target with 780 annual aggregate metrics met.
- Utility Plant Investment was above target with \$220 million in company-funded capital expenditures.
- Return on Equity was above target at 9.93%.\*
- Safety was below target at 4.3 ORIR and 3.3 DART.

**Total 2017 RSU achievement for all executives = 165%**

**Total 2017 short-term incentive award achievement for all executives = 165% (award cannot exceed 200%)**

(1) The Group's 2017 achieved capital expenditures was \$259.2 million as reported in item 7 of the Group's Form 10-K for the year ended December 31, 2017, as filed with the SEC. Excluding developer-funded expenditures of \$17.0 million and including accounts payable accruals of



\$13.8 million for capital project spend, the Group spent \$256.0 million on company-funded capital expenditures for the 2017 performance period.

(2) The Group achieved a return on average common equity in 2017 of 9.93%, as reported in item 7 of the company's Form 10-K for the year ended December 31, 2017, as filed with the SEC.

The table below summarizes the total performance-based incentive compensation paid or earned by our President & CEO, CFO, and the three most highly compensated executives of the Group for the fiscal year ended December 31, 2017.

Name	2017 Performance Stock Earned (\$) <sup>(1)</sup>	2017 Short-Term Incentive Award (\$) <sup>(2)</sup>
Martin A. Kropelnicki	\$773,841	\$1,297,313
Thomas F. Smegal	189,962	140,910
Lynne P. McGhee	189,962	96,690
Paul G. Townsley	189,962	121,440
Robert J. Kuta	174,997	106,260

(1) The performance stock earned represents the 2017 tranche for the 2015, 2016, and 2017 performance stock awards. The shares for the 2015 performance stock award, which is comprised of the years 2015, 2016, and 2017, were granted following the end of the three-year performance period on March 6, 2018. The shares for the 2016 performance stock award, which is comprised of the years 2016, 2017, and 2018, will be granted following the end of the three-year performance period. The shares for the 2017 performance stock award, which is comprised of the years 2017, 2018, and 2019, will be granted following the end of the three-year performance period.

(2) The short-term incentive compensation is paid out annually following certification of the prior year's results by the Committee.

## 2018 Compensation

### *Incentive Awards for 2018*

The Committee increased the target short-term compensation values from 2017 to 2018 under the annual incentive program. There was no increase to the target value of the equity compensation awards.

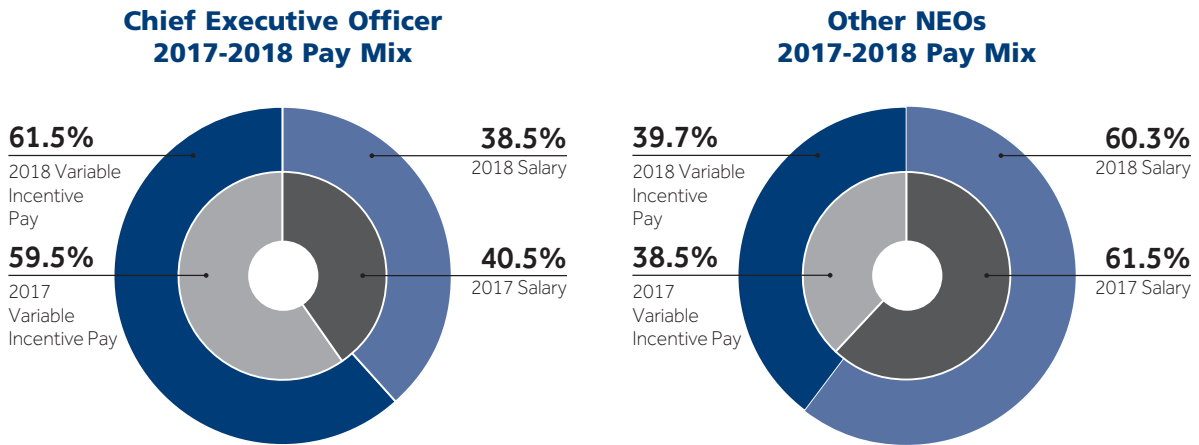
The equity awards vest over three years respectively, with 50% subject to the achievement of performance-based metrics and 50% subject to time-based vesting and continued employment.

On March 6, 2018, the following awards were granted:

- President & CEO – 7,489 shares of RSAs and 7,489 RSUs;
- Vice presidents – 1,954 shares of RSAs and 1,954 RSUs; and
- Other executives – 1,173 shares of RSAs and 1,173 RSUs.

The RSUs are subject to performance-based vesting.

The following charts illustrate variable incentive pay as a percentage of compensation for 2017 and 2018:



### **Basic and Supplemental Pension Plan Benefits**

In addition to the tax-qualified defined benefit plan that covers all permanent employees, the Group provides supplemental retirement benefits to executives under the SERP. The SERP plan is designed primarily to compensate for limitations imposed by the Internal Revenue Code (Code) on allocations and benefits that may be paid to executives under the Group’s tax-qualified plan. Because the Code restricts benefits under the tax-qualified plan, executives otherwise would not be eligible to receive the retirement benefits that are proportional to the benefits received by our employees that generally are based on compensation. The SERP is structured such that benefits are paid to executives on a “pay as you go” basis. The SERP is an unfunded, unsecured obligation of the Group and is designed to assist in attracting and retaining key executives while providing a competitive, total compensation program. Both the qualified pension and SERP expenses are fully recoverable in customer rates.

### **Deferred Compensation Plan**

The Group maintains a deferred compensation plan for its directors, executives, and qualified managers. The plan is intended to promote retention by providing eligible employees, including the executives, with a long-term savings opportunity on an income tax-deferred basis. This plan is voluntary and funded by the individuals who elect to participate in the program. There are no company-matching contributions.

### **401(k) Plan**

All employees satisfying the eligibility requirements are entitled to participate in our 401(k) plan and receive matching contributions from the Group. Pursuant to the plan, all employees, including executives, are entitled to contribute up to the statutory limit set by the Internal Revenue Service (IRS) and the Group matches 75% for each dollar contributed up to eight percent for a maximum company-matching contribution of six percent of employee’s base salary.

### **Limited Perquisites**

As part of the Group’s automobile policy, the Group’s executives have the use of a company-owned automobile, including excess liability insurance. The Committee believes that the use of

a company-owned automobile allows the executives to work more efficiently because many of the geographic areas served by the Group are most effectively reached by automobile as opposed to other forms of transportation, such as air travel. Any personal mileage incurred by the executive is taxed as additional compensation in accordance with IRS regulations and paid for by the executive. The Group offers its executives a supplemental medical reimbursement plan providing proactive health protection services including executive physicals and emergency travel assistance. Additionally, the Group also has a relocation program assisting employees required to move on behalf of the company to remain as productive as possible during the relocation transition. Employees who receive relocation assistance are required to sign a repayment agreement. Other than these benefits, the Committee's general philosophy is not to provide perquisites and other personal benefits of substantial value to the executives.

### **Severance Arrangements**

None of the executives is a party to an individual employment agreement with the Group that provides for severance benefits. Additionally, executives are not provided with single-triggered change in control benefits.

Consistent with the Group's compensation philosophy, the Committee believes that the interests of stockholders are best served if the interests of senior management are aligned with those of the Group's stockholders. To this end, the Group provides change in control severance benefits to executives under the Group's Executive Severance Plan to reduce any reluctance of the executives to pursue or support potential change in control transactions that would be beneficial to stockholders. The Group adopted the plan in 1998, and its purpose is to promote the continued employment and dedication of executives without distraction in the face of a potential change in control transaction. The Executive Severance Plan provides severance pay equal to three times base salary to each of the executives if their employment is terminated without good cause or they resign for good reason during the two-year period following a change in control. Each executive will also be eligible to receive a gross-up payment if the executive is required to pay an excise tax under Section 4999 of the Internal Revenue Code. This provision for a tax gross-up has been a part of the Executive Severance Plan since its inception in 1998 and has not been modified since then.

In the event of a termination not in connection with a change in control, each executive is covered by the Group's general severance policy which states that each non-union employee of Group whose employment is terminated without cause is entitled to severance pay of either one week's pay after completing two years of service or two weeks' pay after completing five or more years of service, provided in each case that at least two weeks' notice is given. Under the Group's policies, all executives are entitled to a pay-out of six weeks of vacation time upon termination of employment.

### **Determining Executive Compensation**

Each year the Committee reviews, assesses, and recommends to the Board all compensation for executives after determining that the compensation for these individuals is competitive relative to companies of comparable size, complexity, location, and business nature (see below for additional discussion of this comparison). In addition, the Committee approves the retention, fees, and termination of any compensation consultant or compensation consulting firm used to assist in the evaluation of executive compensation. With respect to 2017 compensation decisions, the Committee retained the services of an independent compensation consultant, Veritas Executive Compensation Consultants (Veritas), for investigation into and advice on compensation for executives. The Committee believes that having an independent evaluation of compensation is a valuable tool for the Committee, the Group, and stockholders. Veritas is

not engaged to perform any additional work for the Group. The Committee retained Veritas for several purposes, including:

- Constructing and reviewing compensation comparisons from readily available published survey and public filings data; and
- Performing a competitive assessment of the Group’s compensation programs, practices, and levels for its directors and executives.

The Committee made a number of compensation recommendations, including those pertaining to the executives that were based on the competitive assessments provided by and through consultation with Veritas. The Committee’s recommendations were made, however, entirely by the Committee, in its sole discretion.

Total compensation level for executives is based on one or more of the following factors:

- The individual’s duties and responsibilities within the Group;
- The individual’s experience and expertise;
- The compensation levels for the individual’s peers within the Group;
- Compensation levels for similar positions based on a review of published compensation surveys; and
- The levels of compensation necessary to recruit, retain, and motivate executives.

In order to determine competitive compensation practices for 2017, the Committee relied, in part, on published survey compensation data as well as proxy data for individual companies. The individual companies are referred to in this proxy statement as the “Peer Group.” The Peer Group includes companies that are generally gas, water, or multi-utility-based organizations with one-half to two times the annual revenue size of the Group. For 2017, the Committee made a change to the peer group. The Committee added The Empire District Electric Company, MGE Energy, and Ormat Technologies, all of which are similar to the Group in size and industry scope.

On November 29, 2017, the Committee approved the following companies for inclusion in the Peer Group for 2017 for determining competitive compensation levels:

Allete, Inc.	Northwest Natural Gas Company
American States Water Company	NorthWestern Corp.
Aqua America, Inc.	Otter Tail Corporation
Avista Corporation	Ormat Technologies
Black Hills Corp.	PMN Resources
Chesapeake Utilities Corp.	Portland General Electric
El Paso Electric	San Jose Water Company
MGE Energy	South Jersey Industries, Inc.

Veritas utilized the data from these sources (competitive data) to compile the competitive pay information comparing each executive’s compensation to market levels for his/her executive position.

After consideration of the competitive data, the Committee makes decisions regarding each individual executive’s target total compensation opportunities based on the Group and individual performance and the need to attract, motivate, and retain an experienced and effective management team. The Committee examined the relationship of each executive’s

base salary, long-term equity incentives, short-term incentive awards, and total compensation to the competitive data from several perspectives by reviewing the following:

- The competitive data without any adjustments;
- Annual incentive or bonus valued at 50% of median of the market competitive data;
- The lower range of 20% below the median of the market competitive data;
- Target total direct compensation reduced by 20% from the median of the market competitive data; and
- Actual short-term incentive compensation reduced by 20% from the median of the market competitive data.

In making compensation recommendations for the 2017 fiscal year for the executives, the Committee's general objective was to set total compensation within a "competitive range" for each executive's position based on the competitive data. The Committee considers the "competitive range" to mean that compensation levels are within plus or minus 20% of the median compensation levels as determined by reference to the competitive data. Actual compensation decisions for the executives were, however, influenced by a variety of additional factors, including considerations of each individual's experience, expertise, performance and leadership, the Group's performance, and internal equity among the executives. With respect to 2017 compensation planning, the Committee retained the services of Veritas as the independent compensation consultant.

## **Other Compensation Policies**

### ***Stock Ownership Requirements***

The Board adopted requirements for our executives and members of our Board to own shares of Group's stock to further align their interests with those of our stockholders. The requirements were adopted to promote a long-term perspective in managing the Group and to help align the interests of our stockholders, directors, and executives. Each non-employee director and executive must directly own Group stock having a market or intrinsic value (i.e., paper gain for vested, unexercised stock options); whichever is higher, equal to:

- For the Group's President & CEO, three times annual base salary;
- For vice presidents, one and one-half times annual base salary;
- For all other executives, one time annual base salary; and
- For non-employee directors, five times annual base retainer.

Executives must retain 50% of the net after-tax shares from equity awards until the relevant ownership requirement is achieved. Non-employee directors are required to achieve the relevant ownership threshold within five years following adoption of the requirements or five years after commencing service, whichever is later. For executives, the Committee reviews compliance with these requirements annually. The Nominating/Corporate Governance Committee reviews compliance with these requirements for non-employee directors annually.

### ***Anti-hedging and No Pledging Policy***

In 2012, the Board adopted an insider trading policy that prohibits our directors and executives from participating in put or call options transactions, hedging and pledging transactions, or other inherently speculative transactions with respect to Group stock. This policy was adopted as a matter of good corporate governance and, by prohibiting such transactions for executives,

the compensatory value of equity awards on both the upside and the downside remains strong.

### ***Executive Compensation Recovery (“Clawback”) Policy***

In 2012, the Board also adopted an executive compensation recovery, or “clawback,” policy requiring the reimbursement of excess incentive-based compensation provided to the Group’s executives in the event of certain restatements of the company’s financial statements. The policy allows the Group to clawback incentive-based compensation from executives who were actually involved in the fraud or misconduct that triggered the accounting restatement to the extent that the compensation was in excess of what would have been paid under the accounting restatement. This policy is applicable to all incentive-based compensation paid after implementation of the policy, and it covers the three-year period preceding the date on which the Group is required to prepare the accounting restatement.

### ***Tax and Section 162(m) Implications***

When designing compensation policies and setting compensation levels, the Group considers the potential tax treatment of the compensation, but the primary factor influencing program design is the support of business objectives. The Committee has reviewed the Group’s compensation structure in light of Section 162(m) of the Code (Section 162(m)), which limits the amount of compensation that the Group may deduct for federal income tax purposes in any given year to \$1,000,000 for certain executive officers. For 2017, there were certain exceptions to this limit, one of which is for “performance-based compensation,” as defined under Section 162(m). RSAs granted by the Group do not qualify as “performance-based compensation,” and thus counted against the \$1,000,000 deductibility limit in 2017. Despite the Committee’s best intention to implement performance based awards eligible to qualify as tax deductible to the Group under Section 162(m) as in existence at the beginning of 2017, assurances cannot be made that compensation intended to satisfy the requirements for performance-based exemption from Section 162(m) will, due to the ambiguities and uncertainties as to the application and interpretation of Section 162(m) and the regulations issued thereunder.

Effective for taxable years beginning after December 31, 2017, the exemption from Section 162(m)’s deduction limit for performance-based compensation has been repealed. As such, compensation in excess of \$1 million paid to applicable executive officers will not be deductible unless it qualifies for transition relief applicable to certain arrangements in place as of November 2, 2017.

In designing the executive compensation decisions for 2018, the Committee carefully considered the effect of the changes made to Section 162(m) together with our factors relevant to our business needs, but did not make any changes to the executive compensation program as a result of those changes.

## Summary Compensation Table

The table below summarizes the total compensation paid or earned by our President & CEO, CFO, and the three most highly compensated executive of the Group for the fiscal years ended December 31, 2017, 2016, and 2015.

(a) Name and Principal Position	(b) Year	(c) Salary (\$)	(e) Stock Awards (\$) <sup>(1)</sup>	Non-equity Incentive Plan Compensation (\$) <sup>(2)</sup>	(h) Change in Pension Value and Nonqualified Deferred Compensation Earnings (\$) <sup>(3)</sup>	(i) All Other Compensation (\$) <sup>(4)</sup>	(j) Total (\$)
<b>Martin A. Kropelnicki</b> President & CEO	2017	\$921,171	\$590,985	\$1,297,313	\$4,990,347	\$ 39,900	\$7,839,716
	2016	\$824,308	\$565,818	\$ 841,500	\$2,187,960	\$ 29,363	\$4,448,949
	2015	\$768,712	\$509,458	\$ 385,000	\$1,064,617	\$ 32,009	\$2,755,296
<b>Thomas F. Smegal III</b> Vice President, Chief Financial	2017	426,180	150,297	140,910	1,140,173	42,411	1,899,971
	2016	406,980	141,967	82,742	538,025	27,843	1,197,557
	2015	390,592	120,512	49,920	60,668	23,430	645,122
<b>Lynne P. McGhee</b> Vice President, General Counsel	2017	292,340	150,297	96,690	1,005,958	33,293	1,578,578
	2016	275,834	141,967	56,222	537,848	30,047	1,041,918
	2015	264,761	120,512	33,920	200,425	29,979	615,677
<b>Paul G. Townsley</b> Vice President, Rates and Regulatory Matters	2017	367,131	150,297	121,440	558,960	29,788	1,227,616
	2016	345,903	141,967	70,390	428,076	18,406	1,004,742
	2015	335,547	120,512	42,800	276,342	18,482	793,683
<b>Robert J. Kuta</b> Vice President, Engineering	2017	321,390	145,216	106,260	356,131	46,358	975,355
	2016	307,002	116,250	62,424	229,010	43,743	758,429
	2015	228,548	58,924	38,400	125,609	142,230	593,711

- (1) Amounts reflect the full grant date fair value of RSAs and RSUs granted in the years shown, calculated in accordance with FASB Accounting Standards Codification (ASC) Topic 718, disregarding estimates for forfeitures and assuming target performance. Assumptions used in the calculation of these amounts are included in footnote 12 of Group's annual report on Form 10-K filed with the SEC on March 1, 2018. The amounts reported are as follows: Mr. Kropelnicki, RSAs of \$302,195 and RSUs granted in 2017, 2016, and 2015 of \$100,732, \$97,265, and \$90,793, with a maximum value of \$201,464, \$194,531, and \$181,586; Mr. Smegal, RSAs of \$78,829 and RSUs granted in 2017, 2016, and 2015 of \$26,276, \$25,380, and \$19,813 with a maximum value of \$52,553, \$50,760, and \$39,625; Ms. McGhee, RSAs of \$78,829 and RSUs granted in 2017, 2016, and 2015 of \$26,276, \$25,380, and \$19,813 with a maximum value of \$52,553, \$50,760, and \$39,625; Mr. Townsley, RSAs of \$78,829 and RSUs granted in 2017, 2016, and 2015 of \$26,276, \$25,380, and \$19,813 with a maximum value of \$52,553, \$50,760, and \$39,625; and Mr. Kuta, RSAs of \$78,829 and RSUs granted in 2017, 2016, and 2015 of \$26,276, \$25,380, and \$14,731 with a maximum value of \$52,553, \$50,760, and \$29,462. The RSUs reported reflect the grant date fair value of the 2017 portion of the award as performance goals are set for each year of the performance period.
- (2) Amounts in this column reflect the amount paid to each executive pursuant to the performance-based short-term incentive compensation program for the applicable year.
- (3) Amounts in this column are actuarial increases or decreases in the present value of the accrued pension liability and are included in customer rates through a rate recovery mechanism. Fluctuation in the present value of the accrued pension benefit occur year-to-year due to a number of valuation assumptions including changes in the discount rate, changes in mortality rates, changes in compensation, years of service, and vesting. In 2014, the mortality assumption was updated to the RP-2014 Mortality Table, as prescribed by the Society of Actuaries in October 2014, and replaced the RP-2000 Healthy Mortality Table consistent with Section 430 of the Internal Revenue Code. The interest rate and mortality rate assumptions are consistent with those used in the Group's financial

statements and include amounts which the executives may not be entitled to receive due to vesting requirements consistent with the plans. For further information, see the “Basic and Supplemental Pension Plan Benefits” section of this Proxy Statement. Earnings on the nonqualified deferred compensation plan are noted on the Nonqualified Deferred Compensation table for those executives participating in the plan. Earnings have been excluded from this table since earnings were not at above market or at preferential rates.

- (4) All other compensation for 2017 is comprised of 401(k) matching contributions made by the Group on behalf of the executive, the personal use of company-provided vehicles and associated insurance, supplemental medical reimbursement plan, and relocation benefits. The value of the 401(k) matching contributions made by Group on behalf of the named executives was \$16,200 for all five listed executives. The reported value attributable to personal use of company-provided cars are as follows: Mr. Kropelnicki, \$12,468; Mr. Smegal, \$14,979; Ms. McGhee, \$14,321, Mr. Townsley, \$2,356, and Mr. Kuta, \$9,926. The reported values of the supplemental medical reimbursement plan are as follows: Mr. Kropelnicki, \$11,232; Mr. Smegal, \$11,232; Ms. McGhee, \$3,972; Mr. Townsley, \$11,232; and Mr. Kuta, \$11,232. Additionally, the amount for Mr. Kuta in 2017 includes a housing allowance incurred in connection with his relocation to San Jose, California as approved by the Organization and Compensation Committee.

### Grants of Plan-Based Awards for Fiscal Year Ended 2017

The table below sets forth certain information with respect to awards granted during the fiscal year ended December 31, 2017, to each of our NEOs.

Name (a)	Grant Date (b)	Estimated Payouts Under Non-Equity Incentive Plan Awards (\$) <sup>(1)</sup>			Estimated Payouts Under Equity Incentive Plan Awards <sup>(2)</sup>			All Other Stock Awards: Number of Shares of Stock or Units (#) (i)	Grant Date Fair Value of Stock and Options Awards (\$) (l)
		Threshold (\$)	Target (\$)	Maximum (\$)	Threshold (#)	Target (#)	Maximum (#)		
Martin A. Kropelnicki <sup>(3)</sup>	2/28/2017	\$0	\$786,250	\$1,572,500	0	8,223	16,446	8,223	\$604,391
Thomas F. Smegal III <sup>(3)</sup>	2/28/2017	0	85,400	170,800	0	2,145	4,290	2,145	157,658
Lynne P. McGhee <sup>(3)</sup>	2/28/2017	0	58,600	117,200	0	2,145	4,290	2,145	157,658
Paul G. Townsley <sup>(3)</sup>	2/28/2017	0	73,600	147,200	0	2,145	4,290	2,145	157,658
Robert J. Kuta <sup>(3)</sup>	2/28/2017	0	64,400	128,800	0	2,145	4,290	2,145	157,658

- (1) The threshold, target, and maximum values reported are for the performance-based short-term incentive compensation program.
- (2) The threshold, target, and maximum units reported are for the full RSU award.
- (3) The RSAs granted to the executives on February 28, 2017, pursuant to the Incentive Plan vest over three years, with one-third of the RSAs vesting on the first anniversary of the grant date and the remaining RSAs vesting in equal quarterly installments thereafter. The RSUs reported reflect the grant date fair value of the 2017 portion of the award as performance goals are set for each year of the performance period.



## Outstanding Equity Awards at Fiscal 2017 Year-End

Name (a)	Option Awards				Stock Awards		Equity Incentive Plan Awards	
	Number of Securities Underlying Unexercised Options (#) Exercisable (b)	Number of Securities Underlying Unexercised Options (#) Unexercisable (c)	Option Exercise Price (\$) (e)	Option Expiration Date (f)	Number of Shares or Units of Stock That Have Not Vested (g)	Market Value of Shares or Units of Stock That Have Not Vested (\$) <sup>(1)</sup> (h)	Number of Unearned Shares, Units or Other Rights That Have Not Vested (#) (i)	Market Value of Unearned Shares, Units or Other Rights That Have Not Vested (\$) <sup>(1)</sup> (j)
Martin A. Kropelnicki	—	—	—	—	935 <sup>(2)</sup>	42,402	11,209 <sup>(2)</sup>	508,328
	—	—	—	—	4,833 <sup>(4)</sup>	219,177	11,593 <sup>(4)</sup>	525,743
	—	—	—	—	8,223 <sup>(5)</sup>	372,913	8,223 <sup>(5)</sup>	372,913
Thomas F. Smegal III	—	—	—	—	204 <sup>(2)</sup>	9,251	2,446 <sup>(2)</sup>	110,926
	—	—	—	—	1,262 <sup>(4)</sup>	57,232	3,025 <sup>(4)</sup>	137,184
	—	—	—	—	2,145 <sup>(5)</sup>	97,276	2,145 <sup>(5)</sup>	97,276
Lynne P. McGhee	—	—	—	—	204 <sup>(2)</sup>	9,251	2,446 <sup>(2)</sup>	110,926
	—	—	—	—	1,262 <sup>(4)</sup>	57,232	3,025 <sup>(4)</sup>	137,184
	—	—	—	—	2,145 <sup>(5)</sup>	97,276	2,145 <sup>(5)</sup>	97,276
Paul G. Townsley	—	—	—	—	204 <sup>(2)</sup>	9,251	2,446 <sup>(2)</sup>	110,926
	—	—	—	—	1,262 <sup>(4)</sup>	57,232	3,025 <sup>(4)</sup>	137,184
	—	—	—	—	2,145 <sup>(5)</sup>	97,276	2,145 <sup>(5)</sup>	97,276
Robert J. Kuta	—	—	—	—	154 <sup>(3)</sup>	6,984	1,846 <sup>(3)</sup>	83,716
	—	—	—	—	1,262 <sup>(4)</sup>	57,232	3,025 <sup>(4)</sup>	137,184
	—	—	—	—	2,145 <sup>(5)</sup>	97,276	2,145 <sup>(5)</sup>	97,276

- (1) The market value of the stock awards represents the product of the closing price for the Group's common stock on the New York Stock Exchange as of December 31, 2017, which was \$45.35, and the number of shares underlying each such award.
- (2) Awards were granted on March 3, 2015, with 33.3% vesting on the first anniversary of the grant date and the remaining 66.7% vesting ratably over 24 months. RSUs are for performance periods 2015, 2016, and 2017 and vest on March 3, 2018.
- (3) Awards were granted on May 5, 2015, with 33.3% vesting on March 3, 2016 and the remaining 66.7% vesting ratably over 24 months. RSUs are for performance periods 2015, 2016, and 2017 and vest on March 3, 2018.
- (4) Awards were granted on March 1, 2016, with 33.3% vesting on March 1, 2017, and the remaining 66.7% vesting ratably over 24 months. RSUs are for performance periods 2016, 2017, and 2018 and vest on March 1, 2019.
- (5) Awards were granted on February 28, 2017, with 33.3% vesting on February 28, 2018, and the remaining 66.7% vesting ratably over 24 months. RSUs are for performance periods 2017, 2018, and 2019 and vest on February 28, 2020.

## Option Exercises and Stock Vested

### For Fiscal Year Ended 2017

Name (a)	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#) (b)	Value Realized on Exercise (\$) (c)	Number of Shares Acquired on Vesting (#) (d)	Value Realized on Vesting (\$) (e)
Martin A. Kropelnicki	—	—	26,117	\$965,594
Thomas F. Smegal III	—	—	6,329	234,088
Lynne P. McGhee	—	—	6,329	234,088
Paul G. Townsley	—	—	6,329	234,088
Robert J. Kuta	—	—	2,379	90,053

## Pension Benefits

### For Fiscal Year Ended 2017

The table below shows the present value of accumulated benefits payable to each of the NEOs, including the number of years of service credited to each executive under the California Water Service Pension Plan (“Pension Plan”) and the SERP, each of which is described elsewhere in this Proxy Statement.

Name (a)	Plan Name (b)	Number of Years Credited Service (#) <sup>(1)</sup> (c)	Present Value of Accumulated Benefit (\$) <sup>(2)</sup> (d)
Martin A. Kropelnicki President & CEO	California Water Service Pension Plan	11.80	\$ 917,514
	Supplemental Executive Retirement Plan	11.80	10,750,287
Thomas F. Smegal III Vice President, Chief Financial Officer and Treasurer	California Water Service Pension Plan	20.67	1,316,601
	Supplemental Executive Retirement Plan	15.00	3,644,997
Lynne P. McGhee Vice President, General Counsel	California Water Service Pension Plan	14.56	1,064,254
	Supplemental Executive Retirement Plan	14.56	2,526,786
Paul G. Townsley Vice President, Rates and Regulatory Matters	California Water Service Pension Plan	4.83	492,804
	Supplemental Executive Retirement Plan	4.83	1,263,554
Robert J. Kuta Vice President, Engineering	California Water Service Pension Plan	2.71	233,898
	Supplemental Executive Retirement Plan	2.71	476,852

(1) Assumptions used in the calculation of the present value are included in footnote 11 of Group’s annual report on Form 10-K filed with the SEC on March 1, 2018.

(2) Includes amounts the NEOs may not currently be entitled to receive because such amounts are not vested.

The benefits under the SERP are obtained by applying the benefit provisions of the Pension Plan, a tax-qualified plan, to all compensation included under the Pension Plan, without regard to these limits, reduced by benefits actually accrued under the Pension Plan. Under the SERP, all eligible executives are fully vested after 15 years of service and at age 60. SERP participants are eligible for early retirement starting at age 55 and would receive a reduced benefit ranging from 74% to 95% of their monthly SERP benefit upon early retirement between the ages of 55 and 60. Under the Pension Plan, all eligible employees, including executives, are fully vested after 35 years of service. The SERP is structured such that benefits are paid to executives on a “pay as you go” basis. None of the executives received any payments under the Pension Plan or SERP during 2017.

The combined maximum benefit payout under the SERP and Pension Plan achievable by an executive is 60% of the average, eligible compensation paid over the previous 36 months prior to retirement.

## Nonqualified Deferred Compensation

### For Fiscal Year Ended 2017

Name (a)	Executive Contributions in Last FY (\$) <sup>(1)</sup> (b)	Aggregate Earnings in Last FY (\$) <sup>(1)</sup> (d)	Aggregate Withdrawals/ Distributions (\$) (e)	Aggregate Balance at Last FY (\$) <sup>(2)</sup> (f)
Martin A. Kropelnicki	\$490,353	\$139,139	\$—	\$1,183,976
Thomas F. Smegal III	—	—	—	—
Lynne P. McGhee	—	3,214	—	22,579
Paul G. Townsley	40,152	20,506	—	198,790
Robert J. Kuta	3,121	576	—	6,988

(1) All of the amounts reported under “Executive Contributions in Last FY” are included in the Summary Compensation Table for 2017. None of the amounts reported under “Aggregate Earnings in Last FY” are included in the Summary Compensation Table for 2017.

(2) The amounts reported under “Aggregate Balance at Last FY” that are included in the Summary Compensation Table in years prior to 2017 are as follows: Mr. Kropelnicki, \$419,250; Mr. Townsley, \$128,581; and Mr. Kuta, \$3,161.

The Deferred Compensation Plan provides specified benefits to a select group of management and highly compensated employees who contribute materially to the continued growth, development, and future business success of the Group. The Deferred Compensation Plan permits the Group’s executives and eligible managers to defer up to 50% of their base salary. The Group does not make any contributions to the Deferred Compensation Plan. The Deferred Compensation Plan’s investment options are similar, but not identical, to the Group’s tax-qualified 401(k) plan and are funded by a Rabbi trust created for the funding of such benefits. Benefits under the Deferred Compensation Plan are payable by the Group upon separation from service with the Group either in lump sum at separation, in monthly installments over five years following separation, or in lump sum or installments commencing five years following separation.

### Potential Payments upon Termination or Change in Control

The information below describes certain compensation that would have become payable under existing plans and contractual arrangements assuming a termination of employment, or a change in control and termination of employment, had occurred on December 31, 2017, given the executive’s compensation and service levels as of such date. In addition to the benefits described below, upon any termination of employment, each of the executives would also be entitled to the benefits as described in the table of Pension Benefits for Fiscal Year 2016 and the amount shown in the column labeled “Aggregate Balance at Last FY” of the table of Nonqualified Deferred Compensation for Fiscal Year 2017 above.

On December 16, 1998, the Group adopted the Executive Severance Plan. The Executive Severance Plan provides that if within 24 months following a change in control of the Group, the executive’s employment is terminated by the Group for any reason other than good cause or by the executive for good reason, the Group will make a cash payment to the executive in an amount equal to three times such executive’s base salary on the date of the change in control or on the date that the executive’s employment terminates, whichever is greater. The payments would be paid in three equal annual installments commencing on the first of the month following the month in which the executive’s employment terminated and payable thereafter on the anniversary of the initial payment date. Each executive will also receive a

gross-up payment if the executive is required to pay an excise tax under section 4999 of the Internal Revenue Code.

Each executive's entitlement to the severance payment is conditioned upon execution of a release agreement. Additionally, the executive forfeits the right to receive the severance payment if he or she violates the non-solicitation and confidentiality provisions of the Executive Severance Plan.

For purposes of the Executive Severance Plan, the term "change in control" means the occurrence of (i) any merger or consolidation of the Group in which the Group is not the surviving organization, a majority of the capital stock of which is not owned by the stockholders of the Group immediately prior to such merger or consolidation; (ii) a transfer of all or substantially all of the assets of the Group; (iii) any other corporate reorganization in which there is a change in ownership of the outstanding shares of the Group wherein thirty percent (30%) or more of the outstanding shares of the Group are transferred to any person; (iv) the acquisition by or transfer to a person (including all affiliates or associates of such person) of beneficial ownership of capital stock of the Group if after such acquisition or transfer such person (and their affiliates or associates) is entitled to exercise thirty percent (30%) or more of the outstanding voting power of all capital stock of the Group entitled to vote in elections of directors; or (v) the election to the Board of Directors of the Group of candidates who were not recommended for election by the Board of Directors of the Group in office immediately prior to the election, if such candidates constitute a majority of those elected in that particular election.

For purposes of the Executive Severance Plan, "good cause" will be deemed to exist if (i) the applicable executive engages in acts or omissions that result in substantial harm to the business or property of the Group and that constitute dishonesty, intentional breach of fiduciary obligation, or intentional wrongdoing; or (ii) the applicable executive is convicted of a criminal violation involving fraud or dishonesty.

For purposes of the Executive Severance Plan, "good reason" will be deemed to exist if, without the applicable executive's consent, (i) there is a significant change in the nature or the scope of the applicable executive's authority or in his or her overall working environment; (ii) the applicable executive is assigned duties materially inconsistent with his or her present duties, responsibilities and status; (iii) there is a reduction in the applicable executive's rate of base salary or bonus; or (iv) the Group changes by 100 miles or more the principal location in which the applicable executive is required to perform services. Had a change in control occurred during fiscal year 2017 and had their employment been terminated on December 31, 2017, either without good cause or by the executive for good reason, the NEOs would have been eligible to receive the payments set forth in the table below.

In addition to the Executive Severance Plan, each executive is covered by the Group's general severance policy. Under the severance policy, each non-union employee of Group whose employment is terminated without cause is entitled to severance pay of either one week's pay after completing two years of service or two weeks' pay after completing five or more years of service, provided at least two weeks' notice is given. In addition, all executives are entitled to a payout of six weeks of vacation time upon any termination of employment, to be paid in a lump sum at termination. In the absence of a change in control, had their employment been terminated on December 31, 2017, without cause, the executives would have been eligible to receive the payments set forth below.

## Potential Payments upon Termination or Change in Control

Name	Change in Control and Termination of Employment Severance Amount (\$)	Termination of Employment without a Change in Control Severance Amount (\$)
Martin A. Kropelnicki	\$2,775,000	\$142,308
Thomas F. Smegal III	1,281,000	65,692
Lynne P. McGhee	879,000	45,077
Paul G. Townsley	1,104,000	49,538
Robert J. Kuta	966,000	43,346

## CEO Pay Ratio

As required by Section 953(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act, and Item 402(u) of Regulation S-K, we are providing the following information about the ratio of the annual total compensation, calculated in accordance with the requirements of Item 402(c)(2)(x) of Regulation S-K of our median compensated employee and the annual total compensation of our President & CEO, Martin A. Kropelnicki.

The 2017 annual total compensation of the median compensated of all our employees who were employed on December 30, 2017, other than our President & CEO, was \$127,258; Mr. Kropelnicki's 2017 annual total compensation was \$7,839,716, inclusive of \$4,990,347 which as previously disclosed represents the estimated present value changes in the actuarial projections of his future potential pension benefits under the groups authorized retirement plans; the ratio of these amounts was 1-to-62. Actual benefits earned are contingent upon a number of factors including years of service, age at retirement, expected life mortality tables, interest rates, and service level vesting requirements. Excluding the \$4,990,347 estimated change in present value of the actuarially projected pension benefits, the 2017 annual total compensation of both Mr. Kropelnicki's and our median compensated employee would result in 2017 annual compensation of \$2,849,367 and \$88,243 respectively, the ratio of these amounts was 1-to-32.

The SEC's rules for identifying the median compensated employee and calculating the pay ratio based on that employee's annual total compensation allow companies to adopt a variety of methodologies, to apply certain exclusions, and to make reasonable estimates and assumptions that reflect their employee populations and compensation practices. As a result, the pay ratio reported by other companies may not be comparable to the pay ratio reported above, as other companies have different employee populations and compensation practices and may utilize different methodologies, exclusions, estimates and assumptions in calculating their own pay ratios.

The pay ratio reported above is a reasonable estimate calculated in a manner consistent with SEC rules based on our payroll and employment records and the methodology described below. For these purposes, we identified the median compensated employee by first including full-time, part-time, seasonal, and temporary employees, excluding the President & CEO, for a total of 1,178 employees in the median compensation pool. We used actual salary and compensation paid in 2017, as reflected in our payroll records, excluding equity awards and bonus payments as these are not broadly distributed, to determine the median employee. We then calculated the median employee's total compensation in accordance with SEC rules to determine the pay ratio. We did not annualize the compensation for any employee who did

not work for the entire year. We identified our employee population as of December 30, 2017 based on our payroll records.

## Director Compensation

### For Fiscal Year Ended 2017

The Group's non-employee directors receive retainers comprised of both a cash award and an equity award along with meeting fees for their service. The Nominating/Corporate Governance Committee is responsible for non-employee director compensation and makes recommendations to the Board. For 2017, the Nominating/Corporate Governance retained the services of Veritas for determining non-employee director compensation.

Our 2017 director compensation program is summarized in the table below:

<b>2017 Director Compensation Program</b>	
<b>Board Retainers:</b>	
Annual Base Retainer – All Directors	\$50,000
Chairman of the Board Retainer	\$60,000
Lead Director Retainer	\$22,000
<b>Committee Chair Retainers:</b>	
Audit Committee Chair Retainer	\$15,000
Organization and Compensation Committee Chair Retainer	\$12,000
Nominating and Corporate Governance Committee Chair Retainer	\$ 9,500
Finance and Risk Management Committee Chair Retainer	\$ 7,000
<b>Board/Committee Meeting Attendance Fees:</b>	
Chairman of the Board – Board Attendance Fee	\$ 4,600
All other Directors – Board Attendance Fee	\$ 2,300
Chairman of the Board – Committee Attendance Fee	\$ 1,800
All other Directors – Committee Attendance Fees	\$ 1,800
<b>Equity:</b>	
Annual RSA Equity Grants <sup>(1)</sup>	\$72,000

(1) In 2017, non-employee directors received grants of restricted stock valued at \$72,000 as the Board retainer. The restricted stock grants were made on March 1, 2017, and were fully vested on the first anniversary of the grant date.

In September of 2017, Veritas provided assistance to the Nominating/Corporate Governance Committee in the annual review of director compensation, with recommendations based on competitive positioning, both in terms of individual compensation components and total compensation. With consideration for this review, the Nominating/Corporate Governance Committee approved increases to the foregoing amounts, effective January 1, 2018, as follows: non-employee directors will receive an annual base retainer of \$55,000 and a grant of restricted stock valued at \$80,000. The Finance and Risk Management Committee chair will receive a retainer of \$10,000, the Organization and Compensation Committee chair will receive a \$13,500 retainer, the Nominating/Corporate Governance Committee chair will receive a \$12,500 retainer, and the Audit Committee chair will receive a \$15,000 retainer. Board and committee meeting fees for the chairman and other non-employee directors will remain unchanged for 2017. The chairman will receive a Board retainer of \$55,000 and a chairman retainer of \$60,000 for 2018. The lead director will receive a \$22,000 retainer due to continued increased responsibilities, including stockholder engagement.

The Board of Directors requires non-employee directors to maintain a certain amount of stock ownership consistent with our stock ownership requirements. Pursuant to the Group's Corporate Governance Guidelines, available on the Group's website at <http://www.calwatergroup.com>, beneficial ownership of an aggregate amount of shares having a value of five times the amount of the annual base retainer is required. Non-employee directors are required to achieve the relevant ownership threshold within five years following adoption of the requirements or five years after commencing service, whichever is later. The Nominating/Corporate Governance Committee will review compliance with these requirements for non-employee directors on an annual basis.

Directors may elect to defer cash compensation payable to them under the Group's deferred compensation plan in the same manner as applicable to the Group's executives as described above. In addition, the Group maintains a Director Retirement Plan for the benefit of its non-employee directors. In December 2005, this plan was closed to new participants; however Mr. Magnuson and Mr. Vera were, at that time, participants in the plan and thus continues to accrue benefits thereunder. Under the Director Retirement Plan, a director who participates in the plan and retires after serving on the Board for a total of five or more years will receive a retirement benefit equivalent to \$22,000 per year. This benefit will be paid for the number of years the director served on the Board, up to 10 years. Amounts were paid to directors under this program in 2017 for former directors Douglas M. Brown, Robert W. Foy, Bonnie G. Hill, and Linda R. Meier.

### Non-Employee Director Compensation

Name (a)	Fees Earned or Paid in Cash (\$) (b)	Stock Awards (\$) <sup>(2)(3)</sup> (c)	Change in Pension Value and Non-Qualified Deferred Compensation Earnings (\$) <sup>(4)</sup> (f)	Total (\$) (h)
Peter C. Nelson <sup>(1)</sup> Chairman	\$174,800	\$75,705	\$ —	\$250,505
Richard P. Magnuson Lead Director	122,000	75,705	8,275	205,980
Gregory E. Aliff	83,300	75,705	—	159,005
Terry P. Bayer	79,200	75,705	—	154,905
Edwin A. Guiles	101,100	75,705	—	176,805
Bonnie G. Hill	31,334	31,164	4,922	67,420
Thomas M. Krummel, M.D.	100,700	75,705	—	176,405
Carol M. Pottenger	23,567	24,066	—	47,633
Lester A. Snow	81,500	75,705	—	157,205
George A. Vera	110,900	75,705	10,521	197,126

(1) Mr. Nelson's retainer consists of \$60,000 for his role as Chairman of the Board.

(2) Amounts reflect the full grant date fair value of each RSA granted in 2017 to the non-employee directors, calculated in accordance with FASB ASC Topic 718, disregarding estimates for forfeitures. Assumptions used in the calculation of these amounts are included in footnote 12 of Group's annual report on Form 10-K filed with the Securities and Exchange Commission on March 1, 2018.

(3) At the end of 2017, the aggregate number of RSAs held by each current non-employee director was as follows: Peter C. Nelson, 15,118; Gregory E. Aliff, 5,647; Terry P. Bayer, 9,231; Edwin A. Guiles, 25,562; Dr. Thomas M. Krummel, M.D., 19,652; Richard P. Magnuson, 28,112; Carol M. Pottenger, 573; Lester A. Snow, 15,982; and George A. Vera, 28,112.

(4) Amounts in this column represent the actuarial increase in the present value of the director benefits under the Group's Director Retirement Plan. In December 2005, this plan was closed to new participants; however, any director active in 2005 will continue to accrue benefits.

## REPORT OF THE ORGANIZATION AND COMPENSATION COMMITTEE OF THE BOARD OF DIRECTORS ON EXECUTIVE COMPENSATION

The Organization and Compensation Committee of the Group's Board of Directors has submitted the following report for inclusion in this Proxy Statement:

The Organization and Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis contained in this Proxy Statement with management. Based on our review of and the discussions with management with respect to the Compensation Discussion and Analysis, the Organization and Compensation Committee recommended to the Board of Directors that the Compensation Discussion and Analysis be included in this Proxy Statement and in the Group's annual report on Form 10-K for the fiscal year ended December 31, 2017, for filing with the SEC.

The foregoing report is provided by the following directors, who constitute the Organization and Compensation Committee:

### *ORGANIZATION AND COMPENSATION COMMITTEE*

Thomas M. Krummel, M.D., Committee Chair  
Terry P. Bayer  
Edwin A. Guiles  
Lester A. Snow

## ORGANIZATION AND COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

The following directors were members of the Organization and Compensation Committee during the 2017 fiscal year: Thomas M. Krummel, M.D., Committee Chair, Terry P. Bayer, Edwin A. Guiles, and Lester A. Snow. No member of the Organization and Compensation Committee was an executive or employee of the Group or any of its subsidiaries during 2017, nor was any such member previously an executive of the Group or any of its subsidiaries. No member of the Organization and Compensation Committee had any material interest in a transaction of the Group or a business relationship with, or any indebtedness to the Group, in each case that would require disclosure under "Procedures for Approval of Related Person Transactions" included elsewhere in this Proxy Statement.

None of the executives of the Group have served on the board of directors or on the compensation committee of any other entity, any of whose executives served either on the Board of Directors or on the Organization and Compensation Committee of the Group.

## PROCEDURES FOR APPROVAL OF RELATED PERSON TRANSACTIONS

Transactions involving related persons are reviewed on a case-by-case basis and approved as appropriate. The Board's Nominating/Corporate Governance Committee is responsible for review, approval, or ratification of "related person transactions" involving the Group or its subsidiaries and related persons. Under rules of the Securities and Exchange Commission, a related person is a director, executive, nominee for director, or a greater than 5% stockholder of the Group since the beginning of the previous fiscal year. Potential related person transactions are brought to the attention of management and the Board in a number of ways. Each of our directors and executives is instructed and periodically reminded to inform the Corporate Secretary of any potential related person transactions. In addition, each director and executive completes a questionnaire on an annual basis designed to elicit information about any potential related person transactions.

Since the beginning of 2017, there were no related person transactions under the relevant standards.



