

State of Florida



Public Service Commission

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

DATE: July 6, 2001
TO: Division of Economic Regulation (Fitch)
FROM: Division of Regulatory Oversight (Vandiver) *OV*
RE: Docket No. 010403-WU; Holmes Utilities, Inc.; Staff assisted rate case; Audit Control No. 01-123-3-2

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

Attachment

cc: Division of Regulatory Oversight (Hoppe, Harvey, District Offices, File Folder)
Division of Commission Clerk and Administrative Services (2)
Division of Legal Services

Mr. Daniel Holmes
Holmes Utilities, Inc.
760 Henscratch Road
Lake Placid, FL 33852-8397

DOCUMENT NUMBER- DATE
08276 JUL-60
REGULATORY RECORDS/REPORTING



FLORIDA PUBLIC SERVICE COMMISSION

*DIVISION OF REGULATORY OVERSIGHT
BUREAU OF AUDITING SERVICES*

Orlando District Office

HOLMES UTILITIES, INC.

STAFF-ASSISTED RATE CASE AUDIT

HISTORICAL PERIOD ENDED DECEMBER 31, 2000

DOCKET NO. 010403-WU

AUDIT CONTROL NO. 01-099-3-2

A handwritten signature in cursive script, appearing to read "Richard F. Brown".

Richard F. Brown, Audit Manager

A handwritten signature in cursive script, appearing to read "Charleston J. Winston".

Charleston J. Winston, District Audit Supervisor

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**DIVISION OF REGULATORY OVERSIGHT
AUDITOR'S REPORT**

JUNE 26, 2001

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

We have applied the procedures described later in this report to audit the accompanying schedules for Rate Base, Net Operating Income, and Capital Structure for the historical 12-month period ended December 31, 2000, for Holmes Utilities, Inc. The attached schedules were prepared by the audit staff as part of our work in the utility's application for a Staff-Assisted Rate Case in Docket No. 010403-WU.

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

Water utility plant-in-service was overstated by \$26,708.13.

Accumulated depreciation was understated by \$1,572.00.

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.

Scanned - The documents or accounts were read quickly looking for obvious errors.

Verified - The items were tested for accuracy, and compared to the substantiating documentation.

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

RATE BASE: Compiled account balances for utility plant-in-service (UPIS), contributions-in-aid-of-construction (CIAC), accumulated depreciation, and accumulated amortization of CIAC from August 1, 1995. Tested 100 percent of plant additions for the proper amount, period and classification. Verified 95 percent of CIAC additions selected using auditor judgement and agreed to FPSC-approved tariff amounts. Recalculated accumulated depreciation and accumulated amortization per the Commission rule. Computed the working capital allowance using the one-eighth of operation and maintenance expenses.

NET OPERATING INCOME: Compiled utility revenue and operation and maintenance accounts for the period ended December 31, 2000. Recomputed operating revenues. Verified 95 percent of operation and maintenance expenses. Verified support for taxes other than income.

CAPITAL STRUCTURE: Compiled components for the capital structure as of December 31, 2000. Agreed interest expense to the terms of the note.

OTHER: Scanned the federal income tax returns from 1995 through 2000. Prepared a trial balance and billing analysis.

Exception No. 1

Subject: Books and Records

Statement of Fact: Holmes Utilities, Inc. maintains its books and records on a semi-accrual basis. However, it does utilize the NARUC System of Accounts.

Rule 25-30.115, Florida Administrative Code (F.A.C.), requires all water and wastewater utilities to maintain their accounts and records in conformity with the 1996 NARUC Uniform System of Accounts (USOA).

In accordance with NARUC, Class C, Accounting Instruction No. 2. A.,

The books and accounts of all water utilities shall be kept by the double entry method on an accrual basis. Each utility shall keep its books of accounts monthly and shall close its books at the end of each calendar year.

Recommendation: The audit staff recommends that the utility maintain its books and records in compliance with the referenced instruction.

Exception No. 2

Subject: Water Utility Plant-in-Service (UPIS)

Statement of Fact: The utility was built in 1987 and was transferred to the present owners on August 1, 1995.

Holmes Utilities, Inc., the present owners, reflected a water utility plant-in-service balance of \$47,967.17, per its books and records as of December 31, 2000.

Recommendation: The audit staff verified, in supporting documentation, \$21,259.04 of the \$47,967.17. The remaining \$26,708.13 were plant expenditures disbursed and/or accrued by the former utility owner. However, the corresponding documentation was not provided to the current owners.

The FPSC engineer is performing an Original Cost Study on the utility. The audit staff defers to the engineer and analyst final disposition as to the appropriate amount of plant-in-service.

Exception No. 3

Subject: Accumulated Depreciation

Statement of Fact: The books and records of Holmes Utilities, Inc. reflected a balance of \$5,436.00 in Account No. 108, Accumulated Depreciation, as of December 31, 2000. The related depreciation expense for the 12-month period ended December 31, 2000, was \$1,085.00, per utility books.

