

State of Florida



## Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD  
TALLAHASSEE, FLORIDA 32399-0850

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

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**DATE:** October 29, 2007  
**TO:** Stephen B. Fletcher, Professional Accountant Specialist, Division of Economic Regulation  
**FROM:** Denise N. Vandiver, Chief of Auditing, Division of Regulatory Compliance & Consumer Assistance *DNV*  
**RE:** Docket No: 070293-SU; Company Name: KW Resort Utilities Corp.;  
Audit Purpose: File and Suspend Rate Case;  
Audit Control No: 07-233-4-1:

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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. There are confidential work papers associated with this audit.

DNV:bj  
Attachments

Copy: Division of Regulatory Compliance and Consumer Assistance (Hoppe, District Offices, File Folder)  
Division of Commission Clerk (2)  
Division of Competitive Markets and Enforcement (Harvey)  
General Counsel  
Office of Public Counsel

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DOCUMENT NUMBER-DATE

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FPSC-COMMISSION CLERK



FLORIDA PUBLIC SERVICE COMMISSION  
*DIVISION OF REGULATORY COMPLIANCE & CONSUMER ASSISTANCE*  
*BUREAU OF AUDITING*

*Miami District Office*

**KW RESORT UTILITIES CORP.**  
**FILE AND SUSPEND RATE CASE INVESTIGATION**

**AS OF DECEMBER 31, 2006**

**DOCKET NO. 070293-SU**  
**AUDIT CONTROL NO. 07-233-4-1**

*Iliana Piedra*  
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DOCUMENT NO. 0474

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CSO - COMMISSION CLAIMS

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**DIVISION OF REGULATORY COMPLIANCE & CONSUMER ASSISTANCE  
AUDITOR'S REPORT**

**October 25, 2007**

**TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES**

We have performed the procedures described later in this report to meet the agreed upon objectives set forth by the Division of Economic Regulation in its audit service request dated August 22, 2007. We have applied these procedures to the attached schedules which were prepared by KW Resort Utilities Corporation in support of its filing for rate relief in Docket No. 070293-SU.

This audit was performed following general standards and field work standards found in the AICPA Statements on Standards for Attestation Engagements. This report is based on agreed upon procedures which are only for internal Commission use.

## OBJECTIVES AND PROCEDURES

### RATE BASE

#### Utility-Plant-in-Service

*Objective:* To determine that property exists and is owned by the utility. To determine that additions to plant are authentic, recorded at original cost, and properly classified in compliance with Commission rules and the NARUC Uniform System of Accounts. To verify that the proper retirements of plant were made when a replacement item was put in service.

*Procedures:* We sampled plant additions for the period January 1, 1998 through December 31, 2006 for compliance with the stated objectives above. We were unable to audit 1984 to 1997 because when the stock transfer in 1998 took place, the current owners did not obtain the records of the previous owner. We verified that the utility properly recorded retirements to plant when a capital item was removed or replaced. We toured the utility plant sites to observe whether assets additions were completed and to ascertain if asset retirements were properly recorded. We sampled construction project additions and the corresponding source documentation. Audit finding one discusses the original cost study done for 1984 to 1997. Audit finding two discusses the affiliate transactions with Green Fairways. Audit finding three discusses the affiliate transactions with Key's Environmental Service. Audit finding four discusses the franchise account. Audit finding five discusses a one sided correction made by the utility. Audit finding six discusses a retirement not booked with the proforma adjustment. We reconciled the proforma adjustment to the current construction project contract.

#### Land and Land Rights

*Objective:* To determine that utility land is recorded at original cost and is owned or secured under a long-term lease.

*Procedures:* We verified that there have been no changes to utility land since its last rate proceeding by searching the county's public records. We obtained the deeds for land and determined they were recorded at original cost. The proforma adjustment was reconciled to the cost of the land.

#### Contributions-in-Aid-of-Construction (CIAC) and Advances for Construction

*Objective:* To determine that additions to CIAC and Advances are properly recorded in compliance with Commission rules and the NARUC Uniform System of Accounts. To verify that CIAC additions and Advances are reflective of the utility's Commission approved service availability tariff. To verify and insure that all donated property is properly accounted for and recorded as CIAC and plant.

*Procedures:* We sampled CIAC and Advance additions for the period January 1, 1998 through December 31, 2006 for compliance with the stated objectives above. We scanned the utility's cash receipts records for unrecorded cash and property. We reviewed developer agreements for unrecorded CIAC. We traced utility CIAC schedules to the general ledger and the utility's authorized tariff rates. We toured the utility's authorized service territory to look for new developments that may have included contributed property. We reviewed the agreement with Monroe County to determine if it was properly reflected in the utility books. We reconciled plant in the tax return to plant in the ledger to determine if any contributed property was not

recorded. Since we were unable to obtain the records from 1984 to 1997, we were unable to verify CIAC for those years and could not determine if any contributed assets were not recorded. Audit finding eight discusses the Monroe County agreement.

#### Accumulated Depreciation

*Objective:* To determine that accruals to accumulated depreciation are properly recorded in compliance with Commission rules and the NARUC Uniform System of Accounts. To verify that depreciation expense accruals are calculated using the Commission authorized rates and that retirements are properly recorded.

*Procedures:* We traced the accumulated depreciation schedules to the corresponding plant schedules from 1990 to 2006. We were unable to obtain supporting documentation for depreciation calculations from 1984 to 1990. We verified that the utility used Commission authorized rates to depreciate its plant accounts by calculating a sample of accumulated depreciation account balances to test for calculation errors. We verified that the utility properly recorded retirements to accumulated depreciation when the corresponding plant was removed or replaced. Audit finding seven discusses rates not in compliance with the rule and other depreciation issues.

#### Accumulated Amortization of CIAC

*Objective:* To determine that accruals to accumulated amortization of CIAC are properly recorded in compliance with Commission rules and the NARUC Uniform System of Accounts. To verify that CIAC amortization expense accruals are properly recorded and calculated based on the rates and method used in the utility's last rate proceeding.

*Procedures:* We traced the accumulated amortization of CIAC schedules to the corresponding CIAC schedules. We verified that the utility used Commission authorized rates to amortize its CIAC accounts by calculating a sample of accumulated amortization account balances to test for calculation errors. We recalculated a sample of accumulated amortization of CIAC account balances as of December 31, 2006. Audit finding seven discusses the change in amortization because of the adjustment to depreciation expense.

#### Working Capital

*Objective:* To determine that the utility's working capital balance is properly calculated in compliance with Commission rules.

*Procedures:* We recalculated the utility's working capital balance as of December 31, 2006. Audit finding nine discusses the inclusion of interest earning accounts.

### **NET OPERATING INCOME**

#### General

*Objective:* To determine that the utility's filing represents its results from continuing operations.

*Procedures:* We reconciled the following individual component net operating income balances to the utility's general ledger for the 12-month period ended December 31, 2006.

### Revenues

*Objective:* To determine that revenues are properly recorded in compliance with Commission rules and are based on the utility's Commission approved tariff rates.

*Procedures:* We traced revenues to the general ledger and utility billing registers and selected a sample of customer bills from each commercial customer rate class on a random basis and recalculated the bills using the Commission approved tariff rates. The utility is still billing its residential customers at a flat rate. The file used to determine gallonage was obtained. The billing analysis in the filing and the annualizing adjustments were tested and traced to supporting documentation. Audit finding ten discusses revenues not recorded.

### Operation and Maintenance Expenses (O&M)

*Objective:* To determine that operation and maintenance expenses are properly recorded in compliance with Commission rules and were reasonable and prudent for ongoing utility operations.

*Procedures:* We sampled O&M expense items from the general ledger based on auditor judgment. We reviewed the sample for the proper utility system, classification, NARUC account, amount, period and recurring nature. We examined invoices and supporting documentation to determine if the above objectives were met. We obtained documentation from the engineer to support the utility proforma adjustment for electricity, chemicals, and sludge hauling. The staff engineer needs to review the supporting documentation obtained for reasonableness. See audit finding three for the discussion of the affiliate transactions with Keys Environmental. See audit findings 11-17 and 19 for the discussion of various adjustments to expenses.

### Taxes-Other-Than-Income

*Objective:* To determine that taxes other than income tax expense is properly recorded, in compliance with Commission rules and were reasonable and prudent for ongoing utility operations.

*Procedures:* We recalculated the regulatory assessment fee amounts and reconciled them to the general ledger. We obtained the property tax bills for review and to determine if the amount booked reflects the discount amount. See audit finding 18 for an adjustment to taxes other than income.

