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# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

# FORM 10-Q

**(Mark One)**

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

**For the quarterly period ended March 31, 2013**

**or**

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

**For the transition period from to**

**Commission file number 1-13883**

# CALIFORNIA WATER SERVICE GROUP

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware**<br>(State or other jurisdiction of incorporation or organization) | **77-0448994**<br>(I.R.S. Employer identification No.) |
| **1720 North First Street, San Jose, CA.**<br>(Address of principal executive offices) | **95112**<br>(Zip Code) |

**408-367-8200**
(Registrant's telephone number, including area code)

**Not Applicable**
(Former name, former address and former fiscal year, if changed since last report)

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

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

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

| | |
|---|---|
| Large accelerated Filer ☒ | Accelerated filer ☐ |
| Non-accelerated filer ☐<br>(Do not check if a smaller reporting company) | Smaller reporting company ☐ |

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. Common shares outstanding as of May 1, 2013 — 47,728,775

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PART I FINANCIAL INFORMATION

Item 1.

FINANCIAL STATEMENTS

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

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

Unaudited
(In thousands, except per share data)

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| **ASSETS** | | |
| **Utility plant:** | | |
| Utility plant | $ 2,123,935 | $ 2,096,363 |
| Less accumulated depreciation and amortization | (655,345 ) | (639,307 ) |
| Net utility plant | 1,468,590 | 1,457,056 |
| **Current assets:** | | |
| Cash and cash equivalents | 127,677 | 38,790 |
| Receivables: | | |
| Customers | 29,204 | 29,958 |
| Regulatory balancing accounts | 29,607 | 34,020 |
| Other | 11,577 | 11,943 |
| Unbilled revenue | 15,551 | 15,394 |
| Materials and supplies at weighted average cost | 5,687 | 5,874 |
| Taxes, prepaid expenses and other assets | 12,393 | 10,585 |
| Total current assets | 231,696 | 146,564 |
| **Other assets:** | | |
| Regulatory assets | 353,606 | 344,419 |
| Goodwill | 2,615 | 2,615 |
| Other assets | 47,848 | 45,270 |
| Total other assets | 404,069 | 392,304 |
| | $ 2,104,355 | $ 1,995,924 |
| **CAPITALIZATION AND LIABILITIES** | | |
| **Capitalization:** | | |
| Common stock, $.01 par value; 68,000,000 shares authorized, 47,729,000 and 41,908,000 outstanding in 2013 and 2012, respectively | $ 477 | $ 419 |
| Additional paid-in capital | 327,178 | 221,013 |
| Retained earnings | 244,502 | 252,280 |
| Total common stockholders' equity | 572,157 | 473,712 |
| Long-term debt, less current maturities | 434,153 | 434,467 |
| Total capitalization | 1,006,310 | 908,179 |
| **Current liabilities:** | | |
| Current maturities of long-term debt | 46,743 | 46,783 |
| Short-term borrowings | 93,275 | 89,475 |
| Accounts payable | 44,293 | 47,199 |
| Regulatory balancing accounts | 6,132 | 5,018 |
| Accrued interest | 11,003 | 4,705 |
| Accrued expenses and other liabilities | 55,308 | 49,887 |
| Total current liabilities | 256,754 | 243,067 |
| **Unamortized investment tax credits** | 2,180 | 2,180 |
| **Deferred income taxes, net** | 158,037 | 158,846 |
| **Pension and postretirement benefits other than pensions** | 248,385 | 244,901 |
| **Regulatory and other liabilities** | 88,476 | 92,593 |
| **Advances for construction** | 186,242 | 187,584 |
| **Contributions in aid of construction** | 157,971 | 158,574 |
| **Commitments and contingencies** | — | — |
| | $ 2,104,355 | $ 1,995,924 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements





**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS)**

Unaudited
(In thousands, except per share data)

| For the three months ended | March 31, 2013 | March 31, 2012 |
|---|---|---|
| **Operating revenue** | $ 111,444 | $ 116,749 |
| **Operating expenses:** | | |
| Operations: | | |
| Water production costs | 41,697 | 38,952 |
| Administrative and general | 25,281 | 23,018 |
| Other operations | 15,645 | 23,826 |
| Maintenance | 4,133 | 5,760 |
| Depreciation and amortization | 14,629 | 13,951 |
| Income tax (benefit) expense | (1,146 ) | 28 |
| Property and other taxes | 5,435 | 4,607 |
| Total operating expenses | 105,674 | 110,142 |
| Net operating income | 5,770 | 6,607 |
| **Other income and expenses:** | | |
| Non-regulated revenue | 3,522 | 4,136 |
| Non-regulated expenses, net | (2,417 ) | (2,099 ) |
| Income tax (expense) on other income and expenses | (451 ) | (823 ) |
| Net other income | 654 | 1,214 |
| **Interest expense:** | | |
| Interest expense | 8,037 | 7,639 |
| Less: capitalized interest | (540 ) | (903 ) |
| Net interest expense | 7,497 | 6,736 |
| **Net (loss) income** | $ (1,073 ) | $ 1,085 |
| **(Loss) Earnings per share** | | |
| Basic | $ (0.03 ) | $ 0.03 |
| Diluted | $ (0.03 ) | $ 0.03 |
| **Weighted average shares outstanding** | | |
| Basic | 42,248 | 41,842 |
| Diluted | 42,248 | 41,842 |
| **Dividends declared per share of common stock** | $ 0.1600 | $ 0.1575 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements





**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

Unaudited
(In thousands)

| For the three months ended: | March 31, 2013 | March 31, 2012 |
|---|---|---|
| **Operating activities** | | |
| Net (loss) income | $ (1,073 ) | $ 1,085 |
| Adjustments to reconcile net (loss) income to net cash provided by operating activities: | | |
| Depreciation and amortization | 15,110 | 14,410 |
| Change in value of life insurance contracts | (510 ) | (1,713 ) |
| Other changes in noncurrent assets and liabilities | (38 ) | 2,802 |
| Changes in operating assets and liabilities: | | |
| Receivables | (1,645 ) | 3,524 |
| Accounts payable | (730 ) | 334 |
| Other current assets | (1,729 ) | (3,371 ) |
| Other current liabilities | 10,164 | 5,845 |
| Net cash provided by operating activities | 19,549 | 22,916 |
| **Investing activities:** | | |
| Utility plant expenditures | (32,101 ) | (28,665 ) |
| Purchase of life insurance | (1,539 ) | (1,357 ) |
| Changes in restricted cash and other changes, net | 108 | 102 |
| Net cash used in investing activities | (33,532 ) | (29,920 ) |
| **Financing activities:** | | |
| Short-term borrowings | 3,800 | 5,650 |
| Repayment of short-term borrowings | — | (2,000 ) |
| Repayment of long-term debt | (355 ) | (431 ) |
| Advances and contributions in aid of construction | 1,916 | 1,156 |
| Refunds of advances for construction | (1,621 ) | (1,974 ) |
| Issuance of common stock | 110,688 | — |
| Common stock issuance costs | (4,853 ) | — |
| Dividends paid | (6,705 ) | (6,586 ) |
| Net cash provided (used in) by financing activities | 102,870 | (4,185 ) |
| Change in cash and cash equivalents | 88,887 | (11,189 ) |
| Cash and cash equivalents at beginning of period | 38,790 | 27,203 |
| Cash and cash equivalents at end of period | $ 127,677 | $ 16,014 |
| **Supplemental information** | | |
| Cash paid for interest (net of amounts capitalized) | $ 1,061 | $ 283 |

| | | | | |
|---|---|---|---|---|
| Cash paid for income taxes | | — | | — |
| **Supplemental disclosure of non-cash activities:** | | | | |
| Accrued payables for investments in utility plant | $ | 6,959 | $ | 12,519 |
| Utility plant contribution by developers | | 1,278 | | 2,586 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements





CALIFORNIA WATER SERVICE GROUP
Notes to Unaudited Condensed Consolidated Financial Statements
March 31, 2013
(Amounts in thousands, except share and per share amounts)

Note 1. Organization and Operations and Basis of Presentation

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

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

*Basis of Presentation*

The unaudited interim financial information has been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X promulgated by the Securities and Exchange Commission (SEC) and therefore do not contain all of the information and footnotes required by GAAP and the SEC for annual financial statements. The condensed consolidated financial statements should be read in conjunction with the Company's consolidated financial statements for the year ended December 31, 2012, included in its annual report on Form 10-K as filed with the SEC on February 28, 2013.

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

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

Due to the seasonal nature of the water business, the results for interim periods are not indicative of the results for a 12-month period. Revenue and income are generally higher in the warm, dry summer months when water usage and sales are greater. Revenue and income are lower in the winter months when cooler temperatures and rainfall curtail water usage and sales.

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

Note 2. Summary of Significant Accounting Policies

*Revenue*

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

The Company's regulated water and waste water revenue requirements are authorized by the Commissions in the states in which it operates. The revenue requirements are intended to provide the Company a reasonable opportunity to recover its operating costs and earn a return on investments.

