

MEMORANDUM

September 9, 1998

TO: DIVISION OF RECORDS AND REPORTING
FROM: DIVISION OF AUDITING AND FINANCIAL ANALYSIS (VANDIVER) *a*
RE: DOCKET NO. 980726-WU -- DIXIE GROVE ESTATES, INC.
STAFF-ASSISTED RATE CASE
AUDIT CONTROL NO. 98-196-2-1

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 audit report to:

Dixie Grove Estates, Inc.
Judron F. Potter
P. O. Box 845
New Port Richey, FL 34656-0845

DNV/sp

Attachment

cc: Chairman Johnson
Commissioner Clark
Commissioner Deason
Commissioner Garcia
Commissioner Jacobs
Mary Andrews Bane, Deputy Executive Director/Technical
Legal Services
Division of Auditing and Financial Analysis (Devlin/Causseaux/
File Folder)
Division of Water and Wastewater (Casey)
Tampa District Office
Research and Regulatory Review (Harvey)
Office of Public Counsel

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FPSC-RECORDS/REPORTING



FLORIDA PUBLIC SERVICE COMMISSION

*DIVISION OF AUDITING AND FINANCIAL ANALYSIS
BUREAU OF AUDITING*

TAMPA DISTRICT OFFICE

DIXIE GROVE ESTATES, INC.

STAFF ASSISTED RATE CASE

HISTORICAL YEAR ENDED JUNE 30, 1998

DOCKET NO. 980726-WU

AUDIT CONTROL NO. 98-196-2-1

A handwritten signature in cursive script, appearing to read "Simon Ojada", written over a horizontal line.

Simon Ojada, Audit Manager

A handwritten signature in cursive script, appearing to read "James A. McPherson", written over a horizontal line.

James A. McPherson, Audit Supervisor

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**DIVISION OF AUDITING AND FINANCIAL ANALYSIS
AUDITOR'S REPORT**

AUGUST 21, 1998

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

We have applied the procedures described later in this report to prepare the accompanying schedules of Rate Base, Net Operating Income, and Capital Structure for the historical 12-month period ended June 30, 1998, for Dixie Grove Estates, Inc. These schedules were prepared by the auditor as part of the utility's petition for a Staff Assisted Rate Case in Docket No. 980726-WU. There is no confidential information associated with this audit, and there are no audit staff minority opinions.

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.

In our opinion, the schedules referred to above present fairly, in all material respects, the utility's books and records, maintained in conformity with accounting practices prescribed by the Florida Public Service Commission. The expressed opinion extends only to the scope of work described in this report. The attached findings discuss all differences and other matters which were noted during our examination.

SUMMARY OF SIGNIFICANT FINDINGS:

The utility collects a \$30.00 deposit from its customers and does not pay interest on the deposits. Rate base was adjusted to reconcile with prior Commission Orders, increased for capital items that were expensed per books, and reduced for unsupported plant additions.

SUMMARY OF SIGNIFICANT PROCEDURES

Our audit was performed by examining, on a test basis, certain transactions and account balances which we believe are sufficient to base our opinion. Our examination did not entail a complete review of all financial transactions of the company. Our more important audit procedures are summarized below. The following definitions apply when used in this report:

Compiled - The exhibit amounts were reconciled with the general ledger, and accounts were scanned for error or inconsistency.

Reviewed - The exhibit amounts were reconciled with the general ledger. The general ledger account balances were traced to subsidiary ledgers, and selective analytical review procedures were applied.

Verify - The item was tested for accuracy, and substantiating documentation was examined.

RATF BASE: Prepared a schedule from annual reports and compiled account balances for Utility-Plant-in-Service (UPIS), Contributions-in-Aid-of-Construction (CIAC), accumulated depreciation, and accumulated amortization of CIAC from December 31, 1980. Reconciled rate base balances authorized in Commission Order No. 10535, issued 1-20-82 to December 31, 1980 annual report. Reviewed for CIAC additions. Calculated working capital using one-eighth of operation and maintenance expenses. Calculated accumulated depreciation. Computed amortization of CIAC using PSC authorized rates.

NET OPERATING INCOME: Compiled utility revenue and operation and maintenance accounts for the period ended June 30, 1998. Chose a judgmental sample of customer bills and recalculated using FPSC approved rates. Reviewed operation and maintenance expenses and examined invoices or other supporting documentation. Recalculated depreciation expense. Verified taxes other than income.

CAPITAL STRUCTURE: Compiled components of the capital structures for the period ended June 30, 1998.

