

State of Florida



Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: October 10, 2006
TO: Tiffany L. Joyce, Professional Accountant, Division of Economic Regulation
FROM: Denise N. Vandiver, Chief of Auditing, Division of Regulatory Compliance & Consumer Assistance *DNV*
RE: **Docket No:** 060262-WS **Company Name:** Labrador Utilities, Inc.
Audit Purpose: File and Suspend Rate Case
Audit Control No: 06-209-2-3

Attached is the final audit report for the utility stated above. I am sending the utility a copy of this memo and the audit report. If the utility desires to file a response to the audit report, it should send the response to the Division of Commission Clerk and Administrative Services. There are no confidential work papers associated with this audit.

DNV:sbj
Attachments

Copy: Division of Regulatory Compliance and Consumer Assistance (Hoppe, District Offices, File Folder)
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FPSC-COMMISSION CLERK



FLORIDA PUBLIC SERVICE COMMISSION

DIVISION OF REGULATORY COMPLIANCE & CONSUMER ASSISTANCE
BUREAU OF AUDITING

Tampa District Office

LABRADOR UTILITIES INC.

FILE AND SUSPEND RATE CASE INVESTIGATION

AS OF DECEMBER 31, 2005

DOCKET NO. 060262-WS
AUDIT CONTROL NO. 06-209-2-3

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**DIVISION OF REGULATORY COMPLIANCE & CONSUMER ASSISTANCE
AUDITOR'S REPORT**

October 4, 2006

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

We have performed the procedures described later in this report to meet the agreed upon objectives set forth by the Division of Economic Regulation in its audit service request dated July 27, 2006. We have applied these procedures to the attached schedules which were prepared by Labrador Utilities, Inc. in support of its filing for rate relief in Docket No. 060262-WS.

This audit was performed following general standards and field work standards found in the AICPA Statements on Standards for Attestation Engagements. This report is based on agreed upon procedures which are only for internal Commission use.

OBJECTIVES AND PROCEDURES

RATE BASE

General

Objective: To determine that the utility's filing represents its recorded results from continuing operations.

Procedures: We reconciled the following individual component rate base balances to the utility's general ledger as of December 31, 2005 and verified that adjustments required in Order No. PSC-04-1281-PAA-WS, issued December 28, 2004, were recorded. Audit Finding No. 1 discusses our adjustments to correct the utility's adjustment to UPIS and accumulated depreciation to record the prior order's rate base balance.

Utility-Plant-in-Service (UPIS)

Objective: To determine that property exists and is owned by the utility. To determine that additions to UPIS are authentic, recorded at original cost, and properly classified in compliance with Commission rules and the NARUC Uniform System of Accounts. To verify that the proper retirements of UPIS were made when a replacement item was put in service.

Procedures: We sampled UPIS additions for the period January 1, 2003 through December 31, 2005 for compliance with the stated objectives above. We verified that the utility properly recorded retirements to UPIS when a capital item was removed or replaced. We toured the utility plant sites to observe whether assets additions were completed and to ascertain if asset retirements were properly recorded. We sampled construction project additions and the corresponding source documentation. We verified that the utility used Commission approved AFUDC rates and traced the capitalized salaries to individual employee time sheets. Audit Finding No. 2 discusses our adjustment to remove unapproved organization cost. Audit Finding No. 3 discusses our adjustment to retire UPIS that was replaced. Audit Finding No. 4 discusses our adjustment that corrects the transportation account balance.

Land and Land Rights

Objective: To determine that utility land is recorded at original cost and is owned or secured under a long-term lease.

Procedures: We verified that there have been no changes to the utility's lease of the water and wastewater site property since its last rate proceeding. Audit Finding No. 9 discusses our adjustments to the utility's property lease.

Accumulated Depreciation

Objective: To determine that accruals to accumulated depreciation are properly recorded in compliance with Commission rules and the NARUC Uniform System of Accounts. To verify that depreciation expense accruals are calculated using the Commission authorized rates and that retirements are properly recorded.

Procedures: We traced the accumulated depreciation schedules to the corresponding UPIS schedules. We verified that the utility used Commission authorized rates to depreciate its UPIS accounts by calculating a sample of accumulated depreciation account balances to test for calculation errors. We verified that the utility properly recorded retirements to

accumulated depreciation when the corresponding UPIS was removed or replaced and included an adjustment where replacements to UPIS did not include a retirement amount. We recalculated a sample of accumulated depreciation account balances as of December 31, 2005. Audit Finding No. 2 discusses our adjustment to include the corresponding accumulated depreciation balance for franchise fees that were included in the filing. Audit Finding No. 3 discusses our adjustment to retire UPIS that was replaced and the corresponding effect on accumulated depreciation. Audit Finding No. 4 discusses our adjustment that corrects the accumulated depreciation account balance for transportation equipment.

Working Capital

Objective: To determine that the utility's working capital balance is properly calculated in compliance with Commission rules.

Procedures: We recalculated the utility's working capital balance as of December 31, 2005. Audit Finding No. 8 discusses our adjustment to include a historical working capital balance that was left out of the utility's filing.

Other Rate Base Items

Objective: To determine that other component balances affecting rate base are properly stated and authorized by Commission rules or prior orders.

Procedures: Determine that adjustments to include allocated rate base balances for subsidiary operations are properly reported in the filing. Audit Finding No. 5 discusses our adjustment to remove an unauthorized contribution in aid of construction account balance. Audit Finding No. 6 discusses our adjustments to allocate UIF rate base balances to the utility's wastewater system. Audit Finding No. 7 discusses our adjustments to WSC allocated rate base balances based on the affiliate transaction investigation performed in Docket No. 060253-WS.

NET OPERATING INCOME

General

Objective: To determine that the utility's filing represents its results from continuing operations.

Procedures: We reconciled the following individual component net operating income balances to the utility's general ledger for the 12-month period ended December 31, 2005.

Revenues

Objective: To determine that revenues are properly recorded in compliance with Commission rules and are based on the utility's Commission approved tariff rates.

Procedures: We traced revenues to the general ledger and utility billing registers and selected a sample of customer bills from each customer rate class on a random basis and recalculated the bills using the Commission approved tariff rates. Audit Finding No. 12 discusses our adjustments to correct the utility's revenue adjustments for the test year.

Operation and Maintenance Expenses (O&M)

Objective: To determine that operation and maintenance expenses are properly recorded in compliance with Commission rules and were reasonable and prudent for ongoing utility operations.

Procedures: We sampled O&M expense items from the general ledger based on auditor judgment. We reviewed the sample for the proper utility system, water or wastewater classification, NARUC account, amount, period and recurring nature. We examined invoices and supporting documentation to determine if the above objectives were met. Audit Finding No. 10 discusses our adjustments to remove unauthorized rate case expense. Audit Finding No. 11 discusses our adjustments to WSC allocated expense balances based on the affiliate transaction investigation performed in Docket No. 060253-WS. Audit Finding No. 13 provides information on transportation expense.

Taxes-Other-Than-Income (TOTI)

Objective: To determine that taxes other than income tax expenses is properly recorded in compliance with Commission rules and were reasonable and prudent for ongoing utility operations.

Procedures: We obtained the regulatory assessment fee filings and reconciled them to the general ledger. We obtained the property tax bills for review and to determine if the amount booked reflects the discount amount. Audit Finding No. 12 discusses our adjustments to restate regulatory assessment fees to the actual test year balance and to correct the utility's adjustments for the test year.

Depreciation Expense

Objective: To determine that depreciation expense is properly recorded in compliance with Commission rules and that it accurately represents the depreciation of UPIS assets and amortization of CIAC assets for ongoing utility operations.

Procedures: We recalculated a sample of UPIS depreciation expense and CIAC amortization expense balances for the period using Commission approved rates and we verified that CIAC amortization expense was properly netted against depreciation expense. Audit Finding No. 2 discusses our adjustment to include the corresponding depreciation expense balance for franchise fees that were included in the filing. Audit Finding No. 3 discusses our adjustment to retire UPIS that was replaced and the corresponding effect on depreciation expense.

CAPITAL STRUCTURE

General

Objective: To determine that components of the utility's capital structure and the respective cost rates used to arrive at the overall weighted cost of capital are properly recorded in compliance with Commission rules and that it accurately represents the ongoing utility operations.

Procedures: We reconciled the following individual component capital structure balances to the utility's general ledger as of December 31, 2005. Audit Finding No. 14 provides information on the utility's capital structure component balances.

Long-Term-Debt

Objective: To determine that long-term debt balances represent actual obligations of the utility's parent and that they are properly recorded in compliance with Commission rules.

Procedures: We traced long-term debt balances to the original documents and verified the terms and interest rate of each note payable.

Short-Term-Debt

Objective: To determine that short-term debt balances represent actual obligations of the utility's parent and that they are properly recorded in compliance with Commission rules.

Procedures: We traced short-term debt balances to the original documents and verified the terms and interest rate and period. We recalculated test year interest expense.