### Depreciation Expense

*Objective:* To determine that depreciation expense is properly recorded in compliance with Commission rules and that it accurately represents the depreciation of plant assets and amortization of CIAC assets for ongoing utility operations.

*Procedures:* We recalculated a sample of plant depreciation expense and CIAC amortization expense balances for the period using Commission approved rates and we verified that CIAC amortization expense was properly netted against depreciation expense.

## CAPITAL STRUCTURE

### General

*Objective:* To determine the components of the utility's capital structure and the respective cost rates used to arrive at the overall weighted cost of capital are properly recorded in compliance with Commission rules and that it accurately represents the ongoing utility operations.

*Procedures:* We reconciled the following individual component capital structure balances to the utility's general ledger as of December 31, 2006.

### Long-Term-Debt

*Objective:* To determine that long-term debt balances represent actual obligations of the utility's parent and that they are properly recorded in compliance with Commission rules.

*Procedures:* We traced long-term debt balances to the original documents and verified the terms and interest rate of each note payable.

### Accumulated Deferred Income Taxes

*Objective:* To determine that accumulated deferred income taxes are properly stated and calculated based on the recorded differences between utility book and taxable income.

*Procedures:* Recalculated a sample of deferred tax balances for the period using Commission authorized rates and federal tax rates.

### Customer Deposits

*Objective:* To determine that customer deposit balances represent actual obligations of the utility and are properly recorded in compliance with Commission rules.

*Procedures:* We traced a sample of customer deposit balances to supporting documentation and verified that customer deposits were refunded and credited with interest payments in compliance with Commission rules.



**AUDIT FINDING NO. 1**

**SUBJECT: COST STUDY**

**AUDIT ANALYSIS:** The last rate case order used a test year of December 31, 1983. The utility was taken over by Citicorp as a result of a default on its mortgage. In 1998, the current owners took over the utility through a stock purchase. The new owners did not obtain the books and records from Citicorp. We were not able to obtain supporting documentation for plant or contribution in aid of construction additions from 1984 to 1997. However, we were able to obtain depreciation and amortization schedules back to 1990.

There are \$2,137,961.86 of unsubstantiated plant additions for 1984 to 1997. Depreciation on these additions was \$330,066.33 and the annual impact on depreciation expense is \$10,523.24. There were \$867,668 of additions to contributions in aid of construction from 1984 to 1997. In addition, without the records we were unable to determine if there was any unrecorded CIAC. Accumulated amortization additions on this amount were \$32,219.

We asked the utility to prepare an original cost study for these additions. It was not received at the time the report was issued.

We calculated accumulated depreciation of \$330,066.33 by taking the ending accumulated depreciation at 12/31/97 and reducing it for depreciation on the last ordered balance for 14 years. We determined the depreciation expense of \$10,523.24 taking the difference in plant accounts times the current depreciation rates. A schedule can be found on the following page.

**EFFECT ON THE GENERAL LEDGER:** If the cost study does not support the additions, the following should be removed from rate base:

	DEBIT	CREDIT
UNDOCUMENTED PLANT	972,446.53	
CIAC	867,668.00	
ACCUMULATED DEPRECIATION	330,066.33	
PLANT		2,137,961.86
ACCUMULATED AMORTIZATION		32,219.00

**EFFECT ON THE FILING:** Average rate base should be reduced by \$972,446.53 and depreciation expense should be reduced by \$10,523.24.

PLANT ACCOUNT	AMOUNT 1983 PLANT	COMPANY RATE	DEPRECIATION EACH YEAR	YEARS 1984-1997	1997			2006	
					DEPRECIATION 1984-1997	ACCUMULATED DEPRECIATION	DIFFERENCE	RATE	DEPRECIATION DIFFERENCE
354	18,684.00	3.33%	622.18	14.00	8,710.48	39,418.95	30,708.47	3.33%	1,022.59
354						8,530.33	8,530.33	3.33%	284.06
361	50,448.00	3.33%	1,679.92	14.00	23,518.86	163,171.46	139,652.60	2.22%	3,100.29
371	225,351.00	10.00%	22,535.10	14.00	225,351.00	251,138.42	25,787.42	5.56%	1,433.78
381 now									
361	192,420.00	5.00%	9,621.00	14.00	134,694.00	235,673.89	100,979.89	2.22%	2,241.75
390	2,478.00	10.00%	247.80	14.00	2,478.00	2,477.97	(0.03)	6.67%	(0.00)
398 now									
380	577,145.00	6.66%	38,437.86	14.00	538,130.00	562,537.65	24,407.65	10.00%	2,440.77
	<u>1,066,526.00</u>		<u>73,143.85</u>		<u>932,882.34</u>	<u>1,262,948.67</u>	<u>330,066.33</u>		<u>10,523.24</u>

## **AUDIT FINDING NO. 2**

### **SUBJECT: GREEN FAIRWAYS:**

**AUDIT ANALYSIS:** Mr. William L. Smith, president of KW Resort Utilities Corp., has a law practice and owns several other businesses. The following businesses are managed through Green Fairways.

Key West Golf Course  
Venetian Partners-office Building in San Francisco  
KW Resort Utilities, Corp.  
900 Commerce-offices in Oakbrook, Illinois  
Portland Court-office building in Addison  
Rail Golf Course-in Springfield, Illinois  
Deer Creek Golf Course-University Park, Illinois

Three employees are paid by Green Fairways. Mike Misheck runs the golf courses and Key West Golf club. Bill Ski runs the office buildings and Bill Smith oversees all the businesses and runs KW Resort.

Bill Smith performs the following duties for the utility:

Reviews all bids  
Hires key employees for all companies (used to use Davis and Synagro)  
Approves and reviews budgets  
Coordinates financing  
Advances funds  
Monitors contract employees  
Coordinates public relations  
Engages accountants and lawyers  
Coordinates with Florida Keys Aqueduct Authority  
Engages engineers  
Coordinates county contract  
Negotiates customer contracts  
Supervises expansion  
Coordinates the rate case

Mr. Smith indicates that 1/3 of his time is spent on the utility. According to a letter provided by his accountant, one third of his actual salary far exceeds the amount included in KW Resort expense. But, Mr. Smith manages many companies and there are no time records to support the allocation of his time spent on the utility. It should also be noted that most of Mr. Smith's salary is not provided in a W-2 since his businesses are limited partnerships. This is the reason we requested the letter from the accountant regarding his total salary. Less than 10% of Mr. Smith's salary comes from Green Fairways, because he is paid the excess of Green Fairways revenues less expense. Because we cannot determine the actual hours spent on the utility, we cannot

determine the reasonableness of the charges in relation to his other companies.

Green Fairways charged \$60,000 to expense as a management fee. It also charges 10% of large construction projects to plant for the management of the construction project. Green Fairways charged the utility \$107,198.07 in 2002 and \$194,376.80 in 2003 for the project of lining the collection system with a fiberglass liner in order to keep from having to replace the crumbling clay system. In 2006, \$124,983.76 has been charged for the work on the Advanced Wastewater Treatment plant expansion project. Additional charges may be incurred for the project. However, they have not been included in the proforma.

Based on Mr. Smith's W-2's from Green Fairways, and the management fees and project administration fees, the following analysis was prepared. The salary Mr. Smith received is less than the amount charged as a management fee in 2006.

YEAR	BILL SMITH W-2 GREEN FAIRWAYS SAL.	MANAGEMENT FEES TO KW RESORT IN EXP.	PROJECT ADMINISTRATION FEES IN PLANT	TOTAL CHARGED KW RESORT
2001	55,000.00	60,000.00		60,000.00
2002	190,000.00	60,000.00	107,198.07	167,198.07
2003	70,000.00	100,000.00	194,376.80	294,376.80
2004	70,000.00	80,000.00		80,000.00
2005	35,000.00	81,667.00		81,667.00
2006	40,000.00	60,000.00	124,983.78	184,983.78

**EFFECT ON THE GENERAL LEDGER:** This finding is for informational purposes only.

**EFFECT ON THE FILING:** This finding is for informational purposes only.

**AUDIT FINDING NO. 3**

**SUBJECT: KEY'S ENVIRONMENTAL SERVICE**

**AUDIT ANALYSIS:** Key's Environmental Service was started by Mr. Smith's son-in-law to service KW Resort Utilities. Key's Environmental Service also has contracts to service some of the privately owned lift stations. Key's Environmental has its offices in the utility owned trailer. It pays the utility \$24,000 for the use of this trailer. It also uses the utility owned trucks but pays for its own gasoline and vehicle maintenance.

