State of Florida

Public Service Commission

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DATE: October 4, 2011

TO: Office of Commission Clerk

FROM: Clarence J. Prestwood, Chief of Auditing, Office of Auditing and Performance Analysis CJP

RE: Docket No.: 110165-SU
Company Name: Utility Corporation of Florida, Inc.
Company Code: SU916
Audit Purpose: Staff-Assisted Rate Case
Audit Control No: 11-165-2-1

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.

CJP/klh

Attachments: Audit Report

cc: Office of Auditing and Performance Analysis File

State of Florida

Public Service Commission

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

Auditor's Report

Utility Corporation of Florida, Inc.
Staff-Assisted Rate Case

12 Months Ended December 31, 2010

Docket No. 110165-SU
Audit Control No. 11-165-2-1
September 14, 2011

Jocelyn Y. Stephens

Jocelyn Y. Stephens
Audit Manager

Jocelyn Stephens for Jeffery A. Small

Jeffery A. Small
Audit Staff

Linda Hill-Slaughter

Linda Hill-Slaughter
Reviewer

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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 June 15, 2011. We have applied these procedures to the attached schedules prepared by staff.

This audit was performed following General Standards and Fieldwork Standards found in the AICPA Statements on Standards for Attestation Engagements. Our report is based on agreed-upon procedures. The report is intended only for internal Commission use.

Objectives and Procedures

General

Utility Information

Utility Corporation of Florida, Inc. is a Class C utility that provides wastewater services to 317 customers in Highlands County, Florida. The Utility is owned, managed and operated by Mr. Michael Tellschow, Mrs. Lois Schlabach and Mr. Thomas Quinn, respectively. Per information on the Florida Department of State's website, documents for incorporation were filed September 20, 2007.

Definitions

The term "Utility" used within this report refers to Utility Corporation of Florida, Inc. The term "FPSC" refers to the Florida Public Service Commission. The term "Affiliate" refers to Spring Lake Club, Inc. which is also owned by Mr. Michael Tellschow.

Historical Record

The Utility's facility has been in existence with service provided to the public for compensation since September of 1988 but was only certificated by the Commission in October 2008. We determined that the Utility has not had a prior rate case establishing rate base and that rates for wastewater service were approved and tariffed by the Commission in October 2008. We also determined that the Commission has established only one prior docket pertaining to the following action.

Docket No.	Order No.	Purpose
080079-SU	08-0646-PAA-SU 08-0717-CO-SU	Application for certificate to provide wastewater service in Highlands County by Utility Corporation of Florida, Inc.

Utility Books and Records

Objectives: Our objectives were to:

1) Reconcile the Utility's books to the Utility's annual report or tax return and have the Utility provide explanations of the differences,
2) Review outside auditor's report or workpapers, and
3) 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).

Procedures: We reviewed the Utility's accounting systems, the workpapers prepared by the plant consultant, and entries in the general ledger. The outside accountant, when preparing the FPSC Annual Reports included some of the entries that are not recorded in the general ledger. Therefore, the annual report provides a better representation of the actual plant balances than the balances reported in the general ledger. Therefore, we used the annual reports for the "per book" plant balances. For Net Operating Income and Capital Structure, we used the Utility's general ledger for per book amounts. We reconciled Utility Plant in Service (UPIS), as recorded in the Utility's annual reports, to the 2008 and 2009 Federal Income Tax Returns. Finding 1 discusses our findings and recommendations for the Utility's accounting system.

Rate Base

Land & Land Rights

Objectives: Our objectives were to:

1) Determine that utility land is recorded at original cost and is owned or secured under a long-term lease,
2) Review the warranty deed or other evidence of the Utility's land ownership for any purchase, sale, or transactions which have occurred since the original acquisition, and
3) Review for related party transactions.

Procedures: We verified that the Utility does not own the land upon which the wastewater plant and the percolation/holding pond sit. Instead, the Utility entered into a 99 year lease for use of the land. The landlord and owner of the land, as verified by staff, is an affiliate company of the Utility. The lease payment also includes the cost of rental for utility office space.

For purposes of determining allowable lease expense for rate case purposes, we obtained and reviewed the warranty deed, the purchase and mortgage agreements of the Parent company and the land lease agreement. Finding 11 discusses our findings and recommendations for Land.

Utility Plant in Service

Objectives: Our objectives were to:

1) Test additions and retirements to plant,
2) Describe major additions, retirements or adjustments,
3) Prepare a schedule of UPIS, by account, with year to year additions and retirements,
4) Review appropriate documentation to ensure that the Utility owns all assets associated with the provision of service to its customers, and
5) Interview the Utility's owner regarding the Utility's plans for new or expanded plant and provide a summary of interview.

Procedures: We noted that on January 1, 2008, the Utility made a lump sum entry to the general ledger of $25,889. This entry represented the net effect of a transfer from the Affiliate company for Plant, Accumulated Depreciation, Contributions in Aid of Construction (CIAC) and Accumulated Amortization CIAC.

Using the Proforma Balance Sheet from the Utility's Application for Original Certificate (filed February 2008 from the Utility's plant consultant, and plant activity from the Utility's 2008, 2009 and 2010 FPSC Annual Reports, we scheduled additions to plant in service, by account, for the period January 2008 through December 2010. The Utility did not provide account detail for the balance of UPIS as of December 31, 2007. Also, the Utility did not provide supporting documentation for the balance of UPIS as of December 31, 2007, nor for all its 2008 additions. We prepared adjustments to the plant balances recorded in the annual reports based upon our analysis. Findings 2, 3, 4 and 7 discuss our findings and recommendations for the Utility's Plant in Service.

