

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-

DATE: October 2, 2015
TO: Office of Commission Clerk
FROM: Lynn M. Deamer, Chief of Auditing, Office of Auditing and Performance Analysis
RE: Docket No.: 150149-WS
Company Name: Silver Lake Utilities
Company Code: WS907
Audit Purpose: Staff Assisted Rate Case
Audit Control No.: 15-177-4-1

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 is no confidential work papers associated with this audit.

LMD/cp

Attachment: 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
Miami District Office

Auditor's Report

Silver Lake Utilities, Inc.
Staff-Assisted Rate Case

12 Months Ended March 31, 2015

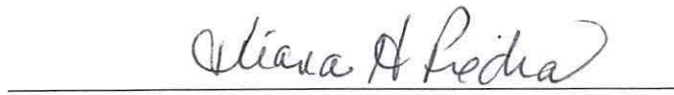
Docket No. 150149-WS
Audit Control No. 15-177-4-1
September 30, 2015



Jeffery A. Small
Audit Manager



Yen N. Ngo
Audit Staff



Iliana H. Piedra
Reviewer

Table of Contents

Purpose	1
Objectives and Procedures.....	2
Audit Findings	
1: Utility Plant in Service	6
2: Accumulated Depreciation	9
3: Capital Structure	12
4: Operating Revenue	13
5: Operation and Maintenance Expense	15
6: Taxes Other Than Income	19
7: Information on Original Cost	20
8: Information on Accumulated Depreciation	22
9: Information on Utility Infrastructure and Customer Base.....	24
Exhibits	
1: Rate Base	25
2: Capital Structure	26
3: Net Operating Income	27

Purpose

To: Florida Public Service Commission

We have performed the procedures described later in this report to meet the objectives set forth by the Division of Accounting and Finance in its audit service request dated June 19, 2015. We have applied these procedures to the attached schedules prepared by the audit staff in support of Silver Lake Utilities, Inc.'s request for a Staff-Assisted Rate Case in Docket No. 150149-WS.

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

Objectives and Procedures

Definitions

SLU/Utility refers to Silver Lake Utilities, Inc.

Test Year refers to the twelve months ended March 31, 2015.

NARUC refers to the National Association of Regulatory Utility Commissioners.

USOA refers to the NARUC Uniform System of Accounts as adopted by Rule 25-30.115 – Uniform System of Accounts for Water and Wastewater Utilities, Florida Administrative Code. (F.A.C.)

Background

Silver Lake Utilities, Inc. is a Class C utility serving approximately 44 residential and 23 general service customers in Glades and Highlands Counties. In Docket No. 060726-WS, the Florida Public Service Commission (Commission) granted SLU both water and wastewater certificates to operate utilities in territory located in Glades and Highland Counties. The Utility commenced operations in 2007. In Docket No. 080213-WU, SLU was granted authority to extend its water service area in Highlands County. Rate base has never been formally established by this Commission, but rates were initially set in Order No. PSC-07-0983-PAA-WS, issued September 4, 2007. SLU has never availed itself of the opportunity to adjust its rates by means of the Commission's authorized Price Index or Pass Through administrative proceedings. Although authorized, SLU has neither constructed nor provided any wastewater services to date in its service territory.

SLU is incorporated with the Florida Department of State Division of Corporations and files an 1120 U.S. Corporate Tax Return. SLU is 100 percent owned by Lykes Bros. Inc. (LB) and is governed by the same board of directors. LB Citrus and Ranch Divisions account for all but one of SLU's total customer base. Additional information pertaining to SLU's infrastructure and customer base can be found in Finding 9.

General

Objective: The objective was to determine whether the Utility maintains its books and records in conformity with NARUC USOA.

Procedure: We reviewed the Utility's accounting system by examining the records provided for this proceeding and compared them to the NARUC USOA. No exceptions were noted.

Rate Base

Utility Plant in Service

Objectives: The objectives were to determine whether Utility Plant in Service (UPIS): 1) Consists of property that exists and is owned by the Utility, 2) Additions are recorded at original

cost, 3) Retirements are made when a replacement asset was put in service, and 4) Adjustments required in the Utility's last rate proceeding were recorded in its books and records.

Procedures: We obtained original cost information for the UPIS beginning balances that were posted to the general ledger on December 31, 2007. We scheduled subsequent water UPIS activity through March 31, 2015. We traced asset additions and retirements to supporting documentation. We determined the year end and simple average UPIS balance as of March 31, 2015. Our recommended adjustment to UPIS is discussed in Finding 1. Finding 9 provides additional information about the UPIS infrastructure.

Land & Land Rights

Objectives: The objectives were to determine whether utility land was: 1) Recorded at original cost, 2) Owned or secured under a long-term lease agreement, and that 3) Adjustments required in the Utility's last rate proceeding were recorded in its books and records.

Procedures: We reviewed the Utility's annual reports and searched the Highlands and Glade Counties records and determined that no additions were made. We verified that the lands occupied by the Utility's various water supply systems are secured by executed long term leases in the Utility's name. Therefore, no Land balance exists. No exceptions were noted.

Accumulated Depreciation

Objectives: The objectives were to determine whether Accumulated Depreciation: 1) Accruals are properly calculated and recorded based on Rule 25-30.140 - Depreciation, F.A.C., 2) Retirements are recorded when an asset was replaced, and 3) Adjustments required in the Utility's last rate proceeding were recorded to its books and records.

