

Use these links to rapidly review the document

[TABLE OF CONTENTS](#)

[Table of Contents](#)

**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, 2018

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 every Interactive Data File required to be submitted 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 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 the 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, a smaller reporting company or an 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 ☐
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 \$1,872 million on June 30, 2018, 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 11, 2019 was 48,067,000 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement for the California Water Service Group 2018 Annual Meeting are incorporated by reference into Part III hereof.

TABLE OF CONTENTS

	<u>Page</u>
<u>PART I</u>	
Item 1.	Business
	Forward-Looking Statements
	Overview
	Regulated Business
	Non-Regulated Activities
	Operating Segment
	Growth
	Geographical Service Areas and Number of Customer Connections at Year-end
	Rates and Regulation
	Water Supply
	Seasonal Fluctuations
	Utility Plant Construction
	Energy Reliability
	Impact of Climate Change Legislation
	Security at Company Facilities
	Quality of Water Supply
	Competition and Condemnation
	Environmental Matters
	Employees
	Executive Officers of the Registrant
Item 1A.	Risk Factors
Item 1B.	Unresolved Staff Comments
Item 2.	Properties
Item 3.	Legal Proceedings
Item 4.	Mine Safety Disclosures
<u>PART II</u>	
Item 5.	Market for Registrant's Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities
Item 6.	Selected Financial Data
Item 7.	Management's Discussion and Analysis of Financial Condition and Results of Operations
	Overview
	Critical Accounting Policies and Estimates
	Results of Operations
	Rates and Regulation
	Water Supply
	Liquidity and Capital Resources
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk
Item 8.	Financial Statements and Supplementary Data
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure
Item 9A.	Controls and Procedures
Item 9B.	Other Information

	<u>Page</u>
<u>PART III</u>	
Item 10. Directors and Executive Officers and Corporate Governance	91
Item 11. Executive Compensation	91
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	91
Item 13. Certain Relationships and Related Transactions and Director Independence	91
Item 14. Principal Accountant Fees and Services	91
<u>PART IV</u>	
Item 15. Exhibits, Financial Statement Schedules	92
Exhibit Index	92
Signatures	95

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 and other actions;
- 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;
- 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;
- the adequacy of our efforts to mitigate physical and cyber security risks and threats;
- the ability of our enterprise risk management processes to identify or address risks adequately;
- 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 and the adequacy of our emergency preparedness; and
- 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 holds non-utility property and provides non-regulated services to private companies and municipalities outside of California. 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. In some areas we provide wastewater collections and treatment services, including treatment which allows water recycling. 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, 2018, 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

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 at www.calwatergroup.com. The reports are available on our website as soon as reasonably practicable after such reports are filed with the SEC.

The content on any website referred to in this annual report is not incorporated by reference in this annual report unless expressly noted.

Regulated Business

California water operations are conducted by Cal Water, which provides service to approximately 486,900 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 94.1% of our total customer connections and of our total consolidated operating revenue.

Hawaii Water provides service to approximately 4,800 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 3.5% of our total consolidated operating revenue.

Washington Water provides domestic water service to approximately 17,600 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 3.4% of our total customer connections and approximately 1.7% of our total consolidated operating revenue.

New Mexico Water provides service to approximately 8,200 water and wastewater customer connections in the Belen, Los Lunas, Indian Hills, 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 and treat water and treat wastewater 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 of 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 \$10.1 million, \$10.0 million and \$8.5 million in 2018, 2017, and 2016, 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 April of 2018, a renewal agreement was negotiated with the City of Commerce for us to continue to lease and to operate its water system for the next 15 years. Under the agreement, the operating lease requires us to pay \$0.8 million per year in monthly installments. We have operated the City of Commerce water system since 1985 and are responsible for all operations, maintenance, water quality assurance, customer service programs, and financing capital improvements to provide a reliable supply of water that meets federal and state standards to customers served by the City of Commerce system. The City of Commerce will retain title to the system and system improvements and remain responsible for setting its customers' water rates. We bear the risks of operation and collection of amounts billed to customers. In exchange, we receive all revenue from the water system, which was \$3.0 million, \$3.4 million, and \$2.5 million in 2018, 2017, and 2016, respectively. The agreement allows us to request a rate change annually in order to recover costs.

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, 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 \$2.6 million, \$2.2 million, and \$2.1 million in 2018, 2017, and 2016, 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:

(rounded to the nearest hundred)	2018	2017
SAN FRANCISCO BAY AREA/NORTH COAST		
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)	55,800	55,700
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	19,000
Livermore	18,800	18,800
	112,500	112,400
SACRAMENTO VALLEY		
Chico (including Hamilton City)	30,100	29,700
Oroville	3,600	3,600
Marysville	3,800	3,800
Dixon	3,000	2,900
Willows	2,400	2,400
	42,900	42,400
SALINAS VALLEY		
Monterey Region (including Salinas and King City)	31,400	31,300
	31,400	31,300
SAN JOAQUIN VALLEY		
Bakersfield	71,900	71,600
Stockton	44,200	44,000
Visalia	45,300	44,700
Selma	6,500	6,400
Kern River Valley	3,900	4,000
	171,800	170,700

(rounded to the nearest hundred)

	2018	2017
LOS ANGELES AREA		
East Los Angeles	26,800	26,800
Hermosa Redondo (serving Hermosa Beach, Redondo Beach and a portion of Torrance)	27,000	26,900
Dominguez (Carson and portions of Compton, Harbor City, Long Beach, Los Angeles and Torrance)	34,200	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>128,300</u>	<u>128,100</u>
CALIFORNIA TOTAL	486,900	484,900
HAWAII	4,800	4,500
NEW MEXICO	8,200	8,100
WASHINGTON	17,600	16,800
COMPANY TOTAL	<u>517,500</u>	<u>514,300</u>

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 filed its most recent GRC application in July of 2018 requesting rate changes effective January 1, 2020.

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, authorized 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 were subject to the CPUC's earning test protocol.

The CPUC's decision also authorized 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 included \$197.3 million of water system infrastructure improvements that is be subject to the CPUC's advice letter procedure.

2018 GRC Filing

On July 2, 2018, Cal Water filed a GRC requesting new water infrastructure investments of \$828.5 million in accordance with the rate case plan for all of its regulated operating districts for the years 2019, 2020, and 2021. The CPUC will evaluate the new water infrastructure improvement investments along with operating budgets to establish water rates that reflect the actual cost of service. The required filing begins an approximately 18-month review process, with any changes in customer rates expected to become effective in 2020. Cal Water has proposed to the CPUC to increase revenues by \$50.7 million, or 7.6%, in 2020; \$31.5 million, or 4.4%, in 2021; and \$33.0 million, or 4.4%, in 2022 as compared to the last authorized revenue. More than half of Cal Water's proposed \$828.5 million of new infrastructure improvements relate to its transmission and distribution pipeline replacement program, and all are necessary to enhance reliability, augment water supply, and upgrade aging water system infrastructure. The plans also reflect Cal Water's cost-control measures to reduce operating and administrative costs. The GRC involves litigation and potential settlement among Cal Water, the California Public Advocates Office, and other interested parties.

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. On March 22, 2018, the CPUC adopted a revised decision in the cost of capital proceeding for Cal Water and three other water utilities for the years 2018, 2019, and 2020, establishing for Cal Water a 9.20% return on equity and a 5.51% cost of debt, with a capital structure of 46.60% long-term debt and 53.40% common equity, and an authorized return on rate base of 7.48%, compared with Cal Water's prior return on equity of 9.43%, cost of debt of 6.24%, and authorized return on rate base of 7.94%. The adopted capital structure did not change. The adopted returns on debt and equity reduced Cal Water's 2018 adopted revenue by approximately \$6.9 million. The CPUC also authorized continuation of the water cost of capital adjustment mechanism, which provides for an adjustment in the return on equity if the cost of long-term debt as defined by an index of utility debt rates varies from the most recent index by 100 basis points or more in 2019 and 2020.

On March 30, 2018, Cal Water submitted an advice letter that established the Cost of Capital Memorandum Account (CoC MA) to track the difference between current rates and rates based upon the new cost of capital adopted by the CPUC as if the new cost of capital had been in effect beginning January 1, 2018.

In May of 2018, Cal Water submitted an advice letter to adopt the new cost of capital and capital structure for 2018 in customer rates. The annual adopted gross revenue reduction associated with the May 2018 filing was \$6.9 million. The new rates became effective on July 1, 2018.

For the first six months of 2018, Cal Water recorded a \$2.8 million reduction to revenue with a corresponding regulatory liability due to the CoC MA.

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 memorandum account to track the impact of the TCJA on Cal Water. The TAMA will track the revenue requirement impact of the TCJA not otherwise reflected in rates from January 1, 2018 until current rates are modified to reflect all impacts of the TCJA. 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. For 2018,

the Company recorded a \$5.0 million reduction to revenue with a corresponding regulatory liability due to the changes required by the TCJA.

In May of 2018, Cal Water submitted an advice letter to adopt the new federal corporate income tax rate in customer rates. The annual adopted gross revenue reduction associated with the May 2018 filing was \$11.1 million. The new rates became effective on July 1, 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 and 2019 for those districts that passed the earnings test. In November of 2017, Cal Water requested escalation rate increases for 2018 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.

In November of 2018, Cal Water requested escalation rate increases for 2019 in all of its regulated districts. The annual adopted gross revenue associated with the November 2018 filing was \$16.2 million. The new rates became effective on January 1, 2019.

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 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.

In May and June of 2018, Cal Water submitted advice letters to request offsets for increases in purchased water costs and pump taxes in five of its regulated districts totaling \$3.8 million. The new rates became effective on July 1, 2018.

In November of 2018, Cal Water submitted advice letters to request offsets for increases in purchased water costs and pump taxes in five of its regulated districts totaling \$2.0 million. The new rates became effective on January 1, 2019.

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 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.

During the first six months of 2018, Cal Water submitted advice letters to recover \$2.1 million of annual revenue increases for rate base offsets in all of its regulated districts. The new rates became effective on July 1, 2018.

In November of 2018, Cal Water submitted advice letters to recover \$0.2 million of annual revenue increases for rate base offsets in four of its regulated districts. The new rates are expected to become effective on April 15, 2019.

WRAM/MCBA Filings

In April of 2018, Cal Water submitted an advice letter to true up the revenue under-collections in the 2017 annual WRAMs/MCBAs of its regulated districts. A net under-collection of \$50.1 million is being recovered from customers in the form of 12, 18, and greater-than-18-month surcharges. The new rates became effective April 15, 2018. This surcharge is in addition to surcharges/surcredits authorized in prior years which have not yet expired.

Drought Memorandum Account

In March of 2018, Cal Water submitted an advice letter to request recovery of 2016 and 2017 incremental drought expenses of \$3.3 million. On January 10, 2019, the Commission approved Cal Water's request for recovery of the \$3.3 million of incremental expenses; subsequently, Cal Water submitted an advice letter on January 15, 2019 to implement a surcharge to recover the incremental expenses from customers. The new rates are expected to become effective on April 15, 2019.

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.

[Table of Contents](#)

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. As of December 31, 2018, Cal Water has used \$43.9 million of the proceeds on remediation efforts related to the 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.

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 distribute water to most of Travis Air Force Base (TAFB) beginning in 2018. On May 31, 2017, Cal Water submitted an application to the CPUC seeking approval to distribute water service to most of the base and to establish rates for its service.

On December 13, 2018, the CPUC conditionally approved Cal Water's request to own and operate the TAFB water system as a regulated water utility district. Approval was conditioned upon modifying the contract between Cal Water and the Department of Defense to more clearly assert the CPUC's jurisdiction over a new Travis District. In January of 2019, Cal Water fulfilled the condition by submitting a contract amendment that was approved by the CPUC. The decision enables Cal Water to acquire the water distribution assets of TAFB from the U.S. Department of Defense and provide water utility service to the base for a term of 50 years. Subject to the terms of the contract with the Department of Defense and the CPUC decision, Cal Water will begin serving TAFB's more than 15,000 active and reserve personnel and civilians in 2019. The CPUC will regulate water rates, rules, and tariffs for the system as part of Cal Water's normal three-year rate case cycle.

Lead Service Line Memorandum Account (LSL MA)

On September 27, 2016, the Governor signed Senate Bill No. 1398 (SB 1398) which added Section 116885 to the Health and Safety Code. The new section stipulates that water systems compile an inventory of known lead service lines used in their distribution systems and identify areas that may have lead service lines used in its distribution system by July 1, 2018. After completing the inventory, the bill also requires water systems provide a timeline for replacement of those known lead service lines to the State Water Resources Control Board (SWRCB). For those that may have lead service lines, the bill requires water systems to either determine the existence or absence thereof by July 1, 2020, and provide that information to the SWRCB or provide a replacement timeline for those service lines whose lead content cannot be determined. Approval of the timeline rests with the SWRCB. Cal Water met the July 1, 2018 reporting deadline where it described 52% of its service lines were identified as not containing lead and the remaining 48% unknown. In order to meet the July 1, 2020 deadline, Cal Water needs to determine if the remaining 48% of service lines contain lead. If the absence of lead cannot be determined, plans must be made to replace the line pursuant to the requirements in SB 1398. A significant amount of field research is needed to meet the 2020 reporting deadline. To that end, in December of 2018, Cal Water submitted an advice letter that established the LSL MA, which gives Cal Water the opportunity to recover costs associated with this effort. Granted by the CPUC in January of 2019, the LSL MA will track all incremental expenses associated with studying and potentially replacing lead service lines for the benefit of Cal Water's customers.

Regulatory Activity - Other States

2017 Waikoloa (Hawaii Water) GRC Filings

In December of 2017, Hawaii Water filed GRC applications requesting an additional \$3.8 million in annual revenues for its Waikoloa Village and Resort Systems with the Hawaii Public Utilities Commission. 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. On January 1, 2019, the HPUC authorized Waikoloa Village rate increases of \$0.8 million for 2019 and \$0.1 million for 2020. On January 7, 2019, the HPUC authorized Waikoloa Resort rate increases of \$0.8 million for 2019, \$0.8 million for 2020, and \$0.1 million for 2021.

2018 Washington Water GRC Filing

On July 2, 2018, Washington Water submitted a GRC application to the Washington Utilities and Transportation Commission (UTC) to increase revenues to cover the higher costs of providing a reliable, high-quality water supply. The

application requested an increase of \$1.6 million in annual revenue, which is an increase of 13.8% over 2017 revenue. Washington Water requested recovery for numerous water system upgrades and additions that Washington Water had made since its last GRC, which include new pumping equipment, water treatment facilities, wells, water mains, and new storage. Increases in operating costs are also a factor in the proposed increase. The application reflected increases in materials, equipment, depreciation expense due to the addition of new facilities, and increases in employee wages and health care costs. The UTC authorized an annual rate increase of \$1.1 million on November 1, 2018 and the new rates became effective on December 1, 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 half 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 14.0% 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 29.1 billion gallons or 59.4% of our total annual water supply pumped from wells. Our annual groundwater extraction from unmanaged groundwater basins approximates 13.1 billion gallons or 26.6% 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 2018, 2017, and 2016 were \$14.7 million, \$13.9 million, and \$11.3 million, respectively. In 2014, the State of California enacted the Sustainable Groundwater Management Act of 2014. The law and its implementing regulations 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 February 5, 2019, the State of California snowpack water content during the 2018-2019 water year is 111% 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 128% and 133%, respectively, of long-term averages. Management believes that supply pumped from underground aquifers and purchased from wholesale suppliers will be adequate to meet customer demand during 2019 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.

On May 31, 2018, California's Governor Brown signed two bills (Assembly Bill 1668 and Senate Bill 606) into law that will establish long-term standards for water use efficiency. The bills revise and expand the existing urban water management plan requirements to include five year drought risk assessments, water shortage contingency plans, and annual water supply/demand assessments. By June 30, 2022, the California State Water Resources Control Board, in conjunction with the California Department of Water Resources, will establish long-term water use standards for indoor residential use, outdoor residential use, water losses and other uses. Cal Water will also be required to calculate and report on urban water use target by November 1, 2023 and each November 1 thereafter that compares actual urban water use to the target. Management believes that Cal Water is well-positioned to comply with all regulations required of utilities.

[Table of Contents](#)

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 2018. Other than noted below, all other districts receive 100% of their water supply from wells.

District	Water Purchased (MG)	Percentage of Total Water Production	Source of Purchased Supply
SAN FRANCISCO BAY AREA/NORTH COAST			
Bay Area Region*	6,856	99%	San Francisco Public Utilities Commission and Yolo County Flood Control & Water Conservation District
Bear Gulch	3,834	99%	San Francisco Public Utilities Commission
Los Altos	2,464	61%	Santa Clara Valley Water District
Livermore	1,815	70%	Alameda County Flood Control and Water Conservation District, Zone 7
SACRAMENTO VALLEY			
Oroville	766	95%	Pacific Gas and Electric Co. and County of Butte
SAN JOAQUIN VALLEY			
Bakersfield	10,064	49%	Kern County Water Agency and City of Bakersfield
Stockton	7,126	93%	Stockton East Water District
LOS ANGELES AREA			
East Los Angeles	1,578	34%	Central Basin Municipal Water District
Dominguez	10,232	84%	West Basin Municipal Water District and City of Torrance
City of Commerce	111	17%	Central Basin Municipal Water District
Hawthorne	924	69%	West Basin Municipal Water District
Hermosa Redondo	3,417	95%	West Basin Municipal Water District
Los Angeles County Region**	5,807	97%	West Basin Municipal Water District and Antelope Valley-East Kern Water Agency
Westlake	2,482	100%	Calleguas Municipal Water District and Oak Park Water Service
Kern River Valley	45	16%	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.

