

MEMORANDUM

July 17, 1996

TO: DIVISION OF RECORDS AND REPORTING

FROM: DIVISION OF AUDITING AND FINANCIAL ANALYSIS (VANDIVER) *W*

RE: DOCKET NO. 960517-WU -- HEARTLAND UTILITIES, INC.
STAFF-ASSISTED RATE CASE AUDIT REPORT - PERIOD ENDED DECEMBER 31, 1995
AUDIT CONTROL NO. 96-149-3-2

The above-referenced audit report is forwarded. Audit exceptions document deviations from the Uniform System of Accounts, Commission rule or order, Staff Accounting Bulletin and generally accepted accounting principles. Audit disclosures show information that may influence the decision process.

The audit was prepared using a micro computer and has been recorded on one diskette. The diskette may be reviewed using IBM compatible equipment and LOTUS 1-2-3 software. There are no confidential working papers associated with this audit.

Please forward a complete copy of this report to:

Heartland Utilities, Inc.
Howard Short
10405 U.S. 27 South
Sebring, FL 33871-9783

DNV/sp

Attachment

cc: Chairman Clark
Commissioner Deason
Commissioner Johnson
Commissioner Kiesling
Commissioner Garcia
Mary Andrews Bane, Deputy Executive Director/Technical
Legal Services
Division of Auditing and Financial Analysis (Devlin/Causseaux/
File Folder)
Division of Water and Wastewater (Mann)
Orlando District Office (Forbes)

Research and Regulatory Review (Harvey)
Office of Public Counsel

DOCUMENT NUMBER-DATE

07560 JUL 18 1996

FPSC-RECORDS/REPORTING

FLORIDA PUBLIC SERVICE COMMISSION
AUDIT REPORT

TWELVE MONTHS ENDED DECEMBER 31, 1995
FIELD WORK COMPLETED JUNE 28, 1996

HEARTLAND UTILITIES, INC.
SEBRING, FLORIDA
HIGHLANDS COUNTY

STAFF-ASSISTED RATE CASE
DOCKET NUMBER 960517-WU
AUDIT CONTROL NUMBER 96-149-3-2

Richard F. Brown

RICHARD F. BROWN
AUDIT MANAGER

Ian J. Forbes

IAN J. FORBES
REGULATORY ANALYST SUPERVISOR
ORLANDO DISTRICT OFFICE

DOCUMENT NUMBER-DATE
07561 JUL 18 96
FPSC-RECORDS/REPORTING

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I. EXECUTIVE SUMMARY

AUDIT PURPOSE: We have applied the procedures described in Section II of this report to prepare proposed schedules of Rate Base, Net Operating Income, and Capital Structure for the twelve months ended December 31, 1995, for Heartland Utilities, Inc. and prepare pro forma adjustments which are presented as audit disclosures.

SCOPE LIMITATIONS: There were no confidential documents associated with the audit.

DISCLAIM PUBLIC USE: This is an internal accounting report prepared after performing a limited scope audit; accordingly, this document must not be relied upon for any purpose except to assist the Commission staff in the performance of their duties. Substantial additional work would have to be performed to satisfy generally accepted auditing standards and produce audited financial statements for public use.

OPINION: The schedules of Rate Base, Net Operating Income, and Capital Structure for the twelve-month period ended December 31, 1995, represent Heartland Utilities, Inc. Company books and records are maintained in substantial compliance with the Commission directives. The expressed opinions extend only to the scope of work described in Section II of this report.

II. AUDIT SCOPE

The opinions contained in this report are based on the audit work described below. When used in this report, COMPILED means that audit work includes:

COMPILED: means that the audit staff reconciled exhibit amounts with the general ledger; visually scanned accounts for error or inconsistency; disclosed any unresolved error, irregularity or inconsistency; and except as noted, performed no other audit work.