Procedures: We obtained original cost information for the Accumulated Depreciation beginning balances that were posted to the general ledger on December 31, 2007. We calculated annual accruals to Accumulated Depreciation using the depreciation rates established by Rule 25-30.140(2), F.A.C., as of March 31, 2015. We determined the year end and simple average Accumulated Depreciation balance as of March 31, 2015. Our recommended adjustment to accumulated depreciation is discussed in Finding 2. Additional information concerning the depreciation rates used by the Utility is discussed in Finding 8.

Contributions-in-Aid-of-Construction

Objectives: The objectives were to determine whether Contributions-in-Aid-of-Construction (CIAC): 1) Consist of cash or property contributions that exist and are owned by the Utility, 2) Additions are recorded using Commission approved tariffs, 3) Retirements are recorded when a contributed asset was replaced, and 4) Adjustments required in the Utility's last rate proceeding were recorded to its books and records.

Procedures: We determined that SLU currently does not have any CIAC as of March 31, 2015.

Accumulated Amortization of CIAC

Objectives: The objectives were to determine whether Accumulated Amortization of CIAC: 1) Accruals are properly calculated and recorded based on Rule 25-30.140 - Depreciation, F.A.C.,

2) Retirements are recorded when a contributed asset was replaced, and 3) Adjustments required in the Utility's last rate proceeding were recorded to its books and records.

Procedures: We determined that SLU currently does not have any Accumulated Amortization of CIAC as of March 31, 2015.

Working Capital

Objectives: The objective was to determine the working capital adjustment to be included in rate base per Rule 25-30.433- Rate Proceedings, F.A.C.

Procedures: We calculated the working capital adjustment for the test year ended March 31, 2015, using one-eighth of Operation and Maintenance (O&M) Expense as required by Rule. Our recommended Working Capital adjustment is discussed in Finding 5.

Capital Structure

Objectives: The objectives were to determine the: 1) Components of the Utility's capital structure, 2) Cost rate for each class of capital, 3) Overall weighted cost of capital, and that 4) Components are properly recorded in compliance with the NARUC USOA.

Procedures: We reviewed the Utility's annual reports and determined that the Utility's Capital Structure is composed of common equity and long term debt. We determined the year end and simple average Capital Structure balance and its weighted average cost as of March 31, 2015. No exceptions were noted. Our recommended average Capital Structure and its weighted average cost are discussed in Finding 3.

Net Operating Income

Operating Revenue

Objectives: The objectives were to determine whether Revenues are: 1) Representative of the Utility's operations for the test year 2) Calculated using Commission approved tariff rates, and 3) Recorded in compliance with NARUC USOA.

Procedures: We determined individual customer consumption for the test year ended March 31, 2015, using the Utility's monthly customer billings. We calculated test year Revenues based on billing determinates and compared our calculated revenue amount to the revenues reflected in the general ledger. We determined whether the Utility is charging its authorized tariff rates. We determined that there were no Miscellaneous Revenues collected during the test year. Our recommended amount for Revenues for the test year is discussed in Finding 4. Finding 9 provides additional information about the Utility's customer base.

Operation and Maintenance Expense

Objectives: The objectives were to determine whether Operation and Maintenance Expense (O&M) is: 1) Representative of the Utility's ongoing operations for the test year, 2) Recorded in the appropriate period for the correct amount, 3) Required for the provision of utility services, and 4) Recorded in compliance with the NARUC USOA.

Procedures: We reviewed a sample of invoices for the Utility's O&M Expense for the test year ended March 31, 2015. We ensured all expenses were correctly classified, and verified that they were recurring in nature. We verified each expense against the invoice and supporting documentation. Our recommended amount for O&M Expense for the test year is discussed in Finding 5.

Depreciation Expense

Objectives: The objectives were to determine whether Depreciation Expense is properly calculated and recorded in compliance with the NARUC USOA.

Procedures: We calculated the Utility's Depreciation Expense for the test year ended March 31, 2015, using the rates established by Rule 25-30.140, F.A.C. Our recommended amount for Depreciation Expense is discussed in Finding 2. Additional information concerning Depreciation Expense is discussed in Finding 8.

Taxes Other than Income

Objectives: The objectives were to determine whether Taxes Other Than Income Expense (TOTI) is: 1) Representative of the Utility's ongoing operations for the test year, 2) Recorded in the appropriate period for the correct amount, 3) Required for the provision of utility services, and 4) Recorded in compliance with the NARUC USOA.

Procedures: We compiled the Utility's TOTI Expense for the test year ended March 31, 2015, using the documentation provided. We included property taxes and Regulatory Assessment Fees (RAF) for the test year and confirmed their utility classification. We recalculated RAFs based on test year Revenues. Our recommended amount for TOTI Expense for the test year is discussed in Finding 6.

Audit Findings

Finding 1: Utility Plant in Service

Audit Analysis: The Utility's general ledger reflects a Utility Plant in Service (UPIS) balance of \$1,246,881, as of March 31, 2015.

Rate base has never been established for the Utility in a Commission proceeding. The Utility's general ledger reflects the following activity since it obtained its original certificate to provide water utility services.

Period End	Activity	UPIS Balance
Beg Bal		\$606,123
12/31/07	\$0	\$606,123
12/31/08	\$521	\$606,644
12/31/09	\$644,747	\$1,251,391
12/31/10	(\$190)	\$1,251,201
12/31/11	(\$4,320)	\$1,246,881
12/31/12	\$0	\$1,246,881
12/31/13	\$0	\$1,246,881
03/31/14	\$0	\$1,246,881
03/31/15	\$0	\$1,246,881

Small differences are due to rounding.