Key's Environmental purchases supplies, chemicals, and sludge hauling and then bills the utility company for these services. Whenever a related party charges a utility for service, we are concerned that the related party bill the utility at actual cost and does not use the affiliate company to inflate prices to the utility. We attempted to determine if Key's Environmental inflates the costs for these re-bills. We have reviewed a sample of the costs to prices on the internet, and the Tallahassee engineer will determine if these appear reasonable. We made other comparisons, to determine the reasonableness of the costs, and these are explained later in this finding.

Some of the Key's Environmental invoices have been capitalized and some expensed. The following schedule indicates the total invoices by year that have been capitalized.

YEAR	TOTAL
2003	82,940.00
2004	12,834.46
2005	109,306.14
2006	154,590.06
	<u>359,670.66</u>

Of this amount, \$252,690.08 was paid for performing services as a hookup coordinator. The duties include five field visits and a hydrostatic test of the PVC lateral from the building to the point of connection. Other costs include site preparation work for the new clarifier, power poles, effluent lines, relocation of the chlorine tank, pumps, surge tank, and a blower.

The utility has a contract with Key's Environmental that requires two full time operators, a manager to work a minimum of eight hours a day on weekdays and two hours a day on the weekends. The contract includes customer relations, periodic inspections, minor maintenance, inspecting pumping stations daily, preventative maintenance programs, monitor collection systems, monitor reclaimed water lines, monitor meters, pumps, and blowers. Key's reads the meters and maintains an answering service and dispatch. The contract also says they will do the sampling and testing and supervise and inspect new customer tie in's.

In 2006, \$450,774.11 was charged to expense for invoices from Key's Environmental. These costs include:

278,472.00	Monthly Operations Fee for 12 months at \$23,206 a month
39,999.96	Monthly charge for Air Vac service for 12 months
<u>318,471.96</u>	
(81,232.57)	Fees received from developers for review and inspection were used to reduce the monthly operating fee amount
<u>237,239.39</u>	
15,000.00	Hookup fees that should be capitalized
43,202.75	Chemicals and supplies
981.60	Trailer repairs
59,283.14	Plant repairs
24,004.42	Vacuum repairs
19,472.10	Sludge hauling
2,392.60	Filter beds work
6,651.94	Generator work
631.41	Equipment and supplies
2,853.50	Lift Station cleaning
37,404.67	Lift Station repair
1,637.28	Pump repair
1,376.00	Sewer line cleaning
10,180.68	Sewer line repair
24,895.47	Vacuum collection system
14,535.92	Effluent repairs
1,530.00	Miscellaneous
(52,496.76)	Transferred to plant
<u>450,776.11</u>	

Included in the chemicals and supplies charges is \$1,313.65 for lab testing. Sampling and testing was supposed to be part of the contract. These charges need to be removed.

The \$15,000 of hookup fees charged to the operations account should be transferred to plant account 363. Depreciation at 2.63% for one-half year is \$197.25. However, the operations contract does say that supervising and inspecting new tie in's is part of the contract. The description of what Key's Environmental is doing for the connection fee appears to be more extensive. We recommend that the staff engineer determine if the work being done exceeds what is in the operations contract. If not, the \$252,690.08 plus the misclassified \$15,000 or \$276,690.08 should all be removed from plant. The accumulated depreciation related to these additions would be \$12,026.33 and depreciation expense would be \$3,308.40.

Included in various accounts were \$51,662.97 of items that appeared to be capital items. The utility was asked to justify why these items were expensed. We did not receive an answer to this request. The items are listed below and should be reviewed by the Tallahassee engineer.

DATE	CHECK NUMBER	DESCRIPTION	COST
2/13/2006	1305/1309	INSTALLED NEW 5 HP 230 VOLT 60 HZ PUMP GC MAIN 3300.24 AND WHR5-23 1/2 HP 230 VOLD 2" DISCHARE AND 20' CORD AT 739.92 2 SPARE PUMPS REBUILT FOR LS L2A, FORCE MAIN AND GOLF	4,407.67
3/11/2006	1345/1322	COURSE MAIN L1 CROSS AND 5TH, SET POLE AND INSTALL 120/240 VAC 100 AMP	3,784.65
3/11/2006	1345/1322	SERVICE	3,700.95
3/11/2006	1345/1322	REBUILD YOMAN SEWERAGE PUMP AT VACUUM STATION	3,473.93
3/11/2006	1345/1322	FABRICATED DIFFUSERS NEW PLANT 1.5 HOURS CURTIS	135.00
3/11/2006	1345/1322	4 SHELVING UNITS FOR TRAILER GENERATOR KOHLER SET UP NEXT TO MAINT BUILDING- 4.5	668.31
4/10/2006	1364	HOURS CRANE AND OPERATOR	877.50
4/10/2006	1364	CRANE AND CONTROLS FOR WELDING	573.80
4/10/2006	1364	PVC FOR NEW AIR DIFFUSER PROJECT	489.39
4/10/2006	1364	ALL S & V SUPPLIES FOR WWTP FOR AIR HEADER AND DIFFUSER	882.48
4/10/2006	1364	NIPPLE, PVC AND FITTINGS FOR AIR DIFFUSER	644.13
4/10/2006	1364	PVC FITTING FOR NEW AIR HEADER	60.12
4/10/2006	1364	FITTING, SAW BLADE AND HAND RAP FOR AIR HEADER	155.46
4/10/2006	1364	SCAFFOLDING RENTED FOR NEW AIR HEADER	78.26
4/10/2006	1364	4 CHLORINE TURBIDITY FEED PUMPS	560.19
4/10/2006	1364	WIRE FOR WWTP AND CS	516.31
4/10/2006	1364	AIR HEADER DIFFUSER JOB	145.35
5/16/2006	1397	PVC PARTS FOR DRYING BED AIR LINE FITTINGS TO REPLACE 3 PIECE UNIONS THAT WERE INSTALLED	1,716.96
5/16/2006	1397	ON NEW PVC DIFFUSERS	65.40
5/16/2006	1397	SPARE ALTERNATOR FOR LIFT STATION 3 GRINDER IMPELLER FOR LS L2A, FM GC MAIN AND 2 SHREDDING	1,212.69
5/16/2006	1397	RINGS	1,568.75
5/16/2006	1397	SPARE CONTACTORS FOR L2A, FM AND GC MAIN	453.09
5/16/2006	1397	KWRU GENERATORS STAND BY FOR FUEL TANK NEW SURGE PUMP 2 FOR OLD WWTP-GOULD'S MODEL 388804 SUB	955.27
6/6/2006	1404/1412	2650.7 AND FOULDS PN A 1-6 RADIUS ELBOW 142.35	3,002.53
7/10/2006	1460	8 CLEAN OUT BOXES AND LIDS	804.63
8/9/2006	1479	SHADE AT WWTP CANOPY	527.05
8/9/2006	1479	EMERGENCY GENERATOR CONNECTOR FOR LS	502.09
8/9/2006	1479	COLLECTION SYSTEM VOLTAGE REGULATORS 2	972.62
10/5/2006	1554	#3 BLOWER	1,478.44
11/8/2006	1589	CUTTING TORCH FOR REMOVAL OF THICKENER	820.25
11/8/2006	1589	8 FILTER ELEMENTS AND BLOWER 1476.09	2,259.61
11/8/2006	1589	NORTH CLORINE CONTACT CHAMBER VALVE	1,994.79
11/8/2006	1589	GOLF COURSE POND LS PUMP	1,361.49
12/7/2006	1607	NEW PLANT SURGE TANK PUMPS -2	9,105.80
12/7/2006	1607	SETTING SURGE PUMPS	341.25
12/7/2006	1607	SPARE SLUDGE DRIVE MOTOR	533.85
12/7/2006	1607	POWER TOOLS V18-4pk	832.91
			51,662.97

Also included in the expense accounts was a bill for \$2,082.31 for damage to a pit vacuum that was caused by Waste Management. This is expected to be recovered from Waste Management and should be removed from expenses. There was also an invoice for the Oceanside Marina of \$995.30 that is supposed to be reimbursed by the County.

To determine the reasonableness of the monthly maintenance fee, we reviewed an estimate the utility received from US Water for a monthly operations fee of \$33,171.34. The contract appeared to have similar terms but had 1.5 licensed operators and the Key's Environmental has two. The Key's Environmental contract contains provisions for a lead mechanic and a field tech that are not separately shown on the Key's Environmental contract. However, Key's

Environmental does have more employees than just the two licensed operators.

The utility also provided a contract from 2002 with AirVac Inc. for the same services performed by Key's Environmental now for \$3,333.33 a month. The 2002 contract was for \$5,500 a month and \$60 an hour for emergency service. The utility usually pays \$90 to Key's Environmental for emergency service and \$3,333 for the air vac system operation.