For metered customers, Cal Water recognizes revenue from rates which are designed and authorized by the California Public Utilities Commission (CPUC). Under the Water Revenue Adjustment Mechanism (WRAM), Cal Water records the adopted level





of volumetric revenues, which would include recovery of cost of service and a return on investments, as established by the CPUC for metered accounts (adopted volumetric revenues). In addition to volumetric-based revenues, the revenue requirements approved by the CPUC include service charges, flat rate charges, and other items not subject to the WRAM. The adopted volumetric revenue considers the seasonality of consumption of water based upon historical averages. The variance between adopted volumetric revenues and actual billed volumetric revenues for metered accounts is recorded as a component of revenue with an offsetting entry to a regulatory asset or liability balancing account (tracked individually for each Cal Water district) subject to certain criteria under the accounting for regulated operations being met. The variance amount may be positive or negative and represents amounts that will be billed or refunded to customers in the future.

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

The balances in the WRAM and MCBA assets and liabilities accounts will fluctuate on a monthly basis depending upon the variance between adopted and actual results. The recovery or refund of the WRAM is netted against the MCBA over- or under-recovery for the corresponding district and is interest bearing at the current 90 day commercial paper rate. At the end of any calendar year, Cal Water files with the CPUC to refund or collect the balance in the accounts. Most undercollected net WRAM and MCBA receivable balances are collected over 12 and 18 months. Cal Water defers net WRAM and MCBA operating revenues and associated costs whenever the net receivable balances are estimated to be collected more than 24 months after the respective reporting periods in which it was recognized. The deferred net WRAM and MCBA revenues and associated costs were determined using forecasts of rate payer consumption trends in future reporting periods and the timing of when the CPUC will authorize Cal Water's filings to recover the undercollected balances. Deferred net WRAM and MCBA revenues and associated costs will be recognized as revenues and costs in future periods when collection is within twenty-four months of the respective reporting period.

The change to deferred net WRAM and MCBA balances during the first quarter of 2013 was:

| | Operating Revenues | Operating Costs | Income Before Income Taxes |
|---|---|---|---|
| Net WRAM and MCBA deferral as of December 31, 2012 | $ 882 | $ 719 | $ 163 |
| Less: reversal of prior year deferral during the first quarter of 2013 | (16) | 25 | (41) |
| Add: net WRAM and MCBA deferral the first quarter of 2013 | 1,125 | 967 | 158 |
| Net amount recorded during the first quarter of 2013 | 1,109 | 992 | 117 |
| Net WRAM and MCBA deferral as of March 31, 2013 | $ 1,991 | $ 1,711 | $ 280 |

The change to deferred net WRAM and MCBA balances during the first quarter of 2012 was:

| | Operating Revenues | Operating Costs | Income Before Income Taxes |
|---|---|---|---|
| Net WRAM and MCBA deferral as of December 31, 2011 | $ 12,864 | $ 10,492 | $ 2,372 |
| Less: reversal of prior year deferral during the first quarter of 2012 | (8,846) | (7,215) | (1,631) |
| Add: net WRAM and MCBA deferral the first quarter of 2012 | 110 | 90 | 20 |
| Net amount recorded during the first quarter of 2012 | (8,736) | (7,125) | (1,611) |
| Net WRAM and MCBA deferral as of March 31, 2012 | $ 4,128 | $ 3,367 | $ 761 |



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The net WRAM and MCBA under- or overcollected balances are:

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Net short-term receivable | $ 29,607 | $ 34,020 |
| Net long-term receivable | 19,031 | 12,051 |
| Total receivable | $ 48,638 | $ 46,071 |
| Net short-term payable | $ 338 | $ 371 |
| Net long-term payable | 374 | 119 |
| Total payable | $ 712 | $ 490 |

Flat rate customers are billed in advance at the beginning of the service period. The revenue is prorated so that the portion of revenue applicable to the current period is included in that period's revenue, with the balance recorded as unearned revenue on the balance sheet and recognized as revenue when earned in the subsequent accounting period. Unearned revenue liability was $1.7 million as of March 31, 2013 and December 31, 2012. This liability is included in "accrued expenses and other liabilities" on the condensed consolidated balance sheets.

Cash and Cash Equivalents

Cash equivalents include highly liquid investments with maturities of three months or less. Cash and cash equivalents was $127.7 million and $38.8 million as of March 31, 2013 and December 31, 2012, respectively. The $105.8 million net cash proceeds from the March 26, 2013 equity offering was included in Cash and cash equivalents as of March 31, 2013. Restricted cash was presented on the condensed consolidated balance sheet as "taxes, prepaid expenses and other assets" and was $2.2 million and $2.3 million as of March 31, 2013 and December 31, 2012, respectively.

Adoption of New Accounting Standards

On February 1, 2013, the Financial Accounting Standards Board issued an accounting standards update (ASU) for the recognition, measurement, and disclosure of obligations resulting from joint and several liability arrangements. The ASU will impact the Company's recognition, measurement, and disclosure requirements for guarantees on third party debt of its 100%-owned subsidiaries. The ASU effective date for the Company's interim and annual reporting is January 1, 2014. The adoption of the new ASU in 2014 is not expected to have a material impact on the Company's condensed consolidated financial statements.

Note 3. Stock-based Compensation

*Equity Incentive Plan*

The Company's equity incentive plan was approved by stockholders on April 27, 2005. The Company is authorized to issue awards up to 2,000,000 shares of common stock.

During the three months ended March 31, 2013 and 2012, the Company granted annual Restricted Stock Awards (RSAs) of 70,557 and 89,980 shares, respectively, of common stock to officers and directors of the Company and no RSAs were cancelled. Employee RSAs granted in 2013 vest over 36 months and RSAs granted in 2012 vest over 48 months. Director RSAs generally vest at the end of 12 months. During the first three months of 2013 and 2012, the shares granted were valued at $20.62 and $17.98 per share, respectively, based upon the fair market value of the Company's common stock on the date of grant.

On March 1, 2013, the Company granted performance-based Restricted Stock Unit Awards (RSUs) of 50,267 shares of common stock to officers. Each award reflects a target number of shares that may be issued to the award recipient. The awards may be earned upon the completion of the three-year performance period ending February 28, 2016. 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, and water quality standards. Depending on the results achieved during the three-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 for financial reporting until earned. The RSUs are recognized as expense ratably over the three year performance period using a fair market value of $20.62 per share and an estimate of RSUs earned during the performance period.



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The Company has recorded compensation costs for the RSAs and RSUs in Operating Expense in the amount of $0.4 million and $0.3 million for the three months ended March 31, 2013 and March 31, 2012, respectively.

Note 4. Equity

The Company's changes in equity for the three months ended March 31, 2013 were as follows:

| | Total Stockholders' Equity |
|---|---|
| Balance at December 31, 2012 | $ 473,712 |
| Common stock issued, net | 105,835 |
| Share-based compensation expense | 388 |
| Common stock dividends declared | (6,705) |
| Net loss | (1,073) |
| Balance at March 31, 2013 | $ 572,157 |

On March 26, 2013, the Company sold 5,750,000 shares of its common stock in an underwritten public offering for cash proceeds of approximately $105.8 million, net of $4.9 million underwriting discounts and commissions and offering expenses. The net proceeds from the sale of common stock were added to our general funds to be used for general corporate purposes. In April 2013, the Company used a portion of the net proceeds from the offering to repay outstanding borrowings on the Company and Cal Water lines of credit of $68.3 million and $25.0 million, respectively. The issuance of shares of common stock was applied to the condensed consolidated financial statements for the first quarter ended March 31, 2013.

Note 5. Earnings Per Share Calculations

The computations of basic and diluted earnings per share are noted below. Basic earnings per share are computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts were exercised or converted into common stock. RSAs are included in the common shares outstanding because the shares have all the same voting and dividend rights as issued and unrestricted common stock.

The Company's weighted average number of common shares outstanding during the three months ended March 31, 2013 has been adjusted for the March 26, 2013 equity offering. A total of 333,856 shares of Stock Appreciation Rights were vested and outstanding and all were anti-dilutive as of March 31, 2013 and March 31, 2012 as shown in the table below.

| | Three Months Ended March 31 | |
|---|---|---|
| | 2013 | 2012 |
| Net (loss) income available to common stockholders | $ (1,073) | $ 1,085 |
| Weighted average common shares, basic | 42,248 | 41,842 |
| Dilutive common stock options (treasury method) | — | — |
| Shares used for dilutive computation | 42,248 | 41,842 |
| Net (loss) income per share - basic | $ (0.03) | $ 0.03 |
| Net (loss) income per share - diluted | $ (0.03) | $ 0.03 |

Note 6. Pension Plan and Other Postretirement Benefits

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



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

Cash payments by the Company related to pension plans and other postretirement benefit plans were $7.5 million for the three months ended March 31, 2013 and were $6.0 million during the three months ended March 31, 2012. The 2013 estimated cash contribution to the pension plans is $31.3 million and to the other postretirement benefit plans is $9.6 million.