Accumulated Depreciation

Objectives: Our objectives were to:

1) Test the annual accruals to Accumulated Depreciation based on adjusted plant, using the last authorized depreciation rates up to the beginning of the test year and the rates prescribed by Rule 25-30.140, F.A.C. for the test year, and
2) Prepare a schedule of Accumulated Depreciation balances by plant account from inception with year to year additions and retirements.

Procedures: We verified that the Utility used the depreciation rates prescribed in Commission Rule 25-30.140, F.A.C. for its 2008, 2009 and 2010 plant additions. For the plant incurred prior to 2008, the Utility used a composite depreciation rate. Using the prescribed rates, we calculated Depreciation Expense and Accumulated Depreciation for the years 2008 through 2010 using the staff adjusted plant balances. Finding 5 discusses our findings and recommendations for the Utility's Accumulated Depreciation.

Contributions-in-Aid-of-Construction

Objectives: Our objectives were to:

1) Test CIAC additions and adjustments since inception,
2) Test the annual accruals to accumulated amortization of CIAC applying the annual composite depreciation rate, and
3) Test to determine whether the appropriate test year depreciation and amortization rates have been used for test year expenses.

Procedures: We noted that CIAC was not recorded in the general ledger. However, CIAC was recorded in the 2008 through 2010 FPSC's Annual Reports of the Utility in the amount of $125,000. Mr. Tellschow explained that there was no contributed plant and no customers were charged to hook into the collection lines. The amount was a cash payment made to the Utility by the owner. Finding 6 discusses our findings and recommendations for the Utility's CIAC.

We prepared a schedule of Rate Base which is shown as Exhibit 1.

Net Operating Income

Operating Revenue

Objectives: Our objectives were to:

1) Test revenue transactions with the tariff rate and perform simple calculation estimations to determine what test year revenues should be, and

2) Examine and list the dollar amount, type and frequency of miscellaneous service charges in the test year.

Procedures: Using Order No. PSC-08-0646-PAA-SU, we determined the FPSC approved rates for wastewater and irrigation services. Because customer billing is on a flat rate, we verified the billing for 100% of the Utility's customers.

We also calculated revenues for irrigation services to a golf course owned by the Affiliate. Finding 8 discusses our findings and recommendations for the Utility's Revenues.

<u>Operation and Maintenance Expense</u>

Objectives: Our objectives were to:

1) Sample test year Operation and Maintenance (O&M) expense accounts. If any problems arise, contact the accounting analyst and if necessary, audit the complete accounts,
    a. Examine the expense for
        i. Proper Period
        ii. Amount
        iii. Classification
        iv. Supporting Documentation
        v. Utility vs. Non-Utility
        vi. Recurring
2) Prepare or obtain the Utility's schedule of contracted services for the test period,
    a. Separate services by:
        i. Engineering
        ii. Accounting
        iii. Legal
        iv. Billing
        v. Testing
        vi. Management
    b. Test documentation for amounts paid, period of service, and that the service was related to utility operations,
3) Provide the number of hours per month, employees and/or contracted vendors spend on operating, billing, testing, maintenance, and general management activities,
4) Note expense areas where the Utility has no costs assigned, but where benefits to the Utility's operation are evident, and

5) Note all related party relationships and transactions. Determine that related party transactions are competitive with non-affiliated transactions and that any contractual agreements have been negotiated with terms similar to arm's length transactions.

Procedures: For non-related third party expenses incurred by the Utility, we verified third party supporting documentation and cancelled checks. These included sludge removal, purchased power, chemicals, materials and supplies, insurance, testing and repairs. We prepared schedules summarizing the costs incurred.

For costs incurred by the Utility for contract labor and management costs, we reviewed a schedule created by the Utility which included a description of the task performed, hourly rate, and time spent involving utility activities. We also noted that no entries were made in the general ledger for these expenses.

All expenses were analyzed for the proper period, proper amount and proper classification. Expenses were also analyzed to determine if they were utility related, recurring, or had adequate supporting documentation.

The Utility rents office space from the Affiliate company. The cost of the office rent is imbedded in the commercial lease agreement for land. Total costs charged per lease agreement are $950. The Utility allocated the lease 50% to land use and 50% to office use. Finding 9 discusses our findings and recommendations for the Utility's Operation and Maintenance expense.

We prepared a schedule of Net Operating Income which is shown as Exhibit 2.

Taxes Other than Income

Objective: Our objective was to perform an analysis of Taxes Other than Income (TOTI).

Procedures: Using audit adjusted amounts, we calculated payroll taxes and the regulatory assessment fees. We also verified the State Corporation Fees. Finding 10 discusses our findings and recommendations for the Utility's TOTI.

Federal Income Tax Returns

Objectives: Our objectives were to:

1) Request copies of the Utility's tax returns for 2008, 2009 and 2010, and
2) Verify amounts for plant and current year Net Operating Income.

Procedures: We received copies of the 2008 and 2009 Federal Income Tax Returns. The Utility responded that the federal income tax return for 2010 has not yet been prepared. We reconciled plant in service, as recorded on the tax returns to plant in service recorded in the FPSC's Annual Reports filed by the Utility for calendar years 2008 and 2009.

Capital Structure

Objectives: Our objectives were to:

1) Determine the equity balance, transactions and adjustments from the previous audited period forward are in compliance with Commission Rules and the USOA,

2) Determine that notes payable, long-term debt, and debt equivalents are authorized and properly classified in compliance with the USOA and presented in the capital structure exhibits in compliance with Commission Rules,

3) Determine that related interest expense, including amortization of debt discount, premium, and issuance expense, have been properly recognized and accounted for in compliance with the USOA, and

4) Determine if deferred income taxes represent the effect of timing differences and are accounted for according to the USOA.