A summary of the adjustments follows:

Remove hookup fees	(15,000.00)
Remove testing fees	(1,313.65)
Remove amount due from Waste Management	(2,082.31)
Remove amount due from County	(995.30)
	<u>(19,391.26)</u>
Possible adjustments	(51,662.97)

**EFFECT ON THE GENERAL LEDGER:** The following entries should be made:

	DEBIT	CREDIT
363.0 Services to Customers	15,000.00	
907.1 Operations-Management		15,000.00
Depreciation Expense	197.25	
Accumulated Depreciation		197.25
Account Receivable Key's Environmental	4,391.26	
901.0 Chemicals and Supplies		1,313.65
903.8 Vacuum Collection		3,077.61

Additional entries may be necessary for the \$51,662.97 after a review by the staff engineer.

**EFFECT ON THE FILING:** Average plant should be increased by \$13,846.15 (\$15,000\*12/13). Average accumulated depreciation should be increased by \$98.64. Expenses should be reduced by \$19,391.26. Additional adjustments may be necessary after a review by the staff engineer.

Additional adjustments may be necessary for the \$51,662.97 after a review by the staff engineer.



January	16.44
February	32.88
March	49.32
April	65.76
May	82.20
June	98.64
July	115.08
August	131.52
September	147.96
October	164.40
November	180.84
December	197.25
	<u>1,282.26</u>
Average	98.64

**AUDIT FINDING NO. 4**

**SUBJECT: FRANCHISE FEES**

**AUDIT ANALYSIS:** In 1999, the utility recorded \$125,364.06 as franchise fees. The utility used this account because they claim that the charges were to set laws in place to force people to hook up to the utility system. A summary of the charges follows:

25,000.00	Consulting Fees Jack London
18,919.44	Legal Fees Franchise Expansion
81,444.62	Weiler Engineering for Design of Plant Expansion
<u>125,364.06</u>	

The engineering related to the new plant does not appear to relate to franchises but instead to design of the new treatment plant. If the \$81,444.62 of engineering fees were transferred to treatment and disposal plant, it would be depreciated at 5.56% instead of 2.5%. This would increase depreciation expense by \$2,492.21 a year, and increase accumulated depreciation by 7.5 years of additional depreciation expense, or \$18,691.54.

**EFFECT ON THE GENERAL LEDGER:** The following entry should be made:

	DEBIT	CREDIT
Treatment and Disposal Equipment	81,444.62	
Franchise		81,444.62
Retained Earnings	16,199.33	
Accumulated Depreciation Franchise	15,270.87	
Depreciation Expense	2,492.21	
Accumulated Depreciation Treatment Eq.		33,962.41

**EFFECT ON THE FILING:** Average accumulated depreciation should be reduced by \$9,345.78. Depreciation expense should be increased by \$2,492.21.

JANUARY	1,557.63
FEBRUARY	3,115.26
MARCH	4,672.89
APRIL	6,230.52
MAY	7,788.15
JUNE	9,345.78
JULY	10,903.41
AUGUST	12,461.04
SEPTEMBER	14,018.67
OCTOBER	15,576.30
NOVEMBER	17,133.93
DECEMBER	18,691.54
TOTAL	<u>121,495.10</u>
AVERAGE	<u>9,345.78</u>

**AUDIT FINDING NO. 5**

**SUBJECT: OFFSET TO LAND ENTRY**

**AUDIT ANALYSIS:** Schedule A-4, a summary of plant by year, shows a reduction to land in 1989 for \$152,255. The filing correctly increased land for the same amount in the proforma adjustments. This brings the land account back to the ordered balance and the amount that matches the documentary stamps for the land purchase. However, no adjustment was made for the other side of the entry that reduced land. The debit to the original entry was a debit to three plant accounts: structures by \$38,063.56, collection sewers by \$38,064.11 and plant sewers by \$76,126.96

Since land was increased to its original value, structures should be reduced by \$38,063.56, collection sewers by \$38,064.11, and plant sewers by \$76,126.96. In 1998, plant sewers were incorporated into account 380, treatment and disposal equipment. Collection sewers were incorporated into account 360, force mains.

Accumulated depreciation is adjusted in a separate exception in this report. Using the adjusted rates, the accumulated depreciation adjustment related to these findings is \$23,449.06, \$23,458.27, and \$33,407.47. The associated depreciation expense should be reduced by \$6,765.59. The detail can be found on the next page.

**EFFECT ON THE GENERAL LEDGER:** The following entries should be made:

	DEBIT	CREDIT
354 STRUCTURES AND IMPROVEMENTS		38,065
360 COLLECTION SEWERS FORCE		38,064
380 TREATMENT AND DISPOSAL EQ.		76,127
353 LAND	152,255	
108 ACC. DEP. STRUCTURES	23,449	
108 ACC. DEP. COLLECTION SEWERS FORCE	23,458	
108 ACC. DEP. TREATMENT AND DISPOSAL	33,407	
DEPRECIATION EXPENSE		6,766
RETAINED EARNINGS		73,549

**EFFECT ON THE FILING:** Average plant should be reduced by \$152,255. Average accumulated depreciation should be reduced by \$71,274.36. Depreciation expense should be reduced by \$6,765.59.

	2006 DEP. EXP. WITHOUT ADJUSTMENT	2006 DEP. EXP. WITH ADJUSTMENT	DIFFERENCE	2006 A/D WITHOUT ADJUSTMENT	2006 A/D WITH ADJUSTMENT	DIFFERENCE
351 ORGANIZATION	0.00	0.00	0.00	0.00	0.00	0.00
352 FRANCHISES	(3,134.10)	(3,134.10)	0.00	(23,505.75)	(23,505.75)	0.00
353 LAND & LAND RIGHTS STRUCTURE AND	0.00	0.00	0.00	0.00	0.00	0.00
354 IMPROVEMENTS POWER GENERATION	(18,826.19)	(17,558.67)	(1,267.52)	(169,184.06)	(145,735.01)	(23,449.06)
355 EQUIPMENT COLLECTION SEWERS -	(6,370.13)	(6,370.13)	0.00	(2,392.33)	(2,392.33)	0.00
360 FORCE COLLECTION SEWERS -	(122,118.57)	(120,849.77)	(1,268.80)	(994,949.13)	(971,490.86)	(23,458.27)
361 GRAVITY SPECIAL COLLECTING	(19,082.57)	(19,082.56)	(0.00)	(126,087.60)	(126,087.60)	(0.00)
362 STRUCTURES	0.00	0.00	0.00	0.00	0.00	0.00
363 SERVICES TO CUSTOMERS	(6,705.89)	(6,705.89)	0.00	(9,124.26)	(9,124.26)	0.00
364 FLOW MEASURING DEVICES FLOW MEASURING	0.00	0.00	0.00	0.00	0.00	0.00
365 INSTALLATIONS	0.00	0.00	0.00	0.00	0.00	0.00
366 REUSE SERVICES REUSE METERS AND METER	0.00	0.00	0.00	0.00	0.00	0.00
367 INSTALLATIONS	0.00	0.00	0.00	0.00	0.00	0.00
370 RECEIVING WELLS	(29,064.43)	(29,064.43)	0.00	(101,618.98)	(101,618.98)	0.00
371 PUMPING EQUIPMENT REUSE DISTRIBUTION	(11,194.75)	(11,194.75)	0.00	(200,489.28)	(200,489.28)	0.00
374 RESERVOIRS REUSE TRANSMISSION AND	0.00	0.00	0.00	0.00	0.00	0.00
375 DISTRIBUTION SYSTEM TREATMENT & DISPOSAL	(5,639.01)	(5,639.01)	0.00	2,348.71	2,348.71	0.00
380 EQUIPMENT	(140,071.67)	(135,842.39)	(4,229.28)	(1,553,536.99)	(1,520,129.52)	(33,407.47)
381 PLANT SEWERS	(517.84)	(517.84)	0.00	(716.80)	(716.80)	0.00
382 OUTFALL SEWER LINES OTHER	0.00	0.00	0.00	0.00	0.00	0.00
PLANT/MISCELLANEOUS						
389 EQUIPMENT OFFICE FURNITURE &	(2,455.72)	(2,455.72)	0.00	29,217.66	29,217.66	0.00
390 EQUIPMENT TRANSPORTATION	(1,221.93)	(1,221.93)	0.00	(7,710.37)	(7,710.37)	0.00
391 EQUIPMENT	(7,748.33)	(7,748.33)	0.00	(12,809.50)	(12,809.50)	0.00
392 STORES EQUIPMENT TOOLS, SHOP AND GARAGE	0.00	0.00	0.00	0.00	0.00	0.00
393 EQUIPMENT	(1,482.78)	(1,482.78)	0.00	(5,149.19)	(5,149.19)	0.00
394 LABORATORY EQUIPMENT POWER OPERATED	(144.90)	(144.90)	0.00	(330.40)	(330.40)	0.00
395 EQUIPMENT COMMUNICATION	(3,987.88)	(3,987.88)	0.00	(16,470.74)	(16,470.74)	0.00
396 EQUIPMENT MISCELLANEOUS	0.00	0.00	0.00	0.00	0.00	0.00
397 EQUIPMENT	0.00	0.00	0.00	0.00	0.00	0.00
398 OTHER TANGIBLE PLANT	0.00	0.00	0.00	0.00	0.00	0.00
	<b>(379,766.69)</b>	<b>(373,001.10)</b>	<b>(6,765.59)</b>	<b>(3,192,509.01)</b>	<b>(3,112,194.22)</b>	<b>(80,314.79)</b>