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

| | Three Months Ended March 31 | | | |
|---|---|---|---|---|
| | Pension Plan | | Other Benefits | |
| | 2013 | 2012 | 2013 | 2012 |
| Service cost | $ 4,658 | $ 4,016 | $ 1,695 | $ 1,417 |
| Interest cost | 4,063 | 3,779 | 1,109 | 967 |
| Expected return on plan assets | (3,565) | (2,893) | (598) | (468) |
| Recognized net initial APBO (1) | N/A | N/A | 2 | 69 |
| Amortization of prior service cost | 1,541 | 1,571 | 20 | 29 |
| Recognized net actuarial loss | 2,224 | 1,926 | 916 | 764 |
| Net periodic benefit cost | $ 8,921 | $ 8,399 | $ 3,144 | $ 2,778 |

(1) APBO - Accumulated postretirement benefit obligation

Note 7. Short-term and Long-term Borrowings

On June 29, 2011, 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 $400 million. The Syndicated Credit Facilities amend, expand, and replace the Company's and its subsidiaries' existing credit facilities originally entered into on October 27, 2009. The new credit facilities extended the terms until June 29, 2016, increased the Company's and Cal Water's unsecured revolving lines of credit, and lowered interest rates and fees. The Company and subsidiaries that it designates may borrow up to $100 million under the Company's revolving credit facility. Cal Water may borrow up to $300 million under its revolving credit facility; however, all borrowings need to be repaid within 12-months unless otherwise authorized by the CPUC. 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.

Both short-term unsecured 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 and interest coverage ratio. As of March 31, 2013, the Company and Cal Water have met all borrowing covenants for both credit agreements.

As of March 31, 2013 and December 31, 2012, the outstanding borrowings on the Company lines of credit were $68.3 million and $64.5 million, respectively, and were $25.0 million as of March 31, 2013 and December 31, 2012 on the Cal Water lines of credit, respectively. For the three months ended March 31, 2013, the average borrowing rate was 2.26% compared to 1.60% for the same period last year.

Note 8. 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 bases. Measurement of the deferred tax assets and liabilities is at enacted tax rates expected to



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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.

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 us rate increases 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.

During 2012, the Company filed an application for a change in accounting method (section 481 adjustment) with the Internal Revenue Service (IRS) to implement the new repairs and maintenance deduction. The new deduction is for qualified tangible property placed into service during 2012 and prior years. The new tax regulations allow the Company to deduct a significant amount of costs previously capitalized for book and tax purposes. The 2012 repairs and maintenance deductions resulted in a federal net operating loss (NOL) of $26.0 million and a state NOL of $55.7 million. The NOL carry-forward amounts are more likely than not to be recovered and therefore require no valuation allowance. The NOL carry-forward does not begin to expire until 2033.

The American Taxpayer Relief Act of 2012 provided the Company with additional 50% first-year bonus depreciation for assets placed in service from December 31, 2012 to December 31, 2013. The federal income tax deduction was estimated at $1.6 million in 2012. The 2012 estimate will be finalized when we file the 2012 tax returns in the third quarter of 2013.

The IRS is presently auditing the Company's 2010 and 2011 federal income tax returns. It is uncertain when the IRS will complete its audit. The Company believes that the final resolution of the IRS audit will not have a material adverse impact on its financial condition or results of operations.

Note 9. Regulatory Assets and Liabilities

During 2011, the CPUC issued a decision regarding the $34.2 million of litigation proceeds previously received by Cal Water during 2008 which is being used to replace infrastructure damaged by the gasoline additive Methyl tert-butyl ether (MTBE). The decision requires use of these proceeds for costs incurred as a result of MTBE contamination with any related benefits to be provided to Cal Water customers. Such usage includes transfer of the amount to contributions in aid of construction (CIAC) for remediation or replacement project costs once complete. Usage of the proceeds is reported to the CPUC through an Advice Letter or General Rate Case filing. As of December 31, 2012, $22.4 million of the proceeds was recorded as CIAC. Cal Water did not use any of the proceeds to replace damaged infrastructure during the first quarter of 2013. The remaining balance of $11.8 million is recorded as other long-term liabilities.

During 2011, Cal Water added balancing accounts for its pension plans and conservation program. Both balancing account effective dates were January 1, 2011. The pension plans balancing account is a two-way balancing account that tracks the differences between actual expenses and adopted rate recovery which will result in either a regulatory asset or liability. The conservation program is a one-way balancing account that tracks the differences between actual expenses and adopted rate recovery which may result in a regulatory liability if actual conservation expenses are less than adopted over the three year period ending December 31, 2013. As of March 31, 2013 and December 31, 2012, the pension balancing account was a regulatory receivable of $3.1 million and $2.4 million, respectively. The conservation balancing account was a regulatory liability of $5.6 million and $6.5 million as of March 31, 2013 and December 31, 2012, respectively.

Note 10. Commitment and Contingencies

*Commitments*

The Company has significant commitments to lease certain office spaces and water systems and to purchase water from water wholesalers. These commitments are described in Form 10-K for the year ended December 31, 2012. As of March 31, 2013, there were no significant changes from December 31, 2012.

*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

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Commission's general policy requires all proceeds from contamination litigation to be used first to pay transactional expenses, then to make ratepayers whole for water treatment costs to comply with the Commission's water quality standards. The Commission 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 Commission 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 Commission's general policy.

*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 recognized a liability of $1.3 million and $0.2 million for all known legal matters as of March 31, 2013 and March 31, 2012, respectively. 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, dependant on the nature of the settlement.

Note 11. Fair Value of Financial Assets and Liabilities

The accounting guidance for fair value measurements and disclosures (Accounting Standards Update No. 2011-04 and Accounting Standards Codification No. 270-10-45-19, effective January 1, 2012), provides a single definition of fair value and requires certain disclosures about assets and liabilities measured at fair value. A hierarchal 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 as follows:

Level 1 - Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. The types of assets and liabilities included in Level 1 are highly liquid and actively traded instruments with quoted prices.

Level 2 - Pricing inputs are other than quoted prices inactive markets, but are either directly or indirectly observable as of the reporting date. The types of assets and liabilities included in Level 2 are typically either comparable to actively traded securities or contracts, or priced with discounted cash flow or option pricing models using highly observable inputs.

Level 3 - Significant inputs to pricing have little or no observability as of the reporting date. The types of assets and liabilities included in Level 3 are those valued with models requiring significant management judgment or estimation.

Specific valuation methods include the following:

Cash equivalents, 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 1.19%.

Advances for construction fair values were estimated using broker quotes from companies that frequently purchase these investments.

| | March 31, 2013 | | | | |
|---|---|---|---|---|---|
| | | Fair Value | | | |
| | Cost | Level 1 | Level 2 | Level 3 | Total |
| Money market investments | $ 107,418 | $ 107,418 | — | — | $ 107,418 |
| Long -term debt, including current maturities | 480,896 | — | 608,302 | — | 608,302 |
| Advances for construction | 186,242 | — | 72,073 | — | 72,073 |
| Total | $ 774,556 | $ 107,418 | $ 680,375 | $ — | $ 787,793 |

| | December 31, 2012 | | | | |
|---|---|---|---|---|---|
| | | Fair Value | | | |
| | Cost | Level 1 | Level 2 | Level 3 | Total |
| Long -term debt, including current maturities | $ 481,250 | $ — | $ 613,211 | $ — | $ 613,211 |
| Advances for construction | 187,584 | — | 70,914 | — | 70,914 |
| Total | $ 668,834 | | $ 684,125 | $ — | $ 684,125 |



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Note 12. Condensed Consolidating Financial Statements

On April 17, 2009, Cal Water issued $100 million aggregate principal amount of 5.875% First Mortgage Bonds due 2019, and on November 17, 2010, Cal Water issued $100 million aggregate principal amount of 5.500% First Mortgage Bonds due 2040, all of which are fully and unconditionally guaranteed by the Company.

The following tables present the condensed consolidating balance sheets as of March 31, 2013 and December 31, 2012, the condensed consolidating statements of income (loss) for the three months ended March 31, 2013 and 2012 and the condensed consolidating statements of cash flows for the three months ended March 31, 2013 and 2012 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 consolidated subsidiaries of California Water Service Group.