Purchases for the Los Altos, Livermore, Oroville, Redwood Valley, Stockton, and Bakersfield districts are pursuant to long-term contracts expiring on various dates after 2018. 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.

[Table of Contents](#)

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 2018 and estimated wholesaler price rates and percent changes for 2019. In 2018, several districts experienced purchased water rate increases, resulting in the filing of several purchased water offsets.

District	Effective Month	2018		Effective Month	2019	
		Unit Cost	Percent Change		Unit Cost	Percent Change
Antelope	January	\$560.00 /af	7.5 %	January	\$602.00 /af	7.5 %
Bakersfield(1)	July	\$169.00 /af	2.4 %	July	\$169.00 /af	—
Bear Gulch	July	\$4.10 /ccf	—	July	\$4.10 /ccf	—
Commerce(2)	July	\$1,150.00 /af	5.3 %	January	\$1,185.00 /af	3.0 %
Dominguez(2)	July	\$1,354.00 /af	1.7 %	January	\$1,385.00 /af	2.3 %
East Los Angeles(2)	July	\$1,150.00 /af	5.3 %	January	\$1,185.00 /af	3.0 %
Hawthorne(2)	July	\$1,354.00 /af	1.7 %	January	\$1,385.00 /af	2.3 %
Hermosa Redondo(2)	July	\$1,354.00 /af	1.7 %	January	\$1,385.00 /af	2.3 %
Livermore	January	\$2.04 /ccf	(20.0)%	January	\$2.01 /ccf	(1.5)%
Los Altos	July	\$1,289.00 /af	1.1 %	July	\$1,289.00 /af	—
Oroville(2)	April	\$178,829.04 /yr	2.2 %	April	\$178,829.04 /yr	—
Palos Verdes(2)	July	\$1,354.00 /af	1.7 %	January	\$1,385.00 /af	2.3 %
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	\$1,059,796.50 /mo	(0.7)%	April	\$1,059,796.50 /mo	—
Westlake	January	\$1,375.00 /af	5.8 %	January	\$1,423.00 /af	3.5 %

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 customers 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 and Regulation

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 U.S. 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 Customer Support Services 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 used to monitor and regulate additional potential contaminants to address public health concerns. The State of California has continued to adopt new water quality regulations which may be in addition to those adopted by the EPA. 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, 2018, we had 1,184 employees, including 51 at Washington Water, 46 at Hawaii Water, and 16 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, 2018, we had 751 union employees. In January 2015, the Company negotiated a six-year contract. Wage increases for both unions in 2015, 2016, and 2017 was 3.25%, 2.75%, and 2.75%, respectively. For 2018, 2019, and 2020, union wage changes were tied to the changes in the Consumer Price Index (CPI) for Los Angeles, Riverside, and Orange County. 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. In 2018, the applicable CPI was 3.1%. Union wages were increased 3.1% for all union employees. The applicable CPI published in October of 2018 was 3.9%. The union requested to re-open wage negotiations due to increases in the 2018 CPI index above 3.25%. The Company and both unions negotiated an agreement for the 2019 and 2020 wage increases whereby the base pay for all employees was increased by 3.4% (the CPI for the Western US) effective January 1, 2019. In addition, the agreement established three regions for pay purposes (Region 1, Region 2, and Region 3). Employees in Region 2 will receive the 3.4% increase in base pay, plus a regional differential of 0.5% added to their pay (based on the CPI for the Los Angeles area). Employees in Region 3 will receive the 3.4% increase in base pay, plus a 0.9% regional differential (based on the CPI for the San Francisco area). For 2020, we will follow this same methodology to determine the base pay increase for all union positions (i.e. Region 1), plus the applicable regional differential for Region 2 and Region 3. The current agreement with the unions is effective through 2020. Management believes that it maintains good relationships with the unions.

In 2018, Hawaii Water employees voted to unionize in the fourth quarter of 2018. The Company and union representatives are in the process of negotiating a contract.

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

Executive Officers of the Registrant

<u>Name</u>	<u>Positions and Offices with California Water Service Group</u>	<u>Age</u>
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).	52
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).	51
Paul G. Townsley (2)	Vice President of Corporate Development and Chief Regulatory Matters Officer effective January 1, 2019. Formerly Vice President of Rates and Regulatory Matters (2013-2018), 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).	61
Robert J. Kuta (2)	Vice President of Engineering and Chief Water Quality and Environmental Compliance Officer effective January 1, 2019. Formerly Vice President of Engineering (2015-2018), 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).	54
Michael B. Luu (2)	Vice President of Customer Service and Chief Information Officer since 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.	39
Timothy D. Treloar (2) (3)	Vice President of Water Quality and Chief Utility Operations Officer since 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).	61
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).	62

<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).	54
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).	62
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).	51
Gerald A. Simon (2)	Vice President, Chief Safety, Security, and Emergency Preparedness Officer effective January 1, 2019. Formerly Chief Safety and Emergency Preparedness Officer (2016-2018), 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).	64
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 Pillar Data Systems (2006-2007), Hitachi Global Storage (2005), Abbot Laboratories (1998-2004), and Symantec (1998-2001).	44
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).	50

(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.

(3) Scheduled to retire on April 1, 2019.

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 and financial condition.

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 with any gain on sales accruing to the stockholders, subject to certain conditions. If the Commissions disagree with our characterization, 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. 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, state water quality regulators, and other state regulatory authorities promulgate numerous nationally and locally 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 and regulation designed to mitigate or adapt to climate change may impact our operations.

Future legislation or regulation 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 or regulation 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 in California.

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) 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. Although we would likely seek permission to recover these costs through rate increases, we can give no assurance that the CPUC would approve rate increases to enable us to recover these additional compliance costs.

Cap and trade regulations were implemented in California in 2012 with the goal of reducing emissions to 1990 levels by the year 2020. Although we would likely seek permission to recover these costs through rate increases, we can give no assurance that the CPUC would approve rate increases to enable us to recover these additional compliance costs.

We have been 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 and availability of appropriate treatment technology;
- 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 35.2% and 35.0% of our total operating costs in 2018 and 2017, 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 2018 and 2017, purchased power expense represented 5.3% 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. 94.1% 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, physical and cyber security processes, 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 obtaining 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 \$164.3 million, or 24.3%, of our 2018 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.

Natural disasters, climate change, and other factors may change the population in our service areas.

In the event that some outside factor such as a wildfire, flood, changed climate pattern, or change in the local economy reduces or eliminates our customer base in a service area, we could face unrecoverable costs. In those circumstances the remaining customers might not be able to pay for the operating costs or capital costs of the water system. The company may not be able to recover capital costs of property which is no longer used and useful in utility service. Although we would likely seek permission to recover these costs through rate increases on remaining customers or in statewide rates, we can give no assurance that the Commissions would approve rate increases to enable us to recover these costs.

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, 2018, 751 of our 1,184 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 94.1% 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, attacks by third parties, 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 third-party attacks, including physical attacks, terrorist attacks, and cyber 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, to protect against third-party attacks, including physical attacks, terrorist attacks and cyber attacks. 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 third-party attacks 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 human resources to ensure uninterrupted service in all of the districts that we serve.

If any of these catastrophic events were to occur, we can give no assurance that our emergency preparedness plans would be adequate and that we would respond effectively, which could result in public or employee harm.

We retain certain risks not covered by our insurance policies.

We evaluate our risks and insurance coverage annually or more frequently if circumstances dictate. 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 may be at risk for litigation under the principle of inverse condemnation for activities in the normal course of business which have a damaging effect on private property

The California constitution allows compensation for a public utility taking or damaging private property, even when damage occurs through no fault of the utility and regardless of whether the damage could be foreseen. This is known as the doctrine of inverse condemnation. Based on recent legal activity in this area, Cal Water could be sued under inverse condemnation if its facilities or operations damage private property. A court finding of inverse condemnation does not obligate the CPUC to allow Cal Water to recover damage awards from customers.

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 or physical attacks.

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.

Our enterprise risk management processes may not be effective in identifying and mitigating the risks to which we are subject, or in reducing the potential for losses in connection with such risks.

Our enterprise risk management processes are designed to minimize or mitigate the risks to which we are subject, as well as any losses stemming from such risks. Although we seek to identify, measure, monitor, report, and control our exposure to such risks, and employ a broad and diversified set of risk monitoring and mitigation techniques in the process, those techniques are inherently limited in their ability to anticipate the existence or development of risks that are currently unknown and unanticipated. The ineffectiveness of our enterprise risk management processes in mitigating the impact of known risks or the emergence of previously unknown or unanticipated risks may result in our incurring losses in the future that could adversely impact our financial condition and results of operations.

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 September 13, 2018, 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 \$805.9 million was outstanding at December 31, 2018. 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, 2018, our California utility was in compliance with the covenants of the California Indenture.

Cal Water owns 596 wells and operates ten leased wells. There are 443 owned storage tanks with a capacity of 283 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 5,849 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 351 wells and manages 8 wells. There are 147 owned storage tanks and 2 managed storage tanks with a storage capacity of 7.8 million gallons. There are 405 miles of supply and distribution lines.

New Mexico Water owns 20 wells. There are 19 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 0.62 million gallons per day. There are eight life stations and 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, 2018, there were 48,065,000 common shares outstanding. There were 1,901 common stockholders of record as of February 11, 2019.

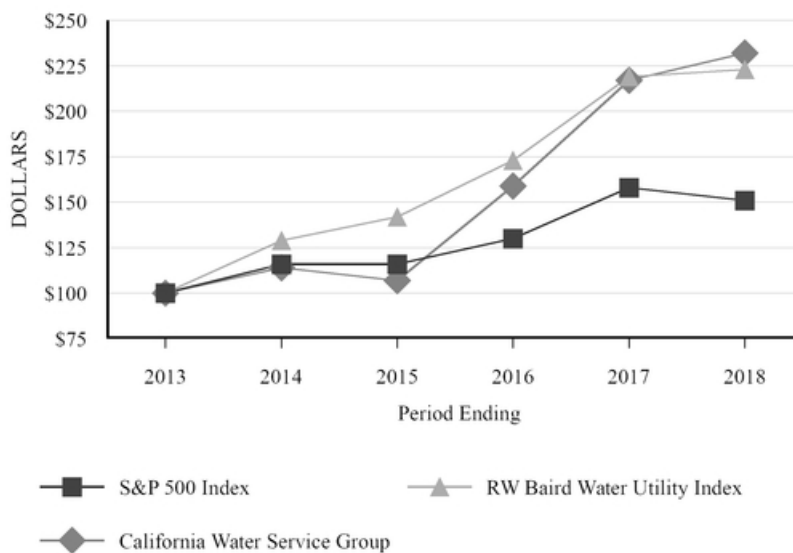
During 2018, we paid a cash dividend of \$0.7500 per common share, or \$0.1875 per quarter. During 2017, we paid a cash dividend of \$0.7200 per common share, or \$0.1800 per quarter. On January 30, 2019, our Board of Directors declared a quarterly cash dividend of \$0.1975 per common share payable on February 22, 2019, to stockholders of record on February 11, 2019. This represents an indicated annual cash dividend of \$0.7900, and is our 52nd consecutive year of increasing the annual dividend and marks the 296th 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.

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, 2018. The comparison assumes \$100 was invested on December 31, 2013, 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:

	2013	2014	2015	2016	2017	2018
California Water Service Group	100	114	107	159	217	232
S&P 500	100	116	116	130	158	151
RW Baird Water Utility Index	100	129	142	173	219	223

An initial \$100 investment in the common stock of California Water Service Group on December 31, 2013 including reinvestment of dividends would be worth \$232 at the end of the 5-year period ending December 31, 2018.

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

	2018	2017 (d)	2016	2015	2014
(Dollars in thousands, except per common share and other data)					
Summary of Operations					
Operating revenue	698,196	676,113	609,370	588,368	597,499
Total operating expenses (b)	587,656	569,030	526,734	506,803	508,631
Interest expense, other income and expenses, net (b)	44,956	34,143	33,961	36,548	32,130
Net income	\$ 65,584	\$ 72,940	\$ 48,675	\$ 45,017	\$ 56,738
Common Share Data					
Earnings per share—diluted	\$ 1.36	\$ 1.52	\$ 1.01	\$ 0.94	\$ 1.19
Dividend paid	0.7500	0.7200	0.6900	0.6700	0.6500
Dividend payout ratio	55.15%	47.37%	68.32%	71.28%	54.62%
Book value per share	\$ 15.19	\$ 14.56	\$ 13.75	\$ 13.41	\$ 13.11
Market price at year-end	47.66	45.35	33.90	23.27	24.61
Common shares outstanding at year-end (in thousands)	48,065	48,012	47,965	47,875	47,806
Return on average common stockholders' equity	9.18%	10.73%	7.50%	7.10%	9.30%
Long-term debt interest coverage	3.57	4.58	3.45	3.67	4.29
Balance Sheet Data					
Net utility plant	\$ 2,232,723	\$ 2,047,965	\$ 1,859,277	\$ 1,701,768	\$ 1,590,431
Total assets (a)	2,837,704	2,744,710	2,411,745	2,241,253	2,182,711
Long-term debt including current portion, net (a)	814,938	531,713	557,953	514,045	421,200
Capitalization ratios:					
Common stockholders' equity (a)	47.30%	56.80%	54.20%	55.50%	59.80%
Long-term debt (a)	52.70%	43.20%	45.80%	44.50%	40.20%
Other Data					
Estimated water production (million gallons)					
Wells and surface supply	54,228	53,855	50,942	51,413	61,848
Purchased	53,361	51,131	48,154	47,486	56,434
Total estimated water production	107,589	104,986	99,096	98,899	118,282
Metered customers	494,600	490,100	485,200	477,300	472,500
Flat-rate customers	22,900	24,200	26,300	31,700	33,600
Customers at year-end (c)	517,500	514,300	511,500	509,000	506,100
New customers added	3,200	2,800	2,500	2,900	3,200
Revenue per customer	\$ 1,394	\$ 1,315	\$ 1,191	\$ 1,156	\$ 1,181
Utility plant per customer	6,240	5,775	5,312	4,925	4,628
Employees at year-end	1,184	1,176	1,163	1,155	1,105

(a) The five year financial review for 2015 and 2014 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.

(b) The five year financial review for 2017, 2016, 2015, and 2014 reflect the retrospective adoption of ASU 2017-07 (see note 2). The Company adopted this guidance effective January 1, 2018.

(c) Includes customers of the City of Hawthorne and City of Commerce

(d) The 2017 as reported financial data was adjusted for an immaterial computational error that understated operating revenue, total operating expenses, net income, and earnings per share (see Note 17).

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

Overview

Correction of prior period financial data

As discussed further in Notes 15 and 17 the Company corrected an immaterial computational error that understated revenue in 2017 and the first 9 months of 2018.

In 2018 and 2017, net income was \$65.6 million and \$72.9 million, respectively. Diluted earnings per share decreased \$0.16 to \$1.36 or 10.5% from 2017 to 2018. The \$7.3 million decrease in net income was driven primarily by a \$6.9 million reduction in revenue due to the Cal Water cost of capital decision and a \$5.0 million increase in new business development expenses. In addition, increases in depreciation and amortization expense of \$7.0 million, labor costs of \$3.9 million, maintenance costs of \$2.0 million, property tax expenses of \$2.5 million, and interest expense of \$3.9 million also decreased net income. These factors were partially offset by rate increases of \$20.3 million, a California Public Utilities Commission (CPUC) authorization to recover \$3.3 million of 2016 and 2017 incremental drought program costs, and a \$16.7 million decrease in income taxes due to a decrease in pre-tax income, reduction in the federal income tax rate, and increase in tax benefits from "repairs" deductions. Also, there were other changes driven by factors outside the Company's immediate control that decreased net income, including a \$5.4 million reduction in unrealized income from certain benefit plan investments due to market conditions, a \$0.9 million reduction in unbilled revenue accrual, and a \$0.6 million decrease in gain on sale of property that was partially offset by a \$1.1 million benefit from Company-owned life insurance.

In 2017 and 2016, net income was \$72.9 million and \$48.7 million, respectively. Diluted earnings per share increased \$0.51 to \$1.52 or 50.5% from 2016 to 2017. The \$24.2 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 increases to net income were partially offset by increases in depreciation and amortization, employee wage, property tax, and net interest expenses. Net other loss decreased \$3.3 million to \$0.2 million in 2017, due primarily to the authorization of allowance for equity funds used during construction 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 from contracts with customers

The Company principally generates operating revenue from contracts with customers by providing regulated water and wastewater services at tariff-rates authorized by the Commissions in the states in which they operate and non-regulated water and wastewater services at rates authorized by contracts with government agencies. Revenue from contracts with customers reflects amounts billed for the volume of consumption at authorized per unit rates, for a service charge, and for other authorized charges.

