



# Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD

TALLAHASSEE, FLORIDA 32399-0850 10 DEC 15 PM 2:20

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

COMMISSION  
CLERK

**DATE:** December 15, 2010

**TO:** Jay Donoho, Regulatory Analyst II, Division of Economic Regulation

**FROM:** Clarence Prestwood, Chief of Auditing, Office of Auditing and Performance Analysis *CP*

**RE:** Docket No.: 100126-WS  
 Company Name: C.F.A.T. H2O, Inc.  
 Company Code: WS719  
 Audit Purpose: Rate Case  
 Audit Control No: 10-274-2-1

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, it should send a response to the Office of Commission Clerk. There were no confidential work papers associated with this audit.

CP/ip  
 Attachment: Audit Report

cc: (With Attachment)  
 Office of Auditing and Performance Analysis (Mailhot, Prestwood, File Folder)  
 Office of Commission Clerk  
 Office of the General Counsel

(Without Attachment)  
 Office of Auditing and Performance Analysis (Harvey, Tampa District Office, Miami District Office, Tallahassee District Office)

**COM** \_\_\_\_\_  
**APA** \_\_\_\_\_  
**ECR** \_\_\_\_\_  
**GCL** \_\_\_\_\_  
**RAD** \_\_\_\_\_  
**SSC** \_\_\_\_\_  
**ADM** \_\_\_\_\_  
**OPC** \_\_\_\_\_  
**CLK**   1  

DOCUMENT NUMBER DATE

09956 DEC 15 2010

FPSC-COMMISSION CLERK

State of Florida



**Public Service Commission**

Office of Auditing and Performance Analysis  
Bureau of Auditing  
Tampa District Office

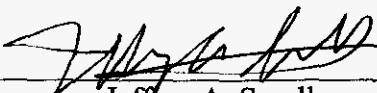
**Auditor's Report**


C.F.A.T. H2O, Inc.  
File and Suspend Rate Case Audit

Twelve Month Period Ended December 31, 2009

Docket No. 100126-WU  
Audit Control No. 10-274-2-1  
December 8, 2010

  
Intesar Terkawi  
Audit Manager

  
Jeffery A. Small  
Audit Staff

  
Linda Hill-Slaughter  
Reviewer

DOCUMENT NUMBER-DATE

09956 DEC 15 2010

FPSC-COMMISSION CLERK

## Table of Contents

	Page
Purpose .....	1
Objectives and Procedures.....	2
 <b>Audit Findings</b>	
1 Adjustment to Utility Plant in Service and Accumulated Depreciation .....	6
2 Adjustment to Contributions in Aid of Construction (CIAC) and Accumulated <i>Amortization of CIAC</i> .....	8
3 Adjustment to Capital Structure.....	11
4 Adjustment to Direct Operation and Maintenance Expense.....	12
5 Adjustment to Allocated Operation and Maintenance Expense .....	13
6 Adjustment to Taxes Other Than Income Expense .....	15
 <b>Exhibits</b>	
1 Schedule of Water Rate Base.....	16
2 Schedule of Water Net Operating Income .....	17
3 Schedule of Requested Cost of Capital.....	18

## Purpose

To: Florida Public Service Commission

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 September 28, 2010. We have applied these procedures to the attached schedules which were prepared by C.F.A.T. H2O, Inc. in support of its filing for rate relief in Docket No. 100126-WU.

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

## Objectives and Procedures

### **General**

#### Utility Information

C.F.A.T. H2O, Inc. (CFAT) is a Class C utility that provides water and wastewater services to approximately 221 residential and commercial customers in Marion County, Florida. CFAT is requesting a rate increase for its water operations only in this filing. The Utility is managed by Mr. Charles deMenzes, one of two shareholders with equal ownership interest in CFAT. Additionally, Mr. deMenzes owns and manages M.I.R.A. International, Inc. (MIRA) which provides payroll services, general maintenance and office services for CFAT and three other utilities under the Florida Public Service Commission's jurisdiction.

#### Definitions

The term "Utility" used within this report refers to C.F.A.T. H2O, Inc. The term "Company" refers to M.I.R.A. International, Inc., the Utility's "parent" or Service Company.

#### Utility Books and Records

**Objective:** Our objective was to determine that the Utility maintains its accounts and records in conformity with the National Association of Regulatory Utility Commissioners' (NARUC) Uniform System of Accounts (USOA).

**Procedure:** We reviewed the Utility's accounting system and determined that it is in substantial compliance with the NARUC USOA.

### **Rate Base**

#### Utility Plant in Service (UPIS)

**Objectives:** Our objectives were to; 1) Determine that property exists and is owned by the Utility and that additions to UPIS are authentic, recorded at original cost, and properly classified in compliance with Commission rules and the NARUC USOA, 2) Verify that the proper retirements of UPIS were made when a replacement item was put in service.

**Procedures:** We determined the UPIS balance that was established in Docket No. 931080-WS.<sup>1</sup> We reviewed UPIS additions for the period January 1, 1994, through December 31, 2009, to determine the UPIS balance for this proceeding. We ensured that retirements to UPIS were made when a capital item was removed or replaced. We toured the water utility plant site to observe whether asset additions were completed and to ascertain if asset retirements were needed. Audit Finding 1 discusses our findings and recommended adjustments to UPIS.