The beginning balances for UPIS were based on an original cost study that Lykes Bros. Inc. (LB) performed to determine the transfer cost of utility assets from its Citrus and Ranch Divisions. See Finding 7 for information on these balances.

2008 Activity

The net increase of \$521 consists of \$521 of additions that were supported without exception.

2009 Activity

The net increase of \$644,747 (\$6,640+\$638,107) consists of \$6,640 of additions that were supported without exception and the five water treatment plant acquisitions from LB. The original cost and accounting treatment for these acquisitions are discussed in Finding 7.

Asset	UPIS
Brighton Ranch Water Treatment Plant	\$349,622
Brighton Grove Water Treatment Plant	\$153,239
Lake Placid Water Treatment Plant	\$71,017
Dinner Lake Water Treatment Plant	\$2,885
Mulch Plant	\$61,344
Total	\$638,107

2010 Activity

The net decrease of \$190 consists of a \$190 journal entry to correct a 2009 recording error that was supported without exception.

2011 Activity

The net decrease \$4,320 (\$58,125-\$62,595) consists of \$58,125 of invoiced additions and the retirement of the Mulch Plant, purchased in 2009, at original cost of \$61,344 plus additions of \$1,101 for a total retirement of \$62,445. We decreased the invoiced additions amount by \$57,525 to reclassify the organization cost associated the Muse Development to Account 103-Plant Held for Future Use. The Utility was granted an extension of its service territory in Docket Nos. 080213-WU and 080613-SU in anticipation of expanding plant facilities to serve the proposed Muse development which never occurred. Only assets that are providing service to the Utility's customers should be included in current operations.

Test Year 2014-2015 Activity

We increased UPIS by \$4,400 (\$1,805+\$2,595) to reclassify two capital additions that were transferred from test year Operating and Maintenance Expense. See Finding 5 for additional details. These were new asset additions, therefore no retirement is required.

The Utility's average UPIS is \$1,191,556, as of March 31, 2015. Table 1-1 displays our adjustments by plant account.

Accumulated depreciation and test year depreciation expense are discussed in Finding 2.

Effect on the General Ledger: The following entry is needed to correct the general ledger.

<u>NARUC Account No.</u>	<u>Description</u>	<u>Debit</u>	<u>Credit</u>
101 301	Organization Cost		\$57,525
101 311	Pumping Equipment	\$1,805	
101 336	Backflow Preventers	\$2,595	
103 301	Plant Held for Future Use	\$57,525	
401 620	Materials & Supplies		\$4,400

Effect on the Filing: Average UPIS is \$1,191,556 for the test year ended, March 15, 2015

Table 1-1

Acct. No.	Description	As of March 31, 2015			Simple Average
		Per Utility	Adjustment	Per Audit	
101 301	Organization Cost	\$228,464	(\$57,525)	\$170,938	\$170,938
101 304	Structures & Improv.	\$111,814	\$0	\$111,814	\$111,814
101 307	Wells & Springs	\$267,516	\$0	\$267,516	\$267,516
101 310	Power Generation Equip.	\$50,918	\$0	\$50,918	\$50,918
101 311	Pumping Equip.	\$54,760	\$1,804	\$56,564	\$55,662
101 320	Water Treatment Equip.	\$249,553	\$0	\$249,553	\$249,553
101 330	Dist., Reservoir & Standpipes	\$22,174	\$0	\$22,174	\$22,174
101 331	Transmission & Dist. Mains	\$247,158	\$0	\$247,158	\$247,158
101 334	Meters	\$13,908	\$0	\$13,908	\$13,908
101 336	Backflow Preventers	\$0	\$2,595	\$2,595	\$1,298
101 345	Power Operated Equip.	\$617	\$0	\$617	\$617
Total		\$1,246,881	(\$53,126)	\$1,193,755	\$1,191,555

Small differences are due to rounding.

Finding 2: Accumulated Depreciation

Audit Analysis: The Utility’s general ledger reflects an Accumulated Depreciation balance of \$484,818, as of March 31, 2015.

Rate base has never been established for the Utility in a Commission proceeding. The Utility’s general ledger reflects the following activity since it obtained its original certificate to provide water utility services.

Period End	Accumulated Depreciation	
	Activity	Balance
Beg Bal		(\$205,855)
12/31/07	(\$10,402)	(\$216,257)
12/31/08	(\$8,362)	(\$224,619)
12/31/09	(\$63,125)	(\$287,743)
12/31/10	(\$36,577)	(\$324,320)
12/31/11	(\$27,967)	(\$352,287)
12/31/12	(\$40,779)	(\$393,066)
12/31/13	(\$40,778)	(\$433,844)
03/31/14	(\$10,195)	(\$444,039)
03/31/15	(\$40,778)	(\$484,818)

Small differences are due to rounding.

The beginning balances for accumulated depreciation were based on an original cost study that Lykes Bros. Inc. (LB) performed to determine the transfer cost of utility assets from its Citrus and Ranch Divisions. See Finding 7 for information on these balances.

The accumulated depreciation activity displayed above reflects the use of Class C and Class B depreciation rates. In 2010, based on planned growth in its service territory, the Utility believed a large capital investment and revenue growth would occur requiring a change from a class C to a class B utility. In anticipation of this change the Utility requested its accounting consultant to prepare its 2010 Annual Report reflecting an accumulated depreciation balance as if class B service lives were in place since the original certificates were granted.

We scheduled and recalculated accumulated depreciation accruals on UPIS based on our adjusted UPIS balances in Finding 1. We calculated our accruals using the Class B service lives prescribed in Rule 25-30.143 - Depreciation, F.A.C. Additional information explaining our action and the Utility’s use of Class B service lives is provided in Finding 9. Based on our calculations, we have reduced accumulated depreciation and depreciation expense by \$6,724 and \$264, respectively, for the test year ended March 31, 2015. See Tables 2-1 and 2-2 for details.