The Company satisfies its performance obligation to provide water and wastewater services over time as services are rendered. The Company applies the invoice practical expedient and recognizes revenue from contracts with customers in the amount for which the Company has a right to invoice. The Company has a right to invoice for the volume of consumption, for the service charge, and for other authorized charges.

The measurement of sales to customers is generally based on the reading of their meters, which occurs on a systematic basis throughout the month. At the end of each month, the Company estimates consumption since the date of the last meter

reading and a corresponding unbilled revenue is recognized. The estimate is based upon the number of unbilled days that month and the average daily customer billing rate from the previous month (which fluctuates based upon customer usage).

Contract terms are generally short-term and at will by customers and, as a result, no separate financing component is recognized for the Company's collections from customers, which generally require payment within 30 days of billing. The Company applies judgment, based principally on historical payment experience, in estimating its customers' ability to pay.

Certain customers are not billed for volumetric consumption, but are instead billed a flat rate at the beginning of each monthly service period. The amount billed is initially deferred and subsequently recognized over the monthly service period, as the performance obligation is satisfied. The deferred revenue balance, which is included in "other accrued liabilities" on the consolidated balance sheets, is inconsequential.

Regulatory balancing account revenue

The Company's ability to recover revenue requirements authorized by the California Public Utilities Commission (CPUC) in its triennial General Rate Case (GRC), is decoupled from the volume of the sales. Regulatory balancing account revenue is revenue related to rate mechanisms authorized in California by the CPUC, which allow the Company to recover the authorized revenue and are not considered contracts with customers.

The Water Revenue Adjustment Mechanism (WRAM) allows the Company to recognize the adopted level of volumetric revenues. The variance between adopted volumetric revenues and actual billed volumetric revenues for metered accounts is recorded as regulatory balancing account revenue.

Cost-recovery rates, such as the Modified Cost Balancing Account (MCBA), provide for recovery of the adopted levels of expenses for purchased water, purchased power, pump taxes, water conservation programs, pension, and health care. Variances between adopted and actual costs are recorded as regulatory balancing account revenue.

Each district's WRAM and MCBA regulatory assets and liabilities are allowed to be netted against one another. The Company recognizes regulatory balancing account revenues that have been authorized for rate recovery, are objectively determinable and probable of recovery, and are expected to be collected within 24 months. To the extent that regulatory balancing account revenue is estimated to be collectible beyond 24 months, recognition is deferred.

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, 2018 and December 31, 2017.

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 \$107.0 million as of December 31, 2018. The TCJA lowered ratepayers' rates in 2018 due to lower income tax expense recoveries and resulted in the quantification of excess deferred income tax balances collected from ratepayers. The 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 for excess deferred income taxes collected from ratepayers in prior years that complies with the 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, 2018, to changes in actuarial assumptions:

	Increase/(Decrease) in Pension Benefits Actuarial Assumption	Increase/(Decrease) in 2018 Net Periodic Benefit Cost	Increase/(Decrease) in Projected Benefit Obligation as of December 31, 2018
Discount rate	(0.5)%	\$ 8,187	\$ 63,151
Long-term rate of return on plan assets	(0.5)%	2,131	—
Rate of compensation increases	(0.5)%	(3,449)	(16,446)
Cost of living adjustment	(0.5)%	(6,242)	(38,829)
Discount rate	0.5 %	(7,169)	(55,098)
Long-term rate of return on plan assets	0.5 %	(2,130)	—
Rate of compensation increases	0.5 %	3,733	17,635
Cost of living adjustment	0.5 %	6,742	41,859

Results of Operations

Operating Revenue

Operating revenue in 2018 was \$698.2 million, an increase of \$22.1 million, or 3.3%, over 2017. Operating revenue in 2017 was \$676.1 million, an increase of \$66.7 million, or 11.0%, over 2016. The sources of changes in operating revenue were:

	2018	2017
	Dollars in millions	
Net change in WRAM, service charges, usage, and other (1)	\$ 9.3	\$ 65.0
MCBA revenue (2)	3.5	1.2
Other balancing account revenue (3)	3.1	2.7
Deferral of revenue (4)	6.2	(2.2)
Net change	\$ 22.1	\$ 66.7

- (1) In 2018, the operating revenue increase is due to rate increases, which increase WRAM and service charges (see table in Rates and Regulation section below). In 2017, the operating revenue increase is due to rate increases, which increase WRAM and service charges (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.
- (2) The MCBA revenue increase in 2018 resulted from an increase in actual water production costs relative to adopted water production costs in 2018 as compared to 2017. 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. 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 2018, the increase in other balancing account revenue was due to an increase in actual pension and health care expenses relative to adopted in 2018, which were partially offset by a decrease in actual conservation expenses relative to adopted in 2018. In 2017, the increase in other balancing account revenue was due to by an increase in actual pension expenses relative to adopted in 2017, which was partially offset by a decrease in actual health care and conservation expenses relative to adopted in 2017.
- (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 2018, the deferral decreased as compared to 2017 due to a decrease in the balancing account revenue expected to be collected beyond 24 months. In 2017, the deferral increased as compared to 2016 due to an increase in the balancing account revenue expected to be collected beyond 24 months.

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 43.0% and 42.5%, of total operating costs in 2018 and 2017, 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:

	2018			2017		
	Amount	Change	% Change	Amount	Change	% Change
	Dollars in millions					
Purchased water	\$ 207.1	\$ 8.0	4.0%	\$ 199.1	\$ 17.6	9.7%
Purchased power	31.1	2.2	7.6%	28.9	1.7	6.2%
Pump taxes	14.7	0.8	5.8%	13.9	2.6	23.2%
Total water production expenses	\$ 252.9	\$ 11.0	4.5%	\$ 241.9	\$ 21.9	9.9%

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:

	2018			2017			2016		
	MG	% of Total	% change from prior year	MG	% of Total	% change from prior year	MG	% of Total	% change from prior year
Millions of gallons (MG)									
Source:									
Wells	49,340	45.9%	1.3 %	48,729	46.4%	5.4%	46,239	46.6%	(4.1) %
Purchased	53,361	49.6%	4.4 %	51,131	48.7%	6.2%	48,154	48.6%	1.4 %
Surface	4,888	4.5%	(4.6) %	5,126	4.9%	9.0%	4,703	4.8%	46.4 %
Total	107,589	100.0%	2.5 %	104,986	100.0%	5.9%	99,096	100%	0.2 %

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 2018, the \$8.0 million increase in purchased water expenses is due to a 4.4% increase in purchased quantities.

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.

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 2018, purchased power expenses increased \$2.2 million, or 7.7%, mainly due to 2.5% increase in water production. In 2017, purchased power expenses increased \$1.7 million, or 6.2%, mainly due to 5.4% increase in well water production.

Changes in climate change regulations could increase the cost of power 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 2018, administrative and general expenses increased \$7.5 million or 8.0%, as compared to 2017. The increase was mostly due to increases in employee pension costs of \$3.5 million, employee and retiree medical expenses of \$ 2.7 million, employee wage increases of \$0.8 million, consulting and outside service cost increases of \$2.6 million. These costs increases were partially offset by CPUC authorization to recover \$2.6 million of 2016 and 2017 drought program costs. 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 2017, administrative and general expenses increased \$5.7 million or 6.5%, 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.

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 2018, other operations expenses increased \$5.4 million, or 7.3%, compared to 2017. The increase was mostly due to increases in costs associated with the deferral of operating revenue of \$4.9 million, employee wage increases of \$2.0 million, district office maintenance and landscaping expense increases of \$0.7 million, and bacterial lab cost increases of \$0.6 million. These costs increases were partially offset by a decrease in conservation program expenses of \$2.2 million and CPUC authorization to recover \$0.7 million of 2016 and 2017 drought program costs. 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 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.

Maintenance

Maintenance expenses increased \$2.0 million, or 8.7%, in 2018, compared to 2017 due to increased costs for repairs of transmission and distribution mains and services.

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.

Depreciation and Amortization

Depreciation and amortization increased \$7.0 million in 2018, or 9.1%, mostly due to capital additions.

Depreciation and amortization increased \$13.2 million in 2017, or 20.7%, mostly due to 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.

Income Taxes

For 2018, income taxes decreased \$16.7 million, or 47.3%, to \$18.6 million as compared to 2017. The decrease was mostly due to a reduction in pre-tax income, a decrease in federal income tax rate from 35 percent to 21 percent beginning on January 1, 2018, and an increase in the tax benefit from the flow through method of accounting for repairs deductions on state corporate income tax filings. The Company's effective combined income tax rate for 2018 is 19.5 percent.

For 2017, income taxes increased \$6.1 million, or 20.7%, 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.

Property and Other Taxes

For 2018, property and other taxes increased \$2.5 million, or 10.1%, as compared to 2017. The increase was due to an increase in our assessed property values for utility plant placed in service during the year and a decrease in federal income tax rate from 35 percent to 21 percent.

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.

Other Income and Expenses

In 2018, net other loss increased \$6.9 million to a net loss of \$7.1 million as compared to a net loss of \$0.2 million in 2017. The increase was due primarily to a \$5.0 million increase in new business development expenses and a \$5.4 million reduction in unrealized income from certain benefit plan investments due to market conditions.

[Table of Contents](#)

In 2017, net other loss decreased \$3.3 million, or 93.8%, as compared to 2016. The decrease 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.

Interest Expenses

In 2018, net interest expense increased \$3.9 million as compared to 2017. The increase relates to an increase in average daily borrowings on the unsecured revolving credit facilities, which were used to fund capital expenditures and general corporate purposes.

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.

Rates and Regulation

The following is a summary of 2018 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.

Type of Filing	Decision/Resolution	Approval Date	Increase (Decrease) Annual Revenue	CA District/ Subsidiary
GRC and Offset Filings				
2018 Expense Offset	AL 2276-2280	Jan 2018	\$2.2 million	5 Districts
2018 Rate Base Offset	AL 2284	Jan 2018	\$1.4 million	1 District
2018 Escalation rate increases	AL 2286-2287	Jan 2018	\$15.9 million	All Districts
2018 Rate Base Offset	AL 2296-2299, 2306	July 2018	\$2.1 million	All Districts
2018 Expense Offset	AL 2205, 2207-2309, 2313	July 2018	\$6.0 million	5 Districts
Cost of capital	AL 2310	July 2018	(\$6.9 million)	All Districts
Tax cuts jobs act	AL 2310	July 2018	(\$11.1 million)	All Districts
Washington Water GRC		Dec 2018	\$1.1 million	Washington Water

The estimated impact of current and prior year rate changes on operating revenues compared to prior years is listed in the following table:

	2018	2017	2016
	Dollars in millions		
General Rate Case (GRC) (a)	\$ 4.9	\$ 44.2	\$ 2.2
Escalation rate increases (b)	15.4	—	4.9
Offset (purchased water/pump taxes) (c)	5.8	10.7	23.6
Tax Cut Jobs Act (d)	(10.7)	—	—
Cost of capital (d)	(6.3)	—	—
Total rate increases	\$ 9.1	\$ 54.9	\$ 30.7

- (a) Includes rate changes for the Cal Water 2015 GRC decision in 2017, rate base offsets in 2018, 2017 and 2016, Hawaii Water GRC decisions in 2018, 2017, and 2016 and Washington Water GRC decision in 2018.
- (b) Includes rate changes for escalation rate increases in 2018 and 2016.
- (c) Includes purchased water and pump tax offsets for 2018, 2017 and 2016.
- (d) Customer rates were reduced beginning July 1, 2018 for the Tax Cuts Jobs Act and Cost of Capital decision in California. Includes revenue reduction recorded as regulatory liability for the first six months 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.

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 2019 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 2018, we generated cash flow from operations of \$179.0 million, compared to \$147.8 million during 2017. The increase in 2018 was mostly due to an increase in customer usage and an increase in customer billing rates.

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.

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 2018, 2017, and 2016, we used \$271.7 million, \$259.2 million and \$228.9 million, respectively, of cash for capital expenditures, both Company-funded and developer-funded. The 2018 capital expenditures exceeded the high end of the budgeted capital expenditures of \$260.0 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 received \$56.0 million in TCP settlement proceeds and applied \$35.2 million to capital investment TCP remediation projects as of December 31, 2018.

Financing Activities

During 2018, we borrowed \$151.0 million, and paid down \$361.0 million on our unsecured revolving credit facilities to fund capital expenditures and general corporate purposes. We also added \$18.6 million of advances and contributions in aid of construction, which was reduced by refunds to developers of \$7.3 million. We issued \$300.0 million of floating rate First Mortgage Bonds on September 13, 2018 in a private placement and used the net proceeds to pay down Cal Water's unsecured revolving credit facility and for general corporate purposes. We also repaid \$15.6 million of First Mortgage Bonds that matured in 2018.

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.

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 \$56.1 million, \$69.1 million, and \$37.1 million as of December 31, 2018, 2017, and 2016, respectively. The decrease of \$13.0 million as of December 31, 2018 compared to the prior year was mostly due to the triggering of the SRM which allowed the Company to favorably adjust its adopted sales forecast for 2018. The increase of \$32.0 million as of December 31, 2017 compared to the prior year was mostly due to actual customer usage being lower than adopted. 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 \$16.5 million during 2018, \$26.8 million during 2017, and \$7.0 million during 2016. In addition, Cal Water has \$100.0 million of First Mortgage Bonds maturing during the second quarter of 2019, which is expected to be repaid using Cal Water's line of credit until long-term financing can be arranged.

At the January 2019 meeting, the Board of Directors declared the quarterly dividend, increasing it for the 52nd consecutive year. The quarterly dividend was raised from \$0.1875 to \$0.1975 per common share, or an annual rate of \$0.7900 per common share. Dividends have been paid for 73 consecutive years. The annual dividends paid per common share in 2018, 2017, and 2016 were \$0.7500, \$0.7200, and \$0.6900, respectively. Earnings not paid as dividends are reinvested in the business for the benefit of stockholders. The dividend payout ratio was 55.2% in 2018, 47.4% in 2017 and 68.3% in 2016 for an average of 56.9% 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, 2018, there were short-term borrowings

of \$65.1 million outstanding on our unsecured revolving line of credit, compared to \$275.1 million outstanding on our unsecured revolving line of credit as of December 31, 2017. 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.

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, 2018, our consolidated total capitalization ratio was 57.2% (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 2018. Management does not expect this restriction to have a material impact on the Company's ability to meet its cash obligations in 2019 and beyond.

On September 13, 2018, Cal Water sold \$300.0 million of First Mortgage Bonds in a private placement and used the net proceeds to pay down Cal Water's unsecured revolving credit facility and for general corporate purposes. The Company made principal payments on First Mortgage Bonds and other long-term debt of \$16.5 million during 2018 and \$26.8 million during 2017. 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, 2018.

	Total	Less than 1 Year	1 - 3 Years	3 - 5 Years	After 5 Years
	(In thousands)				
Long-term debt (a)	\$ 812,552	\$ 105,243	\$ 326,689	\$ 6,208	\$ 374,412
Interest payments	355,922	36,138	43,102	40,415	236,267
Advances for construction	186,342	7,896	15,346	15,293	147,807
Pension and postretirement benefits (b)	263,732	17,461	40,336	48,547	157,388
Capital lease obligations (c)	9,374	1,477	2,340	2,340	3,217
Facility leases	6,078	926	1,504	926	2,722
System lease	12,041	845	1,690	1,690	7,816
Water supply contracts (d)	675,935	31,082	62,166	62,169	520,518
TOTAL	\$ 2,321,976	\$ 201,068	\$ 493,173	\$ 177,588	\$ 1,450,147

- (a) Excludes capital lease obligations as reported below. Also, excludes unamortized debt issuance costs of \$3.8 million.
- (b) Pension and postretirement benefits include \$1.9 million of short-term pension obligations.
- (c) Capital lease obligations represent total cash payments to be made in the future and include interest expense of \$1.5 million.
- (d) Estimated annual contractual obligations are based on the same payment levels as 2018.

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 \$271.7 million, \$259.2 million, and \$228.9 million in 2018, 2017, and 2016, respectively. A majority of capital expenditures was associated with mains and water treatment equipment.

For 2019, the Company's capital program will be dependent in part on the timing and nature of regulatory approvals in connection with Cal Water's 2018 GRC filing. The Company proposed to the CPUC spending \$828.5 million on new projects in 2019-2021. 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 2019. 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 \$730.2 million at December 31, 2018, compared to \$699.2 million at December 31, 2017. In 2018, Cal Water issued \$300.0 million of floating rate First Mortgage Bonds in a private placement and repaid \$15.6 million for First Mortgage Bonds that matured in 2018. The Company did not sell shares of its common stock in 2018.

Total capitalization, including the current portion of long-term debt, was \$1,545.1 million at December 31, 2018 and \$1,230.9 million at December 31, 2017. 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:

	2018	2017
Common equity	47.3 %	56.8 %
Long-term debt	52.7 %	43.2 %

The return (from both regulated and non-regulated operations) on average common equity was 9.18% in 2018 compared to 10.74% in 2017. 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 \$199.1 million at December 31, 2018 and \$167.2 million at December 31, 2017.