Accumulated Deferred Income Taxes

Objective To determine that accumulated deferred income taxes are properly stated and calculated based on the recorded differences between utility book and taxable income.

Procedures Recalculated a sample of deferred tax balances for the period using Commission authorized rates and federal tax rates. Audit Finding No. 15 provides information on the utility's deferred tax balances.

Customer Deposits

Objective: To determine that customer deposit balances represent actual obligations of the utility and are properly recorded in compliance with Commission rules.

Procedures: We traced a sample of customer deposit balances to supporting documentation and verified that customer deposits were refunded and credited with interest payments in compliance with Commission rules.

AUDIT FINDING NO. 1

SUBJECT: CORRECTIONS TO PRIOR ORDER ADJUSTMENTS

SUMMARY: The utility's average water and wastewater rate base balances are overstated by \$23,979 and understated by \$22,252, respectively as of December 31, 2005

STATEMENT OF FACT: Order No. PSC-04-1281-PAA-WS, issued December 28, 2004 required specific adjustments to the utility's utility plant in service (UPIS) and accumulated depreciation balances as of December 31, 2003.

Our analysis of the utility's journal entry to record the ordered adjustments indicates that the utility only recorded some of the required adjustments and that the journal entry was not posted until December 2005.

The schedule on page eight of this report shows the adjustments ordered by the Commission in the above order, the utility's journal entry adjustments posted in December 2005 to book the order, and the additional adjustments needed to correct the utility's posted journal entry.

EFFECT ON GENERAL LEDGER: The following entries are needed to correct the utility's general ledger balances.

Utility Acct. No	NARUC Acct. No.	Account Description	Debit	Credit
1082000	108	Wat & W/Wat Acc/Dep Transportation	\$3,320	
1083621	103	Water Acc/Dep - Structure and Improv.		\$23,348
1083025	108	Water Acc/Dep - Pumping Equip.		\$56
1083043	108	Water Acc/Dep - Tran. And Distr. Mains	\$5,818	
1083094	108	Water Acc/Dep - Tools & Shop		\$2,454
1084003	108	W/Water Acc/Dep - Structure and Improv.	\$1,852	
1084005	108	W/Water Acc/Dep - Sewer Treatment Plant	\$12,858	
2151000	215	Retained Earnings	\$1,444	
3043021	304	Water Structure and Improv.	\$2,703	
3315043	331	Water Tran. And Distr. Mains		\$5,567
3547003	354	W/Water Structure and Improv.		\$18,591
3804005	380	W/Water Sewer Treatment Plant	\$21,455	
4032021	403	Water Dep. Exp. - Structure and Improv.	\$85	
4032043	403	Water Dep. Exp. - Tran. And Distr. Mains		\$130
4033003	403	W/Water Dep. Exp. - Structure and Improv.		\$582
4033005	403	W/Water Dep. Exp. - Sewer Treatment Plant	\$1,193	

EFFECT ON FILING: The utility's average water and wastewater rate base balance should be decreased by \$23,979 (\$21,115 + \$2,864) and increased by \$22,252 (\$2,864 + \$19,388), respectively as of December 31, 2005. The utility's water and wastewater depreciation expense balances should be decreased by \$45 and increased by \$611, respectively, for the 12-month period ended December 31, 2005. See the audit staff's calculations on the following pages.

General Ledger and Filing Adjustments

Adjustment to UPIS: Debit (Credit)

Utility	NARUC		Dec-04	2005	Dec-05	Average
<u>Acct. No.</u>	<u>Acct. No.</u>	<u>Acct. Description</u>	<u>UPIS Adjustment</u>	<u>UPIS Adjustment</u>	<u>UPIS Adjustment</u>	<u>UPIS Adjustment</u>
3043021	304	Structures and Improv.	\$2,703	\$0	\$2,703	\$2,703
3315043	331	T&D Mains	(5,567)	0	(5,567)	(5,567)
Total Water UPIS Adjustment			<u>(\$2,864)</u>	<u>\$0</u>	<u>(\$2,864)</u>	<u>(\$2,864)</u>
3547003	354	Structures and Improv.	(\$18,591)	\$0	(\$18,591)	(\$18,591)
3804005	380	Sewer Treatment Plant	21,455	0	21,455	21,455
Total Wastewater UPIS Adjustment			<u>\$2,864</u>	<u>\$0</u>	<u>\$2,864</u>	<u>\$2,864</u>

Adjustment to Acc/Dep: Debit (Credit)

Utility	NARUC		Dec-04	2005	Dec-05	Average
<u>Acct. No.</u>	<u>Acct. No.</u>	<u>Acct. Description</u>	<u>Acc/Dep Adjustment</u>	<u>Accrual Adjustment</u>	<u>Acc/Dep Adjustment</u>	<u>Acc/Dep Adjustment</u>
1082000	108	Transportation - Order	(\$1,053)	\$0	(\$1,053)	(\$1,053)
1083021	108	Struc. & Improv. - Order	(\$23,136)	\$0	(\$23,136)	(\$23,136)
1083021	108	Struc. & Improv. - Cumulative	(127)	(85)	(212)	(169)
			(\$23,263)	(\$85)	(\$23,348)	(\$23,305)
1083025	108	Pumping Equip.	(\$56)	\$0	(\$56)	(\$56)
1083043	108	T&D Mains - Order	\$5,494	\$0	\$5,494	\$5,494
1083043	108	T&D Mains - Cumulative	195	130	324	259
			\$5,689	\$130	\$5,818	\$5,753
1083094	108	Tools & Shop - Order	(\$2,454)	\$0	(\$2,454)	(\$2,454)
Total Water Acc/Dep Adjustment			<u>(\$21,137)</u>	<u>\$45</u>	<u>(\$21,093)</u>	<u>(\$21,115)</u>

Utility	NARUC		Dec-04	2005	Dec-05	Average
<u>Acct. No.</u>	<u>Acct. No.</u>	<u>Acct. Description</u>	<u>Acc/Dep Adjustment</u>	<u>Accrual Adjustment</u>	<u>Acc/Dep Adjustment</u>	<u>Acc/Dep Adjustment</u>
1082000	108	Transportation - Order	\$4,373	\$0	\$4,373	\$4,373
1084003	108	Struc. & Improv. - Order	\$397	\$0	\$397	\$397
1084003	108	Struc. & Improv. - Cumulative	873	582	1,455	1,164
			\$1,270	\$582	\$1,852	\$1,561
1084005	108	Sewer Treatment Plant - Order	\$15,840	\$0	\$15,840	\$15,840
1084005	108	Sewer Treatment Plant - Cumulative	(1,789)	(1,193)	(2,982)	(2,386)
			\$14,051	(\$1,193)	\$12,858	\$13,454
Total Wastewater Acc/Dep Adjustment			<u>\$19,694</u>	<u>(\$611)</u>	<u>\$19,083</u>	<u>\$19,388</u>

Calculations:

2004 Cumulative Acc/Dep adjustment balance = (2005 adjustment - 2005 Dep. Exp. accrual)

Average Acc/Dep adjustment = (2004 Acc/Dep adjustment + 2005 Acc/Dep adjustment) / 2

UPIS Adjustment to Order and Cumulative Effect

Correcting adjustments to the order balance: Debit (Credit)

Utility <u>Acct. No.</u>	NARUC <u>Acct. No.</u>	<u>Acct. Description</u>	Per Order <u>Adjustment</u>	Correction <u>Required</u>	Per Utility <u>Adjustment</u>
3043021	304	Structures and Improv.	\$2,703	\$2,703	\$0
3113028	311	Pumping Equip.	(557)	0	(557)
3315043	331	T&D Mains	(5,567)	(5,567)	0
3917000	341	Transportation Equip.	(12,217)	0	(12,217)
3466094	346	Tools & Shop	(5,873)	0	(5,873)
Water utility plant in service adjustment			(21,511)	(\$2,864)	(\$18,647)

Utility <u>Acct. No.</u>	NARUC <u>Acct. No.</u>	<u>Acct. Description</u>	Per Order <u>Adjustment</u>	Correction <u>Required</u>	Per Utility <u>Adjustment</u>
3547003	354	Structures and Improv.	(\$18,591)	(\$18,591)	\$0
3804005	380	Sewer Treatment Plant	21,455	21,455	0
3917000	391	Transportation Equip.	(6,836)	0	(6,836)
Wastewater utility plant in service adjustment			(\$3,972)	\$2,864	(\$6,836)

Audit staff's adjustment to UPIS is made as of December 2003.
Therefore the average 2005 ending UPIS adjustment equals the total correction.

