

State of Florida



Public Service Commission

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

DATE: October 16, 2000
TO: Division of Economic Regulation (Fitch)
FROM: Division of Regulatory Oversight (Vandiver) *OV*
RE: 000985-WU; C.S. Water Company, Inc.
 Audit Report; Staff-assisted Rate Case
 Audit Control No. 00-235-2-1

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, they should send it to the Division of Records and Reporting. There are no confidential work papers associated with this audit.

DNV/sp

Attachment

cc: Division of Regulatory Oversight (Hoppe/Harvey/File Folder)
 Tampa District Office (McPherson) w/o attachment
 Division of Records and Reporting
 Division of Legal Services

Clyde A. Biston
 C.S. Water Company, Inc.
 P. O. Box 3000
 Crystal Springs, FL 33524-3000

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FPSC-RECORDS/REPORTING



FLORIDA PUBLIC SERVICE COMMISSION

*DIVISION OF REGULATORY OVERSIGHT
BUREAU OF AUDITING SERVICES*

TAMPA DISTRICT OFFICE

C. S. WATER COMPANY, INC.

STAFF ASSISTED RATE CASE

FOR THE TWELVE MONTHS ENDED JUNE 30, 2000

Docket No. 000985-WU



Vincent C. Aldridge, Audit Manager



James A. McPherson, Tampa District Supervisor

DOCUMENT NUMBER-DATE

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FPSC-RECORDS/REPORTING

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DIVISION OF REGULATORY OVERSIGHT

AUDIT REPORT

OCTOBER 4, 2000

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

We have applied the procedures described later in this report to prepare and audit the accompanying schedules of Rate Base, Net Operating Income and Capital Structure for the historical twelve month period ended June 30, 2000 for C.S. Water Company, Inc. These schedules were prepared as part of a Staff Assisted Rate Case. 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 report should 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.

SUMMARY OF SIGNIFICANT FINDINGS

The utility did not adjust its records to reflect changes to accumulated depreciation as directed by FPSC Order No. 23853, issued December 10, 1990. The utility has not been using guideline depreciation rates as required by Rule 25-30.140, Florida Administrative Code. The utility has not been regularly collecting meter fees and system capacity charges as authorized by its tariff. The utility has three customers which are not billed for water provided.

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.

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

RATE BASE: Reconciled beginning rate base to prior FPSC Order No. 23853 establishing rate base as of April 30, 1990. Tested the plant balances by reviewing invoices on a judgmental basis. Computed and scheduled accumulated depreciation using currently approved guideline rates, and accumulated amortization of CIAC, based upon staff adjusted plant and CIAC balances. Computed working capital on the one-eighth of O&M expense method.

NET OPERATING INCOME: Compiled utility expenses. Verified Operating and Maintenance (O&M) expenses on a judgmental basis. Performed billing analysis. Performed reasonableness test for utility revenues based upon billing analysis. Recalculated depreciation and amortization of CIAC expenses using appropriate guideline rates. Analyzed taxes other than income.

CAPITAL STRUCTURE: Compiled the capital structure of the utility as of June 30, 2000.

Disclosure No. 1

Subject: Plant Accounts

Statement of Fact: The utility's books and records showed a plant balance of \$204,965 as of June 30, 2000.

Recommendation: Several adjustments to the utility's plant accounts should be made.

1. The utility purchased a new truck in 1998. This gave the utility two vehicles. For a utility of this size, two vehicles appears to be excessive. We recommend reclassifying the older vehicle and its accumulated depreciation to non-utility plant for ratemaking purposes.
2. The utility added a propane powered backup generator (required by DEP) in 1999. This generator was donated by the owner of the utility, but no transaction has been recorded. Account 311 - Pumping Equipment should be increased by \$6,500 and Account 211 - Other Paid-In Capital should be increased by a like amount to record the value of this transaction.
3. The utility capitalized \$300 worth of items that should have been expensed in June of 1999.

Plant per utility books:		\$204,205
Reclassify utility vehicle to non-utility plant:	(8,349)	
Add propane powered generator acquired in 1999:	6,500	
Remove items that should have been expensed:	(300)	

Adjustment:		(2,149)

Total plant per audit:		\$202,056
		=====

Adjustments to accumulated depreciation are included in Disclosure No. 2.

