



OFFICE OF ENERGY INFRASTRUCTURE SAFETY

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Caroline Thomas Jacobs, Director

December 27, 2021

Chris Alario
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Mr. Alario,

On June 29, 2020, the California Public Utilities Commission's (CPUC) Wildfire Safety Division (WSD) engaged Crowe LLP (Crowe) to conduct an independent audit of wildfire mitigation expenditures by the six investor-owned utilities (IOUs), who submitted 2019 and 2020 Wildfire Mitigation Plans (WMPs). WSD, along with all its functions, transitioned to the Office of Energy Infrastructure Safety (Energy Safety), a new department under the California Natural Resources Agency on July 1, 2021. Crowe recently completed its audit and Energy Safety is publicly releasing Crowe's final audit reports.

The purpose of Crowe's audit was to examine IOUs' spending in the execution of its WMP programs and initiatives relative to its prior General Rate Cases (GRCs). Crowe assessed the relationship between expenses and/or investments identified in the 2019 and 2020 WMPs and operating and capital expenditures approved in previous GRCs.

Enclosed is Crowe's Performance Audit of Liberty Utilities LLC Wildfire Mitigation Plan Expenditures Final Report. The report identifies one finding and offers Crowe's recommendations on potential considerations for further action. Energy Safety may consider the final audit report in completing its annual report on compliance for the 2020 WMP. Energy Safety also provides this report to the CPUC for their review and consideration as the CPUC deems appropriate.

Sincerely,

Caroline Thomas Jacobs
Director
Office of Energy Infrastructure Safety

Performance Audit of Liberty Utilities
Wildfire Mitigation Plan Expenditures

December 23, 2021



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Independent Auditor's Report

Crowe has conducted a performance audit of Liberty Utilities (Liberty) for the period from January 1, 2019, through December 31, 2020, to determine whether Liberty complied with General Rate Case (GRC) rules and regulations and to determine whether any expenses and/or investments identified in the 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.

We have conducted our performance audit in accordance with *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusion based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for the findings and conclusions based on our audit objectives.

Our audit was limited to the following three objectives:

1. Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations.
2. Determine whether operating or capital expenditures identified in Liberty's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2019 GRC.
3. Determine whether Liberty's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that Liberty received approval and funding from GRCs or similar applications submitted to California Public Utilities Commission (CPUC) between 2017 and 2020.

Solely to assist us in planning and performing our performance audit, we obtained an understanding of the internal controls of Liberty to determine the audit procedures that are appropriate for the purpose of providing a conclusion on Liberty adherence to GRC rules and regulations and wildfire related accounting practices, as specified, but not for the purpose of expressing an opinion on the effectiveness of internal control. Accordingly, we do not express any assurance on the internal control.

The results of our tests indicated that, Liberty met the objectives for the period of January 1, 2019, through December 31, 2020, in all significant respects. We identified one (1) finding that was not significant to the audit objectives which we described in Finding 1.

Liberty elected not to provide written responses to the audit report finding.



Crowe LLP

Executive Summary

Crowe LLP (Crowe) conducted a performance audit of Liberty Utilities (Liberty) in accordance with Generally Accepted Government Auditing Standards (GAGAS). In this section we provide background on the performance audit, an overview of the project background and scope, and a summary of Crowe's findings and recommendations related to this examination.

- A. *Project Background and Scope*
- B. *Crowe Findings and Recommendations*
- C. *Report Organization*

A. Project Background and Scope

The California Public Utilities Commission (CPUC) and its Wildfire Safety Division (WSD) (which is now the Office of Energy Infrastructure Safety (Energy Safety) with the California Natural Resources Agency¹) engaged Crowe to conduct an independent performance audit, in accordance with Generally Accepted Government Auditing Standards (GAGAS), of Liberty, and submitted 2019 and 2020 Wildfire Mitigation Plans (WMPs). The CPUC and the WSD wanted to determine whether actual Liberty expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. They were also interested to determine whether any expenses and/or investments identified in the 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.

The audit period covers electric line of business expenditures from January 1, 2019, through December 31, 2020, and includes Liberty's final and approved 2019 and 2020 WMPs and the most recent GRC application filed by Liberty that is final and approved, any applications or advice letter requests that the IOU has filed with the CPUC as necessary to meet the scope of work.

| Wildfire Mitigation Plan | Cost Data Presented in WMP | | Applicable GRCs Used in Crowe Analysis |
|--------------------------|----------------------------|-----------|--|
| | 2019 | 2020 | |
| 2019 Plan | Actual | N/A | 2019 GRC |
| 2020 Plan | Actual | Projected | 2019 GRC |

B. Crowe Findings and Recommendations

This performance audit resulted in one (1) finding, which we summarize in **Exhibit ES-1**. We also provide recommendations to address this finding.

¹ During the course of this engagement, the CPUC's Wildfire Safety Division transitioned into the Office of Energy Infrastructure Safety, a new department under the California Natural Resources Agency.