Procedures: We substantiated the amount and cost of long term debt. We analyzed the detail of the owners equity and retained earnings transactions. We determined that the Utility has no customer deposits. Finding 13 discusses our findings and recommendations for Long-Term Debt.

We prepared a Capital Structure which is shown on Exhibit 3.

Audit Findings

Finding 1: Company Books and Records

Audit Analysis: In our analysis of the Utility's books and records, we noted that the Utility does not comply fully with the NARUC USOA. We also noted that the Utility does not post all applicable and necessary accounting entries to the general ledger. The accounting entries not posted include, but are not limited to, accruals, deferred debits, intercompany payables, and adjusting journal entries prepared by an outside accountant - Utility Plant Consulting.

The outside accountant, when preparing the FPSC's Annual Report included some of the entries that are not recorded in the general ledger. As a result, the Annual Report provides a better representation of the actual plant balances than the balances reported in the general ledger. In our analysis of Rate Base, we used the annual report as per books. The 2010 Annual Report was filed with the Commission on May 26, 2011.

For Net Operating Income, we noted that the O&M Expenses recorded in the 2010 general ledger did not agree to the expenses recorded in the 2010 Annual Report. On July 16, 2011 we requested that the Utility reconcile these differences. This was necessary because the Utility's representative stated that the 2010 Annual Report balances included adjusting journal entries prepared by the outside accountant, but which were not recorded in the general ledger.

In several conversations with the outside accountant, he stated that he did not assist the Utility in the preparation of the 2010 Annual Report. However, on September 15, 2011, the Consultant faxed a reconciliation to the Tampa District Office with the explanation that he forgot he had prepared the reconciliation. The reconciliation was received subsequent to the analysis and preparation of an O&M expense schedule by the staff. The reconciliation is being provided to the analyst separately for their consideration.

Balances used for the capital structure schedule were obtained from the general ledger.

We recommend that the Utility be ordered to maintain its books in compliance with Commission Rules and NARUC USOA.

Effect on the General Ledger: See Findings 4, 5, 6, 8, 9, 10 and 12.

Finding 2: Utility Plant in Service Transferred to Utility

Audit Analysis: The Utility filed for incorporation on September 20, 2007. Prior to this time, the Utility's facilities were owned and operated by the Utility's Affiliate. The Utility's facility has been in existence with service provided to the public for compensation since September of 1988. The FPSC granted the Utility a certificate effective September 29, 2008.

The Utility recorded net plant of $25,889 in Account 101, labeled Utility Plant in Service – Other on January 1, 2008. The calculation of the original entry recorded in the Utility's general ledger for UPIS is shown below.

Category	Amount @ 12/31/2007
UPIS	$ 311,858
Acc Depr	(202,636)
CIAC	(112,500)
Acc Amort-CIAC	29,167
Net Plant	$ 25,889

The Utility did not provide any documentation to substantiate the beginning plant balance when the Utility came under the jurisdiction of the FPSC. In a conversation with the owner, he stated that he donated $112,500 which was treated as CIAC by the Utility's former outside accountant.

In its 2008 Annual Report, the Utility recorded the individual components of the above net plant in various schedules. Without documentation, the $311,858 cannot be detailed by account. UPIS is treated as a composite entry and is recorded on Schedule S-1–Wastewater Utility Plant Accounts. Accumulated Depreciation is recorded on Schedule S-2 – Analysis of Accumulated Depreciation by Primary Account -Wastewater at a rate of 2.71% for 2008, 2009 and 2010. CIAC and Accumulated Amortization of CIAC are recorded on Schedule F-8. There have been no additions to CIAC. CIAC is being amortized, in the annual reports, at the rates of 2.77%, 2.94% and 2.97% for 2008, 2009, and 2010, respectively.

We recommend that the Utility be required to provide supporting documentation for the plant transferred from its Affiliate of $311,858.

Effect on the General Ledger: Presented for informational purposes.

Finding 3: Cost of Removal

Audit Analysis: In our analysis of plant additions, we noted that the Utility did not post general journal adjustments prepared by its plant consultant to the general ledger. These journal entries represented reclassification to/from expense accounts, capitalized labor, and overhead billings. Additionally, we noted that the annual report did not include all plant additions recorded to the general ledger.

We reviewed all construction work orders that had been prepared by the professional plant accountant for 2008, 2009 and 2010. We determined that the accountant segregated invoice costs, for all plant replacements, between material costs and calculated labor costs. One-half of the calculated labor costs were then classified as cost of removal. Additionally, the accountant calculated an overhead charge for planning and for in-house. He also calculated contract labor, when applicable. The overhead planning was a surcharge to incorporate costs billed to the Utility by the professional plant accountant. The in-house and contract labor overhead were for capitalizable costs incurred when the Utility's employee or contract labor were used in the repair, replacement or installation of an UPIS item.

Per the accountant, the segregation between labor and material costs is based upon his experience and informed judgment after a best estimate input from the plant operator. The sum of the material, calculated labor at 50% and overhead costs were recorded as a plant addition with 75% of the plant addition recorded as a retirement. The remaining 50% of calculated labor was charged to Accumulated Depreciation as cost of removal. Per Commission practice, 100% of labor for installation of the new plant is capitalized, even though some of the labor may be related to the cost of removal of the old plant. The cost of removal is not factored into plant retirements.

Staff calculated the necessary adjustments to reverse all cost of removal charged to Accumulated Depreciation and to reclassify these costs as additions to UPIS and to calculate the retirement costs associated with these plant additions. Below is a summary schedule for these reclassifications.

