

FLORIDA PUBLIC SERVICE COMMISSION

AUDIT REPORT

RATE AUDIT

YEAR ENDED DECEMBER 31, 1995

Field Work Completed

November 19, 1996

UNITED WATER FLORIDA INC.

Jacksonville, Florida

Duval County

DOCKET NO. 960451-WS

Audit Control Number 96-214-1-2

Audit Staff

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Minority Opinion

Yes _____ No RTM
Yes _____ No MC
Yes _____ No Dnt
Yes _____ No DD by RH
Yes _____ No evk

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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 audit the schedules of Rate Base, Net Operating Income, and Capital Structure for the test period ending December 31, 1995, prepared by United Water Florida Inc., for their Petition for rate relief, FPSC Docket 960451-WS. This report is not based on confidential information.

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 audited MFR's of Rate Base, Net Operating Income, and Capital Structure for the test period ending December 31, 1995 represent United Water Florida Inc. books and records which have not been maintained in substantial compliance with Commission directives as expressed in the following exceptions and disclosure. The expressed opinions extend only to the scope of the 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, the following definitions shall apply.

COMPILED - 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: Compiled Plant-in-Service; tested selected additions and retirements for the year ended December 31, 1995; recomputed Construction Work in Progress; selected Work Order amounts and traced journal entries to accounts payable ledgers and vendor invoices; recomputed accumulated depreciation balances; recomputed working capital including interest bearing amounts, unfunded reserves, and non-utility transactions; traced CIAC total balances to the general ledger for the year ended December 31, 1995. Traced Accumulated Amortization of CIAC to the general ledger for the year ended December 31, 1995.

NET OPERATING INCOME: Compiled the Operation and Maintenance Expenses for the year ending December 31, 1995; matched company's O&M accounting structure (non-USOA format) to the rate filing format (USOA), and traced data from the general ledger to the company's rate filing schedules; performed a selective analysis of the following accounts: Purchased Water; Purchased Power; Chemicals; Materials and Supplies; Contractual Services Other; Rental; Transportation; Insurance vehicle; Insurance general liability; Insurance workmans comp; Miscellaneous expenses; Purchased Sewage Treatment; Sludge Removal expense. Reviewed selected invoices and selected checks, equipment, and automobile leases, and other documentation to support the accounting data. Reviewed the allocation of corporate management costs and other overhead charges flowing down to the books of United Water Florida (being charged into the Contract Services Management Fees - Clearing account of United Water Florida).

CAPITAL STRUCTURE: Recomputed 13 month averages for each General Ledger account in capital; recomputed cost rates for all General Ledger accounts; reconciled all General Ledger balances of the parent's (United Waterworks, Inc.) capital; obtained copies of all long term debt agreements; recomputed short term debt daily average; recomputed Deferred Income Taxes; recomputed parent company's cost of capital for use in allocating Florida's Equity; recomputed United Water Florida's Weighted Cost.

OTHER: Read the Board of Directors Minutes for 1991 to 1995; obtained federal and state income tax returns; obtained gross receipts tax returns and ad valorem tax returns; obtained internal audit reports for 1994 and 1995.

III. AUDIT EXCEPTIONS:

AUDIT EXCEPTION NO. 1

SUBJECT: UNIFORM SYSTEM OF ACCOUNTS FOR WATER AND WASTEWATER

STATEMENT OF FACT: Rule 25-30.115 F.A.C. (1) states "Water and wastewater utilities shall, effective January 1, 1986, maintain its accounts and records in conformity with the 1984 NARUC Uniform System of Accounts (USOA) adopted by the National Association of Regulatory Utility Commissioners."

AUDIT OPINION: The Company General Ledger does not follow the USOA. The table provided by the Company to cross-reference the General Ledger accounts to the USOA also does not fully comply with the USOA.