Effect on the General Ledger: The following entry is needed to correct the general ledger.

NARUC Account No.		Description	Debit	Credit
108	301	Organization Cost	\$12,197	
108	304	Structures & Improv.		\$2,599
108	307	Wells & Springs		\$6,131
108	310	Power Generation Equip.	\$201	
108	311	Pumping Equip.		\$8,719
108	320	Water Treatment Equip.		\$2,704
108	330	Dist., Reservoir & Standpipes	\$374	
108	331	Transmission & Dist. Mains	\$265	
108	334	Meters	\$479	
108	336	Backflow Preventers		\$87
		To be determined by the Utility	\$6,724	

Effect on the Filing: Average Accumulated Depreciation is \$471,285 and Depreciation Expense is \$40,514, respectively, for the test year ended, March 15, 2015.

Table 2-1

Acct. No.	Description	As of March 31, 2015			Simple Average
		Per Utility	Adjustment	Per Audit	
108 301	Organization Cost	(\$46,905)	\$12,197	(\$34,708)	(\$32,571)
108 304	Structures & Improv.	(\$20,124)	(\$2,599)	(\$22,723)	(\$20,976)
108 307	Wells & Springs	(\$159,079)	(\$6,131)	(\$165,210)	(\$160,752)
108 310	Power Generation Equip.	(\$14,639)	\$201	(\$14,438)	(\$13,165)
108 311	Pumping Equip.	(\$19,713)	(\$8,719)	(\$28,432)	(\$27,063)
108 320	Water Treatment Equip.	(\$78,378)	(\$2,704)	(\$81,082)	(\$75,411)
108 330	Dist., Reservoir & Standpipes	(\$12,045)	\$374	(\$11,671)	(\$11,371)
108 331	Transmission & Dist. Mains	(\$128,350)	\$265	(\$128,085)	(\$125,201)
108 334	Meters	(\$5,289)	\$479	(\$4,810)	(\$4,463)
108 336	Backflow Preventers	\$0	(\$87)	(\$87)	(\$43)
108 345	Power Operated Equip.	(\$296)	\$0	(\$296)	(\$269)
Total		(\$484,818)	(\$6,724)	(\$491,542)	(\$471,285)

Small differences are due to rounding.

The major reason for differences between Utility and Audit balances for accounts with no audit adjustment is due to the 2009 UPIS addition of \$638,107. The Utility did not begin depreciation accruals until the following year. The audit calculation includes one-half year accrual in 2009. Other differences are due to timing issues.

Table 2-2

Acct. No.	Description	Test Year Ended March 31, 2015		
		Per Utility	Adjustment	Per Audit
403 301	Organization Cost	\$5,712	(\$1,439)	\$4,273
403 304	Structures & Improv.	\$3,500	(\$6)	\$3,494
403 307	Wells & Springs	\$8,908	\$9	\$8,917
403 310	Power Generation Equip.	\$2,546	\$0	\$2,546
403 311	Pumping Equip.	\$2,459	\$279	\$2,738
403 320	Water Treatment Equip.	\$10,550	\$794	\$11,343
403 330	Dist., Reservoir & Standpipes	\$599	\$0	\$599
403 331	Transmission & Dist. Mains	\$5,759	\$10	\$5,769
403 334	Meters	\$695	\$0	\$695
403 336	Backflow Preventers	\$0	\$87	\$87
403 345	Power Operated Equip.	\$51	\$0	\$51
Total		\$40,778	(\$267)	\$40,514

Small differences are due to rounding.

Finding 3: Capital Structure

Audit Analysis: The Utility's general ledger reflects a combined Equity and Loan Term Note Payable balance of \$370,892 and \$424,000, respectively, as of the test year ended March 31, 2015.

The ratio of debt to equity is 53.34 percent ($\$424,000 / (\$370,892 + \$424,000)$). We calculate a Return on Equity (ROE) rate of 10.58 percent, based on the Commissions' leverage graph calculation, approved in Order No. PSC-15-0259-WS, issued July 2, 2015.

The cost rate for the long term note payable is 4.50 percent on the face of the note. However, the Utility stated that in 2015 the rate was reduced to 3.00 percent to reflect the actual cost to borrow in today's market by the notes' holder, Lykes Bros. Inc.

The Utility is authorized to collect a customer deposit of \$76 with the provision of residential service per its tariff. However, no deposits have been collected since there is only one non-affiliated customer. See Finding 9 for additional information on the Utility's customer base and customer billing operation.

The Utility's Capital Structure is comprised of 46.66 percent equity and 53.34 percent debt. The average capital structure balance is \$739,327 when reconciled to the average rate base balance displayed in Exhibit 1. The weighted average cost for its capital structure is 6.54 percent. See Exhibit 2 for our calculations.

Effect on the General Ledger: None.

Effect on the Filing: The average capital structure balance is \$739,327 with a weighted average cost of 6.54 percent for the test year ended, March 31, 2015.

Finding 4: Operating Revenue

Audit Analysis: The Utility's general ledger reflects adjusted Revenues of \$43,397 for the test year ended March 31, 2015. The revenues were generated by combined billings to Lykes Bros. Inc. Citrus and Ranch Divisions and to one non-affiliated general service customer.