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**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATING BALANCE SHEET**
**As of March 31, 2013**

**(In thousands)**

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| **Utility plant:** | | | | | |
| Utility plant | $ 930 | $ 1,951,750 | $ 178,452 | $ (7,197) | $ 2,123,935 |
| Less accumulated depreciation and amortization | (122) | (622,808) | (33,946) | 1,531 | (655,345) |
| Net utility plant | 808 | 1,328,942 | 144,506 | (5,666) | 1,468,590 |
| **Current assets:** | | | | | |
| Cash and cash equivalents | 107,418 | 18,262 | 1,997 | — | 127,677 |
| Receivables and unbilled revenue | 139 | 82,418 | 3,382 | — | 85,939 |
| Receivables from affiliates | 23,677 | 3,105 | 952 | (27,734) | — |
| Other current assets | 177 | 16,871 | 1,032 | — | 18,080 |
| Total current assets | 131,411 | 120,656 | 7,363 | (27,734) | 231,696 |
| **Other assets:** | | | | | |
| Regulatory assets | — | 351,031 | 2,575 | — | 353,606 |
| Investments in affiliates | 484,269 | — | — | (484,269) | — |
| Long-term affiliate notes receivable | 30,900 | 7,769 | — | (38,669) | — |
| Other assets | 1,335 | 42,198 | 7,133 | (203) | 50,463 |
| Total other assets | 516,504 | 400,998 | 9,708 | (523,141) | 404,069 |
| | $ 648,723 | $ 1,850,596 | $ 161,577 | $ (556,541) | $ 2,104,355 |
| **CAPITALIZATION AND LIABILITIES** | | | | | |
| **Capitalization:** | | | | | |
| Common stockholders' equity | $ 572,157 | $ 436,664 | $ 53,084 | $ (489,748) | $ 572,157 |
| Affiliate long-term debt | 7,768 | — | 30,901 | (38,669) | — |
| Long-term debt, less current maturities | — | 431,230 | 2,923 | — | 434,153 |
| Total capitalization | 579,925 | 867,894 | 86,908 | (528,417) | 1,006,310 |
| **Current liabilities:** | | | | | |
| Current maturities of long-term debt | — | 46,112 | 631 | — | 46,743 |
| Short-term borrowings | 68,275 | 25,000 | — | — | 93,275 |
| Payables to affiliates | 955 | 952 | 25,827 | (27,734) | — |
| Accounts payable | 75 | 40,241 | 3,977 | — | 44,293 |
| Accrued expenses and other liabilities | 72 | 70,081 | 2,290 | — | 72,443 |
| Total current liabilities | 69,377 | 182,386 | 32,725 | (27,734) | 256,754 |
| **Unamortized investment tax credits** | — | 2,180 | — | — | 2,180 |
| **Deferred income taxes, net** | (579) | 154,672 | 4,334 | (390) | 158,037 |
| **Pension and postretirement benefits other than pensions** | — | 248,385 | — | — | 248,385 |
| **Regulatory and other liabilities** | — | 79,786 | 8,690 | — | 88,476 |
| **Advances for construction** | — | 185,503 | 739 | — | 186,242 |
| **Contributions in aid of construction** | — | 129,790 | 28,181 | — | 157,971 |
| | $ 648,723 | $ 1,850,596 | $ 161,577 | $ (556,541) | $ 2,104,355 |



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**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATING BALANCE SHEET**
**As of December 31, 2012**

**(In thousands)**

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| **Utility plant:** | | | | | |
| Utility plant | $ 606 | $ 1,927,190 | $ 175,764 | $ (7,197) | $ 2,096,363 |
| Less accumulated depreciation and amortization | (108) | (607,992) | (32,710) | 1,503 | (639,307) |
| Net utility plant | 498 | 1,319,198 | 143,054 | (5,694) | 1,457,056 |
| **Current assets:** | | | | | |
| Cash and cash equivalents | 1,470 | 34,609 | 2,711 | — | 38,790 |
| Receivables | — | 87,482 | 3,833 | — | 91,315 |
| Receivables from affiliates | 19,367 | 3,195 | 1,152 | (23,714) | — |
| Other current assets | — | 15,535 | 924 | — | 16,459 |
| Total current assets | 20,837 | 140,821 | 8,620 | (23,714) | 146,564 |
| **Other assets:** | | | | | |
| Regulatory assets | — | 341,877 | 2,542 | — | 344,419 |
| Investments in affiliates | 492,188 | — | — | (492,188) | — |
| Long-term affiliate notes receivable | 31,218 | 7,781 | — | (38,999) | — |
| Other assets | 1,023 | 40,005 | 7,062 | (205) | 47,885 |
| Total other assets | 524,429 | 389,663 | 9,604 | (531,392) | 392,304 |
| | $ 545,764 | $ 1,849,682 | $ 161,278 | $ (560,800) | $ 1,995,924 |
| **CAPITALIZATION AND LIABILITIES** | | | | | |
| **Capitalization:** | | | | | |

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| Common stockholders' equity | $ 473,712 | $ 442,923 | $ 54,774 | $ (497,697) | $ 473,712 |
| Affiliate long-term debt | 7,781 | — | 31,218 | (38,999) | — |
| Long-term debt, less current maturities | — | 431,433 | 3,034 | — | 434,467 |
| Total capitalization | 481,493 | 874,356 | 89,026 | (536,696) | 908,179 |
| **Current liabilities:** | | | | | |
| Current maturities of long-term debt | — | 46,104 | 679 | — | 46,783 |
| Short-term borrowings | 64,475 | 25,000 | — | — | 89,475 |
| Payables to affiliates | 77 | 1,152 | 22,485 | (23,714) | — |
| Accounts payable | — | 41,352 | 5,847 | — | 47,199 |
| Accrued expenses and other liabilities | 298 | 58,293 | 1,019 | — | 59,610 |
| Total current liabilities | 64,850 | 171,901 | 30,030 | (23,714) | 243,067 |
| **Unamortized investment tax credits** | — | 2,180 | — | — | 2,180 |
| **Deferred income taxes, net** | (579) | 155,481 | 4,334 | (390) | 158,846 |
| **Pension and postretirement benefits other than pensions** | — | 244,901 | — | — | 244,901 |
| **Regulatory and other liabilities** | — | 83,942 | 8,651 | — | 92,593 |
| **Advances for construction** | — | 186,753 | 831 | — | 187,584 |
| **Contributions in aid of construction** | — | 130,168 | 28,406 | — | 158,574 |
| | $ 545,764 | $ 1,849,682 | $ 161,278 | $ (560,800) | $ 1,995,924 |



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**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATING STATEMENT OF INCOME (LOSS)**
**For the three months ended March 31, 2013**

**(In thousands)**

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| **Operating revenue** | $ — | $ 104,431 | $ 7,013 | $ — | $ 111,444 |
| **Operating expenses:** | | | | | |
| Operations: | | | | | |
| Water production costs | — | 39,441 | 2,256 | — | 41,697 |
| Administrative and general | — | 22,609 | 2,672 | — | 25,281 |
| Other | — | 14,189 | 1,583 | (127) | 15,645 |
| Maintenance | — | 3,965 | 168 | — | 4,133 |
| Depreciation and amortization | — | 13,757 | 900 | (28) | 14,629 |
| Income tax (benefit) | (136) | (727) | (629) | 346 | (1,146) |
| Taxes other than income taxes | — | 4,854 | 581 | — | 5,435 |
| **Total operating (income) expenses** | (136) | 98,088 | 7,531 | 191 | 105,674 |
| **Net operating income (loss)** | 136 | 6,343 | (518) | (191) | 5,770 |
| **Other Income and Expenses:** | | | | | |
| Non-regulated revenue | 570 | 3,182 | 532 | (762) | 3,522 |
| Non-regulated expenses, net | — | (1,920) | (497) | — | (2,417) |
| Income tax (expense) on other income and expense | (232) | (514) | (39) | 334 | (451) |
| Net other income (expense) | 338 | 748 | (4) | (428) | 654 |
| **Interest:** | | | | | |
| Interest expense | 334 | 7,727 | 612 | (636) | 8,037 |
| Less: capitalized interest | — | (379) | (161) | — | (540) |
| Net interest expense | 334 | 7,348 | 451 | (636) | 7,497 |
| **Equity earnings of subsidiaries** | (1,213) | — | — | 1,213 | — |
| **Net (loss)** | $ (1,073) | $ (257) | $ (973) | $ 1,230 | $ (1,073) |



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**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATING STATEMENT OF INCOME (LOSS)**
**For the three months ended March 31, 2012**

**(In thousands)**

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| **Operating revenue** | $ — | $ 109,825 | $ 6,924 | $ — | $ 116,749 |
| **Operating expenses:** | | | | | |
| Operations: | | | | | |
| Water production costs | — | 36,542 | 2,410 | — | 38,952 |
| Administrative and general | 36 | 20,652 | 2,330 | — | 23,018 |
| Other | — | 22,372 | 1,580 | (126) | 23,826 |
| Maintenance | — | 5,557 | 203 | — | 5,760 |
| Depreciation and amortization | (5) | 13,300 | 686 | (30) | 13,951 |
| Income tax (benefit) expense | (140) | 247 | (415) | 336 | 28 |
| Taxes other than income taxes | — | 4,059 | 548 | — | 4,607 |
| **Total operating (income) expenses** | (109) | 102,729 | 7,342 | 180 | 110,142 |
| **Net operating income (loss)** | 109 | 7,096 | (418) | (180) | 6,607 |