Recommendation: The audit staff recomputed the reserve and related depreciation expense based on Rule 25-30.140, F.A.C., and the plant-in-service balance established in Exception No. 2.

Rate differences between Rule 25-30.140, F.A.C., and utility-applied rates for plant accounts that had documented balances, are as follows:

<u>Account</u>	<u>Rule 25-30.140, F.A.C.</u>	<u>Utility Rates</u>
Wells & Equipment (108-307)	3.7%	2.0%
Pumping Equipment (108-311)	5.88%	2.5%
Meters (108-334)	5.88%	2.5%

The audit staff's computations reflected balances of \$7,008.00 and \$915.81, respectively, for accumulated depreciation and depreciation expense for the aforementioned period.

It is therefore recommended that accumulated depreciation be increased by \$1,572.00 (\$7,008.00 - \$5,436.00) and depreciation expense be reduced by \$169.19 (\$915.81 - \$1,085.00).

Exception No. 4

Subject: Amortization of Contributions-in-Aid-of-Construction (CIAC)

Statement of Fact: The books and records of Holmes Utilities, Inc. reflected a balance of \$894.00 in Account No. 272, Accumulated Amortization of CIAC, as of December 31, 2000. The related amortization expense for the 12-month period ended December 31, 2000, was \$296.00, per utility books.

Recommendation: The audit staff recomputed the amortization based on the Florida Public Service Commission composite rate of 3.1 percent, as the utility calculated its rate based on a plant composite rate that included \$26,708.13 of undocumented additions that were excluded from utility plant-in-service. (See Exception No. 1.)

The audit staff's computations reflected balances of \$1,076.42 and \$372.02, respectively, for accumulated amortization of CIAC and amortization expense for the aforementioned period.

It is therefore recommended that accumulated amortization be increased by \$182.42 (\$1,076.42 - \$894.00) and amortization be increased by \$76.02 (\$372.02 - \$296.00).

Exception No. 5

Subject: Working Capital Allowance

Statement of Fact: The working capital allowance has been computed based on the one-eighth of operation and maintenance expenses formula method to comply with Rule 25-30.433(2), F.A.C.

The water working capital allowance was computed as \$1,997.66 based on staff-adjusted operation and maintenance expense of \$15,981.28.

Recommendation: Staff recommends that water rate base be increased by \$1,997.66 to reflect the working capital allowance.

Exception No. 6

Subject: Operating Revenues

Statement of Fact: The utility records operating revenues, per its books, annually via journal entry. The cash basis entry is determined by the deposits on the bank statements made during the year.

Recommendation: Field staff recomputed revenues based on customer consumption for the 12-month period ended December 31, 2000, thereby converting to accrual recognition.

It was determined that revenues based on the accrual basis were \$10,610.90 as opposed to \$8,669.40 reflected by the utility on the cash basis.

It is recommended that operating revenues be increased by \$1,941.50 to reflect the conversion in accounting.

Disclosure No. 1

Subject: Acquisition of Utility

Statement of Fact: Per Order No. PSC-97-0568-FOF-WU, issued May 20, 1997, Holmes Utilities, Inc. purchased the utility on August 1, 1995.

Recommendation: According to Holmes Utilities' application for a staff-assisted rate case dated April 5, 2001, the utility was purchased from Mitch Harvey for \$1.00.

Utility representatives informed the audit staff that there was no purchase agreement.

Disclosure No. 2

Subject: Pro Forma Adjustments

Statement of Fact: Holmes Utilities, Inc. submitted an itemization of various pro forma expenses on the following page to the audit staff.

Recommendation: The audit staff informed utility representatives that the information would be forwarded to the Tallahassee analyst and engineer for consideration and disposition.

ATTACHMENT

Pugh Utilities Service, Inc.
760 Henscratch Road
Lake Placid, FL 33852

Country Walk/Holmes Utilities, Inc.
760 Henscratch Road
Lake Placid, FL 33852

January 2001

Manager/Owner fee	\$1,600.00 Monthly
Secretarial Maintenance	\$1,200.00 Monthly
Making sure all reports are filed in a timely manner to all necessary agencies Does collection / turn on and turn off Banking / pay bills / office space / making sure all necessary tax forms and reports are filed in a timely manner	
Operational and Maintenance	\$600.00 Monthly
Operation of water plant 6 day a week On call 24 hours a day /7 days a week Monitor and pick up required lab and maintain chemicals.	
Laboratory Fees	
Bacteriological Sampling 3 samples per month	\$60.00
Nitrate and Nitrite Sampling 1 sample per year	\$ 70.00
Lead and Copper Sampling 10 samples every 3 years	\$400.00
Triennial sampling	\$2800.00
Chemicals	
Liquid Chlorine	\$ 1.81 per gallon
Sequestall —100 lb. drum	\$250.00
Labor	\$45.00 per hour
Water main flushing	
Mow/Clean Facility	
Read meters	
Service Calls	
Extra Work	
Billing	
Billing and postage	\$1.15 per customer
Materials	
Tapin & Meter installation	\$250.00
Other parts charged out as necessary	

Disclosure No. 3

Subject: Customer Connection Charges

Statement of Fact: A customer connection (tap-in) 5/8" x 3/4" meter charge of \$550.00 was approved for Holmes Utilities, Inc. per Order No. PSC-97-0568-FOF-SU.