Cumulative effect of posting 2003 adjustments in 2005: Debt (Credit)

Utility <u>Acct. No.</u>	NARUC <u>Acct. No.</u>	<u>Acct. Description</u>	Correction <u>Amount</u>	Depreciation <u>Rule Rate</u>	Acc/Dep <u>Adjustment</u>	Dep. Exp <u>Adjustment</u>
3043021	304	Structures and Improv.	\$2,703	3.13%	(\$212)	\$85
3315043	331	Tran. and Distr. Mains	(5,567)	2.33%	324	(130)
Water Acc/Dep and Dep. Exp. adjustment			(\$2,864)		\$113	(\$45)

Utility <u>Acct. No.</u>	NARUC <u>Acct. No.</u>	<u>Acct. Description</u>	Correction <u>Amount</u>	Depreciation <u>Rule Rate</u>	Acc/Dep <u>Adjustment</u>	Dep. Exp <u>Adjustment</u>
3547003	354	Structures and Improv.	(\$18,591)	3.13%	\$1,455	(\$582)
3804005	380	Sewer Treatment Plant	21,455	5.56%	(2,982)	1,193
Water Acc/Dep and Dep. Exp. adjustment			\$2,864		(\$1,527)	\$611

Accumulated depreciation adjustment equals ((Correction amount x Dep. Rate) x 2.5 years)
Depreciation expense adjustment equals (Correction amount x Dep. Rate)

Acc/Dep Adjustment to Order

Correcting adjustments to the order balance: Debit (Credit)

Utility <u>Acct. No.</u>	NARUC <u>Acct. No.</u>	<u>Acct. Description</u>	Per Order <u>Adjustment</u>	Correction <u>Required</u>	Per Utility <u>Adjustment</u>
1082000	108	Acc/Dep - Transportation Equipment	\$8,475	(\$1,053)	\$9,528
1083021	108	Acc/Dep - Structure and Improv.	(23,136)	(23,136)	0
1083025	108	Acc/Dep - Pumping Equip.	14	(56)	70
1083043	108	Acc/Dep - Tran. And Distr. Mains	5,494	5,494	0
1083094	108	Acc/Dep - Tools & Shop	2,397	(2,454)	4,851
Water accumulated depreciation adjustment			(\$6,756)	(\$21,205)	\$14,449

Utility <u>Acct. No.</u>	NARUC <u>Acct. No.</u>	<u>Acct. Description</u>	Per Order <u>Adjustment</u>	Correction <u>Required</u>	Per Utility <u>Adjustment</u>
1082000	108	Acc/Dep - Transportation Equipment	\$4,373	\$4,373	\$0
1084003	108	Acc/Dep - Structure and Improv.	397	397	0
1084005	108	Acc/Dep - Sewer Treatment Plant	15,840	15,840	0
Wastewater accumulated depreciation adjustment			\$20,610	\$20,610	\$0

Audit staff's adjustment to accumulated depreciation is made as of December 2003.
Therefore the average 2005 ending accumulated depreciation adjustment equals the total correction.

AUDIT FINDING NO. 2

SUBJECT: ADJUSTMENT TO ORGANIZATION COST AND FRANCHISE FEES

SUMMARY: The utility's water and wastewater average rate base balances are overstated by \$16,420 and \$1,504, respectively, as of December 31, 2005

STATEMENT OF FACT: In its filing, the utility included average balances of \$15,313 for water organization cost and \$7,933, each, for water and wastewater franchise fees. The filing, however, does not include the corresponding accumulated depreciation and depreciation expense balances. The utility did, however, remove the organization cost from rate base as a proforma adjustment to determine the adjusted test year balance.

The organization cost balance was removed for rate case purposes in the utility's last rate filing and not included in the rate base balance established by the Commission as of December 31, 2003. Therefore, it should be removed for this rate case filing also.

The filing should have included the balances for accumulated depreciation and depreciation expense that correspond to the respective franchise fee accounts.

The utility's general ledger reflects the following accumulated depreciation and depreciation expense balances for franchise fees. The utility did not record any depreciation on the water franchise fees in 2005. Therefore, it should be increased by \$198 (\$7,993 x 2.5% Rule Rate)

<u>System</u>	<u>Utility</u> <u>Acct. No.</u>	<u>Acct. Description</u>	<u>Balance</u> <u>Dec-04</u>	<u>Balance</u> <u>Dec-05</u>	<u>Average</u>
Water	1083002	Acc/Dep - Franchise	(\$1,008)	(\$1,008)	(\$1,008)
W/Water	1084020	Acc/Dep - Franchise	(\$1,405)	(\$1,934)	(\$1,669)
Water	4032002	Dep. Exp. - Franchise		\$0	
W/Water	4033020	Dep. Exp. - Franchise		(\$529)	

It appears that the utility posted the entire depreciation accrual for franchise fees to the wastewater account. The average gross balance for franchise fees is \$23,246. (\$15,3133 + \$7,933) If you divide the wastewater depreciation expense by this amount the result is 2.3 percent which is approximately the same rate of 2.5 percent that is reflected in the utility's annual reports. (\$529/\$23,246) Since the wastewater franchise fee balance equals the water balance of \$7,933, the same amount of \$198 in depreciation expense should be applied.

EFFECT ON GENERAL LEDGER: The following entry should be made to correct the water and wastewater franchise fee accounts.

Utility	NARUC			
<u>Acct. No.</u>	<u>Acct. No.</u>	<u>Account Description</u>	<u>Debit</u>	<u>Credit</u>
1083002	108	Acc/Dep - Franchise - Water		\$198
1084020	108	Acc/Dep - Franchise - W/Water	\$328	
4032002	403	Dep. Exp. - Franchise Water	\$198	
4033020	403	Dep. Exp. - Franchise - W/Water		\$328

EFFECT ON FILING: The utility's water and wastewater average rate base balances should be reduced by \$16,420 and \$1,504, respectively, as of December 31, 2005 and its water and wastewater depreciation expense balances should be increased by \$198, each, respectively for the 12-month period ended December 31, 2005. See our calculations below.

Adjustments to the Filing

	Average	Average	
<u>Acct. No. 301 - Organization Cost</u>	<u>Water</u>	<u>W/Water</u>	
Per Audit	\$0	-na-	
Per Utility	<u>15,313</u>	<u>-na-</u>	
Adjustment	(15,313)	-na-	
	Average	Average	
<u>Acct. No. 108 - Acc/Dep - Franchise Fees</u>	<u>Water</u>	<u>W/Water</u>	
Per Audit	(\$1,107)	(\$1,504)	
Per Utility	<u>0</u>	<u>\$0</u>	
Adjustment	(\$1,107)	(\$1,504)	
Average Rate Base Adjustment	<u>(\$16,420)</u>	<u>(\$1,504)</u>	
	Balance	Balance	
<u>Acct. No. 108 - Acc/Dep - Franchise Fees</u>	<u>Dec-04</u>	<u>Dec-05</u>	<u>Average</u>
Water	(\$1,008)	(\$1,206)	(\$1,107)
Wastewater	(\$1,405)	(\$1,603)	(\$1,504)
	2005	2005	
<u>Acct. No. 403 - Dep. Exp. - Franchise Fees</u>	<u>Water</u>	<u>W/Water</u>	
Per Audit	\$198	\$198	
Per Utility	<u>0</u>	<u>0</u>	
Dep. Expense Adjustment	<u>\$198</u>	<u>\$198</u>	

AUDIT FINDING NO. 3

SUBJECT: ADJUSTMENT TO RETIRE UTILITY PLANT IN SERVICE

SUMMARY: The utility's average rate base is understated by \$265 as of December 31, 2005.

STATEMENT OF FACTS: The utility recorded three capital additions to utility plant in service that should have included a corresponding retirement amount. The utility's policy is to retire 75 percent of the capital assets purchase price when the original cost can not be determined.

Year Added	Utility Acct. No.	NARUC Acct. No.	Account Description	Invoice Ref# and Vendor	Amount	Associated Retirement	Dep. Rate	Dep. Exp.	Acc. Dep.
2004	3113025	311	Pumping Equip.	47231*08189*Thompson	\$4,662	\$3,497	5.00%	\$175	\$262
2005	3345046	334	Meters	81259*00109*Badger M	2,269	1,702	5.00%	43	43
2005	3345046	334	Meters	81259*00109*Badger M	<u>7,350</u>	<u>5,513</u>	5.00%	<u>138</u>	<u>138</u>
					\$14,281	\$10,711		\$355	\$442
								Acc/Dep adjustment @ 12/31/04 (\$442 - \$355)	\$87
								Acc/Dep adjustment @ 12/31/05	\$442

Retirement amount was calculated as 75 percent of the cost of the new asset addition.

Dep. Exp. of \$175 = \$3,497 x 5.0% x 1 year of service

Acc/Dep of \$262 = \$3,497 x 5.0% x 1.5 years of service

Dep. Exp. & Acc/Dep of \$43 = \$1,702 x 5.0% x 0.5 year of service

Dep. Exp. & Acc/Dep of \$138 = \$5,512 x 5.0% x 0.5 year of service

EFFECT ON GENERAL LEDGER: The following entries are needed to correct the utility's general ledger balances to properly record the retirements discussed above.