---

<sup>1</sup> See Order No. PSC-94-0701-PAA-WS, issued June 8, 1994, Docket No.931080-WS, In Re: Application For Transfer of Certificate Nos. 552-W and 481-S From Resolution Trust Corporation to C.F.A.T. H2O, Inc. in Marion County.

## Land

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

**Procedure:** We verified that there has been no change to the Utility's land balance or ownership since its last rate case proceeding in Docket No. 931080-WS.

## Contributions in Aid of Construction (CIAC)

**Objectives:** Our objectives were to; 1) Determine that additions to CIAC are properly recorded in compliance with Commission rules and the NARUC USOA, 2) Verify that donated property is properly accounted for and recorded as CIAC.

**Procedures:** We determined the Utility's CIAC balance that was established in Docket No. 931080-WS. We reviewed additions to CIAC for the period January 1, 1994, through December 31, 2009, to determine the Utility's CIAC balance for this rate case proceeding. We searched the Utility's 2005 through 2009 Federal Income Tax returns for unrecorded cash and property contributions. Audit Finding 2 discusses our findings and recommended adjustments to CIAC.

## Accumulated Depreciation

**Objectives:** Our objectives were to; 1) Determine that accruals to accumulated depreciation are properly recorded in compliance with Commission rules and the NARUC USOA, 2) Verify that depreciation expense accruals are calculated using the Commission's authorized rates, 3) Verify that retirements are properly recorded.

**Procedures:** We determined the Utility's accumulated depreciation balance that was established in Docket No. 931080-WS. We verified the accumulated depreciation accruals for the period January 1, 1994, through December 31, 2009, to determine the Utility's accumulated depreciation balance for this proceeding. We ensured that retirements to accumulated depreciation were made when a capital item was removed or replaced. Audit Finding 1 discusses our findings and recommended adjustments for accumulated depreciation.

## Accumulated Amortization of CIAC

**Objective:** Our objective was to determine that accruals to accumulated amortization of CIAC are properly recorded in compliance with Commission rules.

**Procedures:** We determined the Utility's accumulated amortization of CIAC balance that was established in Docket No. 931080-WS. We verified accumulated amortization of CIAC accruals for the period January 1, 1994, through December 31, 2009, to determine the Utility's accumulated amortization of CIAC balance for this proceeding. Audit Finding 2 discusses our findings and recommended adjustments for accumulated amortization of CIAC.

## Working Capital

**Objective:** Our objective was to determine that the Utility's working capital balance is properly calculated in compliance with Commission rules.

**Procedure:** We verified the Utility's calculation of the working capital balance as of December 31, 2009, using one-eighth of operation and maintenance expense as required by Commission Rule 30.433 (2), F.A.C.

## **Net Operating Income**

### Operating Revenue

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

**Procedures:** We verified the Utility's revenues for the 12-month period ending December 31, 2009, by tracing them to the Utility's general ledger and billing register system. We verified that the Utility is using the correct tariff rates established by the Commission by recalculating a sample of customer bills in the test year period.

### Operation and Maintenance Expense

**Objective:** Our objective was to determine that operation and maintenance expenses are properly recorded in compliance with NARUC USOA and Commission rules and are representative of ongoing utility operations.

**Procedures:** We verified operation and maintenance expenses for the 12-month period ending December 31, 2009, by tracing a sample of invoices to its original source documentation. We reviewed invoices for proper amount, period, classification, NARUC account and recurring nature. We reviewed related party allocations from MIRA for payroll, general maintenance and office services. We determined the proper allocation of expenses between CFAT's related party and its water and wastewater operations. Audit Findings 4 and 5 discuss our findings and recommended adjustments to operation and maintenance expense for the 12-month period ending December 31, 2009.

### Depreciation and CIAC Amortization Expense

**Objectives:** Our objectives were to determine that depreciation and CIAC amortization expenses are properly recorded in compliance with Commission rules and that they accurately represent the depreciation of UPIS and the amortization of CIAC from ongoing utility operations.

**Procedure:** We verified the calculation of depreciation expense and CIAC amortization expense balances. Audit Findings 1 and 2 discuss our findings and recommended adjustments to

depreciation expense and CIAC amortization expense balances for the 12-month period ending December 31, 2009.

#### Taxes Other than Income (TOTI)

**Objective:** Our objective was to determine that TOTI expenses are properly recorded in compliance with Commission rules and are reasonable and prudent for ongoing utility operations.

**Procedures:** We verified TOTI expenses for the 12-month period ending December 31, 2009. We traced the invoiced property taxes to the original source documentation. We reviewed related party allocations from MIRA for payroll taxes. We determined the proper allocation of tax expense between CFAT's related party operations and its water and wastewater operations. We audited the 2009 regulatory assessment fee returns and no exceptions were noted. Audit Finding 6 discusses our findings and recommended adjustments to TOTI expense for the 12-month period ending December 31, 2009.

#### **Capital Structure**

**Objective:** Our objective was to determine that 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 requirements.

**Procedure:** We determined that the Utility's capital structure is comprised of long term debt, customer deposits and shareholders equity. Audit Finding 3 discusses our findings and recommended adjustments to the Utility's capital structure.