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| **Other Income and Expenses:** | | | | | |
| Non-regulated revenue | 471 | 3,824 | 573 | (732) | 4,136 |
| Non-regulated expenses, net | — | (1,698) | (401) | — | (2,099) |
| Income tax (expense) on other income and expense | (192) | (866) | (89) | 324 | (823) |
| Net other income | 279 | 1,260 | 83 | (408) | 1,214 |
| **Interest:** | | | | | |
| Interest expense | 314 | 7,406 | 525 | (606) | 7,639 |
| Less: capitalized interest | — | (598) | (305) | — | (903) |
| Net interest expense | 314 | 6,808 | 220 | (606) | 6,736 |
| **Equity earnings of subsidiaries** | 1,011 | — | — | (1,011) | — |
| **Net income (loss)** | $ 1,085 | $ 1,548 | $ (555) | $ (993) | $ 1,085 |



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**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**
**For the three months ended March 31, 2013**

**(In thousands)**

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| **Operating activities:** | | | | | |
| Net (loss) | $ (1,073) | $ (257) | $ (973) | $ 1,230 | $ (1,073) |
| Adjustments to reconcile net (loss) to net cash provided by (used in) operating activities: | | | | | |
| Equity earnings of subsidiaries | 1,213 | — | — | (1,213) | — |
| Dividends received from affiliates | 6,705 | — | — | (6,705) | — |
| Depreciation and amortization | 14 | 14,192 | 932 | (28) | 15,110 |
| Change in value of life insurance contracts | — | (510) | — | — | (510) |
| Other changes in noncurrent assets and liabilities | 77 | (63) | (63) | 11 | (38) |
| Changes in operating assets and liabilities: | | | | | |
| Other changes, net | (466) | 4,853 | 1,673 | — | 6,060 |
| Net cash provided by operating activities | 6,470 | 18,215 | 1,569 | (6,705) | 19,549 |
| **Investing activities:** | | | | | |
| Utility plant expenditures | (324) | (27,161) | (4,616) | — | (32,101) |
| Net changes in affiliate advances | (4,293) | 91 | (243) | 4,445 | — |
| Proceeds from affiliates long-term debt | 300 | 12 | — | (312) | — |
| Purchase of life insurance | — | (1,539) | — | — | (1,539) |
| Changes in restricted cash and other changes, net | — | 108 | — | — | 108 |
| Net cash (used in) investing activities | (4,317) | (28,489) | (4,859) | 4,133 | (33,532) |
| **Financing Activities:** | | | | | |
| Short-term borrowings | 3,800 | — | — | — | 3,800 |
| Repayment of long-term borrowings | — | (195) | (160) | — | (355) |
| Net changes in affiliate advances | 877 | (200) | 3,768 | (4,445) | — |
| Repayment of affiliates long-term borrowings | (12) | — | (300) | 312 | — |
| Advances and contributions in aid for construction | — | 1,903 | 13 | — | 1,916 |
| Refunds of advances for construction | — | (1,592) | (29) | — | (1,621) |
| Dividends paid to non-affiliates | (6,705) | — | — | — | (6,705) |
| Dividends paid to affiliates | — | (5,989) | (716) | 6,705 | — |
| Issuance of common stock, net | 105,835 | — | — | — | 105,835 |
| Net cash provided by (used in) financing activities | 103,795 | (6,073) | 2,576 | 2,572 | 102,870 |
| Change in cash and cash equivalents | 105,948 | (16,347) | (714) | — | 88,887 |
| Cash and cash equivalents at beginning of period | 1,470 | 34,609 | 2,711 | — | 38,790 |
| Cash and cash equivalents at end of period | $ 107,418 | $ 18,262 | $ 1,997 | $ — | $ 127,677 |



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**CALIFORNIA WATER SERVICE GROUP**
**CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**
**For the three months ended March 31, 2012**

**(In thousands)**

| | Parent Company | Cal Water | All Other Subsidiaries | Consolidating Adjustments | Consolidated |
|---|---|---|---|---|---|
| **Operating activities:** | | | | | |
| Net income (loss) | $ 1,085 | $ 1,548 | $ (555) | $ (993) | $ 1,085 |
| Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities: | | | | | |
| Equity earnings of subsidiaries | (1,011) | — | — | 1,011 | — |
| Dividends received from affiliates | 6,586 | — | — | (6,586) | — |
| Depreciation and amortization | 14 | 13,706 | 720 | (30) | 14,410 |
| Change in value of life insurance contracts | — | (1,713) | — | — | (1,713) |
| Other changes in noncurrent assets and liabilities | 433 | 2,365 | (40) | 44 | 2,802 |
| Changes in operating assets and liabilities: | | | | | |

| | | | | | |
|---|---|---|---|---|---|
| Other changes, net | (377) | 13,862 | (7,121) | (32) | 6,332 |
| Net cash provided by (used in) operating activities | 6,730 | 29,768 | (6,996) | (6,586) | 22,916 |
| **Investing activities:** | | | | | |
| Utility plant expenditures | — | (25,717) | (2,948) | — | (28,665) |
| Net changes in affiliate advances | (3,511) | 433 | — | 3,078 | — |
| Proceeds from affiliates long-term debt | 135 | 12 | — | (147) | — |
| Purchase of life insurance | — | (1,357) | — | — | (1,357) |
| Changes in restricted cash and other changes, net | — | 102 | — | — | 102 |
| Net cash (used in) investing activities | (3,376) | (26,527) | (2,948) | 2,931 | (29,920) |
| **Financing Activities:** | | | | | |
| Short-term borrowings | 4,650 | 1,000 | — | — | 5,650 |
| Repayment of short-term borrowings | (1,000) | (1,000) | — | — | (2,000) |
| Repayment of long-term borrowings | — | (266) | (165) | — | (431) |
| Net changes in affiliate advances | — | (124) | 3,202 | (3,078) | — |
| Repayment of affiliates long-term borrowings | (12) | — | (135) | 147 | — |
| Advances and contributions in aid for construction | — | 1,151 | 5 | — | 1,156 |
| Refunds of advances for construction | — | (1,934) | (40) | — | (1,974) |
| Dividends paid to non-affiliates | (6,586) | — | — | — | (6,586) |
| Dividends paid to affiliates | — | (5,882) | (704) | 6,586 | — |
| Net cash (used in) provided by financing activities | (2,948) | (7,055) | 2,163 | 3,655 | (4,185) |
| Change in cash and cash equivalents | 406 | (3,814) | (7,781) | — | (11,189) |
| Cash and cash equivalents at beginning of period | 89 | 18,475 | 8,639 | — | 27,203 |
| Cash and cash equivalents at end of period | $ 495 | $ 14,661 | $ 858 | $ — | $ 16,014 |



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Item 2

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(Dollar amounts in thousands, except where otherwise noted and per share amounts)

FORWARD LOOKING STATEMENTS

This quarterly report, including all documents incorporated by reference, contains forward-looking statements within the meaning established by the Private Securities Litigation Reform Act of 1995 (Act). Forward-looking statements in this quarterly 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;
- changes in regulatory commissions' policies and procedures;
- the timeliness of regulatory commissions' actions concerning rate relief;
- changes in the capital markets and access to sufficient capital on satisfactory terms;
- new legislation;
- changes in accounting valuations and estimates;
- changes in accounting treatment for regulated companies, including adoption of International Financial Reporting Standards, if required;
- electric power interruptions;
- increases in suppliers' prices and the availability of supplies including water and power;
- fluctuations in interest rates;
- changes in environmental compliance and water quality requirements;
- litigation that may result in damages or costs not recoverable from third parties;
- acquisitions and the ability to successfully integrate acquired companies;
- the ability to successfully implement business plans;
- civil disturbances or terrorist threats or acts, or apprehension about the possible future occurrences of acts of this type;
- the involvement of the United States in war or other hostilities;
- our ability to attract and retain qualified employees;

- labor relations matters as we negotiate with the unions;



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- federal health care law changes could result in increases to Company health care costs and additional income tax expenses in future years;
- changes in federal and state income tax regulations and treatment of such by regulatory commissions;
- implementation of new information technology systems;
- changes in operations that result in an impairment to acquisition goodwill;
- 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;
- general economic conditions, including changes in customer growth patterns and our ability to collect billed revenue from customers;
- changes in customer water use patterns and the effects of conservation;
- the impact of weather on water sales and operating results;
- the ability to satisfy requirements related to the Sarbanes-Oxley Act and other regulations on internal controls; and
- the risks set forth in "Risk Factors" included elsewhere in this quarterly 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 quarterly report or as of the date of any document incorporated by reference in this report, as applicable. When considering forward-looking statements, investors should keep in mind the cautionary statements in this quarterly 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.