Acquisitions

In 2018, 2017, and 2016 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 were no significant sales in 2018, a pre-tax gain of \$0.6 million in 2017, and a pre-tax loss of \$0.1 million in 2016. 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 \$104.9 million of the \$814.9 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, 2018 and 2017, the related consolidated statements of income, common stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2018, 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, 2018, 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, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2018, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, because of the effect of the material weakness identified below on the achievement of the objectives of the control criteria, the Company has not maintained effective internal control over financial reporting as of December 31, 2018, 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 Annual 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.

Material Weakness

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. The following material weakness has been identified by management and included in management's assessment: The Company did not design and maintain effective internal controls over its accounting for regulatory assets and liabilities, specifically controls over the accuracy and completeness of the pension balancing and healthcare balancing accounts as they relate to the amounts authorized in the 2015 General Rate Case. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the consolidated financial statements as of and for the year ended December 31, 2018, of the Company, and this report does not affect our report on such financial statements.

/s/ DELOITTE & TOUCHE LLP

San Francisco, California
February 28, 2019

We have served as the Company's auditor since 2008.

CALIFORNIA WATER SERVICE GROUP

Consolidated Balance Sheets

	December 31,	
	2018	2017
	(In thousands, except per share data)	
ASSETS		
Utility plant:		
Land	\$ 44,019	\$ 42,517
Depreciable plant and equipment	2,950,424	2,729,757
Construction work in progress	210,260	175,693
Intangible assets	24,743	22,212
Total utility plant	3,229,446	2,970,179
Less accumulated depreciation and amortization	(996,723)	(922,214)
Net utility plant	2,232,723	2,047,965
Current assets:		
Cash and cash equivalents	47,176	94,776
Receivables: net of allowance for doubtful accounts of \$757 and \$773 in 2018 and 2017, respectively		
Customers	30,037	32,451
Regulatory balancing accounts	42,394	36,783
Other	17,101	16,464
Unbilled revenue	33,427	29,756
Materials and supplies at weighted average cost	6,586	6,463
Taxes, prepaid expenses, and other assets	11,981	11,180
Total current assets	188,702	227,873
Other assets:		
Regulatory assets	353,569	405,482
Goodwill	2,615	2,615
Other	60,095	60,775
Total other assets	416,279	468,872
TOTAL ASSETS	\$ 2,837,704	\$ 2,744,710
CAPITALIZATION AND LIABILITIES		
Capitalization:		
Common stock, \$0.01 par value; 68,000 shares authorized, 48,065 and 48,012 outstanding in 2018 and 2017, respectively	\$ 481	\$ 480
Additional paid-in capital	337,623	336,229
Retained earnings	392,053	362,512
Total common stockholders' equity	730,157	699,221
Long-term debt, net	710,027	515,793
Total capitalization	1,440,184	1,215,014
Current liabilities:		
Current maturities of long-term debt, net	104,911	15,920
Short-term borrowings	65,100	275,100
Accounts payable	95,580	93,955
Regulatory balancing accounts	12,213	59,303
Accrued other taxes	4,182	3,888
Accrued interest	5,674	6,122
Other accrued liabilities	33,506	36,671
Total current liabilities	321,166	490,959
Unamortized investment tax credits	1,649	1,724
Deferred income taxes	213,033	194,617
Regulatory liabilities	211,275	176,611
Pension and postretirement benefits other than pensions	193,538	252,141
Advances for construction	186,342	182,502
Contributions in aid of construction	225,270	186,721
Other long-term liabilities	45,247	44,421
Commitments and contingencies		
TOTAL CAPITALIZATION AND LIABILITIES	\$ 2,837,704	\$ 2,744,710

See accompanying Notes to Consolidated Financial Statements.

CALIFORNIA WATER SERVICE GROUP

Consolidated Statements of Income

	For the Years Ended December 31,		
	2018	2017	2016
	(In thousands, except per share data)		
Operating revenue	\$ 698,196	\$ 676,113	\$ 609,370
Operating expenses:			
Operations:			
Purchased water	207,103	199,081	181,515
Purchased power	31,080	28,862	27,180
Pump taxes	14,664	13,924	11,298
Administrative and general	100,781	93,326	87,601
Other operations	79,868	74,448	80,082
Maintenance	24,494	22,530	22,993
Depreciation and amortization	83,781	76,783	63,599
Income taxes	18,589	35,279	29,235
Property and other taxes	27,296	24,797	23,231
Total operating expenses	587,656	569,030	526,734
Net operating income	110,540	107,083	82,636
Other income and expenses:			
Non-regulated revenue	18,272	15,898	16,585
Non-regulated expenses	(22,787)	(9,390)	(11,445)
Other components of net periodic benefit cost	(9,308)	(9,588)	(10,873)
Allowance for equity funds used during construction	3,954	3,750	—
Gain (loss) on sale of non-utility property	50	663	(146)
Income tax benefit (expense) on other income and expenses	2,717	(1,548)	2,419
Net other loss	(7,102)	(215)	(3,460)
Interest expense:			
Interest expense	39,917	36,288	33,466
Allowance for borrowed funds used during construction	(2,063)	(2,360)	(2,965)
Net interest expense	37,854	33,928	30,501
Net income	\$ 65,584	\$ 72,940	\$ 48,675
Earnings per share:			
Basic	\$ 1.36	\$ 1.52	\$ 1.02
Diluted	\$ 1.36	\$ 1.52	\$ 1.01
Weighted average number of common shares outstanding:			
Basic	48,060	48,009	47,953
Diluted	48,060	48,009	47,956

See accompanying Notes to Consolidated Financial Statements.

CALIFORNIA WATER SERVICE GROUP

Consolidated Statements of Common Stockholders' Equity

For the Years Ended December 31, 2018, 2017 and 2016

	Common Stock		Additional Paid-in Capital	Retained Earnings	Total Stockholders' Equity
	Shares	Amount			
	(In thousands)				
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				72,940	72,940
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	48,012	480	336,229	362,512	699,221
Net income				65,584	65,584
Issuance of common stock	53	1	1,394		1,395
Dividends paid on common stock (\$0.750 per share)				(36,043)	(36,043)
Balance at December 31, 2018	48,065	\$ 481	\$ 337,623	\$ 392,053	\$ 730,157

See accompanying Notes to Consolidated Financial Statements.

CALIFORNIA WATER SERVICE GROUP

Consolidated Statements of Cash Flows

	For the Years Ended December 31,		
	2018	2017	2016
	(In thousands)		
Operating activities:			
Net income	\$ 65,584	\$ 72,940	\$ 48,675
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	85,707	78,592	65,203
Amortization of debt premium and expenses	1,099	920	871
Changes in normalized deferred income taxes	20,909	21,087	26,818
Change in value of life insurance contracts	2,334	(3,058)	(1,026)
Allowance for equity funds used during construction	(3,954)	(3,750)	—
Stock-based compensation	3,141	3,118	2,849
(Gain) loss on sale of non-utility property	(50)	(663)	146
Write-off of capital costs	410	1,293	3,221
Changes in operating assets and liabilities:			
Receivables	20,422	(31,871)	(343)
Unbilled revenue	(3,671)	(4,528)	(2,047)
Taxes, prepaid expenses, and other assets	(587)	(3,718)	1,276
Accounts payable	4,701	1,564	3,839
Other current liabilities	(4,382)	2,164	4,056
Other changes in noncurrent assets and liabilities	(12,644)	13,752	6,906
Net cash provided by operating activities	179,019	147,842	160,444
Investing activities:			
Utility plant expenditures	(271,707)	(259,194)	(228,938)
Proceeds from sale of non-utility assets	59	666	395
TCP settlement proceeds	—	56,004	—
Life insurance benefits	3,491	1,558	495
Purchase of life insurance	(4,925)	(5,605)	(2,857)
Net cash used in investing activities	(273,082)	(206,571)	(230,905)
Financing activities:			
Short-term borrowings	151,000	265,000	145,100
Repayment of short-term borrowings	(361,000)	(87,000)	(81,615)
Issuance of long-term debt, net of expenses of \$617 for 2018, \$0 for 2017, \$177 for 2016	299,383	—	49,823
Advances and contributions in aid of construction	18,612	21,369	21,448
Refunds of advances for construction	(7,297)	(8,378)	(6,885)
Retirement of long-term debt	(16,532)	(26,829)	(6,996)
Repurchase of common stock	(1,645)	(1,505)	(744)
Dividends paid	(36,043)	(34,563)	(33,081)
Net cash provided by financing activities	46,478	128,094	87,050
Change in cash, cash equivalents, and restricted cash	(47,585)	69,365	16,589
Cash, cash equivalents, and restricted cash at beginning of year	95,300	25,935	9,346
Cash, cash equivalents, and restricted cash at end of year	\$ 47,715	\$ 95,300	\$ 25,935
Supplemental disclosures of cash flow information:			
Cash paid (received) during the year for:			
Interest (net of amounts capitalized)	\$ 35,941	\$ 32,223	\$ 28,038
Income tax refunds	—	(1,697)	—
Supplemental disclosure of investing and financing non-cash activities:			
Accrued payables for investments in utility plant	38,807	41,017	27,150
Utility plant contributed by developers	20,609	19,898	16,824
Litigation proceeds for contamination reclassified from liabilities to depreciable plant and equipment	32,315	2,420	484

See accompanying Notes to Consolidated Financial Statements.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements
December 31, 2018, 2017, and 2016
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

Operating Revenue

The following table disaggregates the Company's operating revenue by source for the years ended December 31, 2018, 2017, and 2016:

	2018	2017	2016
Revenue from contracts with customers	\$ 674,736	\$ 622,474	\$ 589,528
Regulatory balancing account revenue	23,460	53,639	19,842
Total operating revenue	<u>\$ 698,196</u>	<u>\$ 676,113</u>	<u>\$ 609,370</u>

Revenue from contracts with customers

The Company principally generates operating revenue from contracts with customers by providing regulated water and wastewater services at tariff-rates authorized by the Commissions in the states in which they operate and non-regulated water and wastewater services at rates authorized by contracts with government agencies. Revenue from contracts with customers reflects amounts billed for the volume of consumption at authorized per unit rates, for a service charge, and for other authorized charges.

The Company satisfies its performance obligation to provide water and wastewater services over time as services are rendered. The Company applies the invoice practical expedient and recognizes revenue from contracts with customers in the amount for which the Company has a right to invoice. The Company has a right to invoice for the volume of consumption, for the service charge, and for other authorized charges.

The measurement of sales to customers is generally based on the reading of their meters, which occurs on a systematic basis throughout the month. At the end of each month, the Company estimates consumption since the date of the last meter reading and a corresponding unbilled revenue is recognized. The estimate is based upon the number of unbilled days that month and the average daily customer billing rate from the previous month (which fluctuates based upon customer usage).

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Contract terms are generally short-term and at will by customers and, as a result, no separate financing component is recognized for the Company's collections from customers, which generally require payment within 30 days of billing. The Company applies judgment, based principally on historical payment experience, in estimating its customers' ability to pay.

Certain customers are not billed for volumetric consumption, but are instead billed a flat rate at the beginning of each monthly service period. The amount billed is initially deferred and subsequently recognized over the monthly service period, as the performance obligation is satisfied. The deferred revenue balance, which is included in "other accrued liabilities" on the consolidated balance sheets, is inconsequential.

In the following table, revenue from contracts with customers is disaggregated by class of customers for the years ended December 31, 2018, 2017, and 2016:

	2018	2017	2016
Residential	\$ 450,062	\$ 415,893	\$ 394,438
Business	130,041	118,279	117,510
Industrial	34,236	28,905	26,330
Public authorities	34,511	31,671	29,220
Other	25,886	27,726	22,030
Total revenue from contracts with customers	\$ 674,736	\$ 622,474	\$ 589,528

Regulatory balancing account revenue

The Company's ability to recover revenue requirements authorized by the California Public Utilities Commission (CPUC) in its triennial General Rate Case (GRC), is decoupled from the volume of the sales. Regulatory balancing account revenue is revenue related to rate mechanisms authorized in California by the CPUC, which allow the Company to recover the authorized revenue and are not considered contracts with customers.

The Water Revenue Adjustment Mechanism (WRAM) allows the Company to recognize the adopted level of volumetric revenues. The variance between adopted volumetric revenues and actual billed volumetric revenues for metered accounts is recorded as regulatory balancing account revenue.

Cost-recovery rates, such as the Modified Cost Balancing Account (MCBA), provide for recovery of the adopted levels of expenses for purchased water, purchased power, pump taxes, water conservation program costs, pension, and health care. Variances between adopted and actual costs are recorded as regulatory balancing account revenue.

Each district's WRAM and MCBA regulatory assets and liabilities are allowed to be netted against one another. The Company recognizes regulatory balancing account revenues that have been authorized for rate recovery, are objectively determinable and probable of recovery, and are expected to be collected within 24 months. To the extent that regulatory balancing account revenue is estimated to be collectible beyond 24 months, recognition is deferred.

Non-Regulated Revenue

The following tables disaggregate the Company's non-regulated revenue by source for the years ended December 31, 2018, 2017, and 2016:

	2018	2017	2016
Operating and maintenance revenue	\$ 10,258	\$ 8,621	\$ 8,430
Other non-regulated revenue	5,547	5,262	6,232
Non-regulated revenue from contracts with customers	\$ 15,805	\$ 13,883	\$ 14,662
Lease revenue	\$ 2,467	\$ 2,015	\$ 1,923
Total non-regulated revenue	\$ 18,272	\$ 15,898	\$ 16,585

Operating and maintenance services are provided for non-regulated water and wastewater systems owned by private companies and municipalities. The Company negotiates formal agreements with the customers, under which they provide operating, maintenance and customer billing services related to the customers' water system. The formal agreements outline the

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

fee schedule for the services provided. The agreements typically call for a fee-per-service or a flat-rate amount per month. The Company satisfies its performance obligation of providing operating and maintenance services over time as services are rendered; as a result, the Company employs the invoice practical expedient and recognizes revenue in the amount that it has the right to invoice. Contract terms are generally short-term and, as a result, no separate financing component is recognized for its collections from customers, which generally require payment within 30 days of billing.

Other non-regulated revenue primarily relates to services for the design and installation of water mains and other water infrastructure for customers outside the regulated service areas and insurance program administration.

The Company is the lessor in operating lease agreements with telecommunications companies under which cellular phone antennas are placed on the Company's property. Lease revenue is not considered revenue from contracts with customers and is recognized following current operating lease standards.

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 as of December 31, 2018, 2017 and 2016.

The activities in the allowance for doubtful accounts were as follows:

	2018	2017	2016
Beginning Balance	\$ 773	\$ 830	\$ 730
Provision for uncollectible accounts	1,703	1,570	2,111
Net write off of uncollectible accounts	(1,719)	(1,627)	(2,011)
Ending Balance	<u>\$ 757</u>	<u>\$ 773</u>	<u>\$ 830</u>

Other Receivables

As of December 31, 2018 and 2017, other receivables were:

	2018	2017
Accounts receivable from developers	\$ 9,633	\$ 6,425
Other	7,468	10,039
Total other receivables	<u>\$ 17,101</u>	<u>\$ 16,464</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, 2018, 2017, and 2016
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:

	2018	2017
Equipment	\$ 643,581	\$ 592,612
Office buildings and other structures	267,948	245,877
Transmission and distribution plant	2,038,895	1,891,268
Total	\$ 2,950,424	\$ 2,729,757

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:

	Useful Lives
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 3.02% in 2018, 3.00% in 2017 and 2.70% in 2016.

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 2018, 2017, and 2016 are shown in the tables below:

	2018	2017	2016
Allowance for equity funds used during construction	\$ 3,954	\$ 3,750	\$ —
Allowance for borrowed funds used during construction	2,063	2,360	2,965
Total	\$ 6,017	\$ 6,110	\$ 2,965

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, 2018 and 2017, the retirement obligation is estimated to be \$24.3 million and \$21.2 million, respectively. The change only impacted the consolidated balance sheet.