## PROPOSAL NO. 2 – ADVISORY VOTE TO APPROVE EXECUTIVE COMPENSATION

The Group is asking stockholders to vote on an advisory resolution to approve the Group's executive compensation programs as reported in this Proxy Statement in accordance with Section 14(A) of the Securities Exchange Act of 1934. The Board has adopted a policy providing for an annual advisory vote to approve executive compensation. Stockholders previously indicated their preference that the advisory vote on named executive compensation occur once every year.

At last year's Annual Meeting, 93% of the votes cast were "for" the 2016 compensation of our named executive officers as compared with 91% for the 2015 compensation and 92% for the 2014 compensation. We believe that our executive compensation program is now strongly aligned with the long-term interests of our stockholders as well as customers. As discussed in the Compensation Discussion and Analysis section of this Proxy Statement, the Board and the Organization and Compensation Committee considered the results of these "Say-on-Pay" votes and modified our executive compensation program for 2013 and continued to apply the same effective principles when making compensation decisions for 2017.

The Group's goal for its executive compensation programs is to attract, motivate, and retain talented executives who will provide leadership for the Group. The Group seeks to accomplish this goal in a way that rewards performance and is aligned with the long-term interests of customers and stockholders. The Group believes that its executive compensation programs achieve this goal.

The "Compensation Discussion and Analysis" section of this Proxy Statement describes the Group's executive compensation programs and the decisions made by the Organization and Compensation Committee for 2017 in more detail. Highlights of the programs include the following:

- *Performance-based Equity Compensation;*
- *Short-term Performance-based Incentive Compensation;*
- *No Employment Agreements;*
- *No Single Trigger Change in Control Benefits;*
- *No Tax Gross-Ups on Perquisites;*
- *Limited Perquisites;*
- *Director and Executive Stock Ownership Requirements;*
- *Clawback Policy; and*
- *Anti-hedging and Anti-pledging Policies.*

For 2017, 50% of long-term equity awards granted to our executives are in the form of RSUs subject to performance-based vesting criteria and 50% are in the form of time-based RSAs. The performance-based RSUs provide for a three-year performance period and provide for vesting based solely upon the achievement of objective performance criteria. The performance criteria are tied to the following performance metrics: water quality, customer service, plant additions, return on assets, and safety.

Further, in 2014, we introduced annual performance-based short-term incentive compensation for executives as part of the Group's executive compensation program. The Committee believes that our executive compensation program provides a good mix of short-term and long-term compensation that supports the business strategies and creates long-term stockholder value.

The Group is asking stockholders to support the named executive officer compensation as described in this Proxy Statement. The Organization and Compensation Committee and the Board believe that the policies and procedures articulated in the “Compensation Discussion and Analysis” are effective in achieving the Group’s goals and that the compensation of the Group’s named executive officers reported in this Proxy Statement has supported and contributed to the Group’s success. Accordingly, the Group asks stockholders to vote “FOR” the following resolution at the Annual Meeting:

“RESOLVED, that the stockholders of California Water Service Group approve, on an advisory basis, the compensation paid to California Water Service Group’s named executive officers, as disclosed in this Proxy Statement pursuant to the SEC’s compensation disclosure rules, including the Compensation Discussion and Analysis, the compensation tables and related narrative discussion.”

This advisory resolution, commonly referred to as a “Say-on-Pay” resolution, is not binding upon the Group, the Organization and Compensation Committee, or the Board. However, the Board and the Organization and Compensation Committee, which is responsible for designing and administering the Group’s executive compensation programs, value the opinions expressed by stockholders in their vote on this proposal and will consider the outcome of the vote when making future compensation decisions for named executive officers. After consideration of the vote of stockholders at the 2017 Annual Meeting of Stockholders and other factors, the Board decided to hold advisory votes on the approval of executive compensation annually until the next advisory vote on frequency occurs. Unless the Board modifies its policy on the frequency of future advisory votes, the advisory vote to approve the 2018 executive compensation will be held at the 2019 Annual Meeting.

### **Vote Required**

Approval of Proposal No. 2 requires the affirmative vote of a majority of the shares present in person or represented by proxy and entitled to vote at the Annual Meeting.

### **Recommendation of the Board**

Our Board of Directors unanimously recommends that you vote “FOR” this proposal.

## REPORT OF THE AUDIT COMMITTEE

The Audit Committee oversees the Group's financial reporting process on behalf of the Board of Directors. The Audit Committee's purpose and responsibilities are set forth in the Audit Committee charter. The current charter is available on the Group's website at <http://www.calwatergroup.com>. The Audit Committee consists of four members, each of whom meet the New York Stock Exchange standards for independence and the Sarbanes-Oxley Act independence standards for Audit Committee membership, and three of the Audit Committee's four members meet the requirements of an Audit Committee financial expert. During 2017, the Audit Committee met five times.

The Group's management has primary responsibility for preparing the Group's financial statements and the overall reporting process, including the Group's system of internal controls. Deloitte & Touche LLP, the Group's independent registered public accounting firm, audited the financial statements prepared by the Group and expressed their opinion that the financial statements fairly present the Group's financial position, results of operations, and cash flows in conformity with generally accepted accounting principles. Deloitte & Touche LLP also determined that the Group maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017.

In connection with the December 31, 2017 financial statements, the Audit Committee:

- (1) Reviewed and discussed the audited financial statements with management and Deloitte & Touche LLP;
- (2) Discussed with Deloitte & Touche LLP the matters required to be discussed under applicable rules of the Public Company Accounting Oversight Board;
- (3) Received from Deloitte & Touche LLP the written disclosures and the letter required by applicable rules of the Public Company Accounting Oversight Board regarding the firm's communications with the Audit Committee concerning independence, and also discussed with Deloitte & Touche LLP the firm's independence, and considered whether the firm's provision of non-audit services and the fees and costs billed for those services are compatible with Deloitte & Touche LLP's independence; and
- (4) Met privately with Deloitte & Touche LLP and the Group's internal auditor, each of whom has unrestricted access to the Audit Committee, without management present, and discussed their evaluations of the Group's internal controls and overall quality of the Group's financial reporting and accounting principles used in preparation of the financial statements. The Committee also met privately with the Group's President & CEO, the CFO and the Controller to discuss the same issues.

Based upon these reviews and discussions, the Audit Committee recommended to the Board that the audited financial statements be included in the annual report on Form 10-K to be filed with the Securities and Exchange Commission.

### *AUDIT COMMITTEE*

George A. Vera, Committee Chair  
Gregory E. Aliff  
Edwin A. Guiles  
Richard P. Magnuson

## RELATIONSHIP WITH THE INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Audit Committee is directly responsible for the appointment, compensation, retention, and oversight of the Group's independent registered public accounting firm. The Audit Committee evaluates the selection of the independent registered accounting firm each year. In addition, the Audit Committee considers the independence of the independent registered public accounting firm each year and periodically considers whether there should be a regular rotation of the independent registered public auditing firm. The Audit Committee also is involved in considering the selection of Deloitte & Touche LLP's lead engagement partner when rotation is required.

Deloitte & Touche LLP has served as the Group's independent auditor since fiscal 2008. After careful consideration of a number of factors, including the length of time the firm has served in this role, the firm's past performance, and an assessment of the firm's qualifications and resources, the Audit Committee has selected Deloitte & Touche LLP to serve as the Group's independent registered public accounting firm for the year ending December 31, 2018. The Committee's selection of Deloitte & Touche LLP as the Group's independent registered public accounting firm is being submitted for ratification by vote of the stockholders at this Annual Meeting.

The following fees relate to services provided by Deloitte & Touche LLP, the Group's independent registered public accounting firm for fiscal years 2016 and 2017.

<b>Category of Services</b>	<b>2016</b>	<b>2017</b>
Audit Fees <sup>(1)</sup>	\$1,477,500	\$1,434,268
Audit-Related Fees	0	0
Tax Fees	0	0
All Other Fees	0	221,358
<b>Total</b>	<b>1,477,500</b>	<b>1,655,626</b>

(1) The audit services included audits of the Group's annual financial statements for the years ended December 31, 2016 and 2017, and quarterly reviews of the Group's interim financial statements. Included also are fees related to the audit of the effectiveness of internal control over financial reporting.

Fees reported in the above table are those billed or expected to be billed for audit services related to that fiscal year and for other services rendered during that fiscal year.

The Audit Committee is responsible for overseeing audit fee negotiations associated with the retention of Deloitte & Touche LLP for the audit of the Group. Additionally, it is the policy of the Audit Committee, as set forth in its charter, to approve in advance all audit and permissible non-audit services to be provided by the independent registered public accounting firm, as well as related fees. Under applicable law, the Audit Committee may delegate preapproval authority to one or more of its members, and any fees preapproved in this manner must be reported to the Audit Committee at its next scheduled meeting.

## **PROPOSAL NO. 3 – RATIFICATION OF SELECTION OF DELOITTE & TOUCHE LLP AS INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM FOR 2018**

After consideration, and as a matter of good corporate governance, the Board is requesting stockholder ratification of Deloitte & Touche LLP as the independent registered public accounting firm, to audit the Group's books, records, and accounts for the year ending December 31, 2018. The members of the Audit Committee and the Board believe that the continued retention of Deloitte & Touche LLP to serve as the Group's independent registered public accounting firm is in the best interests of the Group and its stockholders. Following the recommendation of the Audit Committee, the Board recommends a vote FOR the adoption of this proposal. Representatives of Deloitte & Touche LLP will be present at the meeting to answer questions and will have an opportunity to make a statement if they desire to do so. If the stockholders do not ratify this appointment, the Audit Committee will reconsider the selection of the independent registered public accounting firm.

### **Vote Required**

Ratification of the selection of the independent registered public accounting firm for 2018 requires the affirmative vote of a majority of the shares present in person or represented by proxy and entitled to vote at the Annual Meeting.

### **Recommendation of the Board**

Our Board of Directors unanimously recommends that you vote "FOR" this proposal.

## PROPOSAL NO. 4 – APPROVAL OF THE GROUP’S 2018 EMPLOYEE STOCK PURCHASE PLAN

On February 28, 2018, the Board of Directors unanimously adopted and approved the Company’s 2018 Employee Stock Purchase Plan (Purchase Plan) and is submitting the Purchase Plan to stockholders for their adoption and approval at the Annual Meeting.

The Purchase Plan is described below.

### **Purchase Plan Background**

The purpose of the Purchase Plan is to offer employees of the Company and eligible subsidiaries the opportunity to purchase shares of Common Stock at a discounted price as an additional incentive to contribute to the prosperity of the Company.

The Committee will administer the Purchase Plan and be responsible for interpreting its provisions. It is the intention of the Company that the Purchase Plan (excluding any sub-plans thereof except as expressly provided in the terms of such sub-plan) qualify as an “Employee Stock Purchase Plan” under Section 423 of the Code, and the Purchase Plan will be administered in accordance with this intent. In addition, the Purchase Plan authorizes the grant of options pursuant to sub-plans or special rules adopted by the Committee designed to achieve desired tax or other objectives in particular locations outside of the United States or to achieve other business objectives in the determination of the Committee, which sub-plans will not be required to comply with the requirements of Section 423 of the Code or all of the specific provisions of the Purchase Plan.

Subject to adjustment as set forth in the Purchase Plan, the aggregate number of shares of Common Stock which may be issued pursuant to the Purchase Plan will be 1,500,000. The maximum number of shares of Common Stock that may be issued to any employee in a given Offering Period (as defined below) will be 2,000 shares of Common Stock. The Committee may change this limitation at any time on a prospective basis to apply to future Offering Periods.

### **Dilution**

The potential dilution from the adoption and approval of the Purchase Plan is 3.1%, based on the total shares of Common Stock outstanding as of December 31, 2017.

The following is a description of the material features of the Purchase Plan. The complete text of the Purchase Plan is attached hereto as Appendix A to this Proxy Statement. The following discussion is qualified in all respects by reference to Appendix A.

### **Eligibility**

Employees of the Company and certain subsidiaries (other than stockholders who own or have the right to acquire 5% or more of the Common Stock and, if so determined by the Committee, individuals deemed “highly compensated employees” under the Code) are eligible to participate under a specific offering period (Offering Period) under the Purchase Plan if they begin working prior to the applicable enrollment period of such Offering Period. As of the December 31, 2017, approximately 13 executive officers and 1,150 other employees of the Company and its subsidiaries were so eligible. The Committee may determine the length of each Offering Period. In the absence of such a determination, the Offering Period will be three months, and there will be no overlapping Offering Periods. No employee will be eligible to participate in the Purchase Plan if such person’s customary employment is for less than twenty (20) hours per week or for less than five (5) months per year. The Committee may establish additional administrative rules requiring that employment commence some minimum period

(not to exceed 90 days) prior to an enrollment period and/or that customary employment exceed a specified number of hours or period during a calendar year to be eligible to participate with respect to the associated Offering Period. Employees participate in the Purchase Plan by electing payroll deductions that accumulate to purchase shares at a discount. Non-employee directors are not eligible to participate in the Purchase Plan.

### **Payroll Deductions**

An employee will become a participant by completing and submitting, on or before the date prescribed by the Committee with respect to a given Offering Period, a completed payroll deduction authorization and plan enrollment form or by following an electronic or other enrollment process as prescribed by the Committee. An eligible employee may authorize payroll deductions at the rate of any whole percentage of the employee's salary, commissions, overtime, shift differentials, incentive or performance-based cash bonuses, and all or any portion of any item of compensation considered by the Company to be part of the employee's regular base earnings (excluding items not considered by the Company to be part of the employee's regular earnings). The rate of deduction cannot be less than one percent (1.0%) and cannot exceed ten percent (10.0%) (or such other percentages as the Committee may establish from time to time before an enrollment period for a future Offering Period) of the employee's eligible compensation on each payday during the Offering Period.

Under procedures and at times established by the Committee, a participant may withdraw from the Purchase Plan during an Offering Period, by completing and filing a new payroll deduction authorization and plan enrollment form with the Company or by following electronic or other procedures prescribed by the Committee. If a participant withdraws from the Purchase Plan during an Offering Period, his or her accumulated payroll deductions will be refunded without interest, his or her right to participate in the current Offering Period will be automatically terminated and no further payroll deductions for the purchase of Common Stock will be made during the Offering Period.

A participant may not increase his or her rate of contribution through payroll deductions or otherwise during a given Offering Period. A Participant may, however, decrease his or her rate of contribution through payroll deductions during a given Offering Period during such times specified by the Committee by filing a new payroll deduction authorization and plan enrollment form or by following electronic or other procedures prescribed by the Committee. To the extent necessary to comply with Section 423 of the Code for a given calendar year, the Committee may reduce a participant's payroll deductions to zero percent (0%) at any time during an Offering Period scheduled to end during such calendar year. Payroll deductions will re-commence at the rate provided in such Participant's enrollment form at the beginning of the first Offering Period which is scheduled to end in the following calendar year, unless terminated by the participant.

### **Purchase Price and Amount of Stock Purchased**

On the commencement date relating to each Offering Period, each eligible employee will be granted an option to purchase a number of whole shares of Common Stock (as may be adjusted under the Purchase Plan) established by the Committee, which may be purchased with the payroll deductions accumulated on behalf of such employee during each Offering Period at the purchase price described below. However, no employee participating in the Purchase Plan will be granted an option to purchase Common Stock under the Purchase Plan if such option would permit his or her rights to purchase stock under all employee stock purchase plans of the Company to accrue at a rate that exceeds \$25,000 of the value of such Common Stock

(determined at the time such option is granted) for each calendar year in which such option is outstanding at any time.

The purchase price under each option will be with respect to an Offering Period the lower of (i) a percentage (not less than eighty-five percent (85%)) (Designated Percentage) of the Offering Price, or (ii) the Designated Percentage of the value of a share of Common Stock on the last trading day of the Offering Period on which the Common Stock is purchased. For a given Offering Period, the Designated Percentage will be established no later than the beginning of the enrollment period for such Offering Period. The Committee may change the Designated Percentage with respect to any future Offering Period, but not to below eighty-five percent (85%), and the Committee may determine with respect to any prospective Offering Period that the purchase price will be the Designated Percentage of the value of a share of the Common Stock solely on the last trading day of the Offering Period on which the Common Stock is purchased. If the Committee does not establish the Designated Percentage prior to the beginning of the Enrollment Period for a given Offering Period, the Designated Percentage for such Offering Period shall be eighty-five percent (85%).

### **Transferability**

Neither payroll deductions credited to a participant's bookkeeping account nor any rights to exercise an option or to receive shares of Common Stock under the Purchase Plan may be voluntarily or involuntarily assigned, transferred, pledged, or otherwise disposed of in any way, and any attempted assignment, transfer, pledge, or other disposition will be null and void and without effect. If a participant in any manner attempts to transfer, assign or otherwise encumber his or her rights or interests under the Purchase Plan, other than as permitted by the Code, such act will be treated as an election by the participant to discontinue participation in the Purchase Plan.

### **Purchase Plan Amendment and Termination**

The Board or the Committee may, in its sole discretion, insofar as permitted by law, terminate or suspend the Purchase Plan, or revise or amend it in any respect whatsoever, except that, without approval of the stockholders, no such revision or amendment will increase the number of shares of Common Stock subject to the Purchase Plan, other than an adjustment in connection with a recapitalization, or make other changes for which stockholder approval is required under applicable law. Upon a termination or suspension of the Purchase Plan, the Board may in its discretion (i) return without interest, the payroll deductions credited to participants' accounts to such participants or (ii) set an earlier purchase date with respect to an offering period then in progress.

### **New Plan Benefits**

The actual number of shares of Common Stock that may be purchased by any individual under the Purchase Plan is not determinable in advance because the number is generally calculated using the contributed amount and the purchase price.

### **Federal Income Tax Information**

The following information is a general summary of some of the current federal income tax consequences of the Purchase Plan to U.S. based participants and to the Company. Tax laws may change, and actual tax consequences will depend on a participant's individual circumstances as well as state and local tax laws. We encourage all participants to seek tax advice when they participate in the Purchase Plan. The Purchase Plan is intended to qualify as an "employee stock purchase plan" under Section 423 of the Internal Revenue Code.



*Tax Treatment of U.S. Participants.* Participants will not recognize income when they enroll in the Purchase Plan or when they purchase shares. All tax consequences are deferred until the participant disposes of the shares. If the participant does not dispose of the shares within one year after the purchase date or two years after the offering date, or if the participant dies while owning the shares, the participant will generally recognize ordinary income when disposing of the shares equal to the difference between the purchase price and the fair market value of the shares on the date of disposition, or 15% (or such lesser discount as the Committee may establish) of the fair market value of the shares on the offering date, whichever is less. Any additional gain will be taxed as long-term capital gain. If the shares are sold for less than the purchase price, there is no ordinary income, but the participant will have a long-term capital loss for the difference between the purchase price and the sale price. If a participant disposes of the shares within one year after the purchase date or two years after the offering date, the participant will generally have ordinary income equal to the difference between the purchase price and the fair market value on the purchase date. The difference between the fair market value of the shares on the date of disposition and the fair market value on the purchase date will be a capital gain or loss.

*Tax Treatment of the Company.* When a participant recognizes ordinary income by disposing of shares before the one-year or two-year holding period ends, the Company will generally be entitled to a tax deduction in the amount of the ordinary income.

### **Vote Required**

Approval of the Purchase Plan requires the affirmative vote of a majority of the shares present or represented by proxy and entitled to vote at the Annual Meeting. In addition, in accordance with the listing requirements of the New York Stock Exchange, approval of the Purchase Plan requires the affirmative vote of a majority of the votes cast on the proposal at the Annual Meeting. Abstentions will have the effect of a vote against the proposal, whereas broker non-votes will not count as votes cast for this purpose and will therefore have no effect on the outcome of the proposal.

### **Recommendation of the Board**

Our Board of Directors unanimously recommends that you vote "FOR" this proposal.

## EQUITY COMPENSATION PLAN INFORMATION

The following table represents securities authorized to be issued under the Group's equity compensation plans, as of December 31, 2017.

<b>Plan Category</b>	<b>Number of Securities to be Issued Upon Exercise of Outstanding Rights (a)</b>	<b>Weighted-Average Exercise Price of Outstanding Rights</b>	<b>Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plan (Excluding Securities Reflected in Column) (a)</b>
Equity compensation plans approved by security holders	—	\$—	808,290
Equity compensation plans not approved by security holders	—	—	—
<b>Total</b>	—	\$—	808,290

## OTHER MATTERS

### **Adjournment**

Notice of adjournment need not be given if the date, time, and place thereof are announced at the Annual Meeting at which the adjournment is taken. However, if the adjournment is for more than 30 days, or if a new record date is fixed for the adjourned Annual Meeting, a notice of the adjourned Annual Meeting will be given to each stockholder entitled to vote at the Annual Meeting. At adjourned annual meetings, any business may be transacted that might have been transacted at the original Annual Meeting.

### **Cost of Proxy Solicitation**

The Group will bear the entire cost of preparing, assembling, printing, and mailing this Proxy Statement, the proxies, and any additional materials which may be furnished by the Board to stockholders. The solicitation of proxies will be made by the use of the U.S. Postal Service and also may be made by telephone, or personally, by directors, officers, and regular employees of the Group, who will receive no extra compensation for such services. Morrow Sodali, LLC, 470 West Avenue, Stamford, CT 06902 was hired to assist in the distribution of proxy materials and solicitation of votes for a \$9,000 fee, plus distribution expenses. The Group will reimburse brokerage houses and other custodians, nominees, and fiduciaries for their reasonable out-of-pocket expenses for forwarding proxy and solicitation materials to stockholders.

### **Other Matters**

The Board is not aware of any other matters to come before the Annual Meeting. If any other matters should be brought before the meeting or any adjournment or postponement thereof, upon which a vote properly may be taken, the proxy holders will vote in their discretion unless otherwise provided in the proxies. The report of the Organization and Compensation Committee, and the report of the Audit Committee, are not to be considered as incorporated by reference into any other filings that the Group makes with the SEC under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended. These portions of this Proxy Statement are not a part of any of those filings unless otherwise stated in those filings.

### **Code of Ethics**

The Group has adopted written codes of ethics for all directors, officers, and employees. The codes are posted on the Group's website at <http://www.calwatergroup.com>. The codes are also available in written form upon request to the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, California 95112-4598.

### **Stockholders Sharing an Address**

The SEC allows the Group to deliver a single proxy statement and annual report to an address shared by two or more of our stockholders. This delivery method, referred to as "householding," can result in significant cost savings for the Group. In order to take advantage of this opportunity, banks and brokerage firms that hold shares for stockholders who are the beneficial owners, but not the record holders, of the Group's shares, have delivered only one proxy statement and annual report to multiple stockholders who share an address, unless one or more of the stockholders has provided contrary instructions. For stockholders who are the record holders of the Group's shares, the Group may follow a similar process absent contrary instructions. The Group will deliver promptly, upon written or oral request, a separate copy of the proxy statement and annual report to a stockholder at a shared address to which a single

copy of the documents was delivered. A stockholder who wishes to receive a separate copy of the proxy statement and annual report, now or in the future, may obtain one, without charge, by addressing a request to the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, California 95112-4598 or calling (408) 367-8200. Stockholders of record sharing an address who are receiving multiple copies of proxy materials and annual reports and wish to receive a single copy of such materials in the future should submit their request by contacting the Group in the same manner. If you are the beneficial owner, but not the record holder, of the Group's shares and wish to receive only one copy of the proxy statement and annual report in the future, you will need to contact your broker, bank, or other nominee to request that only a single copy of each document be mailed to all stockholders at the shared address in the future.

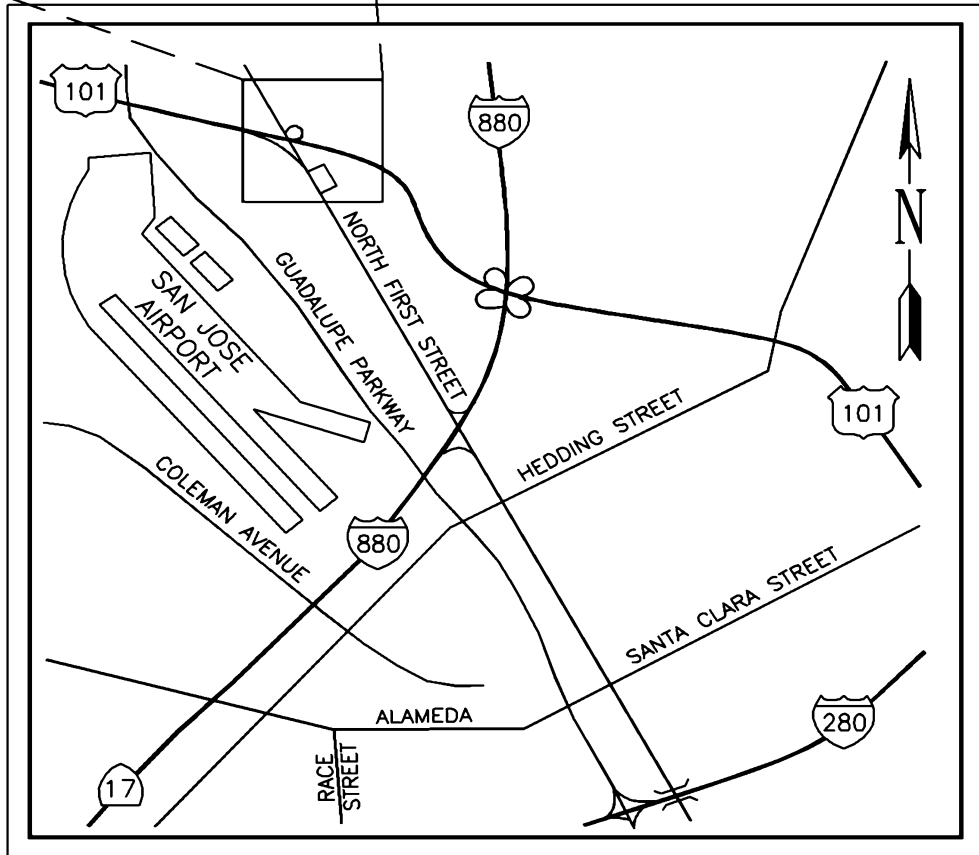
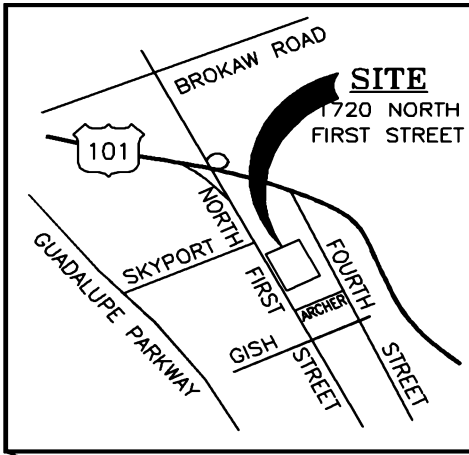
#### **Copies of Annual Report on Form 10-K**

The Group, upon request, will furnish to record and beneficial holders of its common stock, free of charge, a copy of its Annual Report on Form 10-K (including financial statements and schedules but without exhibits) for fiscal year 2017. Copies of exhibits to Form 10-K also will be furnished upon request for a payment of a fee of \$0.50 per page. All requests should be directed to the Corporate Secretary, California Water Service Group, 1720 North First Street, San Jose, California 95112-4598.

Electronic copies of the Group's Form 10-K, including exhibits and this Proxy Statement will be available on the Group's website at <http://www.calwatergroup.com>.

#### **Disclaimer Regarding Website**

The information contained on the Group's website is not to be deemed included or incorporated by reference into this Proxy Statement.



**California Water Service Group**

California Water Service Company,  
Hawaii Water Service Company,  
New Mexico Water Service Company,  
Washington Water Service Company,  
CWS Utility Services, and  
HWS Utility Services  
1720 North First Street  
San Jose, CA 95112-4598  
(408) 367-8200

# APPENDIX A

## CALIFORNIA WATER SERVICE GROUP

### 2018 EMPLOYEE STOCK PURCHASE PLAN

#### Section 1. PURPOSE

The purpose of the Plan is to provide an opportunity for Employees of California Water Service Group, a Delaware corporation ("*Sponsor*") and its Participating Subsidiaries (collectively *Sponsor* and its Participating Subsidiaries shall be referred to as the "*Company*"), to purchase Common Stock of *Sponsor* and thereby to have an additional incentive to contribute to the prosperity of the *Company*. It is the intention of the *Company* that the Plan (excluding any sub-plans thereof except as expressly provided in the terms of such sub-plan) qualify as an "*Employee Stock Purchase Plan*" under Section 423 of the U.S. Internal Revenue Code of 1986, as amended (the "*Code*"), and the Plan shall be administered in accordance with this intent. In addition, the Plan authorizes the grant of options pursuant to sub-plans or special rules adopted by the Committee designed to achieve desired tax or other objectives in particular locations outside of the United States or to achieve other business objectives in the determination of the Committee, which sub-plans shall not be required to comply with the requirements of Section 423 of the Code or all of the specific provisions of the Plan, including but not limited to terms relating to eligibility, Offering Periods or Purchase Price.

#### Section 2. DEFINITIONS

- (a) "*Applicable Law*" shall mean the legal requirements relating to the administration of an employee stock purchase plan under applicable U.S. state corporate laws, U.S. federal and applicable state securities laws, the Code, any stock exchange rules or regulations and the applicable laws of any other country or jurisdiction, as such laws, rules, regulations and requirements shall be in place from time to time.
- (b) "*Board*" shall mean the Board of Directors of *Sponsor*.
- (c) "*Code*" shall mean the Internal Revenue Code of 1986, as such is amended from time to time, and any reference to a section of the Code shall include any successor provision of the Code.
- (d) "*Commencement Date*" shall mean, with respect to a given Offering Period, the first Trading Day during such Offering Period.
- (e) "*Committee*" shall mean the Compensation Committee of the Board (or any successor committee) or the officer, officers or committee appointed by the Compensation Committee in accordance with Section 15 of the Plan (to the extent of the duties and responsibilities delegated by the Compensation Committee of the Board).
- (f) "*Common Stock*" shall mean the common stock of *Sponsor*, par value \$[.01] per share, or any securities into which such Common Stock may be converted.
- (g) "*Compensation*" shall mean the total compensation paid by the *Company* to an Employee with respect to an Offering Period, including salary, commissions, overtime, shift differentials, performance-based cash bonuses, and all or any portion of any item of compensation considered by the *Company* to be part of the Employee's regular earnings, but excluding items not considered by the *Company* to be part of the Employee's regular earnings. Items excluded from the definition of "*Compensation*" include but are not limited to such items as relocation bonuses, expense reimbursements, certain bonuses paid

in connection with mergers and acquisitions, author incentives, recruitment and referral bonuses, foreign service premiums, differentials and allowances, imputed income pursuant to Section 79 of the Code, income realized as a result of participation in any stock option, restricted stock, restricted stock unit, stock purchase or similar equity plan maintained by Sponsor or a Participating Subsidiary, and tuition and other reimbursements. The Committee shall have the authority to determine and approve all forms of pay to be included in the definition of Compensation and may change the definition on a prospective basis.

- (h) *"Effective Date"* shall mean February 28, 2018, the date upon which the Plan was adopted by the Board.
- (i) *"Employee"* shall mean an individual classified as an employee (within the meaning of Code Section 3401(c) and the regulations thereunder) by Sponsor or a Participating Subsidiary on Sponsor's or such Participating Subsidiary's payroll records during the relevant participation period. Notwithstanding the foregoing, no employee of Sponsor or a Participating Subsidiary shall be included within the definition of "Employee" if such person's customary employment is for less than twenty (20) hours per week or for less than five (5) months per year. Individuals classified as independent contractors, consultants or advisers are not considered "Employees."
- (j) *"Enrollment Period"* shall mean, with respect to a given Offering Period, that period established by the Committee prior to the commencement of such Offering Period during which Employees may elect to participate in order to purchase Common Stock at the end of that Offering Period in accordance with the terms of this Plan.
- (k) *"Exchange Act"* shall mean the Securities Exchange Act of 1934, as amended from time to time, and any reference to a section of the Exchange Act shall include any successor provision of the Exchange Act.
- (l) *"Market Value"* on a given date of determination (e.g., a Commencement Date or Purchase Date, as appropriate) means, as of any date, the value of the Common Stock determined as follows:
  - (i) If the Common Stock is listed on any established stock exchange or traded on any established market, the Market Value of a share of Common Stock as of any date of determination will be, unless otherwise determined by the Board or Committee, the closing sales price for such stock as quoted on such exchange or market (or the exchange or market with the greatest volume of trading in the Common Stock) on the date of determination, as reported in a source the Board or Committee deems reliable.
  - (ii) Unless otherwise provided by the Board or Committee, if there is no closing sales price for the Common Stock on the date of determination, then the Market Value will be the closing selling price on the last preceding date for which such quotation exists.
  - (iii) In the absence of such markets for the Common Stock, the Market Value will be determined by the Board or Committee in good faith.
- (m) *"Offering Period"* shall mean a period of no more than twenty-seven (27) months at the end of which an option granted pursuant to the Plan shall be exercised. The Plan shall be implemented by a series of Offering Periods with terms established by the Committee in accordance with the Plan. Once established, the duration and timing of Offering Periods may be changed or modified by the Committee as permitted by the Plan. If the Committee does not establish different rules with respect to an Offering Period, then the duration of an Offering Period shall be three (3) months and there shall be no overlapping Offering Periods.

- (n) *"Offering Price"* shall mean the Market Value of a share of Common Stock on the Commencement Date for a given Offering Period.
- (o) *"Participant"* shall mean a participant in the Plan as described in Section 5 of the Plan.
- (p) *"Participating Subsidiary"* shall mean a Subsidiary that has been designated by the Committee in its sole discretion as eligible to participate in the Plan with respect to its Employees.
- (q) *"Plan"* shall mean this 2018 Employee Stock Purchase Plan, including any sub-plans or appendices hereto.
- (r) *"Purchase Date"* shall mean the last Trading Day of each Offering Period.
- (s) *"Purchase Price"* shall have the meaning set out in Section 8(b).
- (t) *"Securities Act"* shall mean the U.S. Securities Act of 1933, as amended, as amended from time to time, and any reference to a section of the Securities Act shall include any successor provision of the Securities Act.
- (u) *"Stockholder"* shall mean a record holder of shares entitled to vote such shares of Common Stock under Sponsor's by-laws.
- (v) *"Subsidiary"* shall mean any entity treated as a corporation (other than Sponsor) in an unbroken chain of corporations beginning with Sponsor, within the meaning of Code Section 424(f), whether or not such corporation now exists or is hereafter organized or acquired by Sponsor or a Subsidiary.
- (w) *"Trading Day"* shall mean a day on which U.S. national stock exchanges are open for trading and the Common Stock is being publicly traded on one or more of such markets.

### Section 3. ELIGIBILITY

- (a) Any Employee employed by Sponsor or by any Participating Subsidiary at the beginning of an Enrollment Period for a given Offering Period shall be eligible to participate in the Plan with respect to such Offering Period and future Offering Periods, provided that the Committee may establish administrative rules requiring that employment commence some minimum period (not to exceed 90 days) prior to an Enrollment Period and/or that customary employment exceed a specified number of hours or period during a calendar year to be eligible to participate with respect to the associated Offering Period. The Committee may also determine that a designated group of highly compensated Employees is ineligible to participate in the Plan so long as the excluded category fits within the definition of "highly compensated employee" in Code Section 414(q). If the Committee does not establish different rules with respect to an Offering Period, the minimum period of employment that must be completed prior to the beginning of an Enrollment Period shall be twenty (20) working days.
- (b) No Employee may participate in the Plan if immediately after an option is granted the Employee owns or is considered to own (within the meaning of Code Section 424(d)) shares of Common Stock, including Common Stock which the Employee may purchase by conversion of convertible securities or under outstanding options granted by Sponsor or its Subsidiaries, possessing five percent (5%) or more of the total combined voting power or value of all classes of stock of Sponsor or of any of its Subsidiaries. All Employees who participate in the Plan shall have the same rights and privileges under the Plan, except for differences that may be mandated by local law and that are consistent with Code Section 423(b)(5); provided that individuals participating in a sub-plan adopted pursuant to Section 16 which is not designed to qualify under Code Section 423 need not have the



same rights and privileges as Employees participating in the Code Section 423 Plan. No Employee may participate in more than one Offering Period at a time.

#### Section 4. OFFERING PERIODS

The Plan shall be implemented by a series of Offering Periods, which shall possess terms specified by the Committee in accordance with the terms of the Plan. Offering Periods shall continue until the Plan is terminated pursuant to Section 14 hereof. Once established, the Committee shall have the authority to change the frequency and/or duration of Offering Periods (including the Commencement Dates thereof) with respect to future Offering Periods if such change is announced prior to the scheduled occurrence of the Enrollment Period for the first Offering Period to be affected thereafter. If the Committee does not establish different rules with respect to an Offering Period, then the duration of an Offering Period shall be three (3) months and there shall be no overlapping Offering Periods.

#### Section 5. PARTICIPATION

- (a) An Employee who is eligible to participate in the Plan in accordance with its terms at the beginning of an Enrollment Period for an Offering Period and elects to participate in such Offering Period shall automatically receive an option in accordance with Section 8(a). Such an Employee shall become a Participant by completing and submitting, on or before the date prescribed by the Committee with respect to a given Offering Period, a completed payroll deduction authorization and Plan enrollment form provided by Sponsor or its Participating Subsidiaries or by following an electronic or other enrollment process as prescribed by the Committee. An eligible Employee may authorize payroll deductions at the rate of any whole percentage of the Employee's Compensation, not to be less than one percent (1.0%) and not to exceed ten percent (10.0%) of the Employee's Compensation (or such other percentages as the Committee may establish from time to time before an Enrollment Period for a future Offering Period) on each payday during the Offering Period. All payroll deductions will be held in a general corporate account or a trust account. No interest shall be paid or credited to the Participant with respect to such payroll deductions. Sponsor shall maintain or cause to be maintained a separate bookkeeping account for each Participant under the Plan and the amount of each Participant's payroll deductions shall be credited to such account. A Participant may not make any additional payments into such account, unless payroll deductions are prohibited under Applicable Law, in which case the provisions of Section 5(b) of the Plan shall apply.
- (b) Notwithstanding any other provisions of the Plan to the contrary, in locations where local law prohibits payroll deductions, an eligible Employee may elect to participate through contributions to his or her account under the Plan in a form acceptable to the Committee. In such event, any such Employees shall be deemed to be participating in a sub-plan, unless the Committee otherwise expressly provides that such Employees shall be treated as participating in the Plan.
- (c) Under procedures and at times established by the Committee, a Participant may withdraw from the Plan during an Offering Period, by completing and filing a new payroll deduction authorization and Plan enrollment form with the Company or by following electronic or other procedures prescribed by the Committee. If a Participant withdraws from the Plan during an Offering Period, his or her accumulated payroll deductions will be refunded to the Participant without interest, his or her right to participate in the current Offering Period will be automatically terminated and no further payroll deductions for the purchase of Common Stock will be made during the Offering Period. Any Participant who wishes to withdraw from the Plan during an Offering Period, must complete the withdrawal procedures prescribed by the Committee, subject to any rules established by the

Committee, or changes to such rules, pertaining to the timing of withdrawals, limiting the frequency with which Participants may withdraw and re-enroll in the Plan, or imposing a waiting period on Participants wishing to re-enroll following withdrawal.

- (d) A Participant may not increase his or her rate of contribution through payroll deductions or otherwise during a given Offering Period. A Participant may decrease his or her rate of contribution through payroll deductions during a given Offering Period during such times specified by the Committee by filing a new payroll deduction authorization and Plan enrollment form or by following electronic or other procedures prescribed by the Committee. If a Participant has not followed such procedures to change the rate of contribution, the rate of contribution shall continue at the originally elected rate throughout the Offering Period and future Offering Periods. Notwithstanding the foregoing, to the extent necessary to comply with Section 423(b)(8) of the Code for a given calendar year, the Committee may reduce a Participant's payroll deductions to zero percent (0%) at any time during an Offering Period scheduled to end during such calendar year. Payroll deductions shall re-commence at the rate provided in such Participant's enrollment form at the beginning of the first Offering Period which is scheduled to end in the following calendar year, unless terminated by the Participant as provided in Section 5(c).

#### Section 6. TERMINATION OF EMPLOYMENT

In the event any Participant terminates employment with Sponsor and its Participating Subsidiaries for any reason (including death) prior to the expiration of an Offering Period, the Participant's participation in the Plan shall terminate and all amounts credited to the Participant's account shall be paid to the Participant or, in the case of death, to the Participant's heirs or estate, without interest. Whether a termination of employment has occurred shall be determined by the Committee. If a Participant's termination of employment occurs within a certain period of time as specified by the Committee (not to exceed 30 days) prior to the Purchase Date of the Offering Period then in progress, his or her option for the purchase of shares of Common Stock will be exercised on such Purchase Date in accordance with Section 9 as if such Participant were still employed by the Company. If the Committee does not establish different rules with respect to an Offering Period, then if a Participant's termination of employment occurs on or after the fifth (5<sup>th</sup>) working day preceding the Purchase Date of an Offering Period, then his or her option for the purchase of shares of Common Stock will be exercised on such Purchase Date in accordance with Section 9 as if such Participant were still employed by the Company. Following the purchase of shares on such Purchase Date, the Participant's participation in the Plan shall terminate and all amounts credited to the Participant's account shall be paid to the Participant or, in the case of death, to the Participant's heirs or estate, without interest. The Committee may also establish rules regarding when leaves of absence or changes of employment status will be considered to be a termination of employment, including rules regarding transfer of employment among Participating Subsidiaries, Subsidiaries and Sponsor, and the Committee may establish termination-of-employment procedures for this Plan that are independent of similar rules established under other benefit plans of Sponsor and its Subsidiaries; provided that such procedures are not in conflict with the requirements of Section 423 of the Code.

#### Section 7. STOCK

Subject to adjustment as set forth in Section 11, the aggregate number of shares of Common Stock which may be issued pursuant to the Plan shall be one million five hundred thousand (1,500,000) shares (the "Share Reserve").

Notwithstanding the above, subject to adjustment as set forth in Section 11, the maximum number of shares of Common Stock that may be issued to any Employee in a given Offering

Period shall be two thousand (2,000) shares of Common Stock. The Committee may change this limitation at any time on a prospective basis to apply to future Offering Periods. If, on a given Purchase Date, the number of shares with respect to which options are to be exercised exceeds either maximum, the Committee shall make, as applicable, such adjustment or pro rata allocation of the shares remaining available for purchase in as uniform a manner as shall be practicable and as it shall determine to be equitable.

#### Section 8. OFFERING

- (a) On the Commencement Date relating to each Offering Period, each eligible Employee, whether or not such Employee has elected to participate as provided in Section 5(a), shall be granted an option to purchase a number of whole shares of Common Stock (as adjusted as set forth in Section 11) established by the Committee, which may be purchased with the payroll deductions accumulated on behalf of such Employee during each Offering Period at the purchase price specified in Section 8(b) below, subject to the additional limitation that no Employee participating in the Plan shall be granted an option to purchase Common Stock under the Plan if such option would permit his or her rights to purchase stock under all employee stock purchase plans (described in Section 423 of the Code) of Sponsor and its Subsidiaries to accrue at a rate which exceeds U.S. twenty-five thousand dollars (U.S. \$25,000) of the Market Value of such Common Stock (determined at the time such option is granted) for each calendar year in which such option is outstanding at any time. For purposes of the Plan, an option is "*granted*" on a Participant's Commencement Date. An option will expire upon the earliest to occur of (i) the termination of a Participant's participation in the Plan or such Offering Period (ii) the beginning of a subsequent Offering Period in which such Participant is participating; or (iii) the termination of the Offering Period. This Section 8(a) shall be interpreted so as to comply with Code Section 423(b)(8).
- (b) The Purchase Price under each option shall be with respect to an Offering Period the lower of (i) a percentage (not less than eighty-five percent (85%)) ("*Designated Percentage*") of the Offering Price, or (ii) the Designated Percentage of the Market Value of a share of Common Stock on the Purchase Date on which the Common Stock is purchased; provided that the Purchase Price may be adjusted by the Committee pursuant to Sections 11 or 12 in accordance with Section 424(a) of the Code. For a given Offering Period, the Designated Percentage shall be established no later than the beginning of the Enrollment Period for such Offering Period. The Committee may change the Designated Percentage with respect to any future Offering Period, but not to below eighty-five percent (85%), and the Committee may determine with respect to any prospective Offering Period that the Purchase Price shall be the Designated Percentage of the Market Value of a share of the Common Stock solely on the Purchase Date. If the Committee does not establish the Designated Percentage prior to the beginning of the Enrollment Period for a given Offering Period, the Designated Percentage for such Offering Period shall be ninety percent (90%).

#### Section 9. PURCHASE OF STOCK

Unless a Participant withdraws from the Plan as provided in Section 5(c), terminates employment prior to the end of an Offering Period as provided in Section 6, or except as provided in Sections 7, 12 or 14(b), upon the expiration of each Offering Period, a Participant's option shall be exercised automatically for the purchase of that number of whole shares of Common Stock which the accumulated payroll deductions credited to the Participant's account at that time shall purchase at the applicable price specified in Section 8(b) in accordance with the terms of the Plan, including Section 7. Notwithstanding the foregoing, Sponsor or its Participating Subsidiary may make such provisions and take such action as it deems necessary or

appropriate for the withholding of taxes and/or social insurance and/or other amounts which Sponsor or its Participating Subsidiary determines is required by Applicable Law. Each Participant, however, shall be responsible for payment of all individual tax liabilities arising under the Plan. The shares of Common Stock purchased upon exercise of an option hereunder shall be considered for tax purposes to be sold to the Participant on the Purchase Date. A Participant's option to purchase shares of Common Stock hereunder is exercisable only by him or her.