Disclosure No. 2

Subject: Accumulated Depreciation

Statement of Fact: The utility has not been depreciating plant using guideline rates as required by Rule 25-30.140, Florida Administrative Code. Instead, it has been using tax depreciation rates. The company did not adjust its records to reflect changes made in the prior audit as directed by FPSC Order No. 23853, issued December 10, 1990.

Opinion and Conclusion: The accumulated depreciation balances have been recalculated using guideline rates. The calculations reflect the audit adjustments to plant recommended in Disclosure No. 1. The utility's accumulated depreciation balances should be adjusted as follows:

<u>Acct.</u>	<u>Name</u>	<u>Balance</u> <u>Per Books</u>	<u>Audit</u> <u>Adjustments</u>	<u>Balance</u> <u>Per Audit</u>
304	Structures and Improvements	\$ 748	\$ (43)	\$ 705
307	Wells and Springs	13,951	(15,774)	(1,823)
311	Pumping Equipment	1,050	(6,109)	(5,059)
331	Transmission & Distribution	56,858	(31,336)	25,522
334	Meters and Meter Installations	30,016	(13,168)	16,848
339	Other Plant and Misc. Equip.	2,659	(798)	1,861
340	Office Equipment	6,798	(8,446)	(1,647)
	Computers		3,744	3,744
341	Transportation Equipment	17,774	(12,619)	5,155
345	Power Operated Equipment		524	524
347	Miscellaneous Equipment	9,018	(7,985)	1,033
348	Other Tangible Plant	1,422	(1,157)	265
		<u>\$140,296</u>	<u>\$ (93,168)</u>	<u>\$ 47,128</u>

Disclosure No. 3

Subject: CIAC

Statement of Fact: FPSC Order No. 23853, issued December 10, 1990 set balances of CIAC, accumulated amortization of CIAC, meter installation fees, and system capacity charges as follows:

CIAC @ 4/30/90:	(\$76,426)
Amortization of CIAC @ 4/30/90:	22,748
Meter Installation Fees (per connection):	150
System Capacity Charge (per connection):	350

Recommendation: The utility collects the meter installation fees and system capacity charges only sporadically. When it has collected these charges, it has at times recorded them as revenue. For these reasons, it is necessary to impute CIAC for the meter installation fees and system capacity charges not collected and/or not recorded correctly. To do this, we took the number of new connections each year and multiplied that by \$500. According to the utility's annual reports, there were 100 new connections since the last rate case.

\$ 500
100 new connections

50,000 CIAC to impute
76,426 CIAC per Order from last rate case

\$126,426 CIAC per audit

The amortization of CIAC was recalculated to reflect the imputed CIAC and the composite depreciation rate of the utility. Adjustments should be made as follows:

	Per Books <u>@ 6/30/00</u>	Audit <u>Adjustment</u>	Per Audit <u>@ 6/30/00</u>
CIAC	(\$78,278)	(\$48,148)	(\$126,426)
Amort. CIAC	40,796	13,502	54,298
	-----	-----	-----
Net CIAC	<u>(\$37,482)</u>	<u>(\$34,646)</u>	<u>(\$ 72,128)</u>

Disclosure No. 4

Subject: Customer Deposits

Statement of Fact: During the last audit of the utility in 1990, it was noted that the utility was not collecting customer deposits. However, it still had \$210 of customer deposits on its books for customers who had moved and left no forwarding address.

Recommendation: The utility has since changed ownership and the new owners are no more likely to locate these customers than the old owners were in 1990. I recommend that these deposits be turned over to the Comptroller's Office of the State's Department of Banking and Finance as provided for by Chapter 717, Florida Statutes. We have not included them in the utility's capital structure for this audit.