Staff's Adjustment to Annual Report Balances to Remove Cost of Removal of Plant Retirements

A/C No.	A/C Title	2008	2009	Totals
370	Receiving Wells		$ 45	
		-	$ 45	$ 45
380	Treatment and Disposal	$ 250		
380	Treatment and Disposal	250		
380	Treatment and Disposal	250	$ 242	
		$ 750	$ 242	$ 992
389	Oth Plant and Misc Equip	$ 250		
389	Oth Plant and Misc Equip	100		
389	Oth Plant and Misc Equip	423		
389	Oth Plant and Misc Equip	100		
389	Oth Plant and Misc Equip	100		
389	Oth Plant and Misc Equip	200		
		$ 1,173	-	$ 1,173
	Total Addition to Plant	$ 1,923	$ 287	$ 2,210
	Associated Retirement Costs @ 75%	$ (1,442)	$ (215)	$ (1,658)
	Net Plant Adds	$ 481	$ 72	$ 553

Effect on the General Ledger: See Finding 4 for adjustment to be recorded in the general ledger.

Finding 4: Utility Plant in Service

Audit Analysis: In our analysis of UPIS, we prepared a schedule of annual plant activity by account as recorded by the Utility in its 2008, 2009 and 2010 Annual Reports. We used the annual reports for the "per book" UPIS balances. The UPIS balances in the annual reports consisted of plant additions, retirements and overhead charges and in our opinion, provided a more reliable picture of actual plant costs than the UPIS balances recorded in the general ledger. The beginning balance for UPIS was $311,858. See Finding 2 for our recommendation.

After a review of the supporting documentation for UPIS, we calculated adjustments to the Utility's balances recorded in the annual reports in order to comply with Commission practices and NARUC rules and regulations.

Below is a schedule, by year and account of staff's analysis of UPIS per the Annual Reports followed by a summary of staff's adjustments.

Schedule of Plant in Service

			2008			2009			2010			
		Balance	Company	Staff's	Balance	Company	Staff's	Balance	Company	Staff's	Balance
A/C No	Account Description	12/31/2007	Activity	Adjustments	12/31/2008	Activity	Adjustments	12/31/2009	Activity	Adjustments	12/31/2010
101	Composite Plant	$311,858	$(12,625)	$ (1,442) *	$300,319	$ (2,950)	$ (215) *	$297,154	$ (472)	$ (142)	$296,020
				2,528						(520)	
101	Utility Plant in Service-Other				-			-			-
351	Organization Costs		7,166	(2,244)	1,500			1,500			1,500
				(3,422)							
354	Structures and Improvements				-			-			-
370	Receiving Wells				-	683	45 •	728	455	693	1,876
371	Pumping Equipment				-	1,641		1,641	1,603	(629)	3,433
										818	
380	Treatment and Disposal		5,279	750 *	6,029	1,610	242 *	7,881			7,881
389	Oth Plant and Misc Equip		11,554	1,173 *	9,357			9,357			9,357
				(3,370)							
393	Tools,Shop & Garage Equip			1,570	1,570	200	(24)	1,745			1,745
395	Power Operated Equipment										
			$ 11,374	$ (4,458)		$ 1,184	$ 48		$ 1,586	$ 220	
		$311,858			$318,775			$320,006			$321,812
	Less Staff Adjustments				$ 4,458			$ 4,410			
										Avg YE Plt	**$320,909**
	Balance per Federal Tax Return				$323,232			$324,416			

Source: Annual Reports

* See Finding 3 for the explanation of these adjustments.

The schedule that follows describes the staff's adjustments.

Detail of Staff Adjustments to Plant Annual Report Balances

A/C No.	A/C Title	Amount	Purpose
351	Organization Costs	(2,244)	To reclassify costs associated with the acquisition of the 5-yr DEP Permit
		(3,422)	To remove expense amounts incurred
389	Oth Plant and Misc Equip	(3,370)	To remove undocumented costs Thomas Quinn - $2,022. (1,936.41 + 85.59) Alpha General - 766 USA Blue Book - 582 (533.55+48.16)
101	UPIS - Other (Composite)	2,528	To remove retirements associated with undocumented costs
393	Tools, Shop & Garage Equip	1,570	To record acquisition of Hand Held Ph and LDO Probe (Hach - 1/5/2008)
380	Treatment and Disposal	750	To add back costs labeled "Cost to Remove" associated with plant replacements
389	Oth Plant and Misc Equip	1,173	To add back costs labeled "Cost to Remove" associated with plant replacements
101	UPIS - Other (Composite)	(1,442)	To remove retirements associated with "cost of removal" add backs
	2008 Total	(4,458)	
393	Tools, Shop & Garage Equip	(24)	To remove duplicate costs recorded
380	Treatment and Disposal	242	To add back costs labeled "Cost to Remove" associated with plant replacements
370	Receiving Wells	45	To add back costs labeled "Cost to Remove" associated with plant replacements
101	UPIS - Other (Composite)	(215)	To remove retirements associated with "cost of removal" add backs
	2009 Total	48	
371	Pumping Equipment	(629)	To remove duplicate cost of a pump that was returned to the vendor. The vendor issued a credit to the Utility (verified by staff). One pump was capitalized. The other pump was expensed. Staff removed the pump that was capitalized in error and reclassified the pump that was originally expensed
		818	
		189	
370	Receiving Wells	693	To reclassify cost from expense to capital for phase monitor and starter
101	UPIS - Other (Composite)	472	To remove retirement amount for duplicate posting of pump
		(614)	To add retirement amount for a pump previously expensed
		(142)	
101	UPIS - Other (Composite)	(520)	To record retirement amount for phase monitor and starter
	2010 Total	221	

We also prepared an adjustment to be recorded to the general ledger to reflect the staff's actual adjusted balance of UPIS.