Utility Acct. No.	NARUC Acct. No.	Account Description	Debit	Credit
1083025	108	Acc/Dep - Pumping Equipment	\$3,759	
1083046	108	Acc/Dep - Meters	\$7,395	
2151000	215	Retained Earnings		\$87
3113025	311	Pumping Equipment		\$3,497
3345046	334	Meters		\$7,214
4032025	403	Dep. Exp. - Pumping Equipment		\$175
4032046	403	Dep. Exp. - Meters		\$181

Calculations:

$$\$3,759 = \$3,497 + \$262$$

$$\$7,214 = \$1,702 + \$5,512$$

$$\$7,395 = \$1,702 + \$5,512 + \$43 + \$138$$

$$\$181 = \$43 + \$138$$

EFFECT ON FILING: The corresponding decreases to utility plant in service and accumulated depreciation have no effect on the utility's rate base filing since they offset each other. However, average test year accumulated depreciation and depreciation expense should be reduced by \$265 (((\$87+\$442)/2) and \$355, respectively, to remove the cumulative effect of the audit staff's retirement entries on the utility's filing.

AUDIT FINDING NO. 4

SUBJECT: ADJUSTMENT TO TRANSPORTATION EQUIPMENT

SUMMARY: The utility's average water and wastewater rate base balances are overstated by \$473 and understated by \$5,234, respectively, as of December 31, 2005.

STATEMENT OF FACT: The utility's filing reflects the following balances for Acct. No. 341 - Transportation Equipment and Acct. No. 108 - Acc/Dep Transportation.

Utility Acct. No.	Balance Dec-04	Balance Dec-05	Average
3917000	\$16,588	(\$2,409)	\$7,090
1082000	(\$3,317)	\$881	(\$1,218)

The utility posted the following entries to the above accounts in 2004 and 2005.

Acct. No. 3917000 - Transportation Equipment

Period	Per Utility		Per Audit		Average
	Activity	Balance	Activity	Balance	
Dec 2003		\$19,053		\$19,053	
Jul 2004	(\$19,053)		(\$19,053)		
Nov 2004	\$16,588		\$16,588		
Dec 2004		\$16,588		\$16,588	
May 2005	\$56		\$56		
Dec 2005	(\$19,053)		\$0		
Dec 2005		(\$2,409)		\$16,644	\$16,616

Acct. No. 1082000 - Acc/Dep Transportation

Period	Per Utility		Per Audit		Average
	Activity	Balance	Activity	Balance	
Dec 2003		(\$9,908)		(\$9,908)	
Jul 2004	\$9,908		\$9,908		
Dec 2004	(\$3,317)		(\$3,317)		
Dec 2004		(\$3,317)		(\$3,317)	
Dec 2005	(\$5,330)		(\$5,330)		
Dec 2005	\$9,528		\$0		
Dec 2005		\$881		(\$8,647)	(\$5,982)

The journal entries posted in December 2005 for \$19,053 and \$9,528 were the utility's adjustment to a prior order balance that is discussed in Audit Finding No. 1 of this report. The entries were not needed because the utility had already removed the balances referenced in the order in July 2004. That is why the utility's balance for Acct. No. 341 is a credit balance and the associated accumulated depreciation account is debit balance, which are contrary to the normal balances expected for these accounts. Both December 2005 journal entries should be reversed to properly state the correct balances for these accounts.

Additionally, transportation equipment balances should be allocated between water and wastewater operations based on customers.

EFFECT ON GENERAL LEDGER: The following entry should be made to correct the transportation accounts balance. The allocation between water and wastewater is done for the filing only.

Utility Acct. No.	NARUC Acct. No.	Account Description	Debit	Credit
1082000	108	Acc/Dep - Transportation		\$9,528
2151000	215	Retained Earnings		\$9,525
3917000	341	Transportation Equipment	\$19,053	

EFFECT ON FILING: The utility's water and wastewater average rate base should be reduced by \$473 and increased by \$5,234 as of December 31, 2005 to correct the account balances and allocate the balance between water and wastewater operations for the filing.

<u>Acct. No. 3917000</u>	<u>Average Balance</u>	<u>Water</u>	<u>Wastewater</u>
Per Audit	\$16,616	\$8,438	\$8,178
Per Utility	<u>7,091</u>	<u>7,091</u>	<u>0</u>
Adjustment	\$9,525	\$1,347	\$8,178
 Acct No. 1082000			
Per Audit	(\$5,982)	(\$3,038)	(\$2,944)
Per Utility	<u>(1,218)</u>	<u>(1,218)</u>	<u>0</u>
Adjustment	(\$4,764)	(\$1,820)	(\$2,944)
 Net Rate Base Adjustment	 \$4,761	 (\$473)	 \$5,234
 Allocated based on customers		 50.78%	 49.22%

AUDIT FINDING NO. 5

SUBJECT: ADJUSTMENT TO REMOVE CONTRIBUTION

SUMMARY: The utility's rate base is understated by \$171 as of December 31, 2005

STATEMENT OF FACT: The utility recorded \$342 of CIAC in Acct. No. 2711010 - CIAC Water in June 2005. Order PSC-03-0638-PAA-WS, states, "... since the utility was built-out at the time of certification, we did not authorize the utility to collect service availability charges on a going-forward basis."

There was no entry in the general ledger or the filing for accumulated amortization of CIAC or CIAC amortization expense for 2005.

Since the Commission did not authorize the company to collect service availability fees, then the amount should be refunded to the customer charged.

EFFECT ON GENERAL LEDGER: The following entry should be made to correct the CIAC account balance.

<u>Utility</u>	<u>NARUC</u>	<u>Account Description</u>	<u>Debit</u>	<u>Credit</u>
<u>Acct. No.</u>	<u>Acct. No.</u>			
1411000	141	Acct. Receivable (customer refund)		\$342
2711010	271	CIAC - Water	\$342	

EFFECT ON FILING: Average CIAC should be reduced by \$171 since it was posted in 2005. (\$342/2)

AUDIT FINDING NO. 6

SUBJECT: ADJUSTMENT TO ALLOCATED UIF RATE BASE

SUMMARY: The utility's average water and wastewater rate base balances are overstated and understated by \$9,766, each as of December 31, 2005 and its net water and wastewater depreciation expense balances are overstated and understated by \$1,221, each, for the 12-month period ended December 31, 2005, because it did not allocate any allocated rate base or depreciation expense balances to its wastewater operations.

STATEMENT OF FACT: The utility's general ledger reflects the following allocated rate base and corresponding depreciation expense balances that were included in its filing for this proceeding. All of the balances were included in the water system filing only.

Utility Acct. No.	NARUC Acct. No.	Acct. Description	Balance Dec-04	Balance Dec-05	Average	Allocated to W/W
1081050	108	Acc/Dep - Office Furniture & Equip	(\$2,525)	(\$2,101)	(\$2,313)	(\$1,138.46)
1083050	108	Acc/Dep - Other Tangible Plant	(6,695)	(5,504)	(6,100)	(3,002.17)
3406050	340	Office Furniture & Equip.	3,116	2,480	2,798	1,377.18
3486050	348	Other Tangible Plant	<u>29,289</u>	<u>21,625</u>	<u>25,457</u>	<u>12,529.94</u>
			\$23,185	\$16,500	\$19,843	\$9,766.48
UIF						
4032090	403	Dep. Exp. - Other Tangible Plant		\$370		
4032091	403	Dep. Exp. - Office Furniture & Equip.		171		
4032094	403	Dep. Exp. - Communication & Equip.		157		
4032095	403	Dep. Exp. - Laboratory & Equip.		4		
4032097	403	Dep. Exp. - Communication Equip.		116		
4032098	403	Dep. Exp. - Other Tangible Plant		251		
WSC						
4032090	403	Dep. Exp. - Office Structures		333		
4032091	403	Dep. Exp. - Office Furniture		488		
4032093	403	Dep. Exp. - Telephones		13		
4032098	403	Dep. Exp. - Other Tangible Plant		<u>578</u>		
				\$2,481		\$1,221.15

The rate base accounts and four of the depreciation expense accounts were allocated from Utilities Inc. of Florida (UIF), the regional office for all of Utilities, Inc. (Parent) Florida systems. These balances were audited in a separate affiliate transaction audit in Docket No. 060253-WS. No adjustments were noted in the audit report dated July 15, 2005.

The rate base accounts allocated from WSC were included as an adjustment to the utility's rate base in the filing and they are addressed in a separate finding in this report along with the corresponding depreciation expense balances reflected above. That finding did not, however, determine an allocation of depreciation expenses between the utility's water and wastewater operations.

The above balances should have been allocated to the utilities water and wastewater systems. The utility's general policy is to allocate common expenses based on the percentage of water and wastewater customers for each system. The utility's customer percentages are 50.78 percent water and 49.22 percent wastewater based on its customer allocation schedule.