Exception No. 1

Subject: Plant-in-Service

Statement of Fact: Plant in Service was last determined by FPSC as of 9-30-80. FPSC Order No. 10535 issued on 1-20-82 recommended adjustments to plant totaling \$3,716. However, Dixie Grove Estates has not made the recommended adjustments.

The utility was requested to provide invoices and supporting documentation for all plant additions and retirements to utility plant in service from January 1, 1981 through June 30, 1998. The utility was unable to provide invoices or other supporting documentation to substantiate plant additions totaling \$12,496 recorded in its books from January 1, 1987 to December 31, 1994. The utility claimed that the gas chlorination equipment malfunctioned and destroyed their records.

According to the utility officer, all major additions were due to the following: (1) Conversion from gas chlorine to liquid chlorine, (2) a new hydrotank at well No. 2, (3) a new submersible pump at well No. 3, and (4) DEP ordered that the well head at well No. 3 be enclosed with a weather barrier.

Per the National Association of Regulatory Utility Commissioners (NARUC), Regulations to Govern the Preservation of Records of class C Water Utilities, General instructions 2 (B) state: "All books of accounts, together with records and memoranda supporting the entries therein, shall be kept in such a manner as to support fully the facts pertaining to such entries."

The company capitalized \$400 computer software in 1996.

Recommendation: The utility should increase account (304) Structures and Improvements by \$3,811, reduce account (330) Distribution Reservoir by \$2,712, and increase account (347) Other Misc. Equipment by \$2,617 to record PSC recommended adjustments as contained in Order No. 10535.

The auditor reduced Plant in Service by \$12,896 (\$12,496 + \$400) for the unsupported plant additions without associated plant retirements and the computer software which should have been expensed. Audit staff defers to the analyst and the engineer as to the reasonableness of these plant additions.

Exception No. 2

Subject: Customer Deposits

Statement of Fact: The utility collects a \$30.00 deposit from its customers and does not pay interest on the customer deposits.

Florida Administrative Code No. 25-30.311(4) states, "(a) Each utility which requires deposits to be made by its customers shall pay a minimum interest on such deposits of 6 percent per annum .

... (b) The deposit interest shall be simple interest in all cases and settlement shall be made annually, either in cash or by credit on the current bill. This does not prohibit any public utility paying a higher rate of interest than required by this rule."

Recommendation: The utility should be required to pay 6 percent annual interest on customer deposits.

Exception No. 3

Subject: Accumulated Depreciation/Expense

Statement of Fact: Rule 25-30.140 FAC establishes the useful life of depreciable assets for Class C utilities effective March 22, 1984. Prior to this date, the FPSC approved rate was 2.5%. Subsection 4 (b) states "All class C utilities shall maintain depreciation rates and reserve activity data by total depreciable plant, function or account as prescribed by this commission."

Depreciation expense and accumulation of depreciation were recomputed by the auditor from the last rate case as established by the commission (FPSC Order No. 10535 issued 1-20-82 for Dixie Grove Estates water system). The rate (2.5%) as prescribed by the FPSC order was used through 6-30-97. The rates as prescribed by Rule 25-30.140 FAC for class C utilities were used for the test period.

Recommendation: The utility did not use the Commission recommended rates in determining the depreciation of its depreciable assets. Audit staff stopped depreciating the individual asset accounts that became fully depreciated.

Below is the auditor's recomputed depreciation expense for the test year and the accumulated depreciation.

	Expense	Accum
Balance in Utility	1,073	48,730
Balance Per Audit	<u>2,141</u>	<u>37,749</u>
Difference	1,068	10,981

The utility should be required to follow the rules as prescribed by 25-30.140 FAC for depreciation expense and accumulated depreciation. Accept auditor's computed amount for rate making purposes.

Exception No. 4

Subject: Contribution in Aid of Construction (CIAC)

Statement of Fact: FPSC Order No. 10535 issued 1-20-82 established CIAC and Accumulated Amortization of CIAC as of 9-30-80 to be \$9,680 and \$3,953 respectively. These amounts were not recorded in the utility books and records.

In June 1998, the utility recorded \$663 as CIAC for the cost of a new line connection. The corresponding debit was to Accounts Receivable. This addition had not been paid for and the cost was not recorded in Plant in Service.

Recommendation: The auditor started with the balance of CIAC and accumulated amortization of CIAC per PSC Order, used PSC authorized rate of 2.5 percent for 1981 - 1997, and applied the annual composite depreciation rate of 3.88 percent derived from 1998 depreciation schedules for the test period.