Exhibit ES-1**Performance Audit Findings and Recommendations Summary**

| Description of Finding | Questioned Costs | Recommendation(s) |
|---|------------------|--|
| 1. Wildfire Mitigation Cost Categories Provided in WMPs Do Not Align with How Wildfire Mitigation Costs are Categorized and Adopted as Part of GRCs, Making it Difficult to Monitor Incremental Wildfire Mitigation Costs | N/A | <ul style="list-style-type: none"> As part of the WMP process, Liberty should provide wildfire mitigation costs separately for capital and for operating expenditures at a program level that is equivalent to, or can be easily reconciled to, the program level it uses for cost presentation in its GRC and RSARs. |

C. Report Organization

The main body of this report includes the following components.

- **Section 1**

In this section, immediately following the Executive Summary, we provide general information on the scope and objectives of this performance audit and contextual information about Liberty.

- **Section 2**

In this section, we outline our approach, including procedures and sampling methods applied.

- **Section 3**

In this section, we provide our performance audit results, including our findings and recommendations.

Introduction

In this introduction section, we provide background on the performance audit of Liberty Utilities (Liberty). We describe the Liberty wildfire mitigation program, recently applicable general rate case proceedings, and memorandum accounts. This introductory section also provides the scope of the audit and sampling methodology employed. The remainder of this section is organized as follows:

- A. *Project Background*
- B. *Liberty Wildfire Mitigation Program Profile*
- C. *Liberty General Rate Cases*
- D. *Liberty Memorandum Accounts*
- E. *Performance Audit Scope.*

A. Project Background

The CPUC and its WSD (now Energy Safety) engaged Crowe to conduct an independent performance audit, in accordance with Generally Accepted Government Auditing Standards (GAGAS), of Liberty, who is regulated by the CPUC and submitted 2019 and 2020 Wildfire Mitigation Plans (WMPs). The CPUC and WSD wanted to determine whether actual Liberty expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. They also were interested to determine whether any expenses and/or investments identified in the 2019 and 2020 WMPs are duplicative of operating and capital expenditures approved in previous GRCs.

The audit period covers electric line of business expenditures from January 1, 2019, through December 31, 2020, and includes Liberty's final and approved 2019 and 2020 WMPs and the 2019 GRC application

filed by Liberty that is final and approved, any applications or advice letter requests that the IOU has filed with the CPUC as necessary to meet the scope of work.

B. Liberty Wildfire Program Profile

Senate Bill (SB) 901 required all California electric utilities to prepare plans on constructing, maintaining, and operating their electrical lines and equipment to minimize the risk of catastrophic wildfire. In its *Order Instituting Rulemaking to Implement Electric Utility Wildfire Mitigation Plans Pursuant to Senate Bill 901 (2018)*, Rulemaking (R.) 18-10-007 (Wildfire OIR), the CPUC outlined wildfire mitigation plan requirements.

1. 2019 Liberty Wildfire Mitigation Plan

On February 6, 2019, Liberty submitted its 2019 Wildfire Mitigation Plan (referred to as the 2019 WMP). The 2019 WMP provides details on Liberty's strategies and programs to prevent wildfires. Programs included in Liberty's 2019 WMP included:

- *Design & construction*, including system, equipment and structure design and technical upgrades intended to improve system hardening and prevent contact between infrastructure and fuel sources (e.g., vegetation)
- *Inspection & maintenance*, including assessment and diagnostic activities to ensure infrastructure in working condition and vegetation adheres to minimum distance specifications
- *Operational practices*, including proactive day to day actions taken to mitigate wildfire risk (e.g., prepare for de-energization)
- *Situational & conditional awareness*, including methods to improve system visualization and awareness of environmental conditions (e.g., camera installations)
- *Response & recovery*, including procedures to react to de-energization, wildfire or related emergency conditions.

Table 7-1 of the 2019 WMP included Liberty's Fire Mitigation Plans and Programs and is displayed as Exhibit 1.

Exhibit 1 Estimated 2019 Capital and Operating Costs Combined Required to Support Wildfire Mitigation Programs (Source: 2019 Wildfire Mitigation Plans)

| Wildfire Mitigation Category | 2019 Estimated | Unit Cost |
|-------------------------------|------------------------------------|--------------------------|
| Automatic Reclosers | \$7,350,000 | Total |
| Covered Conductors | \$614,000 | Per Mile |
| Pole Loading and Replacement | \$12,000 - \$15,000 | Per Mile |
| Fuse Replacement | \$721,550 | Annual |
| Substation Design Hardening | \$16,500,000 | Total |
| Undergrounding | \$7,290,220 | Total |
| Tree Attachment Removal | \$420,000 | Annual |
| Vegetation Management Plan | \$4,000,000 | Annual |
| Forest Resiliency Corridor | \$661,000 | Contribution above share |
| Weather Station Installations | \$148,720 | Total |
| Total | \$37,717,490 - \$37,732,490 | |

2. 2020 Wildfire Mitigation Plan

On February 28, 2020, Liberty submitted its 2020 WMP. The 2020 WMP incorporated lessons learned from the 2019 wildfire season and outlined the additional programs planned from 2020 to 2022 to prevent catastrophic wildfires.

