

ORIGINAL

*DOCKET NO.:* 960444-WU - [Lake Utility Services, Inc.]

*WITNESS:* **Direct Testimony Of Charleston J. Winston**, Appearing On  
Behalf Of The Staff Of The Florida Public Service Commission,  
Division Of Auditing And Financial Analysis

*DATE FILED:* February 8, 1999

DOCUMENT NUMBER-DATE

**01630 FEB-8 99**

FPSC-RECORDS/REPORTING

1 DIRECT TESTIMONY OF CHARLESTON J. WINSTON

2 Q. Please state your name and business address.

3 A. My name is Charleston J. Winston and my business address is Hurston N.  
4 Tower, Suite N512, 400 W. Robinson Street, Orlando, FL 32801-1775.

5 Q. By whom are you presently employed and in what capacity?

6 A. I am employed by the Florida Public Service Commission as a Regulatory  
7 Analyst IV in the Division of Auditing and Financial Analysis.

8 Q. How long have you been employed by the Commission?

9 A. I have been employed by the Florida Public Service Commission since  
10 January, 1986.

11 Q. Briefly review your educational and professional background.

12 A. I have a Bachelor of Science degree in Accounting and Finance from the  
13 University of South Carolina.

14 Q. Please describe your current responsibilities.

15 A. Currently, I am a Regulatory Analyst IV with the responsibilities of  
16 planning and directing audits of regulated companies, and assisting in  
17 audits of affiliated transactions. I am also responsible for creating  
18 audit work programs to meet a specific audit purpose and I have specific  
19 authority to direct and control assigned staff work as well as  
20 participate as a staff auditor and audit manager.

21 Q. Have you presented expert testimony before this Commission or any other  
22 regulatory agency?

23 A. Yes. I testified in the Southern States Utilities, Inc., rate case,  
24 Docket No. 950495-WS and the United Telephone Company rate case, Docket  
25 No. 910980-TC.

1 Q. What is the purpose of your testimony today?

2 A. The purpose of my testimony is to sponsor specific findings in the staff  
3 audit report of Lake Utility Services, Inc., Docket No. 960444-WU. I  
4 am sponsoring Audit Exceptions 1, 10, 11, and 12. These findings are  
5 filed with my testimony and are identified as CJW-1.

6 Q. Please review the audit exceptions you are sponsoring.

7 A. Audit Exception No. 1 addresses the utility's books and records.  
8 Commission Rule 25-30.115(1), Florida Administrative Code, requires that  
9 water and wastewater utilities shall maintain accounts and records in  
10 conformity with the NARUC Uniform Systems of Accounts (USOA) adopted by  
11 the National Association of Regulatory Utility Commissioners. The USOA,  
12 Accounting Instructions 2.A., requires:

13       Each utility shall keep its books of account, and all other books,  
14 records, and memoranda which support the entries in such books of  
15 account so as to be able to furnish readily full information as to any  
16 item included in any account. Each entry shall be supported by such  
17 detailed information as will permit a ready identification, analysis,  
18 and verification of all facts relevant thereto.

19       Also, Commission rule 25-30.450, Florida Administrative Code,  
20 states:

21       The work sheets, etc., supporting the schedules and data submitted must  
22 be organized in a systematic and rational manner so as to enable  
23 Commission personnel to verify the schedules in an expedient manner and  
24 minimum amount of time.

25       I believe that Lake Utility Services, Inc.'s books and records are

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in violation of the above NARUC Instruction and Commission Rule. The books, records, and Minimum Filing Requirements (MFRs) of the utility did not enable Commission personnel to verify the schedules in an expedient manner and with the minimum amount of time. The following specific items were found to be in violation of the above rules:

- Accumulated depreciation at December 31, 1994, Schedule A-9 of the MFRs, is not in agreement with the general ledger.

- Some plant-in-service items are not supported by proper documentation, invoices, canceled checks, etc.