AUDIT EXCEPTION NO. 2

SUBJECT: CONTINUING PROPERTY RECORDS

STATEMENT OF FACT: NARUC, Class A, Water Utility, Accounting Instruction 2.A., General - Records, states "Each utility shall keep its books of accounts, and all other books, records, and memoranda which support the entries in such books of account so as to furnish readily full information as to any item included in any account."

Company Policy Number 120, Page 1 of 1, adopted by United Water Florida directs:

"1.1 It is the policy of GWC, where directed by the Regulatory Commission, that each company maintain separate Continuing Property Records (CPR) of the original book costs of all water and sewer plant located within each city, town, village or borough of the company service area."

"The CPR when properly established will provide:

- a) An inventory of property records which may be readily spot checked for proof of existence.
- b) The association of costs with such property units to assure accurate accounting of retirements.
- c) The dates of installation and removal of property units to provide age-life data for use in depreciation studies."

AUDIT OPINION: The Company records do not comply with NARUC Uniform Systems of Accounts Class A Water and Wastewater instructions 2.A. The Company also does not follow its own policy for Continuing Property Records. The Company should be directed to comply with NARUC Accounting Instructions.

AUDIT EXCEPTION NO. 3

SUBJECT: ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION

STATEMENT OF FACT: Rule 25-30.116 (3) F.A.C. states "Discounted monthly AFUDC rate. A discounted monthly AFUDC rate, calculated to six decimal places, shall be employed to insure that the annual AFUDC charged does not exceed authorized levels."

Rule 25-30.116 (3)(b) states "The monthly AFUDC rate, carried out to six decimal places, shall be applied to the average monthly balance of eligible CWIP that is not included in rate base."

Rule 25-30.116 (5) states "No utility may charge or change its AFUDC rate without prior Commission approval."

FPSC Order 21492 dated June 30, 1989, states "Ordered by Florida Public Service Commission that the application of Jacksonville Suburban Utilities Corporation for establishment of an 11.12% AFUDC rate is approved."

The company does not use a monthly discounted rate to calculate monthly AFUDC charges. Instead the company divided the AFUDC rate by 12 and calculates monthly charges.

The company did not use the approved AFUDC rate of 11.12% as of January 1, 1995, but used an AFUDC rate of 14.83%.

If the company had used the approved AFUDC rate and monthly discounted rate for the year 1995, the AFUDC charges would have been \$94,515.00 less than what was booked in 1995.

Total AFUDC Booked by Company in 1995:	330,619.00
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Total AFUDC Estimated Per FPSC Order Rate:	<u>236,104.00</u>
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Amount Difference from Ordered Rate	<u>\$94,515.00</u>
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An AFUDC rate of 14.83% is still being used in 1996.

OPINION: The 1995 rate base should be reduced by \$94,515.00. The projected 1996 and 1997, rate bases should also be adjusted.

AUDIT EXCEPTION NO. 4

SUBJECT: CAPITAL STRUCTURE

STATEMENT OF FACT: Numerous errors were made in the MFRs for Capital Structure:

United Waterworks Inc.

1. Preferred Stock Calculation Error (13 Month General Ledger Average understated \$4,631).
2. Short Term Debt 13 Month Average Calculation overstated \$655,595. (Misstatement of average amount outstanding for December 1994, April and June 1995)
3. Long Term Debt Cost Rate should be 8.18%. (Fallout calculation).
4. Short Term Debt Cost Rate recalculation should be 6.41%. (Fallout calculation).
5. Common Equity Cost Rate should be 11.57%. (Fallout calculation).

United Water Florida

1. Deferred Income Tax 13 Month Average understated \$52,779 (Misstatement of December 1995 Total calculation).
2. Investment Tax 13 Month Average overstated \$853,846 (Misstatement of December 1994 Month Amount).
3. Customer Deposits Cost Rate should be 7.00% when a utility elects not to refund a deposit after 23 Months (F.A.C. Rule 25-30.311(4)(a). Laundries are the only customer deposits held.
4. Investment Tax Cost Rate should be 9.69%. (Fallout Calculation)

AUDIT OPINION: The auditor's recalculated 13 Month average capital structure follows.