RATE BASE: Prepared Heartland Utilities, Inc. water rate base at December 31, 1995. Traced approximately seventy-five percent of water plant additions from March 31, 1990 through December 31, 1995, to supporting documentation. Compiled additions to contributions-in-aid-of-construction from March 31, 1990 through December 31, 1995, and traced approximately seventy percent to supporting documentation. Recomputed the depreciation reserve and accumulated amortization at December 31, 1995, and computed the working capital allowance on staff-adjusted operation and maintenance expense. Ascertained that all rate base adjustments per Commission Order 24817 were properly reflected via the Utility's books and records.

NET OPERATING INCOME: Prepared Water Net Operating Income Statement for the twelve-month period ended December 31, 1995. Traced approximately eighty percent of test year operating expenses to source documentation. Recalculated individual test year billings on a sample basis.

CAPITAL STRUCTURE: Compiled equity and debt account balances at December 31, 1995, and obtained a copy of loan agreements funding utility investment.

AUDIT EXCEPTION NO. 1

SUBJECT: MISCLASSIFIED CIAC

FACTS: CIAC of \$2,853.60 and \$57,545.00 received in 1993 and 1995, respectively, was charged to revenues.

CIAC should be recorded to Account 271, Contributions-in-Aid-of-Construction to comply with NARUC Water Class "C" Instructions.

OPINION/CONCLUSIONS: Utility was not in compliance with above-referenced Instruction.

RECOMMENDATION: Field staff recommends that the following correcting journal entry be made by Utility:

Account 481-Installation fee revenue	\$57,545.00	
Account 215-Retained earnings	2,853.60	
Account 271-CIAC		\$60,398.60

AUDIT EXCEPTION NO. 2

SUBJECT: FPSC ORDER 23592 ADJUSTMENTS

FACTS: The Utility did not properly adjust its books to reflect Commission Order 23592 adjustments for the test year ended September 30, 1990.

OPINION/CONCLUSIONS: The following differences exist between order and book amounts:

	<u>UPIS</u>	<u>Acc.Dep.</u>	<u>CIAC</u>	<u>Acc.Amort.</u>
Per Comm. Order 23592	\$840,582	\$(181,083)	\$(758,735)	\$274,075
Per Utility records	<u>892,720</u>	<u>(195,796)</u>	<u>(694,690)</u>	<u>279,398</u>
Difference	<u>\$ 52,138</u>	<u>\$ 14,713</u>	<u>\$(64,045)</u>	<u>\$ 5,323</u>

RECOMMENDATION: Field staff recommends that utility plant-in-service, accumulated depreciation, and accumulated amortization-CIAC be decreased by \$52,138, \$14,713, and \$5,323, respectively. CIAC be increased by \$64,045.

AUDIT EXCEPTION NO. 3

SUBJECT: CONTRACTUAL SERVICES

FACTS: Water plant additions, erroneously classified to Contractual Services, attributed to an overstated balance in the account totaling \$40,214.79.

The overstated amount was determined as follows (Attachment A).

		Acct. 331 <u>Mains</u>	Acct. 333 <u>Services</u>	Acct. 334 <u>Meters</u>	Acct. 215 <u>Retained Earnings</u>	<u>Total</u>
Contractual Services (630) balance per Utility	\$56,224.55					
Deductions:						
a.) Amount paid to Excavation Point, Inc. for water line extension (4-17-95/Ck.2140)	(24,019.00)	\$24,019.00				
b.) Amount paid to Kaipainen Engineering to design water line extension (8-4-95/Ck.2260)	(2,500.00)	2,500.00				
c.) Thirteen rebuilt meters (12-18-95/Ck.2398)	(260.00)			\$ 260.00		
d.) Amount paid to S&M Maintenance applicable to main extension (3-24-95/Ck.2111)	(2,000.00)	2,000.00				
e.) Labor/supervision charges paid to S&M Maintenance to install service lines (4-17-95/Ck.2139)	(9,026.00)		\$ 9,026.00			
f.) Amount paid to S&M Maintenance to install 1" service connector (10-26-95/Ck.2344)	(350.00)		350.00			
g.) Amount paid to S&M Maintenance for 48 meters (12-18-95/Ck.2401)	(1,296.00)			1,296.00		
h.) Amount paid to S&M Maintenance for twelve tap-ins	(1,311.02)		1,311.02			
Additions:						
a.) December 1995 plant maintenance bill (S&M Maintenance) (1-2-96/Ck. 2419)	517.23				\$(517.23)	
	<u>\$15,979.76</u>	<u>\$28,519.00</u>	<u>\$10,687.02</u>	<u>\$1,556.00</u>	<u>\$(517.23)</u>	<u>\$56,224.55</u>
		<u>\$40,244.79</u>				