- The utility is not properly recording its CIAC and advances for construction. There are no ledgers for advances other than the developer/purchase agreements.

- Revenues were misstated in the MFRs due to misclassifications.

Audit Exception No. 10 addresses Allowance for Funds Prudently Invested (AFPI) revenues. The utility included \$32,912 in AFPI revenues in its miscellaneous revenues. A breakdown of this amount, by system, is shown below:

| <u>System Number</u> | <u>System Name</u>    | <u>Amount</u>   |
|----------------------|-----------------------|-----------------|
| 0661                 | Crescent Bay          | \$1,839         |
| 0666                 | Preston Cove          | 12,800          |
| 0667                 | South Clermont Region | <u>18,273</u>   |
|                      | Total:                | <u>\$32,912</u> |

AFPI revenues should not be recorded in revenues for ratemaking purposes. Therefore, I recommend that miscellaneous revenues be reduced by \$32,912.

1           Audit Exception No. 11 addresses deposit interest. In the MFRs,  
2 the Cost of Capital Schedule includes a cost rate of eight percent for  
3 customer deposits. However, in the company's billing registers, the  
4 interest paid on customer deposits was six percent. In addition,  
5 Commission rule 25-30.311(4), Florida Administrative Code, requires six  
6 percent. Therefore, I recommend that the customer deposit rate used in  
7 the MFRs should be reduced to six percent.

8           Audit Exception No. 12 addresses CIAC and advances. The utility's  
9 MFRs included the following amounts for 1995:

|    |                               |             |
|----|-------------------------------|-------------|
| 10 | CIAC                          | \$1,058,113 |
| 11 | CIAC Accumulated Amortization | \$ 126,729  |
| 12 | CIAC Expense                  | \$ 34,599   |
| 13 | Advances                      | \$ 0        |

14           The audit staff found several recording errors, misclassifications, and  
15 unrecorded advances by developers. Therefore, I recommend that CIAC be  
16 increased by \$188,478 and advances be increased by \$405,520. The  
17 utility also used a composite amortization rate of 3.1%. To be  
18 consistent with the auditors' recalculation of accumulated depreciation  
19 I used a composite amortization rate of 2.7% for 1995 and 2.5% for all  
20 other years. Based on this adjustment and the previous adjustment, I  
21 recommend that accumulated amortization be increased by \$8,673 and that  
22 CIAC amortization expense be decreased by \$6,258.

23 Q. Does this conclude your testimony?

24 A. Yes, it does.

25

**EXHIBIT NO.:** \_\_\_\_\_

**WITNESS: CHARLESTON J. WINSTON**

**DOCKET NO.: 960444-WU**

**Application for rate increase by**

**LAKE UTILITY SERVICES, INC.**

**BEFORE THE  
FLORIDA PUBLIC SERVICE  
COMMISSION**

**DESCRIPTION:**

**Exhibit CJW-1: Audit Exceptions 1, 10, 11 and 12 of  
Staff Audit Reports**

**AUDIT EXCEPTION NUMBER 1**

**SUBJECT: COMPANY'S BOOKS AND RECORDS**

**FACTS:** Per NARUC, National Association of Regulatory Utility Commissioners, Accounting Instructions 2.A.,

Each utility shall keep its books of account, and all other books, records, and memoranda which support the entries in such books of account so as to be able to furnish readily full information as to any item included in any account. Each entry shall be supported by such detailed information as will permit a ready identification, analysis, and verification of all facts relevant thereto.

Per Commission Rule 25-30.450,

The work sheets, etc. supporting the schedules and data submitted must be organized in a systematic and rational manner so as to enable Commission personnel to verify the schedules in an expedient manner and minimum amount of time.