#### Section 10. PAYMENT AND DELIVERY

As soon as practicable after the exercise of an option, Sponsor shall deliver or cause to have delivered to the Participant a record of the Common Stock purchased and the balance of any amount of payroll deductions credited to the Participant's account not used for the purchase of Common Stock, except as specified below. The Committee may permit or require that shares be deposited directly with a broker designated by the Committee or to a designated agent of the Company, and the Committee may utilize electronic or automated methods of share transfer. The Committee may require that shares be retained with such broker or agent for a designated period of time and/or may establish other procedures to permit tracking of disqualifying dispositions of such shares. Sponsor or its Participating Subsidiary shall retain the amount of payroll deductions used to purchase Common Stock as full payment for the Common Stock and the Common Stock shall then be fully paid and non-assessable. No Participant shall have any voting, dividend, or other Stockholder rights with respect to shares subject to any option granted under the Plan until the shares subject to the option have been purchased and delivered to the Participant as provided in this Section 10. The Committee may in its discretion direct Sponsor to retain in a Participant's account for the subsequent Offering Period any payroll deductions which are not sufficient to purchase a whole share of Common Stock or return such amount to the Participant. Any other amounts remaining in a Participant's account after a Purchase Date shall be returned to the Participant. If the Committee does not establish different rules with respect to an Offering Period, then all amounts remaining in a Participant's account after a Purchase Date which are not sufficient to purchase a whole share of Common Stock shall be retained in a Participant's account for the subsequent Offering Period.

#### Section 11. RECAPITALIZATION

Subject to any required action by the Stockholders of Sponsor, if there is any change in the outstanding shares of Common Stock or other securities of Sponsor because of a merger, consolidation, spin-off, reorganization, recapitalization, dividend in property other than cash, extraordinary dividend whether in cash and/or other property, stock split, reverse stock split, stock dividend, liquidating dividend, combination or reclassification of the Common Stock or other securities (including any such change in the number of shares of Common Stock or other securities effected in connection with a change in domicile of Sponsor), or any other increase or decrease in the number of shares of Common Stock or other securities effected without receipt of consideration by Sponsor, provided that conversion of any convertible securities of Sponsor shall not be deemed to have been "*effected without receipt of consideration*," the type and number of securities covered by each option under the Plan which has not yet been exercised and the type and number of securities which have been authorized and remain available for issuance under the Plan, as well as the maximum number of securities which may be purchased by a Participant in an Offering Period, and the price per share covered by each option under the Plan which has not yet been exercised, shall be appropriately and proportionally adjusted by the Board, and the Board shall take any further actions which, in the exercise of its discretion, may be necessary or appropriate under the circumstances. The Board's determinations under this Section 11 shall be conclusive and binding on all parties.

## 12. MERGER, LIQUIDATION, OTHER CORPORATE TRANSACTIONS

- (a) In the event of the proposed liquidation or dissolution of Sponsor, the Offering Period will terminate immediately prior to the consummation of such proposed transaction, unless otherwise provided by the Board in its sole discretion, and all outstanding options shall automatically terminate and the amounts of all payroll deductions will be refunded without interest to the Participants.
- (b) In the event of a proposed sale of all or substantially all of the assets of Sponsor, or the merger or consolidation or similar combination of Sponsor with or into another entity, then in the sole discretion of the Board, (1) each option shall be assumed or an equivalent option shall be substituted by the successor corporation or parent or subsidiary of such successor entity, (2) on a date established by the Board on or before the date of consummation of such merger, consolidation, combination or sale, such date shall be treated as a Purchase Date, and all outstanding options shall be exercised on such date, (3) all outstanding options shall terminate and the accumulated payroll deductions will be refunded without interest to the Participants, or (4) outstanding options shall continue unchanged.

## Section 13. TRANSFERABILITY

Neither payroll deductions credited to a Participant's bookkeeping account nor any rights to exercise an option or to receive shares of Common Stock under the Plan may be voluntarily or involuntarily assigned, transferred, pledged, or otherwise disposed of in any way, and any attempted assignment, transfer, pledge, or other disposition shall be null and void and without effect. If a Participant attempts to transfer, assign or otherwise encumber his or her rights or interests under the Plan, other than as permitted by the Code, such act shall be treated as an election by the Participant to discontinue participation in the Plan pursuant to Section 5(c).

## Section 14. AMENDMENT OR TERMINATION OF THE PLAN

- (a) The Plan shall continue from the Effective Date until the time that the Plan is terminated in accordance with Section 14(b).
- (b) The Board or the Committee may, in its sole discretion, insofar as permitted by law, terminate or suspend the Plan, or revise or amend it in any respect whatsoever, except that, without approval of the Stockholders, no such revision or amendment shall increase the number of shares subject to the Plan, other than an adjustment under Section 11 of the Plan, or make other changes for which Stockholder approval is required under Applicable Law. Upon a termination or suspension of the Plan, the Board may in its discretion (i) return without interest, the payroll deductions credited to Participants' accounts to such Participants or (ii) set an earlier Purchase Date with respect to an Offering Period then in progress.

## Section 15. ADMINISTRATION

- (a) The Board has appointed the Compensation Committee of the Board to administer the Plan (the "*Committee*"), who will serve for such period of time as the Board may specify and whom the Board may remove at any time. The Committee will have the authority and responsibility for the day-to-day administration of the Plan, the authority and responsibility specifically provided in this Plan and any additional duty, responsibility and authority delegated to the Committee by the Board, which may include any of the functions assigned to the Board in this Plan. The Committee may delegate to a sub-committee and/or to an officer or officers or employees of Sponsor the day-to-day administration of the Plan. The Committee shall have full power and authority to adopt, amend and rescind any rules and regulations which it deems desirable and appropriate for the proper administration of

the Plan, to construe and interpret the provisions and supervise the administration of the Plan, to make factual determinations relevant to Plan entitlements and to take all action in connection with administration of the Plan as it deems necessary or advisable, consistent with the delegation from the Board. Decisions of the Committee shall be final and binding upon all Participants. Any decision reduced to writing and signed by a majority of the members of the Committee shall be fully effective as if it had been made at a meeting of the Committee duly held. The Company shall pay all expenses incurred in the administration of the Plan.

- (b) In addition to such other rights of indemnification as they may have as members of the Board or officers or employees of the Company, members of the Board and of the Committee and their delegates shall be indemnified by the Company against all reasonable expenses, including attorneys' fees, actually and necessarily incurred in connection with the defense of any action, suit or proceeding, or in connection with any appeal therein, to which they or any of them may be a party by reason of any action taken or failure to act under or in connection with the Plan, or any right granted under the Plan, and against all amounts paid by them in settlement thereof (provided such settlement is approved by independent legal counsel selected by the Sponsor) or paid by them in satisfaction of a judgment in any such action, suit or proceeding, except in relation to matters as to which it shall be adjudged in such action, suit or proceeding that such person is liable for gross negligence, bad faith or intentional misconduct in duties; provided, however, that within sixty (60) days after the institution of such action, suit or proceeding, such person shall offer to the Company, in writing, the opportunity at its own expense to handle and defend the same.

#### Section 16. COMMITTEE RULES FOR FOREIGN JURISDICTIONS

The Committee may adopt rules or procedures relating to the operation and administration of the Plan to accommodate the specific requirements of local laws and procedures. Without limiting the generality of the foregoing, the Committee is specifically authorized to adopt rules and procedures regarding handling of payroll deductions or other contributions by Participants, payment of interest, conversion of local currency, data privacy security, payroll tax, withholding procedures and handling of stock certificates which vary with local requirements; however, if such varying provisions are not in accordance with the provisions of Section 423(b) of the Code, including but not limited to the requirement of Section 423(b)(5) of the Code that all options granted under the Plan shall have the same rights and privileges unless otherwise provided under the Code and the regulations promulgated thereunder, then the individuals affected by such varying provisions shall be deemed to be participating under a sub-plan and not in the Plan. The Committee may also adopt sub-plans applicable to particular Subsidiaries or locations, which sub-plans may be designed to be outside the scope of Code Section 423 and shall be deemed to be outside the scope of Code Section 423, unless the terms of the sub-plan provide otherwise. The rules of such sub-plans may take precedence over other provisions of this Plan, with the exception of Section 7, but unless otherwise superseded by the terms of such sub-plan, the provisions of this Plan shall govern the operation of such sub-plan. The Committee shall not be required to obtain the approval of the Stockholders prior to the adoption, amendment or termination of any sub-plan unless required by the laws of the foreign jurisdiction in which Employees participating in the sub-plan are located.

#### Section 17. SECURITIES LAWS REQUIREMENTS

- (a) No option granted under the Plan may be exercised to any extent unless the shares to be issued upon such exercise under the Plan are covered by an effective registration statement pursuant to the Securities Act and the Plan is in material compliance with all applicable provisions of law, domestic or foreign, including, without limitation, the Securities Act, the

Exchange Act, the rules and regulations promulgated thereunder, applicable state and foreign securities laws and the requirements of any stock exchange upon which the Shares may then be listed, subject to the approval of counsel for the Company with respect to such compliance. If on a Purchase Date in any Offering Period hereunder, the Plan is not so registered or in such compliance, options granted under the Plan which are not in material compliance shall not be exercised on such Purchase Date, and the Purchase Date shall be delayed until the Plan is subject to such an effective registration statement and such compliance, except that the Purchase Date shall not be delayed more than twelve (12) months and the Purchase Date shall in no event be more than twenty-seven (27) months from the Commencement Date relating to such Offering Period. If, on the Purchase Date of any offering hereunder, as delayed to the maximum extent permissible, the Plan is not registered and in such compliance, options granted under the Plan which are not in material compliance shall not be exercised and all payroll deductions accumulated during the Offering Period (reduced to the extent, if any, that such deductions have been used to acquire shares of Common Stock) shall be returned to the Participants, without interest. The provisions of this Section 17 shall comply with the requirements of Section 423(b)(5) of the Code to the extent applicable.

- (b) As a condition to the exercise of an option, Sponsor may require that the person exercising such option represent and warrant at the time of any such exercise that the Shares are being purchased only for investment and without any present intention to sell or distribute such Shares if, in the opinion of counsel for Sponsor, such a representation is required by any of the aforementioned applicable provisions of law.

#### 18. GOVERNMENTAL REGULATIONS

This Plan and Sponsor's obligation to sell and deliver shares of its stock under the Plan shall be subject to the approval of any governmental authority required in connection with the Plan or the authorization, issuance, sale, or delivery of stock hereunder.

#### 19. NO ENLARGEMENT OF EMPLOYEE RIGHTS

Nothing contained in this Plan shall be deemed to give any Employee or other individual the right to be retained in the employ or service of Sponsor or any Participating Subsidiary or to interfere with the right of Sponsor or Participating Subsidiary to discharge any Employee or other individual at any time, for any reason or no reason, with or without notice.

#### 20. GOVERNING LAW

This Plan shall be governed by applicable laws of the State of Delaware and applicable federal law.

#### 21. EFFECTIVE DATE

This Plan shall be effective on the Effective Date, subject to approval of the Stockholders of Sponsor within twelve (12) months before or after its date of adoption by the Board.

#### 22. REPORTS

Individual accounts shall be maintained for each Participant in the Plan. Statements of account shall be made available to Participants at least annually, which statements shall set forth the amounts of payroll deductions, the Purchase Price, the number of shares of Common Stock purchased and the remaining cash balance, if any.

#### 23. DESIGNATION OF BENEFICIARY FOR OWNED SHARES

With respect to shares of Common Stock purchased by the Participant pursuant to the Plan and held in an account maintained by Sponsor or its assignee on the Participant's behalf, the

Participant may be permitted to file a written designation of beneficiary, who is to receive any shares and cash, if any, from the Participant's account under the Plan in the event of such Participant's death subsequent to the end of an Offering Period but prior to delivery to him or her of such shares and cash. In addition, a Participant may file a written designation of a beneficiary who is to receive any cash from the Participant's account under the Plan in the event of such Participant's death prior to the Purchase Date of an Offering Period. If a Participant is married and the designated beneficiary is not the spouse, spousal consent shall be required for such designation to be effective, to the extent required by local law. The Participant (and if required under the preceding sentence, his or her spouse) may change such designation of beneficiary at any time by written notice. Subject to local legal requirements, in the event of a Participant's death, Sponsor or its assignee shall deliver any shares of Common Stock and/or cash to the designated beneficiary. Subject to local law, in the event of the death of a Participant and in the absence of a beneficiary validly designated who is living at the time of such Participant's death, Sponsor shall deliver such shares of Common Stock and/or cash to the executor or administrator of the estate of the Participant, or if no such executor or administrator has been appointed (to the knowledge of Sponsor), Sponsor in its sole discretion, may deliver (or cause its assignee to deliver) such shares of Common Stock and/or cash to the spouse, or to any one or more dependents or relatives of the Participant, or if no spouse, dependent or relative is known to Sponsor, then to such other person as Sponsor may determine. The provisions of this Section 23 shall in no event require Sponsor to violate local law, and Sponsor shall be entitled to take whatever action it reasonably concludes is desirable or appropriate in order to transfer the assets allocated to a deceased Participant's account in compliance with local law.

#### 24. ADDITIONAL RESTRICTIONS OF RULE 16b-3.

The terms and conditions of options granted hereunder to, and the purchase of shares of Common Stock by, persons subject to Section 16 of the Exchange Act shall comply with the applicable provisions of Rule 16b-3. This Plan shall be deemed to contain, and such options shall contain, and the shares of Common Stock issued upon exercise thereof shall be subject to, such additional conditions and restrictions, if any, as may be required by Rule 16b-3 to qualify for the maximum exemption from Section 16 of the Exchange Act with respect to Plan transactions.

#### 25. NOTICES

All notices or other communications by a Participant to Sponsor or the Committee under or in connection with the Plan shall be deemed to have been duly given when received in the form specified by Sponsor or the Committee at the location, or by the person, designated by Sponsor for the receipt thereof.



**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**Form 10-K**

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

For the fiscal year ended December 31, 2017

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 No. 1-13883

**CALIFORNIA WATER SERVICE GROUP**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or Other Jurisdiction of  
Incorporation or Organization)

**1720 North First Street,  
San Jose, California**

(Address of Principal Executive Offices)

**77-0448994**

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

**95112**

(Zip Code)

**(408) 367-8200**

(Registrant's Telephone Number, including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

**Title of Each Class:**

**Name of Each Exchange on Which Registered:**

Common Stock, \$0.01 par value per share

New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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 (§ 232.405 of this chapter) 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company or emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth 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) Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant was \$1,767 million on June 30, 2017, the last business day of the registrant's most recently completed second fiscal quarter. The valuation is based on the closing price of the registrant's common stock as traded on the New York Stock Exchange.

The Common stock outstanding at February 12, 2018 was 48,011,346 shares.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the definitive proxy statement for the California Water Service Group 2017 Annual Meeting are incorporated by reference into Part III hereof.

Form 10-K

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## PART I

### Item 1. *Business.*

#### Forward-Looking Statements

This annual report, including all documents incorporated by reference, contains forward-looking statements within the meaning established by the Private Securities Litigation Reform Act of 1995. Forward-looking statements in this annual report are based on currently available information, expectations, estimates, assumptions and projections, and our management's beliefs, assumptions, judgments and expectations about us, the water utility industry and general economic conditions. These statements are not statements of historical fact. When used in our documents, statements that are not historical in nature, including words like "expects," "intends," "plans," "believes," "may," "estimates," "assumes," "anticipates," "projects," "predicts," "forecasts," "should," "seeks," or variations of these words or similar expressions are intended to identify forward-looking statements. The forward-looking statements are not guarantees of future performance. They are based on numerous assumptions that we believe are reasonable, but they are open to a wide range of uncertainties and business risks. Consequently, actual results may vary materially from what is contained in a forward-looking statement.

Factors which may cause actual results to be different than those expected or anticipated include, but are not limited to:

- governmental and regulatory commissions' decisions, including decisions on proper disposition of property;
- consequences of eminent domain actions relating to our water systems;
- changes in regulatory commissions' policies and procedures;
- the timeliness of regulatory commissions' actions concerning rate relief;
- inability to renew leases to operate city water systems on beneficial terms;
- changes in California State Water Resources Control Board water quality standards;
- changes in environmental compliance and water quality requirements;
- electric power interruptions;
- housing and customer growth index;
- the impact of opposition to rate increases;
- our ability to recover costs;
- availability of water supplies;
- issues with the implementation, maintenance or security of our information technology systems;
- civil disturbances or terrorist threats or acts, or apprehension about the possible future occurrences of acts of this type;
- labor relations matters as we negotiate with the unions;
- restrictive covenants in or changes to the credit ratings on current or future debt that could increase financing costs or affect the ability to borrow, make payments on debt, or pay dividends;
- changes in customer water use patterns and the effects of conservation;

- the impact of weather, climate, natural disasters, and diseases on water quality, water availability, water sales and operating results;
- the risks set forth in “Risk Factors” included elsewhere in this annual report.

In light of these risks, uncertainties and assumptions, investors are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date of this annual report or as of the date of any document incorporated by reference in this annual report, as applicable. When considering forward-looking statements, investors should keep in mind the cautionary statements in this annual report and the documents incorporated by reference. We are not under any obligation, and we expressly disclaim any obligation, to update or alter any forward-looking statements, whether as a result of new information, future events or otherwise.

## Overview

California Water Service Group is a holding company incorporated in Delaware in 1999 with six operating subsidiaries: California Water Service Company (Cal Water), New Mexico Water Service Company (New Mexico Water), Washington Water Service Company (Washington Water), Hawaii Water Service Company, Inc. (Hawaii Water), and CWS Utility Services and HWS Utility Services LLC (CWS Utility Services and HWS Utility Services LLC being referred to collectively in this annual report as Utility Services). Cal Water, New Mexico Water, Washington Water, and Hawaii Water are regulated public utilities. The regulated utility entities also provide some non-regulated services. Utility Services provides non-regulated services to private companies and municipalities. Cal Water was the original operating company and began operations in 1926.

Our business is conducted through our operating subsidiaries and we provide utility services to approximately two million people. The bulk of the business consists of the production, purchase, storage, treatment, testing, distribution and sale of water for domestic, industrial, public and irrigation uses, and for fire protection. We also provide non-regulated water-related services under agreements with municipalities and other private companies. The non-regulated services include full water system operation, billing and meter reading services. Non-regulated operations also include the lease of communication antenna sites, lab services and promotion of other non-regulated services.

During the year ended December 31, 2017, there were no significant changes in the kind of products produced or services rendered by our operating subsidiaries, or in the markets or methods of distribution.

Our mailing address and contact information is:

California Water Service Group  
 1720 North First Street  
 San Jose, California 95112-4598  
 telephone number: 408-367-8200  
[www.calwatergroup.com](http://www.calwatergroup.com)

Annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports are available free of charge through our website. The reports are available on our website as soon as reasonably practicable after such reports are filed with the SEC.

## Regulated Business

California water operations are conducted by the Cal Water and CWS Utility Services entities, which provide service to approximately 484,900 customer connections in approximately 100 California communities through 20 separate districts, which are subject to regulation by the California Public Utilities Commission (CPUC). Cal Water operates two leased water systems, the City

of Hawthorne and the City of Commerce, which are governed through their respective city councils and are outside of the CPUC's jurisdiction. California water operations accounted for approximately 94.3% of our total customer connections and approximately 93.9% of our total consolidated operating revenue.

Hawaii Water provides service to approximately 4,500 water and wastewater customer connections on the islands of Maui and Hawaii, including several large resorts and condominium complexes. Hawaii Water's regulated customer connections are subject to the jurisdiction of the Hawaii Public Utilities Commission (HPUC). Hawaii Water accounts for 0.9% of our total customer connections and approximately 3.6% of our total consolidated operating revenue.

Washington Water provides domestic water service to approximately 16,800 customer connections in the Tacoma and Olympia areas. Washington Water's utility operations are regulated by the Washington Utilities and Transportation Commission. Washington Water accounts for approximately 3.3% of our total customer connections and approximately 1.8% of our total consolidated operating revenue.

New Mexico Water provides service to approximately 8,100 water and wastewater customer connections in the Belen, Los Lunas and Elephant Butte areas in New Mexico. New Mexico's regulated operations are subject to the jurisdiction of the New Mexico Public Regulation Commission. New Mexico Water accounts for approximately 1.6% of our total customer connections and 0.7% of our total consolidated operating revenue.

The state regulatory bodies governing our regulated operations are referred to as the Commissions in this annual report. Rates and operations for regulated customers are subject to the jurisdiction of the respective state's regulatory Commission. The Commissions require that water and wastewater rates for each regulated district be independently determined based on the cost of service, except in Washington, which has a statewide tariff. The Commissions are expected to authorize rates sufficient to recover normal operating expenses and allow the utility to earn a fair and reasonable return on invested capital.

We distribute water in accordance with accepted water utility methods. Where applicable, we hold franchises and permits in the cities and communities where we operate. The franchises and permits allow us to operate and maintain facilities in public streets and right-of-ways as necessary.

We operate the City of Hawthorne and the City of Commerce water systems under lease agreements. In accordance with the lease agreements, we receive all revenues from operating the systems and are responsible for paying the operating costs. The City of Hawthorne and the City of Commerce lease revenues are governed through their respective city councils and are considered non-regulated because they are outside of the CPUC's jurisdiction. We report revenue and expenses for the City of Hawthorne and City of Commerce leases in operating revenue and operating expenses because we are entitled to retain all customer billings and are responsible for all operating expenses. These leases are considered "nontariffed products and services" (NTPS) by the CPUC and require a 10% revenue sharing with regulated customers.

In October 2011, an agreement was negotiated with the City of Hawthorne to lease and operate its water system. The system, which is located near the Hermosa Redondo district, serves about half of Hawthorne's population. The capital lease agreement required an up-front \$8.1 million lease deposit to the city that is being amortized over the lease term. Additionally, annual lease payments will be adjusted based on changes in rates charged to customers. Under the lease we are responsible for all aspects of system operation and capital improvements, although title to the system and system improvements reside with the city. Capital improvements are recorded as depreciable plant and equipment and depreciated per the asset lives set forth in the agreement. In exchange, we receive all revenue from the water system, which was \$10.0 million, \$8.5 million and \$8.0 million in 2017, 2016, and 2015, respectively. At the end of the lease, the city is

required to reimburse us for the unamortized value of capital improvements made during the term of the lease. The City of Hawthorne capital lease is a 15-year lease and expires in 2026.

In July 2003, an agreement was negotiated with the City of Commerce to lease and operate its water system. The lease was a 15-year lease and expires in June 2018. In 2017, we bid to provide services after June 2018 and we expect the City of Commerce to release the results of the bidding process in 2018. Under the current agreement, the operating lease requires us to pay \$0.8 million per year in monthly installments and \$200 per acre-foot for water usage exceeding 2,000 acre-feet per year, plus a percentage of certain operational savings that may be realized. Under the lease agreement, we are responsible for all aspects of the system's operations. The city is responsible for capital expenditures, and title to the system and system improvements resides with the city. We bear the risks of operation and collection of amounts billed to customers. The agreement allows Cal Water to request a rate change in order to recover costs. In exchange, we receive all revenue from the water system, which was \$3.4 million, \$2.5 million, and \$2.0 million in 2017, 2016, and 2015, respectively.

### **Non-Regulated Activities**

Fees for non-regulated activities are based on contracts negotiated between the parties. Under our non-regulated contract arrangements, we operate municipally owned water systems, privately owned water and recycled water distribution systems, but are not responsible for all operating costs. Non-regulated revenue received from water system operations is generally determined on a fee-per-customer basis.

Non-regulated revenue and expenses consist primarily of the operation of water systems that are owned by other entities under lease agreements, leasing of communication antenna sites on our properties, billing of optional third-party insurance programs to our residential customers, and unrealized gains or losses on benefit plan investments.

Effective June 30, 2011, the CPUC adopted new rules related to the provision of non-regulated services using utility assets and employees. As a result, nearly all California non-regulated activities are now considered NTPS. The prescribed accounting for these NTPS is incremental cost allocation plus revenue sharing with regulated customers. Non-regulated services determined to be "active activities" require a 10% revenue sharing, and "passive activities" require a 30% revenue sharing. The amount of non-regulated revenues subject to revenue sharing is the total billed revenues less any authorized pass-through costs. Some examples of CPUC authorized pass-through costs are purchased water, purchased power, and pump taxes. All of our non-regulated services, except for leasing communication antenna sites on our properties and unrealized gains or losses on benefit investments, are "active activities" subject to a 10% revenue sharing. Leasing communication antenna sites on our properties are "passive activities" subject to a 30% revenue sharing. Cal Water's annual revenue sharing with regulated customers was \$2.2 million, \$2.1 million, and \$2.2 million in 2017, 2016, and 2015, respectively.

### **Operating Segment**

We operate in one reportable segment, the supply and distribution of water and providing water-related utility services. For information about revenue from external customers, net income and total assets, see "Item 8. Financial Statements and Supplementary Data."

### **Growth**

We intend to continue exploring opportunities to expand our regulated and non-regulated water and wastewater activities in the western United States. The opportunities could include system acquisitions, lease arrangements similar to the City of Hawthorne and City of Commerce contracts, full service system operation and maintenance agreements, meter reading, billing contracts and other utility-related services.

## Geographical Service Areas and Number of Customer Connections at Year-end

Our principal markets are users of water within our service areas. The approximate number of customer connections served in each regulated district, the City of Hawthorne and the City of Commerce, at December 31 is as follows:

<b>(rounded to the nearest hundred)</b>	<b>2017</b>	<b>2016</b>
<b>SAN FRANCISCO BAY AREA/NORTH COAST</b>		
Bay Area Region (serving South San Francisco, Colma, Broadmoor, San Mateo, San Carlos, Lucerne, Duncans Mills, Guerneville, Dillon Beach, Noel Heights and portions of Santa Rosa) . . . . .	55,700	55,500
Bear Gulch (serving portions of Menlo Park, Atherton, Woodside and Portola Valley) . . . . .	18,900	18,900
Los Altos (including portions of Cupertino, Los Altos Hills, Mountain View and Sunnyvale) . . . . .	19,000	18,900
Livermore . . . . .	18,800	18,600
	<u>112,400</u>	<u>111,900</u>
<b>SACRAMENTO VALLEY</b>		
Chico (including Hamilton City) . . . . .	29,700	29,400
Oroville . . . . .	3,600	3,600
Marysville . . . . .	3,800	3,800
Dixon . . . . .	2,900	2,900
Willows . . . . .	2,400	2,400
	<u>42,400</u>	<u>42,100</u>
<b>SALINAS VALLEY</b>		
Monterey Region (including Salinas and King City) . . . . .	31,300	31,100
	<u>31,300</u>	<u>31,100</u>
<b>SAN JOAQUIN VALLEY</b>		
Bakersfield . . . . .	71,600	71,100
Stockton . . . . .	44,000	43,800
Visalia . . . . .	44,700	44,000
Selma . . . . .	6,400	6,400
Kern River Valley . . . . .	4,000	3,900
	<u>170,700</u>	<u>169,200</u>
<b>LOS ANGELES AREA</b>		
East Los Angeles . . . . .	26,800	26,800
Hermosa Redondo (serving Hermosa Beach, Redondo Beach and a portion of Torrance) . . . . .	26,900	26,900
Dominguez (Carson and portions of Compton, Harbor City, Long Beach, Los Angeles and Torrance) . . . . .	34,100	34,100
Los Angeles County Region (including Palos Verdes Estates, Rancho Palos Verdes, Rolling Hills Estates, Rolling Hills, Fremont Valley, Lake Hughes, Lancaster and Leona Valley) . . . . .	25,600	25,600
Westlake (a portion of Thousand Oaks) . . . . .	7,100	7,100
Hawthorne and Commerce (leased municipal systems) . . . . .	7,600	7,600
	<u>128,100</u>	<u>128,100</u>
<b>CALIFORNIA TOTAL</b> . . . . .	<b>484,900</b>	<b>482,400</b>
<b>HAWAII</b> . . . . .	<b>4,500</b>	<b>4,400</b>
<b>NEW MEXICO</b> . . . . .	<b>8,100</b>	<b>8,000</b>
<b>WASHINGTON</b> . . . . .	<b>16,800</b>	<b>16,700</b>
<b>COMPANY TOTAL</b> . . . . .	<b><u>514,300</u></b>	<b><u>511,500</u></b>



## Rates and Regulation

The Commissions have plenary powers setting both rates and operating standards. As such, the Commissions' decisions significantly impact the Company's revenues, earnings, and cash flows. The amounts discussed herein are generally annual amounts, unless otherwise stated, and the financial impact to recorded revenue is expected to occur over a 12-month period from the effective date of the decision. In California, water utilities are required to make several different types of filings. Certain filings, such as: General Rate Case (GRC) filings, escalation rate increase filings, and offset filings, may result in rate changes that generally remain in place until the next GRC. As explained below, surcharges and surcredits to recover balancing and memorandum accounts as well as GRC interim rate relief are temporary rate changes, which have specific time frames for recovery.

The CPUC follows a rate case plan, which requires Cal Water to file a GRC for each of its regulated operating districts every three years. In a GRC proceeding, the CPUC not only considers the utility's rate setting requests, but may also consider other issues that affect the utility's rates and operations. The CPUC is generally required to issue its GRC decision prior to the first day of the test year or authorize interim rates. In accordance with the rate case plan, Cal Water will file its next GRC application in July of 2018.

Between GRC filings, Cal Water may file escalation rate increases, which allow Cal Water to recover cost increases, primarily from inflation and incremental investments, during the second and third years of the rate case cycle. However, escalation rate increases are district specific and subject to an earnings test. The CPUC may reduce a district's escalation rate increase if, in the most recent 13-month period, the earnings test reflects earnings in excess of what was authorized for that district.

In addition, California water utilities are entitled to make offset requests via advice letter. Offsets may be requested to adjust revenues for construction projects authorized in GRCs when those capital projects go into service (these filings are referred to as "rate base offsets"), or for rate changes charged to Cal Water for purchased water, purchased power, and pump taxes (which are referred to as "expense offsets"). Rate changes approved in offset requests remain in effect until the next GRC is approved.

In pursuit of the CPUC's water conservation goals, the CPUC decoupled Cal Water's revenue requirement from customer consumption levels in 2008 by authorizing a Water Revenue Adjustment Mechanism (WRAM) and Modified Cost Balancing Account (MCBA) for each district. The WRAM and MCBA ensure that Cal Water recovers revenues authorized by the CPUC regardless of customer consumption. This removes the historical disincentive against promoting lower water usage among customers. Through an annual advice letter filing, Cal Water recovers any under-collected metered revenue amounts authorized, or refunds over-collected quantity revenues, via surcharges and surcredits. The advice letters are filed between February and April of each year and address the net WRAM and MCBA balances recorded for the previous calendar year. The majority of WRAM and MCBA balances are collected or refunded through surcharges/surcredits over 12 and 18 months. The WRAM and MCBA amounts are cumulative, so if they are not amortized in a given calendar year, the balance is carried forward and included with the following year balance. Cal Water has a Sales Reconciliation Mechanism (SRM) in place for the second and third years of a GRC that allow the company to adjust its adopted sales forecast if actual sales vary from adopted sales by more than 5.0% in the prior year. The SRM moderates the growth of the net WRAM and MCBA balance.

## **Regulatory Activity—California**

### 2015 GRC filing

On December 15, 2016, the CPUC voted to approve Cal Water's 2015 GRC settlement agreement. The approved decision, which was proposed by the presiding Administrative Law Judge in November 2016, authorizes Cal Water to increase gross revenue by approximately \$45.0 million starting on January 1, 2017, up to \$17.2 million in 2018, up to \$16.3 million in 2019, and up to \$30.0 million upon completion and approval of the Company's advice letter projects. The 2018 and 2019 revenue increases are subject to the CPUC's earning test protocol.

The CPUC's decision also authorizes Cal Water to invest \$658.8 million in water system improvements throughout California over the three-year period of 2016-2018 in order to continue to provide safe and reliable water to its customers. This figure includes \$197.3 million of water system infrastructure improvements that will be subject to the CPUC's advice letter procedure.

### Cost of Capital Application

In April of 2017, Cal Water, along with three other water utilities, filed an application to adopt a new cost of capital and capital structure for 2018. Cal Water requested a return on equity of 10.75% and a 53.4% equity capital structure as well as a water cost of capital adjustment mechanism similar to that last adopted for the company. The California Office of Ratepayer Advocates and other parties submitted testimony and the CPUC held evidentiary hearings in September 2017.

On February 6, 2018, the CPUC issued the proposed decision of the assigned administrative law judge. The proposed decision would lower Cal Water's authorized return on equity from 9.43% to 8.22%. If the proposed decision were adopted without changes, Cal Water would be required to reduce its rates collected from California customers by approximately \$13.0 million, which will reduce Cal Water's 2018 net income and net cash provided by operating activities. A proposed decision must be approved by the full Commission to go into effect. The Commission could modify or reject the proposed decision and will first consider the matter at its meeting on March 22, 2018.

### Escalation increase requests

As a part of the decision on the 2015 GRC, Cal Water was authorized to request annual escalation rate increases for 2018 for those districts that passed the earnings test. In November of 2017, Cal Water requested escalation rate increases in all of its regulated districts. The annual adopted gross revenue associated with the November 2017 filing was \$15.9 million. The new rates became effective on January 1, 2018.

### Expense offset requests

Expense offsets are dollar-for-dollar increases in revenue to match increased expenses, and therefore do not affect net operating income. In October of 2016, Cal Water submitted advice letters to offset increases in purchased water costs and pump taxes in four of its regulated districts, totaling \$1.9 million. The new rates became effective on January 1, 2017.

In March of 2017, Cal Water submitted an advice letter to offset increased purchased water in one of its regulated districts, totaling \$1.0 million. The new rates became effective on April 15, 2017.

In June of 2017, Cal Water submitted advice letters to offset increased purchased water and pump taxes in four of its regulated districts, totaling \$2.7 million. The new rates became effective on July 1, 2017.

In July of 2017, Cal Water submitted an advice letter to offset increased purchased water and pump taxes in one of its regulated districts, totaling \$0.2 million. The new rates became effective on August 1, 2017.

In October of 2017, Cal Water submitted advice letters to request offsets for increases in purchased water costs and pump taxes in five of its regulated districts totaling \$2.2 million. The new rates became effective on January 1, 2018.

#### Rate base offset requests

For construction projects authorized in GRCs as advice letter projects, Cal Water is allowed to request rate base offsets to increase revenues after the project goes into service. In November of 2016, Cal Water submitted an advice letter to recover \$2.6 million of annual revenue increase for rate base offsets in five of its regulated districts. The new rates became effective on January 1, 2017.

In April of 2017, Cal Water submitted advice letters to recover \$0.9 million of annual revenue increase for rate base offsets in two of its regulated districts. The new rates became effective on April 15, 2017.

In May of 2017, Cal Water submitted an advice letter to recover \$0.4 million of annual revenue increase for a rate base offset in one of its regulated districts. The new rates became effective on July 1, 2017.

In November of 2017, Cal Water submitted an advice letter to recover \$1.4 million of annual revenue increase for a rate base offset in one of its regulated districts. The new rates became effective on January 1, 2018.

#### WRAM/MCBA filings

In March of 2017, Cal Water submitted an advice letter to true up the revenue over- and under-collections in the 2016 annual WRAMs/MCBAs of its regulated districts. A net under-collection of \$25.8 million is being recovered from customers in the form of 12, 18, and greater-than-18-month surcharges/surcredits. The new rates became effective April 15, 2017. This surcharge/surcredit in some cases is in addition to surcharges/surcredits authorized in prior years which have not yet expired.

#### Drought Memorandum Account

The incremental costs tracked in the drought memorandum account for the twelve month period ended December 31, 2017 were \$0.2 million, of which less than \$0.1 million was spent on capital. For the twelve month period ended December 31, 2016, incremental costs were \$5.0 million, of which \$0.7 million was spent on capital.

On December 15, 2016, the CPUC approved a resolution to allow Cal Water to begin recovering \$2.9 million of incremental costs related to 2015 and 2014 through a surcharge which became effective on January 1, 2017.

In 2018, Cal Water expects to submit an advice letter to request recovery of 2016 and 2017 incremental drought expenses.

#### 1,2,3 Trichloropropane (TCP) Memorandum Account

Established in December 2009, the TCP memorandum account tracks the costs incurred and proceeds received and applied with respect to litigation against manufacturers and distributors referred to as potentially responsible parties (PRPs) that manufactured and distributed products that contained TCP in California. Cal Water incurred incremental internal and external costs to

support its litigation effort. The TCP memorandum account also tracks litigation awards and settlement proceeds. Finally, the TCP memorandum account will track the application of funds received towards remediation costs, including TCP water treatment expenses and the costs of investments in replacement and treatment property.

On December 20, 2017, Cal Water entered into an \$85.0 million settlement agreement and release of claims with the PRPs, in *California Water Service Company and City of Bakersfield v. The Dow Chemical Company, et al., Civil Case No. CIV-470999* (TCP Action). The TCP Action seeks damages and other relief related to the PRPs' alleged contamination of drinking water supply and water wells with the chemical TCP.

The proceeds from the settlement, after payment of the legal fees, was \$56.0 million and will be used to reimburse a portion of the capital costs associated with Cal Water's remediation efforts related to such alleged TCP contamination. Under the terms of the Agreement, the PRPs are released from all claims regarding 47 of the 57 total claimed wells, and Cal Water agrees to file a dismissal with prejudice of the TCP Action. The PRPs are also released from future claims regarding TCP contamination of any other wells, unless and until Cal Water has installed granular activated carbon filtration systems or other then-approved State treatment technology for TCP on, or replaced, 36 wells due to TCP contamination.

#### 2018 Tax Accounting Memorandum Account (TAMA)

On December 22, 2017, the CPUC sent a letter to All Class A and B Water and Sewer Utilities on the subject of "Changes in Federal Tax Rates for 2018." The CPUC required Cal Water to establish a memo account to track the impact of the Tax Cuts and Jobs Act (TCJA) has on Cal Water. The TAMA will track the revenue requirement impact of the TCJA not otherwise reflected in rates from January 1, 2018 until the effective date of the revenue requirement changes adopted in Cal Water's next GRC. The Hawaii Water, Washington Water, and New Mexico Water Commissions have similar requirements to track the impact of the changes to the federal tax law.

#### School Lead Testing Memorandum Account (SLT MA)

In March of 2017, Cal Water submitted an advice letter that established the SLT MA, which gives Cal Water the opportunity to recover costs related to lead monitoring and testing required by the State Water Resources Control Board's Division of Drinking Water. The SLT MA will track all incremental expenses associated with lead testing conducted at the request of K-12 schools within Cal Water's service territory.

#### Phase 1 Sites Reservoir Memorandum Account (PHASE 1 SITES MA)

In July of 2017, Cal Water submitted an advice letter that established the PHASE 1 SITES MA, which gives Cal Water the opportunity to recover costs associated with participation in phase 1 of the proposed Sites Reservoir project, an off-stream project located on the west side of the Sacramento Valley. The PHASE 1 SITES MA will track amounts paid to the Sites Reservoir Authority for Phase 1 and is capped at \$1.0 million.

#### Travis Air Force Base

On September 29, 2016, Cal Water entered into a 50-year agreement with the U.S. Department of Defense to acquire the water distribution assets of, and to provide water utility service to, the Travis Air Force Base beginning in 2018. On May 31, 2017, Cal Water submitted an application to the CPUC seeking approval to provide water service to the base and to establish rates for its service.

The water system utilizes surface water treated at a water treatment plant and groundwater from five wells, and includes distribution piping, storage tanks, hydrants, and other appurtenances

to serve about 15,280 active and reserve personnel and civilians on the 6,400-acre base. If approved, Cal Water will make initial capital improvements of about \$12.7 million, with an anticipated capital investment of about \$52.0 million over the 50-year term of the utility service contract.

### **Regulatory Activity—Other States**

#### 2016 Pukalani (Hawaii Water) GRC Filing

In December of 2016, Hawaii water filed a GRC for its Pukalani wastewater system requesting an additional \$1.3 million in revenues on an annual basis. The application requested recovery for increases in operating expenses since the previous rate case as well as recovery of the balance of the cost of the wastewater treatment plant that was not approved to be included in customer rates in the previous rate case among other capital investments. On September 15, 2017, the HPUC issued a proposed decision authorizing an \$0.8 million increase in revenues on an annual basis. Pursuant to a settlement agreement between Hawaii Water and the Consumer Advocate, the revenue increase will be phased-in over 4 years (\$0.2 million per year). The first phase of the increase was effective on October 18, 2017.

#### 2017 Waikoloa (Hawaii Water) GRC Filings

In December of 2017, Hawaii Water filed GRC applications requesting an additional \$3.8 million in revenues on an annual basis for its Waikoloa Village and Resort Systems with the HPUC. The GRCs seek recovery of capital investments in the Waikoloa Village and Waikoloa Resort Systems as well as increases in operating expenses since the previous rate case. If approved, the Company anticipates rates would become effective in the fourth quarter of 2018.

### **Water Supply**

Our source of supply varies among our operating districts. Certain districts obtain all of their supply from wells; some districts purchase all of their supply from wholesale suppliers; and other districts obtain supply from a combination of wells and wholesale suppliers. A small portion of supply comes from surface sources and is processed through Company-owned water treatment plants. To the best of management's knowledge, we are meeting water quality, environmental, and other regulatory standards for all Company-owned systems.

Historically, approximately 46.5% of our annual water supply is pumped from wells. State groundwater management agencies operate differently in each state. Some of our wells extract ground water from water basins under state ordinances. These are adjudicated groundwater basins, in which a court has settled the dispute between landowners or other parties over how much annual groundwater can be extracted by each party. All of our adjudicated groundwater basins are located in the State of California. Our annual groundwater extraction from adjudicated groundwater basins approximates 6.8 billion gallons or 14.4% of our total annual water supply pumped from wells. Historically, we have extracted less than 100% of our annual adjudicated groundwater rights and have the right to carry forward up to 20% of the unused amount to the next annual period. All of our remaining wells extract ground water from managed or unmanaged water basins. There are no set limits for the ground water extracted from these water basins. Our annual groundwater extraction from managed groundwater basins approximates 28.0 billion gallons or 58.9% of our total annual water supply pumped from wells. Our annual groundwater extraction from unmanaged groundwater basins approximates 12.7 billion gallons or 26.7% of our total annual water supply pumped from wells. Most of the managed groundwater basins we extract water from have groundwater recharge facilities. We are required to pay well pump taxes to financially support these groundwater recharge facilities. Our well pump taxes for the 12 months ending December 31, 2017, 2016, and 2015 were \$13.9 million, \$11.3 million, and \$11.5 million, respectively. In 2014, the State of California enacted the Sustainable Groundwater Management

Act of 2014. The law and its implementing regulations will require most basins to select a sustainability agency by 2017, develop a sustainability plan by 2022, and show progress toward sustainability by 2027. We expect that in the future, groundwater will be produced mainly from managed and adjudicated basins.

California's normal weather pattern yields little precipitation between mid-spring and mid-fall. The Washington Water service areas receive precipitation in all seasons, with the heaviest amounts during the winter. New Mexico Water's rainfall is heaviest in the summer monsoon season. Hawaii Water receives precipitation throughout the year, with the largest amounts in the winter months. Water usage in all service areas is highest during the warm and dry summers and declines in the cool winter months. Rain and snow during the winter months in California replenish underground water aquifers and fill reservoirs, providing the water supply for subsequent delivery to customers. As of December 31, 2017, the State of California snowpack water content during the 2017-2018 water year is 67% of long-term averages (per the California Department of Water Resources, Northern Sierra Precipitation Accumulation report). The northern Sierra region is the most important for the state's urban water supplies. The central and southern portions of the Sierras also have recorded 26% and 31%, respectively, of long-term averages. In January of 2014, California's Governor Brown proclaimed a drought emergency and directed State officials to take all necessary actions to make water immediately available. On April 7, 2017, the Governor declared an end to the drought emergency in 54 of California's 58 counties. Two of Cal Water's districts remain under a declared drought; these were areas where groundwater was impacted by five years of drought conditions. Management believes that supply pumped from underground aquifers and purchased from wholesale suppliers will be adequate to meet customer demand during 2018 and beyond. Long-term water supply plans are developed for each of our districts to help assure an adequate water supply under various operating and supply conditions. Some districts have unique challenges in meeting water quality standards, but management believes that supplies will meet current standards using current treatment processes.

The following table shows the estimated quantity of water purchased and the percentage of purchased water to total water production in each California operating district that purchased

water in 2017. Other than noted below, all other districts receive 100% of their water supply from wells.

<u>District</u>	<u>Water Purchased (MG)</u>	<u>Percentage of Total Water Production</u>	<u>Source of Purchased Supply</u>
<b>SAN FRANCISCO BAY AREA/ NORTH COAST</b>			
Bay Area Region* . . . . .	6,731	100%	San Francisco Public Utilities Commission and Yolo County Flood Control & Water Conservation District
Bear Gulch . . . . .	3,355	90%	San Francisco Public Utilities Commission
Los Altos . . . . .	2,414	64%	Santa Clara Valley Water District
Livermore . . . . .	2,031	77%	Alameda County Flood Control and Water Conservation District, Zone 7
<b>SACRAMENTO VALLEY</b>			
Oroville . . . . .	630	82%	Pacific Gas and Electric Co. and County of Butte
<b>SAN JOAQUIN VALLEY</b>			
Bakersfield . . . . .	9,937	49%	Kern County Water Agency and City of Bakersfield
Stockton . . . . .	6,623	87%	Stockton East Water District
<b>LOS ANGELES AREA</b>			
East Los Angeles . . . . .	1,458	32%	Central Basin Municipal Water District
Dominguez . . . . .	9,670	85%	West Basin Municipal Water District and City of Torrance
City of Commerce . . . . .	134	20%	Central Basin Municipal Water District
Hawthorne . . . . .	874	67%	West Basin Municipal Water District
Hermosa Redondo . . . . .	3,138	90%	West Basin Municipal Water District
Los Angeles County Region** . . . . .	5,791	97%	West Basin Municipal Water District and Antelope Valley-East Kern Water Agency
Westlake . . . . .	2,384	100%	Calleguas Municipal Water District and Oak Park Water Service
Kern River Valley . . . . .	44	17%	City of Bakersfield

MG = million gallons

\* Bay Area Region includes Bayshore and Redwood Valley

\*\* Los Angeles County Region includes Palos Verdes and Antelope Valley

The Bear Gulch district obtains a portion of its water supply from surface runoff from the local watershed. The Oroville district in the Sacramento Valley, the Bakersfield district in the San Joaquin Valley, and the Kern River Valley district in the Los Angeles Area purchase water from a surface supply. Surface sources are processed through our water treatment plants before being delivered to the distribution system. The Bakersfield district also purchases treated water as a component of its water supply.