United Water Florida, Inc.
 Capital Structure
 13-MONTH AVERAGE
 Rate Base Audit
 Test year ended: 12/31/95

STAFF CALCULATED

Capital Components	UWF Per Book	Equity Allocation based on Parents Capital Structure	Test Year Adjusted	Ratio	Cost Rate	Weighted Cost
Long-Term Debt		32,268,508	32,268,508	52.35%	8.18%	4.28%
Short-Term Debt		291,049	291,049	0.47%	6.41%	0.03%
Preferred Stock		121,588	121,588	0.20%	5.00%	0.01%
Common Equity	59,382,462	26,701,317	26,701,317	43.32%	11.57%	5.01%
Customer Deposits	9,133		9,133	0.01%	7.00%	0.00%
Investment Tax	1,264,038		1,264,038	2.05%	9.69%	0.20%
Acc. Deferred Income Tax	980,755		980,755	1.59%	0.00%	0.00%
	<u>61,636,388</u>	<u>59,382,462</u>	<u>61,636,388</u>	<u>100.00%</u>		<u>9.53%</u>

Equity Percentage $(0.01131/0.4496)+(0.0905)=0.1157$

Allocation based on United Waterworks, Inc. 13 Month Average Capital Structure

	13-Month Average	Ratio	Cost Rate	Weighted Cost
Long-Term Debt	(216,462,668)	54.34%	8.18%	4.45%
Short-Term Debt	(1,952,405)	0.49%	6.41%	0.03%
Preferred Stock	(815,631)	0.20%	5.00%	0.01%
Common Equity	(179,117,000)	44.96%	11.57%	5.20%
	<u>(398,347,704)</u>	<u>100.00%</u>		<u>9.69%</u>

AUDIT EXCEPTION NO. 5

SUBJECT: MFR SCHEDULE A-1 & A-2 RATE BASE: WATER & SEWER

STATEMENT OF FACT: The Company has filed these Schedules entitled 13-month average rate base on a year-end basis instead of the required calculation based on a 13 month average. This results in an overstatement of Water Rate Base of \$1,754,670 and an overstatement of Sewer Rate Base of \$3,487,740.

AUDIT OPINION: The Company should file this Schedule on a 13-month average.

AUDIT EXCEPTION NO. 6

SUBJECT: PROPERTY FOR FUTURE USE

STATEMENT OF FACT: The Company General Ledger reflects \$23,776 in Property for future use. It has been included in Utility Plant in Service, MFR Schedule A-1. The Company shows a \$0 amount for Nonused Plant on MFR A-1.

AUDIT OPINION: \$23,776 should be removed from Rate Base for property not used.

AUDIT EXCEPTION NO. 7

SUBJECT: ACCUMULATED DEPRECIATION

STATEMENT OF FACT: SAB 17 issued February 13, 1990 requires "If a company has previously appeared before this Commission (example would be a revenue rate case) and (1) has received an order to use a certain depreciation rate or set of rates, or (2) a depreciation rate or rates were used to calculate expenses allowed in calculating allowed tariffs, those explicit or implicit depreciation rates from the latest Commission action are in effect until the first Commission action under the new (effective 3-22-84) depreciation rule."

AUDIT OPINION AND CONCLUSION: The Company changed depreciation rates in 1986 from the rates used in the Company's last rate case in 1980.

This change of rates caused the Company to under depreciate sewer plant. The proper balance in year-end accumulated depreciation is \$17,552,424. This balance represents recomputing depreciation from 1981 through 1995 at the same rates in effect in 1980.

The filed 12/31/95 year-end "per books" accumulated depreciation of sewer \$16,909,582 is understated by \$642,842.

The 12/31/95 general ledger balance for accumulated depreciation of sewer \$17,030,424 is understated by \$522,091.

In 1981 and 1982, the Company combined accumulated depreciation for most plant accounts into one amount. In 1983, the Company began to show accumulated depreciation by each plant account.