## **Audit Finding 1**

### **Subject: Adjustment to Utility Plant in Service and Accumulated Depreciation**

**Audit Analysis:** The Utility's average water utility plant in service and accumulated depreciation balances are overstated by \$25,880 and \$24,247, respectively, for the test year 2009.

The following items represent the explanation of each account adjusted:

- 1) Account 301 – Organization, should be reduced by \$2,500 as the Utility did not adjust the balance of the account per Order No. PSC-94-0701-FOF-WS. Our adjustment removes all UPIS and accumulated depreciation balances reflected in the Utility's filing.
- 2) Account 302 – Franchises, should be reduced by \$1,062, as the Utility did not adjust the balance of the account per Order No. PSC-94-0701-FOF-WS. Our adjustment removes all UPIS and accumulated depreciation balances reflected in the Utility's filing.
- 3) Account 310 – Power Generation Equipment, should be reduced by \$11,672. The adjustment removes a generator and an electric service panel totaling \$11,320 that was transferred to wastewater plant as of December 31, 2006. It also removes a \$352 invoice for preventive maintenance on the generator that should have been recorded as a recurring operation and maintenance expense in 2008.
- 4) Account 330 – Distribution Reservoirs and Standpipes should be reduced by \$1,273. This adjustment removes additions to UPIS in 2008 that are not supported by any utility documentation.
- 5) Account 334 – Meter & Meter Installation should be reduced by \$9,373. We determined that the Utility had completed a major asset replacement program that replaced or converted substantially all of its manual read water meters with new automated read water meters. We also determined that there was no corresponding retirement recorded to Acct. No. 334 by the Utility for the replaced water meters. The NARUC USOA<sup>2</sup> and Commission Rule 25-30.115, F.A.C., by adoption require retirements of plant assets when they are replaced or removed from service. We retired \$9,373 from water UPIS as of December 31, 2005, to remove an estimated amount for the water meters that were replaced and to correct the general ledger balance. Our estimated adjustment equaled the corresponding accumulated depreciation balance for Acct. No. 334, as of December 31, 2005. Our approach followed the NARUC USOA accounting instruction cited above that requires equal entries to plant and accumulated depreciation accounts when a plant asset is retired.

The above amounts should be removed along with the cumulative effect on the corresponding accumulated depreciation and depreciation expense balances. See our calculations that follow:

---

<sup>2</sup> See NARUC, Class C, Accounting Instruction No. 5.

NARUC		UPIS Adjustment		Rule	Accumulated Depreciation Adjustment			
Acct. No.	Description	@12/31/2009	Avg. 2009	Rate	@12/31/2008	Dep. Exp.	@12/31/2009	Avg. 2009
301	Organization	(\$2,500)	(\$2,500)		(\$2,500)		(\$2,500)	(\$2,500)
302	Franchises	(\$1,062)	(\$1,062)	3.39%	(\$526)	(\$36)	(\$562)	(\$544)
310	Pumping Equipment	(\$11,320)	(\$11,320)	6.67%	(\$6,556)	(\$755)	(\$7,311)	(\$6,935)
		(352)	(352)	6.67%	(5)	(23)	(27)	(14)
		(\$11,672)	(\$11,672)		(\$6,561)	(\$778)	(\$7,338)	(\$6,949)
330	Dist. Reservoirs & Standpipes	(\$1,273)	(\$1,273)	3.33%	(\$131)	(\$42)	(\$173)	(\$152)
334	Meters	(\$9,373)	(\$9,373)	5.88%	(\$13,427)	(\$1,351)	(\$14,778)	(\$14,102)
Total UPIS Adjustment			<u>(\$25,880)</u>		<u>(\$23,145)</u>		<u>(\$25,351)</u>	<u>(\$24,247)</u>
Total Depreciation Expense Adjustment								<u>(\$2,207)</u>

**Effect on the General Ledger:** The following journal entries should be made to correct the Utility's general ledger as of December 31, 2009.

Utility Acct. No.	NARUC Acct. No.	Description	Debit	Credit
101301	301	Organization		\$2,500
108001	108	Acc. Dep. - Organization	\$2,500	
101302	302	Franchises		\$1,062
108001	108	Acc. Dep. - Franchises	\$526	
101310	310	Power Generation Equipment		\$11,672
108001	108	Acc. Dep. - Power Gen. Equip.	\$7,338	
101330	330	Dist. Reservoirs & Standpipes		\$1,273
108001	108	Acc. Dep. - Reservoirs & Standpipes	\$173	
101334	334	Meter & Meter Installations		\$9,373
108001	108	Acc. Dep. - Meter & Meter Installations	\$14,778	
800403	403	Dep. Exp. Franchises		\$36
800403	403	Dep. Exp. Power Generation Equip		\$778
800403	403	Dep. Exp. Dist. Reservoirs & Standpipes		\$173
800403	403	Dep. Exp. Meter & Meter Installations		\$1,351
315001	215	Retained Earnings	\$2,903	

**Effect on the Filing:** The Utility's average water utility plant in service and accumulated depreciation balances should be reduced by \$25,880 and \$24,247, respectively, for the test year 2009. Additionally, the Utility's test year depreciation expense should be reduced by \$2,207 for the 12-month period ending December 31, 2009.