AUDIT EXCEPTION NO. 3 (cont'd.)

In accordance with NARUC Water Class "C" Instruction per Account 101, all capital additions should be charged to utility plant-in-service.

OPINION/CONCLUSIONS: Utility was not in compliance with above-referenced Instruction.

RECOMMENDATION: Field staff recommends that the Utility record the following journal entry:

Account 331, Mains	\$28,519.00	
Account 333, Services	10,687.02	
Account 334, Meters	1,556.00	
Account 215-Retained Earnings	517.23	
Account 630-Contractual Services		\$40,244.79

Depreciation and reserve will be reflected via Audit Exception No. 4.

AUDIT EXCEPTION NO. 4

SUBJECT: DEPRECIATION/AMORTIZATION

FACTS: The Utility did not properly adjust its books to reflect Commission Order 23592 adjustments to utility Plant-In-Service, Accumulated Depreciation, C.I.A.C. and Accumulated Amortization (see Exception 2).

The utility, in instances, did not apply Rule 25-30.140 rates in its calculation of depreciation and amortization.

In accordance with NARUC, Water Class "C" Accounting Instruction #4, depreciation charges shall be computed according to the method that has been approved by the Commission.

OPINION/CONCLUSION: The Utility was not in compliance with the above referenced instruction. Field staff recomputed test year depreciation and the balance in the reserve at December 31, 1995.

RECOMMENDATION: District staff recommends that Accumulated Amortization of C.I.A.C. and Accumulated Depreciation be decreased by \$248,647.51 and \$177,905.11 respectively; that test year amortization and depreciation be increased by \$5,784.47 and \$3,579.85.

AUDIT EXCEPTION NO. 5

SUBJECT: TAXES OTHER THAN INCOME

FACTS: The Utility recorded Taxes Other Than Income during the test year ended December 31, 1995, as follows:

<u>Description</u>	<u>Account</u>	<u>Amount</u>
Payroll Taxes	Non-NARUC 943	\$ 1,608.53
Regulatory Assessment Fee	665	5,685.00
Other Taxes & Licenses	Non-NARUC 941	<u>5,489.15</u>
		<u>\$12,782.68</u>

In accordance with NARUC Water Class "C" Instructions per Account 408, all Taxes Other Than Income should be reflected therein.

OPINION/CONCLUSIONS: Utility was not in compliance with the above-referenced Instruction.

RECOMMENDATION: Field staff recommends that Account 408, Taxes Other Than Income be increased by \$12,782.68, and Accounts 665, 941, and 943 be reduced by \$5,685.00, \$5,489.15, and \$1,608.53, respectively.

AUDIT EXCEPTION NO. 6

SUBJECT: MATERIALS & SUPPLIES

FACTS: The Utility expensed \$2,865.02 of Materials & Supplies, via Account 620, during the test year ended December 31, 1995.

The following expenditures totaling \$2,342.68, applicable to the purchase of meters and/or accessories, were included in the expensed \$2,865.02 of Materials & Supplies expensed:

<u>Payee</u>	<u>Description</u>	<u>Source</u>	<u>Date</u>	<u>Amount</u>
B&H Sales	24 meter boxes/6 meters	CK 2396	12/15/95	\$ 709.96
B&H Sales	12 water meters & acc.	CK 2334	10/13/95	590.43
B&H Sales	12 water meters & acc.	CK 2188	5/26/95	579.09
B&H Sales	12 water meters	CK 2278	8/18/95	385.20
Lighthouse Electric	DCP recov. meter	CK 2136	4/14/95	44.94
B&H Sales	Saddles for meters	CK 2145	4/25/95	<u>33.06</u>
				<u>\$2,342.68</u>

The cost of meters and other devices used for measuring the quantity of water delivered to users shall be charged to Account 101/334, in accordance with NARUC Water Class "C" Instructions.