A/C No.	Account Description	Staff's Adjusted Balance 12/31/2010	Balance General Ledger	Staff's Adjustments to G/L
101	Composite Plant	$ 296,020	$ (25,889)	$ 270,132
101	Utility Plant in Service-Other	-	(18,366)	(18,366)
351	Organization Costs	1,500	(7,166)	(5,666)
354	Structures and Improvements	-	(12,665)	(12,665)
370	Receiving Wells	1,876	(900)	976
371	Pumping Equipment	3,433	(2,809)	624
380	Treatment and Disposal	7,881	(118)	7,763
389	Oth Plant and Misc Equip	12,727	-	12,727
393	Tools,Shop & Garage Equip	1,745	(145)	1,600
395	Power Operated Equipment		(298)	(298)
		$ 325,183	$ (68,356)	$ 256,827

Effect on the General Ledger:

Utility Plant in Service	$256,827	
Acc Amortization – CIAC	29,167	
Deferred Debits	12,951	
Retained Earnings	16,191	
CIAC		$112,500
Accumulated Depreciation		202,636

Finding 5: Accumulated Depreciation

Audit Analysis: Based upon our analysis of UPIS, we recalculated Accumulated Depreciation and Accumulated Amortization. Our calculation of annual depreciation and amortization expenses was based upon the staff adjusted average year-end plant balances and depreciation rates authorized per Commission Rule 25-30.140 F.A.C. for a Class C Utility.

For the plant recorded prior to 2008, we continued the use of the composite rate established by the Utility's plant consultant of 2.714%.

The Utility has not recorded any Depreciation Expense or Accumulated Depreciation in its general ledger for 2008, 2009 and 2010. Therefore, we prepared an adjustment for Accumulated Depreciation at December 31, 2010, as shown below:

Adjustment to Accumulated Depreciation

A/C No.	Account Description	Depr Rate	Staff's Adjusted Balance 12/31/2010	Balance Per General Ledger 12/31/2010	Staff's Adjustments to G/L
101	Composite Plant	2.714%	$ 211,263	$ -	$ 211,263
351	Organization Costs	2.50%	94	-	94
354	Structures and Improvements		-	-	-
370	Receiving Wells	4.00%	67	-	67
371	Pumping Equipment	6.67%	224	-	224
380	Treatment and Disposal	6.67%	1,190	-	1,190
389	Oth Plant and Misc Equip	6.67%	2,121	-	2,121
393	Tools,Shop & Garage Equip	6.67%	279	-	279
395	Power Operated Equipment	10.00%	-	-	-
			$ 215,238	$ -	$ 215,238
	Simple YE Average Balance		$ 210,917		

Plant Depreciation for the test period is $9,798.

Effect on the General Ledger:

	Debit	Credit
Retained Earnings	$12,602	
Accumulated Depreciation		$12,602*

* See Finding 4 ($215,238 - $202,636)

Finding 6: Contributions-in-Aid-of-Construction

Audit Analysis: We prepared a schedule of CIAC balances by year for 2008 through 2010. We adjusted CIAC for retirements made to UPIS. We also prepared a schedule of Accumulated Amortization – CIAC using the average year-end adjusted balances for CIAC.

In accordance with FPSC rules, we used the same composite depreciation rate as the applicable plant account of 2.714%.

The Utility did not record an amount for CIAC or Accumulated Amortization – CIAC in its general ledger. Therefore we prepared an adjustment for both accounts at December 31, 2010, as shown below.

CIAC and Amortization of CIAC

	Acct 271 Contribution in Aid of Construction		Acct 272 Accum Amortization - CIAC		
	Activity	Ending Balance	Amortization	Retirement	Ending Balance
12/31/2007		$ (112,500)			$ 29,167
2008	11,539		$ 2,897	$ (11,539)	
12/31/2008		(100,961)			20,525
2009	3,165		2,697	(3,165)	
12/31/2009		(97,796)			20,057
2010	1,134		2,639	(1,134)	
12/31/2010		(96,662)			21,562
Balance per G/L		-			-
Staff Adjustment		$ (96,662)			$ 21,562
Simple YE Avg Balance		$ (97,229)			$ 20,809

Amortization of CIAC for the test period is $2,639.

Effect on the General Ledger:

Contributions in Aid of Construction		$15,838*	
[	Accumulated Amortization – CIAC		$ 7,605**
	Retained Earnings		$ 8,233

* See Finding 4 ($112,500 - $96,662)

**See Finding 4 ($29,167 - $21,562)

Finding 7: Capital Improvement/Pro-Forma Plant

Audit Analysis: The Utility provided a schedule of additions and improvements that it anticipates will be needed in the immediate future. Some of these improvements are the result of a non-compliance letter issued to the Utility by the Florida Department of Environmental Protection (DEP) on April 13, 2011.

The schedule of additions is shown below.

Item Description	Estimated Costs
Improvements to Existing Plant	
2 new pumps at the transfer pond to pump water to the golf course. Includes breakers, contactors and metal head works	$ 5,000-$10,000
100 KW Emergency Generator	$ 50,000
Storage Shed	$ 3,000
Chlorine Feed System	$ 4,000
Needed for new construction	
2 Centrifugal blowers 20 HP, 2 motors 20 HP, Electrical connections	$ 15,000
Repair west clarifier	$500 - $1,000
Total	$77,500 - $89,000

The Utility could not provide documentation which supports the costs assigned to listed improvements. Also, the Utility intends to borrow funds from the owner to finance the costs of the above described construction.