Disclosure No. 5

Subject: Capital Structure

Statement of Fact: The utility was carrying four "long term loans" on its books as of June 30, 2000. A list of these "loans" is as follows:

<u>Description</u>	<u>Creditor</u>	<u>Date Originated</u>	<u>Amount@ 6/30/00</u>
1997 Ford F250 Truck	Barnett Bank	May 1998	\$13,027
Loan for utility bill	Al Biston	June 1998	2,885
Loan for line extension	CS Environmental	June 1998	15,803
Various loans for liquidity	Utility Stockholders	December 1997	\$17,260

Recommendation:

Truck Loan

The loan for the truck is a loan which is evidenced by a debt instrument, with a stated interest rate, on which the utility makes regular payments. This should remain classified as a loan in the utility's capital structure.

Other Loans

The other three "loans" are not evidenced by a debt instrument, the utility rarely makes payments on them and there is no stated interest rate. No interest has been paid on these loans. Although the utility has called these transactions "loans", they actually appear to be additional paid-in capital. During audit field work, this issue was discussed with the utility owner and the utility's CPA. The utility reclassified the three loans to other paid-in capital on its books.

We recommend that these "loans" totaling \$35,948 at June 30, 2000, be treated as common equity in the utility's capital structure for ratemaking purposes.

Disclosure No. 6

Subject: Unbilled Water

Statement of Fact: The utility has three customers/metered hook-ups for which it does not bill and does not collect any revenues.

Recommendation: The three customers are the residence of the utility owners, a local church/community center, and a "free water spigot." The free water spigot is for community members who have well water that is apparently not of equal quality to the utility's water. Both the free water spigot and the church/community center have been receiving free water since before the current owners purchased the utility. Apparently the previous owner felt that he was providing a "community service" and being a good neighbor by providing this water at no cost. At the time of the sale of the utility, he asked the new owners to continue that practice and they have done so. The amount of unbilled water during the test year is as follows:

<u>Customer</u>	<u>Gallons</u>	<u>Lost Revenue (including base facility charges)</u>
Biston Residence	1,223,075	\$1,474
Church/Community Center	34,952	100
Free Water Spigot	288,932	457
Total	<u>1,546,959</u>	<u>\$2,031</u>

This information is provided for informational purposes and no specific recommendation is being made as to how to handle it.

Disclosure No. 7

Subject: Payroll and Benefits Expenses

Statement of Fact: The utility's total payroll expense for the test period was \$26,314. The utility did not have any benefits expense during the test period.

Recommendation:

Payroll

During the test period, the utility's only employees were its two owners, a husband and wife. The utility stated that the wife spends, on average, 40 to 50 hours per week on utility business, while the husband spends, on average, 8 to 10 hours per week. The utility stated that it would like to hire an additional employee who would work 20 to 40 hours a week to assist in the day to day operation of the utility. An employee working 20 hours a week at \$10 an hour would create approximately \$10,000 a year in additional payroll expense.

It appears that the utility's payroll expense is low, due to the owners performing all of the work at what appears to be quite low wages. I recommend an increase in payroll expense of \$10,000. Whether the owners use this increase to hire an additional employee or to increase their own compensation would be their choice.

Benefits

Prior to the test year, the utility had been paying for a medical insurance policy for the wife costing \$320 a month. This is an increase of \$3,840 per year for employee pensions and benefits. We recommend an adjustment be made to provide that amount of employee benefits.

Disclosure No. 8

Subject: Out of Period Expenses

Statement of Fact: The utility maintains its books and records on a cash basis. There were out of period expenses included in test year O&M expenses.

Recommendation: The utility had thirteen rental payments of \$216 for its office space during the test year. It also had a \$596 accounting bill that was for work performed outside of the test year. The following adjustments should be made:

<u>Account No.</u>	<u>Account Name</u>	<u>Adjustment</u>
641	Rental of Building/Property	(\$216)
631	Contractual Services- Accounting	(\$596)

		<u>(\$812)</u>

Disclosure No. 9

Subject: Various O&M Expense Adjustments

Statement of Fact: There are several adjustments that need to be made to O&M expenses for various reasons.

Recommendation:

Transportation Expense

The utility recorded only \$38 of transportation expense during the test year. This figure does not seem to accurately reflect the actual transportation costs incurred by the utility during the test year. When asked, the utility stated that it accumulated approximately 3000 miles a year on its vehicle. At \$0.30 per mile, this equals \$900 of transportation expense. This figure appears to be reasonable and more accurately reflects the transportation costs incurred by the utility.