The Chico, Marysville, Dixon, and Willows districts in the Sacramento Valley, the Monterey Region district in the Salinas Valley, and the Selma and Visalia districts in the San Joaquin Valley obtain their entire supply from wells.

Form 10-K

Purchases for the Los Altos, Livermore, Oroville, Redwood Valley, Stockton, and Bakersfield districts are pursuant to long-term contracts expiring on various dates after 2017. The water supplies purchased for the Dominguez, East Los Angeles, Hermosa Redondo, Palos Verdes, and Westlake districts as well as the Hawthorne and Commerce systems are provided by public agencies pursuant to a statutory obligation of continued non-preferential service to purveyors within the agencies' boundaries. Purchases for the Bayshore and Bear Gulch districts are in accordance with long-term contracts with the San Francisco Public Utilities Commission (SFPUC) until June 30, 2034.

Management anticipates water supply contracts will be renewed as they expire though the price of wholesale water purchases is subject to pricing changes imposed by the various wholesalers.

Shown below are wholesaler price rates and increases that became effective in 2017 and estimated wholesaler price rates and percent changes for 2018. In 2017, several districts experienced purchased water rate increases, resulting in the filing of several purchased water offsets.

District	Effective Month	2017		Percent Change	Effective Month	2018	
		Unit Cost				Unit Cost	Percent Change
Antelope . . . . .	January	\$ 521.00 /af	7.4%	January	\$ 560.00 /af	7.5%	
Bakersfield(1) . . . . .	July	\$ 165.00 /af	0.6%	July	\$ 165.00 /af	—	
Bear Gulch . . . . .	July	\$ 4.10 /ccf	—	July	\$ 4.10 /ccf	—	
Commerce(2) . . . . .	July	\$ 1,092.00 /af	5.8%	January	\$ 1,128.00 /af	3.3%	
Dominguez(2) . . . . .	July	\$ 1,332.00 /af	3.8%	January	\$ 1,354.00 /af	1.7%	
East Los Angeles(2) . .	July	\$ 1,092.00 /af	5.8%	January	\$ 1,128.00 /af	3.3%	
Hawthorne(2) . . . . .	July	\$ 1,332.00 /af	3.8%	January	\$ 1,354.00 /af	1.7%	
Hermosa Redondo(2)	July	\$ 1,332.00 /af	3.8%	January	\$ 1,354.00 /af	1.7%	
Livermore . . . . .	January	\$ 2.55 /ccf	(19.0)%	January	\$ 2.04 /ccf	(20.0)%	
Los Altos . . . . .	July	\$ 1,275.00 /af	8.8%	July	\$ 1,275.00 /af	—	
Oroville(2) . . . . .	April	\$ 174,959.04 /yr	2.7%	April	\$ 174,959.04 /yr	—	
Palos Verdes(2) . . . . .	July	\$ 1,332.00 /af	3.8%	January	\$ 1,354.00 /af	1.7%	
Mid-Peninsula . . . . .	July	\$ 4.10 /ccf	—	July	\$ 4.10 /ccf	—	
Redwood Valley . . . .	April	\$ 65.94 /af	—	April	\$ 65.94 /af	—	
South San Francisco .	July	\$ 4.10 /ccf	—	July	\$ 4.10 /ccf	—	
Stockton . . . . .	April	\$1,066,831.31 /mo	(0.4)%	April	\$1,066,831.31 /mo	—	
Westlake . . . . .	January	\$ 1,300.00 /af	3.4%	January	\$ 1,375.00 /af	5.8%	

af = acre foot;

ccf = hundred cubic feet;

yr = fixed annual cost;

mo = fixed monthly cost

(1) untreated water

(2) wholesaler price changes occur every six months

We work with all local suppliers and agencies responsible for water supply to insure adequate, long-term supply for each system.

See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Water Supply" for more information on adequacy of supplies.



## Seasonal Fluctuations

In California, our customers' consumption pattern of water varies with the weather, in terms of rainfall and temperature. In the WRAM and MCBA design, the CPUC considers the historical pattern in determining the adopted sales and production costs. With a majority of our sales being subject to the WRAM and production costs being covered by the MCBA, fluctuations in financial results have been minimized. However, cash flows from operations and short-term borrowings on our credit facilities can be significantly impacted by seasonal fluctuations including recovery of the WRAM and MCBA.

Our water business is seasonal in nature. Weather conditions can have a material effect on customer usage. Customer demand for water generally is lower during the cooler and rainy winter months. Demand increases in the spring when warmer weather returns and the rains end, and customer use more water for outdoor purposes, such as landscape irrigation. Warm temperatures during the generally dry summer months result in increased demand. Water usage declines during the fall as temperatures decrease and the rainy season begins. During years in which precipitation is especially heavy or extends beyond the spring into the early summer, customer demand can decrease from historic normal levels, generally due to reduced outdoor water usage. Likewise, an early start to the rainy season during the fall can cause a decline in customer usage. As a result, seasonality of water usage has a significant impact on our cash flows from operations and borrowing on our short-term facilities.

## Utility Plant Construction

We have continually extended, enlarged, and replaced our facilities as required to meet increasing demands and to maintain the water systems. We obtain construction financing using funds from operations, short-term bank borrowings, long-term financing, advances for construction and contributions in aid of construction that are funded by developers. Advances for construction are cash deposits from developers for construction of water facilities or water facilities deeded from developers. These advances are generally refundable without interest over a period of 40 years in equal annual payment amounts. Contributions in aid of construction consist of nonrefundable cash deposits or facilities transferred from developers, primarily for fire protection and relocation projects. We cannot control the amounts received from developers. This amount fluctuates from year-to-year as the level of construction activity carried on by developers varies. This activity is impacted by the demand for housing, commercial development, and general business conditions, including interest rates.

See Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources" for additional information.

## Energy Reliability

We continue to use power efficiently to minimize the power expenses passed on to our customers, and maintain backup power systems to continue water service to our customers if the power companies' supplies are interrupted. Many of our well sites are equipped with emergency electric generators designed to produce electricity to keep the wells operating during power outages. Storage tanks also provide customers with water during blackout periods.

## Impact of Climate Change Legislation

Our operations depend on power provided by other public utilities and, in emergencies, power generated by our portable and fixed generators. If future legislation limits emissions from the power generation process, our cost of power may increase. Any increase in the cost of power will be

passed along to our California customers through the MCBA or included in our cost of service paid by our customers as requested in our GRC filings.

We maintain a fleet of vehicles to provide service to our customers, including a number of heavy duty diesel vehicles that were retrofitted to meet California emission standards. If future legislation further impacts the cost to operate the fleet or the fleet acquisition cost in order to meet certain emission standards, it will increase our cost of service and our rate base. Any increase in fleet operating costs associated with meeting emission standards will be included in our cost of service paid by our customers as requested in our GRC filings. While recovery of these costs is not guaranteed, we would expect recovery in the regulatory process.

Under the California Environmental Quality Act (CEQA), all capital projects of a certain type (primarily wells, tanks, major pipelines and treatment facilities) require mitigation of greenhouse gas emissions. The cost to prepare the CEQA documentation and permit will be included in our capital cost and added to our rate base, which will be requested to be paid for by our customers. Any increase in the operating cost of the facilities will also be included in our cost of service paid by our customers as requested in our GRC filings. While recovery of these costs is not guaranteed, we would expect recovery in the regulatory process.

Cap and trade regulations were implemented in 2012 with the goal of reducing emissions to 1990 levels by the year 2020. These regulations have not impacted water utilities at this time. In the future, if we are required to comply with these regulations, any increase in operating costs associated with meeting these standards will be included in our cost of service paid by our customers as requested in our GRC filings. While recovery of these costs is not guaranteed, we would expect recovery in the regulatory process.

### **Security at Company Facilities**

Due to terrorism and other risks, we have heightened security at our facilities and have taken added precautions to protect our employees and the water delivered to customers. In 2002, federal legislation was enacted that resulted in new regulations concerning security of water facilities, including submitting vulnerability assessment studies to the federal government. We have complied with regulations issued by the Environmental Protection Agency (EPA) pursuant to federal legislation concerning vulnerability assessments and have made filings to the EPA as required. In addition, communication plans have been developed as a component of our procedures. While we do not make public comments on our security programs, we have been in contact with federal, state, and local law enforcement agencies to coordinate and improve our water delivery systems' security.

### **Quality of Water Supply**

Our operating practices are designed to produce potable water in accordance with accepted water utility practices. Water entering the distribution systems from surface sources is treated in compliance with federal and state Safe Drinking Water Act (SDWA) standards. Most well supplies are chlorinated or chloraminated for disinfection. Water samples from each water system are analyzed on a regular, scheduled basis in compliance with regulatory requirements. We operate a state-certified water quality laboratory at the San Jose General Office that provides testing for most of our California operations. Certain tests in California are contracted with independent certified labs qualified under the Environmental Laboratory Accreditation Program. Local independent state certified labs provide water sample testing for the Washington, New Mexico and Hawaii operations.

In recent years, federal and state water quality regulations have resulted in increased water sampling requirements. The SDWA continues to be amended to address public health concerns. We

monitor water quality standard changes and upgrade our treatment capabilities to maintain compliance with the various regulations.

### **Competition and Condemnation**

Our principal operations are regulated by the Commission of each state. Under state laws, no privately owned public utility may compete within any service territory that we already serve without first obtaining a certificate of public convenience and necessity from the applicable Commission. Issuance of such a certificate would only be made upon finding that our service is deficient. To management's knowledge, no application to provide service to an area served by us has been made.

State law provides that whenever a public agency constructs facilities to extend a utility system into the service area of a privately owned public utility, such an act constitutes the taking of property and requires reimbursement to the utility for its loss. State statutes allow municipalities, water districts and other public agencies to own and operate water systems. These agencies are empowered to condemn properties already operated by privately owned public utilities. The agencies are also authorized to issue bonds, including revenue bonds, for the purpose of acquiring or constructing water systems. However, if a public agency were to acquire utility property by eminent domain action, the utility would be entitled to just compensation for its loss. In Washington, annexation was approved in February 2008 for property served by us on Orcas Island; however, we continue to serve the customers in the annexed area and do not expect the annexation to impact our operations. To management's knowledge, other than the Orcas Island property, no municipality, water district, or other public agency is contemplating or has any action pending to acquire or condemn any of our systems.

### **Environmental Matters**

Our operations are subject to environmental regulation by various governmental authorities. Environmental health and safety programs have been designed to provide compliance with water discharge regulations, underground and aboveground fuel storage tank regulations, hazardous materials management plans, hazardous waste regulations, air quality permitting requirements, wastewater discharge limitations and employee safety issues related to hazardous materials. Also, we actively investigate alternative technologies for meeting environmental regulations and continue the traditional practices of meeting environmental regulations.

For a description of the material effects that compliance with environmental regulations may have on us, see Item 1A. "Risk Factors—Risks Related to Our Regulatory Environment." We expect environmental regulation to increase, resulting in higher operating costs in the future, and there can be no assurance that the Commissions would approve rate increases to enable us to recover these additional compliance costs.

### **Employees**

At December 31, 2017, we had 1,176 employees, including 50 at Washington Water, 41 at Hawaii Water, and 17 at New Mexico Water. In California, most non-supervisory employees are represented by the Utility Workers Union of America, AFL-CIO, except certain engineering and laboratory employees who are represented by the International Federation of Professional and Technical Engineers, AFL-CIO.

At December 31, 2017, we had 750 union employees. In January 2015, we negotiated a six-year contract that included 2015, 2016, and 2017 wage increases with both of our unions of 3.25% and 2.75%, and 2.75%, respectively. Annual wage increases for 2018, 2019, and 2020 are estimated to be in the range from 2.5% to 3.25% based on current forecast inflation rates. The wage changes

will fluctuate with the changes to the Consumer Price Index (CPI) for the Los Angeles area. In the event an annual wage increase is determined to be greater than 3.25% or less than 2.0%, either party may request to re-open negotiations for wages only. Such notice must be served on the other party no later than 60 days after the publication of such CPI data. The current agreement with the unions is effective through 2020. Management believes that it maintains good relationships with the unions.

Employees at Washington Water, New Mexico Water, and Hawaii Water are not represented by unions.

### Executive Officers of the Registrant

Name	Positions and Offices with California Water Service Group	Age
Martin A. Kropelnicki(1)	President and Chief Executive Officer since September 1, 2013. Formerly, President and Chief Operating Officer (2012-2013), Chief Financial Officer and Treasurer (2006-2012), served as Chief Financial Officer of Power Light Corporation (2005-2006), Chief Financial Officer and Executive Vice President of Corporate Services of Hall Kinion and Associates (1997-2004), Deloitte & Touche Consulting (1996-1997), held various positions with Pacific Gas & Electric (1989-1996).	51
Thomas F. Smegal III(2)	Vice President, Chief Financial Officer and Treasurer since October 1, 2012. Formerly, Vice President, Regulatory Matters and Corporate Relations (2008-2012), Manager of Rates (2002-2008), Regulatory Analyst (1997-2002), served as Utilities Engineer at the California Public Utilities Commission (1990-1997).	50
Paul G. Townsley(2)	Vice President of Rates and Regulatory Matters since March 4, 2013. Formerly Divisional Vice President, Operations and Engineering for EPCOR Water USA (2012-2013), served as President of American Water Works Company subsidiaries in Arizona, New Mexico, and Hawaii (2007-2012), served as American Water Works Company's President, Western Region (2002-2007), held various other positions with Citizens Utilities Company (1982-2002).	60

<u>Name</u>	<u>Positions and Offices with California Water Service Group</u>	<u>Age</u>
Robert J. Kuta(2) . . . . .	Vice President of Engineering effective April 15, 2015. Formerly Senior Vice President of Operations Management Services, Water, Environmental and Nuclear markets for CH2M Hill (2006 to 2015), served as Western Region Vice President of Service Delivery and President of Arizona American Water Company (2001 to 2005), and held various management positions at Citizens Water Resource Company, Chaparral City Water Company, and Spring Creek Utilities (1993 to 2001).	53
Michael B. Luu(2) . . . . .	Vice President of Customer Service and Chief Information Officer effective January 1, 2017. Formerly Vice President of Customer Service and Information Technology (2013-2016), Acting California Water Service Company District Manager, Los Altos (2012-2013), Director of Information Technology (2008-2012), CIS Development Manager (2005-2008), held various other positions with California Water Service Company since 1999.	38
Timothy D. Treloar(2) . . . . .	Vice President of Water Quality and Chief Utility Operations Officer effective January 1, 2017. Formerly Vice President of Operations and Water Quality (2013-2016), Director of Water Quality (2013), California Water Service Company District Manager, Bakersfield (2002-2013), Assistant District Manager (1997-2002), General Superintendent (1994-1997).	60
Ronald D. Webb(2) . . . . .	Vice President of Human Resources since August 11, 2014. Formerly Managing Director, Human Resources Partner for United Airlines (2006-2014), served as Vice President of Human Resources for Black & Decker Corporation (1995-2005), Human Resource Manager for General Electric Company (1990-1994), and held various labor relations positions for National Steel and Shipbuilding Company (1982-1989).	61

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<u>Name</u>	<u>Positions and Offices with California Water Service Group</u>	<u>Age</u>
Lynne P. McGhee(2) . . . . .	Vice President and General Counsel since January 1, 2015. Formerly Corporate Secretary (2007-2014), Associate Corporate Counsel (2003-2014), and served as a Commissioner legal advisor and staff counsel at the California Public Utilities Commission (1998-2003).	53
David B. Healey(2) . . . . .	Vice President, Corporate Controller and Assistant Treasurer since January 1, 2015. Formerly Corporate Controller and Assistant Treasurer (2012-2014), Director of Financial Reporting (2009-2012), served as Subsidiary Controller for SunPower Corporation (2005-2009), Corporate Controller for Hall, Kinion & Associates, Inc. (1997-2005), held various other positions with Pacific Gas & Electric Company (1985-1997).	61
Shannon C. Dean(2) . . . . .	Vice President of Corporate Communications & Community Affairs since January 1, 2015. Formerly Director of Corporate Communications (2000-2014), held various corporate communications, government and community relations for Dominguez Water Company (1991-1999).	50
Michelle R. Mortensen(2) . . . . .	Corporate Secretary since January 1, 2015. Formerly Assistant Corporate Secretary (2014), Treasury Manager (2012-2013), Assistant to the Chief Financial Officer (2011), Regulatory Accounting Manager (2008-2010), held various accounting positions at Piller Data Systems (2006-2007), Hitachi Global Storage (2005), Abbot Laboratories (1998-2004), and Symantec (1998-2001).	43

<u>Name</u>	<u>Positions and Offices with California Water Service Group</u>	<u>Age</u>
Elissa Y. Ouyang(2) . . . . .	Chief Procurement and Lead Continuous Improvement Officer since March 1, 2016. Formerly, Interim Procurement Director (2013-2016), Acting District Manager—Los Altos (2013), Interim Vice President of Information Technology (2012-2013), Director of Information Technology—Architecture and Security (2008-2012), Business Application Manager (2003-2007), Project Lead/Senior Developer (2001-2003), held various business consulting positions at KPMG Consulting/BearingPoint (1998-2001), and RR Donnelley (1996-1998).	49
Gerald A. Simon(2) . . . . .	Chief Safety and Emergency Preparedness Officer since March 1, 2016. Formerly, Director of Safety and Emergency Services (2015), Emergency Services Manager (2014), Emergency Services Coordinator (2013), served as Fire Chief for Oakland, CA (2008-2011) and (1999-2004), Fire Chief for Fort Lauderdale, FL (2006-2007), Fire Chief for Union City, CA (2005-2006), Fire Chief for Santa Clara, CA (1993-1999) held various other positions at Santa Clara Fire Department (1976-1999), and Fire Services Consultant (1985-2015).	63

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- (1) Holds the same position with California Water Service Company, CWS Utility Services, Hawaii Water Service Company, Inc., and New Mexico Water Service Company; Chief Executive Officer of Washington Water Service Company.
  - (2) Holds the same position with California Water Service Company, CWS Utility Services, Hawaii Water Service Company, Inc., New Mexico Water Service Company, and Washington Water Service Company.

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## **Item 1A. Risk Factors.**

If any of the following risks actually occur, our financial condition and results of operations could be materially and adversely affected.

### **Risks Related to Our Regulatory Environment**

***Our business is heavily regulated by state and federal regulatory agencies and our financial viability depends upon our ability to recover costs from our customers through rates that must be approved by state public utility commissions.***

California Water Service Company, New Mexico Water Service Company, Washington Water Service Company and Hawaii Water Service Company, Inc., are regulated public utilities which provide water and water-related service to our customers. The rates that we charge our water customers are subject to the jurisdiction of the regulatory commissions in the states in which we operate. These Commissions may set water and water-related rates for each operating district independently because the systems are not interconnected. The Commissions authorize us to charge rates that they consider to be sufficient to recover normal operating expenses, to provide funds for adding new or replacing water infrastructure, and to allow us to earn what the Commissions consider to be a fair and reasonable return on invested capital.

Our revenues and consequently our ability to meet our financial objectives are dependent upon the rates we are authorized to charge our customers by the Commissions and our ability to recover our costs in these rates. Our management uses forecasts, models and estimates in order to set rates that will provide a fair and reasonable return on our invested capital. While our rates must be approved by the Commissions, no assurance can be given that our forecasts, models and estimates will be correct or that the Commissions will agree with our forecasts, models and estimates. If our rates are set too low, our revenues may be insufficient to cover our operating expenses, capital expenditure requirements and desired dividend levels.

We periodically file rate increase applications with the Commissions. The ensuing administrative and hearing process may be lengthy and costly. The decisions of the Commissions are beyond our control and we can provide no assurances that our rate increase requests will be granted by the Commissions. Even if approved, there is no guarantee that approval will be given in a timely manner or at a sufficient level to cover our expenses and provide a reasonable return on our investment. If the rate increase decisions are delayed, our earnings may be adversely affected.

***Our evaluation of the probability of recovery of regulatory assets is subject to adjustment by regulatory agencies and any such adjustment could adversely affect our results of operations.***

Regulatory decisions may also impact prospective revenues and earnings, affect the timing of the recognition of revenues and expenses and may overturn past decisions used in determining our revenues and expenses. Our management continually evaluates the anticipated recovery of regulatory assets and revenues subject to refund and provides for allowances and/or reserves as deemed necessary. Current accounting procedures allow us to defer certain costs if we believe it is probable that we will be allowed to recover those costs through future rate increases. If the Commissions determined that a portion of our assets were not recoverable in customer rates, we may suffer an asset impairment which would require a write down in such asset's valuation which would be recorded through operations.

If our assessment as to the probability of recovery through the ratemaking process is incorrect, the associated regulatory asset would be adjusted to reflect the change in our assessment or any regulatory disallowances. A change in our evaluation of the probability of recovery of regulatory



assets or a regulatory disallowance of all or a portion of our cost could have a material adverse effect on our financial results.

***Regulatory agencies may disagree with our valuation and characterization of certain of our assets.***

If we determine that assets are no longer used or useful for utility operations, we may remove them from our rate base and subsequently sell those assets. If the Commissions disagree with our characterization, we could be subjected to penalties. Furthermore, there is a risk that the Commissions could determine that realized appreciation in property value should be awarded to customers rather than our stockholders.

***Changes in laws, rules and policies of regulatory agencies can significantly affect our business.***

Regulatory agencies may change their rules and policies for various reasons, including changes in the local political environment. In some states, regulators are elected by popular vote or are appointed by elected officials, and the results of elections may change the long-established rules and policies of an agency dramatically. For example, in 2001 regulation regarding recovery of increases in electrical rates changed in California. For over 20 years prior to 2001, the CPUC allowed recovery of electric rate increases under its operating rules. However, in 2003, the CPUC reinstated its policy to allow utilities to adjust their rates for rate changes by the power companies. The original decision by the CPUC to change its policy, as well as its subsequent decision to reinstate that policy, affected our business.

We rely on policies and regulations promulgated by the various state commissions in order to recover capital expenditures, maintain favorable treatment on gains from the sale of real property, offset certain production and operating costs, recover the cost of debt, maintain an optimal equity structure without over-leveraging, and have financial and operational flexibility to engage in non-regulated operations. If any of the Commissions with jurisdiction over us implements policies and regulations that do not allow us to accomplish some or all of the items listed above, our future operating results may be adversely affected.

In addition, legislatures may repeal, relax or tighten existing laws, or enact new laws that impact the regulatory agencies with jurisdiction over our business or affect our business directly. If changes in existing laws or the implementation of new laws limit our ability to accomplish some of our business objectives, our future operating results may be adversely affected.

***We expect environmental health and safety regulation to increase, resulting in higher operating costs in the future.***

Our water and wastewater services are governed by various federal and state environmental protection, health and safety laws and regulations. These provisions establish criteria for drinking water and for discharges of water, wastewater and airborne substances. The EPA promulgates numerous nationally applicable standards, including maximum contaminant levels (MCLs) for drinking water. We believe we are currently in compliance with all of the MCLs promulgated to date. Although we have a rigorous water quality assurance program in place, we cannot guarantee that we will continue to comply with all standards. If we violate any federal or state regulations or laws governing health and safety, we could be subject to substantial fines or otherwise sanctioned.

Environmental health and safety laws are complex and change frequently. They tend to become more stringent over time. As new or stricter standards are introduced, they could increase our operating costs. Although we would likely seek permission to recover these costs through rate

increases, we can give no assurance that the Commissions would approve rate increases to enable us to recover these additional compliance costs.

We are required to test our water quality for certain chemicals and potential contaminants on a regular basis. If the test results indicate that our water exceeds allowable limits, we may be required either to commence treatment to remove the contaminant or to develop an alternate water source. Either of these results may be costly. Although we would likely seek permission to recover these through rate increases, there can be no assurance that the Commissions would approve rate increases to enable us to recover these additional compliance costs.

***New and/or more stringent water quality regulations could increase our operating costs.***

We are subject to water quality standards set by federal, state and local authorities that have the power to issue new regulations. Compliance with new regulations that are more stringent than current regulations could increase our operating costs.

On July 1, 2014, the California Department of Public Health (CDPH) changed the water quality standard for chromium-6 in our water supply. The new standard requires us to have 10 parts per billion or less of chromium-6 in our California water supply. The CPUC authorized a memorandum account in 2014 to track all costs associated with compliance with the new chromium-6 standard. Although we would likely seek permission to recover additional costs of compliance through rate increases, we can give no assurance that the CPUC would approve rate increases to enable us to recover these additional compliance costs.

***Legislation regarding climate change may impact our operations.***

Future legislation regarding climate change may restrict our operations or impose new costs on our business. Our operations depend on power provided by other public utilities and, in emergencies, power generated by our portable and fixed generators. If future legislation limits emissions from the power generation process, our cost of power may increase. Any increase in the cost of power will be passed along to our California customers through the MCBA or included in our cost of service paid by our customers as requested in our GRC filings. While recovery of these costs is not guaranteed, we would expect recovery in the regulatory process.

Starting January 1, 2010, under the California Environmental Quality Act (CEQA), all capital projects of a certain type (primarily wells, tanks, major pipelines and treatment facilities) will require mitigation of greenhouse gas emissions. The cost to prepare the CEQA documentation and permit will add an estimated ten thousand dollars to such capital projects. This cost will be included in our capital cost and added to our rate base, which will be requested to be paid for by our customers. Any increase in the operating cost of the facilities will also be included in our cost of service paid by our customers as requested in our GRC filings. While recovery of these costs is not guaranteed, we would expect recovery in the regulatory process.

Cap and trade regulations were implemented in 2012 with the goal of reducing emissions to 1990 levels by the year 2020. While recovery of these costs is not guaranteed, we would expect recovery in the regulatory process.

***We are party to a toxic contamination lawsuit which could result in us paying damages not covered by insurance.***

We have been and may be in the future, party to water contamination lawsuits, which may not be fully covered by insurance.

The number of environmental and product-related lawsuits against other water utilities have increased in frequency in recent years. If we are subject to additional environmental or product-

related lawsuits, we might incur significant legal costs and it is uncertain whether we would be able to recover the legal costs from customers or other third parties. In addition, if current California law regarding CPUC's preemptive jurisdiction over regulated public utilities for claims about compliance with California Department of Health Services and United States EPA water quality standards changes, our legal exposure may be significantly increased.

## **Risks Related to Our Business Operations**

### ***Wastewater operations entail significant risks.***

While wastewater collection and treatment is not presently a major component of our revenues, wastewater collection and treatment involve many risks associated with damage to the surrounding environment. If collection or treatment systems fail or do not operate properly, untreated or partially treated wastewater could discharge onto property or into nearby streams and rivers, causing property damage or injury to aquatic life, or even human life. Liabilities resulting from such damage could materially and adversely affect our results of operations and financial condition.

### ***Demand for our water is subject to various factors and is affected by seasonal fluctuations.***

Demand for our water during the warmer, dry months is generally greater than during cooler or rainy months due primarily to additional requirements for water in connection with irrigation systems, swimming pools, cooling systems and other outside water use. Throughout the year, and particularly during typically warmer months, demand will vary with temperature and rainfall levels. If temperatures during the typically warmer months are cooler than normal, or if there is more rainfall than normal, the demand for our water may decrease. Under the WRAM mechanism, lower water usage in our California operations impacts our cash flows in the year of usage, but results in higher cash flows in the following years.

In addition, governmental restrictions on water usage during drought conditions may result in a decreased demand for our water, even if our water reserves are sufficient to serve our customers during these drought conditions. The Commissions may not allow surcharges to collect lost revenues caused by customers' conservation during a drought. Regardless of whether we may surcharge our customers during a conservation period, they may use less water even after a drought has passed because of conservation patterns developed during the drought. Furthermore, our customers may wish to use recycled water as a substitute for potable water. If rights are granted to others to serve our customers recycled water, there will likely be a decrease in demand for our water.

Finally, changes in prevailing weather patterns due to climate change may affect customer demand. If increased ambient temperatures affect our service areas, water used for irrigation and cooling may increase. If rainfall patterns change, our customers may change their patterns of water use including the amount of outdoor irrigation and the type of landscape they install. Government agencies may also mandate changes to customer irrigation or landscape patterns in response to changes in weather and climate.

### ***The adequacy of our water supplies depends upon a variety of factors beyond our control. Interruption in the water supply may adversely affect our earnings.***

We depend on an adequate water supply to meet the present and future needs of our customers. Whether we have an adequate supply varies depending upon a variety of factors, many of which are partially or completely beyond our control, including:

- the amount of rainfall;

- the amount of water stored in reservoirs;
- underground water supply from which well water is pumped;
- availability from water wholesalers;
- changes in the amount of water used by our customers;
- water quality;
- legal limitations on water use such as rationing restrictions during a drought;
- changes in prevailing weather patterns and climate; and
- population growth.

We purchase our water supply from various governmental agencies and others. Water supply availability may be affected by weather conditions, funding and other political and environmental considerations. In addition, our ability to use surface water is subject to regulations regarding water quality and volume limitations. If new regulations are imposed or existing regulations are changed or given new interpretations, the availability of surface water may be materially reduced. A reduction in surface water could result in the need to procure more costly water from other sources, thereby increasing our water production costs and adversely affecting our operating results if not recovered in rates on a timely basis.

There is strong scientific consensus that human activity including carbon emissions is changing the chemical and thermodynamic characteristics of the atmosphere and the earth's overall climate. Because scientific efforts have been global in nature, and because climate modeling has not yet been predictive on a local scale, there is tremendous uncertainty over the timing, extent, and types of impacts global climate change may have in our service areas. In addition, studies of tree ring data show long periods of drought conditions have occurred in the historical record in California but prior to our operation. Thus, we include potential climate change risks in our water supply planning activities. We also periodically review the climate change plans of our wholesalers to determine whether alternative supplies may be necessary in the future. However, we can give no assurance that replacement water supplies will be available at a reasonable cost or a cost acceptable to our customers and Commissions.

We have entered into long-term water supply agreements, which commit us to making certain minimum payments whether or not we purchase any water. Therefore, if demand is insufficient to use our required purchases we would have to pay for water we did not receive.

From time to time, we enter into water supply agreements with third parties and our business is dependent upon such agreements in order to meet regional demand. For example, we have entered into a water supply contract with the SFPUC that expires on June 30, 2034. We can give no assurance that the SFPUC, or any of the other parties from whom we purchase water, will renew our contracts upon expiration, or that we will not be subject to significant price increases under any such renewed contracts.

The parties from whom we purchase water maintain significant infrastructure and systems to deliver water to us. Maintenance of these facilities is beyond our control. If these facilities are not adequately maintained or if these parties otherwise default on their obligations to supply water to us, we may not have adequate water supplies to meet our customers' needs.

If we are unable to access adequate water supplies we may be unable to satisfy all customer demand, which could result in rationing. Rationing may have an adverse effect on cash flow from operations. We can make no guarantee that we will always have access to an adequate supply of

water that will meet all required quality standards. Water shortages may affect us in a variety of ways. For example, shortages could:

- adversely affect our supply mix by causing us to rely on more expensive purchased water;
- adversely affect operating costs;
- increase the risk of contamination to our systems due to our inability to maintain sufficient pressure; and
- increase capital expenditures for building pipelines to connect to alternative sources of supply, new wells to replace those that are no longer in service or are otherwise inadequate to meet the needs of our customers and reservoirs and other facilities to conserve or reclaim water.

We may or may not be able to recover increased operating and construction costs on a timely basis, or at all, for our regulated systems through the ratemaking process. Although we can give no assurance, we may be able to recover certain of these costs from third parties that may be responsible, or potentially responsible, for groundwater contamination.

***Changes in water supply costs impact our operations.***

The cost to obtain water for delivery to our customers varies depending on the sources of supply, wholesale suppliers' prices, the quality of water required to be treated and the quantity of water produced to fulfill customer water demand. Our source of supply varies among our operating districts. Certain districts obtain all of their supply from wells; some districts purchase all of the supply from wholesale suppliers; and other districts obtain the supply from a combination of wells and wholesale suppliers. A small portion of supply comes from surface sources and is processed through Company-owned water treatment plants. On average, slightly more than half of the water we deliver to our customers is pumped from wells or received from a surface supply with the remainder purchased from wholesale suppliers. Water purchased from suppliers usually costs us more than surface supplied or well pumped water. The cost of purchased water for delivery to customers represented 34.8% and 34.0% of our total operating costs in 2017 and 2016, respectively. Water purchased from suppliers will require renewal of our contracts upon expiration and may result in significant price increases under any such renewed contracts.

Wholesale water suppliers may increase their prices for water delivered to us based on factors that affect their operating costs. Purchased water rate increases are beyond our control. In California, effective July 1, 2008, our ability to recover increases in the cost of purchased water changed with the adoption of the MCBA. With this change, actual purchased water costs are compared to authorized purchased water costs, with variances netted against the variances in purchased power, pump tax, and metered revenue, being recorded to revenue. The balance in the MCBA will be collected in the future by billing the net WRAM and MCBA accounts receivable balances over 12, 18, and 18+ month periods, which may have a short-term negative impact on cash flow.

***Dependency upon adequate supply of electricity and certain chemicals could adversely affect our results of operations.***

Purchased electrical power is required to operate the wells and pumps needed to supply water to our customers. Although there are back-up power generators to operate a number of wells and pumps in emergencies, an extended interruption in power could impact the ability to supply water. In the past, California has been subject to rolling power blackouts due to insufficient power supplies. There is no assurance we will not be subject to power blackouts in the future. Additionally, we require sufficient amounts of certain chemicals in order to treat the water we supply. There are

multiple sources for these chemicals but an extended interruption of supply could adversely affect our ability to adequately treat our water.

Purchased power is a significant operating expense. During 2017 and 2016, purchased power expense represented 5.0% and 5.1%, respectively, of our total operating costs. These costs are beyond our control and can change unpredictably and substantially as occurred in California during 2001 when rates paid for electricity increased 48%. As with purchased water, purchased power costs are included in the MCBA. Cash flows between rate filings may be adversely affected until the Commission authorizes a rate change, but earnings will be minimally impacted. Cost of chemicals used in the delivery of water is not an element of the MCBA, and therefore, variances in quantity or cost could impact the results of operations.

***Our business requires significant capital expenditures to replace or improve aging infrastructure that are dependent on our ability to secure appropriate funding. If we are unable to obtain sufficient capital or if the rates at which we borrow increase, there would be a negative impact on our results of operations.***

The water utility business is capital-intensive. We invest significant funds to replace or improve aging infrastructure such as property, plant and equipment. In addition, water shortages may adversely affect us by causing us to rely on more purchased water. This could cause increases in capital expenditures needed to build pipelines to secure alternative water sources. In addition, we require capital to grow our business through acquisitions. We fund our short-term capital requirements from cash received from operations and funds received from developers. We also borrow funds from banks under short-term bank lending arrangements. We seek to meet our long-term capital needs by raising equity through common or preferred stock issues or issuing debt obligations. We cannot give any assurance that these sources will continue to be adequate or that the cost of funds will remain at levels permitting us to earn a reasonable rate of return. In the event we are unable to obtain sufficient capital, our expansion efforts could be curtailed, which may affect our growth and may affect our future results of operations.

Our ability to access the capital markets is affected by the ratings of certain of our debt securities. Standard & Poor's Rating Agency issues a rating on California Water Service Company's ability to repay certain debt obligations. The credit rating agency could downgrade our credit rating based on reviews of our financial performance and projections or upon the occurrence of other events that could impact our business outlook. Lower ratings by the agency could restrict our ability to access equity and debt capital. We can give no assurance that the rating agency will maintain ratings which allow us to borrow under advantageous conditions and at reasonable interest rates. A future downgrade by the agency could also increase our cost of capital by causing potential investors to require a higher interest rate due to a perceived risk related to our ability to repay outstanding debt obligations.

While the majority of our debt is long term at fixed rates, we do have interest rate exposure in our short-term borrowings which have variable interest rates. We are also subject to interest rate risks on new financings. However, if interest rates were to increase on a long-term basis, our management believes that customer rates would increase accordingly, subject to approval by the appropriate commission. We can give no assurance that the Commission would approve such an increase in customer rates.

We are obligated to comply with specified debt covenants under certain of our loan and debt agreements. Failure to maintain compliance with these covenants could limit future borrowing, and we could face increased borrowing costs, litigation, acceleration of maturity schedules, and cross default issues. Such actions by our creditors could have a material adverse effect on our financial condition and results of operations.

***Our inability to access the capital or financial markets could affect our ability to meet our liquidity needs at reasonable cost and our ability to meet long-term commitments. Changes in economic conditions in our markets could affect our customers' ability to pay for water services. Any of these could adversely affect our results of operations, cash flows and financial condition.***

We rely on our current credit facilities to fund short-term liquidity needs if internal funds are not available from operations. Specifically, given the seasonal fluctuations in demand for our water we commonly draw on our credit facilities to meet our cash requirements at times in the year when demand is relatively low. We also may occasionally use letters of credit issued under our revolving credit facilities. Disruptions in the capital and credit markets could adversely affect our ability to draw on our credit facilities. Our access to funds under our credit facilities is dependent on the ability of our banks to meet their funding commitments.

Many of our customers and suppliers also have exposure to risks that could affect their ability to meet payment and supply commitments. We operate in geographic areas that may be particularly susceptible to declines in the price of real property, which could result in significant declines in demand for our products and services. In the event that any of our significant customers or suppliers, or a significant number of smaller customers and suppliers, are adversely affected by these risks, we may face disruptions in supply, significant reductions in demand for our products and services, inability of customers to pay invoices when due, and other adverse effects that could negatively affect our financial condition, results of operations and/or cash flows.

Our operations and certain contracts for water distribution and treatment depend on the financial capability of state and local governments, and other municipal entities such as water districts. Major disruptions in the financial strength or operations of such entities, such as liquidity limitations, bankruptcy or insolvency, could have an adverse effect on our ability to conduct our business and/or enforce our rights under contracts to which such entities are a party.

***We are a holding company that depends on cash flow from our subsidiaries to meet our obligations and to pay dividends on our common stock.***

As a holding company, we conduct substantially all of our operations through our subsidiaries and our only significant assets are investments in those subsidiaries. 93.9% of our revenues are derived from the operations of California Water Service Company. As a result, we are dependent on cash flow from our subsidiaries, and California Water Service Company in particular, to meet our obligations and to pay dividends on our common stock.

Our subsidiaries are separate and distinct legal entities and generally have no obligation to pay any amounts due on California Water Service Group's debt or to provide California Water Service Group with funds for dividends. Although there are no contractual or regulatory restrictions on the ability of our subsidiaries to transfer funds to us, the reasonableness of our capital structure is one of the factors considered by state and local regulatory agencies in their ratemaking determinations. Therefore, transfer of funds from our subsidiaries to us for the payment of our obligations or dividends may have an adverse effect on ratemaking determinations. Furthermore, our right to receive cash or other assets upon the liquidation or reorganization of a subsidiary is generally subject to the prior claims of creditors of that subsidiary. If we are unable to obtain funds from our subsidiaries in a timely manner, we may be unable to meet our obligations or pay dividends.

We can make dividend payments only from our surplus (the excess, if any, of our net assets over total paid-in capital) or if there is no surplus, the net profits for the current fiscal year or the fiscal year before which the dividend is declared. In addition, we can pay cash dividends only if after paying those dividends we would be able to pay our liabilities as they become due. Owners of our capital stock cannot force us to pay dividends and dividends will only be paid if and when declared

by our board of directors. Our board of directors can elect at any time, and for an indefinite duration, not to declare dividends on our capital stock.

***An important element of our growth strategy is the acquisition of water and wastewater systems. Risks associated with potential acquisitions, divestitures or restructurings may adversely affect us.***

We may seek to acquire or invest in other companies, technologies, services or products that complement our business. The execution of our growth strategy may expose us to different risks than those associated with our utility operations. We can give no assurance that we will succeed in finding attractive acquisition candidates or investments, or that we would be able to reach mutually agreeable terms with such parties. In addition, as consolidation becomes more prevalent in the water and wastewater industries, the prices for suitable acquisition candidates may increase to unacceptable levels and limit our ability to grow through acquisitions. If we are unable to find acquisition candidates or investments, our ability to grow may be limited.

Acquisition and investment transactions may result in the issuance of our equity securities that could be dilutive if the acquisition or business opportunity does not develop in accordance with our business plan. They may also result in significant write-offs and an increase in our debt. The occurrence of any of these events could have a material adverse effect on our business, financial condition and results of operations.

Any of these transactions could involve numerous additional risks, including one or more of the following:

- problems integrating the acquired operations, personnel, technologies or products with our existing businesses and products;
- liabilities inherited from the acquired companies' prior business operations;
- diversion of management time and attention from our core business to the acquired business;
- failure to retain key technical, management, sales and other personnel of the acquired business;
- difficulty in retaining relationships with suppliers and customers of the acquired business; and
- difficulty in getting required regulatory approvals.

In addition, the businesses and other assets we acquire may not achieve the sales and profitability expected. The occurrence of one or more of these events may have a material adverse effect on our business. There can be no assurance that we will be successful in overcoming these or any other significant risks encountered.

***We may not be able to increase or sustain our recent growth rate, and we may not be able to manage our future growth effectively.***

We may be unable to continue to expand our business or manage future growth. To successfully manage our growth and handle the responsibilities of being a public company, we must effectively:

- hire, train, integrate and manage additional qualified engineers for engineering design and construction activities, new business personnel, and financial and information technology personnel;



- retain key management, augment our management team, and retain qualified and certified water and wastewater system operators;
- implement and improve additional and existing administrative, financial and operations systems, procedures and controls;
- expand our technological capabilities; and
- manage multiple relationships with our customers, regulators, suppliers and other third parties.

If we are unable to manage our growth effectively, we may not be able to take advantage of market opportunities, satisfy customer requirements, execute our business plan or respond to competitive pressures.

***We have a number of large-volume commercial and industrial customers and a significant decrease in consumption by one or more of these customers could have an adverse effect on our operating results and cash flows.***

Our billed revenues and cash flows from operations will decrease if a significant business or industrial customer terminates or materially reduces its use of our water. Approximately \$161.7 million, or 24.3%, of our 2017 water utility revenues was derived from business and industrial customers. However, if any of our large business or industrial customers in California reduce or cease its consumption of our water, the impact to net operating income would be minimal to our operations due to the WRAM and MCBA, but could impact our cash flows. In Hawaii, we serve a number of large resorts which if their water usage was reduced or ceased could have a material impact to our Hawaii operation. The delay between such date and the effective date of the rate relief may be significant and could adversely affect our operating results and cash flows.

***Our operating cost and costs of providing services may rise faster than our revenues.***

Our ability to increase rates over time is dependent upon approval of such rate increases by the Commissions, or in the case of the City of Hawthorne and the City of Commerce, the City Council, which may be inclined, for political or other reasons, to limit rate increases. However, our costs, which are subject to market conditions and other factors, may increase significantly. The second largest component of our operating costs after water production is made up of salaries and wages. These costs are affected by the local supply and demand for qualified labor. Other large components of our costs are general insurance, workers compensation insurance, employee benefits and health insurance costs. These costs may increase disproportionately to rate increases authorized by the Commissions and may have a material adverse effect on our future results of operations.

***Demand for our stock may fluctuate due to circumstances beyond our control.***

We believe that stockholders invest in public utility stocks, in part, because they seek reliable dividend payments. If there is an over-supply of stock of public utilities in the market relative to demand by such investors, the trading price of our securities could decrease. Additionally, if interest rates rise above the dividend yield offered by our equity securities, demand for our stock, and consequently its market price, may also decrease. A decline in demand for our stock may have a negative impact on our ability to finance capital projects.

***Adverse investment returns and other factors may increase our pension liability and pension funding requirements.***

A substantial number of our employees are covered by a defined benefit pension plan. At present, the pension plan is underfunded because our projected pension benefit obligation exceeds the aggregate fair value of plan assets. Under applicable law, we are required to make cash contributions to the extent necessary to comply with minimum funding levels imposed by regulatory requirements. The amount of such required cash contribution is based on an actuarial valuation of the plan. The funded status of the plan can be affected by investment returns on plan assets, discount rates, mortality rates of plan participants, pension reform legislation and a number of other factors. There can be no assurance that the value of our pension plan assets will be sufficient to cover future liabilities. Although we have made contributions to our pension plan in recent years, it is possible that we could incur a pension liability adjustment, or could be required to make additional cash contributions to our pension plan, which would reduce the cash available for business and other needs.

***Labor relations matters could adversely affect our operating results.***

At December 31, 2017, 750 of our 1,176 total employees were union employees. Most of our unionized employees are represented by the Utility Workers Union of America, AFL-CIO, except certain engineering and laboratory employees who are represented by the International Federation of Professional and Technical Engineers, AFL-CIO.

We believe our labor relations are good, but in light of rising costs for health care and pensions, contract negotiations in the future may be difficult. Furthermore, changes in applicable law or regulations could have an adverse effect on management's negotiating position with respect to our currently unionized employees and/or employees that decide to unionize in the future. We are subject to a risk of work stoppages and other labor relations matters as we negotiate with the unions to address these issues, which could affect our results of operations and financial condition. We can give no assurance that issues with our labor forces will be resolved favorably to us in the future or that we will not experience work stoppages.

***We depend significantly on the services of the members of our management team, and the departure of any of those persons could cause our operating results to suffer.***

Our success depends significantly on the continued individual and collective contributions of our management team. The loss of the services of any member of our management team could have an adverse effect on our business as our management team has knowledge of our industry and customers and would be difficult to replace.

***Our operations are geographically concentrated in California and this lack of diversification may negatively impact our operations.***

Although we own facilities in a number of states, over 93.9% of our operations are located in California. As a result, we are largely subject to weather, political, water supply, labor, energy cost, regulatory and economic risks affecting California.

We are also affected by the real property market in California. In order to grow our business, we may need to acquire additional real estate or rights to use real property owned by third parties, the cost of which tends to be higher and more volatile in California than in other states. The value of our assets in California may decline if there is a decline in the California real estate market which results in a significant decrease in real property values.