**OPINION AND RECOMMENDATION:** Lake Utility Services, Inc.'s books and records are in violation of the above NARUC and Commission Rule. The books, records, and MFRs of the company did not enable Commission personnel to verify the schedules in an expedient manner and with the minimum amount of time. The following specific items were found to be in violation of the above rules:

1. Accumulated depreciation at December 31, 1994, Schedule A-9 of the MFRs, is not in agreement with the general ledger.
2. Some plant-in-service are not supported by proper documentation, invoices, cancelled checks, etc.
3. The company is not properly recording its CIAC and advances for construction. There are no ledgers for advances other than the developer/purchase agreements. See Audit Exception Number 12.

**AUDIT EXCEPTION NUMBER 1 (cont'd.)**

4. Revenues were misstated in the MFRs due to misclassifications. See Audit Exception Number 10.

The Commission should require the company to maintain its books and records per NARUC and Commission Rules.

**AUDIT EXCEPTION NUMBER 10****SUBJECT: AFPI**

**FACTS:** The company included \$32,912 in its MFRs as a portion of the miscellaneous revenues. A breakdown of the above amount by system is shown below:

| <u>System Number</u> | <u>System Name</u>    | <u>Amount</u>    |
|----------------------|-----------------------|------------------|
| 0661                 | Crescent Bay          | \$ 1,839         |
| 0666                 | Preston Cove          | 12,800           |
| 0667                 | South Clermont Region | 18,273           |
|                      |                       | -----            |
|                      | Total:                | <u>\$ 32,912</u> |

**OPINION AND RECOMMENDATION:** The above amounts are for AFPI, Allowance for Funds Prudently Invested; therefore, they should not be recorded in revenues for ratemaking purposes. However, they are used to determined Regulatory Assessment Fees.

The company's miscellaneous revenues for the year ended 1995 should be reduced by \$32,912.

**AUDIT EXCEPTION NUMBER 11**

**SUBJECT: DEPOSIT INTEREST**

**FACTS:** Per the MFRs Cost of Capital Schedule a cost rate of eight percent was used for customer deposits.

In the company's billing registers the interest paid on customer deposits was six percent.

**OPINION AND RECOMMENDATION:** The customer deposits' rate used in the MFRs should be reduced to six percent.

**AUDIT EXCEPTION NUMBER 12****SUBJECT: CIAC AND ADVANCES**

**FACTS:** The company's MFRs included the following amounts for 1995:

|                               |              |
|-------------------------------|--------------|
| CIAC                          | \$ 1,058,113 |
| CIAC Accumulated Amortization | \$ 126,729   |
| CIAC Expense                  | 34,599       |
| Advances                      | -0-          |

The company used a composite amortization rate of 3.1%.

**OPINION AND RECOMMENDATION:** Due to various recording errors, misclassifications, and unrecorded advances made by developers, the audit staff is recommending the following adjustments to the above amounts:

|                 | <u>Per Audit</u><br><u>12/31/95</u> | <u>Per MFR</u><br><u>12/31/95</u> | <u>Audit</u><br><u>Adjustment</u> |
|-----------------|-------------------------------------|-----------------------------------|-----------------------------------|
| CIAC            | \$ 1,246,591                        | \$ 1,058,113                      | \$ 188,478                        |
| CIAC Acc. Amtz. | 135,402                             | 126,729                           | 8,673                             |
| CIAC Expense    | 28,341                              | 34,599                            | (6,258)                           |
| Advances        | 405,520                             | -0-                               | 405,520                           |

For a breakdown of the above amounts refer to the attached schedule.

The audit staff used a composite amortization rate of 2.7% for 1995 and 2.5% for all other years.

Included in the above advances amount is \$35,000 that was misclassified as miscellaneous revenues in the MFRs. The above adjustments reclassified this amount to advances.

However, miscellaneous revenues should be reduced by \$35,000 and Regulatory Assessment Fees reduced by \$1,575 (35,000 x 4.5%). The company should file a Notice of Regulatory Assessment Fee Adjustment form with the Commission.