CRITICAL ACCOUNTING POLICIES

We maintain our accounting records in accordance with accounting principles generally accepted in the United States of America (GAAP) and as directed by the Commissions to which our operations are subject. The process of preparing financial statements in accordance with GAAP 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. Management believes that the following accounting policies are critical because they involve a higher degree of complexity and judgment, and can have a material impact on our results of operations, financial condition, and cash flows of the business. These policies and their key characteristics are discussed in detail in the 2012 Form 10-K. They include:

- **revenue recognition and the water revenue adjustment mechanism;**
- **modified cost balancing accounts;**
- **expense balancing and memorandum accounts;**
- **regulatory utility accounting;**
- **income taxes;**
- **pension benefits;**
- **workers' compensation and other claims;**
- **goodwill accounting and evaluation for impairment; and**
- **contingencies.**



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For the three-month period ended March 31, 2013, there were no changes in the methodology for computing critical accounting estimates, no additional accounting estimates met the standards for critical accounting policies, and there were no material changes to the important assumptions underlying the critical accounting estimates.

RESULTS OF FIRST QUARTER 2013 OPERATIONS COMPARED TO
FIRST QUARTER 2012 OPERATIONS
Amounts in thousands except share data

Overview

The net loss for the three month period ended March 31, 2013, was $1.1 million, or a $0.03 loss per diluted common share compared to net income of $1.1 million or $0.03 per diluted common share for the three month period ended March 31, 2012. The decrease during the first quarter of 2013 was partially due to the reversal of 2011 deferred WRAM operating revenue of $8.9 million and MCBA associated costs of $7.2 million during the first quarter of 2012, which had added net income of $1.1 million in the first quarter of 2012 compared to the deferral of WRAM operating revenue and MCBA associated costs during the first quarter of 2013 which reduced net income $0.1 million.  Also, the accrual for unbilled operating revenue as of March 31, 2013 decreased pre-tax income $3.0 million compared to the prior year due to a decrease in customer consumption during the first quarter of 2013.  Pre-tax cost increases of $6.5 million in wage and benefit costs, self-insurance costs, and conservation costs were partially offset a pre-tax $1.6 million decrease in maintenance costs. Other income, net of income taxes, decreased $0.6 million, mostly due to a lower unrealized gain on our benefit plan insurance investments during the first quarter of 2013 compared to first quarter 2012.

Operating Revenue

Operating revenue decreased $5.3 million or 5% to $111.4 million in the first quarter of 2013. The factors that impacted the operating revenue for the first quarter of 2013 compared to 2012 are as follows:

| | | |
|---|---|---|
| Rate increases | $ | 2,533 |
| Conservation balancing account | | 1,167 |
| Deferral of net WRAM and MCBA revenue | | (9,841 ) |
| Usage | | (3,501 ) |
| Pension balancing account | | (242 ) |
| Net effect of WRAM and other | | 4,579 |
| Net operating revenue decrease | $ | (5,305) |

The deferral of net WRAM and MCBA revenue in the table above occurs whenever a district net receivable balance is estimated to be collected more than 24 months after the respective reporting period in which it was recognized. The deferrals are reversed when district net receivable balances are estimated to be collected within 24-months. The $9.8 million net revenue decrease during the first quarter of 2013 compared to the first quarter of 2012 was mostly due to an $8.9 million benefit during the first quarter of 2012 from the reversal of the 2011 deferred net WRAM and MCBA revenue and from the deferral of net WRAM and MCBA revenue of $1.1 million during the first quarter of 2013.

The net change in usage in the above table refers primarily to the difference between actual metered customer consumption during the three months ended March 31, 2013 compared to the three months ended March 31, 2012. The $3.5 million usage revenue decrease was due to a decrease in customer consumption during the first quarter of 2013 compared to the prior year. In part, this reflects a $3.0 million decrease in accrued unbilled operating revenue which is not a component of the WRAM. The WRAM is a cash basis mechanism which records changes in billed operating revenue. The quarterly changes in the accrued unbilled operating revenue usually vary year over year. These changes are usually most variable in the first and third quarters due to weather conditions and have not had a significant impact on annual revenue in past years.

The net effect of WRAM and other in the above table refers primarily to the revenue changes recognized by the WRAM and MCBA. The WRAM is impacted by changes in consumption patterns from our historical trends as well as an increase in conservation efforts. The MCBA, which records the differences in production costs from the adopted costs, is recorded as an element of revenue as it represents pass through costs which are billed to customers. The MCBA is impacted by changes in total production quantities, the production mix of the source of water, the price paid for purchased water and power, and the amount of pump taxes paid. The net change during the three months ended March 31, 2013 compared to the three months ended March 31, 2012 resulted in an increase to revenue of $4.6 million.



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The components of the rate increases are as follows:

| | | |
|---|---|---|
| Purchased water offset increases | $ | 1,599 |
| Step rate increases | | 1,425 |
| General rate case (GRC) increases | | 717 |
| Cost of capital adjustment mechanism and other | | (1,208 ) |
| Total increase in rates | $ | 2,533 |

Total Operating Expenses

Total operating expenses were $105.7 million for the first quarter of 2013, versus $110.1 million for the same period in 2012, a 4% decrease.

Water production expense consists of purchased water, purchased power, and pump taxes. It represents the largest component of total operating expenses, accounting for approximately 39% of total operating expenses in the first quarter of 2013. Water production expenses increased 7% compared to the same period last year mostly due to increased costs for purchased water. Our wholly-owned operating subsidiaries, Washington Water, New Mexico Water, and Hawaii Water obtain all of their water supply from wells.

Sources of water as a percent of total water production are listed in the following table:

| | Three Months Ended March 31 | |
|---|---|---|
| | 2013 | 2012 |
| Well production | 43 % | 45 % |
| Purchased | 52 % | 52 % |
| Surface | 5 % | 3 % |
| Total | 100 % | 100 % |

The components of water production costs are shown in the table below:

| | Three Months Ended March 31 | | | | | |
|---|---|---|---|---|---|---|
| | 2013 | | 2012 | | Change | |
| Purchased water | $ | 34,847 | $ | 31,856 | $ | 2,991 |
| Purchased power | | 4,850 | | 5,141 | | (291 ) |
| Pump taxes | | 2,000 | | 1,955 | | 45 |
| Total | $ | 41,697 | $ | 38,952 | $ | 2,745 |

Purchased water costs increased due to price increases from water wholesalers, despite a 7% decrease in water production for the first quarter 2013 compared to first quarter of 2012.

Administrative and general expense and other operations expense decreased 13% to $40.9 million. The decrease was due to changes in deferred MCBA costs associated with the deferral of net WRAM operating revenue. During the first quarter of 2012, a $7.2 million increase to other operations expense was recognized from the reversal of the 2011deferred net WRAM operating revenue and MCBA associated cost adjustment as compared to a $0.9 million reduction to other operations expense during the first quarter of 2013 from the deferred net WRAM operating revenue and MCBA associated cost adjustment. Cost increases of $6.5 million in employee benefits and wage costs, self insurance costs and increases in conservation program expenses during the first quarter of 2013 was offset by the decrease in other operations expense due to the reversal of the 2011 deferred net WRAM operating revenue and MCBA associated costs explained above. Wage increases became effective January 1, 2013. At March 31, 2013, there were 1,131 employees and at March 31, 2012, there were 1,124 employees.

Maintenance expense decreased by 28% to $4.1 million in the first quarter of 2013 compared to $5.8 million in the first quarter of 2012, due to a decrease in main water treatment facilities and transmission and distribution mains repairs.

Depreciation and amortization expense increased $0.7 million, or 5%, mostly due to 2012 capital additions.

Federal and state income taxes charged to operating expenses decreased $1.2 million in the first quarter of 2013 because of a decrease to net operating income and an increase in net interest expense.    Federal and state income taxes charged to other income and expenses decrease $0.4 million in the first quarter of 2013 mostly due to a decrease in unrealized gains on our benefit plan insurance investments.  We expect the effective tax rate to be between 38% and 42% for fiscal year 2013.





Other Income and Expense

Other income decreased $0.6 million in the first quarter of 2013 mostly due to a decrease in unrealized gains on our benefit plan insurance investments. The unrealized gain on our benefit plan insurance investments was $0.5 million during the first quarter of 2013 compared to an unrealized gain of $1.7 million in the same period last year, which was a decrease of $1.2 million.

Interest Expense

Net interest expense, net of interest capitalized, increased $0.8 million, or 11%, to $7.5 million for the first quarter of 2013 compared to the same period last year. The increase was mostly due to an increase in short term borrowing interest rates, and a decrease in capitalized interest charged to construction projects.

REGULATORY MATTERS

**Rates and Regulation**

The state regulatory commissions have plenary powers setting rates and operating standards. As such, state commission decisions significantly impact the Company's revenues, earnings, and cash flows. The amounts discussed herein are generally annual amounts, unless specifically 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. Most filings result in rate changes that remain in place until the next General Rate Case (GRC). As explained below, surcharges and surcredits to recover balancing and memorandum accounts as well as general rate case interim rate relief are temporary rate changes, which have specific time frames for recovery.