***The effects of natural disasters, terrorist activity, pandemics, or poor water quality or contamination to our water supply may result in disruption in our services and litigation which could adversely affect our business, operating results and financial condition.***

We operate in areas that are prone to earthquakes, fires, mudslides and other natural disasters. A significant seismic event or other natural disaster in California where our operations are concentrated could adversely impact our ability to deliver water and adversely affect our costs of operations. A major disaster could damage or destroy substantial capital assets. The CPUC has historically allowed utilities to establish a catastrophic event memorandum account as another possible mechanism to recover costs. However, we can give no assurance that the CPUC or any other commission would allow any such cost recovery mechanism in the future.

Our water supplies are subject to contamination, including contamination from the development of naturally-occurring compounds, chemicals in groundwater systems, pollution resulting from man-made sources, such as MTBE, sea water incursion and possible terrorist attacks. If our water supply is contaminated, we may have to interrupt the use of that water supply until we are able to substitute the flow of water from an uncontaminated water source. In addition, we may incur significant costs in order to treat the contaminated source through expansion of our current treatment facilities, or development of new treatment methods. If we are unable to substitute water supply from an uncontaminated water source, or to adequately treat the contaminated water source in a cost-effective manner, there may be an adverse effect on our revenues, operating results and financial condition. The costs we incur to decontaminate a water source or an underground water system could be significant and may not be recoverable in rates. We could also be held liable for consequences arising out of human exposure to hazardous substances in our water supplies or other environmental damage. For example, private plaintiffs have the right to bring personal injury or other toxic tort claims arising from the presence of hazardous substances in our drinking water supplies. Our insurance policies may not be sufficient to cover the costs of these claims.

We operate a dam. If the dam were to fail for any reason, we would lose a water supply and flooding likely would occur. Whether or not we were responsible for the dam's failure, we could be sued. We can give no assurance that we would be able to successfully defend such a suit.

In light of the threats to the nation's health and security ensuing in the wake of the September 11, 2001 terrorist attacks, we have taken steps to increase security measures at our facilities and heighten employee awareness of threats to our water supply. We have also tightened our security measures regarding the delivery and handling of certain chemicals used in our business. We have and will continue to bear increased costs for security precautions to protect our facilities, operations and supplies. These costs may be significant. Despite these tightened security measures, we may not be in a position to control the outcome of terrorist events should they occur.

We depend upon our skilled and trained workforce to ensure water delivery. Were a pandemic to occur, we can give no assurance that we would be able to maintain sufficient manpower to ensure uninterrupted service in all of the districts that we serve.

***We retain certain risks not covered by our insurance policies.***

We evaluate our risks and insurance coverage annually. Our evaluation considers the costs, risks and benefits of retaining versus insuring various risks as well as the availability of certain types of insurance coverage. Furthermore, we are also affected by increases in prices for insurance coverage; in particular, we have been, and will continue to be, affected by rising health insurance costs. Retained risks are associated with deductible limits, partial self-insurance programs and insurance policy coverage ceilings. If we suffer an uninsured loss, we may be unable to pass all, or any portion, of the loss on to customers because our rates are regulated by regulatory commissions.

Consequently, uninsured losses may negatively affect our financial condition, liquidity and results of operations. There can be no assurance that we will not face uninsured losses pertaining to the risks we have retained.

***We rely on our information technology (“IT”) and a number of complex business systems to assist with the management of our business and customer and supplier relationships, and a disruption of these systems could adversely affect our business.***

Our IT systems are an integral part of our business, and a serious disruption of our IT systems could significantly limit our ability to manage and operate our business efficiently, which, in turn, could cause our business and competitive position to suffer and adversely affect our results of operations. We depend on our IT systems to bill customers, process orders, provide customer service, manage construction projects, manage our financial records, track assets, remotely monitor certain of our plants and facilities and manage human resources, inventory and accounts receivable collections. Our IT systems also enable us to purchase products from our suppliers and bill customers on a timely basis, maintain cost-effective operations and provide service to our customers. Some of our mission and business critical IT systems are older, such as our SCADA (Supervisory Control and Data Acquisition) system. Although we do not believe that our IT systems are at a materially greater risk of cyber security incidents than other similar organizations, our IT systems remain vulnerable to damage or interruption from:

- power loss, computer systems failures, and internet, telecommunications or data network failures;
- operator negligence or improper operation by, or supervision of, employees;
- physical and electronic loss of customer data due to security breaches, cyber attacks, misappropriation and similar events;
- computer viruses;
- intentional security breaches, hacking, denial of services actions, misappropriation of data and similar events; and
- earthquakes, floods, fires, mudslides and other natural disasters.

These events may result in physical and/or electronic loss of customer or financial data, security breaches, misappropriation and other adverse consequences. In addition, the lack of redundancy for certain of our IT systems, including billing systems, could exacerbate the impact of any of these events on us.

In addition, we may not be successful in developing or acquiring technology that is competitive and responsive to the needs of our business, and we might lack sufficient resources to make the necessary upgrades or replacements of our outdated existing technology to allow us to continue to operate at our current level of efficiency.

***The accuracy of our judgments and estimates about financial and accounting matters will impact our operating results and financial condition.***

We make certain estimates and judgments in preparing our financial statements regarding, among others:

- the useful life of intangible rights;
- the number of years to depreciate certain assets;
- amounts to set aside for uncollectible accounts receivable, inventory obsolescence and uninsured losses;

- our legal exposure and the appropriate accrual for claims, including medical claims and workers' compensation claims;
- future costs and assumptions for pensions and other postretirement benefits;
- regulatory recovery of regulatory assets;
- possible tax uncertainties; and
- projected collections of WRAM and MCBA receivables.

The quality and accuracy of those estimates and judgments will have an impact on our operating results and financial condition.

In addition, we must estimate unbilled revenues and costs as of the end of each accounting period. If our estimates are not accurate, we will be required to make an adjustment in a future period. Accounting rules permit us to use expense balancing accounts and memorandum accounts that include cost changes to us that are different from amounts incorporated into the rates approved by the Commissions. These accounts result in expenses and revenues being recognized in periods other than in which they occurred.

***Municipalities, water districts and other public agencies may condemn our property by eminent domain action.***

State statutes allow municipalities, water districts and other public agencies to own and operate water systems. These agencies are empowered to condemn water systems or real property owned by privately owned public utilities in certain circumstances and in compliance with California and federal law. Additionally, whenever a public agency constructs facilities to extend its utility system into the service area of a privately owned public utility, such an act may constitute the taking of property and require reimbursement to the public utility for its loss. If a public agency were to file an eminent domain lawsuit against us, we would incur substantial attorney's fees, consultant and expert fees and other costs in considering a challenge to the right to take our utility property and/or its valuation for just compensation, as well as such fees and costs in any subsequent litigation if necessary. If the public agency prevailed and acquired our utility property, we would be entitled to just compensation for our loss, but we would no longer have access to the condemned property or water system. Neither would we be entitled to any portion of revenue generated from the use of such asset going forward.

**Item 1B. *Unresolved Staff Comments.***

None.

**Item 2. *Properties.***

Our physical properties consist of offices and water facilities to accomplish the production, storage, treatment, and distribution of water. These properties are located in or near the geographic service areas listed above in Item 1, "Business—Geographical Service Areas and Number of Customer Connections at Year-end." Our headquarters, which houses accounting, engineering, information systems, human resources, purchasing, regulatory, water quality, and executive staff, is located in San Jose, California.

The real properties owned are held in fee simple title. Properties owned by Cal Water are subject to the lien of an Indenture of Mortgage and Deed of Trust dated March 16, 2016, October 13, 2015, November 17, 2010, and April 17, 2009 (the California Indenture), securing Cal Water's First Mortgage Bonds, of which \$521.4 million was outstanding at December 31, 2017. The California Indenture contains certain restrictions common to such types of instruments regarding

the disposition of property and includes various covenants and restrictions. At December 31, 2017, our California utility was in compliance with the covenants of the California Indenture.

Cal Water owns 602 wells and operates ten leased wells. There are 444 owned storage tanks with a capacity of 278 million gallons, two leased storage tanks with a capacity of 0.4 million gallons, 30 managed storage tanks with a capacity of 32.4 million gallons, and three surface water reservoirs with a capacity of 220 million gallons. Cal Water owns and operates six surface water treatment plants with a combined capacity of 46 million gallons per day. There are 5,834 miles of supply and distribution mains in the various systems.

Hawaii Water owns 22 wells and manages two irrigation wells. There are 24 storage tanks with a storage capacity of 20.1 million gallons. There are 70 miles of supply and distribution lines. Hawaii Water operates five wastewater treatment facilities with a combined capacity to process approximately 1.8 million gallons per day. There are 26 miles of sewer collection mains.

Washington Water owns 350 wells and manages 57 wells. There are 137 owned storage tanks and 18 managed storage tanks with a storage capacity of 9.5 million gallons. There are 405 miles of supply and distribution lines.

New Mexico Water owns 19 wells. There are 17 storage tanks with a storage capacity of 4.3 million gallons. There are 145 miles of supply and distribution lines. New Mexico operates two waste water treatment facilities with a combined capacity to process 0.6 million gallons per day. There are 34 miles of sewer collection mains.

Washington Water has long-term bank loans that are secured primarily by utility plant owned by Washington Water.

In the leased City of Hawthorne and City of Commerce systems or in systems that are operated under contract for municipalities or private companies, title to the various properties is held exclusively by the municipality or private company.

### **Item 3. *Legal Proceedings.***

Information with respect to this item may be found under the subheading "Commitments and Contingencies" in Note 14 to the consolidated Financial Statements in Item 8, which is incorporated herein by reference.

### **Item 4. *Mine Safety Disclosures.***

Not applicable.

## PART II

### **Item 5. Market for Registrant's Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.**

Our common stock is traded on the New York Stock Exchange under the symbol "CWT." At December 31, 2017, there were 48,012,432 common shares outstanding. There were 1,934 common stockholders of record as of February 12, 2018.

During 2017, we paid a cash dividend of \$0.7200 per common share, or \$0.1800 per quarter. During 2016, we paid a cash dividend of \$0.6900 per common share, or \$0.1725 per quarter. On January 31, 2018, our Board of Directors declared a quarterly cash dividend of \$0.1875 per common share payable on February 23, 2018, to stockholders of record on February 12, 2018. This represents our 51st consecutive year of increasing the annual dividend and marks the 292nd consecutive quarterly dividend.

We presently intend to pay quarterly cash dividends in the future consistent with past practices, subject to our earnings and financial condition, restrictions set forth in our debt instruments, regulatory requirements and such other factors as our Board of Directors may deem relevant.

During 2017 and 2016, the common stock market price range and dividends per share for each quarter were as follows:

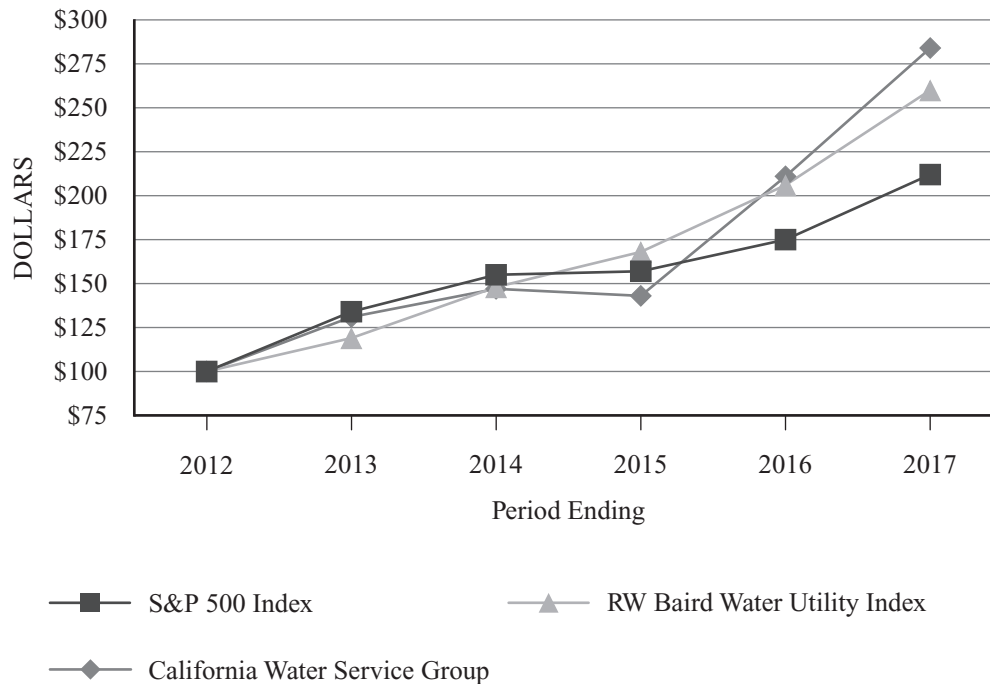
<b><u>2017</u></b>	<b><u>First</u></b>	<b><u>Second</u></b>	<b><u>Third</u></b>	<b><u>Fourth</u></b>
Common stock market price range:				
High . . . . .	\$ 37.60	\$ 39.40	\$ 39.65	\$ 46.15
Low . . . . .	32.45	32.75	36.30	38.15
Dividends paid per common share . . .	0.1800	0.1800	0.1800	0.1800
<b><u>2016</u></b>	<b><u>First</u></b>	<b><u>Second</u></b>	<b><u>Third</u></b>	<b><u>Fourth</u></b>
Common stock market price range:				
High . . . . .	\$ 27.33	\$ 34.95	\$ 35.62	\$ 36.85
Low . . . . .	22.48	26.22	29.93	29.25
Dividends paid per common share . . .	0.1725	0.1725	0.1725	0.1725

Form 10-K

## Five-Year Performance Graph

The following performance graph compares the changes in the cumulative shareholder return on California Water Service Group's common stock with the cumulative total return on the Robert W. Baird Water Utility Index and the Standard & Poor's 500 Index during the last five years ended December 31, 2017. The comparison assumes \$100 was invested on December 31, 2012, in California Water Service Group's common stock and in each of the forgoing indices and assumes reinvestment of dividends.

### Performance Graph Data



The following descriptive data is supplied in accordance with Rule 304(d) of Regulations S-T:

	2012	2013	2014	2015	2016	2017
<b>California Water Service Group</b> . . . . .	100	131	147	143	211	284
<b>S&amp;P 500</b> . . . . .	100	134	155	157	175	212
<b>RW Baird Water Utility Index</b> . . . . .	100	119	148	168	206	260

An initial \$100 investment in the common stock of California Water Service Group on December 31, 2012 including reinvestment of dividends would be worth \$284 at the end of the 5-year period ending December 31, 2017.

### Item 6. Selected Financial Data.

The following selected consolidated financial data should be read in conjunction with our Consolidated Financial Statements and the Notes thereto and the information contained in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Historical results are not necessarily indicative of future results.



## FIVE YEAR FINANCIAL REVIEW

	2017	2016	2015	2014	2013
<b>(Dollars in thousands, except per common share and other data)</b>					
<b>Summary of Operations</b>					
Operating revenue					
Residential . . . . .	\$ 480,229	\$ 439,668	\$ 416,102	\$ 406,322	\$ 406,824
Business . . . . .	132,309	123,395	116,639	111,438	111,529
Industrial . . . . .	29,417	28,086	31,725	24,957	26,290
Public authorities . . . . .	37,716	33,604	26,042	30,810	31,067
Other . . . . .	20,578	19,148	18,094	16,766	17,553
MCBA net adjustment to increase (decrease) revenue . .	(33,359)	(34,531)	(20,234)	7,206	(9,160)
Total operating revenue . . . . .	666,890	609,370	588,368	597,499	584,103
Total operating expenses . . . . .	572,267	533,176	517,215	515,652	510,098
Interest expense, other income and expenses, net . . . . .	27,442	27,519	26,136	25,109	26,751
<b>Net income . . . . .</b>	<b>\$ 67,181</b>	<b>\$ 48,675</b>	<b>\$ 45,017</b>	<b>\$ 56,738</b>	<b>\$ 47,254</b>
<b>Common Share Data</b>					
Earnings per share—diluted . . . . .	\$ 1.40	\$ 1.01	\$ 0.94	\$ 1.19	\$ 1.02
Dividend paid . . . . .	0.720	0.690	0.670	0.650	0.640
Dividend payout ratio . . . . .	51%	68%	71%	55%	63%
Book value per share . . . . .	\$ 14.44	\$ 13.75	\$ 13.41	\$ 13.11	\$ 12.54
Market price at year-end . . . . .	45.35	33.90	23.27	24.61	23.07
Common shares outstanding at year-end (in thousands) . . . . .	48,012	47,965	47,875	47,806	47,741
Return on average common stockholders' equity . . . . .	9.9%	7.5%	7.1%	9.3%	8.8%
Long-term debt interest coverage .	4.28	3.45	3.67	4.29	3.42
<b>Balance Sheet Data</b>					
Net utility plant . . . . .	\$2,047,965	\$1,859,277	\$1,701,768	\$1,590,431	\$1,515,831
Total assets* . . . . .	2,740,375	2,411,745	2,241,253	2,182,711	1,954,741
Long-term debt including current portion* . . . . .	531,713	557,953	514,045	421,200	428,936
Capitalization ratios:					
Common stockholders' equity* .	56.6%	54.2%	55.5%	59.8%	58.3%
Long-term debt* . . . . .	43.4%	45.8%	44.5%	40.2%	41.7%
<b>Other Data</b>					
Estimated water production (million gallons)					
Wells and surface supply . . . . .	53,855	50,942	51,413	61,848	64,161
Purchased . . . . .	51,131	48,154	47,486	56,434	62,202
Total estimated water production .	104,986	99,096	98,899	118,282	126,363
Metered customers . . . . .	490,100	485,200	477,300	472,500	464,800
Flat-rate customers . . . . .	24,200	26,300	31,700	33,600	38,100
Customers at year-end** . . . . .	514,300	511,500	509,000	506,100	502,900
New customers added . . . . .	2,800	2,500	2,900	3,200	2,200
Revenue per customer . . . . .	\$ 1,297	\$ 1,191	\$ 1,156	\$ 1,181	\$ 1,161
Utility plant per customer . . . . .	5,775	5,312	4,925	4,628	4,401
Employees at year-end . . . . .	1,176	1,163	1,155	1,105	1,125

\* The five year financial review for 2015, 2014, and 2013 reflect the retrospective adoption of ASU 2015-03, which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The Company adopted this guidance effective January 1, 2016.

\*\* Includes customers of the City of Hawthorne and City of Commerce

## **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.**

### **Overview**

In 2017 and 2016, net income was \$67.2 million and \$48.7 million, respectively. Diluted earnings per share increased \$0.39 to \$1.40 or 38.6% from 2016 to 2017. The \$18.5 million increase in net income was primarily the result of increased rates adopted in the recent California GRC, a decrease in other operations expense, which included a GRC settlement agreement to write-off \$3.2 million associated with a canceled water supply project in Bakersfield in 2016, and a \$2.5 million increase in estimated unbilled revenue in 2017. These decreases were partially offset by increases in depreciation and amortization, employee wage, property tax, and net interest expenses. Net other income increased \$3.5 million to \$6.5 million in 2017, due primarily to the authorization of allowance for equity funds used during construction and unrealized gains on certain benefit plan investments.

In 2016 and 2015, net income was \$48.7 million and \$45.0 million, respectively. Diluted earnings per share increased \$0.07 to \$1.01 or 7.5% from 2015 to 2016. The \$3.7 million increase in net income was primarily a result of a \$2.8 million net resolution of several regulatory memorandum and balancing accounts in the Cal Water 2015 GRC settlement agreement, a \$1.9 million increase from the recovery of prior years' incremental drought program costs, and a \$1.7 million increase in estimated unbilled revenue in 2016. These increases were partially offset by increases in other operations expense, which included a GRC settlement agreement to write-off \$3.2 million associated with a canceled water supply project in Bakersfield, increases in depreciation and amortization, maintenance, property tax, employee wage, and net interest expenses. Net other income increased \$1.9 million to \$3.0 million in 2016, due primarily to the resolution of \$1.5 million of litigation proceeds in the GRC settlement agreement and unrealized gains on certain benefit plan investments.

We plan to continue to seek rate relief to recover our operating cost increases and receive reasonable returns on invested capital. We expect to fund our long-term capital needs through a combination of debt, common stock offerings, and cash flow from operations.

### **Critical Accounting Policies and Estimates**

We maintain our accounting records in accordance with accounting principles generally accepted in the United States of America and as directed by the Commissions to which our operations are subject. The process of preparing financial statements requires the use of estimates on the part of management. The estimates used by management are based on historic experience and an understanding of current facts and circumstances. A summary of our significant accounting policies is listed in Note 2 of the Notes to Consolidated Financial Statements. The following sections describe those policies where the level of subjectivity, judgment, and variability of estimates could have a material impact on the financial condition, operating performance, and cash flows of the business.

### **Revenue Recognition**

Revenue generally includes monthly cycle customer billings for regulated water and wastewater services at rates authorized by the Commissions (plus an estimate for water used between the customer's last meter reading and the end of the accounting period) and billings to certain non-regulated customers at rates authorized by contract with government agencies.

The Company's regulated water and waste water revenue requirements are authorized by the Commissions in the states in which we operate. The revenue requirements are intended to provide

the Company a reasonable opportunity to recover its cost of service and earn a return on investments.

For metered customers, Cal Water recognizes revenue from rates which are designed and authorized by the CPUC. Under the WRAM, Cal Water records the adopted level of volumetric revenues, which would include recovery of cost of service and a return on investments as established by the CPUC for metered accounts. 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 regulatory asset or liability balancing account (tracked individually for each Cal Water district) subject to certain criteria under the accounting for regulated operations. The variance amount represents amounts that will be billed or refunded to customers in the future. In addition to volumetric revenues, the revenue requirements approved by the CPUC include service charges, flat rate charges, and other items not subject to the WRAM.

Cost-recovery rates are designed to permit full recovery of certain costs allowed to be recovered by the Commissions. Cost-recovery rates such as the MCBA provides for recovery of adopted expense levels for purchased water, purchased power and pump taxes, as established by the CPUC. In addition, cost-recovery rates include recovery of cost related to water conservation programs and certain other operating expenses adopted by the CPUC. Variances (which include the effects of changes in both rate and volume for the MCBA) between adopted and actual costs are recorded as a component of revenue, as the amount of such variances will be recovered from or refunded to our customers at a later date. Cost-recovery expenses are generally recognized when the expenses are incurred with no markup for return or profit.

The balances in the WRAM and MCBA assets and liabilities accounts will 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 the deferred net balances are interest bearing at the current 90-day commercial paper rate. At the end of the calendar year, Cal Water files with the CPUC to refund or collect the balance in the accounts. The majority of under-collected net WRAM and MCBA receivable balances are collected over 12 and 18 months. Cal Water defers any net WRAM and MCBA revenues and associated costs whenever the net receivable balances are estimated to be collected more than 24 months after the respective reporting period in which it was recorded. The deferred net WRAM and MCBA revenue and associated costs were determined using forecasts of customer consumption trends in future reporting periods and the timing of when the CPUC will authorize Cal Water's filings to recover unbilled balances. Deferred revenues and associated costs are recorded in the periods when the collection is within 24 months of the respective reporting period.

Customers' meter reads occur on various business days throughout the month. As a result, there are unmetered or unbilled customer usage each month. The estimated unbilled revenue for monthly unmetered customer usage is recorded using the number of unbilled days for that month and average daily customer billing rate for the previous month. The average daily customer billing rate for the previous month fluctuates depending on customer usage. Estimated unbilled revenue is not included in the WRAM until it is billed.

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 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. Our unearned revenue liability was \$0.7 million as of December 31, 2017 and was \$0.8 million as of December 31, 2016. This liability is included in "other accrued liabilities" on our consolidated balance sheets.

## **Regulated Utility Accounting**

Because we operate almost exclusively in a regulated business, we are subject to the accounting standards for regulated utilities. The Commissions in the states in which we operate establish rates that are designed to permit the recovery of the cost of service and a return on investment. We capitalize and record regulatory assets for costs that would otherwise be charged to expense if it is probable that the incurred costs will be recovered in future rates. Regulatory assets are amortized over the future periods that the costs are expected to be recovered. If costs expected to be incurred in the future are currently being recovered through rates, we record those expected future costs as regulatory liabilities. In addition, we record regulatory liabilities when the Commissions require a refund to be made to our customers over future periods.

Determining probability requires significant judgment by management and includes, but is not limited to, consideration of testimony presented in regulatory hearings, proposed regulatory decisions, final regulatory orders, and the strength or status of applications for rehearing or state court appeals.

If we determine that a portion of our assets used in utility operations is not recoverable in customer rates, we would be required to recognize the loss of the assets disallowed.

## **Income Taxes**

We account for income taxes using the asset and liability method. Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. We measure deferred tax assets and liabilities at enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. We recognize the effect on the deferred tax assets and liabilities of a change in tax rate in the period that includes the enactment date. We also assess the likelihood that deferred tax assets will be recovered in future taxable income and, to the extent recovery is not probable, a valuation allowance would be recorded. In management's view, a valuation allowance was not required as of December 31, 2017 and December 31, 2016.

We anticipate that future rate actions by the regulatory commissions will reflect revenue requirements for the tax effects of temporary differences recognized, which have previously been passed through to customers. The regulatory commissions have granted the Company permission to reflect the normalization of the tax benefits of the federal accelerated methods and available Investment Tax Credits (ITCs) for all assets placed in service after 1980. ITCs are deferred and amortized over the lives of the related properties for book purposes. The CPUC requires flow through accounting for state deferred taxes.

On December 22, 2017, the Tax Cuts and Jobs Act (TCJA) was enacted. Based on the accounting principles generally accepted in the United States of America, the Company is required to re-measure deferred income taxes to reflect the corporate income tax rate change from 35 percent to 21 percent as of the date of enactment. The re-measurement of the deferred income taxes resulted in an estimated excess deferred income tax liability of \$108.0 million as of December 31, 2017. The TCJA will lower customer rates due to lower income tax expense recoveries and the refund of excess deferred income tax. These lower customer rates will be partially offset by the TCJA's effect of increasing rate base in future years. The Company is working with state regulators on the refund process according to federal income tax normalization rules. There are aspects to the TCJA that contain technical matters that require management to interpret the legislation and make judgments until further guidance becomes available. As a result, changes in management's judgments could materially affect amounts recognized in the financial statements.

## Pension and Postretirement Health Care Benefits

We incur costs associated with our pension and postretirement health care benefits plans. To measure the expense of these benefits, our management must estimate compensation increases, mortality rates, future health cost increases and discount rates used to value related liabilities and to determine appropriate funding. Different estimates used by our management could result in significant variances in the cost recognized for pension and postretirement health care benefit plans. The estimates used are based on historical experience, current facts, future expectations, and recommendations from independent advisors and actuaries. We use an investment advisor to provide advice in managing the plan's investments. We anticipate any increases in funding for the pension benefits plans will be recovered in future rate filings, thereby mitigating the financial impact. We believe it is probable that future costs will be recovered in future rates and therefore have recorded a regulatory asset in accordance with generally accepted accounting principles.

Changes to the pension benefits actuarial assumptions can significantly affect pension costs, regulatory assets, and liabilities. The following table reflects the sensitivity of pension amounts reported for the year ended December 31, 2017, to changes in actuarial assumptions:

	Increase/(Decrease) in Pension Benefits Actuarial Assumption	Increase/(Decrease) in 2017 Net Periodic Benefit Cost	Increase/(Decrease) in Projected Benefit Obligation as of December 31, 2017
Discount rate . . . . .	(0.5)%	\$ 6,722	\$ 70,501
Long-term rate of return on plan assets . . . . .	(0.5)%	1,855	—
Rate of compensation increases . .	(0.5)%	(2,831)	(18,590)
Cost of living adjustment . . . . .	(0.5)%	(5,281)	(42,479)
Discount rate . . . . .	0.5%	(5,904)	(61,150)
Long-term rate of return on plan assets . . . . .	0.5%	(1,855)	—
Rate of compensation increases . .	0.5%	3,078	19,929

## Results of Operations

### Operating Revenue

Operating revenue in 2017 was \$666.9 million, an increase of \$57.5 million, or 9.4%, over 2016. Operating revenue in 2016 was \$609.4 million, an increase of \$21.0 million, or 3.6%, over 2015. The sources of changes in operating revenue were:

	2017	2016
	Dollars in millions	
Net change due to rate changes, usage, and other(1) . . . . .	\$65.0	\$ 38.2
MCBA revenue(2) . . . . .	1.2	(14.3)
Other balancing account revenue(3) . . . . .	(6.5)	(7.5)
Deferral of revenue(4) . . . . .	(2.2)	4.6
Net change . . . . .	<u>\$57.5</u>	<u>\$ 21.0</u>

- (1) In 2017, the operating revenue increase is due to rate increases (see table in Rates and Regulation section below) and an increase of \$2.5 million in estimated unbilled revenue mostly due to a combination of higher average daily customer billing rates and an increase in unbilled days at the end of 2017 as compared to 2016. The operating revenue increase in 2016 resulted from rate increases and an increase of

\$2.6 million in estimated unbilled revenue mostly due an increase in unbilled days at the end of 2016 as compared to 2015.

- (2) The MCBA revenue increase in 2017 resulted from an increase in actual water production costs relative to adopted water production costs in 2017 as compared to 2016. The MCBA revenue decrease in 2016 resulted from a significant reduction in customer consumption in California caused by drought conditions. As required by the MCBA mechanism, the change in water production costs in California changes operating revenue in the same amount.
- (3) The other balancing accounts revenue consists of the pension, conservation and health care balancing account revenues. Pension and conservation balancing account revenues are the differences between actual expenses and adopted rate recovery. Health care balancing account revenue is 85% of the difference between actual health care expenses and adopted rate recovery. In 2017, the decrease in other balancing account revenue was due to a decrease in actual health care and conservation expenses relative to adopted in 2017, which was partially offset by an increase in actual pension expenses relative to adopted in 2017. In 2016, the decrease in revenue was due to a decrease in pension expense and a decrease in health care expenses relative to adopted amounts.
- (4) The deferral of revenue consists of amounts that are expected to be collected from customers beyond 24 months following the end of the accounting period in which these revenues were recorded. In 2017, the deferral increased in 2017 as compared to 2016 due to an increase in the balancing account revenue expected to be collected beyond 24 months. In 2016, the balancing account revenue expected to be collected beyond 24 months decreased as a result of drought surcharges.

### **Water Production Expenses**

Water production expenses, which consist of purchased water, purchased power, and pump taxes, comprise the largest segment of total operating expenses. Water production costs accounted for 42.3% and 41.3%, of total operating costs in 2017 and 2016, respectively. The rates charged for wholesale water supplies, electricity, and pump taxes are established by various public agencies. As such, these rates are beyond our control.

The table below provides the change in water production expenses during the past 2 years:

	2017			2016		
	Amount	Change	% Change	Amount	Change	% Change
	<b>Dollars in millions</b>					
Purchased water . . . . .	\$199.1	\$17.6	9.7%	\$181.5	\$13.0	7.7%
Purchased power . . . . .	28.9	1.7	6.2%	27.2	(0.7)	(2.5)%
Pump taxes . . . . .	13.9	2.6	23.2%	11.3	(0.2)	(1.7)%
Total water production expenses . . . . .	<u>\$241.9</u>	<u>\$21.9</u>	<u>9.9%</u>	<u>\$220.0</u>	<u>\$12.1</u>	<u>5.8%</u>

The principal factors affecting water production expenses are the quantity, price and source of the water. Generally, water pumped from wells costs less than water purchased from wholesale suppliers.

The table below provides the amounts, percentage change, and source mix for the respective years:

	2017		2016		2015	
	MG	% of Total	MG	% of Total	MG	% of Total
	Millions of gallons (MG)					
Source:						
Wells . . . . .	48,729	46.4%	46,239	46.6%	48,201	48.7%
% change from prior year . . . . .	5.4%		(4.1)%		(16.7)%	
Purchased . . . . .	51,131	48.7%	48,154	48.6%	47,486	48%
% change from prior year . . . . .	6.2%		1.4%		(15.9)%	
Surface . . . . .	5,126	4.9%	4,703	4.8%	3,212	3.3%
% change from prior year . . . . .	9.0%		46.4%		(19.3)%	
Total . . . . .	104,986	100.0%	99,096	100.0%	98,899	100%
% change from prior year . . . . .	6.0%		0.2%		(16.4)%	

Purchased water expenses are affected by changes in quantities purchased, supplier prices, and cost differences between wholesale suppliers. The MCBA mechanism is designed to recover all incurred purchased water expenses.

For 2017, the \$17.6 million increase in purchased water expenses is due to a 6.2% increase in purchased quantities and an overall blended wholesale water rates increase of 3.3% in 2017.

For 2016, the \$13.0 million increase in purchased water expenses is due to a 1.4% increase in purchased quantities and an overall blended wholesale water rates increase of 6.2% in 2016. Purchased water expenses for 2016 was partially offset by lease water rights credits of \$0.4 million.

Purchased power expenses are affected by the quantity of water pumped from wells and moved through the distribution system, rates charged by electric utility companies, and rate structures applied to usage during peak and non-peak times of the day or season. In 2017, purchased power expenses increased \$1.7 million, or 6.2%, mainly due to 5.4% increase in well water production. In 2016, purchased power expenses decreased \$0.7 million, or 2.5%, mainly due to 4.1% decrease in well water production.

Changes in climate change regulations could increase the cost of purchased power expenses which in turn would result in an increase in the rates our power suppliers charge us. Any change in pricing of our purchased power expenses in California would be recovered from our customers through the MCBA mechanism. Any change in power costs in other states would be requested to be recovered by the customers in those states. The impact of such legislation, is dependent upon the enacted date, the factors that impact our suppliers cost structure, and their ability to pass the costs to us in their approved tariffs. These items are not known at this time.

**Administrative and General Expenses**

Administrative and general expenses include payroll related to administrative and general functions, all employee benefits charged to expense accounts, insurance expenses, legal fees, expenses associated with being a public company, and general corporate expenses.

During 2017, administrative and general expenses increased \$4.4 million or 4.5%, as compared to 2016. The increase was mostly due to increases in uninsured loss costs of \$1.5 million, employee wages of \$1.8 million, and employee pension and other postretirement benefit costs of \$0.7 million. Employee pension benefit expenses are fully recovered in rates and are tracked in a balancing account, such that revenues are recovered on a dollar-for-dollar basis up to the amounts authorized in the 2015 GRC. Employee and retiree medical expenses are recovered in rates through a balancing

account authorized in the 2015 GRC, such that revenues are recovered up to 85% of the variance between adopted and recorded expenses.

During 2016, administrative and general expenses decreased \$14.6 million or 12.9%, as compared to 2015. The decrease was mostly due to decreases in employee pension and other postretirement benefit costs of \$10.2 million, a decrease in California drought program costs of \$3.0 million, and a decrease in uninsured loss costs of \$0.9 million. The decreases were partially offset by employee wage increases of \$1.1 million. Wage increases became effective January 1, 2016. Employee pension benefit expenses are fully recovered in rates and are tracked in a balancing account, such that revenues are recovered on a dollar-for-dollar basis up to the amounts authorized in the 2012 GRC. Employee and retiree medical expenses are recovered in rates through a balancing account authorized in the 2012 GRC, such that revenues are recovered up to 85% of the variance between adopted and recorded expenses.

### ***Other Operations Expenses***

The components of other operations expenses include payroll, material and supplies, and contract service costs of operating the regulated water systems, including the costs associated with water transmission and distribution, pumping, water quality, meter reading, billing, operations of district offices, and water conservation programs.

During 2017, other operations expenses decreased \$5.6 million, or 7.0%, compared to 2016. The decrease was mostly due to conservation program expense decreases of \$4.3 million, the write-off of \$3.2 million of capital costs in 2016, and \$2.0 million of MCBA cost deferral associated with the deferral of operating revenue. The decreases were partially offset by employee wage increases of \$1.3 million, the write-off of \$1.1 million of costs in 2017 that were previously capitalized, state of Department of Public Health fee increase of \$0.7 million, and a software maintenance and licensing cost increase of \$0.7 million. Conservation program expenses are fully recovered in rates and are tracked in a balancing account if it is within the authorized amount, such that revenues are recovered on a dollar-for-dollar basis up to the amounts authorized in the 2015 GRC.

During 2016, other operations expenses increased \$12.8 million, or 19.1%, compared to 2015. The increase was mostly due to \$4.4 million of MCBA costs associated with the recognition of operating revenue that was deferred in prior years, the Cal Water 2015 settlement agreement included a \$3.2 million write-off of capital costs, conservation program expense increases of \$1.8 million, and employee wage increases of \$0.7 million. The \$3.2 million write-off of capital costs was for engineering design costs for a canceled Cal Water and City of Bakersfield water treatment plant project, previously recorded as property held for future use. Conservation program expenses are fully recovered in rates and are tracked in a balancing account if it is within the authorized amount, such that revenues are recovered on a dollar-for-dollar basis up to the amounts authorized in the 2012 GRC.

### ***Maintenance***

Maintenance expenses decreased \$0.5 million, or 2.0%, in 2017, compared to 2016 due to decreased costs for repairs of transmission and distribution mains and services.

Maintenance expenses increased \$1.5 million, or 7.1%, in 2016, compared to 2015 due to increased costs for repairs of transmission and distribution mains, tanks, and services.



### ***Depreciation and Amortization***

Depreciation and amortization increased \$13.2 million in 2017, or 20.7%, mostly due to 2016 capital additions and an increase in the provision for depreciation expressed as a percentage of the aggregate depreciable asset balances from 2.7% in 2016 to 3.0% in 2017.

Depreciation and amortization increased \$2.2 million in 2016, or 3.6%, mostly due to 2015 capital additions.

### ***Income Taxes***

For 2017, income taxes increased \$4.1 million, or 16.6%, as compared to 2016. The increase was mostly due to an increase in operating income in 2017 which was partially offset by an increase in the tax benefit from the flow through method of accounting for repairs deductions on state corporate income tax filings.

For 2016, income taxes increased \$0.3 million, or 1.1%, as compared to 2015. The increase was mostly due to an increase in operating income in 2016 which was partially offset by an increase in the tax benefit from the flow through method of accounting for repairs deductions on state corporate income tax filings.

### ***Property and Other Taxes***

For 2017, property and other taxes increased \$1.6 million, or 6.7%, as compared to 2016. The increase was mostly due to an increase in our assessed property values because of utility plant placed in service during 2016.

For 2016, property and other taxes increased \$1.7 million, or 7.8%, as compared to 2015. The increase was mostly due to an increase in our assessed property values because of utility plant placed in service during 2015.

### ***Non-Regulated Revenue and Expense, Net***

In 2017, non-regulated income net of expenses increased \$3.5 million, or 117.5%, as compared to 2016. The increase was due primarily to the implementation of allowance for equity funds used during construction in 2017 and a \$2.0 million increase in unrealized gains on certain benefit plan investments.

In 2016, non-regulated income net of expenses increased \$1.9 million, or 163.0%, as compared to 2015. The increase was mostly due to the recognition of \$1.5 million of litigation proceeds from the Cal Water 2015 GRC settlement agreement and unrealized gains on certain benefit plan investments.

### ***Interest Expenses***

In 2017, net interest expense increased \$3.4 million as compared to 2016. The increase relates to an increase in borrowings on the unsecured revolving credit facilities, which were used to fund capital expenditures and general corporate purposes.

In 2016, net interest expense, increased \$3.2 million compared to 2015. The increase was mostly due to \$100.0 million of First Mortgage Bonds issued in October 2015 and \$50.0 million of First Mortgage Bonds issued in March 2016, which was partially offset by an increase in capitalized interest charged to construction projects in 2016.

## Rates and Regulation

The following is a summary of 2017 rate filings. A description of the “Type of Filing” can be found in “Item 1—Rates and Regulation” section above. California decisions and resolutions may be found on the CPUC website at [www.cpuc.ca.gov](http://www.cpuc.ca.gov).

Type of Filing	Decision/Resolution	Approval Date	Increase (Decrease) Annual Revenue	CA District/ Subsidiary
<b>GRC and Offset Filings</b>				
2017 Expense Offset . . . . .	AL 2229-2232	Jan 2017	\$ 1.9 million	4 Districts
2017 Rate Base Offset . . . . .	AL 2235-2239	Jan 2017	\$ 2.6 million	5 Districts
2015 GRC . . . . .	AL 2240-2241	Jan 2017	\$ 42.3 million	All Districts
2017 Rate Base Offset . . . . .	AL 2248, 2256	Apr 2017	\$ 0.9 million	2 Districts
2017 Expense Offset . . . . .	AL 2253	Apr 2017	\$ 1.0 million	1 District
2017 Rate Base Offset . . . . .	AL 2261	Jul 2017	\$ 0.4 million	1 District
2017 Expense Offset . . . . .	AL 2263-2266	Jul 2017	\$ 2.7 million	4 Districts
2017 Expense Offset . . . . .	AL 2269	Aug 2017	\$ 0.2 million	1 District
Pukalani GRC . . . . .		Oct 2017	\$ 0.2 million	Hawaii Water

The estimated impact of current and prior year rate changes on operating revenues compared to prior years is listed in the following table:

	2017	2016	2015
	<b>Dollars in millions</b>		
General Rate Case(a) . . . . .	\$44.2	\$ 2.2	\$ 1.0
Step rate increases . . . . .	—	4.9	4.8
Offset (purchased water/pump taxes) . . . . .	10.7	23.6	17.7
Total rate increases . . . . .	<u>\$54.9</u>	<u>\$30.7</u>	<u>\$23.5</u>

(a) Includes rate changes for the Cal Water 2015 GRC decision in 2017, rate base offsets in 2017, 2016 and 2015, and Hawaii Water GRC decisions in 2017, 2016, and 2015.

## Water Supply

Our source of supply varies among our operating districts. Certain districts obtain all of their supply from wells; some districts purchase all of their supply from wholesale suppliers; and other districts obtain supply from a combination of wells and wholesale suppliers. A small portion of supply comes from surface sources and is processed through Company-owned water treatment plants. To the best of management’s knowledge, we are meeting water quality, environmental, and other regulatory standards for all Company-owned systems.

California’s normal weather pattern yields little precipitation between mid-spring and mid-fall. The Washington Water service areas receive precipitation in all seasons, with the heaviest amounts during the winter. New Mexico Water’s rainfall is heaviest in the summer monsoon season. Hawaii Water receives precipitation throughout the year, with the largest amounts in the winter months. Water usage in all service areas is highest during the warm and dry summers and declines in the cool winter months. Rain and snow during the winter months replenish underground water aquifers and fill reservoirs, providing the water supply for subsequent delivery to customers. Management believes that supply pumped from underground aquifers and purchased from wholesale suppliers will be adequate to meet customer demand during 2018 and beyond. However, water rationing may be required in future periods, if declared by the state or local jurisdictions. Long-term water supply plans are developed for each of our districts to help assure an adequate water supply under

various operating and supply conditions. Some districts have unique challenges in meeting water quality standards, but management believes that supplies will meet current standards using current treatment processes.

## **Liquidity and Capital Resources**

### ***Cash flow from Operations***

During 2017, we generated cash flow from operations of \$147.8 million, compared to \$160.4 million during 2016. The decrease in 2017 was mostly due to an increase in the net WRAM and MCBA receivable in 2017 as actual customer usage was below adopted.

During 2016, we generated cash flow from operations of \$160.4 million, compared to \$145.0 million during 2015. The increase in 2016 was mostly due to rate increases as authorized by the Cal Water 2012 GRC decision.

The water business is seasonal. Billed revenue is lower in the cool, wet winter months when less water is used compared to the warm, dry summer months when water use is highest. This seasonality results in the possible need for short-term borrowings under the bank lines of credit in the event cash is not sufficient to cover operating and capital costs during the winter period. The increase in cash flow during the summer allows short-term borrowings to be paid down. Customer water usage can be lower than normal in years when more than normal precipitation falls in our service areas or temperatures are lower than normal, especially in the summer months. The reduction in water usage reduces cash flow from operations and increases the need for short-term bank borrowings. In addition, short-term borrowings are used to finance capital expenditures until long-term financing is arranged.

### ***Investing Activities***

During 2017, 2016, and 2015, we used \$259.2 million, \$228.9 million and \$176.8 million, respectively, of cash for capital expenditures, both Company-funded and developer-funded. The 2017 capital expenditures exceeded the high end of the budgeted capital expenditures of \$230.0 million. Annual expenditures fluctuate each year due to the availability of construction resources and our ability to obtain construction permits in a timely manner. In 2017, we also received \$56.0 million in TCP settlement proceeds.

### ***Financing Activities***

During 2017, we borrowed \$265.0 million, and paid down \$87.0 million on our unsecured revolving credit facilities to fund capital expenditures and general corporate purposes. We also added \$21.4 million of advances and contributions in aid of construction, which was reduced by refunds to developers of \$8.4 million and repayment of \$20.0 million for First Mortgage Bonds that matured in 2017.

During 2016, we sold \$50.0 million of First Mortgage Bonds and used the net proceeds of \$49.8 million to pay down short term borrowings. We also borrowed \$145.1 million, and paid down \$81.6 million on our unsecured revolving credit facilities to fund capital expenditures and general corporate purposes. We added \$21.4 million of advances and contributions in aid of construction, which was reduced by refunds to developers of \$6.9 million.

During 2015, we sold \$100.0 million of First Mortgage Bonds and used the net proceeds of \$99.3 million to pay down outstanding short-term borrowings and fund capital expenditures and general corporate purposes. We also borrowed \$94.3 million, net of the expenses of \$1.2 million, and paid down \$141.0 million on our unsecured revolving credit facilities to fund capital expenditures and general corporate purposes. We added \$16.0 million of advances and contributions in aid of construction, which were reduced by refunds to developers of \$6.7 million.