Effect on the General Ledger: Presented for informational purposes.

Finding 8: Operating Revenues

Audit Analysis: As part of our investigation of Revenues recorded by the Utility, we noted that the Utility did not bill the Spring Lake Club, Inc.'s (SLCI) golf course for treated effluent used to irrigate the golf course.

Order No. PSC-08-0646-PAA-SU authorized the Utility to collect a charge of $.50 per thousand gallons of treated effluent used to provide irrigation to the SLCI golf course facilities (a related property).

Based upon the monthly Daily Sample Results – Part B Reports, staff calculated an annual flow of treated effluent through the wastewater treatment plant to be 6.504. The Utility verified that 100% of the flow is used to irrigate the SLCI golf course facility.

We calculated unbilled and unrecorded revenues from the golf course irrigation of $3,252 as shown below:

Annual Flow	6.504
Multiplier	1,000,000
Total Flow	6,504,000
PSC Approved Rate	$.50/thousand gallons
Reuse Revenues (not billed)	$3,252 (6,504,000/1,000 times $.50)

Additionally, we recalculated annual wastewater revenues based upon all customers' times the Commission authorized rate for each month of the test period. Total revenues based upon the Utility Residential and General Service tariff rates equaled $121,728. Revenues recorded in the general ledger were $121,472. The difference is $256.

We prepared an adjustment to be recorded to the general ledger to reflect the staff's adjusted balance of residential and general Revenues.

Per staff calculation, total revenues earned by the Utility including billed and unbilled was $124,980.

Effect on the General Ledger:

Cash	$3,508	
Residential Revenues		$3,508

Finding 9: Operation and Maintenance Expense

Audit Analysis: We performed an analysis of the O&M expenses recorded in the general ledger. We compared the amounts in the general ledger to the amounts recorded in the annual report. Differences resulted between the amounts recorded in the general ledger and in the annual report. The Utility could neither explain how the expense amounts recorded in its annual report were compiled nor could the Utility adequately reconcile the annual report amounts to the general ledger. We also noted that the Utility could not provide documentation for all the expenses recorded in the G/L.

Our analysis of O&M expenses included requests for documents to perform tests for proper period, amount, classification, supporting documentation, and whether expenses were recurring, reasonable, utility related or related party. We noted areas where the Utility received benefit but where no costs were assigned. We also noted related party relationships and transactions.

We calculated adjustments: 1) for those third party and related party costs which were incurred by the Utility but where no amounts were posted in the general ledger, 2) where costs were recorded but supporting documentation was not provided, 3) for the amortization of deferred debits, 4) to adjust recorded expenses to the actual amount incurred, 5) to reclassify amounts to the proper accounts, and 6) to adjust dollars between capital and expense accounts.

A description of the staff adjustments, along with a schedule of adjustments by account and amount are shown below.

Description of Staff Adjustments

a To reclassify repair charges of surge tank motor starter from UPIS (A/C 370) to expense (A/C 720)
b To record amortization of deferred debits
c To remove costs with no documentation
d To adjust general ledger balance to actual test period amount verified by staff
e To reclassify dollars charged to Travel Expense to Transportation Costs
f To reclassify Salary Expense charged to Transportation Costs
g To adjust Salary Expense to actual amount incurred (DR #2)
h To record invoices not previously recorded in G/L
i To remove duplicate charge
j To reclass capitalized amount from UPIS (A/C 371) to O&M Expense (A/C 720)
k To record staff computed expense, not previously recorded
l To reclassify replacement of sensor caps from UPIS (A/C 380) to expense (A/C 672)
m To capitalized labor & consultant costs

Schedule of O&M Expenses w/Staff Adjustments

	G/L Balance		Staff's Adjustments	Staff's Adjusted Balance
701 · Salary Expense	$ 37,023	g	$ 11,561	$ 49,775
		f	1,416	
		m	(225)	
711 · Sludge Removal	455			455
715 · Electricity	9,493	d	(363)	9,130
718 · Chemicals	4,542	c	(474)	4,068
720 · Materials and supplies	1,682	j	258	1,817
		h	5	
		a	236	
		c	(364)	
749 · Transportation Costs	5,816	e	400	4,800
		f	(1,416)	
649 · Office Supplies	478	c	(229)	249
667 · Professional Fees - Accounting	1,485	i	(720)	765
- Management Fee		k	6,500	6,500
- Consulting	516	m	(150)	366
- Grounds Maintenance		k	650	650
- Customer Billing/Payroll/Regulatory Affairs		k	15,600	15,600
672 · Repairs and Maintenance	2,783	l	118	1,870
		c	(1,030)	
684 · Travel Expense	400	e	(400)	-
735 · Testing and Samples--Short	18,452	c	(3,812)	14,640
740 - Rents (Office)		k	5,700	5,700
740 - Rents (Land)		k	943	943
770 - Bad Debt Expense		k	1,536	1,536
755 · Insurance Expense		k	2,322	2,322
Amortization of Deferred Debit Acct 186.1		b	600	600
Amortization of Deferred Debit Acct 186.2		b	2,859	2,859
Amortization of Deferred Debit Acct 186.3		b	931	931
Amortization of Deferred Debit Acct 186.4		b	530	530
			$ 42,981	
O&M Expenses	**$ 83,124**			**$ 126,106**

Effect on the General Ledger:

O&M Expenses	$42,981	
Intercompany Payable		$29,393
Retained Earnings		8,668
Deferred Debits		4,920

Finding 10: Taxes Other than Income

Audit Analysis: We performed an analysis of Payroll Taxes, State Corporation Fees and Regulatory Assessment Fees based upon applicable test period audit adjustments that were calculated by Staff.