Insurance- Vehicle

This adjustment removes the auto insurance related to the vehicle discussed in Disclosure No. 1 that we recommend be treated as non-utility property.

Misc Exp. (penalties)

This adjustment removes \$139 of penalties paid to the IRS during the test year.

Misc Exp. (wireless phone)

The utility has a wireless phone for which it incurred \$1,047 in charges during the test year for an average of \$87 a month. A review of AT&T Wireless bills showed usage to be upwards of 200+ calls and 500+ minutes a month, which appears to be excessive for a utility of this size. It seems that the utility ought to be able to find a wireless phone plan for \$50 a month, which is the amount that I recommend be allowed. An adjustment of \$447 would be necessary to reflect that amount.

<u>Account No.</u>	<u>Account Name</u>	<u>Adjustment</u>
650	Transportation Expense	\$ 900
656	Insurance- Vehicle	(1,181)
675	Misc. Exp. (penalties)	(139)
675	Misc. Exp. (wireless phone)	(447)

		<u>(\$867)</u>

Disclosure No. 10

Subject: Taxes Other Than Income

Statement of Fact: The utility paid both its 1997 and 1999 Regulatory Assessment Fees during the test year.

Recommendation: The utility had not previously paid its 1997 Regulatory Assessment Fee (RAF). During the test year, it paid \$3601 of RAF, interest and penalties pertaining to 1997. This amount should be removed from taxes other than income expense.

C. S. Water Company, Inc.

Exhibit I

Docket 000985-WU

Rate Base

Staff Assisted Rate Case

As Of June 30, 2000

	<u>Per Utility @ 06/30/1999</u>	<u>Per Utility @ 06/30/2000</u>	<u>Audit Adjustments</u>	<u>Ref</u>	<u>Per Audit @ 06/30/2000</u>	¹ <u>Average @ 06/30/2000</u>
Plant in Service	195,532	204,205	(2,149)	Disc 1	202,056	197,720
Land	760	760	0		760	760
Acc Depreciation of Plant	(132,219)	(140,296)	93,168	Disc 2	(47,128)	(43,090)
CIAC	(78,278)	(78,278)	(48,148)	Disc 3	(126,426)	(126,426)
Amortization of CIAC	38,839	40,796	13,502	Disc 3	54,298	53,320
Working Capital- 2	0	0	7,444		7,444	7,444
Rate Base per Audit	<u>24,634</u>	<u>27,187</u>	<u>63,817</u>		<u>91,004</u>	<u>89,728</u>

1- For the calculation of Average Rate Base, adjustments were made as of 6/30/99 as each of the events prompting the adjustments had occurred by that date.

2- Working Capital was computed using the one-eighth of O&M expense method

C. S. Water Company, Inc.

Exhibit II

Docket 000985-WU

Net Operating Income

Staff Assisted Rate Case

As Of June 30, 2000

	<u>Per Utility @</u> <u>06/30/2000</u>	<u>Audit</u> <u>Adjustments</u>	<u>Ref</u>	<u>Per Audit @</u> <u>06/30/2000</u>
Operating Revenues	(66,749)	0		(66,749)
O&M Expenses	47,391	12,161	Disc 7,8,9	59,552
Depreciation Expense	10,707	859		11,566
Amortization of CIAC	(979)	(6,264)	Disc 3	(7,243)
Taxes- Other	9,788	(3,601)	Disc 10	6,187
Total Profit (Loss)	<u>158</u>	<u>3,155</u>		<u>3,313</u>
	=====	=====		=====

Note: Utility is a Subchapter S Corporation and therefore pays no income tax.