On March 10, 2015, the Company and Cal Water entered into Syndicated Credit Agreements, which provide for unsecured revolving credit facilities of up to an initial aggregate amount of \$450.0 million for a term of five years. The Company and subsidiaries that it designates may borrow up to \$150.0 million under the Company's revolving credit facility. Cal Water may borrow up to \$300.0 million under its revolving credit facility; however, all borrowings need to be repaid within 24 months unless otherwise authorized by the CPUC. The credit facilities may each be expanded by up to \$50.0 million subject to certain conditions. The proceeds from the revolving credit facilities may be used for working capital purposes, including the short-term financing of capital projects. The base loan rate may vary from LIBOR plus 72.5 basis points to LIBOR plus 95 basis points, depending on the Company's total capitalization ratio. Likewise, the unused commitment fee may vary from 8 basis points to 12.5 basis points based on the same ratio.

The under-collected net WRAM and MCBA receivable balances were \$71.6 million, \$39.2 million, and \$42.0 million as of December 31, 2017, 2016, and 2015, respectively. The increase of \$32.4 million as of December 31, 2017 compared to the prior year was mostly due to actual customer usage being lower than adopted. The decrease of \$2.8 million as of December 31, 2016 compared to the prior year was mostly due to \$25.9 million of drought surcharges in 2016, which was partially offset by a 2.7% decrease in customer usage in California. The under-collected net WRAM and MCBA receivable balances were primarily financed by Cal Water with short-term and long-term financing arrangements to meet operational cash requirements. Interest on the under-collected net WRAM and MCBA receivable balances, the interest recoverable from customers, is limited to the current 90-day commercial paper rate, which is significantly lower than Cal Water's short and long-term financing rates.

Bond principal and other long-term debt payments were \$26.8 million during 2017, \$7.0 million during 2016, and \$7.0 million during 2015.

At the January 2018 meeting, the Board of Directors declared the quarterly dividend, increasing it for the 51st consecutive year. The quarterly dividend was raised from \$0.1800 to \$0.1875 per common share, or an annual rate of \$0.7500 per common share. Dividends have been paid for 72 consecutive years. The annual dividends paid per common share in 2017, 2016, and 2015 were \$0.7200, \$0.6900, and \$0.6700, respectively. Earnings not paid as dividends are reinvested in the business for the benefit of stockholders. The dividend payout ratio was 51% in 2017, 68% in 2016 and 71% in 2015 for an average of 63% over the 3-year period. Our long-term targeted dividend payout ratio is 60%.

### ***Short-Term Financing***

Short-term liquidity is provided by the bank lines of credit described above and by internally generated funds. Long-term financing is accomplished through the use of both debt and equity. As of December 31, 2017, there were short-term borrowings of \$275.1 million outstanding on our unsecured revolving line of credit, compared to \$97.1 million outstanding on our unsecured revolving line of credit as of December 31, 2016. As of December 31, 2016, there were short-term borrowings of \$97.1 million outstanding on our unsecured revolving line of credit, compared to \$33.6 million outstanding on our unsecured revolving line of credit as of December 31, 2015.

Given our ability to access our lines of credit on a daily basis, cash balances are managed to levels required for daily cash needs and excess cash is invested in short-term or cash equivalent instruments. Minimal operating levels of cash are maintained for Washington Water, New Mexico Water, and Hawaii Water.

The Company and subsidiaries which it designates may borrow up to \$150.0 million under its short-term credit facility. Cal Water may borrow up to \$300.0 million under its credit facility;

however, all borrowings need to be repaid within 24 months unless otherwise authorized by the CPUC.

Both short-term credit agreements contain affirmative and negative covenants and events of default customary for credit facilities of this type including, among other things, limitations and prohibitions relating to additional indebtedness, liens, mergers, and asset sales. Also, these unsecured credit agreements contain financial covenants governing the Company and its subsidiaries' consolidated total capitalization ratio not to exceed 66.7% and interest coverage ratio of three or more. As of December 31, 2017, our consolidated total capitalization ratio was 56.5% (trade payable and short term borrowings are included as debt for this calculation) and the interest coverage ratio was greater than five. In summary, we have met all of the covenant requirements and are eligible to use the full amounts of these credit agreements.

### ***Long-Term Financing***

Cal Water was authorized to issue \$350.0 million of debt and common stock to finance capital projects and operations by a CPUC decision dated May 12, 2016. In addition, the decision retained \$146.0 million of prior financing authority and determined that refinancing long-term debt did not count against the authorization. The CPUC requires that any loans from Cal Water to the Company be at arm's length. This restriction did not materially impact the Company's ability to meet its cash obligations in 2017. Management does not expect this restriction to have a material impact on the Company's ability to meet its cash obligations in 2018 and beyond.

On March 16, 2016, Cal Water sold \$50.0 million of First Mortgage Bonds and used the net proceeds of \$49.8 million to pay down outstanding short-term borrowings, fund capital expenditures and for general corporate purposes. The Company made principal payments on First Mortgage Bonds and other long-term debt of \$26.8 million during 2017. On October 13, 2015, Cal Water sold \$100.0 million of First Mortgage Bonds and used the net proceeds of \$99.3 million to pay down outstanding short-term borrowings, fund capital expenditures and for general corporate purposes. We made principal payments on First Mortgage Bonds and other long-term debt of \$7.0 million during 2016. Long-term financing, which includes First Mortgage Bonds, senior notes, other debt securities, and common stock, has typically been used to replace short-term borrowings and fund capital expenditures. Internally generated funds, after making dividend payments, provide positive cash flow, but have not been at a level to meet the needs of our capital expenditure requirements. Management expects this trend to continue given our capital expenditures plan for the next five years. Some capital expenditures are funded by payments received from developers for contributions in aid of construction or advances for construction. Funds received for contributions in aid of construction are non-refundable, whereas funds classified as advances in construction are refundable. Management believes long-term financing is available to meet our cash flow needs through issuances in both debt and equity instruments.

Additional information regarding the bank borrowings and long-term debt is presented in Notes 7 and 8 in the Notes to Consolidated Financial Statements.

### ***Off-Balance Sheet Transactions***

We do not utilize off-balance-sheet financing or utilize special purpose entity arrangements for financing. We do not have equity ownership through joint ventures or partnership arrangements.

### ***Contractual Obligations***

The contractual obligations presented in the table below represent our estimates of future payments under fixed contractual obligations and commitments. Changes in our business needs, cancellation provisions and changes in interest rates, as well as action by third parties and other

factors, may cause these estimates to change. Therefore, our actual payments in future periods may vary from those presented in the table below. The following table summarizes our contractual obligations as of December 31, 2017.

	<u>Total</u>	<u>Less than 1 Year</u>	<u>1 - 3 Years</u>	<u>3 - 5 Years</u>	<u>After 5 Years</u>
	(In thousands)				
Long-term debt(*) . . . . .	\$ 528,809	\$ 16,221	\$126,967	\$ 9,907	\$ 375,714
Interest payments . . . . .	349,546	29,109	48,203	40,962	231,272
Advances for construction . . . . .	182,502	7,896	15,346	15,293	143,967
Pension and postretirement benefits(**) . . . . .	262,353	15,742	56,620	44,169	145,822
Capital lease obligations(***) . . . . .	8,849	1,053	2,261	1,954	3,581
Facility leases . . . . .	5,840	950	1,169	643	3,078
System lease . . . . .	422	422	—	—	—
Water supply contracts(****) . . . . .	690,370	30,708	61,417	61,419	536,826
<b>TOTAL . . . . .</b>	<b>\$2,028,691</b>	<b>\$102,101</b>	<b>\$311,983</b>	<b>\$174,347</b>	<b>\$1,440,260</b>

\* Excludes capital lease obligations as reported below. Also, excludes unamortized debt issuance costs of \$4.5 million.

\*\* Pension and postretirement benefits include \$2.0 million of short-term pension obligations.

\*\*\* Capital lease obligations represent total cash payments to be made in the future and include interest expense of \$1.8 million.

\*\*\*\* Estimated annual contractual obligations are based on the same payment levels as 2017.

For pension and postretirement benefits other than pensions obligations, see Note 11 of the Notes to the consolidated Financial Statements.

Long-term debt payments include annual sinking fund payments on First Mortgage Bonds, maturities of long-term debt, and annual payments on other long-term obligations.

Advances for construction represent annual contract refunds to developers for the cost of water systems paid for by the developers. The contracts are non-interest bearing, and refunds are generally on a straight-line basis over a 40-year period. System and facility leases include obligations associated with leasing water systems and rents for office space.

For capital lease obligations, facility leases, and system lease, see Note 14 of the Notes to the consolidated Financial Statements.

Cal Water has water supply contracts with wholesale suppliers in 13 of its operating districts and for the two leased systems in Hawthorne and Commerce. For each contract, the cost of water is established by the wholesale supplier and is generally beyond our control. The amount paid annually to the wholesale suppliers is charged to purchased water expense on our statement of income. Most contracts do not require minimum annual payments and vary with the volume of water purchased. For more details related to water supply contracts, see Note 11 of the Notes to the consolidated Financial Statements.

### **Capital Requirements**

Capital requirements consist primarily of new construction expenditures for expanding and replacing utility plant facilities and the acquisition of water systems. They also include refunds of advances for construction.

Company-funded and developer-funded utility plant expenditures were \$259.2 million, \$228.9 million, and \$176.8 million in 2017, 2016, and 2015, respectively. A majority of capital expenditures was associated with mains and water treatment equipment.

For 2018, the Company is estimating its capital expenditures to be between \$200.0 million and \$220.0 million based on the 2015 GRC in California and normal capital needs in the other subsidiaries. Capital expenditures in California are evaluated in the context of the pending GRC and may change as the case moves forward. We expect our annual capital expenditure to increase during the next five years due to increasing needs to replace and maintain infrastructure.

Management expects developer-funded expenditures in 2018. These expenditures will be financed by developers through refundable advances for construction and non-refundable contributions in aid of construction. Developers are required to deposit the cost of a water construction project with us prior to our commencing construction work, or the developers may construct the facilities themselves and deed the completed facilities to us. Funds are generally received in advance of incurring costs for these projects. Advances are normally refunded over a 40-year period without interest. Future payments for advances received are listed under contractual obligations above. Because non-Company-funded construction activity is solely at the discretion of developers, we cannot predict the level of future activity. The cash flow impact is expected to be minor due to the structure of the arrangements.

### **Capital Structure**

Common stockholders' equity was \$693.5 million at December 31, 2017, compared to \$659.5 million at December 31, 2016. In 2017, Cal Water repaid \$20.0 million for First Mortgage Bonds that matured in 2017. The Company did not sell shares of its common stock in 2017.

Total capitalization, including the current portion of long-term debt, was \$1,225.2 million at December 31, 2017 and \$1,217.4 million at December 31, 2016. In future periods, the Company intends to issue common stock and long-term debt to finance our operations. The capitalization ratios will vary depending upon the method we choose to finance our operations.

At December 31, capitalization ratios were:

	<u>2017</u>	<u>2016</u>
Common equity . . . . .	56.6%	54.2%
Long-term debt . . . . .	43.4%	45.8%

The return (from both regulated and non-regulated operations) on average common equity was 9.9% in 2017 compared to 7.5% in 2016. Cal Water does not include construction work in progress in its regulated rate base; instead, Cal Water was authorized to record AFUDC on construction work in progress, effective January 1, 2017. Construction work in progress for Cal Water was \$167.2 million at December 31, 2017 and \$127.4 million at December 31, 2016.

### **Acquisitions**

In 2017, 2016, and 2015 there were no significant acquisitions.

### **Real Estate Program**

We own real estate. From time to time, certain parcels are deemed no longer used or useful for water utility operations. Most surplus properties have a low cost basis. We developed a program to realize the value of certain surplus properties through sale or lease of those properties. The program will be ongoing for a period of several years. There was a pre-tax gain of \$0.6 million in 2017, a pre-tax loss of \$0.1 million in 2016, and a pre-tax gain of \$0.3 million in 2015. As sales are

dependent on real estate market conditions, future sales, if any, may or may not be at prior year levels.

**Item 7A. Quantitative and Qualitative Disclosures about Market Risk.**

We do not participate in hedge arrangements, such as forward contracts, swap agreements, options, or other contractual agreements to mitigate the impact of market fluctuations on our assets, liabilities, production, or contractual commitments. We operate only in the United States and, therefore, are not subject to foreign currency exchange rate risks.

**Interest Rate Risk**

We are subject to interest rate risk, although this risk is lessened because we operate in a regulated industry. If interest rates were to increase, management believes customer rates would increase accordingly, subject to Commission approval in future GRC filings. The majority of our debt is long-term at a fixed rate. Interest rate risk does exist on short-term borrowings within our credit facilities, as these interest rates are variable. We also have interest rate risk on new financing, as higher interest cost may occur on new debt if interest rates increase.

Over the next 12 months, approximately \$15.9 million of the \$531.7 million of existing long-term debt instruments will mature or require sinking fund payments. Applying a hypothetical 10 percent increase in the rate of interest charged on those borrowings would not have a material effect on our earnings.



## **Item 8. Financial Statements and Supplementary Data.**

### **REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the shareholders and the Board of Directors of  
California Water Service Group  
San Jose, California

#### **Opinions on the Financial Statements and Internal Control over Financial Reporting**

We have audited the accompanying consolidated balance sheets of California Water Service Group and subsidiaries (the "Company") as of December 31, 2017 and 2016, the related consolidated statements of income, common stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the "financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in *Internal Control—Integrated Framework (2013)* issued by COSO.

#### **Basis for Opinions**

The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying *Management's Report on Internal Control over Financial Reporting*. Our responsibility is to express an opinion on these financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures to respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included

performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

### **Definition and Limitations of Internal Control over Financial Reporting**

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ DELOITTE & TOUCHE LLP

San Francisco, California  
March 1, 2018

We have served as the Company's auditor since 2008.

**CALIFORNIA WATER SERVICE GROUP**  
**Consolidated Balance Sheets**

	<b>December 31,</b>	
	<b>2017</b>	<b>2016</b>
	<b>(In thousands, except per share data)</b>	
<b>ASSETS</b>		
Utility plant:		
Land	\$ 42,517	\$ 40,283
Depreciable plant and equipment	2,729,757	2,522,174
Construction work in progress	175,693	132,957
Intangible assets	22,212	21,925
Total utility plant	2,970,179	2,717,339
Less accumulated depreciation and amortization	(922,214)	(858,062)
Net utility plant	2,047,965	1,859,277
Current assets:		
Cash and cash equivalents	94,776	25,492
Receivables: net of allowance for doubtful accounts of \$773 and \$830 in 2017 and 2016, respectively		
Customers	32,451	30,305
Regulatory balancing accounts	36,783	30,332
Other	16,464	17,158
Unbilled revenue	29,756	25,228
Materials and supplies at weighted average cost	6,463	6,292
Taxes, prepaid expenses, and other assets	11,180	7,262
Total current assets	227,873	142,069
Other assets:		
Regulatory assets	401,147	355,930
Goodwill	2,615	2,615
Other	60,775	51,854
Total other assets	464,537	410,399
<b>TOTAL ASSETS</b>	<b>\$2,740,375</b>	<b>\$2,411,745</b>
<b>CAPITALIZATION AND LIABILITIES</b>		
Capitalization:		
Common stock, \$0.01 par value; 68,000 shares authorized, 48,012 and 47,965 outstanding in 2017 and 2016, respectively	\$ 480	\$ 480
Additional paid-in capital	336,229	334,856
Retained earnings	356,753	324,135
Total common stockholders' equity	693,462	659,471
Long-term debt, less current maturities	515,793	531,745
Total capitalization	1,209,255	1,191,216
Current liabilities:		
Current maturities of long-term debt	15,920	26,208
Short-term borrowings	275,100	97,100
Accounts payable	93,955	77,813
Regulatory balancing accounts	59,303	4,759
Accrued other taxes	3,888	3,629
Accrued interest	6,122	5,661
Other accrued liabilities	36,671	35,060
Total current liabilities	490,959	250,230
Unamortized investment tax credits	1,724	1,798
Deferred income taxes	192,946	298,924
Regulatory liabilities	179,706	38,735
Pension and postretirement benefits other than pensions	252,141	222,691
Advances for construction	182,502	182,448
Contributions in aid of construction	186,721	180,790
Other long-term liabilities	44,421	44,913
Commitments and contingencies		
<b>TOTAL CAPITALIZATION AND LIABILITIES</b>	<b>\$2,740,375</b>	<b>\$2,411,745</b>

See accompanying Notes to Consolidated Financial Statements.

**CALIFORNIA WATER SERVICE GROUP**  
**Consolidated Statements of Income**

	<b>For the Years Ended December 31,</b>		
	<b>2017</b>	<b>2016</b>	<b>2015</b>
	<b>(In thousands, except per share data)</b>		
Operating revenue . . . . .	\$666,890	\$609,370	\$588,368
Operating expenses:			
Operations:			
Purchased water . . . . .	199,081	181,515	168,557
Purchased power . . . . .	28,862	27,180	27,890
Pump taxes . . . . .	13,924	11,298	11,479
Administrative and general . . . . .	102,914	98,474	113,110
Other operations . . . . .	74,448	80,082	67,248
Maintenance . . . . .	22,530	22,993	21,463
Depreciation and amortization . . . . .	76,783	63,599	61,381
Income taxes . . . . .	28,928	24,804	24,528
Property and other taxes . . . . .	24,797	23,231	21,559
Total operating expenses . . . . .	<u>572,267</u>	<u>533,176</u>	<u>517,215</u>
Net operating income . . . . .	<u>94,623</u>	<u>76,194</u>	<u>71,153</u>
Other income and expenses:			
Non-regulated revenue . . . . .	15,898	16,585	15,624
Non-regulated expenses . . . . .	(9,390)	(11,445)	(14,044)
Allowance for equity funds used during construction . . . . .	3,750	—	—
Gain (loss) on sale of non-utility property . . . . .	663	(146)	315
Income tax expense on other income and expenses . . . . .	(4,435)	(2,012)	(761)
Net other income . . . . .	<u>6,486</u>	<u>2,982</u>	<u>1,134</u>
Interest expense:			
Interest expense . . . . .	36,288	33,466	29,185
Allowance for borrowed funds used during construction . . . . .	(2,360)	(2,965)	(1,915)
Net interest expense . . . . .	<u>33,928</u>	<u>30,501</u>	<u>27,270</u>
Net income . . . . .	<u>\$ 67,181</u>	<u>\$ 48,675</u>	<u>\$ 45,017</u>
Earnings per share:			
Basic . . . . .	\$ 1.40	\$ 1.02	\$ 0.94
Diluted . . . . .	\$ 1.40	\$ 1.01	\$ 0.94
Weighted average number of common shares outstanding:			
Basic . . . . .	48,009	47,953	47,865
Diluted . . . . .	48,009	47,956	47,880

See accompanying Notes to Consolidated Financial Statements.

**CALIFORNIA WATER SERVICE GROUP**  
**Consolidated Statements of Common Stockholders' Equity**  
**For the Years Ended December 31, 2017, 2016 and 2015**

	<u>Common Stock</u>		<u>Additional</u>	<u>Retained</u>	<u>Total</u>
	<u>Shares</u>	<u>Amount</u>	<u>Paid-in</u>	<u>Earnings</u>	<u>Stockholders'</u>
			<u>Capital</u>		<u>Equity</u>
			(In thousands)		
Balance at December 31, 2014 . . . . .	47,806	\$478	\$330,558	\$295,590	\$626,626
Net income . . . . .				45,017	45,017
Issuance of common stock . . . . .	69	1	2,577		2,578
Dividends paid on common stock (\$0.670 per share) . . . . .				(32,066)	(32,066)
Balance at December 31, 2015 . . . . .	47,875	479	333,135	308,541	642,155
Net income . . . . .				48,675	48,675
Issuance of common stock . . . . .	90	1	1,721		1,722
Dividends paid on common stock (\$0.690 per share) . . . . .				(33,081)	(33,081)
Balance at December 31, 2016 . . . . .	47,965	480	334,856	324,135	659,471
Net income . . . . .				67,181	67,181
Issuance of common stock . . . . .	47	—	1,373		1,373
Dividends paid on common stock (\$0.720 per share) . . . . .				(34,563)	(34,563)
Balance at December 31, 2017 . . . . .	<u>48,012</u>	<u>\$480</u>	<u>\$336,229</u>	<u>\$356,753</u>	<u>\$693,462</u>

See accompanying Notes to Consolidated Financial Statements.

**CALIFORNIA WATER SERVICE GROUP**  
**Consolidated Statements of Cash Flows**

	For the Years Ended December 31,		
	2017	2016	2015
	(In thousands)		
Operating activities:			
Net income	\$ 67,181	\$ 48,675	\$ 45,017
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	78,592	65,203	63,182
Amortization of debt premium and expenses	920	871	825
Changes in normalized deferred income taxes	21,087	26,818	24,393
Change in value of life insurance contracts	(3,058)	(1,026)	218
Allowance for equity funds used during construction	(3,750)	—	—
Stock-based compensation	3,118	2,849	2,578
(Gain) loss on sale of non-utility property	(663)	146	(315)
Write-off of capital costs	1,293	3,221	—
Changes in operating assets and liabilities:			
Receivables	(31,871)	(343)	1,855
Unbilled revenue	(4,528)	(2,047)	559
Taxes, prepaid expenses, and other assets	(3,718)	1,276	(2,366)
Accounts payable	1,564	3,839	(819)
Other current liabilities	2,164	4,056	(1,106)
Other changes in noncurrent assets and liabilities	19,511	6,906	10,948
Net cash provided by operating activities	<u>147,842</u>	<u>160,444</u>	<u>144,969</u>
Investing activities:			
Utility plant expenditures	(259,194)	(228,938)	(176,833)
Proceeds from sale of non-utility assets	666	395	319
TCP settlement proceeds	56,004	—	—
Life insurance benefits	1,558	495	—
Purchase of life insurance	(5,605)	(2,857)	(2,032)
Change in restricted cash	(81)	66	288
Net cash used in investing activities	<u>(206,652)</u>	<u>(230,839)</u>	<u>(178,258)</u>
Financing activities:			
Short-term borrowings, net of expenses of \$0 for 2017 and 2016, and \$1,197 for 2015	265,000	145,100	94,303
Repayment of short-term borrowings	(87,000)	(81,615)	(141,000)
Issuance of long-term debt, net of expenses of \$0 for 2017, \$177 for 2016, and \$707 for 2015	—	49,823	99,343
Advances and contributions in aid of construction	21,369	21,448	16,026
Refunds of advances for construction	(8,378)	(6,885)	(6,726)
Retirement of long-term debt	(26,829)	(6,996)	(7,003)
Repurchase of common stock	(1,505)	(744)	(338)
Dividends paid	(34,563)	(33,081)	(32,066)
Net cash provided by financing activities	<u>128,094</u>	<u>87,050</u>	<u>22,539</u>
Change in cash and cash equivalents	69,284	16,655	(10,750)
Cash and cash equivalents at beginning of year	25,492	8,837	19,587
Cash and cash equivalents at end of year	<u>\$ 94,776</u>	<u>\$ 25,492</u>	<u>\$ 8,837</u>
Supplemental disclosures of cash flow information:			
Cash paid (received) during the year for:			
Interest (net of amounts capitalized)	\$ 32,223	\$ 28,038	\$ 25,345
Income tax refunds	(1,697)	—	—
Supplemental disclosure of investing and financing non-cash activities:			
Accrued payables for investments in utility plant	41,017	27,150	21,546
Utility plant contributed by developers	19,898	16,824	7,383
Litigation proceeds for MTBE contamination reclassified from other long-term liabilities to depreciable plant and equipment	2,420	484	332

See accompanying Notes to Consolidated Financial Statements.

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**1 ORGANIZATION AND OPERATIONS**

California Water Service Group (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 as the Commissions). CWS Utility Services and HWS Utility Services LLC provide non-regulated water utility and utility-related services.

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

***Basis of Presentation***

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and include the Company's accounts and those of its wholly owned subsidiaries. All intercompany transactions and balances have been eliminated from the consolidated financial statements. In the opinion of management, the consolidated financial statements reflect all adjustments that are necessary to provide a fair presentation of the results for the periods covered.

The preparation of the Company's 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 consolidated balance sheet dates and the reported amounts of revenues and expenses for the periods presented. These include, but are not limited to, estimates and assumptions used in determining the Company's regulatory asset and liability balances based upon probability assessments of regulatory recovery, utility plant useful lives, revenues earned but not yet billed, asset retirement obligations, allowance for doubtful accounts, pension and other employee benefit plan liabilities, and income tax-related assets and liabilities. Actual results could differ from these estimates.

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Revenue***

Revenue generally includes monthly cycle customer billings for regulated water and wastewater services at rates authorized by regulatory commissions (plus an estimate for water used between the customer's last meter reading and the end of the accounting period) and billings to certain non-regulated customers at rates authorized by contract with government agencies.

The Company's regulated water and related utility services requirements are authorized by the Commissions in the states in which the Company operates. The revenue requirements are intended to provide the Company a reasonable opportunity to recover its operating costs and earn a return on investments.

For metered customers, Cal Water recognizes revenue from rates which are designed and authorized by the California Public Utilities Commission (CPUC). Under the Water Revenue

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Adjustment Mechanism (WRAM), Cal Water records the adopted level of volumetric revenues, which would include recovery of cost of service and a return on investments, as established by the CPUC for metered accounts. 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 regulatory asset or liability balancing account (tracked individually for each Cal Water district) subject to certain criteria under the accounting guidance for regulated operations. The variance amount represents amounts that will be billed or refunded to customers in the future. In addition to volumetric revenues, the revenue requirements approved by the CPUC include service charges, flat rate charges, and other items not subject to the WRAM.

Cost-recovery rates are designed to permit full recovery of certain costs allowed to be recovered by the Commissions. Cost-recovery rates such as the Modified Cost Balancing Account (MCBA) provide for recovery of adopted expense levels for purchased water, purchased power and pump taxes, as established by the CPUC. In addition, cost-recovery rates include recovery of costs related to water conservation programs and certain other operating expenses adopted by the CPUC. Variances (which include the effects of changes in both rates and volumes for the MCBA) between adopted and actual costs are recorded as a component of revenue, as the amount of such variances will be recovered from or refunded to customers in the future. Cost-recovery expenses are generally recognized when expenses are incurred with no markup for return on investments or profit.

The balances in the WRAM and MCBA assets and liabilities accounts will 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 the deferred net balances are interest bearing at the current 90 day commercial paper rate. Subsequent to calendar year-end, Cal Water files with the CPUC to refund or collect the balance in the accounts. The majority of under-collected net WRAM and MCBA receivable balances are collected over 12 or 18 months. Cal Water defers net WRAM and MCBA operating revenues and associated costs whenever the net receivable balances are estimated to be collected more than 24 months after the respective reporting period in which it was recorded. The deferred net WRAM and MCBA revenue and associated costs were determined using forecasts of customer consumption trends in future reporting periods and the estimated timing of when the CPUC will authorize Cal Water's filings to recover unbilled balances. Deferred revenues and associated costs are recorded in the periods when the collection is within 24 months of the respective reporting period.

Customers' meter reads occur on various business days throughout the month. As a result, there are unmetered or unbilled customer usage each month. The estimated unbilled revenue for monthly unmetered customer usage is recorded using the number of unbilled days for that month and average daily customer billing rate for the previous month. The average daily customer billing rate for the previous month fluctuates depending on customer usage. Estimated unbilled revenue is not included in the WRAM until it is billed.

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 period is included in that period's



**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

revenue, with the balance recorded as unearned revenue on the balance sheet and recognized as revenue when earned in the subsequent accounting period. The unearned revenue liability was \$0.7 million and \$0.8 million as of December 31, 2017 and 2016, respectively. This liability is included in "other accrued liabilities" on our consolidated balance sheets.

***Non-Regulated Revenue***

Revenues from non-regulated operations and maintenance agreements are recognized when services have been rendered to companies or municipalities under such agreements. For construction and design services, revenue is generally recognized on the completed contract method, as most projects are completed in less than 3 months. Other non-regulated revenue is recognized when title has transferred to the buyer, or ratably over the term of the lease.

***Allowance for Doubtful Accounts***

The Company provides an allowance for doubtful accounts receivable. The allowance is based upon specific identified accounts plus an estimate of uncollectible accounts based upon historical percentages. The balance of customer receivables is net of the allowance for doubtful accounts of \$0.8 million, \$0.8 million, and \$0.7 million as of December 31, 2017, 2016 and 2015, respectively.

The activities in the allowance for doubtful accounts are as follows:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Beginning Balance . . . . .	\$ 830	\$ 730	\$ 697
Provision for uncollectible accounts . . . . .	1,570	2,111	1,674
Net write off of uncollectible accounts . . . . .	<u>(1,627)</u>	<u>(2,011)</u>	<u>(1,641)</u>
Ending Balance . . . . .	<u>\$ 773</u>	<u>\$ 830</u>	<u>\$ 730</u>

***Utility Plant***

Utility plant is carried at original cost when first constructed or purchased, or at fair value when acquired through acquisition. When depreciable plant is retired, the cost is eliminated from utility plant accounts and such costs are charged against accumulated depreciation. Maintenance of utility plant is charged to operating expenses as incurred. Maintenance projects are not accrued for in advance.

Intangible assets acquired as part of water systems purchased are recorded at fair value. All other intangibles have been recorded at cost and are amortized over their useful life.

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

The following table represents depreciable plant and equipment as of December 31:

	<u>2017</u>	<u>2016</u>
Equipment . . . . .	\$ 592,612	\$ 561,909
Office buildings and other structures . . . . .	245,877	218,711
Transmission and distribution plant . . . . .	<u>1,891,268</u>	<u>1,741,554</u>
Total . . . . .	<u>\$2,729,757</u>	<u>\$2,522,174</u>

Depreciation of utility plant is computed on a straight-line basis over the assets' estimated useful lives including cost of removal of certain assets as follows:

	<u>Useful Lives</u>
Equipment . . . . .	5 to 50 years
Transmission and distribution plant . . . . .	40 to 65 years
Office Buildings and other structures . . . . .	50 years

The provision for depreciation expressed as a percentage of the aggregate depreciable asset balances was 3.00% in 2017, 2.70% in 2016 and 2.80% in 2015.

***Allowance for Funds Used During Construction***

The allowance for funds used during construction (AFUDC) represents the capitalized cost of funds used to finance the construction of the utility plant. In general, AFUDC is applied to Cal Water construction projects requiring more than one month to complete. No AFUDC is applied to projects funded by customer advances for construction, contributions in aid of construction, or applicable state-revolving fund loans. AFUDC includes the net cost of borrowed funds and a rate of return on other funds when used, and is recovered through water rates as the utility plant is depreciated. Cal Water was authorized by the CPUC to record AFUDC on construction work in progress effective January 1, 2017. Prior to January 1, 2017, the CPUC authorized Cal Water to only record capitalized interest on borrowed funds. Cal Water previously reported the amounts authorized as capitalized interest and a reduction to interest expense. The amount of AFUDC related to equity funds and to borrowed funds for 2017, 2016, and 2015 are shown in the tables below:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Allowance for equity funds used during construction . . . . .	\$3,750	\$ —	\$ —
Allowance for borrowed funds used during construction . . . . .	<u>2,360</u>	<u>2,965</u>	<u>1,915</u>
Total . . . . .	<u>\$6,110</u>	<u>\$2,965</u>	<u>\$1,915</u>

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

***Asset Retirement Obligation***

The Company has a legal obligation to retire wells in accordance with State Water Resources Control Board regulations. In addition, upon decommission of a wastewater plant or lift station certain wastewater infrastructure would need to be retired in accordance with State Water Resources Control Board regulations. An asset retirement cost and corresponding retirement obligation is recorded when a well or waste water infrastructure is placed into service. As of December 31, 2017 and 2016, the retirement obligation is estimated to be \$21.2 million and \$20.3 million, respectively. The change only impacted the consolidated balance sheet.

***Cash and Cash Equivalents***

Cash and cash equivalents include highly liquid investments with remaining maturities of three months or less at the time of acquisition. Cash and cash equivalents was \$94.8 million and \$25.5 million as of December 31, 2017 and December 31, 2016, respectively.

***Restricted Cash***

In 2017 restricted cash includes \$0.5 million of proceeds collected through a surcharge on certain customers' bills plus interest earned on the proceeds and is used to service California Safe Drinking Water Bond obligations. All restricted cash is included in "taxes, prepaid expenses, and other assets". As of December 31, 2017 and 2016, restricted cash was \$0.6 million and \$0.4 million, respectively.

***Regulatory Assets and Liabilities***

Because the Company operates almost exclusively in a regulated business, the Company is subject to the accounting standards for regulated utilities. The Commissions in the states in which the Company operates establish rates that are designed to permit the recovery of the cost of service and a return on investment. The Company capitalizes and records regulatory assets for costs that would otherwise be charged to expense if it is probable that the incurred costs will be recovered in future rates. Regulatory assets are amortized over the future periods that the costs are expected to be recovered. If costs expected to be incurred in the future are currently being recovered through rates, the Company records those expected future costs as regulatory liabilities. In addition, the Company records regulatory liabilities when the Commissions require a refund to be made to the Company's customers over future periods.

Determining probability requires significant judgment by management and includes, but is not limited to, consideration of testimony presented in regulatory hearings, proposed regulatory decisions, final regulatory orders, and the strength or status of applications for rehearing or state court appeals.

If the Company determines that a portion of the Company's assets used in utility operations is not recoverable in customer rates, the Company would be required to recognize the loss of the assets disallowed.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Regulatory assets and liabilities were comprised of the following as of December 31:

	<u>2017</u>	<u>2016</u>
<i>Regulatory Assets</i>		
Pension and retiree group health . . . . .	\$214,249	\$188,880
Property-related temporary differences (tax benefits flowed through to customers) . . . . .	87,323	92,099
Other accrued benefits . . . . .	28,251	27,503
Net WRAM and MCBA long-term accounts receivable . . . . .	34,879	16,148
Asset retirement obligations, net . . . . .	17,126	15,812
Interim rates long-term accounts receivable . . . . .	4,568	4,605
Tank coating . . . . .	10,998	8,452
Health care balancing account . . . . .	496	1,000
Pension balancing account . . . . .	2,322	—
Other regulatory assets . . . . .	935	1,431
Total Regulatory Assets . . . . .	<u>\$401,147</u>	<u>\$355,930</u>
<i>Regulatory Liabilities</i>		
Future tax benefits due to customers . . . . .	\$168,343	\$ 33,231
Health care balancing account . . . . .	7,749	—
Conservation program . . . . .	2,273	584
Pension balancing account . . . . .	364	695
Net WRAM and MCBA long-term payable . . . . .	513	611
Other regulatory liabilities . . . . .	464	3,614
Total Regulatory Liabilities . . . . .	<u>\$179,706</u>	<u>\$ 38,735</u>

The increase in future tax benefits due to customers as of December 31, 2017, as compared to the prior year, was due to federal tax law changes enacted by the federal Tax Cuts and Jobs Act (TCJA) on December 22, 2017. The TCJA reduced the federal corporate income tax rate from 35 percent to 21 percent beginning on January 1, 2018 and GAAP requires the Company to re-measure all existing deferred income tax assets and liabilities to reflect the reduction in the federal tax rate on the enactment date. The Company is working with state regulators to finalize the ratepayer refund process to ensure compliance with federal normalization rules.

The Company's pension and postretirement health care benefits regulatory asset is the amount the Company expects to recover from customers in the future for these plans at the end of the calendar year.

The property-related temporary differences are primarily due to: (i) the difference between book and federal income tax depreciation on utility plant that was placed in service before the regulatory Commissions adopted normalization for rate making purposes; and (ii) certain (state) deferred taxes for which flow through accounting continues to be applied to originating deferred

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

taxes. The regulatory asset will be recovered in rates in future periods as the tax effects of the temporary differences previously flowed-through to customers reverse.

Other accrued benefits are accrued benefits for vacation, self-insured workers' compensation, and directors' retirement benefits. The net WRAM and MCBA long-term accounts receivable is the under-collected portion of recorded revenues that are not expected to be collected from customers within 12 months. The asset retirement obligation regulatory asset represents the difference between costs associated with asset retirement obligations and amounts collected in rates. Tank coating represents the maintenance costs for tank coating projects that are recoverable from customers. The health care balancing account regulatory asset/liability is for incurred health care costs that exceeded/was below the cost recovery in rates and is recoverable/refundable from/to customers.

Short-term regulatory assets and liabilities are excluded from the above table.

The short-term regulatory assets for 2017 and 2016 were \$36.8 million and \$30.3 million, respectively. The short-term regulatory assets, as of December 31, 2017, primarily consist of net WRAM and MCBA receivables. As of December 31, 2016, the short-term regulatory assets were primarily interim rates, 2014-2015 drought recovery, and net WRAM and MCBA receivables.

The short-term portion of regulatory liabilities for 2017 and 2016 were \$59.3 million and \$4.8 million, respectively. The short-term regulatory liabilities, as of December 31, 2017, primarily consist of TCP settlement proceeds (see Note 14—Commitments and Contingencies) and net WRAM and MCBA liability balances. As of December 31, 2016, the short-term regulatory liabilities were primarily net WRAM and MCBA liability balances and net refund balances to customers for the pension and conservation programs from the 2012 GRC.

***Impairment of Long-Lived Assets, Intangibles and Goodwill***

The Company's long-lived assets include transmission and distribution plant, equipment, land, buildings, and intangible assets. Long-lived assets, other than land, are depreciated or amortized over their estimated useful lives, and are reviewed for impairment whenever changes in circumstances indicate the carrying value of the assets may not be recoverable. Such circumstances would include items such as a significant decrease in the market value of a long-lived asset, a significant adverse change in the manner in which the asset is being used or planned to be used or in its physical condition, or a history of operating or cash flow losses associated with the uses of the asset. In addition, changes in the expected useful life of these long-lived assets may also be an impairment indicator. When such events or changes occur, the Company estimates the fair value of the asset from future cash flows expected to result from the use and, if applicable, the eventual disposition of the assets, and compare that to the carrying value of the asset. If the carrying value is greater than the fair value, then an impairment loss is recognized equal to the amount by which the asset's carrying value exceeds its fair value. The key variables that must be estimated include assumptions regarding sales volume, rates, operating costs, labor and other benefit costs, capital additions, assumed discount rates and other economic factors. These variables require significant management judgment and include inherent uncertainties since they are forecasting future events.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

A variation in the assumptions used could lead to a different conclusion regarding the realizability of an asset and, thus could have a significant effect on the consolidated financial statements.

Goodwill is measured as the excess of the cost of an acquisition over the sum of the amounts assigned to identifiable assets acquired less liabilities assumed. Goodwill is not amortized but instead is reviewed annually at November 30th for impairment or more frequently if impairment indicators arise. The impairment test is performed at the reporting unit level using a two-step, fair-value based approach. The first step determines the fair value of the reporting unit and compares it to the reporting unit's carrying value. If the fair value of the reporting unit is less than its carrying amount, a second step is performed to measure the amount of impairment loss, if any. The second step allocates the fair value of the reporting unit to the Company's tangible and intangible assets and liabilities. This derives an implied fair value for the reporting unit's goodwill. If the carrying amount of the reporting unit's goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized equal to the excess.

***Long-Term Debt Premium, Discount and Expense***

The premiums, discounts, and issuance expenses on long-term debt are amortized over the original lives of the related debt on a straight-line basis which approximates the effective interest method. Premiums paid on the early redemption of certain debt and the unamortized original issuance discount and expense are amortized over the life of new debt issued in conjunction with the early redemption. Amortization expense included in interest expense for 2017, 2016, and 2015 was \$0.9 million, \$0.9 million, and \$0.8 million, respectively.

***Advances for Construction***

Advances for construction consist of payments received from developers for installation of water production and distribution facilities to serve new developments. Advances are excluded from rate base for rate setting purposes. Annual refunds are made to developers without interest. Advances of \$182.5 million, and \$182.4 million at December 31, 2017 and 2016, respectively, will be refunded primarily over a 40-year period in equal annual amounts. Estimated refunds of advances for the succeeding 5 years are approximately \$7.9 million in 2018, \$7.7 million in 2019, \$7.7 million in 2020, \$7.6 million in 2021, and \$7.6 million in 2022.

***Contributions in Aid of Construction***

Contributions in aid of construction represent payments received from developers, primarily for fire protection purposes, which are not subject to refunds. Facilities funded by contributions are included in utility plant, but excluded from rate base. Depreciation related to assets acquired from contributions is charged to the Contributions in Aid of Construction account.

***Income Taxes***

The Company accounts for income taxes using the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences

**CALIFORNIA WATER SERVICE GROUP**  
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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Measurement of the deferred tax assets and liabilities is at enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date. The Company evaluates the need for a valuation allowance on deferred tax assets based on historical taxable income and projected taxable income for future tax years.

Historically the Commissions reduced revenue requirements for the tax effects of certain originating temporary differences and allowed recovery of these tax costs as the related temporary differences reverse. The Commissions have granted the Company rate increases to reflect the normalization of the tax benefits of the federal accelerated methods and available Investment Tax Credits (ITC) for all assets placed in service after 1980. ITCs are deferred and amortized over the lives of the related properties for book purposes. The CPUC granted flow through for state taxes.

Subsequent to 1986, Advances for Construction and Contributions in Aid of Construction were taxable for federal income tax purposes. Subsequent to 1991, Advances for Construction and Contributions in Aid of Construction were subject to California income tax. Due to changes in the federal tax law in 1996 and the California tax law in 1997 only deposits for new services were taxable. In late 2000, federal regulations were further modified to exclude contributions of fire services from taxable income. With the enactment of the TCJA, all Advances for Construction and Contributions in Aid of Construction received from developers after December 22, 2017 became taxable for federal income tax purposes.

The accounting standards for accounting for uncertainty in income taxes allows the inclusion of interest and penalties related to uncertain tax positions as a component of income taxes. See note 10 "Income Taxes".

***Workers' Compensation***

For workers' compensation, the Company estimates the liability associated with claims submitted and claims not yet submitted based on historical data. Expenses for workers compensation insurance are included in rates on a pay-as-you-go basis. Therefore, a corresponding regulatory asset has been recorded.

***Earnings per Share***

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 into common stock. Restricted Stock Awards (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.

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**Notes to Consolidated Financial Statements (Continued)**  
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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

The Company did not grant any Stock Appreciation Rights (SARs) in 2017, 2016, and 2015. There were no SARs outstanding as of December 31, 2017 and 2016. As of December 31, 2015, there were 64,500 shares of SARs outstanding.

All SARs were dilutive in 2017, 2016, and 2015. The dilutive effect is shown in the table below:

	2017	2016	2015
	(In thousands, except per share data)		
Net income available to common stockholders . .	\$67,181	\$48,675	\$45,017
Weighted average common shares, basic . . . . .	48,009	47,953	47,865
Dilutive SARs (treasury method) . . . . .	—	3	15
Weighted average common shares, dilutive . . . .	48,009	47,956	47,880
Earnings per share—basic . . . . .	\$ 1.40	\$ 1.02	\$ 0.94
Earnings per share—diluted . . . . .	\$ 1.40	\$ 1.01	\$ 0.94

***Stock-based Compensation***

Stock-based compensation cost is measured at the grant date based on the fair value of the award. The Company recognizes compensation expense on a straight-line basis over the requisite service period, which is the vesting period.

***Comprehensive Income or Loss***

Comprehensive income for all periods presented was the same as net income.

***Accumulated Other Comprehensive Income***

The Company did not have any accumulated other comprehensive income or loss transactions as of December 31, 2017 and 2016.

***Adoption of New Accounting Standards***

In March 2016, the Financial Accounting Standards Board (FASB) issued updated accounting guidance on simplifying the accounting for share-based payments (Accounting Standards Update (ASU) 2016-09), which includes the accounting for share-based payment transactions, the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The Company adopted and implemented the changes to accounting for share-based payments on January 1, 2017 and applied the requirements retrospectively on the statement of cash flows for all periods presented. The Company's forfeiture policy did not change and the Company continues to account for forfeitures when they occur. For the twelve month period ended December 31, 2017, the Company recorded \$0.6 million of income tax benefits in excess of compensation costs for share-based compensation which reduced the effective tax rate. The tax-related cash flows resulting from share-based payments were reported as operating



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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

activities and the associated cash paid by the company for employee tax withholding transactions were reported as financing activities on the consolidated statement of cash flows.

The following tables show the effects of the accounting change to the Condensed Consolidated Statements of Cash Flows for 2016 and 2015:

	<b>2016</b>		
	<b>As Reported on Form 10-K</b>	<b>Adjusted Balance on Form 10-K</b>	<b>Increase (Decrease) from Retrospective Adoption</b>
<i>Cash Flow Classification</i>			
Other changes in noncurrent assets and liabilities . . . . .	\$ 6,162	\$ 6,906	\$ 744
Net cash provided by operating activities . . . . .	159,700	160,444	744
Repurchase of common stock . . . . .	—	(744)	(744)
Net cash provided by financing activities	87,794	87,050	(744)
<b>2015</b>			
	<b>As Reported on Form 10-K</b>	<b>Adjusted Balance on Form 10-K</b>	<b>Increase (Decrease) from Retrospective Adoption</b>
<i>Cash Flow Classification</i>			
Other changes in noncurrent assets and liabilities . . . . .	\$ 10,610	\$ 10,948	\$ 338
Net cash provided by operating activities . . . . .	144,631	144,969	338
Repurchase of common stock . . . . .	—	(338)	(338)
Net cash provided by financing activities	22,877	22,539	(338)

***New Accounting Standards Issued But Not Yet Adopted***

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, which amends the existing revenue recognition guidance. In August 2015, the FASB deferred the effective date of this amendment for public companies by one year to January 1, 2018, with early adoption permitted as of the original effective date of January 1, 2017. The Company completed an evaluation of the new revenue standard and implemented the standard on January 1, 2018 using the modified retrospective method. The adoption of the new revenue standard will not materially impact the timing or recognition of revenue related to the sale and delivery of water to its customers, which is a significant percentage of the Company's revenue. The adoption of the new revenue standard will result in expanded revenue related disclosures. The Company plans to disclose revenues from contracts with customers separately from regulatory balancing account revenue and disaggregate customer contract revenue by customer class.