Exhibit 2 provides Liberty's WMP initiatives by the wildfire mitigation categories identified in the 2020 WMP.

Exhibit 2

Actual 2019 and Estimated 2020 Capital and Operating Costs Combined Required to Support Wildfire Mitigation Programs (Source: 2020 Wildfire Mitigation Plan)

| Situational Awareness | 2019 Actual | 2020 Estimated |
|--|--------------------|---------------------|
| Situational Awareness | \$199,297 | \$450,000 |
| Grid Design & System Hardening | 1,814,148 | 13,240,500 |
| Asset Management and Inspections | 13,044 | 7,258,554 |
| Vegetation Management | 5,214,905 | 8,770,000 |
| Data Governance | - | 665,000 |
| Emergency Planning and Preparedness | - | 240,000 |
| Stakeholder Cooperation and Community Engagement | - | 75,000 |
| Total | \$7,241,394 | \$30,699,054 |

C. Liberty General Rate Cases

Our scope of work required that we review whether Liberty expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. Below we provide an overview of CPUC GRC rules and regulations and background of the 2019 GRC.

1. General Rate Case Rules and Regulations

As specified on the CPUC website:

General rate cases (GRCs) are proceedings used to address the costs of operating and maintaining the utility system and the allocation of those costs among customer classes. For California's three large investor-owned utilities (IOUs), the GRCs are parsed into two phases. Phase I of a GRC determines the total amount the utility is authorized to collect, while Phase II determines the share of the cost each customer class is responsible and the rate schedules for each class. Each large electric utility files a GRC application every three years. For smaller utilities, authorized costs and allocation of costs are done in just one phase.

The CPUC reviews detailed cost data for various areas of utility operations and approves a budget for the first year – called a test year – of the GRC cycle. For years 2 and 3 – called post-test years – the GRC decision prescribes how to adjust the test year budget for inflation and other factors that may affect costs, such as additional capital projects between test years. The Commission has put in place regulatory mechanisms to adjust the costs approved in GRCs for unforeseen circumstances. For example, the Catastrophic Event

Memorandum Account allows utilities to record costs for state emergencies declared by the governor.

Primary rules related to the GRC related to Liberty rates/spending associated with the GRC are summarized in the GRC “Utility General Rate Case – A Manual for Regulatory Analysts,” (Rate Manual) developed by the CPUC’s Policy & Planning Division on November 13, 2017:

- GRCs establish revenue from customers to provide safe and reliable service at just and reasonable rates (costs)
- PUC Codes 454 and 728 hold the Commission responsible for ensuring that rates are just and reasonable
- Major investor-owned utilities operating in California are required to file a GRC application with the Commission every 36 months (3 years)
- IOUs are required to submit a Risk Spending Accountability Report, in which the utility compares its GRC projected spending for approved risk mitigation projects with the actual spending on those projects and explains any discrepancies
- Cost of service regulation sometimes is referred to as rate of return regulation because in cost of service ratemaking utilities have an opportunity to earn authorized rate of return on prudently incurred capital investments. However, utilities are not guaranteed to earn their authorized return. Rates are set prospectively, and an element of the authorized revenues is planned to repay investors for the use of their money. However, if the utility fails to manage its business efficiently and overspends, then it will likely fail to earn its authorized rate of return. This uncertainty is symmetrical, and if the utility spends less than authorized revenues it will earn greater than its authorized return.

Other notable aspects of the GRC process are identified below:

- The year in which the rate is set is referred to the “test year”
- The years between test years are referred to as “attrition years”
- Budgets within the GRC generally are based on a unit cost multiplied by a number of units
- Budgets in the GRC are not reconciled later with actual results
- At the time the GRC is approved, the unit costs in the GRC are not tied out to Liberty’s costs of doing business (e.g., labor or overheads) as there are other sources of funding which Liberty uses to cover its full revenue requirements
- Where unit costs evolve over time for a specific cost area, these unit costs are then adjusted through the ongoing GRC process during each test year.

2. 2019 Liberty General Rate Case

Liberty submitted their 2019 GRC to the CPUC (A. 18-12-001) and CPUC issued the final decision in August 2020. The decision adopted a 2019 Test Year Revenue Requirement of \$86.1 million and a Rate Base of \$263.1 million. The newly adopted revenue requirement increased rates 3.14 percent over present rates and increased the average residential customer’s monthly bill by approximately \$1.74.

The decision included authorizations for increases in Liberty’s Vegetation Management Program, Energy Efficiency programs, and solar incentive program, and an increase in its Energy Cost Adjustment Clause revenues.

D. Liberty Memorandum Accounts

Utilities in California recover a large portion of their revenue requirement through balancing and memorandum accounts.² The Rate Manual indicates:

A balancing account is an account established to record certain authorized amounts for

² Source: GRC Manual, page 7.

recovery through rates and to ensure that the revenue collected matches the authorized amounts. Balancing accounts usually accrue interest – to be additionally returned to ratepayers if the utility is over-collected, or to recover additional revenue if the utility is under-collected.