JANUARY	74,113.00
FEBRUARY	74,676.80
MARCH	75,240.60
APRIL	75,804.40
MAY	76,368.20
JUNE	76,932.00
JULY	77,495.79
AUGUST	78,059.59
SEPTEMBER	78,623.39
OCTOBER	79,187.19
NOVEMBER	79,750.99
DECEMBER	<u>80,314.79</u>
TOTAL	<u>926,566.74</u>
AVERAGE	<u>71,274.36</u>

**AUDIT FINDING NO. 6**

**SUBJECT: RETIREMENTS RELATED TO PLANT PROFORMA**

**AUDIT ANALYSIS:** Filing Schedule A-3 increases plant for the contract with Siemens for the work done on the Advanced Wastewater Treatment (AWT) plant expansion. As part of the expansion, a clarifying unit was installed. To make room for this unit, two drying beds and a sludge thickening unit were removed. The adjustment to increase plant does not take into account the removal and retirement of these items. We could not determine the original cost of these items from the records we have in order to determine the entry needed to the ledger. Since retirements decrease plant and increase accumulated depreciation, there is no effect on rate base. The utility plans to adjust for the retirement when the plant is completed.

**EFFECT ON THE GENERAL LEDGER:** Cannot be determined at this time.

**EFFECT ON THE FILING:** There may be a small effect on accumulated depreciation and depreciation expense if these items are still being depreciated. There is no effect on rate base for the retirement itself.

**AUDIT FINDING NO. 7**

**SUBJECT: ACCUMULATED DEPRECIATION**

**AUDIT ANALYSIS:** Rule 25-30.140, F.A.C. (Depreciation) was not in effect when the utility had its last rate case. The rule must be implemented at the rate case after the rule was made. However, the utility can start using the rule at any time. Once it does, however, it must continue to use the rule. The utility did not follow rule 25-30.140, F.A.C. until the year 2000. However, in implementing the rule, some of the rates used were different than the rule rates. In addition, in 2006, an error in the formula for tools was found. The rule also requires that Contributions in Aid of Construction (CIAC) be segregated by type of addition and that these additions be separately amortized based on type. Since we have not located any contributed property, it appears reasonable that the utility left all the CIAC in one account for capacity fees. However, according to the rule, cash should be amortized using a composite rate. In 2000, 2001, and 2002, the utility mistakenly left out certain accounts in calculating its composite rate. Because of these errors, staff has recomputed depreciation using the proper rule rates. Since the revised depreciation changes the composite rate for amortization we have recalculated the amortization of CIAC.

A schedule showing the difference between staff accumulated depreciation is on the following page. The difference in depreciation expense is shown next. The difference in accumulated amortization and amortization expense follows that. These calculations are made before the adjustments made in finding five.

**EFFECT ON THE GENERAL LEDGER:** The following entry should be made:

	<b>DEBIT</b>	<b>CREDIT</b>
Depreciation Expense	31,543.69	
Retained Earnings	255,568.32	
Accumulated Depreciation		287,112.01
Accumulated Amortization	114,886.45	
Retained Earnings		99,364.18
Amortization Expense		15,522.27

**EFFECT ON THE FILING:** Average Accumulated Depreciation should be increased by \$251,681.06. Average Accumulated Amortization should be increased by \$99,481.92. Depreciation expense should be increased by the net of \$16,021.42.

ACCUMULATED DEPRECIATION		RATES	STAFF DEPRECIATION RATES	STAFF 2006 A/D BALANCE	PER FILING YEAR END	DIFFERENCE
		1988-1999				
351	ORGANIZATION	2.50%	2.50%	0.00		0.00
352	FRANCHISES	2.50%	2.50%	(23,505.75)	(23,506.00)	0.25
353	LAND & LAND RIGHTS			0.00		0.00
354	STRUCTURE AND IMPROVEMENTS	3.33%	3.33%	(169,184.06)	(158,357.00)	(10,827.06)
355	POWER GENERATION EQUIPMENT		5.00%	(2,392.33)	(1,641.00)	(751.33)
360	COLLECTION SEWERS - FORCE	3.33%	3.33%	(994,949.13)	(932,945.00)	(62,004.13)
361	COLLECTION SEWERS - GRAVITY	3.33%	2.22%	(126,087.60)	(190,957.00)	64,869.40
362	SPECIAL COLLECTING STRUCTURES		2.50%	0.00		0.00
363	SERVICES TO CUSTOMERS		2.63%	(9,124.26)	(9,119.00)	(5.26)
364	FLOW MEASURING DEVICES		20.00%	0.00		0.00
365	FLOW MEASURING INSTALLATIONS		2.63%	0.00		0.00
366	REUSE SERVICES		2.50%	0.00		0.00
367	REUSE METERS AND METER INSTALLATIONS		5.00%	0.00		0.00
370	RECEIVING WELLS		3.33%	(101,618.98)	(121,815.00)	20,196.02
371	PUMPING EQUIPMENT	10.00%	5.56%	(200,489.28)	(199,049.00)	(1,440.28)
374	REUSE DISTRIBUTION RESERVOIRS		2.50%	0.00		0.00
375	REUSE T AND D SYSTEM		2.33%	2,348.71	(23,820.00)	26,168.71
380	TREATMENT & DISPOSAL EQUIPMENT	3.33%	5.56%	(1,553,536.99)	(1,176,417.00)	(377,119.99)
381	PLANT SEWERS	5.00%	2.86%	(716.80)	(717.00)	0.20
382	OUTFALL SEWER LINES		3.33%	0.00		0.00
389	OTHER PLANT/MISCELLANEOUS EQUIPMENT	10.00%	5.56%	29,217.66	(24,101.00)	53,318.66
390	OFFICE FURNITURE & EQUIPMENT	10.00%	6.67%	(7,710.37)	(13,498.00)	5,787.63
391	TRANSPORTATION EQUIPMENT	10.00%	16.67%	(12,809.50)	(3,804.00)	(9,005.50)
392	STORES EQUIPMENT		5.56%	0.00		0.00
393	TOOLS, SHOP AND GARAGE EQUIPMENT	10.00%	6.25%	(5,149.19)	(11,242.00)	6,092.81
394	LABORATORY EQUIPMENT		6.67%	(330.40)	(331.00)	0.60
395	POWER OPERATED EQUIPMENT	8.33%	8.33%	(16,470.74)	(14,078.00)	(2,392.74)
396	COMMUNICATION EQUIPMENT		10.00%	0.00		0.00
397	MISCELLANEOUS EQUIPMENT		6.67%	0.00		0.00
398	OTHER TANGIBLE PLANT	6.66%	10.00%	0.00		0.00
				<b>(3,192,509.01)</b>	<b>(2,905,397.00)</b>	<b>(287,112.01)</b>