OPINION/CONCLUSIONS: Utility was not in compliance with above-referenced Instruction.

Depreciation on the plant additions is reflected via Audit Exception No. 4.

RECOMMENDATION: Field staff recommends that Utility Plant Account 101/334, Meter and Meter Installations, be increased by \$2,342.68, and Materials & Supplies, Account 620, be decreased by the same.

AUDIT EXCEPTION NO. 7

SUBJECT: REPAIRS AND MAINTENANCE

FACTS: The Utility paid Powersource, Inc. \$959.98 to rebuild a Peerless 820A water pump on March 10, 1995, via Check 2097.

The amount was charged to non-NARUC Operating Account 930, Repairs and Maintenance.

The expenditures should be capitalized via Plant Account 101/311, Pumping Equipment, to comply with NARUC Water Class "C" Instructions.

OPINION/CONCLUSIONS: Utility was not in compliance with the above-referenced Instruction.

RECOMMENDATION: Field staff recommends that Account 101/311 be increased and 930 be decreased by \$959.98.

AUDIT EXCEPTION NO. 8

SUBJECT: CHEMICALS

FACTS: The Utility charged \$764.50 for chemicals, via Account 618, during the test year ended December 31, 1995.

Field staff determined that \$347.50 of the total \$764.50 was applicable to prior period purchases.

In accordance with NARUC Water Instruction 2-A, Utility books and records should be maintained on the accrual basis.

OPINION/CONCLUSIONS: Utility did not comply with the above-referenced Instruction.

RECOMMENDATION: District staff recommends that Account 618, Chemicals, be reduced by \$347.50 and Net Operating Income be increased by the same.

AUDIT EXCEPTION NO. 9

SUBJECT: PURCHASED POWER

FACTS: The Utility reflected \$7,736.26 of Purchased Power Expense on a cash basis during the test year ended December 31, 1995.

Field staff determined, based on an accrual compilation of all electric billings, that Purchased Power Expense was overstated by \$262.11 during the test year.

In accordance with NARUC Water Instruction 2-A, Utility books and records should be maintained on the accrual basis.

OPINION/CONCLUSIONS: Utility did not comply with the above-referenced Instruction.

RECOMMENDATION: District staff recommends that Purchased Power Expense, Account 615, be reduced by \$262.11 and Net Operating Income be increased by the same.

AUDIT EXCEPTION NO. 10

SUBJECT: MISCELLANEOUS NON-UTILITY EXPENSE

FACTS: The Utility paid \$151.00 to Sebring International Raceway on December 8, 1995, to attend various events at the track.

The amount was charged to non-NARUC Operating Account 928.

All expenses, other than those of utility operations, shall be charged to below the line Account 426 in accordance with NARUC Water Class "C" Instructions.

OPINION/CONCLUSIONS: Utility was not in compliance with above-referenced Instruction.

RECOMMENDATION: Field staff recommends that Account 426 be increased, and Account 928 be decreased by \$151.00.

AUDIT EXCEPTION NO. 11

SUBJECT: WORKING CAPITAL ALLOWANCE

FACTS: The Working Capital Allowance has been computed based on the 1/8 formula method to comply with Commission Order No. 21202.

OPINIONS/CONCLUSIONS: Computed via the formula method, the Working Capital Allowance of \$9412.35 was based on staff-adjusted Operation and Maintenance Expenses of \$75,298.76.

AUDIT DISCLOSURE NO. 1

SUBJECT: INCOME TAXES ON CIAC

FACTS: The Utility received \$5,053.60, \$47,300.00, and \$57,545.00 in 1993, 1994, and 1995, respectively, from DEP to extend its water lines in order to service homes with wells.