The 1983 depreciation schedule shows \$3,129,090 labelled "Reserve for Depreciation prior to 1982" separately. Prior accumulated depreciation was not allocated to the plant accounts.

The beginning balance for accumulated depreciation by account equals only the 1982 depreciation.

The \$3,129,090 was written off by 1985.

RECOMMENDATIONS: The Company should adjust the general ledger and filed amounts for the understatement in sewer depreciation.

AUDIT DISCLOSURE NUMBER 1

SUBJECT: O & M EXPENSES

STATEMENT OF FACT: The O & M Water expense accounts contained items which normally are excluded for rate determination (Charity contributions, Rotary dues, etc.).

#675 Miscellaneous Expenses - Water	(\$3,662)
#604 Life Insurance for Officers and Employees - Water	(\$5,336)

The O&M Sewer expense accounts contained items which normally are excluded for rate determination (Charity contributions, Rotary dues, etc.).

#775 Miscellaneous Expenses - Sewer	(\$5,941)
#704 Life Insurance for Officers and Employees - Sewer	(\$12,451)

In another instance, the O & M expense account was mistitled; (Insurance - Water should have been Travel - Water)

#656 Insurance - Water	(\$10,580)
#675 Travel - Water	\$10,580

Rent also was not allocated to sewer. The following entry should be made:

#641 Rent - Sewer	\$51,330
#741 Rent - Water	(\$51,330)

AUDIT DISCLOSURE NUMBER 2

SUBJECT: INVESTOR RELATIONS

STATEMENT OF FACT: \$78,112 was allocated to United Water Florida for United Water Annual Report, Quarterly Reporting, Annual Meeting, Transfer Agent and other. Order Number 11307 and Order Number PSC-96-1320-FOF-WS disallowed all of these expenses. Order Number PSC-94-0119-FOF-TL disallowed half of these expenses.

All of the Investor Relations Expenses were charged to Water.

Schedule of Water Rate Base
 Company: United Water Florida
 Docket # a: 990481-WS
 Test Year Ended: 12/31/97
 Historic [x] or Projected [x]

Florida Public Service Commission
 Schedule: A-1
 Page 1 of 1
 Preparer: F. McGuire

Explanation: Provide the calculation of 13-month 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. Use the Balance Sheet Method approach to determine working capital.

Line No.	Description	Balance Per Book 12/31/95	1996 Adjustments	Projected Balance 12/31/96	1997 Adjustments	Projected Balance 12/31/97	Supporting Schedules
1	Utility Plant in Service	45,337,308	6,767,325	52,104,634	6,696,985	58,804,319	A-5
2	Utility Land & Land Rights	592,798		592,798		592,798	A-5
3	Total Utility Plant in Svc.	45,930,075	6,174,669	52,104,634	7,292,451	59,397,085	
4	Less: Non-Used & Useful Plant	0					
5	Construction Work in Progress	2,790,000	(2,790,000)	0	0	0	
6	Less Accum. Depreciation	(8,272,767)	(1,262,462)	(9,535,229)	(1,598,780)	(11,134,009)	A-6
7	Less CIAC	(21,843,610)	(2,034,100)	(23,877,610)	(894,400)	(24,872,010)	A-12
8	Accumulated Amortiz. of CIAC	4,824,971	523,599	5,348,570	548,107	5,896,677	A-14
9	Acquisition Adjustments	694,326	0	694,326	0	694,326	G-00
10	Accum. Amort. of Acq. Adjustments		0	0	(22,267)	(22,267)	
11	Less Advances for Construction	(152,370)	0	(152,370)	0	(152,370)	A-16
12	Working Capital Allowance	322,467	13,375	335,842	0	335,842	A-17
14	Total	24,193,192	624,971	24,818,163	5,225,091	30,043,254	

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Schedule of Sewer Rate Base
 Company: United Water Florida
 Docket No.: 980451-W5
 Test Year Ended: 12/31/97
 Historic [x] or Projected [x]