Recommendation: Holmes Utilities, Inc. has contracted with Pugh Utilities to supply and install 5/8" x 3/4" meters at \$200.00 per connection.

The audit staff recommends that the PSC analyst and engineer examine this matter.

Disclosure No. 4

Subject: Revenue Tariff

Statement of Fact: The current revenue tariff in effect for Holmes Utilities, Inc. was established in Order No. PSC-97-0568-FOF-WU.

The water tariff is as follows:

WATER
Monthly Rates

Residential and General Service

Base Rate Facility Charge

Meter Size

5/8" x 3/4"	\$8.00
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Gallage Charge

(Per 1,000 gallons)

0 - 5,000 gallons	\$1.40
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5,001 - 10,000 gallons	\$1.70
------------------------	--------

10,0001 - 15,000 gallons	\$2.00
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Over 15,000 gallons	*
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*Gallage charge increases by \$0.30 for each 5,000-gallon block over 15,000 gallons.

Recommendation: The utility capped the rate billed customers at \$2.00, contrary to the specification of the tariff.

Staff determined that the resulting undercharged revenue for the 12-month period ended December 31, 2000, was an immaterial \$31.20.

It is recommended, however, that the utility comply with its tariff and bill accordingly in future periods.

EXHIBIT I**HOLMES UTILITIES, INC.
DOCKET NO. 010403-WU
WATER RATE BASE
AS OF DECEMBER 31, 2000**

DESCRIPTION	PER COMPANY 12/31/00	AUDIT EXCEPTION	REFER TO(1)	PER AUDIT 12/31/00
UTILITY-PLANT-IN-SERVICE	\$47,967.17	(\$26,708.13)	E-2	\$21,259.04
LAND	745.00	0.00		745.00
ACCUMULATED DEPRECIATION	(5,436.00)	(1,572.00)	E-3	(7,008.00)
CIAC	(13,100.00)	0.00		(13,100.00)
ACCUMULATED AMORTIZATION	894.00	182.42	E-4	1,076.42
WORKING CAPITAL ALLOWANCE	0.00	1,997.66	E-5	1,997.66
	=====	=====		=====
WATER RATE BASE	\$31,070.17	(\$26,100.05)		\$4,970.12

(1) Audit adjustments do not include audit disclosures.

EXHIBIT II

**HOLMES UTILITIES, INC.
DOCKET NO. 010403-WU
NET OPERATING INCOME
12-MONTH PERIOD ENDED DECEMBER 31, 2000**

DESCRIPTION	PER UTILITY 12/31/00	AUDIT EXCEPTION	REFER TO(1)	PER AUDIT 12/31/00
OPERATING REVENUES	\$8,669.40	\$1,941.50	E-6	\$10,610.90
	-----	-----		-----
OPERATING EXPENSES:				
O&M EXPENSE	15,981.28	0.00		15,981.28
DEPRECIATION EXPENSE	1,085.00	(169.19)	E 3	915.81
AMORTIZATION OF CIAC	(296.00)	(76.02)	E 4	(372.02)
TAXES OTHER THAN INCOME	887.73	0.00		887.73
	-----	-----		-----
TOTAL OPERATING EXPENSE	\$17,658.01	(\$245.21)		\$17,412.80
	-----	-----		-----
NET OPERATING INCOME (LOSS)	(\$8,988.61)	\$2,186.71		(\$6,801.90)

(1) Audit adjustments do not include audit disclosures.

(2) S Corporation - Income Taxes are not included.

EXHIBIT III

**HOLMES UTILITIES, INC.
DOCKET NO. 010403-WU
CAPITAL STRUCTURE
AS OF DECEMBER 31, 2000**

DESCRIPTION	PER COMPANY	AUDIT EXCEPTION	REFER TO(1)	PER AUDIT	RATIO	COST RATE(3)	WEIGHTED COST OF CAPITAL
COMMON EQUITY	\$4,970.12			\$4,970.12		8.5%	8.5%
TOTAL	\$4,970.12			\$4,970.12			8.5%

- (1) Audit adjustments do not include audit disclosures.
- (2) Retained Earnings were negative and not included.