Revenue Type	Ranch Division	Citrus Division	Brighton Church	Total
General Service	\$6,175	\$11,577	\$430	\$18,182
Residential Service	\$7,942	\$12,547	\$0	\$20,489
Bulk Service	\$0	\$4,727	\$0	\$4,727
Total	\$14,117	\$28,850	\$430	\$43,397

Using individual water consumption information provided by the Utility we constructed a billing analysis for the test year. Using the billing determinants from our analysis and the Utility's Commission approved tariffs we calculate Revenues of \$47,162 for the test year.

Revenue Type	Per Utility	Adjustment	Per Audit
General Service	\$18,182	\$2,429	\$20,611
Residential Service	\$20,489	(\$1,728)	\$18,761
Bulk Service	\$4,727	\$3,063	\$7,790
Total	\$43,397	\$3,765	\$47,162

The Lake Placid plant uses a three inch master meter to measure the amount of unfinished water pumped by a single eight inch well into a 1,500 gallon pneumatic storage tank. After the storage tank, a supply line is used to distribute unfinished water for irrigation purposes while a second supply line feeds a second 1,000 gallon storage tank for chlorine treatment and ultimate distribution for potable use. The potable water is measured by a two inch meter that distributes the finished water to three general and four residential service customers. None of the customers are individually metered. The Utility calculates irrigation use by subtracting the potable water use from the amount of pumped water recorded by the master meter.

The Utility's calculation is based on the base facility charge of \$304.80 for a three inch meter plus the calculated unfinished use times \$0.91 per thousand gallons. The Utility's water tariff was approved in Order No. PSC-07-0983-PAA-WS and includes a specific tariff for bulk service raw water that includes a rate of \$0.91 per thousand gallons plus a variable base facility charge for the purposes of providing bulk water to future systems or customers. We believe that the Utility is inappropriately applying the \$0.91 usage tariff and should have used the usage tariff for a general service three inch meter which is \$3.79 per thousand gallons. Additionally, for this service, there was a difference between the annual billed usage and the annual usage information that was provided for billing analysis purposes. The difference between the usage and tariff rates is shown below.

	Usage	Tariff	Amount
Gallons per Consumption Information provided	1,090.250	\$3.790	\$4,132
Gallons per Utility Bills	1,174.660	\$0.091	\$1,069
Difference			\$3,063

The remaining difference of \$702 between general and residential service is primarily due to service classifications and the amount of water used and subject to the proper tariff.

Based on the above information we have increased Utility revenues by \$3,765 for the test year.

Effect on the General Ledger: To be determined by the Utility.

Effect on the Filing: The Utility's Revenues are \$47,162 for the test year ended March 31, 2015.

Finding 5: Operation and Maintenance Expense

Audit Analysis: The Utility's general ledger reflects Operation and Maintenance Expenses of \$157,406 for the test year ended March 31, 2015.

Account 601 & 603 – Salaries

The Utility has no employees. All management and routine maintenance services are provided by Lykes Bros. Inc. (LB) employees through established contracts for services described below.

Account 610 – Purchased Water

The Utility's general ledger reflects an amount of \$1,256 for this account. The amount is based on royalties the Utility is required to pay LB, per the long term land lease contracts, for raw water pumped from the aquifer below the real property owned by LB that contains the individual well sites. The royalties are subject to renegotiation every three years but have remained unchanged. We have increased this account by \$108 to include an invoice that was provided in our sample but not included in the general ledger.

Account 615 – Purchased Power

The Utility's general ledger reflects an amount of \$6,364 for this account. We increased this account by \$143 (\$47+\$96) to include a \$47 power bill that was provided in our sample but not included in the general ledger and to reclassify \$96 of power bills that were originally recorded in Account 618-Chemicals.

Account 618 – Chemicals

The Utility's general ledger reflects an amount of \$2,326 for this account. We decreased this account by \$90 (\$113-\$96-\$107) to, reclassify \$96 of power bills to Account 615-Purchased power, to remove three transactions totaling \$107 that were not supported, and, to include two invoices totaling \$113 that were provided in our sample but not included in the general ledger.

Account 620 – Materials and Supplies

The Utility's general ledger reflects an amount of \$14,757 for this account. We decreased this account by \$4,400 (\$1,805+\$2,595) to, reclassify \$1,805 to Account 331 Transmission & Distribution Mains for a 3 horse power booster pump installed at the water plant, and to reclassify \$2,595 to Account 336-Backflow Prevention Devices for a three inch backflow preventer that was installed at the Lake Placid water treatment plant. These were new additions, therefore no retirement was required.

Account 634 - Contractual Services Management

The Utility's general ledger reflects an amount of \$42,177 for this account. All management and routine maintenance services are provided by LB employees through established contracts for services described below.

Account 635 - Contractual Services Testing

The Utility's general ledger reflects an amount of \$6,346 for this account. Based on our audit work in this area no adjustment is needed.

Account 636 – Contractual Services Other

The Utility's general ledger reflects an amount of \$37,177 for this account. We decreased this account by \$720 to adjust an invoice totaling \$900 for pressure washing and painting the water tanks at a water treatment plant. Costs such as these should be recorded to Account 186-Miscellaneous Deferred Debits and amortized over five years per Rule 25-30.433 (8), - Rate Case Proceeding, F.A.C. We left \$180 in this account to include the first year's amortization expense (\$900/5). Additionally, a portion of the routine maintenance services are provided by LB employees through established contracts for services described below.

Account 641 – Rental of Building and Property

The Utility's general ledger reflects an amount of \$44,095 for this account. This includes \$27,826 in land leases for twenty-five well sites and \$16,339 for office space with office support and a truck lease. All rent is provided by LB within the scope of the established contracts for services described below.