EFFECT ON GENERAL LEDGER: The water and wastewater allocation adjustments only apply to the utility's filing.

EFFECT ON FILING: The utility's water and wastewater average net rate base balances should be decreased and increased by \$9,766, each, respectively, as of December 31, 2005. (\$19,843 x 49.22%) The utility's net water and wastewater depreciation expense balances should be decreased and increased by \$1,221, each, respectively, for the 12-month period ended December 31, 2005. (\$2,481 x 49.22%)

AUDIT FINDING NO. 7

SUBJECT: ADJUSTMENT TO ALLOCATED WSC RATE BASE

SUMMARY: The utility's allocated average net rate base from Water Service Corporation (WSC) is \$10,573 as of December 31, 2005. The balance should be further allocated to water and wastewater operations for \$5,369 and \$5,204, respectively.

STATEMENT OF FACT: WSC, the service corporation for the parent company Utilities, Inc., allocates a portion of its common rate base to each subsidiary utility throughout the United States. Labrador Utilities, Inc. received \$8,679, which is the average amount as of December 31, 2005. The allocation is net of accumulated depreciation and accumulated deferred income taxes or approximately 0.50 percent of the total WSC average net rate base of \$1,740,155. The allocation was calculated using a customer equivalent percentage that equates all customers throughout the United States in terms of equivalent residential connections.

The Commission's Division of Regulatory Compliance and Consumer Assistance, at the request of The Division of Economic Regulation, performed an affiliate transaction audit of Utilities, Inc. and its subsidiary WSC for the 12-month period ended December 31, 2005, in Docket No. 060253-WS. The scope of the audit included a review of the WSC rate base components that are allocated to all of its subsidiary operations in 2005. The audit report, issued July 15, 2006, included specific adjustments that increased Labrador Utilities, Inc. allocated average WSC rate base allocation by \$1,894 to \$10,573.

The audit staff has incorporated the findings of the above-mentioned audit report to determine Labrador Utilities, Inc. allocated average WSC rate base balance of \$10,573 for this proceeding.

EFFECT ON GENERAL LEDGER: None, because WSC only allocates its net rate base for rate case proceedings.

EFFECT ON FILING: Increase the utility's average water and wastewater rate base balances by \$962 and \$932, respectively, for the 12-month period ended December 31, 2005.

<u>Simple Average</u>	<u>Total Amount</u>	<u>Water</u>	<u>Allocation Percent</u>	<u>W/Water</u>	<u>Allocation Percent</u>
Per Utility Allocated Rate Base	\$8,679	\$4,407	50.78%	\$4,272	49.22%
Per Audit Allocated Rate Base	<u>\$10,573</u>	<u>\$5,369</u>	50.78%	<u>\$5,204</u>	49.22%
Audit Adjustment	\$1,894	\$962		\$932	

Small differences are due to rounding

AUDIT FINDING NO. 8

SUBJECT: ADJUSTMENT TO WORKING CAPITAL

SUMMARY: The utility's working capital allowance for water and wastewater rate base is \$14,053 and \$22,981, respectively, as of December 31, 2005.

STATEMENT OF FACT: The utility's filing did not include a historical working capital allowance for water and wastewater rate base.

The audit staff has calculated the working capital allowance for water and wastewater rate base to be \$14,053 and \$22,981, respectively, as of December 31, 2005.

	Water	W/Water	Total	
Total O&M Expense	\$112,426	\$183,849	\$296,275	Per MFR Schedule B-1 (Revised) & B
Adjustments (See note below)	<u>0</u>	<u>0</u>	<u>0</u>	
Total Adjusted O&M Expense	\$112,426	\$183,849	\$296,275	
Divided by 8	<u>8</u>	<u>8</u>	<u>8</u>	
Working Capital	\$14,053	\$22,981	\$37,034	

Note: Audit staff adjustments to historical O&M expense in this report include the corresponding affect on working capital in each separate finding.

EFFECT ON GENERAL LEDGER: None, because a working capital adjustment is only calculated for rate case proceedings.

EFFECT ON FILING: Increase water and wastewater rate base by \$14,053 and \$22,981, respectively, as of December 31, 2005.

AUDIT FINDING NO. 9

SUBJECT: ADJUSTMENT TO LAND LEASE EXPENSE

SUMMARY: The utility's water and wastewater O&M expense balances are overstated by \$8,325 and \$8,069, respectively, for the 12-month period ended December 31, 2005

STATEMENT OF FACT: The utility does not own any land. It leases the property from Forest Lake Estates Co-Op, Inc. Order No. PSC-04-1281-PAA-WS; states that the Commission set a cap on the amount that Labrador should be paying to Forest Lake Estates and that the maximum lease amount charged should be the annual rate of return, based on the utility's capital structure, times the original cost of the land when placed in service. At that time the Commission estimated that the total original value of the land for both water and wastewater was \$298,617.

The utility included \$42,165 for lease expense in the filing by allocating \$21,413 for water and \$20,752 for wastewater to Acct. Nos. 675 & 775 - Miscellaneous Expense.

The utility's last authorized rate of return was set at 8.63 percent in its last rate case proceeding.

Per the order calculation discussed above, the maximum amount of lease expense allowed for utility operations is \$25,771. ($\$298,617 \times 8.63\%$)

EFFECT ON LEDGER: There is no effect on the general ledger because the adjustment to lease expense is for rate case purposes only.

EFFECT ON FILING: The utility's water and wastewater O&M expense balances should be reduced by \$8,325 and \$8,069, respectively, for the 12-month period ended December 31, 2005 and the water and wastewater working capital balances should be reduced by \$1,041 and \$1,009, respectively, as of December 31, 2005, which is 1/8th of the O&M expense reductions displayed above.

<u>Lease Expense</u>	<u>Total</u>	<u>Water</u>	<u>Wastewater</u>
Per Audit	\$25,771	\$13,088	\$12,683
Per Utility	<u>42,165</u>	<u>21,413</u>	<u>20,752</u>
Adjustment	(\$16,394)	(\$8,325)	(\$8,069)
Allocated based on customers		50.78%	49.22%

AUDIT FINDING NO. 10

SUBJECT: ADJUSTMENT TO PRIOR RATE CASE EXPENSE

SUMMARY: The utility's water and wastewater operation and maintenance expense (O&M) balances are overstated by \$1,761 and \$2,000, respectively, for the 12-month period ended December 31, 2005, because the rate case expense reflected in the filing is above the amount approved in its last rate case proceeding in Docket No. 030443-WS.

STATEMENT OF FACT: Order PSC-04-1281-PAA-WS, authorized \$68,988 of rate case expenses to be amortized over four years or \$17,247 per year. The utility's new tariffs were approved on February 15, 2004, which is the beginning of the four year amortization period for rate case expense recovery. The unamortized remaining balance is \$35,931 as of December 31, 2005.

Period	Balance Approved	Yearly Amtz.	Accrued Amtz	Un-Amtz. Balance
Feb-04 to Dec-04	\$68,988	(\$15,810)	(\$15,810)	\$53,178
Jan-05 to Dec-05	\$68,988	(\$17,247)	(\$33,057)	\$35,931

The utility has included \$21,008 of prior rate case expense in its filing by allocating \$10,520 to water operations and \$10,488 to wastewater operations in Acct. Nos. 666/766 - Regulatory Commission Expense.

The utility's rate case expense is overstated by \$3,761 (\$21,008 - \$17,247)

EFFECT ON GENERAL LEDGER: There is no adjustment required to the utility's general ledger because rate case expense is determined for rate proceeding purposes. The utility, however, should review the balances for deferred rate case expense in its general ledger to ensure that they properly reflect the approved rate case expense balance discussed above

EFFECT ON FILING: The utility's water and wastewater O&M expense balances should be reduced by \$1,761 and \$2,000, respectively, for the 12-month period ended December 31, 2005 and the water and wastewater working capital balances should be reduced by \$220 and \$250, respectively, as of December 31, 2005, which is 1/8th of the O&M expense reductions displayed below.

Rate Case Expense	Total	Water	Wastewater
Per Audit	\$17,247	\$8,759	\$8,488
Per Utility	<u>21,008</u>	<u>10,520</u>	<u>10,488</u>
Adjustment	(\$3,761)	(\$1,761)	(\$2,000)
Allocated based on customers		50.78%	49.22%

AUDIT FINDING NO. 11

SUBJECT: ADJUSTMENT TO ALLOCATED WSC EXPENSE

SUMMARY: The utility's allocated common operating expense from Water Service Corporation (WSC) is \$34,153 for the 12-month period ended December 31, 2005.

STATEMENT OF FACTS: WSC, the service corporation for the parent company Utilities, Inc., allocates a portion of its common operating expenses to each subsidiary utility throughout the United States. Labrador Utilities, Inc. received \$35,268 or approximately 0.46 percent of \$7,644,705 in total WSC common expenses for the 12-month period ended December 31, 2005. The allocation was calculated using a customer equivalent percentage that equates all customers throughout the United States in terms of equivalent residential connections.