DEPRECIATION EXPENSE		RATES	STAFF	STAFF 2006
		1988-1999	DEPRECIATION RATES	DEP. EXP. BALANCE
351	ORGANIZATION	2.50%	2.50%	0.00
352	FRANCHISES	2.50%	2.50%	3,134.10
353	LAND & LAND RIGHTS			0.00
354	STRUCTURE AND IMPROVEMENTS	3.33%	3.33%	18,826.19
355	POWER GENERATION EQUIPMENT		5.00%	6,370.13
360	COLLECTION SEWERS - FORCE	3.33%	3.33%	122,118.57
361	COLLECTION SEWERS - GRAVITY	3.33%	2.22%	19,082.57
362	SPECIAL COLLECTING STRUCTURES		2.50%	0.00
363	SERVICES TO CUSTOMERS		2.63%	6,705.89
364	FLOW MEASURING DEVICES		20.00%	0.00
365	FLOW MEASURING INSTALLATIONS		2.63%	0.00
366	REUSE SERVICES		2.50%	0.00
367	REUSE METERS AND METER INSTALLATIONS		5.00%	0.00
370	RECEIVING WELLS		3.33%	29,064.43
371	PUMPING EQUIPMENT	10.00%	5.56%	11,194.75
374	REUSE DISTRIBUTION RESERVOIRS		2.50%	0.00
375	REUSE T AND D SYSTEM		2.33%	5,639.01
380	TREATMENT & DISPOSAL EQUIPMENT	3.33%	5.56%	140,071.67
381	PLANT SEWERS	5.00%	2.86%	517.84
382	OUTFALL SEWER LINES		3.33%	0.00
389	OTHER PLANT/MISCELLANEOUS EQUIPMENT	10.00%	5.56%	2,455.72
390	OFFICE FURNITURE & EQUIPMENT	10.00%	6.67%	1,221.93
391	TRANSPORTATION EQUIPMENT	10.00%	16.67%	7,748.33
392	STORES EQUIPMENT		5.56%	0.00
393	TOOLS, SHOP AND GARAGE EQUIPMENT	10.00%	6.25%	1,482.78
394	LABORATORY EQUIPMENT		6.67%	144.90
395	POWER OPERATED EQUIPMENT	8.33%	8.33%	3,987.88
396	COMMUNICATION EQUIPMENT		10.00%	0.00
397	MISCELLANEOUS EQUIPMENT		6.67%	0.00
398	OTHER TANGIBLE PLANT	6.66%	10.00%	0.00
				<u>379,766.69</u>
DEPRECIATION PER FILING				<u>348,223.00</u>
DIFFERENCE				<u>31,543.69</u>

JANUARY	(258,196.96)
FEBRUARY	(260,825.60)
MARCH	(263,454.24)
APRIL	(266,082.88)
MAY	(268,711.52)
JUNE	(271,340.17)
JULY	(273,968.81)
AUGUST	(276,597.45)
SEPTEMBER	(279,226.09)
OCTOBER	(281,854.73)
NOVEMBER	(284,483.37)
DECEMBER	(287,112.01)
TOTAL	<u>(3,271,853.83)</u>
AVERAGE	<u>(251,681.06)</u>

Year	Company's Rate	Total Amortization Per company	Rate per staff	Total Amortization per Staff	Staff less Company's Amtz. Difference	Cumulative Acc. Amort. CIAC
2000	2.95%	42,904.17	4.12%	59,920.39	17,016.23	17,016.23
2001	2.85%	44,581.93	4.00%	62,571.14	17,989.20	35,005.43
2002	2.92%	54,570.47	3.84%	71,763.90	17,193.44	52,198.87
2003	2.41%	65,627.49	3.44%	93,675.75	28,048.26	80,247.13
2004	3.53%	137,196.01	3.39%	131,754.81	(5,441.20)	74,805.93 A
2005	3.30%	150,078.21	3.84%	174,636.47	24,558.25	99,364.18
2006	3.43%	166,379.33	3.75%	181,901.60	15,522.27	114,886.45

A-ADJUSTMENT BECAUSE OF A RETIREMENT

JANUARY	100,657.70
FEBRUARY	101,951.23
MARCH	103,244.75
APRIL	104,538.27
MAY	105,831.79
JUNE	107,125.32
JULY	108,418.84
AUGUST	109,712.36
SEPTEMBER	111,005.88
OCTOBER	112,299.41
NOVEMBER	113,592.93
DECEMBER	114,886.45
TOTAL	<u>1,293,264.92</u>
AVERAGE	<u>99,481.92</u>

**AUDIT FINDING NO. 8**

**SUBJECT: CIAC**

**AUDIT ANALYSIS:** The utility has included both CIAC and Customer Advances for Construction in rate base. The advance account was created because the utility entered into an agreement with the County that provided for the County to pay the utility for the new plant additions. The Utility received \$3,886,674.23 in twelve payments from the County for the addition. These payments were recorded in Advances for Construction. As part of the agreement, when the utility received payments from the individuals hooking to the new vacuum system, the utility would collect and record the \$2,700 per Equivalent Residential Connection (ERC) in the Contributions in Aid of Construction account and then return to the county \$2,100 per ERC. The \$600 per ERC or \$900,000 would be kept by the utility also and should be recorded in CIAC. The tariff allows for \$2,700 per ERC as a capacity charge.

At the end of 2005 the utility had received \$1,009,477.04 in payments from customers for the CIAC. The utility had paid the County \$586,818.36. The utility then gave the County an advance of \$242,000. In 2005, \$4,100 was still owed to the County for the additions and offset the advance of \$242,000. In 2006, the utility then received \$261,052 from additional customers of which \$225,568.45 offset the \$242,000 advance. A balance of \$12,331.55 remained as an advance at the end of 2006. In 2007, the County began a program where the customers can pay the connection fee through their tax bills.

In addition to the \$3,886,674.23 received from the County, the County paid \$146,500 for design and drawings. This amount was recorded in Contributions in Aid of Construction (CIAC). The County also paid \$707,000 toward the \$600 per customer of additional CIAC that the utility is keeping over and above the tariffed amount and recorded this in CIAC even though all the customers have not yet hooked up. A summary of the amounts received from the County follows.

<b>TOTAL AMOUNT</b>	<b>CIAC ACCOUNT</b>	<b>ADVANCE ACCOUNT</b>	
146,500.00	146,500.00		Payment for Plans
707,000.00	707,000.00		Advance from County for share of \$600x 1500 ERC's that the utility will keep
<u>3,886,674.23</u>		<u>3,886,674.23</u>	12 Payments for Plant
<u>4,740,174.23</u>	<u>853,500.00</u>	<u>3,886,674.23</u>	

The utility has prepared a revised schedule showing the \$707,000 being transferred to the advance account. This entry needs to be made. However, the ledger also needs to be adjusted for the portion of the \$600 already received that has not been recorded in CIAC and the excess received from the County in addition to the advance amount.

Before the County started collecting the CIAC itself, the utility collected \$908,101.04 in CIAC from the customers and only paid the county back \$715,110.81. The additional \$192,990.23 that

did not have to be repaid to the county should have been removed from the advance and transferred to CIAC. The County then paid the remainder of the \$900,000 by giving the Utility a check for \$707,000 in advance of the customers signing up. The utility booked the \$707,000 in CIAC instead of the advance account. There is a 9.77 difference that remains. Since the County took over and until the end of 2006, 37.55 ERC's were paid for. At \$600 each, \$22,530 of the \$707,000 advance should have been removed from advances and transferred to CIAC.

Finally, the utility received and booked more in the advance account than it actually owes to the County and this amount needs to be adjusted as follows:

Amount received in twelve payments	3,886,674.23
Less amount of \$600 received by Utility but not transferred to CIAC	(192,990.23)
Less amount of advance at \$2,100	<u>(3,150,000.00)</u>
	543,684.00
Less Advance transferred to CIAC	<u>(450,684.89)</u>
Net remaining to be transferred	92,999.11

**EFFECT ON THE GENERAL LEDGER:** The following entry should be made:  
I did not catch this yesterday, but if I understand this right, shouldn't each of the journal entries below be reversed? Can you check her work papers and see if you can figure it out?

	DEBIT	CREDIT
CIAC	707,000.00	
Advances for Construction		707,000.00
To transfer advance toward \$600 per ERC from CIAC to Advance		
Advances for Construction	192,990.23	
CIAC		192,990.23
To reduce advance and increase CIAC for \$600 per customer left in advance account.		
Advances for Construction	22,536.00	
CIAC		22,536.00
To reduce advance and increase CIAC for \$600 per customer received in \$707,000 check		
Advances for Construction	92,999.11	
CIAC		92,999.11
To transfer balance of additional funds received from County over the amount that was to be refunded.		

**EFFECT ON THE FILING:** There is no effect on the filing because both accounts are included in their entirety.

**AUDIT FINDING NO. 9**

**SUBJECT: TEMPORARY CASH INVESTMENTS**

**AUDIT ANALYSIS:** Cash balances included in the working capital allowance for the period ended December

<u>Account</u>	<u>Description</u>	<u>Amount</u>	
		<u>Dec-06</u>	<u>13-Month Avg.</u>
1002	Escrow A/C - Republic Bank	39,403.24	39,161.51
1003	Money Market A/C – Republic Bank	4,537.07	28,042.83
1005	Wachovia – SSI Escrow A/C	107,729.31	60,723.63
1006	KWRU AWT Escrow Account	1,520.30	40,336.56
	TOTAL	<u>153,189.92</u>	<u>168,264.53</u>

The Commission has always excluded interest earning temporary cash investments from the working capital because they already earn a return and to add a return on rate base is duplicating that.