Memorandum accounts are similar to balancing accounts except that they do not usually establish an authorized revenue requirement and are subject to further scrutiny by the CPUC. Upon Commission review expenses accrued in Memorandum accounts may or may not be recoverable through rates.

Below are specific characteristics of a memorandum account:

- Requires approval from CPUC
- Approval is through an advice letter (AL)
- Captures costs with specific program needs (often unforeseen) and that are in excess of costs included in rates set through the GRC process
- Costs accounted for separately from GRC costs
- Typically, memorandum account costs incurred are subsequently “trued up” or recovered in the next GRC.

Liberty memorandum accounts applicable for this audit are shown in **Exhibit 3**.

Incrementality

- The basic idea of incrementality is that in order to recover any costs recorded in a memorandum account, those costs must be incremental, and not recovered in another way, such as in a GRC. For example, if Liberty had forecast certain wildfire-related costs in a GRC, resulting in those costs being included in rates, they would not be incremental, and Liberty could not record those same costs in a memorandum account and subsequently seek rate recovery. Incremental costs are costs that were not forecasted in the GRCs.
- Commission ratemaking is done on a prospective basis. The Commission's practice is not to authorize increased utility rates to account for *previously* incurred expenses, unless, before the utility incurs those expenses, the Commission has authorized the utility to book those expenses into a memorandum account or balancing account for possible future recovery in rates.

Exhibit 3 Liberty Memorandum Accounts

| Liberty Memorandum Account | Abbrev. | Date Established | Reference | Purpose |
|---|---------|------------------|------------------------|--|
| Catastrophic Event Memorandum Account | CEMA | 1991 | CPUC Resolution E-3238 | Establishes three categories of costs that are eligible for inclusion in the CEMA: (1) restoring utility services to customers; (2) repairing, replacing, or restoring damaged facilities; (3) complying with governmental agency orders in connection with events declared disasters by competent state or federal authorities. |
| Fire Hazard Prevention Memorandum Account | FHPMA | 9/10/2010 | AL-244-E | Record costs related to the implementation of fire hazard prevention measures as adopted in D.09-08-029. |

| Liberty Memorandum Account | Abbrev. | Date Established | Reference | Purpose |
|--|---------|------------------|-----------|---|
| Fire Risk Mitigation Memorandum Account | FRMMA | 3/12/2019 | AL 352-E | Record incremental costs of fire risk mitigation work that are not otherwise recovered in the adopted revenue requirement; track costs before WMP finalized; remain open to track wildfire mitigation costs not included in an approved WMP. |
| Wildfire Mitigation Plan Implementation Memorandum Account | WMPIMA | 6/6/2019 | AL 364-E | The purpose of the WMPIMA is to track the implementation costs incurred for the Commission-approved fire risk mitigation plan that are not otherwise in Liberty's revenue requirement. These costs shall include, but are not limited to, expenses and capital expenditures for increased inspections and patrols; system hardening and infrastructure modernizing, such as fuse upgrades, replacement of line with covered conductors; expanded monitoring automation and system protection such as Supervisory and Data Acquisition (SCADA); improved situational awareness and wildfire detection such as installation of weather stations; enhanced capacity to respond to events and incidents, including animal incidents; and vegetation management activities |

E. Liberty Accounting

Liberty uses Great Plains as its accounting system. Liberty primarily sets up memorandum accounts and associated jobs to track costs that are not funded in the GRC. In situations where the memorandum account is set up to track costs incremental to what is funded in the GRC, the Accounting department reviews the costs in question to exclude what is authorized per the latest GRC decision so that only incremental and unreimbursed costs are recorded in the memorandum account.

F. Other Reports and Applications

In conducting our performance audit procedures, we relied on additional Liberty reports and applications which are described below.

1. Risk Spending Accountability Reports

Liberty is required to submit Risk Spending Accountability Reports (RSAR) on an annual basis. Liberty submits RSARs in order to comply with the Phase Two Decision Adopting Risk Spending Accountability Report Requirements and Safety Performance Metrics for Investor-Owned Utilities and Adopting a Safety Model Approach for Small and Multi-Jurisdictional Utilities (Decision (D.) 19-04-020). RSARs provide a comparison of budgeted to actual for safety, reliability, and maintenance spending. Liberty includes explanations for budget to actual cost variances. Specific RSARs and related documents we used for this project included:

- Liberty (U 933-E) Advice Letter No. 173-E, Submitted June 30, 2021 (Liberty's 2020 Risk Spending Accountability Report)
- Liberty (U 933-E) Advice Letter No. 150-E, Submitted June 30, 2020 (Liberty's 2019 Risk Spending Accountability Report).