**AUDIT EXCEPTION NUMBER 12 SCHEDULE**

| <b>System &amp; Number</b> | <b>CIAC Per Audit 1994</b> | <b>CIAC Per Audit 1995</b> | <b>CIAC Average Balance</b> | <b>CIAC Expense Per Audit 1995</b> | <b>Advances Per Audit 1994</b> | <b>Advances Per Audit 1995</b> | <b>Advances Average Balance</b> | <b>Acc Amtz Per Audit 1994</b> | <b>Acc Amtz Per Audit 1995</b> | <b>Acc Amtz Average Balance</b> |
|----------------------------|----------------------------|----------------------------|-----------------------------|------------------------------------|--------------------------------|--------------------------------|---------------------------------|--------------------------------|--------------------------------|---------------------------------|
| Clermont #0628             | 71,663                     | 75,013                     | 73,338                      | 1,980                              | 5,320                          | 3,520                          | 4,420                           | 34,266                         | 36,246                         | 35,256                          |
| Amber Hill #0631           | 78,641                     | 79,586                     | 79,114                      | 2,136                              |                                |                                |                                 | 16,336                         | 18,472                         | 17,404                          |
| Highland Point #0632       | 61,150                     | 61,850                     | 61,500                      | 1,661                              | 11,850                         | 11,750                         | 11,800                          | 12,251                         | 13,911                         | 13,081                          |
| The Oranges #0633          | 36,350                     | 37,850                     | 37,100                      | 1,002                              | 16,850                         | 15,950                         | 16,400                          | 3,674                          | 4,676                          | 4,175                           |
| Lake Ridge Club #0634      | 16,250                     | 22,350                     | 19,300                      | 521                                | 65,200                         | 61,600                         | 63,400                          | 704                            | 1,225                          | 965                             |
| The Vistas #0636           | 27,150                     | 36,900                     | 32,025                      | 865                                |                                | 35,000                         | 17,500                          | 831                            | 1,695                          | 1,263                           |
| Crescent Bay #0661         | 53,515                     | 58,115                     | 55,815                      | 1,507                              | 125,350                        | 121,050                        | 123,200                         | 5,190                          | 6,697                          | 5,944                           |
| Crescent West #0662        | 90,920                     | 94,420                     | 92,670                      | 2,502                              |                                |                                |                                 | 11,066                         | 13,568                         | 12,317                          |
| Four Lakes #0663           | 26,770                     | 14,390                     | 20,580                      | 556                                |                                |                                |                                 | 10,953                         | 11,509                         | 11,231                          |
| Lake Saunders #0664        | 50,213                     | 50,913                     | 50,563                      | 1,365                              |                                |                                |                                 | 6,712                          | 8,077                          | 7,395                           |
| Crescent Hills #0665       | 23,750                     | 27,600                     | 25,675                      | 693                                |                                |                                |                                 | 943                            | 1,636                          | 1,290                           |
| Preston Cove #0666         | 23,081                     | 70,551                     | 46,816                      | 1,264                              | 15,369                         |                                | 7,685                           | 295                            | 1,559                          | 927                             |
| South Clermont #0667       | 293,260                    | 617,053                    | 455,157                     | 12,289                             | 107,050                        | 156,650                        | 131,850                         | 3,842                          | 16,131                         | 9,987                           |
| <b>Total:</b>              | <b>852,713</b>             | <b>1,246,591</b>           | <b>1,049,652</b>            | <b>28,341</b>                      | <b>346,989</b>                 | <b>405,520</b>                 | <b>376,255</b>                  | <b>107,063</b>                 | <b>135,402</b>                 | <b>121,233</b>                  |
| <b>Per Company:</b>        | <b>704,294</b>             | <b>1,058,113</b>           | <b>881,203</b>              | <b>34,599</b>                      | <b>0</b>                       | <b>0</b>                       | <b>0</b>                        | <b>92,130</b>                  | <b>126,729</b>                 | <b>109,430</b>                  |
| <b>Difference:</b>         | <b>148,419</b>             | <b>188,478</b>             | <b>168,449</b>              | <b>(6,258)</b>                     | <b>346,989</b>                 | <b>405,520</b>                 | <b>376,255</b>                  | <b>14,933</b>                  | <b>8,673</b>                   | <b>11,803</b>                   |