OPINION/CONCLUSIONS: The Utility requested that income taxes paid on the DEP grant be offset and netted against the CIAC received (Attachment B). Field staff defers to FPSC analyst for disposition.

Heartland Utilities, Inc.

P. O. Box 1991
Sebring, Florida 33871

July 1, 1996

Florida Public Service Commission

In the past, Heartland Utilities has received CIAC from DEP to extend water lines in our service area to hook up homes with private wells because of EDB and nitrate contamination. These purchase orders have been provided to you. We do not anticipate any substantial future CIAC.

I am requesting that income taxes paid as a result of this CIAC be offset.

Thank you,


Howard Short

HS/cs

AUDIT DISCLOSURE NO. 2

SUBJECT: PLANT MAINTENANCE

FACTS: Heartland Utilities, Inc. retained S&M Maintenance to maintain its two water plants.

S&M submits an itemized monthly bill for its services.

According to Heartland Vice President, Coleen Short, the five-hundred dollars classified as plant maintenance on the bills is for the rental of the office (\$350) and the mowing of the office grounds (\$150).

OPINION/CONCLUSIONS: Field staff submits for informational purposes.

AUDIT DISCLOSURE NO. 3

SUBJECT: MANAGEMENT SERVICES

FACTS: The Utility did not reflect any compensation for services rendered during the test year from co-owners, Howard E. and Coleen C. Short, the respective President and Vice President of the Utility.

The Utility provided field staff with a Contract for Services Agreement dated January 1, 1996, that calls for a monthly fee of \$2,000 for its services (Attachment C).

OPINION/CONCLUSIONS: Defer to FPSC Analyst for disposition.

Heartland Utilities, Inc.

P. O. Box 1991
Sebring, Florida 33871

January 1, 1996

Contract for Services

Howard E. and Coleen C. Short will provide management services to Heartland Utilities for \$2000 per month as follows:

1. Operation and maintenance of Sebring Country Estates and DeSoto City water plants to meet Department of Environmental Protection requirements. This includes a daily check of both water plants and taking chlorine residuals at the plant and remote tap. A permanent log book is kept at each water plant for daily recordings.
2. Take daily readings from the generators. Check the pumps daily and provide maintenance and repair of water lines, meters, valves, and other equipment as needed. Also replace meter boxes and lids.
3. Flushing lines every two months or sooner if needed.
4. Reread meters when customers complain of high water bills. Usually this happens when we change out their meter. Run meter accuracy checks when requested.
5. Turn on meter or turn off meter as requested.
6. Assist contractor in repairing major leaks.
7. Locate water lines for other underground utility contractors (phone, electric, gas).
8. Replace at least 30 meters per year and 15 curb stops.
9. Standby 24 hours per day 350-360 days per year.
10. Bookkeeping services include maintaining records for payables and receivables, making bank deposits, and running errands as necessary. Submitting monthly reports to DEP and SWFMD. Submitting quarterly work to the accountant. Pick up messages at lab where our office was previously, and picking up mail at the post office on a daily basis.


Howard E. Short, Pres.


Coleen C. Short, Sec-Treas.

AUDIT DISCLOSURE NO. 4

SUBJECT: CUSTOMER DEPOSITS

FACTS: Heartland Utilities has requested that its tariff be revised to reflect a fifty instead of a thirty-dollar customer deposit currently in effect (Attachment D).

OPINION/CONCLUSIONS: Defer to FPSC Analyst for disposition.

Heartland Utilities, Inc.

P. O. Box 1991
Sebring, Florida 33871

July 1, 1996

Mr. Richard Brown
Florida Public Service Commission
400 W. Robinson Street
Orlando, Florida 32801-1775

Re: Request for Deposit Increase

Dear Mr. Brown:

Heartland Utilities is requesting a deposit increase from \$30 to \$50 because of several customers in the past have taken off owing more than the \$30 deposit.