Florida Public Service Commission

Schedule A-2
 Page 1 of 1
 Preparer: F McGuire

Line No.	Description	Balance Per	1996	Projected	1996	Projected	Supporting Schedules
		Books	Adjustments	Balance	Adjustments	Balance	
		12/31/95		12/31/96		12/31/97	
1	Utility Plant in Service	73,864,300	16,583,097	90,447,400	13,646,048	104,093,544	A-6
2	Utility Land & Land Rights	1,018,304		1,018,304		1,018,304	A-6
3	Total Utility Plant in Svc.	74,882,703	16,583,097	91,465,800	13,646,048	105,111,848	A-6
4	Less: Non-Used & Useful Plant						
5	Constr. Work In Progress	1,788,000	(1,788,000)	0		0	
6	Less Accum. Depreciation	(16,908,682)	(1,334,078)	(18,243,000)	(3,671,520)	(21,915,180)	A-10
7	Less CIAC	(32,452,129)	(2,107,000)	(34,559,129)	(1,448,100)	(36,007,229)	A-12
8	Accumulated Amortiz. of CIAC	9,872,888	741,477	10,614,185	786,807	11,400,972	A-14
9	Acquisition Adjustments	867,888	0	867,888	0	867,888	
10	Accum. Amort. of Acq Adjustments		0		(32,549)	(32,549)	
11	Less Advances for Construction	0		0	0	0	
12	Working Capital Allowance	625,865	25,864	651,929	0	651,929	A-17
13	Total	28,655,631	12,141,460	50,797,091	6,260,886	80,077,777	

Schedule of Water Net Operating Income
 Water
 Company: United Water Florida
 Schedule Year Ended
 Interim: 1995

Florida Public Service Commission
 Schedule: S-1
 Page 6 of 6
 Docket No: 890451-WB
 Preparer: Just

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.

Line No.	Description	Balance Per Books	Utility Test Year Adjustments	Requested Revenue Requirement @ Present	Requested Annual Adjustment	Requested Revenue Requirement	Supporting Schedule
		\$8,852,515		\$8,852,515	\$1,148,988	\$8,001,461	S-4
1	OPERATING REVENUES						
2	Operation and Maintenance	3,488,048		3,488,048	7,301	3,486,348	S-6
3	Depreciation, Net of CIAC Amort.	517,733		517,733		517,733	S-14
4	Amortization of Acquisition Adjustment	12,752		12,752		12,752	
5	Taxes Other Than FIT	781,334		781,334	51,703	813,038	S-15
	OPERATING EXPENSES	\$4,779,868		\$4,779,868	\$59,005	\$4,838,870	
6	Operating Income Before FIT	\$2,072,648		\$2,072,648	\$1,089,981	\$3,162,811	
7	Provision for Income Taxes	480,128	(100,378)	359,752	410,152	769,904	C-2
8	NET INCOME	\$1,812,521		\$1,712,896	\$679,809	\$2,392,707	
9	Rate Base			\$24,183,182		\$24,183,182	
10	Rate of Return on Rate Base			7.08%		9.80% *	

*Commission Order No. 18531, Docket No. 818071-WB(CR) established for the rate of return to be used in the interim rate proceeding from 12.60% to 13.23%. However United Water Florida waives that right and opts to use that rate of return developed on Schedule D-1.

Schedule of Water Net Operating Income
Wastewater
Company: United Water Florida
Schedule Year Ended
Interim: 1995

Florida Public Service Commission
Schedule: B-2
Page 3 of 3
Docket No: 980491-WB
Preparer: Joel

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.