Cash, Cash Equivalents, and Restricted Cash

Cash and cash equivalents include highly liquid investments with remaining maturities of three months or less at the time of acquisition. In 2018 and 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.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The following table provides a reconciliation of cash, cash equivalents, and restricted cash within the Consolidated Balance Sheets that total to the amounts shown on the Consolidated Statements of Cash Flows:

	December 31, 2018	December 31, 2017
Cash and cash equivalents	47,176	94,776
Restricted cash (included in "taxes, prepaid expenses and other assets")	539	524
Total cash, cash equivalents, and restricted cash shown in the statements of cash flows	<u>\$ 47,715</u>	<u>\$ 95,300</u>

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 general, the Company does not earn a return on regulatory assets if the related costs do not accrue interest. Accordingly, the Company earns a return only on its regulatory assets for net WRAM and MCBA, pension balancing account, health care balancing account, and interim rates receivable. 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.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Regulatory assets and liabilities were comprised of the following as of December 31:

	Recovery Period	2018	2017
<i>Regulatory Assets</i>			
Pension and retiree group health	Indefinitely	\$ 156,947	\$ 214,249
Property-related temporary differences (tax benefits flowed through to customers)	Indefinitely	99,376	87,323
Other accrued benefits	Indefinitely	25,717	28,251
Net WRAM and MCBA long-term accounts receivable	1-2 years	17,134	34,879
Asset retirement obligations, net	Indefinitely	18,197	17,126
Interim rates long-term accounts receivable	1 year	4,642	4,568
Tank coating	10 years	11,196	10,998
Health care balancing account	1 year	442	496
Pension balancing account	1 year	16,494	6,657
Other components of net periodic benefit cost	Indefinitely	3,221	—
Other regulatory assets	Various	203	935
Total Regulatory Assets		<u>\$ 353,569</u>	<u>\$ 405,482</u>
<i>Regulatory Liabilities</i>			
Future tax benefits due to customers		\$ 180,205	\$ 170,136
Health care balancing account		3,516	2,861
Conservation program		6,880	2,273
Net WRAM and MCBA long-term payable		222	513
Pension balancing account		13	364
Tax accounting memorandum account		5,039	—
Cost of capital memorandum account		2,834	—
1,2,3 trichloropropane settlement proceeds		12,142	—
Other regulatory liabilities		424	464
Total Regulatory Liabilities		<u>\$ 211,275</u>	<u>\$ 176,611</u>

The Company's pension and postretirement health care benefits regulatory asset represents the unfunded obligation of the Company's pension and postretirement benefit plans which the Company expects to recover from customers in the future for these plans. The pension balancing account regulatory asset/liability and the healthcare balancing account regulatory asset/liability represent incurred pension and healthcare costs that exceeded/was below the cost recovery in rates and is recoverable/refundable from/to customers. These plans are discussed in further detail in Note 11. The other components of net periodic benefit cost regulatory asset are authorized by the Commissions and are probable for rate recovery through the capital program (see Note 2).

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 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.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 future tax benefits due to customers primarily resulted from 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 conservation program regulatory liability is for incurred conservation costs that were below the cost recovery in rates and is refundable to customers.

The tax accounting and cost of capital memorandum account regulatory liabilities are related to the estimated customer refunds due to changes in the federal income tax rate and to the March 22, 2018 cost of capital decision for Cal Water (see Item 1. Business - Rates and Regulation).

Short-term regulatory assets and liabilities are excluded from the above table. The short-term regulatory assets for 2018 and 2017 were \$42.4 million and \$36.8 million, respectively. The short-term regulatory assets, as of December 31, 2018 and 2017, primarily consist of net WRAM and MCBA receivables. The short-term portion of regulatory liabilities for 2018 and 2017 were \$12.2 million and \$59.3 million, respectively. The short-term regulatory liabilities, as of December 31, 2018 and 2017, primarily consist of TCP settlement proceeds (see Note 14 - Commitments and Contingencies) and net WRAM and MCBA liability balances.

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. 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 2018, 2017, and 2016 was \$1.1 million, \$0.9 million, and \$0.9 million, respectively.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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 \$186.3 million, and \$182.5 million at December 31, 2018 and 2017, 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 2019, \$7.7 million in 2020, \$7.7 million in 2021, \$7.6 million in 2022, and \$7.6 million in 2023.

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 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 sets rates utilizing the flow through method of accounting for state income 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.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Company did not grant any Stock Appreciation Rights (SARs) in 2018, 2017, and 2016. There were 64,500 SARs outstanding during the first quarter of 2016 which resulted in 3 dilutive SARs for the year. The dilutive effect is shown in the table below:

	2018	2017	2016
	(In thousands, except per share data)		
Net income available to common stockholders	\$ 65,584	\$ 72,940	\$ 48,675
Weighted average common shares, basic	48,060	48,009	47,953
Dilutive SARs (treasury method)	—	—	3
Weighted average common shares, dilutive	48,060	48,009	47,956
Earnings per share—basic	\$ 1.36	\$ 1.52	\$ 1.02
Earnings per share—diluted	\$ 1.36	\$ 1.52	\$ 1.01

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, 2018 and 2017.

Adoption of New Accounting Standards

In May of 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers* (codified in ASC 606), which amends the existing revenue recognition guidance. The Company completed an evaluation of the new revenue standard and implemented the standard on January 1, 2018 using the modified retrospective method for all contracts. The reported results for 2018 reflect the application of ASC 606 guidance, while prior period amounts were not adjusted and continue to be reported in accordance with the accounting standards in effect for those periods. Other than increased disclosures regarding revenues related to contracts with customers, the implementation did not have a significant impact on the Company's consolidated financial statements (see "Operating Revenue" section of Note 2 above).

In August of 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. The Company is required to classify proceeds from the settlement of insurance claims on the basis of the nature of the loss and from the settlement of Company-owned life insurance policies as cash inflows on the Consolidated Statements of Cash Flows. The Company implemented the standard on January 1, 2018 and retrospectively applied the standard in the comparative period. The standard does not have a significant impact to the Company's consolidated financial statements.

In November of 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230) - Restricted Cash*. The update requires the Company to combine restricted cash with cash and cash equivalents when reconciling the beginning and end of period balances in the Consolidated Statements of Cash Flows. The Company implemented the standard on January 1, 2018 and retrospectively applied the standard in the comparative periods.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The following tables show the effect of the accounting change to the Consolidated Statements of Cash Flows for 2017 and 2016:

<i>Consolidated Statement of Cash Flows line item</i>	2017		
	As Previously Reported	Adjustments	As Adjusted
Change in restricted cash	\$ (81)	\$ 81	\$ —
Net cash used in investing activities	\$ (206,652)	\$ 81	\$ (206,571)
Change in cash, cash equivalents, and restricted cash	\$ 69,284	\$ 81	\$ 69,365
Cash, cash equivalents, and restricted cash at beginning of period	\$ 25,492	\$ 443	\$ 25,935
Cash, cash equivalents, and restricted cash at end of period	\$ 94,776	\$ 524	\$ 95,300

<i>Consolidated Statement of Cash Flows line item</i>	2016		
	As Previously Reported	Adjustments	As Adjusted
Change in restricted cash	\$ 66	\$ (66)	\$ —
Net cash used in investing activities	\$ (230,839)	\$ (66)	\$ (230,905)
Change in cash, cash equivalents, and restricted cash	\$ 16,655	\$ (66)	\$ 16,589
Cash, cash equivalents, and restricted cash at beginning of period	\$ 8,837	\$ 509	\$ 9,346
Cash, cash equivalents, and restricted cash at end of period	\$ 25,492	\$ 443	\$ 25,935

In March of 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. In addition, the standard only allows the service cost component to be eligible for capitalization.

The standard became effective as of January 1, 2018. The presentation amendments were applied retrospectively and the capitalization amendments were applied prospectively on and after the effective date. The Company applied the practical expedient that permits the Company to use the amounts disclosed in its pension and other postretirement benefit plan footnote from the prior comparative periods as the estimation basis for applying the retrospective presentation requirements. The Commissions have authorized the Company to recover a portion of the other components of net periodic benefit cost through the Company's capital program. Thus, on and after the effective date, the other components of net periodic benefit cost that have previously been recorded as part of utility plant have been recognized as a regulatory asset. As a result, the changes required by the standard did not have a material impact on the results of operations of financial position.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The following tables show the effect of the accounting change to the Consolidated Statements of Income for 2017 and 2016:

<i>Consolidated Statement of Income line item</i>	2017		
	As Previously Reported	Adjustments	As Adjusted
Administrative and general	\$ 102,914	\$ (9,588)	\$ 93,326
Income taxes	\$ 28,928	\$ 2,887	\$ 31,815
Total operating expenses	\$ 572,267	\$ (6,701)	\$ 565,566
Net operating income	\$ 94,623	\$ 6,701	\$ 101,324
Other components of net periodic benefit cost	\$ —	\$ (9,588)	\$ (9,588)
Income tax expense on other income and expenses	\$ (4,435)	\$ 2,887	\$ (1,548)
Net other income (loss)	\$ 6,486	\$ (6,701)	\$ (215)

<i>Consolidated Statement of Income line item</i>	2016		
	As Previously Reported	Adjustments	As Adjusted
Administrative and general	\$ 98,474	\$ (10,873)	\$ 87,601
Income taxes	\$ 24,804	\$ 4,431	\$ 29,235
Total operating expenses	\$ 533,176	\$ (6,442)	\$ 526,734
Net operating income	\$ 76,194	\$ 6,442	\$ 82,636
Other components of net periodic benefit cost	\$ —	\$ (10,873)	\$ (10,873)
Income tax benefit (expense) on other income and expenses	\$ (2,012)	\$ 4,431	\$ 2,419
Net other income (loss)	\$ 2,982	\$ (6,442)	\$ (3,460)

New Accounting Standards Issued But Not Yet Adopted

In February of 2016, the FASB issued ASU 2016-02, *Leases*, which amends the guidance relating to the definition of a lease, recognition of lease assets and liabilities on the balance sheet, and the related disclosure requirements. In July of 2018, the FASB issued ASU 2018-11, *Leases: Targeted Improvements*, which amends 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 intends to elect certain practical expedients and will carry forward historical conclusions related to (1) contracts that contain leases, (2) existing lease classification for any expired or existing leases, and (3) initial direct costs for any existing leases. The Company will also apply the practical expedient that will allow the Company to elect, as an accounting policy, by asset class, to include both lease and nonlease components as a single component and account for it as a lease. The Company will apply the short-term lease exception for lessees which will allow the Company to not have to apply the recognition requirements of the new leasing guidance for short-term leases and to recognize lease payments in net income on a straight line basis over the lease term. The Company estimates approximately \$13.8 million will be recognized as total right-of-use assets and total lease liabilities on the Company's Consolidated Balance Sheet as of January 1, 2019. Otherwise, the Company does not expect the new standard to have a material impact on the remaining consolidated financial statements.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

3 OTHER INCOME AND EXPENSES

The Company conducts various non-regulated activities as reflected in the table below:

	2018		2017		2016	
	Revenue	Expense	Revenue	Expense	Revenue	Expense
Operating and maintenance	\$ 10,392	\$ 11,895	\$ 8,621	\$ 8,847	\$ 8,430	\$ 9,061
Leases	2,467	135	2,015	182	1,923	204
Design and construction	1,273	1,202	1,918	1,635	1,792	1,473
Meter reading and billing	391	157	256	(6)	242	62
Interest income	133	—	68	—	18	—
Change in value of life insurance contracts loss (gain)	—	2,340	—	(3,057)	—	(1,026)
Other non-regulated income and expenses	3,616	7,058	3,020	1,789	4,180	1,671
Total	\$ 18,272	\$ 22,787	\$ 15,898	\$ 9,390	\$ 16,585	\$ 11,445

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 typically 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. The 2018 other non-regulated income and expenses included \$5.4 million of new business development expenses. Also, the 2016 other non-regulated income and expenses included a litigation gain of \$1.5 million.

4 INTANGIBLE ASSETS

As of December 31, 2018 and 2017, intangible assets that will continue to be amortized and those not amortized were:

	Weighted Average Amortization Period (years)	2018			2017		
		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	\$ 112	\$ 972	\$ 1,084	\$ 108	\$ 976
Water planning studies	9	18,364	11,899	6,465	15,922	10,306	5,616
Leasehold improvements and other	17	1,519	882	637	1,426	804	622
Total		<u>\$ 20,967</u>	<u>\$ 12,893</u>	<u>\$ 8,074</u>	<u>\$ 18,432</u>	<u>\$ 11,218</u>	<u>\$ 7,214</u>
Unamortized intangible assets:							
Perpetual water rights and other		\$ 3,776	\$ —	\$ 3,776	\$ 3,780	\$ —	\$ 3,780

Water pumping rights usage is the amount of water pumped from aquifers to be treated and distributed to customers.

For the year ended December 31, 2018 amortization of intangible assets was \$1.7 million and for the years ended December 31, 2017 and 2016, amortization of intangible assets was \$1.6 million. Estimated future amortization expense related to intangible assets for the succeeding 5 years is approximately \$1.6 million in 2019, \$1.1 million in 2020, \$1.1 million in 2021, \$0.9 million in 2022, \$0.8 million in 2023, and \$2.6 million thereafter.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018 and 2017
Dollar amounts in thousands unless otherwise stated

5 PREFERRED STOCK

The Company is authorized to issue 241,000 shares of Preferred Stock as of December 31, 2018. No shares of Preferred Stock were issued and outstanding as of December 31, 2018 or 2017.

6 COMMON STOCKHOLDERS' EQUITY

As of December 31, 2018 and 2017, 48,064,707 shares and 48,012,432 shares, respectively, of common stock were issued and outstanding.

Effective January 1, 2019, the Company implemented an Employee Stock Purchase Plan (ESPP). Under the ESPP, qualified employees are permitted to purchase the Company's common stock at 90% of the market value of the common stock on the specified stock purchase date. The ESPP is deemed compensatory and compensation costs will be accounted for under ASC 718, Stock Compensation. Employees' payroll deductions for common stock purchases may not exceed 10% of their salaries. Employees may purchase up to 2,000 shares per period provided that the value of the shares purchased in any calendar year may not exceed \$25,000, as calculated pursuant to the ESPP.

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 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 DRIP 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 weighted average interest rate on the lines was 2.91% and 2.05% for the years ended December 31, 2018 and 2017, respectively.

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, 2018 and 2017, the outstanding borrowings on the Company lines of credit were \$55.1 million. The borrowings on the Cal Water lines of credit were \$10.0 million and \$220.0 million as of December 31, 2018 and 2017, respectively.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018 and 2017
Dollar amounts in thousands unless otherwise stated

8 LONG-TERM DEBT

As of December 31, 2018 and 2017, long-term debt outstanding was:

	Series	Interest Rate	Maturity Date	2018	2017
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
	UUU	3-month LIBOR plus 70 basis points	2020	300,000	—
	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
	GGG	5.290%	2022	7,273	9,091
	HHH	5.290%	2022	7,273	9,091
	III	5.540%	2023	4,546	5,454
	JJJ	5.440%	2018	—	909
	LLL	5.480%	2018	—	10,000
	OOO	6.020%	2031	20,000	20,000
	CC	9.860%	2020	16,800	16,900
Total First Mortgage Bonds				805,892	521,445
California Department of Water Resources Loans		2.6% to 8.0%	2018 - 32	5,830	6,201
Other long-term debt				6,978	7,956
Unamortized debt issuance costs				(3,762)	(3,889)
Total long-term debt, net				814,938	531,713
Less current maturities, net				104,911	15,920
Long-term debt excluding current maturities, net				<u>\$ 710,027</u>	<u>\$ 515,793</u>

On September 13, 2018, Cal Water sold \$300.0 million of floating rate First Mortgage Bonds due in September of 2020 in a private placement. The floating interest rate was set at three-month LIBOR plus 70 basis points, will accrue quarterly, and be payable in arrears. The bonds are redeemable at a premium of 02%, or at par after June 13, 2019. The bonds will also rank equally with all of Cal Water's other First Mortgage Bonds and will be secured by liens on Cal Water's properties, subject to certain exceptions and permitted liens.

In 2018, Cal Water repaid \$10.9 million of First Mortgage Bonds JJJ and LLL, which matured in 2018. In 2017, 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 \$5.8 million and \$6.4 million capital lease liability as of December 31, 2018 and 2017 is included in other long-term debt and current maturities set forth above.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

9 OTHER ACCRUED LIABILITIES

As of December 31, 2018 and 2017, other accrued liabilities were:

	2018	2017
Accrued and deferred compensation	\$ 20,229	\$ 23,916
Accrued benefits and workers' compensation claims	5,896	6,640
Other	7,381	6,115
Total other accrued liabilities	<u>\$ 33,506</u>	<u>\$ 36,671</u>

10 INCOME TAXES

Income tax expense (benefit) consisted of the following:

	Federal	State	Total
2018			
Current	\$ —	\$ 3	\$ 3
Deferred	15,995	(126)	15,869
Total	<u>\$ 15,995</u>	<u>\$ (123)</u>	<u>\$ 15,872</u>
2017			
Current	\$ —	\$ 3	\$ 3
Deferred	35,881	943	36,824
Total	<u>\$ 35,881</u>	<u>\$ 946</u>	<u>\$ 36,827</u>
2016			
Current	\$ 130	\$ 2	\$ 132
Deferred	26,603	81	26,684
Total income tax	<u>\$ 26,733</u>	<u>\$ 83</u>	<u>\$ 26,816</u>

The Company's 2018, 2017 and 2016 federal qualified repairs and maintenance deductions totaled \$99.0 million, \$85.7 million, and \$84.9 million, respectively.

The total federal NOL carry-forward was \$62.4 million and the state NOL carry-forward was \$28.0 million as of December 31, 2018. 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 2027.