The Commission's Division of Regulatory Compliance and Consumer Assistance, at the request of The Division of Economic Regulation, performed an affiliate transaction audit of Utilities, Inc. and its subsidiary WSC for the 12-month period ended December 31, 2005, in Docket No. 060253-WS. The scope of the audit included a review of the WSC common expenses that are allocated to all of its subsidiary operations in 2005. The audit report, issued July 15, 2006, included specific adjustments that reduced Labrador Utilities, Inc. allocated common expenses by \$1,115 to \$34,153. Additionally, the corresponding adjustment to reduce working capital for this proceeding is \$138.

The audit staff has incorporated the findings of the above-mentioned audit report to determine Labrador Utilities, Inc. allocated average WSC common expenses is \$34,153 for this proceeding. See audit staffs calculations on the following page.

EFFECT ON THE GENERAL LEDGER:

G/L Acct.	Description	Debit	Credit
2151000	Retained Earnings	\$878	
4032098	Dep. Exp. - Computer		\$10
4191010	Interest Income	\$1	
4272090	Interest Expense	\$236	
6329002	Audit Fees		\$405
6369009	Amtz. Exp. - Computer		\$66
6599090	Insurance Exp. - Other		\$384
6759005	Postage Fees		\$249

EFFECT ON THE FILINGS: The utility's water and wastewater O&M expense balances are overstated by \$571 and \$543, respectively, for the 12-month period ended December 31, 2005. Additionally, water and wastewater working capital balances should be reduced by \$70 and \$68, respectively, as of December 31, 2005 which is 1/8th of the O&M expense reductions mentioned above.

Allocation Schedules	Per Company		Adjustment		Per Audit	
	WSC Expense	Labrador	WSC Expense	Labrador	WSC Expense	Labrador
SE51 Allocated Computer	\$545,445	\$3,151	(\$12,634)	(\$76)	\$532,811	\$3,075
SE52 Allocated Insurance	2,114,495	7,267	(156,711)	(384)	1,957,784	6,883
SE60 Allocated General	<u>4,984,765</u>	<u>24,850</u>	<u>(74,972)</u>	<u>(418)</u>	<u>4,909,793</u>	<u>24,432</u>
Per G/L	\$7,644,705	\$35,268	(\$244,317)	(\$878)	\$7,400,388	\$34,390
Remove interest income and expense not included in the filing						
Per MFR				(237)		(237)
				(\$1,115)		\$34,153

SE51

Acct No.	Per Utility	Adjustment	Per Audit
4032098 Dep. - Computer	\$578	(\$10)	\$568
6369009 Amtz. - Computer	<u>155</u>	<u>(66)</u>	<u>89</u>
	\$733	(\$76)	\$657

SE52

Acct No.	Per Utility	Adjustment	Per Audit
6599090 Insurance - Other	\$7,267	(\$384)	\$6,883

SE60

Acct No.	Per Utility	Adjustment	Per Audit
4191010 Interest Income	(\$1)	\$1	\$0
4272090 Interest Expense	(236)	236	0
6329002 Audit Fees	1,191	(405)	786
6759005 Postage Fees	<u>491</u>	<u>(249)</u>	<u>242</u>
	\$1,445	(\$418)	\$1,028

Acct No.	MFR Acct. No.	Adjustment	MFR B-12	MFR B-12
			50.78% Water	49.22% W/Water
4032098 Dep. - Computer	403 *	(\$10)	(\$10)	\$0
4191010 Interest Income	426 **	0	0	0
4272090 Interest Expense	419/427 **	0	0	0
6329002 Audit Fees	632/732	(405)	(206)	(199)
6369090 Amtz. - Computer	636/736	(66)	(34)	(32)
6599090 Insurance - Other	659/759	(384)	(195)	(189)
6759005 Postage Fees	675/775	<u>(249)</u>	<u>(126)</u>	<u>(123)</u>
O&M Expense Adjustment		(\$1,104)	(\$561)	(\$543)
Total WSC allocated expense adjustment		(\$1,115)	(\$571)	(\$543)
Working Capital Adjustment (1/8 of O&M Expense Adjustment)		(\$138)	(\$70)	(\$68)

* This account was only charged to water operations per the reconciliation schedule provided with the MFRs.

** Per utility these two allocations from WSC are not carried forward into the MFR filing so no adjustment is needed.

AUDIT FINDING NO. 12

SUBJECT: ADJUSTMENT TO REVENUES AND TAXES OTHER THEN INCOME

SUMMARY: The utility's water and wastewater revenue balances are understated by \$3,726 and \$645, respectively, and its RAF balances are understated by \$2,014 and overstated by \$764, respectively, for the 12-month period ended December 31, 2005.

STATEMENT OF FACT: The utility's filing reflects balances of \$4,594 and \$16,156 for regulatory assessment fees (RAF) for the 12-month period ended December 31, 2005.

The above amounts were determined by allocating the following invoiced costs based on the percentage of revenues for the water and wastewater systems.

<u>Invoice Ref# and Vendor</u>	<u>Description</u>	<u>Amount</u>
U69264*75260*Florida	Jan - Dec 2004 RAF- Water	\$4,523
U69265*75260*Florida	Jan - Dec 2004 RAF- W/Water	6,293
U83758*75260*Florida	Jan - Jun 2005 RAF - Water & W/Water	9,783
U74858*75260*Florida	Sec. State Corp. filing fee	<u>150</u>
		\$20,749
	Water RAF	\$4,594
	W/Water RAF	\$16,156

Below is the audit staff's recalculation of the utility's RAF balances based on its RAF filings with the Commission in 2005.

<u>RAF</u>	<u>Water</u>	<u>Wastewater</u>	<u>Explanation</u>
Per Audit	\$1,357	\$8,425	Jan - Jun 2005 RAF
	<u>2,836</u>	<u>6,322</u>	Jul - Dec 2005 RAF
	\$4,193	\$14,747	
Per Utility	<u>4,594</u>	<u>16,156</u>	See above
Audit Adjustment	(\$401)	(\$1,409)	

The utility's filing also included the following historical test year adjustments to its revenue balances.

- 1) Water revenues were increased to remove the affect of a \$58,585 interim refund ordered by the Commission in its last rate case proceeding. Commission documents, however, indicate that the actual refund was \$54,808. Therefore, the utility's water revenues are overstated by \$3,777 for the historical test year 2005. Additionally, the utility did not include a corresponding adjustment to water RAF for the increased revenues in the filing. The RAF increase, based on the actual refund amount of \$54,808, would be \$2,466. ($\$54,808 \times 4.5\%$)
- 2) Water revenues were decreased by \$1,128 and wastewater revenues were increased by \$14,338 to include the affect of a change in its tariff rates during the test year.

3) Water revenues were decreased by \$51 and wastewater revenues were increased by \$645 to include the RAF associated with the annualized revenues mentioned above. The utility's water and wastewater revenues are understated by \$51 and overstated by \$646 because the RAF adjustments should have been included in the taxes other than income section of the utility's filing.

EFFECT ON GENERAL LEDGER: The utility's 2005 RAF should be reduced by a net \$1,810 (\$401 + \$1,409) to properly record the actual RAF for the period. The other adjustments are for rate case purposes and have no effect on the general ledger balance.

EFFECT ON FILING: The utility's water and wastewater revenue balances should be decreased by \$3,726 and \$645, respectively, and its RAF balances should be increased by \$2,014 and reduced by \$764, respectively for the 12-month period ended December 31, 2005.

Adjustments to Utility Revenues	Water Revenues	Wastewater Revenues
Per Utility Adjusted Test Year	\$150,591	\$342,700
Adjustment to interim refund	(3,777)	-na-
Remove annualized RAF	<u>51</u>	<u>(645)</u>
Per Audit Adjusted Test Year	\$146,865	\$342,055
 Audit Adjustment	 (3,726)	 (645)

Adjustment to Utility RAF	Water RAF	Wastewater RAF
Per Utility Adjusted Test Year	\$4,594	\$16,156
Adjustment to actual	(401)	(1,409)
Adjustment to interim refund	2,466	-na-
Add annualized RAF	<u>(51)</u>	<u>645</u>
Per Audit Adjusted Test Year	\$6,608	\$15,392
 Audit Adjustment	 \$2,014	 (764)

AUDIT FINDING NO. 13

SUBJECT: INFORMATION ON TRANSPORTATION EXPENSE

SUMMARY: The support supplied by the utility for transportation expense was not sufficient to determine that the charges relate to the specific vehicles used in each system.

STATEMENT OF FACT: The utility uses GE Capital Fleet to manage its fleet of vehicles. GE Capital provides gas cards for the employees to buy fuel for their vehicles and oversees the maintenance of the fleet. The utility provided the total invoice and its internal allocations of those invoices to each utility system. This did not provide us the information necessary to determine that the charges allocated by the utility actually related to vehicles for that system or whether the repairs were reasonable.