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**2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

In February 2016, the FASB issued ASU 2016-02, *Leases*. This update changes the accounting treatment of leases and related disclosure requirements. In November of 2017, the FASB tentatively decided to amend the new leasing guidance such that entities may elect not to restate their comparative periods in the period of adoption. The guidance requires lessees to recognize an asset and liability on the balance sheet for all of their lease obligations. Operating leases were previously not recognized on the balance sheet. ASU 2016-02 is effective for annual reporting periods beginning after December 15, 2018 and early adoption is permitted. The Company will adopt the standard using the modified retrospective method for its existing leases and expects this standard to increase lease assets and lease liabilities on the Consolidated Balance Sheets. The Company does not expect that the guidance will have a material impact on the Consolidated Statements of Income, Consolidated Statements of Cash Flows, and lease disclosures.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230)—Classification of Certain Cash Receipts and Cash Payments*. This update adds and clarifies guidance on the classification of certain cash receipts and payments in the statement of cash flows. ASU 2016-15 became effective for the Company on January 1, 2018. The Company does not expect the guidance to have a material effect on its consolidated financial statements and related disclosures.

In March 2017, the FASB issued ASU 2017-07, *Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. The update requires employers to present the service cost component of the net periodic benefit cost in the same income statement line item as other employee compensation costs arising from services rendered during the period. The other components of net benefit cost, including interest cost, expected return on plan assets, amortization of prior service cost/credit and actuarial gain/loss, and settlement and curtailment effects, are to be presented as non-operating items. Employers will have to disclose the line(s) used to present the other components of net periodic benefit cost, if the components are not presented separately in the income statement. The standard only allows the service cost component to be eligible for capitalization. The Company has completed an evaluation of the new standard and its impact on its consolidated financial statements and related disclosures and adopted the new accounting standard on January 1, 2018. The adoption of this guidance will change the Company's financial statement presentation of net benefit costs and modify the amounts eligible to be capitalized. However, based on current regulatory authorization, the changes required by the standard will not materially impact the results of operations.

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**3 OTHER INCOME AND EXPENSES**

The Company conducts various non-regulated activities as reflected in the table below:

	2017		2016		2015	
	Revenue	Expense	Revenue	Expense	Revenue	Expense
Operating and maintenance . . . . .	\$ 8,621	\$ 8,847	\$ 8,430	\$ 9,061	\$ 9,385	\$10,438
Leases . . . . .	2,015	182	1,923	204	1,929	208
Design and construction . . . . .	1,918	1,635	1,792	1,473	1,399	1,292
Meter reading and billing . . . . .	256	(6)	242	62	597	434
Interest income . . . . .	68	—	18	—	39	—
Change in value of life insurance contracts (gain) loss . . . . .	—	(3,057)	—	(1,026)	—	218
Other non-regulated income and expenses . . . . .	3,020	1,789	4,180	1,671	2,275	1,454
Total . . . . .	<u>\$15,898</u>	<u>\$ 9,390</u>	<u>\$16,585</u>	<u>\$11,445</u>	<u>\$15,624</u>	<u>\$14,044</u>

Operating and maintenance services and meter reading and billing services are provided for water and wastewater systems owned by private companies and municipalities. The agreements call for a fee-per-service or a flat-rate amount per month. Leases have been entered into with telecommunications companies for cellular phone antennas placed on the Company's property. Design and construction services are for the design and installation of water mains and other water infrastructure for others outside the Company's regulated service areas. Third-party insurance program gains and losses are included in other non-regulated income and expenses. Also, the 2016 other non-regulated income and expenses included a litigation gain of \$1.5 million.

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**4 INTANGIBLE ASSETS**

As of December 31, 2017 and 2016, intangible assets that will continue to be amortized and those not amortized were:

	Weighted Average Amortization Period (years)	2017			2016		
		Gross Carrying Value	Accumulated Amortization	Net Carrying Value	Gross Carrying Value	Accumulated Amortization	Net Carrying Value
Amortized intangible assets:							
Water pumping rights usage		\$ 1,084	\$ 108	\$ 976	\$ 1,084	\$ 105	\$ 979
Water planning studies . . . . .	11	15,922	10,306	5,616	15,734	9,307	6,427
Leasehold improvements and other . . . . .	19	1,426	804	622	1,331	696	635
Total . . . . .		<u>\$18,432</u>	<u>\$11,218</u>	<u>\$7,214</u>	<u>\$18,149</u>	<u>\$10,108</u>	<u>\$8,041</u>
Unamortized intangible assets:							
Perpetual water rights and other . . .		\$ 3,780	\$ —	\$3,780	\$ 3,776	\$ —	\$3,776

Water pumping rights usage is the amount of water pumped from aquifers to be treated and distributed to customers.

For the years ended December 31, 2017 and 2016, amortization of intangible assets was \$1.6 million and for the year ended December 31, 2015, amortization of intangible assets was \$1.4 million. Estimated future amortization expense related to intangible assets for the succeeding 5 years is approximately \$1.4 million in 2018, \$1.2 million in 2019, \$0.7 million in 2020, \$0.6 million in 2021, \$0.5 million in 2022, and \$2.7 million thereafter.

**5 PREFERRED STOCK**

The Company is authorized to issue 241,000 shares of Preferred Stock as of December 31, 2017. No shares of Preferred Stock were issued and outstanding as of December 31, 2017 or 2016.

**6 COMMON STOCKHOLDERS' EQUITY**

As of December 31, 2017 and 2016, 48,012,432 shares and 47,964,915 shares, respectively, of common stock were issued and outstanding.

***Dividend Reinvestment and Stock Repurchase Plan***

The Company has a Dividend Reinvestment and Stock Purchase Plan (DRIP Plan). Under the DRIP Plan, stockholders may reinvest dividends to purchase additional Company common stock

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**6 COMMON STOCKHOLDERS' EQUITY (Continued)**

without commission fees. The DRIP Plan also allows existing stockholders and other interested investors to purchase Company common stock through the transfer agent up to certain limits. The Company's transfer agent operates the DRIP Plan and purchases shares on the open market to provide shares for the Plan.

**7 SHORT-TERM BORROWINGS**

On March 10, 2015, the Company and Cal Water entered into Syndicated Credit Agreements, which provide for unsecured revolving credit facilities of up to an initial aggregate amount of \$450.0 million for a term of 5 years. The Company and subsidiaries that it designates may borrow up to \$150.0 million under the Company's revolving credit facility. Cal Water may borrow up to \$300.0 million under its revolving credit facility; however, all borrowings need to be repaid within 24 months unless otherwise authorized by the CPUC. The credit facilities may each be expanded by up to \$50.0 million subject to certain conditions. The proceeds from the revolving credit facilities may be used for working capital purposes, including the short-term financing of capital projects. The base loan rate may vary from LIBOR plus 72.5 basis points to LIBOR plus 95 basis points, depending on the Company's total capitalization ratio. Likewise, the unused commitment fee may vary from 8 basis points to 12.5 basis points based on the same ratio.

The revolving credit facilities contain affirmative and negative covenants and events of default customary for credit facilities of this type including, among other things, limitations and prohibitions relating to additional indebtedness, liens, mergers, and asset sales. Also, these unsecured credit agreements contain financial covenants governing the Company and its subsidiaries' consolidated total capitalization ratio and interest coverage ratio.

As of December 31, 2017 and December 31, 2016, the outstanding borrowings on the Company lines of credit were \$55.1 million and \$57.1 million, respectively. The borrowings on the Cal Water lines of credit as of December 31, 2017 was \$220.0 million and \$40.0 million as of December 31, 2016.

The following table represents borrowings under the bank lines of credit:

	<u>2017</u>	<u>2016</u>
Maximum short-term borrowings . . . . .	\$275,100	\$97,100
Average amount outstanding . . . . .	\$179,739	\$65,804
Weighted average interest rate . . . . .	2.05%	1.33%

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**8 LONG-TERM DEBT**

As of December 31, 2017 and 2016, long-term debt outstanding was:

	<u>Series</u>	<u>Interest Rate</u>	<u>Maturity Date</u>	<u>2017</u>	<u>2016</u>
First Mortgage Bonds . . . . .	TTT	4.610%	2056	\$ 10,000	\$ 10,000
	SSS	4.410%	2046	40,000	40,000
	QQQ	3.330%	2025	50,000	50,000
	RRR	4.310%	2045	50,000	50,000
	PPP	5.500%	2040	100,000	100,000
	LL	5.875%	2019	100,000	100,000
	AAA	7.280%	2025	20,000	20,000
	BBB	6.770%	2028	20,000	20,000
	CCC	8.150%	2030	20,000	20,000
	DDD	7.130%	2031	20,000	20,000
	EEE	7.110%	2032	20,000	20,000
	FFF	5.900%	2017	—	20,000
	GGG	5.290%	2022	9,091	10,909
	HHH	5.290%	2022	9,091	10,909
	III	5.540%	2023	5,454	6,364
	JJJ	5.440%	2018	909	1,818
	LLL	5.480%	2018	10,000	10,000
	OOO	6.020%	2031	20,000	20,000
	CC	9.860%	2020	16,900	17,000
				<u>521,445</u>	<u>547,000</u>
Total First Mortgage Bonds . . . .					
California Department of Water Resources Loans . . . . .		2.6% to 8.0%	2018 - 32	6,201	6,519
Other Long-term debt . . . . .				7,956	8,909
Unamortized debt issuance costs				(3,889)	(4,475)
Total long-term debt . . . . .				<u>531,713</u>	<u>557,953</u>
Less current maturities . . . . .				<u>15,920</u>	<u>26,208</u>
Long-term debt excluding current maturities . . . . .				<u>\$515,793</u>	<u>\$531,745</u>

Cal Water repaid \$20.0 million of First Mortgage Bond FFF, which matured in 2017.

On October 4, 2011, Cal Water entered into a capital lease arrangement with the City of Hawthorne to operate the City's water system for a 15-year period. The \$6.4 million and \$7.0 million capital lease liability as of December 31, 2017 and 2016 is included in other long-term debt and current maturities set forth above.

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**9 OTHER ACCRUED LIABILITIES**

As of December 31, 2017 and 2016, other accrued liabilities were:

	<u>2017</u>	<u>2016</u>
Accrued and deferred compensation . . . . .	\$23,916	\$22,572
Accrued benefits and workers' compensation claims . . . . .	6,640	6,460
Other . . . . .	6,115	6,028
<b>TOTAL OTHER ACCRUED LIABILITIES . . . . .</b>	<u>\$36,671</u>	<u>\$35,060</u>

**10 INCOME TAXES**

Income tax expense (benefit) consisted of the following:

	<u>Federal</u>	<u>State</u>	<u>Total</u>
<i>2017</i>			
Current . . . . .	\$ —	\$ 3	\$ 3
Deferred . . . . .	32,652	707	33,359
<b>Total . . . . .</b>	<u>\$32,652</u>	<u>\$ 710</u>	<u>\$33,362</u>
<i>2016</i>			
Current . . . . .	\$ 130	\$ 2	\$ 132
Deferred . . . . .	26,603	81	26,684
<b>Total . . . . .</b>	<u>\$26,733</u>	<u>\$ 83</u>	<u>\$26,816</u>
<i>2015</i>			
Current . . . . .	\$ 9,591	\$ 1,706	\$11,297
Deferred . . . . .	15,374	(1,382)	13,992
<b>Total income tax . . . . .</b>	<u>\$24,965</u>	<u>\$ 324</u>	<u>\$25,289</u>

The Company's 2017, 2016 and 2015 federal qualified repairs and maintenance deductions totaled \$85.7 million, \$84.9 million, and \$65.2 million, respectively.

The total federal NOL carry-forward was \$72.6 million and the state NOL carry-forward was \$55.4 million as of December 31, 2017. Management has concluded that the NOL carry-forward amounts are more likely than not to be recovered and therefore require no valuation allowance. The loss and credit carry-forward will begin to expire in 2032.

As of December 31, 2017, the California Enterprise Zone (EZ) credit was \$4.2 million net of federal tax benefit for qualified property purchased before January 1, 2015, and placed in service before January 1, 2016. The Company has carry-forward California EZ credits of \$2.3 million net of any unrecognized tax benefit. Unused State of California EZ credits can carry-forward until 2024.

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**10 INCOME TAXES (Continued)**

The difference between the recorded and the statutory income tax expense was reconciled in the table below:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Statutory income tax . . . . .	\$35,190	\$26,422	\$24,607
Increase (reduction) in taxes due to:			
State income taxes net of federal tax benefit . . . . .	5,781	4,341	4,043
Effect of regulatory treatment of fixed asset differences . . . . .	(4,584)	(4,298)	(3,450)
Investment tax credits . . . . .	(74)	(74)	(74)
AFUDC equity . . . . .	(1,528)	—	—
Share base stock compensation . . . . .	(581)	—	—
Other . . . . .	(842)	425	163
Total income tax . . . . .	<u>\$33,362</u>	<u>\$26,816</u>	<u>\$25,289</u>

The effect of regulatory treatment of fixed asset differences includes estimated repair and maintenance deductions and asset related flow through items.

On December 22, 2017, the U.S. government enacted expansive tax legislation commonly referred to as the TCJA. Among other provisions, the TCJA reduces the federal income tax rate from 35 percent to 21 percent beginning on January 1, 2018 and eliminated bonus depreciation for utilities. The TCJA required the Company to re-measure all existing deferred income tax assets and liabilities to reflect the reduction in the federal tax rate. The Company made reasonable estimates to reflect the impacts of the TCJA and recorded provisional amounts, in accordance with rules issued by the SEC in Staff Accounting Bulletin No. 118, for the re-measurement of deferred tax balances as of December 31, 2017.

During the three months and year ended December 31, 2017, the Company recorded a provisional re-measurement of its deferred tax balances (related mostly to timing differences for plant-related items) which was offset by a change from a net deferred income tax regulatory asset to a net regulatory liability. The Company is working with state regulators to finalize the ratepayer net refund of \$108.0 million to ensure compliance with federal normalization rules.

The final transition impacts of the TCJA may differ from the recorded amounts, possibly materially, due to, among other things, regulatory decisions that could differ from the Company's determination of how the impacts of the TCJA are allocated between customers and shareholders. In addition, while the Company was able to make reasonable estimates of the impact of the reduction in federal tax rate and the elimination of bonus depreciation due to the enactment of the TCJA; the Company has not completed analysis for areas of the TCJA around Internal Revenue Code Section 162(m), full expensing of fixed assets, and other asset related items of the TCJA. Changes in interpretations, guidance on legislative intent, and any changes in accounting standards for income taxes in response to the TCJA could impact the recorded amounts. The Company will finalize and record any adjustments related to the TCJA within the one year measurement period provided under Staff Accounting Bulletin No. 118.



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**10 INCOME TAXES (Continued)**

The deferred tax assets and deferred tax liabilities as of December 31, 2017 and 2016, were presented in the following table:

	<u>2017</u>	<u>2016</u>
Deferred tax assets:		
Developer deposits for extension agreements and contributions in aid of construction . . . . .	\$ 33,552	\$ 46,318
Net operating loss carryforward and tax credits . . . . .	13,329	12,348
Pension . . . . .	7,906	9,865
Income tax regulatory liability . . . . .	41,712	—
Other . . . . .	280	5,651
Total deferred tax assets . . . . .	<u>96,779</u>	<u>74,182</u>
Deferred tax liabilities:		
Property related basis and depreciation differences . . . . .	262,442	347,071
WRAM/MCBA and interim rates balancing accounts . . . . .	24,733	20,714
Other . . . . .	2,550	5,321
Total deferred tax liabilities . . . . .	<u>289,725</u>	<u>373,106</u>
Net deferred tax liabilities . . . . .	<u>\$192,946</u>	<u>\$298,924</u>

The decreases in developer deposits for extension agreements and contributions in aid of construction and property related basis and depreciation differences, as compared to the prior year, were mostly due to the re-measurement of deferred tax balances as required by the TCJA. The increase in the deferred tax asset for the income tax regulatory liability represents the tax gross up to the revenue requirement for the re-measurement of net deferred taxes associated with a lower federal income tax rate as a result of the TCJA, as well as the future tax benefit associated with the expected reduction in revenue.

A valuation allowance was not required at December 31, 2017 and 2016. Based on historical taxable income and future taxable income projections over the period in which the deferred assets are deductible, management believes it is more likely than not that the Company will realize the benefits of the deductible differences.

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**10 INCOME TAXES (Continued)**

The following table reconciles the changes in unrecognized tax benefits:

	<u>December 31, 2017</u>	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Balance at beginning of year . . . . .	\$10,499	\$10,298	\$ 7,916
Additions for tax positions taken during prior year . . . . .	—	—	—
Additions for tax positions taken during current year . . . . .	559	201	2,382
Reductions for tax positions taken during a prior year . . . . .	—	—	—
Lapse of statute of limitations . . . . .	—	—	—
Balance at end of year . . . . .	<u>\$11,058</u>	<u>\$10,499</u>	<u>\$10,298</u>

The Company does not expect a material change in its unrecognized tax benefits within the next 12 months. The component of unrecognized tax benefits that, if recognized, would affect the effective tax rate as of December 31, 2017, for the Company was \$2.1 million, with the remaining balance representing the potential deferral of taxes to later years.

The Company's federal income tax years subject to an examination are from 2013 to 2017 and the state income tax years subject to an examination are from 2012 to 2017.

**11 EMPLOYEE BENEFIT PLANS**

***Savings Plan***

The Company sponsors a 401(k) qualified defined contribution savings plan that allows participants to contribute up to 20% of pre-tax compensation. Effective January 1, 2010, the Company matches 75 cents for each dollar contributed by the employee up to a maximum Company match of 6.0% of base salary. Company contributions were \$5.6 million, \$5.4 million, and \$5.0 million, for the years 2017, 2016, and 2015, respectively.

***Pension Plans***

The Company provides a qualified, defined-benefit, non-contributory pension plan for substantially all employees. The accumulated benefit obligations of the pension plan are \$513.6 million and \$438.0 million as of December 31, 2017 and 2016, respectively. The fair value of pension plan assets was \$460.9 million and \$376.5 million as of December 31, 2017 and 2016, respectively.

Prior to 2010, pension payment obligations were generally funded by the purchase of an annuity from a life insurance company. Beginning in 2010, the pension plan trust pays monthly benefits to retirees, rather than the purchase of an annuity. Expected payments to be made are \$13.5 million in 2018, \$15.0 million in 2019, \$16.5 million in 2020, \$18.1 million in 2021, and \$20.0 million in 2022. The aggregate benefits expected to be paid in the 5 years 2023 through 2027 are \$125.8 million. The expected benefit payments are based upon the same assumptions used to measure the Company's benefit obligation at December 31, 2017, and include estimated future employee service.

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**11 EMPLOYEE BENEFIT PLANS (Continued)**

The Company also maintains an unfunded, non-qualified, supplemental executive retirement plan. The unfunded supplemental executive retirement plan accumulated benefit obligations were \$56.7 million and \$46.0 million as of December 31, 2017 and 2016, respectively. Benefit payments under the supplemental executive retirement plan are paid currently and are included in the preceding paragraph.

The costs of the pension and retirement plans are charged to expense and utility plant. The Company makes annual contributions to fund the amounts accrued for pension cost.

***Other Postretirement Plan***

The Company provides substantially all active, permanent employees with medical, dental, and vision benefits through a self-insured plan. Employees retiring at or after age 58, along with their spouses and dependents, continue participation in the plan by payment of a premium. Plan assets are invested in mutual funds, short-term money market instruments and commercial paper based upon a similar asset mix to the pension plan. Retired employees are also provided with a five thousand dollar life insurance benefit.

The Company records the costs of postretirement benefits other than pensions (PBOP) during the employees' years of active service. Postretirement benefit expense recorded in 2017, 2016, and 2015, was \$8.5 million, \$8.9 million, and \$15.1 million, respectively. The remaining net periodic benefit cost was \$3.5 million at December 31, 2017, and is being recovered through future customer rates and is recorded as a regulatory asset. The expected benefit payments, net of retiree premiums and Medicare Part D subsidies, are \$2.3 million in 2018, \$2.5 million in 2019, \$2.7 million in 2020, \$2.9 million in 2021, and \$3.2 million in 2022. The aggregate benefits expected to be paid in the 5 years 2023 through 2027 are \$20.0 million. The expected Medicare Part D subsidies are \$0.3 million in 2018, \$0.3 million in 2019, \$0.3 million in 2020, \$0.4 million in 2021, and \$0.3 million in 2022.

***Benefit Plan Assets***

The Company actively manages pensions and PBOP trust (Plan) assets. The Company's investment objectives are:

- Maximize the return on the assets, commensurate with the risk that the Company deems appropriate to, meet the obligations of the Plans, minimize the volatility of the pension expense, and account for contingencies;
- Generate a rate of return for the total portfolio that equals or exceeds the actuarial investment rate assumption;

Additionally, the rate of return of the total fund is measured periodically against an index comprised of 35% of the Standard & Poor's Index, 15% of the Russell 2000 Index, 10% of the MSCI EAFE Index, and 40% of the Lehman Aggregate Bond Index. The index is consistent with the Company's rate of return objective and indicates the Company's long-term asset allocation objective.

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**11 EMPLOYEE BENEFIT PLANS (Continued)**

The Company applies a risk management framework for managing the risks associated with employee benefit plan trust assets. The guiding principles of this risk management framework are the clear articulation of roles and responsibilities, appropriate delegation of authority, and proper accountability and documentation. Trust investment policies and investment manager guidelines include provisions to ensure prudent diversification, manage risk through appropriate use of physical direct asset holdings and derivative securities, and identify permitted and prohibited investments.

The Company's target asset allocation percentages for major categories of the pension plan are reflected in the table below:

	<u>Minimum Exposure</u>	<u>Target</u>	<u>Maximum Exposure</u>
Fixed Income . . . . .	35%	40%	45%
Total Domestic Equity: . . . . .	40%	50%	60%
Small Cap Stocks . . . . .	10%	15%	20%
Large Cap Stocks . . . . .	30%	35%	45%
Non-U.S. Equities . . . . .	5%	10%	15%

The fixed income category includes money market funds, short-term bond funds, and cash. The majority of fixed income investments range in maturities from less than 1 to 5 years.

The Company's target allocation percentages for the PBOP trust is similar to the pension plan except for a larger allocation in fixed income investments and a lower allocation in equity investments.

The Company uses the following criteria to select investment funds:

- Fund past performance;
- Fund meets criteria of Employee Retirements Income Security Act (ERISA);
- Timeliness and completeness of fund communications and reporting to investors;
- Stability of fund management company;
- Fund management fees; and
- Administrative costs incurred by the Plan.

***Plan Fair Value Measurements***

The fair value measurements standard establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to

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**11 EMPLOYEE BENEFIT PLANS (Continued)**

unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under the standard are described below:

*Level 1*—Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Plan has the ability to access.

*Level 2*—Inputs to the valuation methodology include:

- Quoted market prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

*Level 3*—Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

All Plan investments are level one investments in mutual funds and are valued at the net asset value (NAV) of the shares held at December 31, 2017 and 2016:

	<b>Pension Benefits</b>				<b>Other Benefits</b>			
	<b>2017</b>	<b>%</b>	<b>2016</b>	<b>%</b>	<b>2017</b>	<b>%</b>	<b>2016</b>	<b>%</b>
Fixed Income . . . . .	\$171,403	37%	\$141,576	38%	\$ 60,438	60%	\$54,166	63%
Domestic Equity: Small Cap								
Stocks . . . . .	73,682	16%	61,036	16%	—	—	—	—
Domestic Equity: Large Cap								
Stocks . . . . .	169,661	37%	136,405	36%	40,125	40%	32,412	37%
Non U.S. Equities . . . . .	46,132	10%	37,532	10%	—	—	—	—
<b>Total Plan Assets . . . . .</b>	<b>\$460,878</b>	<b>100%</b>	<b>\$376,549</b>	<b>100%</b>	<b>\$100,563</b>	<b>100%</b>	<b>\$86,578</b>	<b>100%</b>

The pension benefits fixed income category includes \$22.5 million and \$2.3 million of money market fund investments as of December 31, 2017 and 2016, respectively. The other benefits fixed income category includes \$39.4 million and \$35.5 million of money market fund investments as of December 31, 2017 and 2016, respectively.

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**11 EMPLOYEE BENEFIT PLANS (Continued)**

***Changes in Plan Assets, Benefits Obligations, and Funded Status***

The following table reconciles the funded status of the plans with the accrued pension liability and the net postretirement benefit liability as of December 31, 2017 and 2016:

	<b>Pension Benefits</b>		<b>Other Benefits</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
Change in projected benefit obligation:				
Beginning of year . . . . .	\$ 564,755	\$ 501,879	\$122,108	\$136,736
Service cost . . . . .	23,801	20,971	7,152	6,513
Interest cost . . . . .	23,256	22,226	4,988	4,863
Assumption change . . . . .	60,526	15,599	15,298	(8,748)
Experience loss . . . . .	10,836	14,075	(4,546)	(16,041)
Benefits paid, net of retiree premiums . . . . .	(11,840)	(9,995)	(1,632)	(1,215)
End of year . . . . .	<u>\$ 671,334</u>	<u>\$ 564,755</u>	<u>\$143,368</u>	<u>\$122,108</u>
Change in plan assets:				
Fair value of plan assets at beginning of year . . . . .	\$ 376,549	\$ 328,634	\$ 86,578	\$ 72,886
Actual return on plan assets . . . . .	64,365	27,916	6,508	5,342
Employer contributions . . . . .	31,804	29,994	9,109	9,565
Retiree contributions and Medicare part D subsidies . . . . .	—	—	1,884	1,611
Benefits paid . . . . .	(11,840)	(9,995)	(3,516)	(2,826)
Fair value of plan assets at end of year . . . . .	<u>\$ 460,878</u>	<u>\$ 376,549</u>	<u>\$100,563</u>	<u>\$ 86,578</u>
Funded status(1) . . . . .	\$(210,456)	\$(188,206)	\$(42,805)	\$(35,530)
Unrecognized actuarial loss . . . . .	150,545	126,610	39,796	31,821
Unrecognized prior service cost . . . . .	20,342	26,123	165	207
Net amount recognized . . . . .	<u>\$ (39,569)</u>	<u>\$ (35,473)</u>	<u>\$ (2,844)</u>	<u>\$ (3,502)</u>

(1) The short-term portion of the pension benefits was \$2.0 million as of December 31, 2017 and 2016.

Amounts recognized on the balance sheet consist of:

	<b>Pension Benefits</b>		<b>Other Benefits</b>	
	<b>2017</b>	<b>2016</b>	<b>2017</b>	<b>2016</b>
(Accrued) benefit costs . . . . .	\$ 60	\$ —	\$ (3,461)	\$ (4,119)
Accrued benefit liability . . . . .	(210,456)	(188,206)	(42,805)	(35,530)
Regulatory asset . . . . .	170,827	152,733	43,422	36,147
Net amount recognized . . . . .	<u>\$ (39,569)</u>	<u>\$ (35,473)</u>	<u>\$ (2,844)</u>	<u>\$ (3,502)</u>

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**11 EMPLOYEE BENEFIT PLANS (Continued)**

***Valuation Assumptions***

Below are the actuarial assumptions used in determining the benefit obligation for the benefit plans:

	<u>Pension Benefits</u>		<u>Other Benefits</u>	
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Weighted average assumptions as of December 31:				
Discount rate . . . . .	3.60%	4.15%	3.65%	4.25%
Long-term rate of return on plan assets . . . . .	6.50%	6.50%	5.50%	5.50%
Rate of compensation increases . . . . .	3.25%	3.25%	—	—
Cost of living adjustment . . . . .	2.50%	2.50%	—	—

The discount rate was derived from the Citigroup Pension Discount Curve using the expected payouts for the plan. The long-term rate of return assumption is the expected rate of return on a balanced portfolio invested roughly 60% in equities and 40% in fixed income securities. Returns on equity investments were estimated based on estimates of dividend yield and real earnings added to a 2.50% long-term inflation rate. For the pension and other benefit plans, the assumed returns were 7.23% for domestic equities and 8.15% for foreign equities. Returns on fixed-income investments were projected based on investment maturities and credit spreads added to a 2.50% long-term inflation rate. For the pension and other benefit plans, the assumed returns were 4.80% for fixed income investments and 2.78% for short-term cash investments. The average return for the pension and other benefit plans for the last 5 and 10 years was 9.30% and 6.10%, respectively. The Company is using a long-term rate of return of 6.50% for the pension plan and 5.50% for the other benefit plan, which is between the 25th and 75th percentile of expected results.

In 2017, the Company used the Society of Actuaries 2014 Mortality Tables Report (RP-2014) and Mortality Improvement Scale (MP-2017 with modifications) for measuring retirement plan obligations. The RP-2014 mortality table and improvement scale extended the assumed life expectancy of plan participants which resulted in an increase in the Company's accrued benefit obligation as of December 31, 2017 and 2016.

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**11 EMPLOYEE BENEFIT PLANS (Continued)**

**Components of Net Periodic Benefit Cost**

Net periodic benefit costs for the pension and other postretirement plans for the years ended December 31, 2017, 2016, and 2015 included the following components:

	Pension Plan			Other Benefits		
	2017	2016	2015	2017	2016	2015
Service cost . . . . .	\$ 23,801	\$ 20,971	\$ 21,306	\$ 7,152	\$ 6,513	\$ 8,476
Interest cost . . . . .	23,256	22,226	20,104	4,988	4,863	5,654
Expected return on plan assets . .	(24,119)	(21,826)	(19,138)	(4,875)	(4,129)	(3,519)
Net amortization and deferral . . .	12,962	11,990	15,485	1,186	1,660	4,536
Net periodic benefit cost . . . . .	<u>\$ 35,900</u>	<u>\$ 33,361</u>	<u>\$ 37,757</u>	<u>\$ 8,451</u>	<u>\$ 8,907</u>	<u>\$ 15,147</u>

Below are the actuarial assumptions used in determining the net periodic benefit costs for the benefit plans, which uses the end of the prior year as the measurement date:

	Pension Benefits		Other Benefits	
	2017	2016	2017	2016
Weighted average assumptions as of December 31:				
Discount rate . . . . .	4.15%	4.40%	4.25%	4.40%
Long-term rate of return on plan assets . . . . .	6.50%	6.50%	5.50%	5.50%
Rate of compensation increases . . . . .	3.25%	3.25%	—	—

The health care cost trend rate assumption has a significant effect on the amounts reported. For 2017 measurement purposes, the Company assumed a 6.8% annual rate of increase in the per capita cost of covered benefits with the rate decreasing to 5.2% by 2020, then gradually grading down to 4.7% over the next 50 years. A 1-percentage point change in assumed health care cost trends is estimated to have the following effect:

	1-Percentage Point Increase	1-Percentage Point (Decrease)
Effect on total service and interest costs . . . . .	\$ 3,919	\$ (2,795)
Effect on accumulated postretirement benefit obligation . . . . .	\$39,117	\$(28,762)

The Company intends to make annual contributions that meet the funding requirements of ERISA. The Company estimates in 2018 that the annual contribution to the pension plans will be \$35.7 million and the annual contribution to the other postretirement plan will be \$10.8 million.



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**12 STOCK-BASED COMPENSATION PLANS**

The Company's equity incentive plan was approved and amended by stockholders on April 27, 2005 and May 20, 2014. The Company is authorized to issue awards up to 2,000,000 shares of common stock.

During 2017 and 2016, the Company granted annual Restricted Stock Awards (RSAs) of 49,290 and 72,317, respectively, of common stock to officers and directors of the Company. In 2017 and 2016, 20,747 RSAs and 16,617 RSAs, respectively, were canceled. Officer RSAs granted in 2017 and 2016 vest over 36 months with the first year cliff vesting. Director RSAs generally vest at the end of 12 months. During 2017 and 2016, the RSAs granted were valued at \$36.75 and \$25.17 per share, respectively, based upon the fair market value of the Company's common stock on the date of grant.

The Company granted performance-based Restricted Stock Unit Awards (RSUs) of 31,389 and 43,659 of common stock to officers in 2017 and 2016, respectively. Each award reflects a target number of common shares that may be issued to the award recipient. The 2017 and 2016 awards may be earned upon the completion of a 3-year performance period. During 2017 and 2016, the Company issued 38,709 RSUs and 28,424 RSUs, respectively, to officers, and 19,735 RSUs and 6,602 RSUs, respectively, were canceled. Whether RSUs are earned at the end of the performance period will be determined based on the achievement of certain performance objectives set by the Board of Director Compensation Committee in connection with the issuance of the RSUs. The performance objectives are based on the Company's business plan covering the performance period. The performance objectives include achieving the budgeted return on equity, budgeted investment in utility plant, customer service standards, employee safety standards and water quality standards. Depending on the results achieved during the 3-year performance period, the actual number of shares that a grant recipient receives at the end of the performance period may range from 0% to 200% of the target shares granted, provided that the grantee is continuously employed by the Company through the vesting date. If prior to the vesting date employment is terminated by reason of death, disability or normal retirement, then a pro rata portion of this award will vest. RSUs are not included in diluted shares until earned. The RSUs are recognized as expense ratably over the 3 year performance period using a fair market value of \$36.75 per share for the 2017 RSUs and \$25.17 per share for the 2016 RSUs based on an estimate of RSUs earned during the performance period.

The Company has recorded compensation costs for the RSAs and RSUs which are included in administrative and general operating expenses in the amount of \$3.1 million, \$2.8 million, and \$2.9 million for 2017, 2016 and 2015, respectively.

**13 FAIR VALUE OF FINANCIAL INSTRUMENTS**

The accounting guidance for fair value measurements and disclosures provides a single definition of fair value and requires certain disclosures about assets and liabilities measured at fair value. A hierarchical framework for disclosing the observability of the inputs utilized in measuring assets and liabilities at fair value is established by this guidance. The three levels in the hierarchy are described in Note 11—Employee Benefit Plans.

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
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**13 FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)**

Specific valuation methods include the following:

Accounts receivable and accounts payable carrying amounts approximated the fair value because of the short-term maturity of the instruments.

Long-term debt fair values were estimated using the published quoted market price, if available, or the discounted cash flow analysis, based on the current rates available using a risk-free rate (a U.S. Treasury securities yield curve) plus a risk premium of 1.70%.

Advances for construction fair values were estimated using broker quotes from companies that frequently purchase these investments.

	<b>December 31, 2017</b>				
	<b>Cost</b>	<b>Fair Value</b>			<b>Total</b>
		<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Long-term debt, including current maturities	\$531,713	\$—	\$607,492	\$—	\$607,492
Advances for construction . . . . .	182,502	—	75,083	—	75,083
<b>Total . . . . .</b>	<b>\$714,215</b>	<b>\$—</b>	<b>\$682,575</b>	<b>\$—</b>	<b>\$682,575</b>

	<b>December 31, 2016</b>				
	<b>Cost</b>	<b>Fair Value</b>			<b>Total</b>
		<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	
Long-term debt, including current maturities	\$557,953	\$—	\$630,510	\$—	\$630,510
Advances for construction . . . . .	182,448	—	74,460	—	74,460
<b>Total . . . . .</b>	<b>\$740,401</b>	<b>\$—</b>	<b>\$704,970</b>	<b>\$—</b>	<b>\$704,970</b>

**14 COMMITMENTS AND CONTINGENCIES**

**Commitments**

The Company leases offices, equipment and other facilities, two water systems from cities, and has long-term commitments to purchase water from water wholesalers. The commitments are noted in the table below.

	<b>Facility Leases</b>	<b>System Lease</b>	<b>Water Supply Contracts*</b>	<b>Capital Lease Obligations</b>
2018 . . . . .	\$ 950	\$422	\$ 30,708	\$1,053
2019 . . . . .	620	—	30,708	1,284
2020 . . . . .	549	—	30,709	977
2021 . . . . .	341	—	30,709	977
2022 . . . . .	302	—	30,710	977
Thereafter . . . . .	3,078	—	536,826	3,581

\* Estimated annual contractual obligations are based on the same payment levels as 2017.

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**Notes to Consolidated Financial Statements (Continued)**  
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**14 COMMITMENTS AND CONTINGENCIES (Continued)**

Facility Leases

Company Facility leases include office and other facilities in many of its operating districts. The total paid and charged to operations for such leases was \$1.1 million in 2017, \$1.0 million in 2016, and \$1.1 million in 2015.

System Lease

The system lease is a 15-year lease with the City of Commerce that expires in June of 2018. The lease includes an annual lease payment of \$0.8 million per year plus a cost savings sharing arrangement. In 2017, the Company bid to renew the lease agreement after June 2018 and expects the City of Commerce to release the results of the bidding process in 2018.

Water Supply Contracts

The Company has a long-term contract with the Santa Clara Valley Water District that requires the Company to purchase minimum annual water quantities. Purchases are priced at the districts then-current wholesale water rate. The Company operates to purchase sufficient water to equal or exceed the minimum quantities under the contract. The total paid to Santa Clara Valley Water District was \$9.1 million in 2017, \$8.5 million in 2016, and \$6.3 million in 2015.

The Company also has a water supply contract with Stockton East Water District (SEWD) that requires a fixed, annual payment. Each year, the fixed annual payment is adjusted for changes to SEWD's costs. Because of the fixed annual price arrangement, the Company operates to receive as much water as possible from SEWD in order to minimize the cost of operating Company-owned wells used to supplement SEWD deliveries. The total paid under the contract was \$14.1 million in 2017, \$12.2 million in 2016, and \$9.8 million in 2015. Future increased costs by SEWD are expected to be offset by a decline in the allocation of costs to the Company, as other customers of SEWD are expected to receive a larger allocation based upon growth of their service areas.

On September 21, 2005, the Company entered into an agreement with Kern County Water Agency (Agency) to obtain treated water for the Company's operations. The term of the agreement is to January 1, 2035, or until the repayment of the Agency's bonds (described hereafter) occurs. Under the terms of the agreement, the Company is obligated to purchase approximately 20,500 acre feet of treated water per year. The Company is obligated to pay the Capital Facilities Charge and the Treated Water Charge regardless of whether it can use the water in its operation, and is obligated for these charges even if the Agency cannot produce an adequate amount to supply the 20,500 acre feet in the year. This agreement supersedes a prior agreement with Kern County Water Agency for the supply of 11,500 acre feet of water per year.

Three other parties, including the City of Bakersfield, are also obligated to purchase a total of 32,500 acre feet per year under separate agreements with the Agency. Further, the Agency has the right to proportionally reduce the water supply provided to all of the participants if it cannot produce adequate supplies. If any of the other parties does not use its allocation, that party is obligated to pay its contracted amount.

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
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**14 COMMITMENTS AND CONTINGENCIES (Continued)**

If any of the parties were to default on making payments of the Capital Facilities Charge, then the other parties are obligated to pay for the defaulting party's share on a pro-rata basis. If there is a payment default by a party and the remaining parties have to make payments, they are also entitled to a pro-rata share of the defaulting party's water allocation.

The Company expects to use all its entitled water in its operations every year. In addition, if the Company were to pay for and receive additional amounts of water due to a default of another participating party; the Company believes it could use this additional water in its operations without incurring substantial incremental cost increases. If additional treated water is available, all parties have an option to purchase this additional treated water, subject to the Agency's right to allocate the water among the parties.

The total obligation of all parties, excluding the Company, is approximately \$82.4 million to the Agency. Based on the credit worthiness of the other participants, which are government entities, it is believed to be highly unlikely that the Company would be required to assume any other parties' obligations under the contract due to their default.

The Company pays a capital facilities charge and charges related to treated water that together total \$9.1 million annually, which equates to \$441.9 dollars per acre foot. Total treated water charge for 2017 was \$3.0 million. As treated water is being delivered, the Company will also be obligated for the Company's portion of the operating costs; that portion is currently estimated to be \$64.2 dollars per acre foot. The actual amount will vary due to variations from estimates, inflation, and other changes in the cost structure. Our overall estimated cost of \$441.9 dollars per acre foot is less than the estimated cost of procuring untreated water (assuming water rights could be obtained) and then providing treatment.

*Capital Lease Obligations*

There are two capital leases; the most significant was the City of Hawthorne water system. In 2011, the Company entered into a 15-year capital lease agreement to operate the City of Hawthorne water system. The system, which is located near the Hermosa Redondo district, serves about half of Hawthorne's population. The agreement required us to make an up-front \$8.1 million lease deposit to the city that is being amortized over the lease term. Additionally, annual lease payments of \$1.0 million are made to the city and shall be increased or decreased each year on July 1, by the same percentage that the rates charged to customers served by the water system increased or decreased, exclusive of pass-through increases or decreases in the cost of water, power, and city-imposed fees, compared to the rates in effect on July 1 of the prior year, provided, that in no event will the annual lease payment be less than \$0.9 million. Under the lease the Company is responsible for all aspects of system operation and capital improvements, although title to the system and system improvements reside with the city. In exchange, the Company receives all revenue from the water system, which was \$10.0 million, \$8.5 million, and \$8.0 million in 2017, 2016, and 2015, respectively. At the end of the lease, the city is required to reimburse the Company for the unamortized value of capital improvements made during the term of the lease. The annual payments were \$1.0 million in 2017, \$1.0 million in 2016, and \$0.9 million in 2015. The capital lease asset was \$6.8 million as of December 31, 2017.

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
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**14 COMMITMENTS AND CONTINGENCIES (Continued)**

***Contingencies***

*Groundwater Contamination*

The Company has undertaken litigation against third parties to recover past and future costs related to ground water contamination in our service areas. The cost of litigation is expensed as incurred and any settlement is first offset against such costs. The CPUC's general policy requires all proceeds from contamination litigation to be used first to pay transactional expenses, then to make customers whole for water treatment costs to comply with the CPUC's water quality standards. The CPUC allows for a risk-based consideration of contamination proceeds which exceed the costs of the remediation described above and may result in some sharing of proceeds with the shareholder, determined on a case by case basis. The CPUC has authorized various memorandum accounts that allow the Company to track significant litigation costs to request recovery of these costs in future filings and uses of proceeds to comply with CPUC's general policy.

As previously reported, Cal Water has filed with the City of Bakersfield, in the Superior Court of California, a lawsuit that names potentially PRPs, who manufactured and distributed products containing 1,2,3 trichloropropane (TCP) in California. TCP has been detected in the ground water. The lawsuit seeks to recover treatment costs necessary to remove TCP. On December 20, 2017, Cal Water entered into an \$85.0 million settlement agreement and release of claims with the PRPs, in *California Water Service Company and City of Bakersfield v. The Dow Chemical Company, et al., Civil Case No. CIV-470999* (TCP Action). The TCP Action seeks damages and other relief related to the PRPs' alleged contamination of drinking water supply and water wells with the chemical TCP. The proceeds from the settlement, after payment of the legal fees, was \$56.0 million and will be used to reimburse a portion of the capital costs associated with Cal Water's remediation efforts related to such alleged TCP contamination. Under the terms of the Agreement, the PRPs are released from all claims regarding 47 of the 57 total claimed wells, and Cal Water agrees to file a dismissal with prejudice of the TCP Action. The PRPs are also released from future claims regarding TCP contamination of any other wells, unless and until Cal Water has installed granular activated carbon filtration systems or other then-approved Sate treatment technology for TCP on, or replaced, 36 wells due to TCP contamination. As of December 31, 2017, Cal Water believes the proceeds are non-taxable based upon its intent to reinvest them in qualifying assets.

*Other Legal Matters*

From time to time, the Company is involved in various disputes and litigation matters that arise in the ordinary course of business. The status of each significant matter is reviewed and assessed for potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount of the range of loss can be estimated, a liability is accrued for the estimated loss in accordance with the accounting standards for contingencies. Legal proceedings are subject to uncertainties, and the outcomes are difficult to predict. Because of such uncertainties, accruals are based on the best information available at the time. While the outcome of these disputes and litigation matters cannot be predicted with any certainty, management does not believe when taking into account existing reserves the ultimate resolution of these matters will materially affect the Company's financial position, results of operations, or cash flows. The

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
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**14 COMMITMENTS AND CONTINGENCIES (Continued)**

Company has recognized a liability of \$6.1 million for all known legal matters as of December 31, 2017 mostly due to potable water main leaks and other work related legal matters. The cost of litigation is expensed as incurred and any settlement is first offset against such costs. Any settlement in excess of the cost to litigate is accounted for on a case by case basis, dependent on the nature of the settlement.

**15 QUARTERLY FINANCIAL DATA (UNAUDITED)**

The Company's common stock is traded on the New York Stock Exchange under the symbol "CWT."

<b>2017</b>	<b>First</b>	<b>Second</b>	<b>Third</b>	<b>Fourth</b>
Operating revenue . . . . .	\$122,036	\$171,132	\$211,731	\$161,991
Net operating income . . . . .	8,050	25,259	41,196	20,118
Net income . . . . .	1,132	18,531	33,849	13,669
Diluted earnings per share . . . . .	0.02	0.39	0.70	0.29
Common stock market price range:				
High . . . . .	37.60	39.40	39.65	46.15
Low . . . . .	32.45	32.75	36.30	38.15
Dividends paid per common share . . . . .	0.1800	0.1800	0.1800	0.1800
<b>2016</b>	<b>First</b>	<b>Second</b>	<b>Third</b>	<b>Fourth</b>
Operating revenue . . . . .	\$121,727	\$152,445	\$184,268	\$150,930
Net operating income . . . . .	6,270	18,534	30,055	21,335
Net income . . . . .	(798)	11,508	22,875	15,090
Diluted earnings (loss) per share . . . . .	(0.02)	0.24	0.48	0.31
Common stock market price range:				
High . . . . .	27.33	34.95	35.62	36.85
Low . . . . .	22.48	26.22	29.93	29.25
Dividends paid per common share . . . . .	0.1725	0.1725	0.1725	0.1725

**16 SUBSEQUENT EVENT**

On February 6, 2018, the CPUC issued the proposed decision of the assigned administrative law judge, which applies to Cal Water and three other Class A water companies (the Joint Parties), in response to the Joint Parties' request to set their cost of capital for 2018, 2019, and 2020. The proposed decision would lower Cal Water's authorized return on equity from 9.43% to 8.22%. If the proposed decision were adopted without changes, Cal Water would be required to reduce its rates collected from California customers by approximately \$13.0 million, which will reduce Cal Water's 2018 net income and net cash provided by operating activities. A proposed decision must be approved by the full Commission to go into effect. The Commission could modify or reject the proposed decision and will first consider the matter at its meeting on March 22, 2018.