Performance Audit Approach

The CPUC and its WSD (now Energy Safety) engaged Crowe to conduct this independent Performance Audit, in accordance with the Generally Accepted Government Auditing Standards (GAGAS). In accordance with GAGAS, Crowe followed 2018 Government Audit Standards (GAO-18-568G) which require us to establish an overall approach to apply in planning and performing this audit to obtain sufficient, appropriate evidence that provides a reasonable basis for findings and conclusions based on audit objectives.³

Crowe developed our audit plan and procedures to meet specific CPUC objectives identified in the Request for Proposal for this project. In developing this audit plan, among other factors, we primarily considered the following:

- Understanding the CPUC GRC process and wildfire mitigation program, including other existing forms of Liberty oversight (e.g., GRC review processes)
- Addressing audit objectives specified by the CPUC
- Reducing audit risk to acceptable levels
- Designing a methodology to obtain sufficient audit evidence to provide a reasonable basis for findings and conclusions
- Developing suitable criteria to use to evaluate performance as it related to audit objectives
- Determining the significance or relative importance of the matter
- Communicating results to those in charge with governance or management.

A. Performance Audit Procedures Applied

Our performance audit objectives and procedures are detailed in **Appendix A**. Crowe also reviewed the documents identified in **Appendix B**. The CPUC had three (3) objectives for this performance audit:

1. Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations.
2. Determine whether operating or capital expenditures identified in Liberty's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2019 GRC.
3. Determine whether Liberty's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that Liberty received approval and funding from GRCs or similar applications submitted to the CPUC between 2017 and 2020.

We submitted several data requests to the company which were progressively more focused throughout the engagement as we obtained more detailed data and information on the company's wildfire mitigation accounting practices. We interviewed management to understand Liberty accounting systems and use of supporting information systems. We conducted an internal controls assessment, in particular to obtain an understanding of Liberty internal controls as it related to differentiating GRC-funded expenses from memorandum account funded expenses.⁴ Finally, we also developed workpapers to document results of the performance audit.

As a basis for conducting our procedures, for the population we obtained and relied upon a database of capital and operating expenditures for 2019 through 2020. To test the veracity of Liberty's cost database, we reconciled the cost data in this database to cost data used by Liberty in several published documents

³ Section 8.01 of GAO-18-568G.

⁴ Where internal control is a process effected by an entity's oversight body, management, and other personnel that provides reasonable assurance that the objectives of an entity will be achieved (GAO-18-568, Fieldwork Standards for Performance Audits, Section 8.38c, page 164).

in the record, including the GRC applications, WMPs, and RSARs.

Below, we identify several additional clarifications related to this performance audit:

1. Our scope of work did not serve to validate the process and outcomes associated with the CPUC's GRC proceedings. Our scope was targeted to determining how Liberty spent funds approved in GRC's which provided funding for WMP programs.
2. The timeframe for our audit spanned actual Liberty wildfire expenditures incurred between January 1, 2019, to December 31, 2020.
3. The audit did not cover Liberty's 2021 Wildfire Mitigation Plan. Wildfire mitigation plan requirements and priorities have evolved significantly over the 2019 to 2021 planning period with guidance from Energy Safety, actual program results, and lessons learned.

B. Sampling Methodology

Our sampling methodology used a targeted approach based on isolated risk factors we determined to be significant to the audit objectives. We targeted third party contractor transactions, change orders and for internal repetitive costs (i.e., labor and overhead) we tested the underlying methodology and not specific transactions. Our approach covered nearly \$3.5 million in transactions or approximately 10 percent of total wildfire memorandum account spend. Crowe requested invoices, timesheets, business cases and other relevant documentation to test whether expenditures were allowable wildfire related costs.

- Costs were supported by appropriate documentation, such as approved purchase orders, receiving reports, vendor invoices, canceled checks, timesheets, overhead tables and records, and correctly charged to account, amount, and period.
- Transactions were for an allowable activity under Liberty's wildfire mitigation plan and memorandum account.
- Services were provided in the location or event identified by Liberty.
- Transactions were consistent with policies and procedures (internal procedures, contract agreement, etc.)

Performance Audit Results

The results of our tests indicated that, PacifiCorp met the objectives of the audit in all significant respects. We identified one (1) finding that was not significant to the audit objectives which we describe in the remainder of this section. We have identified observations of controls and processes related to Liberty wildfire mitigation related expenditures. Each finding includes a recommendation to correct the issue, and is organized into the following six (6) components:

- *Condition* – includes the error observed based on facts revealed from the examination.
- *Criteria* – the basis for our evaluation; in this case a specific policy, procedure, or leading practice.
- *Cause* – the underlying reason for why the non-compliance or error occurred.
- *Effect* – the impact on the organization and/or the ratepayer from the error.
- *Recommendation* – a suggested action to correct the deficiency; or what can be done to address both the cause and condition.
- *Management Response* – an opportunity for the company to provide its response to the finding and/or recommendation. Liberty declined to provide a response on December 17, 2021.

Findings and recommendations from this performance audit are provided beginning on the next page.

In **Exhibit 7** below we summarize each of the one (1) finding.