Line No.	Description	Balance Per Books	Utility Test Year Adjustments	Requested Revenue Requirement @ Present	Requested Annual Adjustment	Requested Revenue Requirement	Supporting Schedule
1	OPERATING REVENUES	\$13,638,708		\$13,638,708	\$1,073,860	\$14,712,568	
2	Operation and Maintenance	8,917,138		8,917,138	6,825	8,923,963	B-4
3	Depreciation, Net of CIAC Amort.	1,020,845		1,020,845		1,020,845	B-8
4	Amortization of Acquisition Adjustment	13,408		13,408		13,408	B-14
5	Taxes Other Than FIT	1,886,525		1,886,525	48,328	1,714,853	B-15
	OPERATING EXPENSES	\$8,817,717		\$8,817,717	\$55,152	\$8,872,869	
6	Operating Income Before FIT	4,021,988		4,021,988	1,018,797	5,040,785	
7	Provision for Income Taxes	791,878	42,384	834,370	383,373	1,217,743	C-2
8	NET INCOME	\$3,230,012		\$3,187,618	\$635,424	\$3,823,042	
9	Rate Base			\$38,855,831		\$38,855,831	
10	Rate of Return on Rate Base			8.25%		8.88% *	

*Commission Order No. 18531, Docket No. 818971-WB(CR) established for the rate of return to be used in the interim rate proceeding from 12.40% to 13.23%. However United Water Florida values that right and opts to use that rate of return developed on Schedule D-1.

F:\CASES\JAX\01_PG_2.WK1
 Reconciliation of Capital Structure to
 Requested Rate Base
 13-Month average
 Company: United Water Florida
 Docket No.: 980451-WS
 Test Year ended: 12/31/95
 Historic [x] or Projected []

Florida Public Service Commission

Schedule D-2
 Page 1 of 8
 Preparer: McGuire

Explanation: Provide a reconciliation of the 13-Month Average capital structure to requested rate base.
 Explain all adjustments made. Submit an additional schedule if a year-end basis is used.

<u>Line No.</u>	<u>Class of Capital</u>	<u>Reconciled to To Requested Rate Base</u>	<u>Equity Allocation based on Parent Cap. Struct. See D-2, Page 3</u>	<u>Test Year Adjusted</u>	<u>Ratio</u>
	Test Year ended 12/31/95				
1	Long-Term Debt				
2	Short-Term Debt		32,215,817	32,215,817	51.60%
3	Preferred Stock		388,148	388,148	0.62%
4	Common Equity***		120,700	120,700	0.19%
5	Customer Deposits	59,382,462	26,657,799	26,657,799	42.70%
7	Tax Credit-wtd cost	9,133		9,133	0.01%
8	Accum. Deferred Inc. Tax	2,117,884		2,117,884	3.39%
9	Total	<u>927,976</u>		<u>927,976</u>	<u>1.49%</u>
		<u>62,437,455</u>	<u>59,382,462</u>	<u>62,437,455</u>	<u>100.00%</u>

*** Allocation based on United Waterworks (Parent)
 United Waterworks 13-Month Average Capital Structure
 (see D-2, Pg 3)

<u>Line No.</u>	<u>Class of Capital</u>	<u>(Thousands of \$)</u>	<u>See Schedule D-2, Page 3</u>
11	Short-Term Debt	2,608	0.65%
12	Long-Term Debt	216,462	54.25%
13	Preferred Stock	811	0.20%
14	Common Equity	<u>179,117</u>	<u>44.89%</u>
		<u>\$398,998</u>	<u>100.00%</u>

State of Florida

Commissioners:
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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

November 25, 1996

Mr. Munipalli Sambamurthi
United Water Florida, Inc.
Post Office Box 8004
Jacksonville, Florida 32239-0004

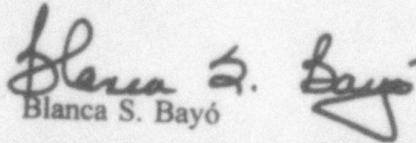
RE: Docket No. 960451-WS -- United Water Florida, Inc.
Rate Case Audit Report - Period Ended December 31, 1995
Audit Control # 96-214-1-2

Dear Mr. Sambamurthi:

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,


Blanca S. Bayo

BSB/cls
Enclosure
cc: Public Counsel
Martin Law Firm