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Schedule of Water Rate Base

Florida Public Service Commission

EXHIBIT I

Company: Lake Utility Services, Inc.  
 Docket No.: 980444-WU  
 Schedule Year Ended: 12/31/95  
 Interim  Final   
 Historic  Projected

Schedule: A-1  
 Page 1 of 1  
 Preparer: MFK

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. If method other than formula approach (1/8 O&M) is used to determine working capital, provide additional schedule showing detail calculation.

| Line No. | (1)<br>Description                         | (2)<br>Balance Per Books<br>YE 12/31/95 | (3)<br>Utility Adjustments | (4)<br>Adjusted Utility Balance<br>YE 12/31/95 | (5)<br>Year End<br>12/31/94 | (6)<br>Test Year Average<br>12/31/95 | (7)<br>Supporting Schedule(s) |
|----------|--|---|----------------------------|--|-----------------------------|--------------------------------------|-------------------------------|
| 1        | Utility Plant in Service                   | \$1,979,991                             | 0                          | \$1,979,991                                    | \$1,912,124                 | \$1,946,058                          | A-5                           |
| 2        | Utility Land & Land Rights                 | 3,730                                   | 0                          | 3,730  | 3,730                       | 3,730                                | A-5                           |
| 3        | Less: Non-Used & Useful Plant              | 0                                       | (49,361)                   | (49,361)                                       | 0                           | (49,361)                             | A-7                           |
| 4        | Construction Work in Progress              | 0                                       | 0                          | 0  | 0                           | 0                                    | -                             |
| 5        | Less: Accumulated Depreciation             | (157,183)                               | 0                          | (157,183)                                      | (106,325)                   | (131,754)                            | A-9                           |
| 6        | Less: CIAC                                 | (1,058,113)                             | 0                          | (1,058,113)                                    | (704,294)                   | (881,203)                            | A-12                          |
| 7        | Accumulated Amortization of CIAC           | 126,729                                 | 0                          | 126,729  | 92,130                      | 109,430                              | A-14                          |
| 8        | Acquisition Adjustments                    | (70,169)                                | 0                          | (70,169)                                       | (70,169)                    | (70,169)                             | -                             |
| 9        | Accum. Amort. of Acq. Adjustments          | 8,182                                   | 0                          | 8,182  | 6,007                       | 7,095                                | -                             |
| 10       | Advances For Construction                  | 0                                       | 0                          | 0  | 0                           | 0                                    | A-16                          |
| 11       | Positive Accumulated Deferred Income Taxes | 250,916                                 | 0                          | 250,916  | (17,633)                    | 116,542                              | C-6                           |
| 12       | Working Capital Allowance                  | 27,371                                  | 3,471                      | 30,841   | 24,815                      | 27,828                               | A-17                          |
| 13       | Total Rate Base                            | <u>\$1,111,454</u>                      | <u>(\$45,890)</u>          | <u>\$1,065,564</u>                             | <u>\$1,140,185</u>          | <u>\$1,078,194</u>                   |                               |

## Schedule of Water Net Operating Income

Florida Public Service Commission

Company: Lake Utility Services, Inc.  
 Docket No.: 960444-WU  
 Schedule Year Ended: 12/31/95  
 Interim  Final   
 Historic  Projected