**EFFECT ON LEDGER:** This finding does not affect the ledger.

**EFFECT ON THE FILING:** The 13-month average Working Capital in rate base should be reduced by \$168,264.53.

**AUDIT FINDING NO. 10**

**SUBJECT: MONROE COUNTY DETENTION CENTER INCOME**

**AUDIT ANALYSIS:** The utility recorded \$19,575 in the general ledger account number 80271 – MCDC Income, for income received from the Monroe County Detention Center. This relates to income for cleaning of their lift stations. This was not included in the Operating Revenues in the Filing Schedule B-2 and B-4.

**EFFECT ON GENERAL LEDGER:** None.

**EFFECT ON FILING:** Revenues should be increased by \$19,575.

**AUDIT FINDING NO. 11**

**SUBJECT: TRAVEL EXPENSES**

**AUDIT ANALYSIS:** The utility has recorded in Account 775- Miscellaneous Expenses various travel expenses for Mr. Smith.

A total of \$6,000 was recorded for lodging expenses paid to Green Fairways. These were recorded at \$1,000 per month for the months of January, March, May, July, September and November of 2006. Also recorded in Account 775 are 4 invoices for Mr. Smith's rental car and air plane fuel. These were recorded in March 2006 for \$2,690.60 and \$1,884.53, in May 2006 for \$3,577.65 and in November 2006 for \$2,622.74. In addition to these invoices two invoices for \$1,258.56 in January 2006 and \$1,071.52 in November 2006 were recorded payable to Island City Flying Service. These relate to payment of aviation fuel.

Approximately \$19,105.60 were recorded in Account 775 for Mr. Smith's travel expenses.

The utility explained that Mr. Smith's cost of travel is allocated on alternating months between the utility and Key West Golf Club (KWGC). Mr. Smith has a house on Stock Island.

These expenses should be reviewed by the analyst for a determination on whether these are reasonable utility expenses.

**EFFECT ON THE GENERAL LEDGER:** None.

**EFFECT ON THE FILING:** If the Commission decides that the utility should not bear the burden of the owner's travel, operating expenses should be reduced by \$19,105.60.

**AUDIT FINDING NO. 12**

**SUBJECT: OFFICE EXPENSE**

**AUDIT ANALYSIS:** The utility has recorded a copier fee in Account 720 – Materials and Supplies for a total of \$5,378.40. This was paid to Weiler Engineering in July 2006. This payment represents a monthly fee of \$224.10 for 24 months for a copier in the plant trailer. The copier charges represent one half of the actual charges because Keys Environmental, Inc. pays the other half of the copying fee at the trailer. The amount for a year would be \$2,689.20.

The utility has also recorded in this account an allocation charge from Key West Golf Club of \$100 per month for copying and supplies fees for the accounting office. The total in the test year is \$1,200. This was reviewed and the percentage allocated to the utility appeared reasonable based on Key West Golf Club supplies account.

**EFFECT ON THE GENERAL LEDGER:** The adjustment for the out of period amount is:

Prepaid Account	\$2,689.20
Account 720	\$2,689.20

**EFFECT ON THE FILING:** The operating expenses should be reduced by \$2,689.20 for out of period charges.



**AUDIT FINDING NO. 13**

**SUBJECT: NON-RECURRING CHARGES**

**AUDIT ANALYSIS:** The utility recorded in Account 711- Sludge Hauling, an expense to haul the sludge for \$11,411.82. This amount is for a total of 66.62 tons. The other four charges in this account were for lower amounts. The utility explained that due to blower and diffusers problems at the plant and also to a high solids inventory, the utility had to haul an inordinate amount of solids to continue to operate within the DEP requirements. This charge is probably not recurring and may need to be amortized over five years. The yearly amortization would be \$2,282.36. The deferred amount would be \$9,129.46.

The contract with Keys Environmental Inc. explains that the additional charge to pump the sewage is 11 cents per gallon and the additional charge to haul the sewage is 5 cents per gallon. This also explains that the charge for pumping, hauling and discharging of any raw sewage shall be 05 cents per gallon. These charges should be reviewed by the Tallahassee engineer.

The utility has recorded \$25,000 in Account 760 – Advertising Expenses, for charges to William Barry for public relations. The utility explained that these charges arose because concerns were raised by Stock Island property owners at a Monroe County Commission meeting. The county stated that the utility should inform the future users of the wastewater system and educate them about the process. The utility hired William Barry to handle public relations, create public awareness and answer any media and county questions. This charge is probably not recurring and may need to be amortized over five years. The yearly amortization would be \$5,000. The deferred amount would be \$20,000.

The utility has recorded in Account 736 - Contractual Services Other, an expense to strip and wax the linoleum floor at the office trailer. The amount recorded was \$1,290 paid to The Carpet Lady. This charge may not be recurring and may need to be amortized over five years. The yearly amortization would be \$258. The deferred amount would be \$1,032.

**EFFECT ON THE GENERAL LEDGER:** If the Commission decides to amortize these amounts, the following entry is needed:

Deferred Expenses	\$30,161.46
Account 711	\$ 9,129.46
Account 760	\$20,000.00
Account 736	\$ 1,032.00

**EFFECT ON THE FILING:** If the Commission decides to amortize these amounts, the operating expenses should be reduced by \$30,161.46.

**AUDIT FINDING NO. 14**

**SUBJECT: TELEPHONE CHARGES**

**AUDIT ANALYSIS:** The utility has included \$13,813.52 in Account 775 – Miscellaneous, for telephone charges. The account includes \$6,305,80 of charges payable to Bellsouth for the line in the accounting office of Key West Golf Club designated for sewer customer service calls, and a line in the plant trailer. A few other charges were tested and it appears that most of the other charges recorded are for telephone purchases and cellular charges for Doug Carter, Bart Smith and Alexander Smith. Doug Carter’s salary is allocated to the utility through the management fee, therefore, his phone charges should not be totally charged to the utility. Approximately 30% of his salary was allocated to the utility. Based on our sample we could not determine the total amount of the cellular charges for Doug Carter. The other individuals do not work for the utility.

**EFFECT ON THE GENERAL LEDGER:**

The \$7,507.72 of telephone expenses that are not directly related to the utility business should not be allowed by the Commission.

Account 426 Misc Non-utility Expense	\$7,507.72	
Account 775		\$7,507.72

**EFFECT ON THE FILING:** The \$7,507.72 of telephone expenses that are not directly related to the utility business should not be allowed by the Commission.

**AUDIT FINDING NO. 15**

**SUBJECT: INSURANCE – GENERAL LIABILITY**

**AUDIT ANALYSIS:** The utility has recorded finance charges in Account 757 - Insurance. Finance charges of \$601.35 in the payments to Imperial Premium Finance Inc. and \$800.11 in the payments to First Insurance Funding Corp were recorded. The company prorated the payments and established a prepaid insurance account in order to determine the finance charges expensed for 2006. The total finance charges included in Account 757 for 2006 total \$700.73

Commission policy has been to reduce operating expenses for interest incurred due to late payments, on the grounds that the expense is avoidable and that the Commission should not condone the incurrence of unnecessary expenses. The Commission has stated that it is inappropriate to require customers to pay for an avoidable cost which should be borne by the utility owners. (Order No. 21137, Docket No. 871262-WS, issued April 27, 1989)

**EFFECT ON GENERAL LEDGER:** Operating expenses should be reduced for the finance charges.

Account 426 Misc Non-utility Expense	\$700.73
Account 757	\$700.73

**EFFECT ON FILING:** Operating Expenses should be reduced by \$700.73.

**AUDIT FINDING NO. 16**

**SUBJECT: POLITICAL EXPENSES**

**AUDIT ANALYSIS:** The utility has recorded \$117.82 of expenses related to a Charlie Crist fund raiser. These were recorded in Account 720 – Materials and Supplies for \$55.03 and Account 775 – Miscellaneous for \$62.79.

The utility also recorded \$335 for a Charlie Crist party staffing, \$250 for a Charlie Crist donation and \$500 for the Citizens for Charlie Crist. These total \$1,085 and were recorded in Account 760 - Advertising.

Commission Rule 25-30.115(1), Florida Administrative Code, requires water and wastewater utilities to maintain accounts and records in conformity with the 1996 National Association of Regulatory Utility Commissioners ( NARUC) Uniform System of Accounts (USOA) adopted by the National Association of Regulatory Utility Commissioners. The USOA prescribes that "expenditures for the purpose of influencing public opinion with respect to the election or appointment of public officials..." should be charged to Account 426, Miscellaneous Non-Utility Expense, a below-the-line account.

**EFFECT ON GENERAL LEDGER:**

Operating expenses should be reduced for the political expenses.