GRCs, escalation rate increase filings, and offset filings change rates to amounts that will remain in effect until the next GRC. 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, the Commission issued a decision on Cal Water's 2009 general rate case filing in the fourth quarter of 2010 with rates effective on January 1, 2011. In accordance with the CPUC's rate case plan for Class A water utilities Cal Water filed a GRC on July 5, 2012, which is applicable to all of its California Districts. Any rate change as a result of that filing is expected to be effective on January 1, 2014.

Between GRC filings utilities may file escalation rate increases, which allow the utility to recover cost increases, primarily from inflation and incremental investment, during the second and third years of the rate case cycle. However, escalation rate increases are subject to a weather-normalized earnings test on a district-by-district basis. Under the earnings test, the CPUC may reduce the escalation rate increase if, in the most recent 12-month period, this earnings test reflects earnings in excess of what was authorized for that district.

In addition, California water utilities are entitled to make offset filings. Offset filings may be filed to adjust revenues for construction projects authorized in GRCs when the plant is placed in service or for rate changes charged to the Company for purchased water, purchased power, and pump taxes (referred to as "offsettable expenses"). Such rate changes approved in offset filings remain in effect until the next GRC is approved.

Cal Water's Water Revenue Adjustment Mechanisms (WRAMs) and Modified Cost Balancing Accounts (MCBAs) were authorized by the CPUC to remove the disincentive associated with lower water consumption levels caused by promoting water conservation programs. In order to maintain revenue neutrality, the CPUC de-coupled Cal Water's revenue requirement from ratepayer usage with the WRAM/MCBA. Under the WRAM/MCBA, Cal Water recovers the full quantity revenue amounts authorized by the CPUC by using advice letter filings for any unbilled quantity revenue amounts or refunds for overcollection, regardless of customer usage volumes.

Advice letters, which implement surcharges and surcredits to amortize balances in the WRAM and MCBA accounts, are filed between February and April of each year based on the district balances for the last calendar year. Based on current CPUC interpretations, most surcharges are amortized between 12 or 18 months. The WRAM and MCBA amounts are cumulative, so if they are not amortized in a given calendar year, the balance will be carried forward and included with the following year balance.





***2012 Regulatory Activity***

*2012 California GRC filing*

On July 5, 2012, Cal Water filed its 2012 GRC application covering all district and general office revenue requirements. The GRC application requested an increase of $92.7 million or 19.4% in rates for 2014, $17.2 million or 3.0% in rates for 2015 and $16.9 million or 2.9% in rates for 2016. Additionally, the GRC includes a number of special requests. The Division of Ratepayer Advocates (DRA) at the CPUC has reviewed the filing and submitted testimony and has made recommendation regarding Cal Water's filing. In addition, five intervening parties representing various ratepayer interests submitted testimony recommending changes to Cal Water's proposals.

Cal Water is in the process of reviewing parties' recommendations and evaluating the validity of underlying data.  Cal Water's rebuttal testimony will challenge those recommendations, as appropriate.  Settlement negotiations with DRA and intervenors will begin in May, and evidentiary hearings are scheduled for mid-June.  Any rate change as a result of this filing is expected to be effective on January 1, 2014.

*Building Renovation on General Office Campus*

On March 4, 2013, Cal Water and the CPUC's Division of Ratepayer Advocates submitted a proposed settlement that would allow Cal Water to recover $5.7 million in capital costs for renovating a building on Cal Water's San Jose campus that houses the information technology, human resources, and customer service departments. Cal Water originally requested recovery of $6.0 million for the renovation, which included reconfiguration and expansion of the old building. While the substantive issues are being evaluated in a separate proceeding, the revenue increase Cal Water proposed in its 2012 GRC filing already includes the $6.0 million requested for the renovation. The level of cost recovery the CPUC authorizes for the renovation in the separate proceeding will be incorporated into the final rates adopted in the 2012 GRC proceeding that are expected to be effective on January 1, 2014.

*Federal Income Tax Bonus Depreciation*

In 2011, Cal Water filed for and received approval to track the benefits from federal income tax accelerated depreciation in a memorandum account due to the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010. Additional federal income tax deductions for assets placed in service after September 8, 2010, and before December 31, 2011, were $0.1 million for 2010 and $12.2 million for 2011. The memorandum account may result in a surcredit because of the impact to Cal Water's revenue requirement for changes to working cash estimates, reductions to federal income tax qualified U.S. production activities deductions (QPAD), and changes to contributions-in-aid-of-construction. As of March 31, 2013, the estimated surcredit range is between $0.6 million and $1.1 million. The CPUC will determine the disposition of amounts recorded in the memorandum account in Cal Water's next GRC.

*Service Line Insurance Billing*

As a consequence of D.07-12-055, which resolved Cal Water's 2006 GRC, Cal Water was required to demonstrate that its non-regulated Extended Service Protection (ESP) business or its successor complies with CPUC rules. Cal Water made an administrative compliance filing in 2008 which was rejected. Cal Water subsequently filed A.08-05-019 requesting Commission confirmation that the interaction between Cal Water, CWS Utility Services, and HomeServe USA complied with all applicable rules. During the proceeding, the CPUC established a memorandum account to record Cal Water's revenues and expenses related to the non-regulated service line insurance business. On February 28, 2013, the CPUC adopted D.13-02-026 and approved the settlement between Cal Water and the CPUC's Division of Ratepayer Advocates resolving all issues in the proceeding and authorizing Cal Water to continue providing billing services to HomeServe USA. Consistent with the settlement, Cal Water will issue a surcredit of $2.2 million to residential ratepayers over a 12-month period, and will amortize and close the memorandum account in early 2014.

*Escalation Increase filings*

As a part of the decision of the 2009 General Rate Case, Cal Water is authorized to file annual escalation rate increases for 2012 and 2013. In January 2012, Cal Water implemented escalation rate increases in 17 districts. The annual gross revenue associated with these increases is $8.7 million. In January 2013, Cal Water implemented escalation rate increases in 19 districts. The annual gross revenue associated with these increases is $9.6 million.





*Expense Offset filings*

In March 2013, Cal Water filed three advice letters to true-up its WRAM/MCBA balances in all of its regulated districts totaling $23.6 million in revenues in the form of 12, 18 or 20+ month surcharges depending on the size of the balance in relation to the annual revenues of the district. Cal Water also filed advice letters to offset increased purchased water and pump tax rates in five of its regulated districts totaling $4.6 million in annual revenue. Expense offsets are dollar-for-dollar increases in revenue to match increased expenses and interact with the WRAM and MCBA mechanisms so that net operating income is not affected by an offset increase.

*Ratebase Offset filings*

In February 2013, Cal Water filed advice letters to offset several infrastructure improvement projects in two districts totaling $0.5 million in annual revenue. For construction projects that are authorized in GRCs as advice letter projects, companies are allowed to file rate base offsets to increase revenues after the plant is placed into service. The projects filed in this quarter were authorized in the 2009 GRC. Some of the remaining advice letter projects approved in the 2009 GRC are scheduled to be completed during 2013 or later, while others may be canceled due to changes in operational needs.

***Regulatory Activity — Other States***

*2011 Pukalani (Hawaii) GRC Filing*

In August 2011, Hawaii Water filed a general rate case for the Pukalani wastewater system requesting $1.3 million in additional annual revenues. Hawaii Water reached a comprehensive and conceptual settlement with the Consumer Advocate. This settlement would result in an increase of $0.2 million in 2013, another increase of $0.2 million in 2014, and another increase of $0.2 million in 2015 each increase is separated by one year. A Decision and Order from the Commission approving this stipulated settlement is currently pending.

*2012 Waikoloa (Hawaii) GRC Filings*

In August 2012, Hawaii Water filed general rate cases for the Waikoloa water, wastewater, and irrigation systems in Waikoloa Village and Waikoloa Resort requesting $6.3 million in additional annual revenues. The cases are being processed at this time on separate schedules. Hawaii Water cannot determine the timing or final amount of rate relief these filings will generate.

LIQUIDITY

Cash flow from Operations

Cash flow from operations for the first quarter of 2013 was $19.5 million compared to $22.9 million for the same period of 2012. Cash generated by operations varies during the year due to customer billings, timing of contributions to our benefit plans, and timing of estimated tax payments.

During the first quarter of 2013 we made contributions of $7.5 million to our pension and retiree health care plans compared to contributions of $6.0 million made during the first quarter of 2012. The 2013 estimated cash contribution to the pension plans is $31.3 million and to the other postretirement benefit plans is $9.6 million.

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 available to cover operating and capital costs during the winter period. The increase in cash flows 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 flows 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 the first quarter of 2013 and 2012, we used $32.1 million and $28.7 million, respectively, of cash for both company-funded and developer-funded capital expenditures. For 2013, our capital budget is approximately $120 to $130 million. Annual expenditures fluctuate each year due to the availability of construction resources and our ability to obtain construction permits in a timely manner.