	<u>CIAC</u>	<u>ACCUM</u>	<u>TEST YR AMORTZ</u>
Balance per utility	663	0	0
Balance per audit	<u>10,343</u>	<u>8,468</u>	<u>401</u>
Difference	9,680	8,468	401

The utility should adjust its books to reflect FPSC approved amounts for CIAC and amortization as shown above.

The utility should also increase account (331) Transmission & Dist. Mains by \$663 to reflect the cost of the connection.

Exception No. 5

Subject: Operation and Maintenance Expense

Statement of Fact: The utility recorded \$30,297 as Contractual Services for the 12 month period ending June 30, 1998.

Opinion: Out of the \$30,297 recorded as Contractual Services, \$5,925 were capital items made up of Pumping Equipment (\$239), Distribution Reservoirs (\$4,136), Transmission and Dist. Mains (\$1,075), Meters and Meters Installations (\$475).

Also, included in Contractual Services were water testing expense of \$2,130. The tests are conducted every three years. Therefore, we removed two thirds of these costs.

We also removed from Contractual Services \$290 out of period expenses and added \$1,420 of test year expenses that had not been recorded as of June 30, 1998.

Recommendation: The following adjustments were made by staff to correct all misclassifications made to operation and maintenance expense account.

Out of period expenses	(290)	
Period expenses noted	<u>1,482</u>	1,192
Items to be capitalized		
Pumping Equipment	(239)	
Distribution Reservoirs	(4,136)	
Transmission and Dist. Mains	(1,075)	
Meters and Meter installations	<u>(475)</u>	(5,925)
Others (2/3 of expenses incurred every 3 yrs)		(1,420)
Total adjustments to O&M expenses.		<u>(6,153)</u>

The utility should be required to record all capital items above

Accept auditor's Operation and Maintenance Expense adjusted balance for rate making purposes.

Exception No. 6

Subject: Taxes Other Than Income

Statement of Fact: The utility included a late filing fee of \$67 for 1997 tangible personal property taxes in Taxes Other Than Income.

Also, the company recorded \$870 as Regulatory Assessment Fee for the test period ended June 30, 1998. The total revenue recorded for the period was \$27,159.

Recommendation: The auditor increased the Regulatory assessment fee of \$870 by \$352 to a total of \$1,222 (Total Revenue of \$27,159 X .045). Taxes Other Than Income was also reduced by \$67 to reflect the late filing fee.

Disclosure No. 1

Subject: Land

Statement of Fact: Dixie Grove Estates, Inc. owns the land on which all utility plant is situated. Land, in the amount of \$1,211 was originally recorded in utility books. In 1995, the utility sold part of the land and reduced the value by \$1,000 leaving a balance of \$211 in its books.

Recommendation: Accept \$211 as the value of utility land for rate making purposes.

Disclosure No. 2

Subject: Capital Structure/Related Party Transactions.

Statement of Fact: Dixie Grove Estates, Inc. has a negative retained earnings balance. All loans in the capital structure are from the owners and previous owners of the utility. Interest on the loans is accrued every month. The utility is not making payments on the principal or the interest.

Below are the details of the loans.

<u>Name</u>	<u>Interest Rate</u>	<u>Loan Balance</u>
F W Potter	8%	\$ 9,378
J F Potter	12.5%	\$12,636
M A Potter	8%	\$ 2,677
Total as @ 6/30/98		<u>\$24,691</u>

Recommendation: Since the retained earnings balance is negative, the utility's capital structure is 100% debt. The auditor defers to the analyst as to the treatment of the loans.

Disclosure No. 3

Subject: Proposed New Submersible Well

Statement of Fact: Dixie Grove Estates, Inc. submitted an estimated cost of capital improvements of \$8,000 to \$10,000. The estimated amount is the cost of providing the design, permit, and construction of a new submersible well to replace the pumping equipment at well No. 2 which is currently not in use. The utility has three wells. Only one of the wells is currently used and useful.

Recommendation: Staff defers to the Division of Water and Wastewater as to the cost of the improvement.

SCHEDULES FOR STAFF ASSISTED RATE BASE
DIXIE GROVE ESTATES, INC.
DOCKET NO. 980726-WU
RATE BASE - WATER
TEST YEAR ENDED 06/30/98

EXHIBIT 1

(a) DESCRIPTION	(b) PER BOOKS 06/30/98	(c) AUDIT EXCEP. 06/30/98	(d) REFER TO	(e) PER AUDIT 06/30/98
UTILITY PLANT IN SERVICE	57,725	3,716 (12,896) 663 5,925	1 1 4 5	55,133
LAND	211	0		211
PLANT HELD FOR FUTURE USE	0	0		0
CIAC	(663)	(9,680)	4	(10,343)
AMORTIZATION OF CIAC	0	8,468	4	8,468
ACCUMULATED DEPRECIATION	(48,730)	10,981	3	(37,749)
WORKING CAPITAL	0	6,015	(1)	6,015
TOTAL	<u>8,543</u>	<u>13,192</u>		<u>21,735</u>

(1). Working Capital Formula: 1/8 Operating and Maintenance Expense.