## Audit Finding 2

### Subject: Adjustment to Contributions in Aid of Construction (CIAC) and Accumulated Amortization of CIAC

**Audit Analysis:** The Utility's filing reflects CIAC and accumulated amortization of CIAC balances of \$114,421 and \$57,849, respectively, as of December 31, 2009.

Order No. PSC-94-0701-FOF-WS, established CIAC and accumulated amortization of CIAC balances of \$86,774 and \$11,653, respectively, as of December 31, 1993. We determined that the Utility did not adjust its CIAC and accumulated amortization of CIAC balances as required in the above mentioned Order. The Utility calculated an annual composite CIAC amortization rate based on its depreciation expense for plant in service to amortize its CIAC balances.

The Utility's CIAC and accumulated amortization of CIAC balances are understated and overstated by \$10,512, and \$1,859, respectively, as of December 31, 2009. The CIAC amortization expense is overstated by \$2,207 for the year ended December 31, 2009. See our calculations on the two schedules that follow.

**Effect on the General Ledger:** The following journal entries should be made to correct the Utility's general ledger.

Acct. No.	Description	Debit	Credit
271	Contributions in Aid of Construction (CIAC)		\$10,512
272	Accumulated Amortization of CIAC		\$1,859
408	CIAC Amortization Expense		\$2,207
215	Retained Earnings	\$14,578	

**Effect on the Filing:** The Utility's average CIAC and average accumulated amortization of CIAC balances should be increased and decreased by \$10,512, and \$756, respectively, as of December 31, 2009. The Utility's test year CIAC amortization expense should be reduced by \$2,207 for the 12-month period ending December 31, 2009.

CIAC	@12/31/2008	Amort. Expense	@12/31/2009	Average
Per Audit	\$124,933	\$0	\$124,933	\$124,933
Per Filing	<u>114,421</u>	<u>0</u>	<u>114,421</u>	<u>114,421</u>
Adjustment	\$10,512	\$0	\$10,512	\$10,512

Accumulated Amortization of CIAC	@12/31/2008	Test Year Amort. Expense	@12/31/2009	Average
Per Audit	\$53,082	\$2,908	\$55,990	\$54,536
Per Filing	<u>52,734</u>	<u>5,115</u>	<u>57,849</u>	<u>55,292</u>
Adjustment	\$348	(\$2,207)	(\$1,859)	(\$756)

**Audit Finding 2**  
**Schedule 1 of 2**

CIAC Acct. No.	Per Order @ 12/31/1993	Audit Balance Additions @ 12/31/1994	Audit Balance Additions @ 12/31/1995	Audit Balance Additions @ 12/31/1996	Audit Balance Additions @ 12/31/1997	Audit Balance Additions @ 12/31/1998
303	\$ 19,500	\$ -	\$ 19,500	\$ -	\$ 19,500	\$ -
311	4,370	-	4,370	-	4,370	-
330	13,000	-	13,000	-	13,000	-
331	38,589	-	38,589	-	38,589	18,539
333	11,315	-	11,315	-	11,315	-
334	-	-	-	-	-	6,899
<b>Total</b>	<b>\$ 86,774</b>	<b>\$ -</b>	<b>\$ 86,774</b>	<b>\$ -</b>	<b>\$ 86,774</b>	<b>\$ 25,438</b>

Acct. No.	Audit Balance Additions @ 12/31/1999	Audit Balance Additions @ 12/31/2000	Audit Balance Additions @ 12/31/2001	Audit Balance Additions @ 12/31/2002	Audit Balance Additions @ 12/31/2003	Audit Balance Additions
303	\$ -	\$ 19,500	\$ -	\$ 19,500	\$ -	\$ 19,500
311	-	4,370	-	4,370	-	4,370
330	-	13,000	-	13,000	-	13,000
331	12,086	69,214	-	69,214	-	69,214
333	-	11,315	-	11,315	-	11,315
334	-	6,899	-	6,899	-	6,899
	<b>\$ 12,086</b>	<b>\$ 124,298</b>	<b>\$ -</b>	<b>\$ 124,298</b>	<b>\$ -</b>	<b>\$ 124,298</b>

Acct. No.	Audit Balance @ 12/31/2004	Audit Balance Additions @ 12/31/2005	Audit Balance Additions @ 12/31/2006	Audit Balance Additions @ 12/31/2007	Audit Balance Additions @ 12/31/2008	Audit Balance Additions @ 12/31/2009
303	\$ 19,500	\$ -	\$ 19,500	\$ -	\$ 19,500	\$ -
311	4,370	-	4,370	-	4,370	-
330	13,000	-	13,000	-	13,000	-
331	69,214	-	69,214	-	69,214	635
333	11,315	-	11,315	-	11,315	-
334	6,899	-	6,899	-	6,899	-
	<b>\$ 124,298</b>	<b>\$ -</b>	<b>\$ 124,298</b>	<b>\$ -</b>	<b>\$ 124,933</b>	<b>\$ -</b>