Payroll taxes were calculated upon salary expense of $50,000. Regulatory Assessment Fees were calculated based upon Operating Revenues of $124,980. The difference between RAF owed and RAF paid for 2010 was immaterial. The Utility does not own land therefore no property taxes were incurred.

A schedule of adjustments to Taxes Other than Income is shown below.

Summary of Taxes Other Than Income

Acct. No.	Account Description	Balance Per G/L @ 12/31/2010	Audit Adjustments	Balance Per Audit @ 12/31/2010
408.1	Regulatory Assessment Fee	$ 5,476	$ 148	$ 5,624
408.2	Payroll Taxes	200	(200)	$ 4,369
	Social Security ($50,000 * 6.2%)		3,100	
	Medicare ($50,000 * 1.45%)		725	
	FUTA		56	
	SUTA		488	
	Property Taxes	-		$ -
408.4	State Corporation Fees	150		$ 150
665	Payroll Taxes	1,099	(1,099)	$ -
			$ 3,218	
		$ 6,926		$ 10,144

Effect on the General Ledger:

Taxes Other than Income	$3,218	
Retained Earnings		$3,218

Finding 11: Original Cost of Land

Audit Analysis: On January 1, 2008, the Utility entered into a commercial lease agreement for the use of land and a building owned by the Parent.

Per Utility documents, the lease is for a term of 99 years at a current rate of $950 and is allocated 50/50 between the land and the office building. The annual office rent of $5,700 includes electric, water and telephone service. Annual land rental is also calculated at $5,700. We noted that the Utility did not record an amount for rent expense in its general ledger for 2008, 2009 or 2010.

It has been the Commission's practice to calculate an appropriate rent expense based upon multiplying the annual rate of return, based on the Utility's current capital structure, by the original cost of the land when first dedicated to public service.

In our analysis of land, we determined that the land was originally purchased by Mr. Tellschow. Mr. Tellschow purchased the land from Links Property Corporation on December 3, 1985, for $1,000,000. The land consisted of Parcels A, B, D, F, G, H and J and Fairway Lakes, which consisted of approximately 600 acres. In 1987, Mr. Tellschow filed a quitclaim deed transferring title of the land to Spring Lake Club Inc. The majority of the land was used to develop a subdivision and to construct a golf course. It was determined that the wastewater plant is located within Parcel A of the legal description for the golf course. The wastewater plant as well as the percolation pond are in the middle of the golf course and cover approximately six acres.

In order to determine when the land was first dedicated, we visited the office of the Clerk of Court – Highlands County, Florida. We viewed the original Plat of Fairway Lakes PB 12 Page 43 and the Amended Plat of Fairway Lakes PB 15 Page 17. The original Plat of Fairway Lakes PB 12 Page 43 shows that the lots were originally platted for single-family homes with private wells and septic tanks. The Amended Plat of Fairway Lakes PB 15 Page 17 created smaller lot sizes as well as the villas. Both were silent concerning utilities, utility set asides or easements.

Staff calculated an amount for Rent Expense – Land as shown below:

Calculation of Land Rental

Purchase Price of Land	$ 1,000,000	Parcels A, B, D, F, G, H AND J FAIRWAY LAKES - December 1985
# of Acres	600	
	$ 1,667	Calculated price per acre
	6	Acreage for Sewer Plant
Staff Calculated Purchase Price Price for Utility Land	$ 10,000	
Annual Rate of Return	8.82%	Order No. PSC-11-0287-PAA-WS Docket 110006-WS
Staff Calculated Land Rent	882	
	7%	Highlands County Sales Tax Rate
Rent Expense - Land	$ 943	

Effect on the General Ledger: See Finding 4 for adjustment to be recorded in the general ledger.

Finding 12: Amortization of Deferred Debits

Audit Analysis: In 2008 and 2009, the Utility incurred costs for the preparation of a DEP permit and for major rehab of a surge tank and a lift station motor. We recorded these costs as deferred debits and amortized them over several years.

The schedule below provides detail for calculating the deferred amounts and the applicable amortization.

Detail of Staff's Adjustments

A/C No.	A/C Title	Amount	Purpose
2008			
186.4	Deferred Debit - Permit Acquisition Costs	$ 2,244	To reclassify costs associated with 5-yr DEP Permit
		405	To record additional costs incurred associated with the acquisition of DEP Permit
		$ 2,649	
186.1	DEP Permit	$ 3,000	To record cost of DEP 5-yr permit
186.2	Surge Tank Rehab	$ 9,217	To record cost surge tank rehab costs recorded in W/O 0805
		2,218	To record additional documented costs incurred in the rehab of surge tank
		$ 11,435	
2009			
186.3	Main Lift Station Motor Rehab	$ 2,792	To record costs of motor rehab

Based upon the Utility's estimate of the service lives of the deferred items, we calculated annual amortization over the applicable years.

Amortization of Deferred Debits

A/C No.	A/C Title	Amount	2008	2009	2010	2011	2012
			Annual Amortization				
2008							
186.4	Deferred Debit - Permit Acquisition Costs	$ 2,244					
		405					
		$ 2,649	$ 530	$ 530	$ 530	$ 530	$ 529
186.1	DEP Permit	$ 3,000	600	600	600	600	600
186.2	Surge Tank Rehab	$ 9,217					
		2,218					
		$ 11,435	2859	2859	2859	2858	
2009							
186.3	Main Lift Station Motor Rehab	$ 2,792		931	931	930	
					$ 4,920		

Annual amortization of deferred debits

Effect on the General Ledger:

Amortization Expense	$ 4,920	
Deferred Debit		$ 4,920

Finding 13: Long Term Debt

Audit Analysis: Using the general ledger, we performed an analysis of the components of the Utility's Capital Structure. We noted that the balances recorded in the FPSC's 2010 Annual Report were different from the balances recorded in the general ledger.