Our consideration of internal control was for the limited purpose of designing procedures that were

appropriate in the circumstances for the purpose of making a conclusion as to whether Liberty met the performance audit objectives but not for the purpose of expressing an opinion on the effectiveness of Liberty’s internal control. Accordingly, we do not express an opinion on the effectiveness of Liberty’s internal control. Our consideration of internal control was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified one (1) deficiency in internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements in a timely manner. A material weakness in internal control is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that misstatements will not be prevented or detected and corrected in a timely manner. We did not identify any material weaknesses.

A significant deficiency in internal control is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We did not identify any significant deficiencies.

**Exhibit 7
Summary of Findings and Questioned Costs**

| Description of Finding | Questioned Costs | Failure to Meet Which of the 3 Audit Objectives |
|---|------------------|---|
| 1. Wildfire Mitigation Cost Categories Provided in WMPs Do Not Align with How Wildfire Mitigation Costs are Categorized and Adopted as Part of GRCs, Making it Difficult to Monitor Incremental Wildfire Mitigation Costs | N/A | 2, 3 ⁵ |

⁵ This finding was not considered significant to objectives 2 and 3.

Finding 1 - Wildfire Mitigation Cost Categories Provided in WMPs Do Not Align with How Wildfire Mitigation Costs are Categorized and Adopted as Part of GRCs, Making it Difficult to Monitor Incremental Wildfire Mitigation Costs

Deficiency

Condition:

In the past, Liberty Wildfire Mitigation Plans (WMPs) have included cost information at the following levels:

2019 Plan

- By program strategy, including operational practices, plans for inspection, vegetation management, system hardening, and situational awareness (as estimated annual costs). These costs were presented separately for capital and operating expenditures.

2020 Plan

- Wildlife mitigation activity (2019 planned, 2019 actual spend, 2020 spend target), organized into situational awareness and forecasting, grid design and system hardening, asset management and inspections, and vegetation management and inspection. These costs were presented as separately for capital and operating expenditures.

We find that approved Liberty WMP capital and operating costs provided at these levels alone are inadequate for purposes of reconciling these costs to those adopted as part of the GRC process. During the course of the GRC process, and in its RSARs, Liberty provides costs at a program level separately for capital and operating expenditures. However, while the 2019 and 2020 WMPs costs are also provided at a general program area level, these program categories are different from those used in the GRC. This creates challenges for reconciling GRC funded costs to WMP authorized costs.

Criteria:

WMP requirements are delineated in the following documents:

- 2019 WMP – D1905036 Guidance Decision on 2019 Wildfire Mitigation Plans
- 2020 WMP – RES WSD-002 Final Guidance Resolution, and Guidance Appendices
- 2021 WMP – 2021 WMP Guidelines Template.

Cause:

The CPUC has not required capital and operating expenditures delineated to a level that aligns with GRC cost categories as part of WMP content requirements. Additionally, WMP content requirements are evolving as Energy Safety gains more experience and knowledge of program needs.

Effect:

Energy Safety will have difficulty reconciling future Liberty wildfire mitigation related capital and operating expenditures approved as part of the WMPs to those funded through the GRC process.

Recommendation

As part of the WMP process, Liberty should provide wildfire mitigation costs separately for capital and for operating expenditures at a program level that is equivalent to, or can be easily reconciled to, the program level it uses for cost presentation in its GRC and RSARs.

Management Response

Liberty did not provide a management response.

Appendix A – Procedures Performed

The CPUC and its WSD (now Energy Safety) specified three (3) objectives for this performance audit of Liberty. In **Exhibit A-1**, we list these three (3) objectives. **Exhibit A-2** provides a list of nineteen (19) tests we performed to meet the three (3) objectives.

Exhibit A-1 Performance Audit Objectives

| Number | Objective |
|--------|--|
| 1 | Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. |
| 2 | Determine whether operating or capital expenditures identified in Liberty's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2019 GRC. |
| 3 | Determine whether Liberty's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that Liberty received approval and funding from GRCs or similar applications submitted to the CPUC between 2017 and 2020. |

Exhibit A-2 Performance Audit Procedures

| Objective | Procedures |
|---|---|
| 1 - Determine whether actual expenditures to date, and documented future planned expenditures, comply with approved General Rate Case (GRC) funding, related to wildfire mitigation activities, in accordance with GRC rules and regulations. | 1. Obtain and review GRC guidelines available in resolutions, decisions, and GRC proceedings (for the 2019 and 2020 rate cases) applicable to spending GRC funds for wildfire mitigation. |
| | 2. Interview Liberty regulatory and finance management to assess how the IOU is complying with applicable GRC resolutions, decisions, and proceedings related to wildfire mitigation spending. |
| | 3. Compare actual Liberty wildfire mitigation activity spending practices with GRC rules and regulations and assess compliance. |
| | 4. Document non-compliance with GRC rules and regulations related to wildfire mitigation activity spending. |
| 2 - Determine whether operating or capital expenditures identified in Liberty's 2019 and 2020 Wildfire Mitigation Plans (WMPs) are duplicative of operating or capital expenditures approved in the 2019 | 1. Request and obtain a database of actual Liberty capital and operating expenditures covering the period from January 1, 2017 through the present, including expenses for electric operations (transmission and distribution). |
| | 2. Reconcile expenditure amounts included in the database with amounts reported in Liberty's audited financial statements. |
| | 3. Reconcile GRC-funded expenditure amounts included in the database to amounts approved by the CPUC in the GRCs. To perform this test, obtain and review workpapers and exhibits associated with GRC rate case proceedings. |