Per Filing \$114,421  
Average and Year End Adjustment \$ 10,512

**Audit Finding 2**  
**Schedule 2 of 2**

Amort. of CIAC	Per Order @	Audit		Audit		Audit		Audit		Audit		Audit
Acct. No.	Amort. Rate	12/31/1993	Accruals	Balance @ 12/31/1994	Accruals	Balance @ 12/31/1995	Accruals	Balance @ 12/31/1996	Accruals	Balance @ 12/31/1997	Accruals	Balance @ 12/31/1998
311	6.67%	\$ 757	\$ 291	\$ 1,048	\$ 291	\$ 1,339	\$ 291	\$ 1,630	\$ 291	\$ 1,921	\$ 291	\$ 2,212
330	3.33%	2,252	433	2,685	433	3,118	433	3,551	433	3,984	433	4,417
331	2.50%	6,684	965	7,649	965	8,614	965	9,579	965	10,544	1,196	11,740
333	2.86%	1,960	323	2,283	323	2,606	323	2,929	323	3,252	323	3,575
334	5.88%	-	-	-	-	-	-	-	-	-	203	203
		\$ 11,653	\$ 2,012	\$ 13,665	\$ 2,012	\$ 15,677	\$ 2,012	\$ 17,689	\$ 2,012	\$ 19,701	\$ 2,446	\$ 22,147

Amort. of CIAC	Amort. Rate	Accruals	Audit		Audit		Audit		Audit		Audit	
Acct. No.	Amort. Rate	Accruals	Balance @ 12/31/1999	Accruals	Balance @ 12/31/2000	Accruals	Balance @ 12/31/2001	Accruals	Balance @ 12/31/2002	Accruals	Balance @ 12/31/2003	Accruals
311	6.67%	\$ 291	\$ 2,503	\$ 291	\$ 2,794	\$ 291	\$ 3,085	\$ 291	\$ 3,376	\$ 291	\$ 3,667	\$ 291
330	3.33%	433	4,850	433	5,283	433	5,716	433	6,149	433	6,582	433
331	2.50%	1,579	13,319	1,730	15,049	1,730	16,779	1,730	18,509	1,730	20,239	1,730
333	2.86%	323	3,898	323	4,221	323	4,544	323	4,867	323	5,190	323
334	5.88%	406	609	406	1,015	406	1,421	406	1,827	406	2,233	406
		\$ 3,032	\$ 25,179	\$ 3,183	\$ 28,362	\$ 3,183	\$ 31,545	\$ 3,183	\$ 34,728	\$ 3,183	\$ 37,911	\$ 3,183

Amort. of CIAC	Amort. Rate	Balance @ 12/31/2004	Audit		Audit		Audit		Audit		Audit	
Acct. No.	Amort. Rate	Balance @ 12/31/2004	Accruals	Balance @ 12/31/2005	Accruals	Balance @ 12/31/2006	Accruals	Balance @ 12/31/2007	Accruals	Balance @ 12/31/2008	Accruals	Balance @ 12/31/2009
311	6.67%	\$ 3,958	\$ 291	\$ 4,249	\$ 121	\$ 4,370	\$ -	\$ 4,370	\$ -	\$ 4,370	\$ -	\$ 4,370
330	3.33%	7,015	433	7,448	433	7,881	433	8,314	433	8,747	433	9,180
331	2.50%	21,969	1,730	23,699	1,730	25,429	1,730	27,159	1,738	28,897	1,746	30,643
333	2.86%	5,513	323	5,836	323	6,159	323	6,482	323	6,805	323	7,128
334	5.88%	2,639	406	3,045	406	3,451	406	3,857	406	4,263	406	4,669
		\$ 41,094	\$ 3,183	\$ 44,277	\$ 3,013	\$ 47,290	\$ 2,892	\$ 50,182	\$ 2,900	\$ 53,082	\$ 2,908	\$ 55,990

Per Filing: 52,734 5,115 57,849  
Year End Adjustment \$ 348 \$ (2,207) \$ (1,859)

### Audit Finding 3

#### Subject: Adjustment to Capital Structure

**Audit Analysis:** The Utility's filing reflects the following components for capital structure balances for the test year 2009.

Class of Capital	@12/31/2008	@12/31/2009	Average 2009
Long Term Debt	\$399,400	\$378,359	\$388,880
Common Equity	127,483	127,483	127,483
Customer Deposits	17,572	18,762	18,167
Shareholder Loan	<u>100,000</u>	<u>10,000</u>	<u>55,000</u>
Total	\$644,455	\$534,604	\$589,530

The Utility's general ledger reflects the following liabilities and shareholder equity balances as of year end 2008 and 2009.

Account Description	@12/31/2008	@12/31/2009	Average 2009
<u>Current Liabilities</u>			
Due Management Fees	\$132,213	\$165,213	\$148,713
Stockholder Loan	100,000	10,000	55,000
Customer Deposits	<u>17,572</u>	<u>18,762</u>	<u>18,167</u>
	\$249,785	\$193,975	\$221,880
<u>Long Term Liabilities</u>			
Independent Bank Debt	\$393,000	\$378,359	\$385,680
Advances for Construction	<u>6,400</u>	<u>0</u>	<u>3,200</u>
	\$399,400	\$378,359	\$388,880
<u>Owners Equity</u>			
Common Stock	\$200	\$200	\$200
Paid in Capital	127,483	127,483	127,483
Retained Earnings	<u>(149,057)</u>	<u>(185,472)</u>	<u>(167,264)</u>
	(\$21,374)	(\$57,789)	(\$39,581)

We have determined that the Utility's average combined capital structure balance are overstated by \$3,200, for the test year 2009, based on the following findings during our audit investigation.