C. S. Water Company, Inc.

Exhibit III

Docket 000985-WU

Capital Structure

Staff Assisted Rate Case

As Of June 30, 2000

	<u>Per Utility @ 06/30/1999</u>	<u>Per Utility @ 06/30/2000</u>	<u>Audit Adjustments</u>	<u>Ref</u>	<u>Per Audit @ 06/30/2000</u>	<u>Average @ 06/30/2000</u>	<u>Ratio</u>	<u>Cost Rate</u>	<u>Weighted Cost of Capital</u>
Common Stock	50	50			50	50			
			6,500	Disc 1					
			<u>35,949</u>	Disc 5					
Pd In Capital	84,910	84,910	42,449		127,359	124,352			
Retained Earnings	(61,702)	(65,549)			(65,549)	(63,626)			
Common Equity	23,258	19,411	84,898		61,860	60,776	78.07%	9.47%	7.39%
Note- Truck	16,534	13,027			13,027	14,780	18.99%	7.90%	1.50%
Note- AMEX Finan	1,504	0			0	752	0.97%	18.82%	0.18%
Note- AAC	3,079	0			0	1,539	1.98%	15.78%	0.31%
Note- CES	15,803	15,803	(15,803)	Disc 5	0	0	0.00%	0.00%	0.00%
Note- Biston	2,535	2,885	(2,885)	Disc 5	0	0	0.00%	0.00%	0.00%
Note- S/H	11,596	17,260	(17,260)	Disc 5	0	0	0.00%	0.00%	0.00%
Long Term Debt	51,052	48,975	(35,948)		13,027	17,072	21.93%		1.99%
Customer Deposits	210	210	(210)	Disc 4	0	0	0.00%		0.00%
Total	74,520	68,596	48,740		74,887	77,848	100%		9.39%

Note: Equity based on leverage formula in Order No. PSC-00-1162-PAA-WS

AUDIT CRITIQUE AND EVALUATION (ACE) FORM
DIVISION OF REGULATORY OVERSIGHT ♦ BUREAU OF AUDITING
 RETURN TO RGO BEFORE: Oct. 16, 2000

Company Name: C.S. Water Co., Inc.

Docket No.: 000985-WU

Audit Control No.: 00-235-2-1 (Aldridge)

Analyst Assigned: Econ. Reg. (Fitch)

	Excellent 3	Satisfactory 2	Unsatisfactory 1	Not Applicable 0
AUDIT REPORT				
<i>Accuracy of the report</i>	3	2	1	0
<i>Clarity of the report</i>	3	2	1	0
<i>Usefulness of information in report</i>	3	2	1	0
<i>Conclusions in report are supported</i>	3	2	1	0

This audit report included unique features that I would like to see in future audit reports. These features were as follows:

I would have liked to have seen the following in the audit report:

AUDIT WORK PAPERS

<i>The work papers supported the audit conclusions</i>	3	2	1	0
<i>The work papers included accurate information</i>	3	2	1	0
<i>Cross references allowed tracing of audit work</i>	3	2	1	0
<i>Indexing assisted in locating information</i>	3	2	1	0

These audit work papers included unique features that I would like to see in future work papers. These features were as follows:

In support of items in the Audit Service Request and the Audit Manual audit guide, I would have liked to have seen the following in the audit work papers:

AUDIT CRITIQUE AND EVALUATION (ACE) FORM
DIVISION OF REGULATORY OVERSIGHT ♦ BUREAU OF AUDITING
 RETURN TO RGO BEFORE: Oct. 16, 2000

Company Name: C.S. Water Co., Inc.

Docket No.: 000985-WU

Audit Control No.: 00-235-2-1 (Aldridge)

Analyst Assigned: Econ. Reg. (Fitch)

Excellent	Satisfactory	Unsatisfactory	Poor
3	2	1	0

COMMUNICATION AND CONDUCT

I was satisfied with how often the auditor communicated with me.

3	2	1	0
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The information provided by the auditor during the audit process was useful.

3	2	1	0
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Conduct & general helpfulness of auditor(s)

3	2	1	0
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I appreciated the auditor(s) letting me know the following before the audit was complete:

While reviewing the audit work papers, I discovered the following information which I would have liked to have known about earlier:

OVERALL AUDIT PROCESS

Extent to which this audit met my needs

3	2	1	0
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Fulfillment of scope and objectives

3	2	1	0
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OTHER COMMENTS BENEFICIAL TO IMPROVING FUTURE AUDITS OR AUDITOR PERFORMANCE:

Please comment specifically on any unsatisfactory work indicated above.