(2). All amounts rounded to the nearest whole dollar.

SCHEDULES FOR STAFF ASSISTED RATE BASE
DIXIE GROVE ESTATES, INC
DOCKET NO 980726-WU
NET OPERATING INCOME - WATER
TEST YEAR ENDED 06/30/98

EXHIBIT II

DESCRIPTION	(1) BALANCE PER BOOKS 06/30/98	(2) AUDIT EXCEPTION ADJUST	(3) Refer to	(4) AUDITED BALANCE
OPERATING REVENUES	27,159		0	27,159
<hr/>				
OPERATING EXPENSES				
OPERATION AND MAINTENANCE EXPENSE	54,273	(6,153)	5	48,120
DEPRECIATION EXPENSE	1,073	1,068	3	2,141
AMORTIZATION EXPENSE	0	(401)	4	(401)
TAXES OTHER THAN INCOME	3,987	284	6	4,271
TOTAL OPERATING EXPENSES	59,333	(5,202)		54,131
NET OPERATING INCOME/LOSS	(32,174)	(5,202)		(26,972)

DIXIE GROVE ESTATES, INC.
DOCKET 980726-WU
CAPITAL STRUCTURE
AS OF JUNE 30, 1998

EXHIBIT III

DESCRIPTION	(a) BALANCE PER T/B 06/30/97	(b) BALANCE PER T/B 06/30/98	(c) SIMPLE AVERAGE PER T/B	(d) AUDIT ADJUST- MENTS	(e) BALANCE PER AUDIT 06/30/98	(f) SIMPLE AVERAGE PER AUDIT	(g) RATIO	(h) COST RATE	(i) WEIGHTED COST OF CAPITAL
COMMON EQUITY (A)	11,197	(17,807)	(3,305)	0	(17,807)	(3,305)	0.00%	10.46%	0.00%
COMMON STOCK	10,000	10,000	10,000		10,000	10,000			
RETAINED EARN.	1,197	(27,807)	(13,305)		(27,807)	(13,305)			
PD IN CAPITAL	0	0	0	C	0	0			
L/T DEBT- FWP	9,166	9,378	9,272		9,378	9,272	52.14%	8.00%	4.17%
L/T DEBT- JFP	4,768	12,636	8,702	0	12,636	8,702	48.93%	12.50%	6.12%
L/T DEBT- MAP	1,000	2,677	1,839		2,677	1,839	10.34%	8.00%	0.83%
CUSTOMER DEPOSITS	1,145	1,406	1,276		1,406	1,276	7.17%	6.00%	0.43%
OTHER					0	0	0.00%	0.00%	0.00%
TOTAL	27,276	8,290	17,783	0	8,290	17,783	118.59%		11.55%

Required Footnotes:

- (1) Audit adjustments do not include audit disclosures.
- (2) Equity cost based on FPSC Order No 97-0660-FOF-WS issued 6/10/97.

STATE OF FLORIDA

Commissioners:
JULIA L. JOHNSON, CHAIRMAN
J. TERRY DEASON
SUSAN F. CLARK
JOE GARCIA
E. LEON JACOBS, JR.



DIVISION OF RECORDS & REPORTING
BLANCA S. BAYÓ
DIRECTOR
(850) 413-6770

Public Service Commission

September 10, 1998

Judson F. Potter, President
Dixie Grove Estates, Inc.
Post Office Box 845
New Port Richey, Florida 34656-0845

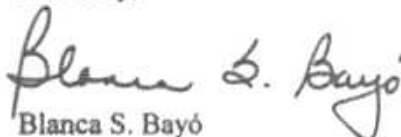
Re: Docket No. 980726 - WU - Dixie Grove Estates, Inc.
Audit Report - Staff-assisted Rate Case - Period Ended June 30, 1998
Audit Control # 98-196-2-1

Dear Mr. Potter:

The enclosed audit report is forwarded for your review. Any company response filed with this office within ten (10) work days of the above case 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. Bayó

BSB/abf
Enclosure

cc: Public Counsel
Division of Audit and Financial Analysis