- 1 We have reduced long term debt by \$6,400 as of December 31, 2008, to remove a \$6,400 cash advance from a Utility shareholder that was recorded prior to 2008. The cash advance was repaid and not included in the December 31, 2009 utility balance. Transactions such as this are not considered long term debt because they are not included in the original loan documents.

- 2 We have removed the shareholder loan balance because the utility classifies it as a current liability and there are no documents that reflect the associated terms, repayment, or interest rate for a loan. This account balance and the management fee liability account balance appear to be used to manage the Utility's operating cash flow. We defer any determination on this issue to the analyst in Tallahassee.
- 3 We have set the common equity to zero because the Utility's general ledger reflects a negative equity balance for year end 2008 and 2009.

Our adjustments are displayed below.

Class of Capital	Per Utility Average 2009	Audit Adjustments	Per Audit Average 2009
Long Term Debt	\$388,880	(\$3,200)	\$385,680
Common Equity	127,483	(127,483)	0
Customer Deposits	18,167	0	18,167
Shareholder Loan	<u>55,000</u>	<u>(\$55,000)</u>	<u>0</u>
Total	\$589,530	(\$185,683)	\$403,847

The Utility's combined water and wastewater capital structure is composed of long term debt and customer deposits. The Utility's weighted cost for capital before rate base reconciliation is 5.7 percent for the test year 2009.

Class of Capital	Avg. 2009	Ratio	Cost Rate	Weighted Cost
Long term debt	\$385,680	95.50%	5.69%	5.43%
Common Equity	0	0.00%	10.85%	0.00%
Customer Deposits	18,167	4.50%	6.00%	0.27%
Shareholder Loan	<u>0</u>	<u>0.00%</u>	0.00%	<u>0.00%</u>
Total	\$403,847	100.00%		5.70%

**Effect on the General Ledger:** None.

**Effect on the Filing:** The Utility's combined average capital structure balance before rate base reconciliation should be reduced by \$185,683 for the test year 2009.

## Audit Finding 4

### Subject: Adjustment to Direct Operation and Maintenance Expense

**Audit Analysis:** The Utility's operation and maintenance (O&M) expense is overstated by \$2,862 for the 12-month period ending December 31, 2009.

The Utility included the following invoiced expenses in the indicated accounts during 2009.

Acct. No.	Vendor	Amount	Service Provided
618	Custom Controls & Pumps	\$208	Chemicals
636	Pro-Tech Water & WW Services	700	Maintenance work
675	FMMA	250	School Donation
675	CFAT	<u>1,704</u>	Acquisition Adjustment
Total		\$2,862	

Our analysis of the above mentioned invoices indicated the following.

- 1) The chemical invoice of \$208 is erroneously charged to CFAT, it belongs to Residential Utilities, Inc.
- 2) The \$700 invoice for maintenance work does not have any supporting documentation.
- 3) The \$250 should be disallowed because it is a charitable contribution that should be posted to NARUC Account No. 426 – Miscellaneous Nonutility Expenses.
- 4) The \$1,704 acquisition adjustment represents twelve monthly accruals of \$142 for an unapproved acquisition adjustment balance included in the Utility's general ledger. The entire amount should be transferred to NARUC Account No. 426 - Miscellaneous Nonutility Expenses.

**Effect on the General Ledger:** None.

**Effect on the Filing:** The Utility's O&M expense balance should be reduced by \$2,862 for the 12-month period ending December 31, 2009.

Acct. No.	Description	Credit
618	Chemicals	(\$208)
636	Contractual Service-Other	(700)
675	Miscellaneous Expense	(250)
675	Miscellaneous Expense	<u>(1,704)</u>
Total		(\$2,862)



## Audit Finding 5

### Subject: Adjustment to Allocated Operation & Maintenance Expense

**Audit Analysis:** The Utility's filing includes \$16,718 of charges to water O&M expense from M.I.R.A. International, Inc., (MIRA) an administrative Service Company which is a related party. The charges are for employee and officer payroll and payroll tax expenses, employee benefits, office space and support for customer billing and collections, general maintenance materials and supplies and other general administrative support operations as needed for utility operations. CFAT has no employees of its own and all administrative and general maintenance services are provided MIRA.

MIRA's general ledger reflects \$784,456 of operating expenses for its operations in 2009. We have reviewed MIRA's operations and related expenses and have determined that it supports the following utility and nonutility organizations. The support for nonutility organizations is limited to payroll and other related employee expense types identified above.

- ▶ Alternative Phone Company, Inc.      Payroll and related expenses only (nonutility)
- ▶ Source One Medical, Inc.              Payroll and related expenses only (nonutility)
- BFF Corporation                          { Payroll and related expenses as well as      }
- C.F.A.T. H2O, Inc.                        { general maintenance supplies and services,    }
- ▶ Residential Utility Services, Inc.      { administrative office space and supplies and   }
- Tradewinds Utilities, Inc.              { other supporting services and operations.      }

We audited MIRA's operating expenses in 2009 and made the following adjustments.