The City of Sebring requires a \$60 deposit for water.

Thank you.


Howard Short

HS/cs

HEARTLAND UTILITIES, INC.
 WATER RATE BASE
 @ 12-31-95

EXHIBIT 1

	Per Utility Books @12-31-95	Adjustments	refer to	Staff Adjusted Balance @12-31-95
Utility Plant in Service	\$1,051,887.04	(552,138.00)	AE 2	\$1,043,813.72
		40,762.02	AE 3	
		2,342.68	AE 6	
		959.98	AE 7	
Acc. Depreciation	(345,318.70)	14,713.00	AE 2	(152,700.59)
		177,905.11	AE 4	
CIAC	(794,381.25)	(60,398.60)	AE 1	(918,824.85)
		(64,045.00)	AE 2	
Acc. Amortz. - CIAC	394,070.85	(5,323.00)	AE 2	140,100.34
		(248,647.51)	AE 4	
Working Capital	0.00	9,412.35	AE 11	9,412.35
RATE BASE	\$306,057.94	(\$184,456.97)		\$121,600.97

HEARTLAND UTILITIES, INC.
NET OPERATING INCOME-WATER
@ 12-31-95

	Per Utility Books @12-31-95	Adjustments	refer to	Staff Adjusted Balance @12-31-95
Operating Revenues	\$191,512.56	(\$57,545.00)	AE 1	\$133,967.56
Operating Expenses:				
Operation & Maintenance	132,389.50	(40,244.79)	AE 3	75,298.76
		(12,782.68)	AE 5	
		(2,342.68)	AE 6	
		(959.98)	AE 7	
		(347.50)	AE 8	
		(282.11)	AE 9	
		(151.00)	AE 10	
Depreciation	33,798.36	3,579.85	AE 4	37,378.21
Amortization-CIAC	(24,675.76)	(5,784.47)	AE 4	(30,460.23)
Taxes other than income	101.00	12,782.68	AE 5	12,883.68
Total Operating Expenses	<u>\$141,813.10</u>	<u>(\$46,512.68)</u>		<u>\$95,100.42</u>
Net Operating Income	<u>\$49,899.46</u>	<u>(\$11,032.32)</u>		<u>\$38,867.14</u>

EXHIBIT III

HEARTLAND UTILITIES, INC.
COST OF CAPITAL
TYE 12-31-95

	<u>Cost Per Books</u>	<u>Ratio</u>	<u>Cost Rate</u>	<u>Weighted Cost of Capital</u>
Equity	\$ 5,008.29	1.67	9.7	.16
N/P - Home Savings Bank	287,456.04	95.54	9.0	8.60
Customer Deposits	5,003.00	1.66	8.0	.13
N/P - First Union	<u>3,408.30</u>	<u>1.13</u>	9.0	<u>.10</u>
	<u>\$300,875.63</u>	<u>100.00%</u>		<u>8.99</u>

State of Florida

Commissioners:
SUSAN F. CLARK, CHAIRMAN
J. TERRY DEASON
JULIA L. JOHNSON
DIANE K. KIESLING
JOE GARCIA



DIVISION OF RECORDS &
REPORTING
BLANCA S. BAYO
DIRECTOR
(904) 413-6770

Public Service Commission

July 19, 1996

Howard Short, President
Heartland Utilities, Inc.
Post Office Box 1991
Sebring, Florida 33871-1991

RE: Docket No. 960517-WU -- Heartland Utilities, Inc.
Staff-assisted Rate Case Audit Report - Period Ended March 31, 1995
Audit Control #96-149-3-2

Dear Mr. Short:

The enclosed audit report is forwarded for your review. Any company response filed with this office within ten (10) work days of the above date will be forwarded for consideration by the staff analyst in the preparation of a recommendation for this case.

Thank you for your cooperation.

Sincerely,

A handwritten signature in cursive script that reads "Kay Flynn".

Kay Flynn
Chief, Bureau of Records

KF/mas
Enclosure
cc: Public Counsel