Account 426 Misc Non-utility Expense	\$1,202.82
Account 720	\$ 55.03
Account 775	\$ 62.79
Account 760	\$1,085.00

**EFFECT ON FILING:** Operating Expenses should be reduced by \$1,202.82.

**AUDIT FINDING NO. 17**

**SUBJECT: ALLOCATION FROM KEY WEST GOLF CLUB**

**AUDIT ANALYSIS:** The utility has recorded in Account 736 – Contractual Services Other, a monthly \$200 charge allocated from Key West Golf Club for use of a golf cart for utilities operations. The invoiced amount of the golf cart, paid by Key West Golf Club to Yamaha, for the month of March 2006 is \$6,034.33 for 85 golf carts. The invoiced amount for one golf cart for this month is \$71. The \$71 for the twelve months is \$852. This is \$1,548 less than the total \$2,400 that is being allocated to Account 736.

**EFFECT ON THE GENERAL LEDGER:** The following entry should be made:

Affiliate Receivable	\$1,548
Account 736	\$1,548

**EFFECT ON THE FILING:** Operating Expenses should be reduced by \$1,548.

**AUDIT FINDING NO. 18**

**SUBJECT: PERMIT FEES**

**AUDIT ANALYSIS:** The utility has recorded \$9,000 payable to the Florida Department of Environmental Protection in Account 408 – Licenses and Permits. This amount includes \$3,750 for preliminary design review required for the modification to AWT, \$2,250 for the renewal of the class V injection wells and \$3,000 for the renewal application review.

The utility explained that the AWT review fees are a one time charge, as advised by the engineering company, and that the permit renewals are valid for 5 years.

The permit renewals of \$2,250 and \$3,000 should be amortized over 5 years and the account should be reduced by \$1,800 and \$2,400, respectively.

The Tallahassee engineer should determine if the \$3,750 permit for the design review should be capitalized. If so, depreciation at 5.56% results in a test year expense of \$104.25 using ½ year convention. This was recorded in November 2006.

**EFFECT ON GENERAL LEDGER:** The following entries should be made:

Deferred Permits	\$4,200	
Account 408		\$4,200
Account 380 – Treat & Disp.	\$3,750	
Account 408		\$3,750
Depreciation Exp	\$ 104.25	
Accumulated Depr.		\$ 104.25

**EFFECT ON FILING:** Average Plant in Service should be increased by \$576.92 . Average Accumulated Depreciation should be increased by \$52.12. Depreciation expense should be increased by \$104.25. Taxes Other Than Income should be reduced by \$7,950.

**AUDIT FINDING NO. 19**

**SUBJECT: RENTAL OF BEACHCLEANER**

**AUDIT ANALYSIS:** The utility has included in account 742 - Rental of Equipment, charges for the rental of a Cherrington Model 3000 beachcleaner. This equipment is used to clean the sludge beds. The total charges paid in account 742 were \$11,825 to Cherrington Enterprises, Inc. The agreement with the vendor shows that 100% of the payment was to be applied to the purchase price of \$33,900, which had to occur by December 31, 2006. The utility purchased the equipment on December 29, 2006 for an additional \$24,617.50 and was recorded in Plant in Service. These payments (\$11,825 + \$24,617.50) total \$36,442.50. This equates to the purchase price of \$33,900 plus tax of 7.5% or \$36,442.50

The depreciation rate for transportation equipment is 6 years or 16.67%. The depreciation expense for 2006 is calculated using ½ year convention..

**EFFECT ON GENERAL LEDGER:** The following entry should be made:

Plant in Service	\$11,825.00	
Depreciation Expense	\$ 985.61	
Accumulated Depreciation		\$ 985.61
Account 742		\$11,825.00

**EFFECT ON FILING:** Average Plant in Service should be increased by \$909.62. Average Accumulated Depreciation should be increased by \$492.78. Depreciation expense should be increased by \$985.61. Operating Expenses should be decreased by \$11,825.

#### **IV. EXHIBITS**



Schedule of Wastewater Rate Base

Florida Public Service Commission

Company: KW Resort Utilities Corp.  
 Docket No.: 070293-SU  
 Schedule Year Ended: December 31, 2006  
 Interim [ ] Final [X]  
 Historic [X] Projected [ ]

Schedule: A-2  
 Page 1 of 1  
 Preparer: CJNW

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) Description	(2) Balance Per Books	(3) A-3 Utility Adjustments	(4) Adjusted Utility Balance	(5) Supporting Schedule(s)
1	Utility Plant In Service	\$ 9,371,002	\$ 1,139,707 (A)	\$ 10,510,709	A-6
2	Utility Land & Land Rights	222,745	152,255 (B)	375,000	A-6
3	Less: Non-Used & Useful Plant			-	A-7
4	Construction Work in Progress	265,413	(265,413) (C)	-	A-18
5	Less: Accumulated Depreciation	(2,740,042)	(63,368) (D)	(2,803,410)	A-10
6	Less: CIAC	(4,856,429)	(707,000) (E)	(5,563,429)	A-12
7	Accumulated Amortization of CIAC	686,844	39,309 (F)	726,153	A-14
8	Advances for Construction	(2,777,630)		(2,777,630)	A-19
8	Acquisition Adjustments				-
9	Accum. Amort. of Acq. Adjustments				-
10	Working Capital Allowance	-	496,846 (G)	496,846	A-17
11	Total Rate Base	\$ 171,903	\$ 792,336	\$ 964,239	

Schedule of Wastewater Net Operating Income

Florida Public Service Commission

Company: KW Resort Utilities Corp.  
 Docket No.: 070293-SU  
 Schedule Year Ended: December 31, 2006  
 Interim [ ] Final [X]  
 Historic [X] Projected [ ]

Schedule: B-2  
 Page 1 of 1  
 Preparer: CJNW

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) Description	(2) Balance Per Books	(3) Utility Test Year Adjustments	(4) Utility Adjusted Test Year	(5) Requested Revenue Adjustment	(6) Requested Annual Revenues	(7) Supporting Schedule(s)
1	OPERATING REVENUES	\$ 1,012,695	\$ 33,619 (A)	\$ 1,046,314	\$ 601,684 (F)	\$ 1,647,998	B-4, E-13
2	Operation & Maintenance	1,017,156	222,154 (B)	1,239,310		1,239,310	B-6, B-3
3	Depreciation, net of CIAC Amort.	181,844	24,059 (C)	205,903		205,903	B-14, B-3
4	Amortization (Deferred expenses (1))	5,297	(968) (D)	4,329		4,329	
5	Taxes Other Than Income	79,594	10,886 (E)	90,480	27,076 (G)	117,556	B-15, B-3
6	Provision for Income Taxes	-	-	-	-	-	C-1, B-3
7	OPERATING EXPENSES	<u>1,283,891</u>	<u>256,131</u>	<u>1,540,022</u>	<u>27,076</u>	<u>1,567,098</u>	
8	NET OPERATING INCOME	<u>\$ (271,196)</u>	<u>\$ (222,512)</u>	<u>\$ (493,708)</u>	<u>\$ 574,608</u>	<u>\$ 80,900</u>	
9	RATE BASE	<u>\$ 171,903</u>		<u>\$ 964,239</u>		<u>\$ 964,239</u>	
10	RATE OF RETURN	<u>-</u> %		<u>-</u> %		<u>8.39</u> %	

Note (1): The Company is amortizing deferred permitting costs (\$4,329) and deferred loan closing costs (\$968) in Account 407 - Amortization.

Schedule of Requested Cost of Capital (Final Rates)  
 Beginning and End of Year Average

Florida Public Service Commission

Company: KW Resort Utilities Corp.  
 Docket No.: 070293-SU  
 Schedule Year Ended: December 31, 2006  
 Interim [ ] Final [X]  
 Historic [X] Projected [ ]

Schedule: D-1  
 Page 1 of 1  
 Preparer: CJNW

Subsidiary [X] or Consolidated [ ]

Explanation: Provide a schedule which calculates the requested Cost of Capital on a 13-month average basis. If a year-end basis is used, submit an additional schedule reflecting year-end calculations.

Line No.	(1) Total Capital	(2) Ratio	(3) Cost Rate	(4) Weighted Cost
1	Long-Term Debt \$ 671,737	69.66 %	7.17 %	4.99 %
2	Short-Term Debt			
3	Preferred Stock			
4	Customer Deposits 39,746	4.12	6.00	0.25
5	Common Equity 252,756	26.22	12.01	3.15
6	Tax Credits - Zero Cost			
7	Accumulated Deferred Income Tax			
8	Other (Explain)			
9	Total \$ 964,239	100.00 %		8.39 %