Account 650 – Transportation Expense

The Utility does not have any transportation vehicles. All transportation is provided by LB within the scope of the established contracts for services described below.

Account 655 – Insurance Expense

No amount for insurance is included in this account. All insurance is provided by LB within the scope of the established contracts for services described below.

Account 670 - Bad Debt Expense

No amount for Bad Debt Expense is included in this account. LB is the Utility's primary customer and concerns of non payment are not an issue.

Account 675 – Miscellaneous Expense

The Utility's general ledger reflects an amount of \$2,908 for this account. Based on our audit work in this area no adjustment is need.

Contracts

The Utility has executed contracts for services and land leases of twenty-five well sites with LB Citrus and Ranch Divisions. We obtained and reviewed the contracts and traced the terms and rates within the contracts to the invoices provided to support the charges posted to the general ledger accounts above. Based on our audit work in this area no adjustment is need. However, we defer to the staff analyst the task of determining whether the fees and terms for contract services developed by LB are reasonable and justified for inclusion as operating expense for the instant proceeding.

O&M Summary

The Utility's O&M Expense should be reduced by \$4,959 to \$152,447, for the test year ended March 31, 2015. Our adjustments and test year end balance are displayed on Table 5-1.

The corresponding Working Capital adjustment for this proceeding is \$19,056, which represents 1/8th of test year O&M Expense, per Rule 25-30.433 (2), F.A.C.

Effect on the General Ledger: To be determined by the Utility.

Effect on the Filing: Operating and Maintenance Expense is \$152,447 for the test year ended March 31, 2015. The working capital adjustment for rate base is \$19,056.

Table 5-1

**Operation & Maintenance Expense
12-Months Ended December 31, 2014**

Acct. Nos.	Acct. Description	Per Utility	Adjustment	Per Audit
601	Salaries & Wages - Employees	\$0	\$0	\$0
610	Purchased Water	\$1,256	\$108	\$1,364
615	Purchased Power	\$6,364	\$143	\$6,507
618	Chemicals	\$2,326	(\$90)	\$2,235
620	Materials & Supplies	\$14,757	(\$4,400)	\$10,357
634	Contractual Services - Management	\$42,177	\$0	\$42,177
635	Contractual Services - Testing	\$6,346	\$0	\$6,346
636	Contractual Services - Other	\$37,177	(\$720)	\$36,457
641	Rental of Building/Real Property	\$44,095	\$0	\$44,095
650	Transportation Expense	\$0	\$0	\$0
655	Insurance Expense	\$0	\$0	\$0
665	Reg. Commission Expense	\$0	\$0	\$0
670	Bad Debt Expense	\$0	\$0	\$0
675	Miscellaneous Expense	\$2,908	\$0	\$2,908
Total		\$157,406	(\$4,959)	\$152,447

Finding 6: Taxes Other Than Income

Audit Analysis: The Utility’s general ledger reflects the following amounts for Taxes Other Than Income Expense for the test year ended March 31, 2015.

<u>NARUC Acct.</u>	<u>Description</u>	<u>Amount</u>
408 11000	Property Taxes	\$0
408 12000	License & Fees	\$1,180
408 13000	Regulatory Assessment Fees	\$1,979
Total		\$3,159

Property Taxes

In prior years the Utility posts a journal entry in March to record the allocated property taxes for each of the well sites, per the terms of the long-term land lease with Lykes Bros. Inc. This should have occurred in March 2015, within the current test year period. The Utility provided audit staff with the calculation and supporting documents for the journal entry that should have been recorded. The Utility’s property tax amount was \$1,282 in 2015. We reduced that amount by \$173 to remove property taxes associated with the Utility’s wastewater plant site lease. Therefore we have increased property taxes by \$1,109 (\$1,282 - \$173) for the test year.

License & Fees

The Utility’s general ledger reflects \$1,180 in this account for annual permit fees paid to Glades and Highlands Counties. Based on our audit work in this area no adjustment is need

Regulatory Assessment Fees (RAF)

The \$1,979 amount represents water and wastewater RAF’s paid by the Utility in 2014. We increased this amount by \$143 to \$2,122 which equals the RAFs associated with our Revenue amount in Finding 4 (\$47,162 x 4.50%).

We have increased TOTI by \$1,252 (\$1,109+\$143) to \$4,411 (\$3,159+\$1,252), for the test year ended March 31, 2015.

Effect on the General Ledger: To be determined by the Utility.

Effect on the Filing: Taxes Other Than Income Expense is \$4,411 for the test year ended March 31, 2015.

Finding 7: Information on Original Cost

Audit Analysis: The Utility's general ledger reflects the following balances posted to the general ledger in 2007 for the original cost of UPIS with a corresponding accumulated depreciation amount.

Acct.	Account Description	UPIS	Acc. Dep.
301	Org Costs-Intangible Plant-Water	\$170,938	(\$3,369)
307	Wells & Springs-Supply Plant-Water	\$178,867	(\$92,966)
311	Pumping Equip-Supply Plant-Water	\$5,572	(\$4,394)
320	Water Treat Equip-Water Treat Plant	\$17,694	(\$14,393)
330	Distrib Reservoirs-Trans/Dist Plant-Water	\$14,344	(\$7,634)
331	Trans/Distribution Mains-Trans/Dist Plant-Water	\$208,379	(\$83,099)
334	Meters/Meter Installations-Trans/Dist Plant-Water	\$10,329	\$0
Totals		\$606,123	(\$205,855)
Net Balance		\$400,268	

Rate base has never been established for the Utility in a Commission proceeding. All of the balances reflected above, except Organization Cost, represent the Utility's estimated value for the existing utility water system. These costs were included in its application for original water and wastewater certificates as filed in Docket No. 060726-WS. The balance for Organization Cost is substantially different than the \$40,000 originally requested in its initial application for rates in Docket No. 060726-WS, because it now includes the actual cost expended by the Utility to secure its original certificates and establish initial rates. We reviewed those costs for this proceeding and no exceptions were noted.