Schedule: B-1  
 Page 1 of 1  
 Preparer: MPK

EXHIBIT II

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. | (1)<br>Description         | (2)<br>Utility Test Year<br>12/31/95 | (3)<br>Utility Test Year<br>Adjustments | (4)<br>Utility Adjusted<br>Test Year<br>12/31/95 | (5)<br>Requested<br>Revenue<br>Adjustment | (6)<br>Requested<br>Annual<br>Revenues | Supporting<br>Schedule(s) |
|----------|----------------------------|--------------------------------------|---|--|---|--|---------------------------|
| 1        | OPERATING REVENUES         | \$339,294                            | (\$25,348)                              | \$313,946  | \$133,236                                 | \$447,182                              | B-3 & B-4                 |
| 2        | Operation & Maintenance    | 218,965                              | 27,767                                  | 246,732  | 0   | 246,732                                | B-3 & B-5                 |
| 3        | Depreciation               | 64,177                               | (1,724)                                 | 62,453   | 0   | 62,453                                 | B-3 & B-13                |
| 4        | Acq. Adj. Amortization     | (2,175)                              | 0                                       | (2,175)  | 0   | (2,175)                                |                           |
| 5        | CIAC Amortization          | (34,599)                             | 0                                       | (34,599)   | 0   | (34,599)                               | B-3                       |
| 6        | Taxes Other Than Income    | 35,332                               | 2,256                                   | 37,588   | 5,996                                     | 43,583                                 | B-3 & B-15                |
| 7        | Provision for Income Taxes | 9,066                                | (7,645)                                 | 1,421  | 19,353                                    | 20,774                                 | B-3 & C-1                 |
| 8        | OPERATING EXPENSES         | 290,766                              | 20,653                                  | 311,419  | 25,348                                    | 336,768                                |                           |
| 9        | NET OPERATING INCOME       | \$48,528                             | (\$46,001)                              | \$2,527  | \$107,888                                 | \$110,414                              |                           |
| 13       | RATE BASE                  | \$1,078,194                          |   | \$1,078,194                                      |   | \$1,078,194                            |                           |
| 14       | RATE OF RETURN             | 4.50%                                |   | 0.23%  |   | 10.24%                                 |                           |

Schedule of Requested Cost of Capital  
Beginning and End of Year Average

Florida Public Service Commission

EXHIBIT III

Schedule: Utilities, Inc. (Parent Company)  
Company: Lake Utility Services, Inc.  
Docket No.: 960444-WU  
Test Year Ended: 12/31/95  
Schedule Year Ended: 12/31/95  
Historic [X] Projected [ ]

Schedule: D-1  
Page 1 of 2  
Preparer: MFK

Subsidiary [X] or Consolidated [ ]

Simple average capital structure.

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. | Class of Capital             | (1)<br>Reconciled<br>To Requested<br>Rate Base<br>AYE 12/31/95 | (2)<br>Ratio | (3)<br>Cost<br>Rate | (4)<br>Weighted<br>Cost |
|----------|------------------------------|--|--------------|---------------------|-------------------------|
| 1        | Long-Term Debt               | \$503,195  | 46.67%       | 9.19%               | 4.29%                   |
| 2        | Short-Term Debt              | 91,427   | 8.48%        | 9.12%               | 0.77%                   |
| 3        | Preferred Stock              | 0  | 0.00%        | 0.00%               | 0.00%                   |
| 4        | Customer Deposits            | 14,518   | 1.35%        | 8.00%               | 0.11%                   |
| 5        | Common Equity                | 469,055  | 43.50%       | 11.65%              | 5.07%                   |
| 6        | Tax Credits - Zero Cost      | 0  | 0.00%        | 0.00%               | 0.00%                   |
| 7        | Tax Credits - Wtd. Cost      | 0  | 0.00%        | 0.00%               | 0.00%                   |
| 8        | Accum. Deferred Income Taxes | 0  | 0.00%        | 0.00%               | 0.00%                   |
| 9        | Other (Explain)              | 0  | 0.00%        | 0.00%               | 0.00%                   |
| 10       | Total                        | \$1,078,194  | 100.00%      |                     | 10.24%                  |

Supporting Schedules: D-2  
Recap Schedules: A-1, A-2

Note: Leverage Formula:  $9.05 + (1.131/43.5\%)$