EFFECT ON GENERAL LEDGER: Expenses may need to be re-allocated among systems.

EFFECT ON FILING: Expenses may need to be reduced.

AUDIT FINDING NO. 14

SUBJECT: INFORMATION ON CAPITAL STRUCTURE BALANCES

SUMMARY: The utility's average capital structure balance is \$229,314,162 as of December 31, 2005 and its cost rate for long-term debt is 6.73 percent.

STATEMENT OF FACTS: The utility's filing reflects the following capital structure balances prior to the reconciliation with its average rate base as of December 31, 2005.

Class of Capital	Prior Year 12/31/2004	Test Year 12/31/2005	Average	Cost Rate
Long Term Debt	\$112,803,215	\$135,285,191	\$124,044,203	6.81%
Short Term Debt	18,768,000	3,926,000	11,347,000	2.00%
Common Equity	88,963,597	92,611,247	90,787,422	11.77%
Customer Deposits	0	0	0	6.00%
Acc. Deferred Income Tax	<u>43,167</u>	<u>41,898</u>	<u>42,533</u>	0.00%
Totals	\$220,577,979	\$231,864,336	\$226,221,158	

The Commission's Division of Regulatory Compliance and Consumer Assistance, at the request of The Division of Economic Regulation, performed an affiliate transaction audit of Utilities, Inc. and its subsidiary WSC for the 12-month period ended December 31, 2005, in Docket No. 060253-WS. The scope of the audit included a review of the Utilities, Inc., the parent, capital structure component balances as of December 31, 2005. The audit report, issued July 15, 2006, determined the following average balances for Labrador's parent, Utilities Inc. as of December 31, 2005.

Class of Capital	Prior Year 12/31/2004	Test Year 12/31/2005	Average	Cost Rate
Parent Level				
Long Term Debt	\$112,803,215	\$135,285,191	\$124,044,203	6.73%
Short Term Debt	18,768,000	3,926,000	11,347,000	2.00%
* Common Equity	92,087,507	95,673,345	93,880,426	
Labrador Level				
** Customer Deposits	0	0	0	6.00%
** Acc. Deferred Income Tax	<u>43,167</u>	<u>41,898</u>	<u>42,533</u>	0.00%
Totals	\$223,701,889	\$234,926,434	\$229,314,162	

* The cost rate for common equity to be determined after reconciliation to the utility's average rate base.

** These balances do not include other audit adjustments in this report where applicable.

Based on the above-mentioned affiliate audit report findings the average common equity balance should be increased by \$3,093,004 (\$93,880,426 - \$90,787,422), the long-term debt cost rate should be reduced by 0.08 percent (6.81% - 6.73%).

EFFECT ON GENERAL LEDGER: None, because capital structure balances are only used in rate case proceedings

EFFECT ON FILING: To be determined by the analyst in Tallahassee.

AUDIT FINDING NO. 15

SUBJECT: INFORMATION ON DEFERRED TAXES

SUMMARY: The utility reports \$41,898 upon its books in net deferred income taxes in 2005. This amount is reported at average as \$42,533. As a result of our testing as described below, the average balance used in this case should be changed from \$42,533 by \$4,707 to report a net deferred tax balance of \$47,240. This amount contains estimates which have been presented to the utility and are subject to adjustments based upon further findings during this case.

<u>Calculations:</u>	<u>Average</u>	<u>Year End</u>
Beginning Balance	\$42,533	\$41,898
Deferred Income Tax		
Corrections		
State Depreciation	916	916
State Intangible	1,470	1,227
Federal Intangible	2,321	900
Federal Depreciation	<u>Pending</u>	<u>Pending</u>
Total	\$47,240	\$44,941

EFFECT ON FILING: If all the findings are accepted there is no direct effect on rate base or utility income. The effect on capital structure is to reduce the provision for equity and debt by \$4,707 and increase deferred taxes by \$4,707.

Deferred Taxes -- Item 1: Accelerated Depreciation - State of Florida

When the utility takes tax benefits due to accelerated depreciation, the utility must record deferred income taxes. In this case, the utility failed to record sufficient state deferred taxes in its accounts. The estimated correction at average is \$916 and at year end is \$916.

EFFECT ON GENERAL LEDGER:

NARUC

<u>Acct. No.</u>	<u>Acct. Description</u>	<u>Debit</u>	<u>Credit</u>
215	Retained Earnings	\$916	
190	State Deferred Taxes – Depreciation		\$916

Deferred Taxes -- Item 2: Deferred Taxes Intangible Plant – Federal and State of Florida

Intangible plant is recorded as an asset in water and sewer plant accounts as either organization plant or as franchise plant. For income tax purposes, this intangible plant is expensed and deferred taxes are recorded. Intangible plant and deferred taxes for intangible plant during the normal course of business are not reduced unless a utility's assets are sold.

Utility intangible plant did not match the expected balance of deferred income taxes. Further the State of Florida deferred taxes had not been properly recorded. The estimated correction to Federal deferred accounts at average is a decrease of \$2,321 and at year end is \$900. The estimated correction to state deferred account is \$1,470 at average and at year end is \$1,227.

EFFECT ON GENERAL LEDGER:

NARUC

<u>Acct. No.</u>	<u>Acct. Description</u>	<u>Debit</u>	<u>Credit</u>
215	Retained Earnings	\$2,127	
190	Federal Deferred Taxes – Intangible Plant		\$900
190	State Deferred Taxes – Intangible Plant		\$1,227

Deferred Taxes -- Item 3: Accelerated Depreciation – Federal

Accelerated depreciation is a difficult account for a utility to maintain and difficult for the Commission to audit. We found there was a possibility of errors and non utility effects in the account. There was not enough available audit time for staff to verify the details in this account sufficiently to comment the account was free of error, free of non utility effects and reflected necessary Commission adjustments appropriately.

Absent available audit resources, we have asked the utility to present additional information concerning its deferred taxes in this matter. Absent additional audit procedures, we recommend industry staff use reported plant additions, retirements and Commission adjustments along with known state and federal depreciation rates to determine what level for Federal Accumulated Deferred Income Tax is reasonable. Once a Federal Deferred Tax – Accelerated Depreciation level is set, it would be appropriate to revise the estimate presented in item 2: Deferred Taxes -- Accelerated Depreciation State of Florida.

Possible Accounts Affected upon General ledger:

Retained Earnings

State Deferred Income Taxes – Depreciation

Federal Deferred Income Taxes – Depreciation

State Non Utility Deferred Income Taxes – Depreciation

Federal Non Utility Deferred Income taxes -- Depreciation

Deferred Taxes -- Item 4: Accounting for Post 2000 Tap Fees

Treasury Regulation Section 1.118-2(b) (3) excludes customer connection fees from the definition of CIAC for tax purposes. Therefore, Commission staff has advised that subsequent to the year 2000, CIAC in the form of cash tap fees paid to the utility is taxable. This appears to be a significant item in future utility accounting and ratemaking.

The utility records the effects of (1) taxable CIAC and (2) its amortization correctly in its deferred tax accounts, but the also utility reports (3) additional book depreciation in its reports

where no book depreciation exists. Further, it appears that the taxable CIAC effects are at an accelerated rate rather than the straight line rate used by the utility. This reporting does not affect the setting of rates in this case, but it clouds the auditing and determination of deferred taxes and the utility's ongoing and future reports such as annual report schedule F-23 and MFR schedules C-1 and C-2, and C-5. Clarification on this matter is needed.

From the auditor's perspective, it appears the proper accounting for taxable CIAC is to treat the amortization of tax on CIAC as income statement amortization and not provide a corresponding provision for income taxes on this amortization in ratemaking. Treating this item entirely in deferred tax accounts on the balance sheet seems to cause long-lived problems in assessing the impact of taxable CIAC and accelerated depreciation on rates.

Deferred Taxes -- Item 5: Error in Utility MFR

Utility information contained in its filing schedules C-1, C-2 and C-5 that report the provision for income taxes did not match utility schedule B-1 or Annual Report Schedule F-23 or Annual Report Schedule F-3. This type of error causes audit inefficiencies. Staff has relied upon annual report schedules during this audit of deferred income taxes.

Deferred Taxes -- Item 6: AFUDC

Based upon a review of cash flow model, it is apparent that when setting rates for a utility receiving both an income tax allowance and AFUDC, for ratemaking, it is appropriate to adjust the final calculations for income tax expense by the tax effect of equity AFUDC depreciation.

In the past, this item could be considered immaterial but the issue grows as AFUDC is accrued by utilities year-after-year which receive allowances for federal income tax.

Due to audit time constraints, the auditor was not able to fully research this utility's AFUDC history or determine the correct amount of equity AFUDC depreciation in this case.