The Utility states that the original cost amounts were developed in-house based on the existing operating records of Lykes Bros. Inc. (LB) Citrus and Ranch Divisions. Documents provided by the Utility state that LB used an existing detailed inventory of all of the systems components that existed in 2005. LB employees, with well drilling experience, were used, along with conversations with company vendors, to develop estimated original cost values for each of the individual well systems being transferred to the Utility. The estimated values were then depreciated by a constant percentage over the life for each system. The depreciated original cost of \$232,699 for the systems was added to the actual net organization cost amount of \$167,569 (\$170,938-\$3,369) to establish a purchase price of \$400,268. The purchase price is supported by an executed bill of sale dated December 7, 2007, between LB and the Utility.

The Utility purchased similar assets from LB Citrus and Ranch Divisions in 2009, as referenced below. The Utility used the same methodology to determining the original cost to record the purchase in the general ledger.

Asset	UPIS	Acc. Dep.
Brighton Ranch Water Treatment Plant	\$349,622	\$0
Brighton Grove Water Treatment Plant	\$153,239	\$0
Lake Placid Water Treatment Plant	\$71,017	(\$25,902)
Dinner Lake Water Treatment Plant	\$2,885	(\$1,358)
Mulch Plant	\$61,344	\$0
Total	\$638,107	(\$27,260)

The Mulch Plant was subsequently sold in 2011 and UPIS was reversed by the same amount.

We reviewed the documents provided by the Utility and recalculated the depreciation accruals and ending balances for original cost balances displayed above without exceptions.

Effect on the General Ledger: None

Effect on the Filing: Provided as additional information for Staff to consider. We defer to the staff engineers the task of determining whether the original cost balances developed by LB for these purchases are reasonable and justified for determining the Utility's rate base for the instant proceeding. We have used them as our beginning balances and thus, are included in the Rate Base exhibit in this Report.

Finding 8: Information on Accumulated Depreciation

Audit Analysis: Silver Lake Utilities, Inc. is a Class C water and wastewater utility that filed for original certificates to provide water and wastewater service in Glades County and water service in Highlands County on November 3, 2006. Order No. PSC-07-0717-FOF-WS, issued September 7, 2007, in Docket No. 060726-WS, granted its request and issued Certificate Nos. 636-W and 546-S to serve the requested territory. Order No. PSC-07-0983-PAA-WS, in the same docket, approved initial rates and charges based on projected rate base, cost of capital, operating and maintenance expenses, and customer growth.

Order Nos. PSC-08-0520-FOF-WS, issued August 12, 2008 and PSC-09-0086-FOF-SU, in Docket Nos. 080213-WU and 080613-SU, respectively, granted a request to amend the original certificates and extend the service areas in Highlands County.

In 2010, based on planned growth in its service territory, the Utility believed a large capital investment and revenue growth would occur requiring a change from a class C to a class B utility. In anticipation of this change the Utility requested its accounting consultant to prepare its 2010 Annual Report reflecting an accumulated depreciation balance as if class B service lives were in place since the original certificates were granted.

The Utility's 2010 general ledger and Annual Report were adjusted to reflect this change. The Utility has continued using class B service lives to calculate depreciation accruals and annual depreciation expense through the test year ended March 31, 2015. The balances for accumulated depreciation and test year depreciation expense displayed in Finding 2 continue with the Utility's existing policy.

The anticipated customer growth and utility capital investments never occurred and no further expansion to the Utility's system or service territory are planned in the near future.

We prepared a schedule that calculates the Utility's accumulated depreciation balance, as of the test year ended March 31, 2015, had Class C service lives been in place since the Utility begun operations in 2007. Our schedule incorporates the adjustments to UPIS we made in Finding 1.

The adjustment to accumulated depreciation and test year depreciation expense, should the Commission require the Utility to resume the use of Class C service lives, is displayed in Tables 7-1 and 7-2.

Effect on the General Ledger: None

Effect on the Filing: Provided as additional information for Staff to consider.

Table 8-1

Acct. No.	Description	As of March 31, 2015			Simple Average
		Per Utility	Adjustment	Per Audit	
108 301	Organization Cost	(\$46,905)	\$12,197	(\$34,708)	(\$32,571)
108 304	Structures & Improv.	(\$20,124)	(\$6,372)	(\$26,496)	(\$24,425)
108 307	Wells & Springs	(\$159,079)	(\$12,898)	(\$171,977)	(\$167,023)
108 310	Power Generation Equip.	(\$14,639)	(\$2,808)	(\$17,447)	(\$15,950)
108 311	Pumping Equip.	(\$19,713)	(\$11,804)	(\$31,517)	(\$29,907)
108 320	Water Treatment Equip.	(\$78,378)	(\$22,332)	(\$100,710)	(\$93,371)
108 330	Dist., Reservoir & Standpipes	(\$12,045)	(\$638)	(\$12,683)	(\$12,314)
108 331	Transmission & Dist. Mains	(\$128,350)	(\$5,136)	(\$133,486)	(\$130,222)
108 334	Meters	(\$5,289)	(\$384)	(\$5,673)	(\$5,264)
108 336	Backflow Preventers	\$0	(\$130)	(\$130)	(\$65)
108 345	Power Operated Equip.	(\$296)	(\$59)	(\$355)	(\$324)
Total		(\$484,818)	(\$50,364)	(\$535,182)	(\$511,436)

Small differences are due to rounding.