The capital structure consisted of only two components – Retained Earnings and Long Term Debt from Spring Lake Club, Inc. We were told that there is no debt agreement nor is an interest rate assigned. We did not observe any payments toward reducing this debt.

In Order No. PSC-11-1165-PAA-WS, issued June 27, 2000, in Docket No. 990243-WS, where a utility also had no debt instrument, the Commission characterized the debt as other common equity and stated as follows: "No cost is assigned to the long term debt and no debt instrument was available. The debt is from the Utility's Parent company. Therefore, we find that it is appropriate to characterize the long term debt as other common equity rather than long-term debt, given the related party status of the [debt]."

In this instance, the debt is from the Utility's Owner.

Additionally, we noted that the Utility's Owner provided $112,500 towards the construction of the wastewater system. The Utility treated this amount as CIAC.

We recommend that the Note Payable to the Owner be treated as equity for rate making purposes, and as such, we have prepared a Cost of Capital schedule with this classification.

Effect on the General Ledger: N/A

Exhibits

Exhibit 1: Rate Base

Utility Corporation of Florida, Inc
Average Rate Base*
12 Months Ended 12/31/2010

	Per Company	Staff's Adjustments		Staff's Adjusted Balance
Plant in Service	$ 68,355	$ 256,828	$ (904)	$ 324,279
Land	-			-
Accumulated Depreciation	-	4,332	(215,238)	(210,906)
CIAC	-		(96,662) (567)	(97,229)
Accumulated Amortization - CIAC	-	21,562	(753)	20,809
Working Capital Allowance (!/8 of O&M)		15,763		15,763
		$ 298,485	$ (314,124)	
Wastewater Rate Base	$ 68,355			$ 52,716

Schedule of Adjustments to Rate Base

		UPIS	Acc Depr	CIAC	Acc Amort CIAC
To adjust UPIS to balance calculated by staff analysis	Finding 8	$ 256,828	$ (202,636)	$ (112,500)	$ 29,167
To record Accumulated Depreciation to balance calculated by staff analysis	Finding 9		(12,602)		
To adjust CIAC to balance calculated by staff analysis	Finding 10			15,838	
To adjust Acc Amortization CIAC to balance calculated by staff analysis	Finding 10				(7,605)
		$ 256,828	$ (215,238)	$ (96,662)	$ 21,562
To record average adjustment		(904)	4,332	(567)	(753)
		$ 255,924	$ (210,906)	$ (97,229)	$ 20,809

*Simple Average

Exhibit 2: Net Operating Income

Utility Corporation of Florida, Inc.
Net Operating Income
12 Months Ended 12/31/2010

	Per Company	Staff's Adjustments		Staff's Adjusted Balance
Operating Revenues	$ 121,472	$ 3,508		$ 124,980
Operating Expenses:				
O&M Expenses	83,124	42,982		126,106
Depreciation Expense	-	9,798		9,798
Amortization of CIAC	-	(2,639)		(2,639)
Taxes Other Than Income	6,925	3,217		10,142
Total Operating Expenses	90,050	53,358	-	143,408
Operating Income/(Loss)	$ 31,422	$ (49,850)	-	$ (18,428)
Wastewater Rate Base	$ 68,355			$ 52,716
Rate of Return	45.97%			-34.96%

Schedule of Adjustments to Net Operating Income

To reclassify revenues from Uncategorized Income	$ 256
To record revenues from golf course irrigation	3,252
	$ 3,508
To adjust O&M expense for previously unrecorded expenses	$ 42,982
To adjust Depreciation Expense to amount calculated by staff analysis of UPIS	$ 9,798
To adjust Amortization Expense to amount calculated by staff analysis of CIAC	$ (2,639)
To adjust Taxes other than Income to tax due based upon staff analysis of expenses and revenues	$ 3,217

Exhibit3: Capital Structure

Utility Corporation of Florida, Inc.
Average Capital Structure*
12 Months Ended 12/31/2010

	Per Utility	Specific Adjustments (c)	Balance before Prorata Adjustments	Prorata Adjustment	Adjusted Balance	Percent of Total	Cost (b)	Weighted Cost
Long-Term Debt (a)	$ 69,447	$ (69,447)	$ -					
Common Stock (d)	$ 1,000		$ 1,000					
Retained Earnings	$ 5,547		$ 5,547					
Equity	$ -	$ 69,447	$ 69,447					
Total Common Equity			$ 75,994	$ (23,278)	$ 52,716	100%	8.74%	8.74%
Customer Deposits	$ -		-					
Total	$ 75,994	-	$ 151,988	$ (23,278)	$ 52,716 (e)	100%	8.74%	8.74%

Notes:

(a) This is related party debt. No cost is assigned to the long term debt and no debt instrument was available. No payments have been made towards reducing this debt.
(b) From Order No. 11-0287-PAA-WS, Docket 110006-WS
(c) Long term debt is recharacterized as equity (See Order No. PSC-04-1264-PAA-SU)
(d) Value for Common Stock comes from Form 1120S - U.S. Income Tax Return for an S Corporation
(e) Staff Adjusted Rate Base of $52,716

*Simple Average