Financing Activities

On March 26, 2013, the Company sold 5,750,000 shares of its common stock in an underwritten public offering for cash proceeds of approximately $105.8 million, net of underwriting discounts and commissions and offering expenses. The net proceeds from the sale of common stock were added to our general funds to be used for general corporate purposes. In April 2013, the Company used a portion of the net proceeds from the offering to repay outstanding borrowings on the Company and Cal Water lines of credit of $68.3 million and $25.0 million, respectively.

During the first quarter of 2013, the Company borrowed $3.8 million on our unsecured revolving credit facilities.

The undercollected net WRAM and MCBA receivable balances were $48.6 million as of March 31, 2013 and $46.1 million as of December 31, 2012, respectively. The CPUC shortened the amortization periods for undercollected net WRAM and MCBA balances such that most balances will be collected within 18-months. This change is expected to improve cash flows during 2013. The undercollected balances were primarily financed by Cal Water using short-term and long-term financing arrangements to meet operational cash requirements. Interest on the undercollected balances, the interest recoverable from ratepayers, is limited to the current 90-day commercial paper rates which is significantly lower than Cal Water's short and long-term financing rates.

Short-Term and Long-Term Financing

Short-term liquidity is provided by our unsecured revolving credit facilities, which were amended and replaced on June 29, 2011, and internally generated funds. Long-term financing is accomplished through the use of both debt and equity. On September 23, 2010, the CPUC authorized Cal Water to issue $350 million of debt and common stock to finance capital projects and operations.

During the first quarter of 2013, we utilized cash generated from the sale of Company common stock, operations, and borrowings on the unsecured revolving credit facilities. We did not issue any first mortgage bonds in 2013. In future periods, management anticipates funding our capital needs through a relatively balanced approach between long term debt and equity.

As of March 31, 2013, there were short-term borrowings of $93.3 million outstanding on the unsecured revolving credit facilities compared to $89.5 million as of December 31, 2012. The March 31, 2013 short-term borrowings were paid in-full during the month of April 2013.

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.

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 an interest coverage ratio of three or more. As of March 31, 2013, the Company's total capitalization ratio was 52.1% (trade payable is included as debt for this calculation) and interest 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. As of March 31, 2013, we have met all of the covenant requirements and are eligible to use the full amount of the commitment.

Bond principal and other long-term debt payments were $0.4 million during the first quarter of 2013 compared to $2.4 million during the first quarter of 2012.

Long-term financing, which includes 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.

Dividends, Book Value and Shareholders

The first quarter of 2013 common stock dividend of $0.16 per share was paid on February 22, 2013, compared to a quarterly dividend in the first quarter of 2012 of $0.1575. This was our 272nd consecutive quarterly dividend. Annualized, the 2013





dividend rate is $0.64 per common share, compared to $0.63 in 2012. For the full year 2012, the payout ratio was 54% of net income. On a long-term basis, our goal is to achieve a dividend payout ratio of 60% of net income accomplished through future earnings growth.

At its April 24, 2013 meeting, the Board declared the second quarter dividend of $0.16 per share payable on May 17, 2013, to stockholders of record on May 6, 2013. This was our 273rd consecutive quarterly dividend.

2013 Financing Plan

We intend to fund our capital needs in future periods through a relatively balanced approach between long-term debt and equity. The Company and Cal Water have a three-year syndicated unsecured revolving line of credit of $100 million and $300 million, respectively for short-term borrowings. As of March 31, 2013, the Company's availability on these unsecured revolving lines of credit was $306.7 million.

Book Value and Stockholders of Record

Book value per common share was $11.99 at March 31, 2013 compared to $11.30 at December 31, 2012.

There were approximately 2,329 stockholders of record for our common stock as of April 24, 2013.

Utility Plant Expenditures

During the first quarter of 2013, capital expenditures totaled $32.1 million for company-funded and developer-funded projects. The planned 2013 company-funded capital expenditure budget is approximately $120 to $130 million. The actual amount may vary from the budget number due to timing of actual payments related to current year and prior year projects. We do not control third-party-funded capital expenditures and therefore are unable to estimate the amount of such projects for 2013.

At March 31, 2013, construction work in progress was $147.5 million compared to $123.2 million at March 31, 2012. Work in progress includes projects that are under construction but not yet complete and placed in service.

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. As of April 1, 2013, the State of California snowpack water content and rainfall accumulation during the 2012 — 2013 water year is 95% of normal (per the California Department of Water Resources, Northern Sierra Precipitation Accumulation report). Precipitation in California during the three months ended March 31, 2013 was normal. Management believes that supply pumped from underground aquifers and purchased from wholesale suppliers will be adequate to meet customer demand during 2013 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.

CONTRACTUAL OBLIGATIONS

During the three-months ended March 31, 2013, there were no material changes in contractual obligations outside the normal course of business.





Item 3.

QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

We do not hold, trade in or issue derivative financial instruments and therefore are not exposed to risks these instruments present. Our market risk to interest rate exposure is limited because the cost of long-term financing and short-term bank borrowings, including interest costs, is covered in consumer water rates as approved by the commissions. We do not have foreign operations; therefore, we do not have a foreign currency exchange risk. Our business is sensitive to commodity prices and is most affected by changes in purchased water and purchased power costs.

Historically, the CPUC's balancing account or offsetable expense procedures allowed for increases in purchased water and purchased power costs to be passed on to consumers. Traditionally, a significant percentage of our net income and cash flows comes from California regulated operations; therefore the CPUC's actions have a significant impact on our business. See Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies - Expense Balancing and Memorandum Accounts" and "Regulatory Matters".

Item 4.

CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(c) under the Exchange Act) that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act 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 CEO and CFO, as appropriate, to allow for timely decisions regarding required disclosure.

In designing and evaluating the disclosure controls and procedures, management 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 CEO and our CFO, evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2013. Based on that evaluation, we concluded that our disclosure controls and procedures were effective at the reasonable assurance level.

(b) Changes to Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting that occurred during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

Item 1.

LEGAL PROCEEDINGS

From time to time, the Company has been named as a co-defendant in asbestos-related lawsuits. Several of these cases against the Company have been dismissed without prejudice. In other cases the Company's contractors and insurance policy carriers have settled the cases with no effect on the Company's financial statements. As such, the Company does not currently believe there is any potential loss that is probable to occur related to these matters and therefore no accrual has been recorded.

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. In the future, we may be involved in disputes and litigation related to a wide range of matters, including employment, construction, environmental issues and operations. Litigation can be time consuming and expensive and could divert management’s time and attention from our business. In addition, if we are subject to additional lawsuits



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or disputes, we might incur significant legal costs and it is uncertain whether we would be able to recover the legal costs from ratepayers or other third parties.

Item 1A.

RISK FACTORS

There have been no material changes to the Company’s risk factors set forth in Part I, Item 1A of the Company’s Annual Report on Form 10-K for the year-ended December 31, 2012, filed with the SEC on February 28, 2013.

Item 6.

EXHIBITS

| Exhibit | Description |
|---|---|
| 31.1 | Chief Executive Officer certification of financial statements pursuant to Section 302 of the Sarbanes- Oxley Act of 2002 |
| 31.2 | Chief Financial Officer certification of financial statements pursuant to Section 302 of the Sarbanes- Oxley Act of 2002 |
| 32 | Chief Executive Officer and Chief Financial Officer Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes- Oxley Act of 2002 |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema Document |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |



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SIGNATURES

Pursuant to the requirement 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
Registrant

May 6, 2013

By: /s/ Thomas F. Smegal III
Thomas F. Smegal III
Vice President,
Chief Financial Officer and Treasurer



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Exhibit Index

| Exhibit | Description |
|---|---|
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**Exhibit 31.1**

**CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER**
**PURSUANT TO SECTION 302 OF**
**THE SARBANES-OXLEY ACT OF 2002**

I, Peter C. Nelson, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the quarter ended March 31, 2013, 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(e)) 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: May 6, 2013 | By: | /s/ Peter C. Nelson |
| | | Peter C. Nelson |
| | | Chairman of the Board and Chief Executive Officer |

**Exhibit 31.2**

**CERTIFICATION OF THE CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002**

I, Thomas F. Smegal, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the quarter ended March 31, 2013, 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(e)) 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: May 6, 2013

By: /s/ Thomas F. Smegal III
Thomas F. Smegal III
Vice President, Chief Financial Officer and Treasurer

**Exhibit 32**

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 certifies that this quarterly report on Form 10-Q for the period ended March 31, 2013, fully complies with the requirements of Section 13(a) or 15(d), as applicable, of the Securities Exchange Act of 1934 and that the information contained in this Report fairly presents, in all material respects, the financial condition and results of operations of California Water Service Group.

| | | |
|---|---|---|
| Date: May 6, 2013 | By: | /s/ Peter C. Nelson<br>PETER C. NELSON<br>Chairman of the Board and Chief Executive Officer<br>California Water Service Group |
| Date: May 6, 2013 | By: | /s/ Thomas F. Smegal III<br>THOMAS F. SMEGAL III<br>Vice President, Chief Financial Officer and Treasurer<br>California Water Service Group |