Table 8-2

Acct. No.	Description	Test Year Ended March 31, 2015		
		Per Utility	Adjustment	Per Audit
403 301	Organization Cost	\$5,712	(\$1,439)	\$4,273
403 304	Structures & Improv.	\$3,500	\$641	\$4,141
403 307	Wells & Springs	\$8,908	\$1,000	\$9,908
403 310	Power Generation Equip.	\$2,546	\$449	\$2,995
403 311	Pumping Equip.	\$2,459	\$762	\$3,221
403 320	Water Treatment Equip.	\$10,550	\$4,130	\$14,680
403 330	Dist., Reservoir & Standpipes	\$599	\$0	\$739
403 331	Transmission & Dist. Mains	\$5,759	\$769	\$6,528
403 334	Meters	\$695	\$123	\$818
403 336	Backflow Preventers	\$0	\$130	\$130
403 345	Power Operated Equip.	\$51	\$10	\$62
Total		\$40,778	\$6,575	\$47,495

Small differences are due to rounding.

Finding 9: Information on Utility Infrastructure and Customer Base

Audit Analysis: The Utility served 62 customers at the end of the test year, March 31, 2015. Only one of the Utility's customers, Brighton Baptist Church, is a non-related entity that receives an individual monthly bill. The church is classified as a general service customer.

The remaining sixty-one residential and general service customers are combined and billed on two separate monthly bills, one identified as the Ranch Division and one identified as the Citrus Division.

The Utility has twenty-nine individual wells that supply raw water to twenty-seven water treatment plants (WTP) as identified below.

Three of the twenty-nine wells fall under the Florida Departments of Environmental Protection (FDEP) reporting jurisdiction.

- Lake Placid WTP
- Buckhorn Housing WTP
- Brighton Ranch WTP

Two of the twenty-nine wells provide a multi-service function for general service, residential service and raw water irrigation service. None of the customers in these two systems are individually metered. Usage is based on the master meter readings at the water plant site.

- Lake Placid WTP
- Brighton Grove WTP

Two of the WTP have two wells that supply raw water for treatment.

- Brighton Ranch
- Brighton Grove

Approximately seventeen of the twenty-nine systems are single wells with only one customer. In these instances the supply meter at the well is used to determine customer usage and is assumed to provide five-eighths inch metered service.

Effect on the General Ledger: None

Effect on the Filing: Provided as additional information for Staff to consider.

Exhibits

Exhibit 1: Rate Base

**Silver Lake Utilities, Inc.
Docket No.150149-WS
As of March 31, 2015**

Description	Per Utility @03/31/15	Adjustments	Per Audit @03/31/15	Test Year Average
Plant in Service	\$1,246,881	(\$53,126)	\$1,193,755	\$1,191,555
Land & Land Rights	\$0	\$0	\$0	\$0
Contributions in Aid of Construction	\$0	\$0	\$0	\$0
Accumulated Depreciation	(\$484,818)	(\$6,723)	(\$491,541)	(\$471,284)
Accumulated Amortization of CIAC	\$0	\$0	\$0	\$0
Working Capital	\$0	\$19,056	\$19,056	\$19,056
Total	\$762,063	(\$40,793)	\$721,270	\$739,327

Small differences are due to rounding.

Exhibit 2: Capital Structure

Silver Lake Utilities, Inc.
Docket No.150149-WS
As of March 31, 2015

Description	Per Utility @03/31/15	Audit Adjustments	Per Audit @03/31/15	Cost Rate	Ratio	Weighted Average Cost
Common Equity	\$370,892	(\$25,926)	\$344,966	10.58%	46.66%	4.94%
Long Term Debt	\$424,000	(\$29,639)	\$394,361	3.00%	53.34%	1.60%
Customer Deposits	\$0	\$0	\$0	2.00%	0.00%	0.00%
Total	\$794,892	(\$55,565)	\$739,327			6.54%

The ratio of debt to equity is 53.34 percent ($\$424,000 / (\$370,892 + \$424,000)$). We calculate a Return on Equity (ROE) rate of 10.58 percent, based on the Commissions' leverage graph calculation, approved in Order No. PSC-15-0259-WS, issued July 2, 2015. Audit adjustments reconcile the Capital Structure to the average rate base displayed in Exhibit 1.

Exhibit 3: Net Operating Income

Silver Lake Utilities, Inc.
Docket No.150149-WS
Twelve Months Ended March 31, 2015

Description	Per Utility	Adjustments	Per Audit
Operating Revenues	\$43,397	\$3,765	\$47,162
Operating Expenses			
Operation & Maintenance Expense	\$157,406	(\$4,959)	\$152,447
Depreciation Expense	\$40,778	(\$264)	\$40,514
CIAC Amortization Expense	\$0	\$0	\$0
Taxes Other Than Income Expense	\$3,159	\$1,252	\$4,411
Income Tax Expense (See note below)	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
Total Operating Expenses	\$201,343	(\$3,971)	\$197,372
Net Operating Income	(\$157,946)	\$7,736	(\$150,210)

The Utility's 2014 Federal Tax return reflects a Net Operating Loss Carryover balance of \$1,734,913. We do not believe that the Utility will present a positive taxable income any time in the near future. Therefore, we have set Income Tax Expense to \$0.