| Objective | Procedures |
|--|---|
| GRC. | <ol style="list-style-type: none"> 4. Reconcile capital and operating expenditure amounts included in the database to amounts approved in the 2019 and 2020 WMPs. 5. Perform analytical procedures to determine whether expenditures reported as GRC funded in the database are also captured as incremental in a memorandum account. 6. Perform risk assessment of transaction types to inform risk-based sample selection in cost categories with potential duplication between GRC and memorandum accounts. Develop a sample of transactions to test to determine that wildfire mitigation activity expenditures are recorded properly as either GRC funded or incremental in a memorandum account or similar account. 7. Interview Liberty and document procedures used by Liberty to establish approved GRC expenditures by cost category and to track actual expenditures up to approved amounts. This includes potential imputing of approved GRC costs into subordinate cost categories. 8. Document and quantify instances of duplication between GRC-funded expenditures and incremental (memorandum account) expenditures. |
| <p>3 - Determine whether Liberty's actual expenditures to date, and documented future planned expenditures, comply with the 2019 and 2020 WMPs for activities that Liberty received approval and funding from GRCs or similar applications submitted to the CPUC between 2017 and 2020.</p> | <ol style="list-style-type: none"> 1. Using prior GRCs or similar applications, and supporting workpapers and exhibits, create a data set of approved wildfire mitigation related expenditures by cost category. 2. Using data provided in approved 2019 and 2020 WMPs, create a data set of actual and planned capital and operating wildfire mitigation expenditures by planned funding source. 3. Link the data sets in item 1 and 2 above to identify funding for 2019 and 2020 WMP activities where Liberty has received approval for in prior GRCs or similar applications. 4. Link the database in Item 6a to compare approved WMP capital and operating expenditures with actual WMP capital and operating expenditures. 5. Assess whether Liberty is spending or plans to spend funds approved for in past GRCs or similar applications. 6. Perform risk assessment of transaction types to inform risk-based sample selection in cost categories with ambiguity between approved amounts and actual spend amounts. Develop a sample of transactions to test to assess whether actual recorded wildfire mitigation activity expenditures are aligned with approved expenditures. 7. Assess whether actual Liberty wildfire mitigation spending is in accordance with the 2019 and 2020 WMPs and consistent with funding provided in past GRCs or similar applications. Document exceptions. |

Appendix B – List of Records Examined

1. 2019 Wildfire Mitigation Plan, dated February 6, 2019
2. 2020 Wildfire Mitigation Plan, dated February 28, 2020
3. Risk Spending Accountability Report (RSAR)
 - a. 2019 RSAR, submitted June 30, 2020
 - b. 2020 RSAR, submitted June 30, 2021
4. 2019 General Rate Case Application 18-12-001
5. 2019 General Rate Case Decision 20-08-030, dated August 27, 2020
6. Audited Financial Statements for calendar years 2019 and 2020
7. Internal policies and procedures related to internal controls, procurement, capital expenditure planning and accounting systems.
8. Capital and operating expenditures for calendar years 2019 and 2020

Appendix C – Comparison of 2019 GRC Authorized Costs to Actual Costs

In this appendix we compare costs authorized as part of the 2019 General Rate Case for 2019 and 2020 with actual costs incurred by Liberty. This appendix includes the following four (4) exhibits:

- Exhibit C-1 – Comparison of Authorized to Expenses (2019)
- Exhibit C-2 – Balancing and Memo Account Balances (2019)
- Exhibit C-3 – Comparison of Authorized to Actual Expenses (2020)
- Exhibit C-4 – Balancing and Memo Account Balances (2020).

Exhibit C-1
Liberty Utilities
2019 General Rate Case
Comparison of Authorized to Actual Expenses
(Calendar Year 2019)

| Category | 2019 Recorded | 2016 Authorized* | Variance (Recorded vs 2016 Authorized) | 2019 GRC Request | Variance (Recorded vs 2019 GRC) |
|-----------------------------------|---------------|------------------|--|------------------|---------------------------------|
| Fleet | 2,286 | 1,047 | 1,240 | 2,059 | 227 |
| Overhead and Underground Failures | 430 | 1,026 | (596) | 1,315 | (885) |
| Distribution System Capital | 6,104 | 6,091 | 13 | 5,146 | 958 |
| Substation Capital | 1,389 | 1,429 | (39) | 482 | 907 |
| Total Capital | 10,209 | 9,592 | 618 | 9,002 | 1,207 |