As of December 31, 2018, 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.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

10 INCOME TAXES (Continued)

The difference between the recorded and the statutory income tax expense is reconciled in the table below:

	2018	2017	2016
Statutory income tax	\$ 17,105	\$ 38,419	\$ 26,422
Increase (reduction) in taxes due to:			
State income taxes net of federal tax benefit	5,685	6,017	4,341
Effect of regulatory treatment of fixed asset differences	(5,954)	(4,584)	(4,298)
Investment tax credits	(74)	(74)	(74)
AFUDC equity	(1,106)	(1,528)	—
Share base stock compensation	(278)	(581)	—
Other	494	(842)	425
Total income tax	<u>\$ 15,872</u>	<u>\$ 36,827</u>	<u>\$ 26,816</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 adjusted and recorded the impacts of the TCJA 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.

A TCJA refund of \$108.0 million was recorded as a provisional estimate on December 31, 2017. During the year ended December 31, 2018, the Company completed its analysis of its deferred tax balances which resulted in a change from a net deferred income tax regulatory asset to a net regulatory liability. The TCJA refund was \$107.0 million, with gross up \$42.0 million, total regulatory liabilities for TCJA was \$149 million as of December 31, 2018. The Company is still working with state regulators to finalize the ratepayer net refund of \$107.0 million to ensure compliance with federal normalization rules. 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 deferred tax assets and deferred tax liabilities as of December 31, 2018 and 2017, are presented in the following table:

	2018	2017
Deferred tax assets:		
Developer deposits for extension agreements and contributions in aid of construction	\$ 39,074	\$ 33,552
Net operating loss carryforward and tax credits	8,257	13,329
Pension liability	8,725	7,906
Income tax regulatory liability	44,072	41,712
Other	4,273	280
Total deferred tax assets	<u>104,401</u>	<u>96,779</u>
Deferred tax liabilities:		
Property related basis and depreciation differences	288,544	262,442
WRAM/MCBA and interim rates balancing accounts	26,348	26,404
Other	2,542	2,550
Total deferred tax liabilities	<u>317,434</u>	<u>291,396</u>
Net deferred tax liabilities	<u>\$ 213,033</u>	<u>\$ 194,617</u>

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

10 INCOME TAXES (Continued)

The increases in developer deposits for extension agreements and contributions in aid of construction (CIAC) and property related basis and depreciation differences, as compared to the prior year, were mostly due to the TCJA. All developer deposits for CIAC are taxable in 2018 for federal income tax purposes. 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 and reclassification of certain amounts to income tax regulatory liability, as well as the future tax benefit associated with the expected reduction in revenues related to the recovery of lower income taxes through customer rates.

A valuation allowance was not required at December 31, 2018 and 2017. 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.

The following table reconciles the changes in unrecognized tax benefits:

	December 31, 2018	December 31, 2017	December 31, 2016
Balance at beginning of year	\$ 11,058	\$ 10,499	\$ 10,298
Additions for tax positions taken during prior year	—	—	—
Additions for tax positions taken during current year	1,787	559	201
Reduction to prior year tax position	(3,129)	—	—
Lapse of statute of limitations	—	—	—
Balance at end of year	<u>\$ 9,716</u>	<u>\$ 11,058</u>	<u>\$ 10,499</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, 2018, was \$2.9 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 2018 and the state income tax years subject to an examination are from 2012 to 2018.

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 \$6.0 million, \$5.6 million, and \$5.4 million, for the years 2018, 2017, and 2016, 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 \$492.4 million and \$513.6 million as of December 31, 2018 and 2017, respectively. The fair value of pension plan assets was \$469.8 million and \$460.9 million as of December 31, 2018 and 2017, 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 \$14.8 million in 2019, \$16.2 million in 2020, \$17.9 million in 2021, \$19.8 million in 2022, and \$21.4 million in 2023. The aggregate benefits expected to be paid in the 5 years 2024 through 2028 are \$133.9 million. The expected benefit payments are based upon the same assumptions used to measure the Company's benefit obligation at December 31, 2018, and include estimated future employee service.

The Company also maintains an unfunded, non-qualified, supplemental executive retirement plan. The unfunded supplemental executive retirement plan accumulated benefit obligations were \$56.8 million and \$56.7 million as of December 31,

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

11 EMPLOYEE BENEFIT PLANS (Continued)

2018 and 2017, 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 2018, 2017, and 2016, was \$8.8 million, \$8.5 million, and \$8.9 million, respectively. The remaining net periodic benefit cost was \$2.8 million at December 31, 2018, 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 \$2.7 million in 2019, \$3.0 million in 2020, \$3.2 million in 2021, \$3.5 million in 2022, and \$3.8 million in 2023. The aggregate benefits expected to be paid in the 5 years 2024 through 2028 are \$23.5 million. The expected Medicare Part D subsidies are \$0.3 million in 2019, \$0.3 million in 2020, \$0.3 million in 2021, \$0.4 million in 2022, and \$0.4 million in 2023. The aggregate Medicare part D subsidies expected to be paid in the 5 years 2024 through 2028 are \$2.6 million.

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.

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:

	Minimum Exposure	Target	Maximum Exposure
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 5 years.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

11 EMPLOYEE BENEFIT PLANS (Continued)

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 Retirement 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 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, 2018 and 2017:

	Pension Benefits				Other Benefits			
	2018	%	2017	%	2018	%	2017	%
Fixed Income	\$ 188,934	40%	\$ 171,403	37%	\$ 45,446	44%	\$ 60,438	60%
Domestic Equity: Small Cap Stocks	68,843	15%	73,682	16%	—	—	—	—
Domestic Equity: Large Cap Stocks	165,862	35%	169,661	37%	57,179	56%	40,125	40%
Non U.S. Equities	46,135	10%	46,132	10%	—	—	—	—
Total Plan Assets	\$ 469,774	100%	\$ 460,878	100%	\$ 102,625	100%	\$ 100,563	100%

The pension benefits fixed income category includes \$5.0 million and \$22.5 million of money market fund investments as of December 31, 2018 and 2017, respectively. The other benefits fixed income category includes \$9.9 million and \$39.4 million of money market fund investments as of December 31, 2018 and 2017, respectively.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

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, 2018 and 2017:

	Pension Benefits		Other Benefits	
	2018	2017	2018	2017
Change in projected benefit obligation:				
Beginning of year	\$ 671,334	\$ 564,755	\$ 143,368	\$ 122,108
Service cost	29,027	23,801	8,317	7,152
Interest cost	23,994	23,256	4,873	4,988
Assumption change	(80,192)	60,526	(21,672)	15,298
Plan amendment	—	—	2,203	—
Experience loss (gain)	8,523	10,836	(8,226)	(4,546)
Benefits paid, net of retiree premiums	(12,765)	(11,840)	(1,659)	(1,632)
End of year	\$ 639,921	\$ 671,334	\$ 127,204	\$ 143,368
Change in plan assets:				
Fair value of plan assets at beginning of year	\$ 460,878	\$ 376,549	\$ 100,563	\$ 86,578
Actual return on plan assets	(22,576)	64,365	(4,320)	6,508
Employer contributions	44,237	31,804	8,041	9,109
Retiree contributions and Medicare part D subsidies	—	—	2,025	1,884
Benefits paid	(12,765)	(11,840)	(3,684)	(3,516)
Fair value of plan assets at end of year	\$ 469,774	\$ 460,878	\$ 102,625	\$ 100,563
Funded status(1)	\$ (170,147)	\$ (210,456)	\$ (24,579)	\$ (42,805)
Unrecognized actuarial loss	117,973	150,545	18,618	39,796
Unrecognized prior service cost	15,290	20,342	2,326	165
Net amount recognized	\$ (36,884)	\$ (39,569)	\$ (3,635)	\$ (2,844)

(1) The short-term portion of the pension benefits was \$1.9 million as of December 31, 2018 and \$2.0 million as of December 31, 2017 and is recorded as part of other accrued liabilities on the Company's 2018 and 2017 Consolidated Balance Sheets.

Amounts recognized on the balance sheet consist of:

	Pension Benefits		Other Benefits	
	2018	2017	2018	2017
(Accrued) benefit costs	\$ 62	\$ 60	\$ (2,802)	\$ (3,461)
Accrued benefit liability	(170,147)	(210,456)	(24,579)	(42,805)
Regulatory asset	133,201	170,827	23,746	43,422
Net amount recognized	\$ (36,884)	\$ (39,569)	\$ (3,635)	\$ (2,844)

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

11 EMPLOYEE BENEFIT PLANS (Continued)
Valuation Assumptions

Below are the actuarial assumptions used in determining the benefit obligation for the benefit plans:

	Pension Benefits		Other Benefits	
	2018	2017	2018	2017
Weighted average assumptions as of December 31:				
Discount rate	4.20 %	3.60 %	4.25 %	3.65 %
Long-term rate of return on plan assets	6.50 %	6.50 %	5.50 %	5.50 %
Rate of compensation increases - pension plan	3.25 %	3.25 %	—	—
Rate of compensation increases - SERP	3.75 %	3.75 %	—	—
Cost of living adjustment	2.50 %	2.50 %	—	—

The discount rate was derived from the FTSE 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 7.62% for domestic equities and 8.73% 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 4.78% for fixed income investments and 2.90% for short-term cash investments. The average return for the pension and other benefit plans for the last 5 and 10 years was 5.00% and 8.20%, 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 2018, the Company used the Society of Actuaries 2014 Mortality Tables Report (RP-2014) and Mortality Improvement Scale (MP-2018 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, 2018.

Components of Net Periodic Benefit Cost

Net periodic benefit costs for the pension and other postretirement plans for the years ended December 31, 2018, 2017, and 2016 included the following components:

	Pension Plan			Other Benefits		
	2018	2017	2016	2018	2017	2016
Service cost	\$ 29,027	\$ 23,801	\$ 20,971	\$ 8,317	\$ 7,152	\$ 6,513
Interest cost	23,994	23,256	22,226	4,873	4,988	4,863
Expected return on plan assets	(27,702)	(24,119)	(21,826)	(5,639)	(4,875)	(4,129)
Net amortization and deferral	16,233	12,962	11,990	1,281	1,186	1,660
Net periodic benefit cost	\$ 41,552	\$ 35,900	\$ 33,361	\$ 8,832	\$ 8,451	\$ 8,907

Service cost portion of the pension plan and other postretirement benefits is recognized in administrative and general within the Consolidated Statements of Income. Other components of net periodic benefit costs include interest costs, expected return on plan assets, amortization of prior service costs, and recognized net actuarial loss and are reported together as other components of net periodic benefit cost within the Consolidated Statements of Income (see Note 2).

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

11 EMPLOYEE BENEFIT PLANS (Continued)

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	
	2018	2017	2018	2017
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 - pension plan	3.25 %	3.25 %	—	—
Rate of compensation increases - SERP	3.75 %	3.75 %	—	—
Cost of living adjustment	2.50 %	2.50 %		

The health care cost trend rate assumption has a significant effect on the amounts reported. For 2018 measurement purposes, the Company assumed a 6.3% annual rate of increase in the per capita cost of covered benefits with the rate decreasing to 5.5% by 2020, then gradually grading down to 4.5% 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	\$ 4,213	\$ (3,017)
Effect on accumulated postretirement benefit obligation	\$ 29,286	\$ (22,137)

The Company intends to make annual contributions that meet the funding requirements of ERISA. The Company estimates in 2019 that the annual contribution to the pension plans will be \$20.7 million and the annual contribution to the other postretirement plan will be \$9.4 million.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

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 2018 and 2017, the Company granted annual Restricted Stock Awards (RSAs) of 47,273 and 49,290, respectively, of common stock to officers and directors of the Company. In 2018 and 2017, 19,742 RSAs and 20,747 RSAs, respectively, were canceled. Officer RSAs granted in 2018 and 2017 vest over 36 months with the first year cliff vesting. Director RSAs generally vest at the end of 12 months. During 2018 and 2017, the RSAs granted were valued at \$35.40 and \$36.75 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 28,594 and 31,389 of common stock to officers in 2018 and 2017, respectively. Each award reflects a target number of common shares that may be issued to the award recipient. The 2018 and 2017 awards may be earned upon the completion of a 3-year performance period. During 2018 and 2017, the Company issued 48,753 RSUs and 38,709 RSUs, respectively, to officers, and 24,009 RSUs and 19,735 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 \$35.40 per share for the 2018 RSUs and \$36.75 per share for the 2017 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, \$3.1 million, and \$2.8 million for 2018, 2017 and 2016, respectively.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

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.

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.

December 31, 2018					
	Cost	Fair Value			
		Level 1	Level 2	Level 3	Total
Long-term debt, including current maturities, net	\$ 814,938	\$ —	\$ 849,551	\$ —	\$ 849,551
Advances for construction	186,342	—	77,204	—	77,204
Total	\$ 1,001,280	\$ —	\$ 926,755	\$ —	\$ 926,755

December 31, 2017					
	Cost	Fair Value			
		Level 1	Level 2	Level 3	Total
Long-term debt, including current maturities, net	\$ 531,713	\$ —	\$ 607,492	\$ —	\$ 607,492
Advances for construction	182,502	—	75,083	—	75,083
Total	\$ 714,215	\$ —	\$ 682,575	\$ —	\$ 682,575

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

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.

	Facility Leases	System Lease	Water Supply Contracts*	Capital Lease Obligations
2019	\$ 926	\$ 845	\$ 31,082	\$ 1,477
2020	864	845	31,083	1,170
2021	640	845	31,083	1,170
2022	510	845	31,084	1,170
2023	416	845	31,085	1,170
Thereafter	2,722	7,816	520,518	3,217

* Estimated annual contractual obligations are based on the same payment levels as 2018.

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 \$1.2 million in 2018, \$1.1 million in 2017, and \$1.0 million in 2016.

System Lease

The system lease is a 15-year lease with the City of Commerce that was renewed in April in 2018 for an additional 5 years. The lease includes an annual lease payment of \$0.8 million. The Company has operated the City of Commerce water system since 1985 and is responsible for all operations, maintenance, water quality assurance, customer service programs, and financing capital improvements to provide a reliable supply of water that meets federal and state standards to customers served by the City of Commerce system. The City of Commerce will retain title to the system and system improvements and remain responsible for setting its customers' water rates. The Company bears the risks of operation and collection of amounts billed to customers. In exchange, the Company receives all revenue from the water system, which was \$3.0 million, \$3.4 million, and \$2.5 million in 2018, 2017, and 2016, respectively. The agreement allows the Company to request a rate change annually in order to recover costs.

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 \$9.7 million in 2018, \$9.1 million in 2017, and \$8.5 million in 2016.

The Company also has a water supply contract with Stockton East Water District (SEWD) that requires a fixed monthly payment. Each year, the fixed monthly payment is adjusted for changes to SEWD's costs. The total paid under the contract was \$13.7 million in 2018, \$14.1 million in 2017, and \$12.2 million in 2016.

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

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

14 COMMITMENTS AND CONTINGENCIES (Continued)

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.

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 \$9.7 million annually, which equates to \$473.42 dollars per acre foot. Total treated water charge for 2018 was \$3.5 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 \$64.21 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 \$473.42 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 \$10.1 million, \$10.0 million, and \$8.5 million in 2018, 2017, and 2016, 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 \$1.2 million in 2018, \$1.1 million in 2017, and \$1.0 million in 2016. The capital lease asset was \$5.8 million as of December 31, 2018.

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,

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

14 COMMITMENTS AND CONTINGENCIES (Continued)

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. As of December 31, 2018, Cal Water has used \$43.9 million of the proceeds on remediation efforts related to the 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, 2018, 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 Company has recognized a liability of \$2.3 million for all known legal matters as of December 31, 2018 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.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018 and 2017
Dollar amounts in thousands unless otherwise stated

15 QUARTERLY FINANCIAL DATA (UNAUDITED)

The Company's common stock is traded on the New York Stock Exchange under the symbol "CWT." The four quarters of 2017 were adjusted for an immaterial computational error that understated operating revenue (see Note 17). Additionally, the quarterly financial data for the first three quarters of 2018 were also adjusted to reflect the correction of the immaterial computational error that understated operating revenue for the first 9 months of 2018. The Company intends to correct this error prospectively in subsequent quarterly filings.