- 1) We reduced MIRA's operating expense balance by \$380,000 to remove the employee salaries, payroll taxes and employee benefits for MIRA employees that worked for the two nonutility operations identified above. MIRA has a staff of twelve employees, of which seven work exclusively for the two nonutility affiliates identified above. Four of the remaining five employees work exclusively for the four utility operations identified above. The president, and CEO of MIRA, indicates that his time is split equally between utility and nonutility operations. We included fifty percent of his salary in the \$380,000 adjustment discussed above.
- 2) The remaining utility only expense balance of \$404,456 (\$784,456 - \$380,000) was further reduced by \$24,080 to remove invoices that we found during our audit investigation for materials or services that would not be allowed or recoverable based on Commissions' rules.

We reviewed and determined that the MIRA's allocation of expenses to utility operations was not applied consistently to the four utilities identified above. Therefore, we calculated a new allocation based on the Equivalent Residential Connection (ERC's) for each of the four utilities' operations as of December 31, 2009. This is consistent with the Commissions prior policy in other rate case proceedings that included affiliated operations<sup>3</sup>. Our calculations, balances and adjustments are displayed on the following schedule.

---

<sup>3</sup> See Order No. PSC-03-1440-FOF-WS, issued December 22, 2003, Docket No.020071-WS, In Re: Application For Rate Increase in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida.

**Effect on the General Ledger:** None

**Effect on the Filing:** The Utility's O&M expense balance should be increased by \$17,862 for the 12-month period ending December 31, 2009.

**Effect on Affiliate Operations:** Our adjustments above will also effect CFAT's wastewater operations by reducing its operating expenses by \$31,680 for 2009. We defer any determination on this issue, as well as the corresponding effect on MIRA's three other affiliated utility operations identified above, to the analyst in Tallahassee.

**Audit Finding 5**  
**Schedule 1 of 1**

**C.F.A.T. H2O, Inc.**  
**MIRA Allocations of Common Cost**

	ERC's per 2009 Annual Report					107	227	221	964	612	366	2,497
						4.29%	9.09%	8.85%	38.61%	24.51%	14.66%	100.00%
	Total	Remove	Utility	Audit	Adj. Utility	BFF	CFAT	CFAT	Residential	Tradewinds	Tradewinds	Total for
	Balance	Non-Utility	Balance	Adjustment	Balance	W/Water	Water	W/Water	Water	Water	W/Water	all Utility
<b>MIRA Expenses</b>												
MIRA COS	(\$70,668)	\$3,107	(\$67,561)	\$2,314	(\$65,247)	(\$2,796)	(\$5,932)	(\$5,775)	(\$25,190)	(\$15,992)	(\$9,564)	(\$65,247)
MIRA O&M	(133,634)	17,852	(115,782)	21,766	(94,016)	(4,029)	(8,547)	(8,321)	(36,296)	(23,043)	(13,780)	(94,016)
MIRA Payroll Taxes	(43,104)	26,991	(16,113)	0	(16,113)	(690)	(1,465)	(1,426)	(6,221)	(3,949)	(2,362)	(16,113)
MIRA Officer Salaries	(223,600)	124,800	(98,800)	0	(98,800)	(4,234)	(8,982)	(8,744)	(38,143)	(24,215)	(14,482)	(98,800)
MIRA Employee Salaries	<u>(313,450)</u>	<u>207,250</u>	<u>(106,200)</u>	<u>0</u>	<u>(106,200)</u>	<u>(4,551)</u>	<u>(9,655)</u>	<u>(9,399)</u>	<u>(41,000)</u>	<u>(26,029)</u>	<u>(15,566)</u>	<u>(106,200)</u>
<b>Total Expenses</b>	<b>(\$784,456)</b>	<b>\$380,000</b>	<b>(\$404,456)</b>	<b>\$24,080</b>	<b>(\$380,376)</b>	<b>(\$16,300)</b>	<b>(\$34,580)</b>	<b>(\$33,666)</b>	<b>(\$146,849)</b>	<b>(\$93,228)</b>	<b>(\$55,754)</b>	<b>(\$380,376)</b>
						Total MIRA Recoverable	\$16,300	\$34,580	\$146,849	\$93,228	\$55,754	\$380,376
						Current MIRA Allocation	8,385	16,718	65,346	161,994	100,276	484,194
						Audit Adjustment Increase(Decrease)	\$7,915	\$17,862	(\$31,680)	(\$15,145)	(\$7,048)	(\$103,817)

## Audit Finding 6

### Subject: Adjustment to Taxes Other Than Income Expense

**Audit Analysis:** The Utility's filing reflects a balance of \$996 for real estate and personal property taxes for the 12-month period ending December 31, 2009. Included in this balance was a water system allocation of \$353 for intangible property taxes on the personal property of the Utility.

We recalculated and reallocated the tangible property tax expense based on the ratio of the respective water and wastewater net plant in service balances at the end of the test year.