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**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS**

On April 17, 2009, Cal Water issued \$100.0 million aggregate principal amount of 5.875% First Mortgage Bonds due 2019, and on November 17, 2010, Cal Water issued \$100.0 million aggregate principal amount of 5.500% First Mortgage Bonds due 2040, all of which are fully and unconditionally guaranteed by the Company. As a result of these guarantee arrangements, the Company is required to present the following condensed consolidating financial information. The investments in affiliates are accounted for and presented using the “equity method” of accounting

The following tables present the condensed consolidating balance sheets as of December 31, 2017 and 2016, the condensed consolidating statements of income for the years ended December 31, 2017, 2016, and 2015, and the condensed consolidating statements of cash flows for the years ended December 31, 2017, 2016, and 2015, of (i) California Water Service Group, the guarantor of the First Mortgage Bonds and the parent company; (ii) California Water Service Company, the issuer of the First Mortgage Bonds and a 100% owned consolidated subsidiary of California Water Service Group; and (iii) the other 100% owned non-guarantor consolidated subsidiaries of California Water Service Group. No other subsidiary of the Company guarantees the securities. The condensed consolidating statement of cash flows for the years ended December 31, 2016 and 2015 reflect the retrospective adoption of ASU 2016-09 (refer to Note 2 Summary of Significant Accounting Policies for more details).

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
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**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING BALANCE SHEET**  
**As of December 31, 2017**

	<u>Parent Company</u>	<u>Cal Water</u>	<u>All Other Subsidiaries</u>	<u>Consolidating Adjustments</u>	<u>Consolidated</u>
	(In thousands)				
<b>ASSETS</b>					
<b>Utility plant:</b>					
Utility plant . . . . .	\$ 1,321	\$2,771,259	\$204,795	\$ (7,196)	\$2,970,179
Less accumulated depreciation and amortization . . . . .	(919)	(868,762)	(54,543)	2,010	(922,214)
Net utility plant . . . . .	<u>402</u>	<u>1,902,497</u>	<u>150,252</u>	<u>(5,186)</u>	<u>2,047,965</u>
<b>Current assets:</b>					
Cash and cash equivalents . . . . .	4,728	80,940	9,108	—	94,776
Receivables and unbilled revenue . . . . .	—	110,928	4,526	—	115,454
Receivables from affiliates . . . . .	19,952	4,093	43	(24,088)	—
Other current assets . . . . .	80	16,569	994	—	17,643
Total current assets . . . . .	<u>24,760</u>	<u>212,530</u>	<u>14,671</u>	<u>(24,088)</u>	<u>227,873</u>
<b>Other assets:</b>					
Regulatory assets . . . . .	—	397,333	3,814	—	401,147
Investments in affiliates . . . . .	698,690	—	—	(698,690)	—
Long-term affiliate notes receivable . . . . .	26,441	—	—	(26,441)	—
Other assets . . . . .	192	59,581	3,822	(205)	63,390
Total other assets . . . . .	<u>725,323</u>	<u>456,914</u>	<u>7,636</u>	<u>(725,336)</u>	<u>464,537</u>
<b>TOTAL ASSETS</b> . . . . .	<u>\$750,485</u>	<u>\$2,571,941</u>	<u>\$172,559</u>	<u>\$(754,610)</u>	<u>\$2,740,375</u>
<b>CAPITALIZATION AND LIABILITIES</b>					
<b>Capitalization:</b>					
Common stockholders' equity . . . . .	\$693,462	\$ 626,300	\$ 77,647	\$(703,947)	\$ 693,462
Affiliate long-term debt . . . . .	—	—	26,441	(26,441)	—
Long-term debt, less current maturities . . . . .	—	514,952	841	—	515,793
Total capitalization . . . . .	<u>693,462</u>	<u>1,141,252</u>	<u>104,929</u>	<u>(730,388)</u>	<u>1,209,255</u>
<b>Current liabilities:</b>					
Current maturities of long-term debt . . . . .	—	15,598	322	—	15,920
Short-term borrowings . . . . .	55,100	220,000	—	—	275,100
Payables to affiliates . . . . .	—	580	23,508	(24,088)	—
Accounts payable . . . . .	—	90,561	3,394	—	93,955
Accrued expenses and other liabilities . . . . .	271	104,002	1,711	—	105,984
Total current liabilities . . . . .	<u>55,371</u>	<u>430,741</u>	<u>28,935</u>	<u>(24,088)</u>	<u>490,959</u>
<b>Unamortized investment tax credits</b> . . . . .	—	1,724	—	—	1,724
<b>Deferred income taxes</b> . . . . .	1,652	189,004	2,424	(134)	192,946
<b>Pension and postretirement benefits other than pensions</b> . . . . .	—	252,141	—	—	252,141
<b>Regulatory and other long-term liabilities</b> . . . . .	—	220,779	3,348	—	224,127
<b>Advances for construction</b> . . . . .	—	181,979	523	—	182,502
<b>Contributions in aid of construction</b> . . . . .	—	154,321	32,400	—	186,721
<b>TOTAL CAPITALIZATION AND LIABILITIES</b> . . . . .	<u>\$750,485</u>	<u>\$2,571,941</u>	<u>\$172,559</u>	<u>\$(754,610)</u>	<u>\$2,740,375</u>



**CALIFORNIA WATER SERVICE GROUP**  
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**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING BALANCE SHEET**  
**As of December 31, 2016**

	<u>Parent Company</u>	<u>Cal Water</u>	<u>All Other Subsidiaries</u>	<u>Consolidating Adjustments</u>	<u>Consolidated</u>
	(In thousands)				
<b>ASSETS</b>					
<b>Utility plant:</b>					
Utility plant . . . . .	\$ 1,318	\$2,519,785	\$203,433	\$ (7,197)	\$2,717,339
Less accumulated depreciation and amortization . . . . .	(826)	(805,992)	(53,163)	1,919	(858,062)
Net utility plant . . . . .	<u>492</u>	<u>1,713,793</u>	<u>150,270</u>	<u>(5,278)</u>	<u>1,859,277</u>
<b>Current assets:</b>					
Cash and cash equivalents . . . . .	5,216	13,215	7,061	—	25,492
Receivables and unbilled revenue . . . . .	—	98,850	4,173	—	103,023
Receivables from affiliates . . . . .	19,566	3,608	8	(23,182)	—
Other current assets . . . . .	80	12,442	1,032	—	13,554
Total current assets . . . . .	<u>24,862</u>	<u>128,115</u>	<u>12,274</u>	<u>(23,182)</u>	<u>142,069</u>
<b>Other assets:</b>					
Regulatory assets . . . . .	—	352,139	3,791	—	355,930
Investments in affiliates . . . . .	666,525	—	—	(666,525)	—
Long-term affiliate notes receivable . . . . .	25,744	—	—	(25,744)	—
Other assets . . . . .	376	50,361	3,765	(33)	54,469
Total other assets . . . . .	<u>692,645</u>	<u>402,500</u>	<u>7,556</u>	<u>(692,302)</u>	<u>410,399</u>
<b>TOTAL ASSETS</b> . . . . .	<u>\$717,999</u>	<u>\$2,244,408</u>	<u>\$170,100</u>	<u>\$(720,762)</u>	<u>\$2,411,745</u>
<b>CAPITALIZATION AND LIABILITIES</b>					
<b>Capitalization:</b>					
Common stockholders' equity . . . . .	\$659,471	\$ 595,003	\$ 76,833	\$(671,836)	\$ 659,471
Affiliate long-term debt . . . . .	—	—	25,744	(25,744)	—
Long-term debt, less current maturities . . . . .	—	530,850	895	—	531,745
Total capitalization . . . . .	<u>659,471</u>	<u>1,125,853</u>	<u>103,472</u>	<u>(697,580)</u>	<u>1,191,216</u>
<b>Current liabilities:</b>					
Current maturities of long-term debt . . . . .	—	25,657	551	—	26,208
Short-term borrowings . . . . .	57,100	40,000	—	—	97,100
Payables to affiliates . . . . .	—	539	22,643	(23,182)	—
Accounts payable . . . . .	—	74,998	2,815	—	77,813
Accrued expenses and other liabilities . . . . .	88	47,232	1,789	—	49,109
Total current liabilities . . . . .	<u>57,188</u>	<u>188,426</u>	<u>27,798</u>	<u>(23,182)</u>	<u>250,230</u>
<b>Unamortized investment tax credits</b> . . . . .	—	1,798	—	—	1,798
<b>Deferred income taxes</b> . . . . .	1,340	296,781	803	—	298,924
<b>Pension and postretirement benefits other than pensions</b> . . . . .	—	222,691	—	—	222,691
<b>Regulatory and other long-term liabilities</b> . . . . .	—	80,518	3,130	—	83,648
<b>Advances for construction</b> . . . . .	—	181,907	541	—	182,448
<b>Contributions in aid of construction</b> . . . . .	—	146,434	34,356	—	180,790
<b>TOTAL CAPITALIZATION AND LIABILITIES</b> . . . . .	<u>\$717,999</u>	<u>\$2,244,408</u>	<u>\$170,100</u>	<u>\$(720,762)</u>	<u>\$2,411,745</u>

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING STATEMENT OF INCOME**  
**For the Year Ended December 31, 2017**

	<u>Parent Company</u>	<u>Cal Water</u>	<u>All Other Subsidiaries</u>	<u>Consolidating Adjustments</u>	<u>Consolidated</u>
	(In thousands)				
<b>Operating revenue</b> . . . . .	\$ —	\$626,381	\$40,509	\$ —	\$666,890
<b>Operating expenses:</b>					
Operations:					
Purchased water . . . . .	—	198,682	399	—	199,081
Purchased power . . . . .	—	21,021	7,841	—	28,862
Pump taxes . . . . .	—	13,924	—	—	13,924
Administrative and general . . . . .	—	92,195	10,719	—	102,914
Other . . . . .	—	67,069	7,903	(524)	74,448
Maintenance . . . . .	—	21,595	935	—	22,530
Depreciation and amortization . . . . .	94	72,327	4,453	(91)	76,783
Income tax (benefit) expense . . . . .	(498)	27,129	1,238	1,059	28,928
Property and other taxes . . . . .	(4)	21,778	3,023	—	24,797
<b>Total operating (income)</b>					
<b>expenses</b> . . . . .	(408)	535,720	36,511	444	572,267
<b>Net operating income</b> . . . . .	408	90,661	3,998	(444)	94,623
<b>Other income and expenses:</b>					
Non-regulated revenue . . . . .	1,985	14,608	1,814	(2,509)	15,898
Non-regulated expenses . . . . .	—	(8,139)	(1,251)	—	(9,390)
Allowance for equity funds used during construction . . . . .	—	3,750	—	—	3,750
Gain on non-utility properties . . . . .	—	663	—	—	663
Income tax expense on other income and expenses . . . . .	(809)	(4,434)	(214)	1,022	(4,435)
Net other income . . . . .	1,176	6,448	349	(1,487)	6,486
<b>Interest:</b>					
Interest expense . . . . .	1,131	35,116	2,026	(1,985)	36,288
Allowance for borrowed funds used during construction . . . . .	—	(2,319)	(41)	—	(2,360)
Net interest expense . . . . .	1,131	32,797	1,985	(1,985)	33,928
<b>Equity earnings of subsidiaries</b> . . . . .	66,728	—	—	(66,728)	—
<b>Net income</b> . . . . .	\$67,181	\$ 64,312	\$ 2,362	\$(66,674)	\$ 67,181

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING STATEMENT OF INCOME**  
**For the Year Ended December 31, 2016**

	<u>Parent Company</u>	<u>Cal Water</u>	<u>All Other Subsidiaries</u>	<u>Consolidating Adjustments</u>	<u>Consolidated</u>
	(In thousands)				
<b>Operating revenue</b> . . . . .	\$ —	\$570,514	\$38,856	\$ —	\$609,370
<b>Operating expenses:</b>					
Operations:					
Purchased water . . . . .	—	181,018	497	—	181,515
Purchased power . . . . .	—	19,791	7,389	—	27,180
Pump taxes . . . . .	—	11,298	—	—	11,298
Administrative and general . . . . .	—	88,001	10,473	—	98,474
Other . . . . .	—	73,918	6,669	(505)	80,082
Maintenance . . . . .	—	22,053	940	—	22,993
Depreciation and amortization . . . . .	220	59,138	4,337	(96)	63,599
Income tax (benefit) expense . . . . .	(398)	22,743	1,449	1,010	24,804
Property and other taxes . . . . .	—	20,331	2,900	—	23,231
<b>Total operating (income)</b>					
<b>expenses</b> . . . . .	(178)	498,291	34,654	409	533,176
<b>Net operating income</b> . . . . .	178	72,223	4,202	(409)	76,194
<b>Other Income and Expenses:</b>					
Non-regulated revenue . . . . .	1,850	15,114	2,006	(2,385)	16,585
Non-regulated expenses . . . . .	—	(10,122)	(1,323)	—	(11,445)
Gain on sale of non-utility properties . . . . .	—	(146)	—	—	(146)
Income tax expense on other income and expenses . . . . .	(754)	(1,976)	(254)	972	(2,012)
Net other income . . . . .	1,096	2,870	429	(1,413)	2,982
<b>Interest:</b>					
Interest expense . . . . .	757	32,682	1,906	(1,879)	33,466
Allowance for borrowed funds used during construction . . . . .	—	(2,905)	(60)	—	(2,965)
Net interest expense . . . . .	757	29,777	1,846	(1,879)	30,501
<b>Equity earnings of subsidiaries</b> . . . . .	48,158	—	—	(48,158)	—
<b>Net income</b> . . . . .	\$48,675	\$ 45,316	\$ 2,785	\$(48,101)	\$ 48,675

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING STATEMENT OF INCOME**  
**For the Year Ended December 31, 2015**

	<u>Parent Company</u>	<u>Cal Water</u>	<u>All Other Subsidiaries</u>	<u>Consolidating Adjustments</u>	<u>Consolidated</u>
	(In thousands)				
<b>Operating revenue</b> . . . . .	\$ —	\$552,202	\$36,166	\$ —	\$588,368
<b>Operating expenses:</b>					
Operations:					
Purchased water . . . . .	—	168,157	400	—	168,557
Purchased power . . . . .	—	20,282	7,608	—	27,890
Pump taxes . . . . .	—	11,479	—	—	11,479
Administrative and general . . .	—	101,244	11,866	—	113,110
Other . . . . .	—	61,154	6,599	(505)	67,248
Maintenance . . . . .	—	20,659	804	—	21,463
Depreciation and amortization . .	228	56,911	4,343	(101)	61,381
Income tax (benefit) expense . . .	(388)	23,964	(56)	1,008	24,528
Property and other taxes . . . . .	—	18,848	2,711	—	21,559
<b>Total operating expenses</b> . . .	<u>(160)</u>	<u>482,698</u>	<u>34,275</u>	<u>402</u>	<u>517,215</u>
<b>Net operating income</b> . . . . .	<u>160</u>	<u>69,504</u>	<u>1,891</u>	<u>(402)</u>	<u>71,153</u>
<b>Other Income and Expenses:</b>					
Non-regulated revenue . . . . .	1,787	14,460	1,699	(2,322)	15,624
Non-regulated expenses . . . . .	—	(12,870)	(1,174)	—	(14,044)
Gain on sale of non-utility properties . . . . .	—	315	—	—	315
Income tax expense on other income and expenses . . . . .	<u>(728)</u>	<u>(776)</u>	<u>(224)</u>	<u>967</u>	<u>(761)</u>
Net other income . . . . .	<u>1,059</u>	<u>1,129</u>	<u>301</u>	<u>(1,355)</u>	<u>1,134</u>
<b>Interest:</b>					
Interest expense . . . . .	718	28,450	1,834	(1,817)	29,185
Allowance for borrowed funds used during construction . . . . .	—	(1,873)	(42)	—	(1,915)
Net interest expense . . . . .	<u>718</u>	<u>26,577</u>	<u>1,792</u>	<u>(1,817)</u>	<u>27,270</u>
<b>Equity earnings of subsidiaries</b> . .	44,516	—	—	(44,516)	—
<b>Net income (loss)</b> . . . . .	<u>\$45,017</u>	<u>\$ 44,056</u>	<u>\$ 400</u>	<u>\$(44,456)</u>	<u>\$ 45,017</u>

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**  
**For the Year Ended December 31, 2017**

	<u>Parent Company</u>	<u>Cal Water</u>	<u>All Other Subsidiaries</u>	<u>Consolidating Adjustments</u>	<u>Consolidated</u>
	(In thousands)				
<b>Operating activities:</b>					
Net income	\$ 67,181	\$ 64,312	\$ 2,362	\$(66,674)	\$ 67,181
Adjustments to reconcile net income to net cash provided by operating activities:					
Equity earnings of subsidiaries	(66,728)	—	—	66,728	—
Dividends received from Affiliates	34,563	—	—	(34,563)	—
Depreciation and amortization	94	74,041	4,548	(91)	78,592
Change in value of life insurance contract	—	(3,058)	—	—	(3,058)
Stock-based compensation	3,118	—	—	—	3,118
Gain on sale of non-utility properties	—	(663)	—	—	(663)
Changes in normalized deferred income taxes	—	21,087	—	—	21,087
Allowance for equity funds used during construction	—	(3,750)	—	—	(3,750)
Changes in operating assets and liabilities	184	(36,611)	38	—	(36,389)
Other changes in noncurrent assets and liabilities	254	18,860	2,573	37	21,724
Net cash provided by operating activities	<u>38,666</u>	<u>134,218</u>	<u>9,521</u>	<u>(34,563)</u>	<u>147,842</u>
<b>Investing activities:</b>					
Utility plant expenditures	(4)	(252,055)	(7,135)	—	(259,194)
TCP settlement proceeds	—	56,004	—	—	56,004
Proceeds from sale of non-utility assets	—	666	—	—	666
Change in affiliate advances	172	(485)	(50)	363	—
Issuance of affiliate short-term borrowings	(2,610)	—	—	2,610	—
Reduction of affiliate long-term debt	1,356	—	—	(1,356)	—
Life insurance benefits	—	1,558	—	—	1,558
Purchase of life insurance	—	(5,605)	—	—	(5,605)
Change in restricted cash	—	(81)	—	—	(81)
Net cash used in investing activities	<u>(1,086)</u>	<u>(199,998)</u>	<u>(7,185)</u>	<u>1,617</u>	<u>(206,652)</u>
<b>Financing Activities:</b>					
Short-term borrowings, net of expenses	—	265,000	—	—	265,000
Repayment of short-term borrowings	(2,000)	(85,000)	—	—	(87,000)
Change in affiliate advances	—	41	322	(363)	—
Proceeds from affiliate short-term borrowings	—	—	2,610	(2,610)	—
Repayment of affiliates long-term debt	—	—	(1,356)	1,356	—
Retirement of long-term debt	—	(26,223)	(606)	—	(26,829)
Advances and contribution in aid of construction	—	21,075	294	—	21,369
Refunds of advances for construction	—	(8,373)	(5)	—	(8,378)
Repurchase of common stock	(1,505)	—	—	—	(1,505)
Dividends paid to non-affiliates	(34,563)	—	—	—	(34,563)
Dividends paid to affiliates	—	(33,015)	(1,548)	34,563	—
Net cash provided by (used in) financing activities	<u>(38,068)</u>	<u>133,505</u>	<u>(289)</u>	<u>32,946</u>	<u>128,094</u>
Change in cash and cash equivalents	(488)	67,725	2,047	—	69,284
Cash and cash equivalents at beginning of period	5,216	13,215	7,061	—	25,492
Cash and cash equivalents at end of year	<u>\$ 4,728</u>	<u>\$ 80,940</u>	<u>\$ 9,108</u>	<u>\$ —</u>	<u>\$ 94,776</u>

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**  
**For the Year Ended December 31, 2016**

	<u>Parent Company</u>	<u>Cal Water</u>	<u>All Other Subsidiaries</u>	<u>Consolidating Adjustments</u>	<u>Consolidated</u>
	(In thousands)				
<b>Operating activities:</b>					
Net income	\$ 48,675	\$ 45,316	\$ 2,785	\$(48,101)	\$ 48,675
Adjustments to reconcile net income to net cash provided by operating activities:					
Equity earnings of subsidiaries	(48,158)	—	—	48,158	—
Dividends received from affiliates	33,081	—	—	(33,081)	—
Depreciation and amortization	220	60,572	4,507	(96)	65,203
Amortization of debt premium	—	871	—	—	871
Changes in normalized deferred income taxes	—	26,818	—	—	26,818
Change in value of life insurance contracts	—	(1,026)	—	—	(1,026)
Stock-based compensation	2,849	—	—	—	2,849
(Gain) on sale of non-utility properties	—	146	—	—	146
Write-off of capital costs	—	3,221	—	—	3,221
Changes in operating assets and liabilities	(14)	6,534	261	—	6,781
Other changes in noncurrent assets and liabilities	355	4,645	1,867	39	6,906
Net cash provided by operating activities	<u>37,008</u>	<u>147,097</u>	<u>9,420</u>	<u>(33,081)</u>	<u>160,444</u>
<b>Investing activities:</b>					
Utility plant expenditures	—	(224,378)	(4,560)	—	(228,938)
Proceeds from sale of non-utility assets	—	395	—	—	395
Change in affiliate advances	291	1,111	(67)	(1,335)	—
Collection of affiliate short-term borrowings	365	42,100	—	(42,465)	—
Issuance of affiliate short-term borrowings	(2,365)	(20,600)	—	22,965	—
Collection of affiliate long-term debt	1,175	—	—	(1,175)	—
Life insurance benefits	—	495	—	—	495
Purchase of life insurance	—	(2,857)	—	—	(2,857)
Change in restricted cash	—	66	—	—	66
Net cash used in investing activities	<u>(534)</u>	<u>(203,668)</u>	<u>(4,627)</u>	<u>(22,010)</u>	<u>(230,839)</u>
<b>Financing Activities:</b>					
Short-term borrowings	44,100	101,000	—	—	145,100
Repayment of short-term borrowings	(20,615)	(61,000)	—	—	(81,615)
Change in affiliate advances	—	(128)	(1,207)	1,335	—
Proceeds from affiliate short-term borrowings	20,600	—	2,365	(22,965)	—
Repayment of affiliate short-term borrowings	(42,100)	—	(365)	42,465	—
Repayment of affiliates long-term debt	—	—	(1,175)	1,175	—
Issuance of long term debt, net of expenses	—	49,823	—	—	49,823
Advances and contribution in aid of construction	—	21,329	119	—	21,448
Refunds of advances for construction	—	(6,855)	(30)	—	(6,885)
Retirement of long-term debt	—	(6,548)	(448)	—	(6,996)
Repurchase of common stock	(744)	—	—	—	(744)
Dividends paid to non-affiliates	(33,081)	—	—	—	(33,081)
Dividends paid to affiliates	—	(32,105)	(976)	33,081	—
Net cash provided by (used in) financing activities	<u>(31,840)</u>	<u>65,516</u>	<u>(1,717)</u>	<u>55,091</u>	<u>87,050</u>
Change in cash and cash equivalents	4,634	8,945	3,076	—	16,655
Cash and cash equivalents at beginning of period	582	4,270	3,985	—	8,837
Cash and cash equivalents at end of year	<u>\$ 5,216</u>	<u>\$ 13,215</u>	<u>\$ 7,061</u>	<u>\$ —</u>	<u>\$ 25,492</u>

**CALIFORNIA WATER SERVICE GROUP**  
**Notes to Consolidated Financial Statements (Continued)**  
**December 31, 2017, 2016, and 2015**  
**Dollar amounts in thousands unless otherwise stated**

**17 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)**

**CALIFORNIA WATER SERVICE GROUP**  
**CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**  
**For the Year Ended December 31, 2015**

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
	(In thousands)				
<b>Operating activities:</b>					
Net income	\$ 45,017	\$ 44,056	\$ 400	\$(44,456)	\$ 45,017
Adjustments to reconcile net income to net cash provided by operating activities:					
Equity earnings of subsidiaries	(44,516)	—	—	44,516	—
Dividends received from affiliates	32,066	—	—	(32,066)	—
Depreciation and amortization	228	58,385	4,670	(101)	63,182
Change in value of life insurance contracts	—	218	—	—	218
Stock-based compensation	2,578	—	—	—	2,578
(Gain) on sale of non-utility properties	—	(315)	—	—	(315)
Changes in normalized deferred income taxes	—	24,393	—	—	24,393
Changes in operating assets and liabilities	(758)	(6,417)	5,392	(94)	(1,877)
Other changes in noncurrent assets and liabilities	1,774	14,807	(4,943)	135	11,773
Net cash provided by operating activities	<u>36,389</u>	<u>135,127</u>	<u>5,519</u>	<u>(32,066)</u>	<u>144,969</u>
<b>Investing activities:</b>					
Utility plant expenditures	—	(171,645)	(5,188)	—	(176,833)
Proceeds from sale of non-utility assets	—	319	—	—	319
Investment in affiliates	(1,000)	—	—	1,000	—
Issuance of affiliate short-term borrowings	(3,280)	(21,500)	—	24,780	—
Collection of affiliate short-term borrowings	3,000	—	—	(3,000)	—
Change in affiliate advances	(239)	(1,111)	115	1,235	—
Collection of affiliate long-term debt	1,007	—	—	(1,007)	—
Purchase of life insurance	—	(2,032)	—	—	(2,032)
Change in restricted cash	—	288	—	—	288
Net cash used in investing activities	<u>(512)</u>	<u>(195,681)</u>	<u>(5,073)</u>	<u>23,008</u>	<u>(178,258)</u>
<b>Financing Activities:</b>					
Short-term borrowings, net of expenses	15,101	79,202	—	—	94,303
Repayment of short-term borrowings	(43,600)	(97,400)	—	—	(141,000)
Investment from affiliates	—	—	1,000	(1,000)	—
Change in affiliate advances	—	397	838	(1,235)	—
Proceeds from affiliate short-term borrowings	21,500	—	3,280	(24,780)	—
Repayment of affiliate short-term borrowings	—	—	(3,000)	3,000	—
Repayment of affiliate long-term debt	—	—	(1,007)	1,007	—
Proceeds from long-term debt	—	99,293	50	—	99,343
Retirement of long-term debt	—	(6,528)	(475)	—	(7,003)
Advances and contributions in aid of construction	—	14,195	1,831	—	16,026
Refunds of advances for construction	—	(6,681)	(45)	—	(6,726)
Repurchase of common stock	(338)	—	—	—	(338)
Dividends paid to non-affiliates	(32,066)	—	—	—	(32,066)
Dividends paid to affiliates	—	(31,583)	(483)	32,066	—
Net cash provided by (used in) financing activities	<u>(39,403)</u>	<u>50,895</u>	<u>1,989</u>	<u>9,058</u>	<u>22,539</u>
Change in cash and cash equivalents	(3,526)	(9,659)	2,435	—	(10,750)
Cash and cash equivalents at beginning of period	4,108	13,929	1,550	—	19,587
Cash and cash equivalents at end of year	<u>\$ 582</u>	<u>\$ 4,270</u>	<u>\$ 3,985</u>	<u>\$ —</u>	<u>\$ 8,837</u>

**Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.***

None

**Item 9A. *Controls and Procedures.***

**Management’s Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure.

In designing and evaluating the disclosure controls and procedures, management, including the Chief Executive Officer and Chief Financial Officer, recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Accordingly, our disclosure controls and procedures have been designed to provide reasonable assurance of achieving their objectives.

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2017. Based on that evaluation, we concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

There was no change in our internal control over financial reporting during the quarter ended December 31, 2017, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Management’s Report on Internal Control over Financial Reporting**

Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended). Management assessed the effectiveness of our internal control over financial reporting as of December 31, 2017. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in “Internal Control—Integrated Framework (2013)”. Management has concluded that, as of December 31, 2017 our internal control over financial reporting is effective based on these criteria. Our independent registered public accounting firm, Deloitte & Touche LLP, has audited the effectiveness of our internal control over financial reporting as of December 31, 2017, as stated in their report, which is included in Item 8 and incorporated herein.

**Item 9B. *Other Information.***

None.



### PART III

#### **Item 10. Directors and Executive Officers and Corporate Governance.**

The information required by this Item as to directors of the Company and the Company's Audit Committee is contained in the sections captioned "Board Structure" and "Proposal No. 1—Election of Directors" of the 2017 Proxy Statement, and is incorporated herein by reference.

Information required by this Item regarding executive officers is included in a separate section captioned "Executive Officers of the Registrant" contained in Part I of this annual report.

We have adopted a code of ethics that applies to all of our directors, officers, and employees, including our principal executive, financial and accounting officers, or persons performing similar functions. Our Code of Ethics is posted on our corporate governance website located at <http://www.calwatergroup.com>. In addition, amendments to the Code of Ethics and any grant of a waiver from a provision of the Code of Ethics requiring disclosure under applicable SEC and NYSE rules will be disclosed at the same location as the Code of Ethics on our corporate governance website located at <http://www.calwatergroup.com>.

#### **Item 11. Executive Compensation.**

The information required by this Item is contained under the captions "Compensation Discussion and Analysis," "Report of the Organization and Compensation Committee of the Board of Directors on Executive Compensation," and "Organization and Compensation Committee Interlocks and Insider Participation" of the 2017 Proxy Statement and is incorporated herein by reference.

#### **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.**

The information required by this Item regarding security ownership of certain beneficial owners and management is contained in the section captioned "Stock Ownership of Management and Certain Beneficial Owners" of the 2017 Proxy Statement and is incorporated herein by reference.

The following table represents securities authorized to be issued under our equity compensation plan:

<u>Plan Category</u>	<u>Number of Securities to be Issued Upon Exercise of Outstanding Rights (a)</u>	<u>Weighted-Average Exercise Price of Outstanding Rights</u>	<u>Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plan (Excluding Securities Reflected in Column) (a)</u>
Equity compensation plans approved by security holders . . . . .	—	—	808,290
Equity compensation plans not approved by security holders . . . . .	—	—	—
Total . . . . .	—	\$—	808,290

**Item 13. *Certain Relationships and Related Transactions and Director Independence.***

The information required by this Item is contained in the sections captioned “Certain Related Persons Transactions” and “Board Structure” of the 2017 Proxy Statement and is incorporated herein by reference.

**Item 14. *Principal Accountant Fees and Services.***

The information required by this Item is contained in the section captioned “Report of the Audit Committee” and “Relationship with the Independent Registered Public Accounting Firm” of the 2017 Proxy Statement and is incorporated herein by reference.

**PART IV**

**Item 15. *Exhibits, Financial Statement Schedules.***

(a) As part of this Form 10-K, the following documents are being filed:

1. *Financial Statement:* See “Index to Consolidated Financial Statements” in Part II, Item 8 of this Form 10-K.
2. *Financial Statement Schedules:* No financial statement schedules are being included since the information otherwise required is included in the financial statements and the notes thereto.
3. *Exhibits:* The exhibits listed in the accompanying index to exhibits are filed or incorporated by reference.

## EXHIBIT INDEX

Unless filed with this Form 10-K, the documents listed are incorporated by reference to the filings referred to:

### **Exhibit Number**

- 3.1 Certificate of Incorporation of California Water Service Group (Exhibit 3.1 to the Quarterly Report on Form 10-Q filed August 9, 2006)
- 3.2 Certificate of Amendment to Certificate of Incorporation of California Water Service Group (Exhibit 3.1 to the Current Report on Form 8-K filed June 10, 2011)
- 3.3 Amended and Restated Bylaws of California Water Service Group, as amended on October 28, 2015 (Exhibit 3 to the Quarterly Report on Form 10-Q filed October 29, 2015)
- 4.1 Certificate of Designations regarding Series D Participating Preferred Stock, as filed with Delaware Secretary of State on September 16, 1999 (Exhibit 4.2 to Annual Report on Form 10-K for the year ended December 31, 2003)
- 4.2 Thirty-Ninth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee (Exhibit 4.1 to Current Report on Form 8-K filed April 21, 2009)
- 4.3 Fortieth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 9.86% First Mortgage Bonds due 2020, Series CC. (Exhibit 4.2 to Current Report on Form 8-K filed April 21, 2009)
- 4.4 Forty-First Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.875% First Mortgage Bonds due 2019, Series LL. (Exhibit 4.3 to Current Report on Form 8-K filed April 21, 2009)
- 4.5 Forty-Third Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 7.28% First Mortgage Bonds due 2025, Series AAA. (Exhibit 4.5 to Current Report on Form 8-K filed April 21, 2009)
- 4.6 Forty-Fourth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 6.77% First Mortgage Bonds due 2028, Series BBB. (Exhibit 4.6 to Current Report on Form 8-K filed April 21, 2009)
- 4.7 Forty-Fifth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 8.15% First Mortgage Bonds due 2030, Series CCC. (Exhibit 4.7 to Current Report on Form 8-K filed April 21, 2009)
- 4.8 Forty-Sixth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 7.13% First Mortgage Bonds due 2031, Series DDD. (Exhibit 4.8 to Current Report on Form 8-K filed April 21, 2009)

**Exhibit  
Number**

- 4.9 Forty-Seventh Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 7.11% First Mortgage Bonds due 2032, Series EEE. (Exhibit 4.9 to Current Report on Form 8-K filed April 21, 2009)
- 4.10 Forty-Eighth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.90% First Mortgage Bonds due 2017, Series FFF. (Exhibit 4.10 to Current Report on Form 8-K filed April 21, 2009)
- 4.11 Forty-Ninth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.29% First Mortgage Bonds due 2022, Series GGG. (Exhibit 4.11 to Current Report on Form 8-K filed April 21, 2009)
- 4.12 Fiftieth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.29% First Mortgage Bonds due 2022, Series HHH. (Exhibit 4.12 to Current Report on Form 8-K filed April 21, 2009)
- 4.13 Fifty-First Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.54% First Mortgage Bonds due 2023, Series III. (Exhibit 4.13 to Current Report on Form 8-K filed April 21, 2009)
- 4.14 Fifty-Second Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.44% First Mortgage Bonds due 2018, Series JJJ. (Exhibit 4.14 to Current Report on Form 8-K filed April 21, 2009)
- 4.15 Fifty-Fourth Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.48% First Mortgage Bonds due 2018, Series LLL. (Exhibit 4.16 to Current Report on Form 8-K filed April 21, 2009)
- 4.16 Fifty-Seventh Supplemental Indenture dated as of April 17, 2009, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 6.02% First Mortgage Bonds due 2031, Series OOO. (Exhibit 4.19 to Current Report on Form 8-K filed April 21, 2009)
- 4.17 Fifty-Eighth Supplemental Indenture dated as of November 22, 2010, between California Water Service Company and U.S. Bank National Association, as Trustee, covering 5.50% First Mortgage Bonds due 2040, Series PPP. (Exhibit 4.1 to Current Report on form 8-K filed November 22, 2010).
- 4.18 The Company agrees to furnish upon request to the Securities and Exchange Commission a copy of each instrument defining the rights of holders of long-term debt of the Company.

**Exhibit  
Number**

- 10.1 Water Supply Contract between Cal Water and County of Butte relating to Cal Water's Oroville District; Water Supply Contract between Cal Water and the Kern County Water Agency relating to Cal Water's Bakersfield District; Water Supply Contract between Cal Water and Stockton East Water District relating to Cal Water's Stockton District. (Exhibits 5(g), 5(h), 5(i), 5(j), Registration Statement No. 2-53678, which exhibits are incorporated by reference to Annual Report on Form 10-K for the year ended December 31, 1974)
- 10.2 Water Supply Contract between the City and County of San Francisco and wholesale customers in Alameda County, San Mateo County and Santa Clara County for a term of twenty-five years beginning on July 1, 2009 and ending on June 30, 2034. The agreement was dated June 24, 2009. (Exhibit 10.3 to Quarterly Report on Form 10-Q for the quarter ending September 30, 2009).
- 10.3 Water Supply Contract dated July 1, 2009 between the City and County of San Francisco and California Water Service Company to provide water to Bear Gulch and Bayshore service areas for a term of twenty-five years beginning July 1, 2009 and ending June 30, 2034. (Exhibit 10.4 to Quarterly Report on Form 10-Q for the quarter ending September 30, 2009).
- 10.4 Water Supply Contract dated January 27, 1981, between Cal Water and the Santa Clara Valley Water District relating to Cal Water's Los Altos District (Exhibit 10.3 to Annual Report on Form 10-K for the year ended December 31, 1992)
- 10.5 Amendments No. 3, 6 and 7 and Amendment dated June 17, 1980, to Water Supply Contract between Cal Water and the County of Butte relating to Cal Water's Oroville District. (Exhibit 10.5 to Annual Report on Form 10-K for the year ended December 31, 1992)
- 10.6 Amendment dated May 31, 1977, to Water Supply Contract between Cal Water and Stockton East Water District relating to Cal Water's Stockton District. (Exhibit 10.6 to Annual Report on Form 10-K for the year ended December 31, 1992)
- 10.7 Second Amended Contract dated September 25, 1987, among Stockton East Water District, California Water Service Company, the City of Stockton, the Lincoln Village Maintenance District, and the Colonial Heights Maintenance District Providing for the Sale of Treated Water. (Exhibit 10.7 to Annual Report on Form 10-K for the year ended December 31, 1987)
- 10.8 Water Supply Contract dated April 19, 1927, and Supplemental Agreement dated June 5, 1953, between Cal Water and Pacific Gas and Electric Company relating to Cal Water's Oroville District. (Exhibit 10.9 to Annual Report on Form 10-K for the year ended December 31, 1992)
- 10.9 Agreement between the City of Hawthorne and California Water Service Company for the 15-year lease of the City's water system. (Exhibit 10.17 to Quarterly Report on Form 10-Q for the quarter ended March 31, 1996)
- 10.10 Water Supply Agreement dated September 25, 1996, between the City of Bakersfield and California Water Service Company. (Exhibit 10.18 to Quarterly Report on Form 10-Q for the quarter ended September 30, 1996)

**Exhibit  
Number**

- 10.11 Water Supply Contract dated November 16, 1994, between California Water Service Company and Alameda County Flood Control and Water Conservation District relating to Cal Water's Livermore District (Exhibit 10.15 to Annual Report on Form 10-K for the year ended December 31, 1994)
- 10.12 California Water Service Group Directors' Retirement Plan (As amended and restated on February 22, 2006) (Exhibit 10.14 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.13 Credit Agreement dated as of March 10, 2015 among California Water Service Group and certain of its subsidiaries from time to time party thereto, as borrowers, Bank of America, N.A., as administrative agent, swing line lender and letter of credit issuer, Merrill Lynch, Pierce, Fenner & Smith incorporated, as sole lead arranger and sole bookrunner, CoBank, ACB and U.S. Bank National Association, as co-syndication agents, and Bank of China, Los Angeles Branch, as documentation agent, and the other lender parties thereto (Exhibit 10.1 to the Current Report on Form 8-K filed March 11, 2015).
- 10.14 Credit Agreement dated as of March 10, 2015 among California Water Service Company, as borrower, Bank of America, N.A., as administrative agent, swing line lender and letter of credit issuer, Merrill Lynch, Pierce, Fenner & Smith Incorporated, as sole lead arranger and sole bookrunner, CoBank, ACB and U.S. Bank National Association, as co-syndication agents, and Bank of China, Los Angeles Branch, as documentation agent, and the other lender parties thereto (Exhibit 10.2 to the Current Report on Form 8-K filed March 11, 2015).
- 10.15 Executive Severance Plan (Exhibit 10.24 to Annual Report on Form 10-K for the year ended December 31, 1998)\*
- 10.16 California Water Service Group Long-Term Incentive Plan (filed as Appendix A of the California Water Service Group proxy statement dated March 17, 2000)\*
- 10.17 California Water Service Group Deferred Compensation Plan effective January 1, 2001 (Exhibit 10.22 to Annual Report on Form 10-K for the year ended December 31, 2000)\*
- 10.18 California Water Service Company Supplemental Executive Retirement Plan effective January 1, 2001 (Exhibit 10.23 to Annual Report on Form 10-K for the year ended December 31, 2000)\*
- 10.19 Amendment No. 1 to California Water Service Company Supplemental Executive Retirement Plan effective January 1, 2001 (Exhibit 10.22 to Quarterly Report on Form 10-Q for the quarter ended September 30, 2004)\*
- 10.20 Water Supply Contract 99-73 between the City of Bakersfield and California Water Service Company, dated March 31, 1999 (Exhibit 10.25 to Quarterly Report on Form 10-Q for the quarter ended September 30, 2003)
- 10.21 Amendment No. 1 to Water Supply Contract between the City of Bakersfield and California Water Service Company, dated October 3, 2001 (Exhibit 10.26 to Quarterly Report on Form 10-Q for the quarter ended September 30, 2003)
- 10.22 Amendment No. 2 to California Water Service Company Supplemental Executive Retirement Plan effective January 1, 2001 (Exhibit 10.27 to Quarterly Report on Form 10-Q for the quarter ended September 30, 2004)\*

**Exhibit  
Number**

- 10.23 California Water Service Group Equity Incentive Plan (filed as Appendix B of the California Water Service Group proxy statement dated March 25, 2005, for its Annual Meeting of Stockholders to be held on April 27, 2005, as filed with the SEC on March 22, 2005 (File No. 1-13883))\*
- 10.24 The registrant's policy on option repricing under its Equity Incentive Plan (incorporated by reference to Item 8.01 Other Events in the registrant's Current Report on Form 8-K dated April 7, 2005)\*
- 10.25 Water Supply Contract dated September 21, 2005, between Cal Water and the Kern County Water Agency. (Exhibit 10.1 to Current Report on Form 8-K filed on September 21, 2005)
- 10.26 Separation Agreement between California Water Service Group and Richard D. Nye. (Exhibit 10 to Current Report on Form 8-K filed on December 22, 2005)\*
- 10.27 Form of Stock Appreciation Right Grant Notice under the California Water Service Group Equity Incentive Plan. (Exhibit 10.34 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.28 Form of Stock Appreciation Right Agreement under the California Water Service Group Equity Incentive Plan with Notice of Exercise. (Exhibit 10.35 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.29 Form of Restricted Stock Award Grant Notice under the California Water Service Group Equity Incentive Plan. (Exhibit 10.36 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.30 Form of Restricted Stock Award Agreement under the California Water Service Group Equity Incentive Plan with Assignment Separate From Certificate and Joint Escrow Instructions. (Exhibit 10.38 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.31 Form of Stock Option Grant Notice for outside director under the California Water Service Group Equity Incentive Plan. (Exhibit 10.39 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.32 Form of Stock Option Grant Notice under the California Water Service Group Equity Incentive Plan. (Exhibit 10.40 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.33 Form of Stock Option Agreement (Incentive Stock Option or Nonstatutory Stock Option) under the California Water Service Group Equity Incentive Plan with Notice of Exercise. (Exhibit 10.41 to the Annual Report on Form 10-K for the year ended December 31, 2005)
- 10.34 Offer Letter between the registrant and Martin A. Kropelnicki, dated February 15, 2006 (incorporated by reference to Exhibit 10.1 to Amendment No. 1 to Current Report on Form 8-K of the registrant, dated February 22, 2006)
- 10.35 Form of Indemnification Agreement to be entered between California Water Service Group and its directors and officers. (Exhibit 10.44 to the Annual Report on Form 10-K for the year ended December 31, 2006)
- 12.10 Computation of Ratios of Earnings to Fixed Charges
- 21.0 Subsidiaries of the Registrant

**Exhibit  
Number**

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- 23.1 Consent of Independent Registered Public Accounting Firm
- 31.1 Chief Executive Officer certification of financial statements pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Chief Financial Officer certification of financial statements pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.0 Chief Executive Officer and Chief Financial Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB XBRL Taxonomy Extension Label Linkbase
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase

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\* Management contract or compensatory plan or arrangement



## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized

### CALIFORNIA WATER SERVICE GROUP

By           /s/ MARTIN A. KROPELNICKI            
MARTIN A. KROPELNICKI,  
*President and Chief Executive Officer*

Date: March 1, 2018

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>          /s/ PETER C. NELSON          </u> PETER C. NELSON	Chairman, Board of Directors	Date: March 1, 2018
<u>          /s/ GREGORY E. ALIFF          </u> GREGORY E. ALIFF	Member, Board of Directors	Date: March 1, 2018
<u>          /s/ TERRY P. BAYER          </u> TERRY P. BAYER	Member, Board of Directors	Date: March 1, 2018
<u>          /s/ EDWIN A. GUILLES          </u> EDWIN A. GUILLES	Member, Board of Directors	Date: March 1, 2018
<u>          /s/ THOMAS M. KRUMMEL          </u> THOMAS M. KRUMMEL, M.D.	Member, Board of Directors	Date: March 1, 2018
<u>          /s/ RICHARD P. MAGNUSON          </u> RICHARD P. MAGNUSON	Member, Board of Directors	Date: March 1, 2018
<u>          /s/ CAROL M. POTTENGER          </u> CAROL M. POTTENGER	Member, Board of Directors	Date: March 1, 2018
<u>          /s/ LESTER A. SNOW          </u> LESTER A. SNOW	Member, Board of Directors	Date: March 1, 2018

<p>/s/ GEORGE A. VERA</p> <hr/> <p>GEORGE A. VERA</p>	<p>Member, Board of Directors</p>	<p>Date: March 1, 2018</p>
<p>/s/ MARTIN A. KROPELNICKI</p> <hr/> <p>MARTIN A. KROPELNICKI</p>	<p>President and Chief Executive Officer; Principal Executive Officer; Member, Board of Directors</p>	<p>Date: March 1, 2018</p>
<p>/s/ THOMAS F. SMEGAL III</p> <hr/> <p>THOMAS F. SMEGAL III</p>	<p>Vice President, Chief Financial Officer and Treasurer; Principal Financial Officer</p>	<p>Date: March 1, 2018</p>
<p>/s/ DAVID B. HEALEY</p> <hr/> <p>DAVID B. HEALEY</p>	<p>Vice President, Corporate Controller and Assistant Treasurer; Principal Accounting Officer</p>	<p>Date: March 1, 2018</p>

**CALIFORNIA WATER SERVICE GROUP**

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