2018	First		Second		Third		Fourth	
	As Previously Reported	As Corrected	As Previously Reported	As Corrected	As Previously Reported	As Corrected		
Operating revenue	\$ 132,247	\$ 134,553	\$ 172,632	\$ 174,938	\$ 218,983	\$ 221,288	\$	167,417
Net operating income	8,053	9,836	25,056	26,839	45,548	47,329		26,536
Net (loss) income	(2,545)	(762)	13,022	14,805	34,392	36,173		15,368
Diluted (loss) earnings per share	(0.05)	(0.02)	0.27	0.31	0.72	0.75		0.32
Common stock market price range:								
High	45.85	45.85	41.65	41.65	42.95	42.95		49.07
Low	35.25	35.25	35.60	35.60	38.85	38.85		40.10
Dividends paid per common share	0.1875	0.1875	0.1875	0.1875	0.1875	0.1875		0.1875

2017	First		Second		Third		Fourth	
	As Previously Reported	As Corrected	As Previously Reported	As Corrected	As Previously Reported	As Corrected	As Adjusted	As Corrected
Operating revenue	\$ 122,036	\$ 124,342	\$ 171,132	\$ 173,438	\$ 211,731	\$ 214,037	\$ 161,991	\$ 164,296
Net operating income (a)	10,553	11,993	26,671	28,111	42,462	43,902	21,638	23,077
Net income	1,132	2,572	18,531	19,971	33,849	35,289	13,669	15,108
Diluted earnings per share	0.02	0.05	0.39	0.42	0.70	0.74	0.29	0.31
Common stock market price range:								
High	37.60	37.60	39.40	39.40	39.65	39.65	46.15	46.15
Low	32.45	32.45	32.75	32.75	36.30	36.30	38.15	38.15
Dividends paid per common share	0.1800	0.1800	0.1800	0.1800	0.1800	0.1800	0.1800	0.1800

(a) The 2017 net operating income reflects the retrospective adoption of ASU 2017-07 (see Note 2). The Company adopted this guidance effective January 1, 2018.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016

Amounts in thousands, except share and per share data or as otherwise stated

16 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, 2018 and 2017, the Condensed Consolidating Statements of Income for the years ended December 31, 2018, 2017, and 2016, and the Condensed Consolidating Statements of Cash Flows for the years ended December 31, 2018, 2017, and 2016, 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 statements of cash flows for the years ended December 31, 2017 and 2016 reflect the retrospective adoption of ASU 2016-09 (see Note 2), which affected California Water Service Company and the other subsidiaries. The Condensed Consolidating Statements of Income for the years ended December 31, 2017 and 2016 reflect the retrospective adoption of ASU 2017-07 (see Note 2), which affect California Water Service Company and the other subsidiaries.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATING BALANCE SHEET
As of December 31, 2018

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
(In thousands)					
ASSETS					
Utility plant:					
Utility plant	\$ 1,318	\$ 3,021,437	\$ 213,888	\$ (7,197)	\$ 3,229,446
Less accumulated depreciation and amortization	(1,013)	(938,072)	(59,735)	2,097	(996,723)
Net utility plant	305	2,083,365	154,153	(5,100)	2,232,723
Current assets:					
Cash and cash equivalents	3,779	33,763	9,634	—	47,176
Receivables and unbilled revenue	126	118,632	4,201	—	122,959
Receivables from affiliates	21,318	4,074	61	(25,453)	—
Other current assets	80	16,907	1,580	—	18,567
Total current assets	25,303	173,376	15,476	(25,453)	188,702
Other assets:					
Regulatory assets	—	349,414	4,155	—	353,569
Investments in affiliates	733,156	—	—	(733,156)	—
Long-term affiliate notes receivable	27,829	—	—	(27,829)	—
Other assets	133	58,959	3,821	(203)	62,710
Total other assets	761,118	408,373	7,976	(761,188)	416,279
TOTAL ASSETS	\$ 786,726	\$ 2,665,114	\$ 177,605	\$ (791,741)	\$ 2,837,704
CAPITALIZATION AND LIABILITIES					
Capitalization:					
Common stockholders' equity	\$ 730,157	\$ 659,340	\$ 79,093	\$ (738,433)	\$ 730,157
Affiliate long-term debt	—	—	27,828	(27,828)	—
Long-term debt, net	—	709,444	583	—	710,027
Total capitalization	730,157	1,368,784	107,504	(766,261)	1,440,184
Current liabilities:					
Current maturities of long-term debt, net	—	104,664	247	—	104,911
Short-term borrowings	55,100	10,000	—	—	65,100
Payables to affiliates	17	488	24,948	(25,453)	—
Accounts payable	—	92,310	3,270	—	95,580
Accrued expenses and other liabilities	107	53,655	1,813	—	55,575
Total current liabilities	55,224	261,117	30,278	(25,453)	321,166
Unamortized investment tax credits	—	1,649	—	—	1,649
Deferred income taxes	1,376	210,052	1,648	(43)	213,033
Pension and postretirement benefits other than pensions	—	193,538	—	—	193,538
Regulatory and other long-term liabilities	(31)	250,720	5,817	16	256,522
Advances for construction	—	185,843	499	—	186,342
Contributions in aid of construction	—	193,411	31,859	—	225,270
TOTAL CAPITALIZATION AND LIABILITIES	\$ 786,726	\$ 2,665,114	\$ 177,605	\$ (791,741)	\$ 2,837,704

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATING BALANCE SHEET
As of December 31, 2017

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
(In thousands)					
ASSETS					
Utility plant:					
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	402	1,902,497	150,252	(5,186)	2,047,965
Current assets:					
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	24,760	212,530	14,671	(24,088)	227,873
Other assets:					
Regulatory assets	—	401,668	3,814	—	405,482
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	725,323	461,249	7,636	(725,336)	468,872
TOTAL ASSETS	\$ 750,485	\$ 2,576,276	\$ 172,559	\$ (754,610)	\$ 2,744,710
CAPITALIZATION AND LIABILITIES					
Capitalization:					
Common stockholders' equity	\$ 693,462	\$ 632,059	\$ 77,647	\$ (703,947)	\$ 699,221
Affiliate long-term debt	—	—	26,441	(26,441)	—
Long-term debt, net	—	514,952	841	—	515,793
Total capitalization	693,462	1,147,011	104,929	(730,388)	1,215,014
Current liabilities:					
Current maturities of long-term debt, net	—	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	55,371	430,741	28,935	(24,088)	490,959
Unamortized investment tax credits	—	1,724	—	—	1,724
Deferred income taxes	1,652	190,675	2,424	(134)	194,617
Pension and postretirement benefits other than pensions	—	252,141	—	—	252,141
Regulatory and other long-term liabilities	—	217,684	3,348	—	221,032
Advances for construction	—	181,979	523	—	182,502
Contributions in aid of construction	—	154,321	32,400	—	186,721
TOTAL CAPITALIZATION AND LIABILITIES	\$ 750,485	\$ 2,576,276	\$ 172,559	\$ (754,610)	\$ 2,744,710

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATING STATEMENT OF INCOME
For the Year Ended December 31, 2018

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
	(In thousands)				
Operating revenue	\$ —	\$ 656,939	\$ 41,257	\$ —	\$ 698,196
Operating expenses:					
Operations:					
Purchased water	—	206,675	428	—	207,103
Purchased power	—	22,460	8,620	—	31,080
Pump taxes	—	14,664	—	—	14,664
Administrative and general	—	90,563	10,218	—	100,781
Other operations	—	73,521	6,930	(583)	79,868
Maintenance	—	23,573	921	—	24,494
Depreciation and amortization	94	78,601	5,173	(87)	83,781
Income tax (benefit) expense	(960)	17,678	948	923	18,589
Property and other taxes	—	24,190	3,106	—	27,296
Total operating (income) expenses	(866)	551,925	36,344	253	587,656
Net operating income	866	105,014	4,913	(253)	110,540
Other income and expenses:					
Non-regulated revenue	2,333	17,658	1,197	(2,916)	18,272
Non-regulated expenses	—	(22,122)	(665)	—	(22,787)
Other components of net periodic benefit cost	—	(8,886)	(422)	—	(9,308)
Allowance for equity funds used during construction	—	3,954	—	—	3,954
Gain on non-utility properties	—	50	—	—	50
Income tax expense (benefit) on other income and expenses	(652)	2,616	(63)	816	2,717
Net other income (loss)	1,681	(6,730)	47	(2,100)	(7,102)
Interest:					
Interest expense	1,711	38,288	2,251	(2,333)	39,917
Allowance for borrowed funds used during construction	—	(1,909)	(154)	—	(2,063)
Net interest expense	1,711	36,379	2,097	(2,333)	37,854
Equity earnings of subsidiaries	64,748	—	—	(64,748)	—
Net income	\$ 65,584	\$ 61,905	\$ 2,863	\$ (64,768)	\$ 65,584

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATING STATEMENT OF INCOME
For the Year Ended December 31, 2017

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
	(In thousands)				
Operating revenue	\$ —	\$ 635,604	\$ 40,509	\$ —	\$ 676,113
Operating expenses:					
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	—	83,163	10,163	—	93,326
Other operations	—	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)	33,313	1,405	1,059	35,279
Property and other taxes	(4)	21,778	3,023	—	24,797
Total operating (income) expenses	(408)	532,872	36,122	444	569,030
Net operating income	408	102,732	4,387	(444)	107,083
Other Income and Expenses:					
Non-regulated revenue	1,985	14,608	1,814	(2,509)	15,898
Non-regulated expenses	—	(8,139)	(1,251)	—	(9,390)
Other components of net periodic benefit cost	—	(9,032)	(556)	—	(9,588)
Allowance for equity funds used during construction	—	3,750	—	—	3,750
Gain on sale of non-utility properties	—	663	—	—	663
Income tax expense on other income and expenses	(809)	(1,714)	(47)	1,022	(1,548)
Net other income (loss)	1,176	136	(40)	(1,487)	(215)
Interest:					
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
Equity earnings of subsidiaries	72,487	—	—	(72,487)	—
Net income	\$ 72,940	\$ 70,071	\$ 2,362	\$ (72,433)	\$ 72,940

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATING STATEMENT OF INCOME
For the Year Ended December 31, 2016

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
	(In thousands)				
Operating revenue	\$ —	\$ 570,514	\$ 38,856	\$ —	\$ 609,370
Operating expenses:					
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	—	77,247	10,354	—	87,601
Other operations	—	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)	27,125	1,498	1,010	29,235
Property and other taxes	—	20,331	2,900	—	23,231
Total operating (income) expenses	(178)	491,919	34,584	409	526,734
Net operating income	178	78,595	4,272	(409)	82,636
Other Income and Expenses:					
Non-regulated revenue	1,850	15,114	2,006	(2,385)	16,585
Non-regulated expenses	—	(10,122)	(1,323)	—	(11,445)
Other components of net periodic benefit cost	—	(10,754)	(119)	—	(10,873)
Gain on sale of non-utility properties	—	(146)	—	—	(146)
Income tax expense (benefit) on other income and expenses	(754)	2,406	(205)	972	2,419
Net other income (loss)	1,096	(3,502)	359	(1,413)	(3,460)
Interest:					
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
Equity earnings of subsidiaries	48,158	—	—	(48,158)	—
Net income	\$ 48,675	\$ 45,316	\$ 2,785	\$ (48,101)	\$ 48,675

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2018

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
	(In thousands)				
Operating activities:					
Net income	\$ 65,584	\$ 61,905	\$ 2,863	\$ (64,768)	\$ 65,584
Adjustments to reconcile net income to net cash provided by operating activities:					
Equity earnings of subsidiaries	(64,748)	—	—	64,748	—
Dividends received from Affiliates	36,043	—	—	(36,043)	—
Depreciation and amortization	94	80,442	5,258	(87)	85,707
Change in value of life insurance contract	—	2,334	—	—	2,334
Stock-based compensation	3,141	—	—	—	3,141
Gain on sale of non-utility properties	—	(50)	—	—	(50)
Changes in normalized deferred income taxes	—	20,909	—	—	20,909
Allowance for equity funds used during construction	—	(3,954)	—	—	(3,954)
Changes in operating assets and liabilities	(290)	16,943	(170)	—	16,483
Other changes in noncurrent assets and liabilities	(348)	(12,284)	1,390	107	(11,135)
Net cash provided by operating activities	39,476	166,245	9,341	(36,043)	179,019
Investing activities:					
Utility plant expenditures	—	(261,456)	(10,251)	—	(271,707)
Proceeds from sale of non-utility assets	—	59	—	—	59
Change in affiliate advances	(689)	19	53	617	—
Issuance of affiliate short-term borrowings	(23,700)	—	—	23,700	—
Collection of affiliate short-term debt	20,000	—	—	(20,000)	—
Collection of affiliate long-term debt	1,635	—	—	(1,635)	—
Life insurance benefits	—	3,491	—	—	3,491
Purchase of life insurance	—	(4,925)	—	—	(4,925)
Net cash used in investing activities	(2,754)	(262,812)	(10,198)	2,682	(273,082)
Financing Activities:					
Short-term borrowings	20,000	131,000	—	—	151,000
Repayment of short-term borrowings	(20,000)	(341,000)	—	—	(361,000)
Change in affiliate advances	17	(93)	693	(617)	—
Proceeds from affiliate short-term borrowings	20,000	—	3,700	(23,700)	—
Repayment of affiliates short-term debt	(20,000)	—	—	20,000	—
Repayment of affiliates long-term debt	—	—	(1,635)	1,635	—
Issuance of long-term debt, net of expenses	—	299,383	—	—	299,383
Retirement of long-term debt	—	(16,200)	(332)	—	(16,532)
Advances and contribution in aid of construction	—	18,218	394	—	18,612
Refunds of advances for construction	—	(7,279)	(18)	—	(7,297)
Repurchase of common stock	(1,645)	—	—	—	(1,645)
Dividends paid to non-affiliates	(36,043)	—	—	—	(36,043)
Dividends paid to affiliates	—	(34,624)	(1,419)	36,043	—
Net cash (used in) provided by financing activities	(37,671)	49,405	1,383	33,361	46,478
Change in cash, cash equivalents, and restricted cash	(949)	(47,162)	526	—	(47,585)
Cash, cash equivalents, and restricted cash at beginning of period	4,728	81,401	9,171	—	95,300
Cash, cash equivalents, and restricted cash at end of year	\$ 3,779	\$ 34,239	\$ 9,697	\$ —	\$ 47,715

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

CALIFORNIA WATER SERVICE GROUP
CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2017

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
	(In thousands)				
Operating activities:					
Net income	\$ 72,940	\$ 70,071	\$ 2,362	\$ (72,433)	\$ 72,940
Adjustments to reconcile net income to net cash provided by operating activities:					
Equity earnings of subsidiaries	(72,487)	—	—	72,487	—
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	13,101	2,573	37	15,965
Net cash provided by operating activities	38,666	134,218	9,521	(34,563)	147,842
Investing activities:					
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	—
Collection of affiliate long-term debt	1,356	—	—	(1,356)	—
Life insurance benefits	—	1,558	—	—	1,558
Purchase of life insurance	—	(5,605)	—	—	(5,605)
Net cash used in investing activities	(1,086)	(199,917)	(7,185)	1,617	(206,571)
Financing Activities:					
Short-term borrowings	—	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 (used in) provided by financing activities	(38,068)	133,505	(289)	32,946	128,094
Change in cash, cash equivalents, and restricted cash	(488)	67,806	2,047	—	69,365
Cash, cash equivalents, and restricted cash at beginning of period	5,216	13,595	7,124	—	25,935
Cash, cash equivalents, and restricted cash at end of year	\$ 4,728	\$ 81,401	\$ 9,171	\$ —	\$ 95,300

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

16 CONDENSED CONSOLIDATING FINANCIAL STATEMENTS (Continued)

California Water Service Group
CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2016

	Parent Company	Cal Water	All Other Subsidiaries	Consolidating Adjustments	Consolidated
	(In thousands)				
Operating activities:					
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
Loss 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	37,008	147,097	9,420	(33,081)	160,444
Investing activities:					
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)
Net cash used in investing activities	(534)	(203,734)	(4,627)	(22,010)	(230,905)
Financing Activities:					
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)
Dividends paid to non-affiliates	(33,081)	—	—	—	(33,081)
Repurchase of common stock	(744)	—	—	—	(744)
Dividends paid to affiliates	—	(32,105)	(976)	33,081	—
Net cash (used in) provided by financing activities	(31,840)	65,516	(1,717)	55,091	87,050
Change in cash, cash equivalents, and restricted cash	4,634	8,879	3,076	—	16,589
Cash, cash equivalents, and restricted cash at beginning of period	582	4,716	4,048	—	9,346
Cash, cash equivalents, and restricted cash at end of year	\$ 5,216	\$ 13,595	\$ 7,124	\$ —	\$ 25,935

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

17 IMMATERIAL RESTATEMENT OF PRIOR PERIOD FINANCIAL STATEMENTS

Subsequent to the issuance of the Company's Consolidated Financial Statements for the year ended December 31, 2017, the Company identified an immaterial computational error related to the amount of authorized revenue recorded pursuant to the Company's pension and health care cost recovery balancing accounts. In accordance with the 2015 GRC, the Company adjusts the revenue and corresponding balancing accounts quarterly to reflect actual pension and health care costs, subject to certain limitations prescribed by the 2015 GRC. The error does not impact the billings to customers or the cash collected from customers in this GRC period, which ends on December 31, 2019. As provided for in the 2015 GRC, the amounts included in the balancing account will be recovered from or refunded to customers during the next GRC period.

The Company corrected the error in the accompanying Consolidated Financial Statements for the year ended December 31, 2017. The Company believes the correction of the error is immaterial to the previously issued Consolidated Financial Statements for prior periods.

The corrections to the Company's Consolidated Statement of Income for the year ended December 31, 2017 were as follows:

Consolidated Statement of Income

	2017				
	As Previously Reported	Adjustments (a)	As Adjusted	Corrections	As Corrected
	(In thousands, except per share data)				
Operating revenue	\$ 666,890	\$ —	\$ 666,890	\$ 9,223	\$ 676,113
Operating expenses:					
Income taxes	28,928	2,887	31,815	3,464	35,279
Total operating expenses	572,267	(6,701)	565,566	3,464	569,030
Net operating income	94,623	6,701	101,324	5,759	107,083
Net income	\$ 67,181	\$ —	\$ 67,181	\$ 5,759	\$ 72,940
Earnings per share:					
Basic	\$ 1.40	\$ —	\$ 1.40	\$ 0.12	\$ 1.52
Diluted	\$ 1.40	\$ —	\$ 1.40	\$ 0.12	\$ 1.52

(a) Reflects the retrospective adoption of ASU 2017-07 (see Note 2). The Company adopted this guidance effective January 1, 2018.