EXHIBIT 1

Water Rate Base
 Company: Liberator Utilities, Inc.
 Docket No.: 052082-00
 Test Year End: December 31, 2005

Florida Public Service Commission
 Revised Schedule A-1
 Page 1 of 1
 Preparer: Viretrow, Krause

attached
 on:

Line No.	Description	As Reported Balance Per Books	AR Current Year Ended 12/31/2005	Difference	Utility Adjustments	Adjusted Books Balance	Proforma Adjustments	Adjusted Utility Balance	Supporting Schedule(s)
1	Utility Plant in Service (Average)	\$ 541,963	\$ 554,604	\$ (12,741)	-	\$ 554,604	\$ 72,042	\$ 626,646	A-5, A-3
2	Utility Land & Land Rights	30	-	-	-	-	-	-	A-5
3	Less: Non-Used & Unpaid Plant	-	-	-	-	-	-	-	A-3, A-7
4	Construction Work in Progress	78,116	78,116	-	(78,116) D	-	-	-	A-3, A-18
5	Less: Accumulated Depreciation (Average)	(111,220)	(118,445)	7,225	-	(118,445)	66,982	(51,463)	A-9
6	Less: CMC	(171)	(171)	-	-	(171)	-	(171)	A-12
7	Accumulated Amortization of CIAC	-	-	-	-	-	-	0	A-14
8	Acquisition Adjustment	(335,285)	(735,285)	-	335,285	-	-	-	A-3, A-18
9	Accum. Amort. Of Acq. Adjustments	9,204	9,204	-	(9,204) E	-	-	-	A-3, A-18
10	Advances for Construction	-	-	-	-	-	-	-	A-16
11	Working Capital Allowance	-	-	-	-	-	14,053	14,053	A-17, A-3
12	Total Rate Base	\$ 182,508	\$ 188,022	\$ (5,517)	\$ 247,965	\$ 435,589	\$ 14,053	\$ 599,065	

The differences in the 2005 Utility Plant in Service and Accumulated depreciation average balances are directly related to commission ordered adjustments. The adjustments impacted Average Plant 12,741 (25,483) and Accumulated depreciation 7,225 (14,449). See schedules A-5 and A-9.

EXHIBIT 2

Sewer Rate Base

Company: Labrador Utilities, Inc.
 Docket No.: 060262-ws
 Test Year End: December 31, 2006
 Interim [] or Final [x]
 Historic [x] or Projected []

Florida Public Service Commission

Schedule: A-2
 Page: 1 of 1
 Preparer: Virchow, Krause

Explanation: Provide the calculation of average rate base for the test year, showing all adjustments. All non-used and useful items should be reported as Plant Held For Future Use.

Line No.	(1) Description	(2) Balance Per Books	(3) Utility Adjustments	(4) Adjusted Books Balance	(5) Proforma Adjustments	(4) Adjusted Utility Balance	(5) Supporting Schedule(s)
1	Utility Plant in Service	\$ 1,550,631	\$ -	\$ 1,550,061	\$ 61,921 A	\$ 1,611,981	A-6
2	Utility Land & Land Rights	-	-	-	-	-	A-6
3	Less: Non-Used & Useful Plant	-	-	-	- C	-	A-3, A-7
4	Construction Work in Progress	31,815	(31,815) D	-	-	-	A-3, A-18
5	Less: Accumulated Depreciation	(385,535)	-	(385,535)	(2,958) B	(388,493)	A-10, A-3
6	Less: CIAC	-	-	-	-	-	A-12
7	Accumulated Amortization of CIAC	-	-	-	-	-	A-14
8	Acquisition Adjustment	-	-	-	-	-	A-3, A-18
9	Accum. Amort. Of Acq. Adjustments	-	-	-	-	-	A-3, A-18
10	Advances for Construction	-	-	-	-	-	A-16
11	Working Capital Allowance	-	-	-	22,981 F	22,981	A-17, A-3
12	Total Rate Base	\$ 1,196,341	\$ (31,815)	\$ 1,164,526		\$ 1,246,470	

EXHIBIT 3

Net Operating Income Statement - Water

Company: Labrador Utilities, Inc.
 Docket No.: 060262-ws
 Test Year End: December 31, 2005

Florida Public Service Commission

Corrected Schedule B1
 Page 1 of 1

tion:
 Provide

Line No	Description	Corrected Balance Per Books	Utility Test Year Adjustments		Utility Adjusted Test Year	Requested Revenue Adjustment	Requested Annual Revenues	Supporting Schedule(s)
1	OPERATING REVENUES	\$ 93,184	\$ 57,407	A	\$ 150,591	\$ 25,859	\$ 176,449	#N/A
2	Operation & Maintenance	112,426	-		112,426	27,840	140,266	#N/A
3	Depreciation, net of CIAC amort.	20,355	-		20,355	(66,982)	(46,627)	#N/A
4	Amortization	(7,894)	7,894	B	-	-	-	
5	Taxes Other Than Income	14,757	-		14,757	1,605	16,362	#N/A
6	Provision for Income Taxes	(31,671)	31,671	C	-	16,497	16,497	C-1, B-3
7	OPERATING EXPENSES	107,973	39,565		147,538	(21,040)	126,498	
8	NET OPERATING INCOME	\$ (14,789)	\$ 17,842		\$ 3,053	\$ 46,899	\$ 49,952	
9	RATE BASE	\$ 182,506			\$ 430,471		\$ 583,548	#N/A
10	RATE OF RETURN	-8.10%			0.71%		8.56%	

(1) The Amortization expense amount of (\$7,894) agrees to the Annual Report. No deficiency appears to exist. See schedule W-3 Attached.

EXHIBIT 4

Net Operating Income Statement - Sewer

Company: Labrador Utilities, Inc.
 Docket No.: 000282-ws
 Test Year End: December 31, 2005
 Interim [] or Final [x]
 Historic [x] or Projected []

Florida Public Service Commission

Schedule: B-2
 Page 1 of 1
 Preparer: Virchow, Krause

Explanation: Provide the calculation of net operating income for the test year. If amortization (Line 4) is related to any amount other than an acquisition adjustment, submit an additional schedule showing a description and calculation of charge.

(1) Line No.	(2) Description	(3) Balance Per Books	(4) Utility Test Year Adjustments	(5) Utility Adjusted Test Year	(6) Requested Revenue Adjustment	(7) Requested Annual Revenues	(8) Supporting Schedule(s)
1	OPERATING REVENUES	\$ 327,718	\$ 14,984 A	\$ 342,700	\$ 145,481 I	\$ 488,181	B-4, E-2
2	Operation & Maintenance	183,849	-	183,849	39,997 E, F, G, L	223,846	B-6
3	Depreciation, net of CIAC amort.	50,837	-	50,837	2,958 D	53,795	B-14
4	Amortization	529	(529) B	-	-	-	B-3
5	Taxes Other Than Income	37,165	-	37,165	6,973 K, M	44,138	B-15
6	Provision for Income Taxes	15,148	- C	15,148	44,537 J	59,685	
7	OPERATING EXPENSES	287,526	(529)	286,999	94,464	381,463	
8	NET OPERATING INCOME	\$ 40,188	\$ 15,513	\$ 55,701	\$ 50,897	\$ 106,598	
9	RATE BASE	\$ 1,196,341		\$ 1,164,526		\$ 1,246,470	A-2
10	RATE OF RETURN	3.36%		4.78%		8.56%	

Dependents:
 Schedule: A-17

EXHIBIT 5

Requested Cost of Capital

Florida Public Service Commission

Company: Labrador Utilities, Inc.
 Docket No.: 060262-ws
 Test Year End: December 31, 2005
 Schedule Year End: December 31, 2005
 Interim [] or Final [x]
 Historic [x] or Projected []

Schedule: D-1
 Page 1 of 1
 Preparer: Kirsten E. Weeks

Explanation: Provide a schedule which calculates the requested Cost of Capital on a beginning and end of year average basis. If a year-end basis is used, submit an additional schedule reflecting year-end calculations.

Line No.	(1) Class of Capital	(2) Total Capital	(3) Ratio	(4) Cost Rate	(5) Weighted Cost
1	Long Term Debt	\$ 980,319	54.84%	6.81%	3.73%
2	Short Term Debt	89,675	5.02%	2.00%	0.10%
3	Preferred Stock	-	0.00%	0.00%	0.00%
4	Common Equity	717,491	40.14%	11.77%	4.72%
5	Customer Deposits	-	0.00%	6.00%	0.00%
6	Tax Credits - Zero Cost	-	0.00%	0.00%	0.00%
7	Tax Credits - Weighted Cost	-	0.00%	0.00%	0.00%
8	Accumulated Deferred Income Tax	42,533	0.00%	0.00%	0.00%
9	Other (Explain)	-	0.00%	0.00%	0.00%
10	Total	\$ 1,830,018	100%		8.56%

Note: The cost of equity is based on the leverage formula in effect pursuant to Order No. PSC-050006. Since the equity ratio is greater than 40.00%, a(n) 11.77% cost rate has been used.