* Authorized 2016 Capital from 2016 GRC, escalated to 2019 dollars

| FERC Acct | Description | 2019 Recorded | 2016 Authorized (Escalated) | Variance (Recorded vs 2016 Authorized) | 2019 GRC Request | Variance (Recorded vs 2019 GRC) |
|-----------|--|---------------|-----------------------------|--|------------------|---------------------------------|
| 581 | Load Dispatching | 245 | 642 | (397) | 714 | (469) |
| 582 | Station Expense | 7 | 81 | (74) | 30 | (23) |
| 583 | Overhead Line Expense | 118 | 267 | (150) | 161 | (44) |
| 584 | Underground Line Expense | 51 | 152 | (101) | 89 | (38) |
| 585 | Street Lights / Signal System | - | 2 | (2) | 2 | (2) |
| 588 | Miscellaneous Distribution Expense | 2,701 | 2,774 | (73) | 1,446 | 1,255 |
| | Total Operation | 3,122 | 3,919 | (797) | 2,442 | 680 |
| 591 | Maintenance of Structures | 4 | 0 | 4 | 37 | (33) |
| 592 | Maintenance of Station Equipment | 130 | 153 | (23) | 162 | (32) |
| 593 | Maintenance of Overhead Lines | 1,882 | 585 | 1,297 | 1,892 | (10) |
| 594 | Maintenance of Underground Lines | 352 | 143 | 209 | 294 | 58 |
| 595 | Maintenance of Line Transformers | 7 | 25 | (18) | 16 | (9) |
| 596 | Maintenance of Street Lights / Signal Syst | 4 | 17 | (13) | 5 | (1) |
| 597 | Maintenance of Meters | 43 | 17 | 27 | 45 | (1) |
| 598 | Maintenance of Misc. Distribution Plant | 776 | (21) | 797 | 303 | 473 |
| | Total Maintenance | 3,198 | 920 | 2,279 | 2,753 | 446 |
| | Total Distribution | 6,321 | 4,839 | 1,482 | 5,195 | 1,125 |

2016 Authorized from 2016 GRC Decision and Settlement Model
2019 Recorded from 2019 FERC Form 1

Exhibit C-2
Liberty Utilities
2019 General Rate Case
Balancing and Memo Account Balances
(Calendar Year 2019)

| Balancing / Memo Account | Balance as of December 31, 2019 |
|---|---------------------------------|
| Vegetation Management Balancing Account | \$7,590,000 |

Exhibit C-3
Liberty Utilities
2019 General Rate Case
Comparison of Authorized to Actual Expenses
(Calendar Year 2020)

| Liberty 2020 Safety, Reliability, and Maintenance Capital Expenditures | | | | |
|--|-------------------------|---------------|---------------|------------------|
| \$(000) | | | | |
| Project | PTAM-Authorized Capital | | | 2020 Recorded |
| | 2020 | 2021 | Total | |
| 7300 Line Rebuild | 1,700 | 1,700 | 3,400 | 3,563 |
| Topaz 1261 Line Reconductor | 810 | 810 | 1,620 | 2,479 |
| MHP Conversions | 3,496 | 1,298 | 4,794 | - |
| Distribution Replacements | 6,300 | 6,300 | 12,600 | 8,518 |
| 625/650 Phase 2 | 13,000 | - | 13,000 | 8,515 |
| Total | 25,306 | 10,108 | 35,414 | 23,075 |

| Liberty 2020 Authorized and Recorded O&M Expenses | | | |
|---|--------------------|------------------|----------------|
| \$(000) | | | |
| | 2020 Authorized | 2020 Recorded | Variance |
| 581 Load dispatching | 727 | 679 | 49 |
| 582 Station expenses | 30 | (30) | 60 |
| 583 Overhead line expenses | 164 | 79 | 85 |
| 584 Underground line expenses | 91 | 51 | 40 |
| 585 Street lighting & signal system expenses | 2 | - | 2 |
| 588 Miscellaneous distribution expenses | 1,473 | 2,105 | (632) |
| Total Operation | 2,488 | 2,884 | (396) |
| 591 Maintenance of structures | 38 | 27 | 11 |
| 592 Maintenance of station equipment | 165 | 74 | 91 |
| 593 Maintenance of overhead lines | 1,927 | 2,382 | (455) |
| 594 Maintenance of underground lines | 300 | 606 | (306) |
| 595 Maintenance of line transformers | 16 | - | 16 |
| 596 Maintenance of street lighting & signal systems | 5 | 9 | (4) |
| 597 Maintenance of meters | 46 | 61 | (15) |
| 598 Maintenance of miscellaneous distribution plant | 308 | 787 | (478) |
| Total Maintenance | 2,804 | 3,945 | (1,141) |
| Total Distribution | 5,292 | 6,829 | (1,537) |

Exhibit C-4
Liberty Utilities
2019 General Rate Case
Balancing and Memo Account Balances
(Calendar Year 2020)

| Balancing / Memo Account | Balance as of December 31, 2020 |
|---|---------------------------------|
| Vegetation Management Balancing Account | \$7,005,000 |
| Catastrophic Events Memorandum Account | \$5,489,000 |
| Fire Risk Mitigation Memorandum Account | \$900,000 |
| Wildfire Mitigation Plan Memorandum Account | \$1,976,000 |