<u>Rate Base Description</u>	<u>Water</u>	<u>Wastewater</u>	<u>Total</u>
UPIS	\$557,132	\$356,581	\$913,713
Land	(19,500)	(39,000)	(58,500)
Accumulated Depreciation	<u>(139,991)</u>	<u>(161,315)</u>	<u>(301,306)</u>
Net Plant Balance	\$397,641	\$156,266	\$553,907
Ratio	71.79%	28.21%	100.00%
Tangible Property Tax per audit	\$836	\$329	\$1,165
Tangible Property Tax per utility	<u>353</u>		
Audit Adjustment	\$483		

**Effect on the General Ledger:** None

**Effect on the Filing:** The Utility's TOTI expense balance should be increased by \$483 for the 12-Month period ending December 31, 2009.

# Exhibit 1

Schedule of Water Rate Base

Florida Public Service Commission

Company: CFAT H2O, Inc.  
 Docket No.: 100126  
 Historical Test Year Ended: December 31, 2009  
 Interim [ ] Final [X]

Schedule: A-1  
 Page 1 of 1  
 Preparer: W. Wade Horgan, CRRA

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.

Line No.	(1) Description	(2) Average Amount Per Books	(3) A-3 Utility Adjustments	(4) Adjusted Utility Balance	(5) Supporting Schedule(s)
1	Utility Plant In Service	\$ 537,632	\$ -	\$ 537,632	A-3, A-5
2					
3	Utility Land & Land Rights	19,500	-	19,500	A-3, A-5
4					
5	Less: Non-Used & Useful Plant	-	-	-	A-7
6					
7	Construction Work In Progress	-	-	-	A-3
8					
9	Less: Accumulated Depreciation	127,972	-	127,972	A-3, A-9
10					
11	Less: CIAC	114,421	-	114,421	A-12
12					
13	Accumulated Amortization of CIAC	55,292	-	55,292	A-14
14					
15	Acquisition Adjustments	46,269	(46,269) (A)	-	A-3
16					
17	Advances For Construction	-	-	-	A-16
18					
19	Working Capital Allowance	-	5,909 (B)	5,909	A-17
20					
21	<b>Total Rate Base</b>	<b>\$ 416,300</b>	<b>\$ (40,360)</b>	<b>\$ 375,939</b>	
22					
23	Explanation of Adjustments				
24	A. Adjustment to remove Acquisition adjustment from rate base		(46,269)		
25	B. Adjustment to calculate working capital, per Schedule A-17		5,909		

# Exhibit 2

Schedule of Water Net Operating Income

Florida Public Service Commission

Company: CFAT H2O, Inc.

Schedule: B-1 [Interim]

Docket No.: 100126

Page 1 of 1

Historical Test Year Ended: December 31, 2009

Preparer: W. Wade Horgan, CRRA

Interim  Final

Explanation: Provide the calculation of net operating income for the test year. If amortization (Line 7) 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 Revenue	(7) Supporting Schedules
1	OPERATING REVENUES	\$ 43,579	\$ -	\$ 43,579	\$ 45,850	\$ 59,429	B-4, B-3
2							
3	Operation & Maintenance	38,236	2,886	41,121	602	41,923	B-3, B-5
4							
5	Depreciation, net of CIAC Amort.	18,923	-	18,923	-	18,923	B-13, B-3
6							
7	Amortization	-	-	-	-	-	
8							
9	Taxes Other Than Income Taxes	2,857	-	2,857	2,063	5,020	B-15, B-3
10							
11	Provision for Income Taxes	-	-	-	-	-	C-1, B-3
12							
13	OPERATING EXPENSES	60,115	2,886	63,001	2,886	65,889	
14							
15	NET OPERATING INCOME	\$ (18,536)	\$ (2,886)	\$ (19,422)	\$ 42,964	\$ 23,543	
16							
17							
18	RATE BASE	\$ 418,300	\$ (41,029)	\$ 375,271		\$ 375,271	
19							
20							
21	RATE OF RETURN	-3.97%		-5.18%		6.28%	

# Exhibit 3

Schedule of Requested Cost of Capital  
Simple Average Balance

Florida Public Service Commission

Company: CFAT H2O, Inc.  
Docket No.: 100126  
Historical Test Year Ended: December 31, 2009  
Interim [ ] Final [X]

Schedule: D-1  
Page 1 of 1

Preparer: W. Wade Horgan, CRRA

Explanation: Provide a schedule which calculates the requested cost of capital on a simple average basis. If a year-end basis is used, submit an additional schedule reflecting year-end calculations.

Line No.	(1) Class of Capital	(2)	(3)	(4)	(5)
		Reconciled to Requested Rate Base AYE	Ratio	Cost Rate	Weighted Cost
1	Long Term Debt	\$ 247,988	65.96%	5.69%	3.75%
2	Short Term debt	-	0.00%	0.00%	0.00%
3	Preferred stock	-	0.00%	0.00%	0.00%
4	Common Equity	81,295	21.62%	10.85%	2.35%
5	Customer Deposits	11,565	3.08%	6.00%	0.18%
6	Shareholder Loan	35,073	9.33%	0.00%	0.00%
7	Tax Credits - Weighted Cost	-	0.00%	0.00%	0.00%
8	Accumulated Deferred Income Tax	-	0.00%	0.00%	0.00%
9	Other	-	0.00%	0.00%	0.00%
10					
11	Total	\$ 375,939	100.00%		6.28%

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