CALIFORNIA WATER SERVICE GROUP
Notes to Consolidated Financial Statements (Continued)
December 31, 2018, 2017, and 2016
Dollar amounts in thousands unless otherwise stated

17 IMMATERIAL RESTATEMENT OF PRIOR PERIOD FINANCIAL STATEMENTS (Continued)

The corrections to the Company's Consolidated Balance Sheet as of December 31, 2017 were as follows:

					December 31, 2017		
					As Previously Reported	Corrections	As Corrected
					(In thousands, except per share data)		
ASSETS							
Other assets:							
Regulatory assets		\$	401,147	\$	4,335	\$	405,482
Total other assets			464,537		4,335		468,872
TOTAL ASSETS		\$	2,740,375	\$	4,335	\$	2,744,710
CAPITALIZATION AND LIABILITIES							
Capitalization:							
Retained earnings		\$	356,753	\$	5,759	\$	362,512
Total common stockholders' equity			693,462		5,759		699,221
Total capitalization			1,209,255		5,759		1,215,014
Deferred income taxes			192,946		1,671		194,617
Regulatory liabilities			179,706		(3,095)		176,611
TOTAL CAPITALIZATION AND LIABILITIES		\$	2,740,375	\$	4,335	\$	2,744,710

The corrections to the Company's Consolidated Statement of Cash Flows for the year ended December 31, 2017 were as follows:

					2017		
					As Previously Reported	Corrections	As Corrected
					(In thousands)		
Operating activities:							
Net income		\$	67,181	\$	5,759	\$	72,940
Other changes in noncurrent assets and liabilities			19,511		(5,759)		13,752
Net cash provided by operating activities		\$	147,842	\$	—	\$	147,842

Other than for the correction to net income, retained earnings, and total stockholders' equity shown above, the corrections had no impact to the Consolidated Statement of Common Stockholders' Equity for the year ended December 31, 2017.

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, 2018. Based on that evaluation, we concluded that our disclosure controls and procedures were not effective due to a material weakness in internal control over financial reporting described below.

In connection with the Company's Annual Report on Form 10-K for the year ended December 31, 2017, filed on March 1, 2018, the CEO and CFO evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of December 31, 2017. Based upon those evaluations, the CEO and CFO concluded that the Company's disclosure controls and procedures were effective as of December 31, 2017. Subsequent to that evaluation and as a result of a computational error identified by management, the CEO and CFO concluded that the Company's disclosure controls and procedures were not effective as of December 31, 2017, and December 31, 2018, due to the material weakness described below relating to the accounting for regulatory assets and liabilities, specifically controls over the accuracy and completeness of the pension and healthcare cost balancing accounts as they relate to the values authorized in the 2015 General Rate Case (GRC).

Notwithstanding the material weakness described below, based on the additional analysis and other post-closing procedures performed, the Company believes the audited Consolidated Financial Statements and other financial information included in this Annual Report on Form 10-K, are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

Management's Annual 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, 2018. 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)". As a result of the material weakness in internal control over financial reporting described below, management has concluded that, our internal control over financial reporting was not effective as of December 31, 2018. Our independent registered public accounting firm, Deloitte & Touche LLP, has audited the effectiveness of our internal control over financial reporting as of December 31, 2018, as stated in their report, which is included in Item 8 and incorporated herein.

A material weakness, as defined in Exchange Act Rule 12b-2, is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis.

Identification of the Material Weakness in Internal Controls over Financial Reporting: The Company did not design and maintain effective internal controls over its accounting for regulatory assets and liabilities, specifically controls over the accuracy and completeness of the pension balancing (PCBA) and healthcare balancing (HCBA) accounts as they relate to the amounts authorized in the 2015 GRC. Each account was initially recorded using an incorrect input amount from the 2015 GRC. The material weakness resulted in an error to revenue, regulatory assets, and regulatory liabilities balances for the year ended December 31, 2017 and for the first three quarters of 2018, included in the Company's financial statements, that was identified during the fourth quarter of 2018. The error was corrected by revising the financial information for the prior year and for the three quarters of 2018 presented herein. Refer to Note 17 to the audited Consolidated Financial Statements for further information.

Changes in Internal Control over Financial Reporting: Other than the material weakness noted above, there were no changes in the Company's internal controls over financial reporting that occurred during the quarter ended December 31, 2018, that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

Plan for Remediation of the Material Weakness in Internal Control over Financial Reporting: Company management, with the oversight of the Audit Committee of the Board of Directors, is actively engaged in the planning for and implementation of remediation efforts to address the material weakness. Management plans to implement the following changes in order to remediate the material weakness:

- Management will revise the design of the following existing control. The accounting function will prepare the detailed calculations of the balancing account revenue for the PCBA and HCBA accounts. That calculation will be reviewed

monthly by the Director of Financial Reporting, and then provided as part of the package to be reviewed by the Regulatory Accounting and Rates Teams monthly. The review will include a validation of all assumptions and inputs used to determine the balancing account revenue and related balance sheet accounts.

- Management will implement the following new control. When a new GRC is approved or there is a rate case settlement, the Accounting and Rates teams will review GRC provisions/events/requirements that have financial reporting impacts. The Accounting Department will prepare a memo outlining the specific accounting procedures for each balancing account and will include the applicable calculations and documents supporting the proposed financial reporting impact resulting from the GRC. These documents will be provided to the Rate Department to be reviewed and approved.

Management is committed to continuous improvement of the Company's financial reporting controls and will continue to diligently review the Company's internal controls over financial reporting. As management continues to evaluate and work to improve internal controls over financial reporting, the Company may determine to take additional measures to address the material weakness or determine to modify certain of the remediation measures described above.

Management has addressed and corrected the computation error and is implementing the remediation plan during the first quarter of 2019.

Item 9B. *Other Information.*

On February 27, 2019, the Company filed with the Delaware Secretary of State a Certificate of Elimination of Series D Participating Preferred Stock, which returned the 221,000 shares that had previously been designated as Series D Preferred Stock but had never been issued to the status of preferred shares of the Company, without designation as to series.

The foregoing summary of the Certificate of Elimination is qualified in its entirety by reference to the full text of the Certificate of Elimination, a copy of which is attached as Exhibit 4.2.

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 2018 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> within four business days of such amendment or waiver.

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 2018 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 2018 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	—	—	730,185
Equity compensation plans not approved by security holders	—	—	—
Total	—	\$ —	730,185

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 2018 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 2018 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	Certificate of Elimination of the Series D Participating Preferred Stock, as filed with Delaware Secretary of State on February 27, 2019
4.3	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)
4.4	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)
4.5	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)
4.6	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)
4.7	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)
4.8	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)
4.9	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)
4.1	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)
4.11	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)
4.12	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)

Table of Contents

Exhibit Number	
4.13	<u>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)</u>
4.14	<u>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)</u>
4.15	<u>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)</u>
4.16	<u>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)</u>
4.17	<u>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)</u>
4.18	<u>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).</u>
4.19	<u>Sixty-First Supplemental Indenture dated as of September 13, 2018, between California Water Service Company and U.S. Bank National Association, as Trustee, covering Floating Rate First Mortgage Bonds due 2020, Series UUU. (Exhibit 4.1 to Quarterly Report on form 10-Q filed November 1, 2018).</u>
4.20	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.
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	<u>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).</u>
10.3	<u>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).</u>
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)
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)

Table of Contents

Exhibit Number	
10.12	<u>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)</u>
10.13	<u>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).</u>
10.14	<u>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).</u>
10.15	<u>Executive Severance Plan (Exhibit 10.24 to Annual Report on Form 10-K for the year ended December 31, 1998)*</u>
10.16	<u>California Water Service Group Long-Term Incentive Plan (filed as Appendix A of the California Water Service Group proxy statement dated March 17, 2000)*</u>
10.17	<u>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)*</u>
10.18	<u>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)*</u>
10.19	<u>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)*</u>
10.20	<u>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)</u>
10.21	<u>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)</u>
10.22	<u>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)*</u>
10.23	<u>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))*</u>
10.24	<u>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)*</u>
10.25	<u>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)</u>
10.26	<u>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)*</u>
10.27	<u>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)</u>
10.28	<u>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)</u>
10.29	<u>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)</u>
10.30	<u>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)</u>
10.31	<u>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)</u>
10.32	<u>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)</u>
10.33	<u>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)</u>

Table of Contents

Exhibit Number	
10.34	<u>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)</u>
10.35	<u>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)</u>
21.0	<u>Subsidiaries of the Registrant</u>
23.1	<u>Consent of Independent Registered Public Accounting Firm</u>
31.1	<u>Chief Executive Officer certification of financial statements pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
31.2	<u>Chief Financial Officer certification of financial statements pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
32.0	<u>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</u>
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

* 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: February 28, 2019

[Table of Contents](#)

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: February 28, 2019
<u>/s/ GREGORY E. ALIFF</u> GREGORY E. ALIFF	Member, Board of Directors	Date: February 28, 2019
<u>/s/ TERRY P. BAYER</u> TERRY P. BAYER	Member, Board of Directors	Date: February 28, 2019
<u>/s/ SHELLY M. ESQUE</u> SHELLY M. ESQUE	Member, Board of Directors	Date: February 28, 2019
<u>/s/ EDWIN A. GUILLES</u> EDWIN A. GUILLES	Member, Board of Directors	Date: February 28, 2019
<u>/s/ THOMAS M. KRUMMEL</u> THOMAS M. KRUMMEL, M.D.	Member, Board of Directors	Date: February 28, 2019
<u>/s/ RICHARD P. MAGNUSON</u> RICHARD P. MAGNUSON	Member, Board of Directors	Date: February 28, 2019
<u>/s/ CAROL M. POTTENGER</u> CAROL M. POTTENGER	Member, Board of Directors	Date: February 28, 2019
<u>/s/ LESTER A. SNOW</u> LESTER A. SNOW	Member, Board of Directors	Date: February 28, 2019
<u>/s/ MARTIN A. KROPELNICKI</u> MARTIN A. KROPELNICKI	President and Chief Executive Officer; Principal Executive Officer; Member, Board of Directors	Date: February 28, 2019
<u>/s/ THOMAS F. SMEGAL III</u> THOMAS F. SMEGAL III	Vice President, Chief Financial Officer and Treasurer; Principal Financial Officer	Date: February 28, 2019
<u>/s/ DAVID B. HEALEY</u> DAVID B. HEALEY	Vice President, Corporate Controller and Assistant Treasurer; Principal Accounting Officer	Date: February 28, 2019

**CERTIFICATE OF ELIMINATION OF THE
SERIES D PARTICIPATING PREFERRED STOCK OF
CALIFORNIA WATER SERVICE GROUP**

Pursuant to Section 151(g)
of the General Corporation Law
of the State of Delaware

California Water Service Group, a corporation organized and existing under the laws of the State of Delaware (the “**Corporation**”), in accordance with the provisions of Section 151(g) of the General Corporation Law of the State of Delaware (the “**DGCL**”), hereby certifies as follows:

1. That, pursuant to the provisions of Section 151(g) of the DGCL and authority granted in the Certificate of Incorporation of the Corporation, as theretofore amended, the Board of Directors of the Corporation (the “**Board**”), by resolution duly adopted, authorized the issuance of a series of 221,000 shares of Series D Participating Preferred Stock, par value \$0.01 per share (the “**Series D Preferred Stock**”), and established the voting powers, preferences and relative, participating, optional and other special rights of the shares of such series, and the qualifications, limitations or restrictions thereof, and, on September 16, 1999, filed a Certificate of Designation with respect to such Series D Preferred Stock in the office of the Secretary of State of the State of Delaware.

2. That no shares of said Series D Preferred Stock are outstanding and no shares thereof will be issued subject to the Certificate of Designation.

3. That the Board has adopted the following resolutions:

WHEREAS, by resolution of the Board of Directors (the “**Board**”) of California Water Service Group, a Delaware corporation (the “**Corporation**”) and by a Certificate of Designation (the “**Certificate of Designation**”) filed in the office of the Secretary of State of the State of Delaware on September 16, 1999, the Corporation authorized the issuance of 221,000 shares of preferred stock designated as “Series D Participating Preferred Stock” (the “**Series D Preferred Stock**”) and established the voting powers, preferences and relative, participating, optional and other special rights of the shares of such series, and the qualifications, limitations or restrictions thereof;

WHEREAS, as of the date hereof, no shares of Series D Preferred Stock are outstanding and no shares of such Series D Preferred Stock will be issued subject to said Certificate of Designation; and

WHEREAS, the Board has determined that it is advisable and in the best interests of the Corporation and its shareholders that all references to the Series D Preferred Stock set forth in the Certificate of Designation be eliminated from the Certificate of Incorporation of the Corporation, as heretofore amended (the “**Certificate of Incorporation**”).

NOW, THEREFORE, BE IT RESOLVED, that the officers of the Corporation be, and hereby are, authorized and directed to file a Certificate of Elimination (the “**Certificate of Elimination**”) with the office of the Secretary of State of the State of Delaware setting forth a copy of these resolutions;

RESOLVED FURTHER, that when the Certificate of Elimination setting forth these resolutions becomes effective, it shall have the effect of eliminating from the Certificate of Incorporation all references to the Series D Preferred Stock set forth in the Certificate of Designation and all of the shares that were designated as Series D Preferred Stock shall be returned to the status of preferred shares of the Corporation, without designation as to series; and

RESOLVED FURTHER, that the officers of the Corporation be, and each of them hereby is, authorized, empowered and directed, in the name and on behalf of the Corporation, to take or cause to be taken all such other actions and to execute, acknowledge and deliver all such other instruments as the officers, or any one or more of them, approve as necessary, appropriate or desirable in order to carry out and perform the purposes and intent of the foregoing resolutions, the taking of such actions or execution of such instruments to be conclusive evidence of the necessity or desirability thereof.

4. That, pursuant to the provisions of Section 151(g) of the DGCL, accordingly, all references to the Series D Preferred Stock set forth in the Certificate of Designation be, and hereby are, eliminated from the Certificate of Incorporation, as heretofore amended, of the Corporation and all of the shares that were designated as Series D Preferred Stock are returned to the status of preferred shares of the Corporation, without designation as to series.

IN WITNESS WHEREOF, California Water Service Group has caused this certificate to be duly executed this 27th day of February, 2019.

CALIFORNIA WATER SERVICE GROUP

By: /s/ Martin A. Kropelnicki

Name: Martin A. Kropelnicki

Title: President and Chief Executive Officer

Subsidiaries of the Registrant

<u>Subsidiary Name</u>	<u>State of Incorporation</u>	<u>Business Name</u>
California Water Service Company	California	California Water Service Company
CWS Utility Services	California	CWS Utility Services
New Mexico Water Service Company	New Mexico	New Mexico Water Service Company
Washington Water Service Company	Washington	Washington Water Service Company
Hawaii Water Service Company, Inc.	Hawaii	Hawaii Water Service Company
HWS Utility Services LLC	Hawaii	HWS Utility Services

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in Registration Statement Nos. 333-158484 and 333-181329 on Form S-3 and Nos.333-60810, 333-127495, and 333-228824 on Form S-8 of our report dated February 28, 2019, relating to the consolidated financial statements of California Water Service Group, and California Water Service Group's internal control over financial reporting (which report expresses an adverse opinion on the effectiveness of the Company's internal control over financial reporting because of a material weakness), appearing in this Annual Report on Form 10-K of California Water Service Group for the year ended December 31, 2018.

/s/ DELOITTE & TOUCHE LLP

San Francisco, California

February 28, 2019

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
CERTIFICATION**

I, Martin A. Kropelnicki, certify that:

1. I have reviewed this annual report on Form 10-K of California Water Service Group;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(c)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2019

By: /s/ MARTIN A. KROPELNICKI

Martin A. Kropelnicki
President and Chief Executive Officer

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
CERTIFICATION**

I, Thomas F. Smegal III, certify that:

1. I have reviewed this annual report on Form 10-K of California Water Service Group;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(c)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2019

By: /s/ THOMAS F. SMEGAL III

Thomas F. Smegal III
Vice President, Chief Financial Officer and Treasurer

**CERTIFICATION OF CEO AND CFO
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, each of the undersigned hereby certifies, in his capacity as an officer of California Water Service Group, that the Annual Report of California Water Service Group on Form 10-K for the period ended December 31, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Annual Report"), fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, and that the information contained in the Annual Report fairly presents, in all material respects, the financial condition and results of operations of California Water Service Group.

Date: February 28, 2019

By: /s/ MARTIN A. KROPELNICKI

MARTIN A. KROPELNICKI
Chief Executive Officer
California Water Service Group

Date: February 28, 2019

By: /s/ THOMAS F. SMEGAL III

THOMAS F. SMEGAL III
Chief Financial Officer
California Water Service Group