

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: February 10, 2016
TO: Office of Commission Clerk
FROM: Lynn M. Deamer, Chief of Auditing, Office of Auditing and Performance Analysis
RE: Docket No.: 150224-WU
Company Name: Pinecrest Utilities, LLC
Company Code: WU954
Audit Purpose: Staff Assisted Rate Case
Audit Control No.: 15-320-1-1

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/cm

Attachment: Copy of Letter

cc: Office of Auditing and Performance Analysis File

State of Florida



Public Service Commission

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

Auditor's Report

Pinecrest Utilities, LLC
Staff-Assisted Rate Case

Twelve Months Ended September 30, 2015

Docket No. 150224-WU
Audit Control No. 15-320-1-1
January 29, 2016

A handwritten signature in black ink, appearing to read "Debra M.", written over a horizontal line.

Debra Dobiac
Audit Manager

A handwritten signature in black ink, appearing to read "George Simmons", written over a horizontal line.

George Simmons
Audit Staff

A handwritten signature in blue ink, appearing to read "Lynn M. Deamer", written over a horizontal line.

Lynn M. Deamer
Reviewer

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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 November 12, 2015. We have applied these procedures to the attached schedules prepared by the audit staff in support of Pincrest Utilities, LLC's request for a Staff-Assisted Rate Case in Docket No.150224-WU.

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

General

Definitions

PCU/Utility refers to Pinecrest Utilities, LLC.

FUS1 refers to Florida Utility Services 1, LLC.

Test Year refers to the twelve months ended September 30, 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

Pinecrest Utility LLC is a Class C utility serving approximately 148 residential and two general service water customers in Polk County. Rate base and rates were last established by the Florida Public Service Commission (Commission) in Docket No. 120269-WU by Order No. PSC-13-0320-PAA-WU, issued August 13, 2013.

Mr. Smallridge owns Pinecrest Utilities, LLC; Holiday Gardens Utilities, LLC; Crestridge Utilities, LLC; Charlie Creek Utilities, LLC; and East Marion Utilities, LLC. He also manages West Lakeland Wastewater, Inc., Four Points Utility Corporation, Bimini Bay Utilities Corporation, and Lake Forest Utility. As of January 1, 2015, Mr. Smallridge has been recording common costs on FUS1's books. Common costs include salaries, employee benefits, rent, electric, telephone, internet, transportation, material and supplies, office supplies, and postage. These costs were allocated among all the utilities based on customer count.

Mr. Smallridge files a Form 1040, which includes Schedule C – Profit or Loss from Business. One of these schedules represented Pinecrest Utilities, LLC.

Utility Books and Records

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

Procedures: 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 into service, and 4) Adjustments required in the Utility's last rate proceeding were recorded in its books and records.

Procedures: We reconciled the beginning balances for UPIS, as of September 30, 2012 from Order No. PSC-13-0320-PAA-WU to the general ledger. We scheduled UPIS activity from September 30, 2012 through September 30, 2015. We traced asset additions to supporting documentation. We ensured that retirements were made when an asset was removed or replaced. We examined related party transactions with other utilities owned or managed by Mr. Smallridge including the common plant for Office Furniture and Equipment, Transportation, and Tools, Shop and Garage Equipment. We determined the year-end and simple average balances as of September 30, 2015. Findings 1 and 3 discuss our recommended adjustments to UPIS.

Land & Land Rights

Objectives: The objectives were to determine whether the utility land is: 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 case proceeding were recorded in its books and records.

Procedures: We reconciled the beginning balances for land, as of September 30, 2012 from Order No. PSC-13-0320-PAA-WU to the general ledger. We scheduled land activity from September 30, 2012 through September 30, 2015. We verified that the land is owned by the Utility and determined that there have been no changes to the Utility's cost of land since the last rate case. We determined the year-end and simple average balances as of September 30, 2015. 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 in its books and records.

Procedures: We reconciled the beginning balances for accumulated depreciation, as of September 30, 2012 from Order PSC-13-0320-PAA-WU to the general ledger. We calculated annual accruals to accumulated depreciation using the depreciation rates established by Rule 25-30.140(2), F.A.C., from September 30, 2012 to September 30, 2015. We determined the year-end and simple average balances as of September 30, 2015. Findings 2 and 3 discuss our recommended adjustments to accumulated depreciation.

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 in the Utility's last rate proceeding were recorded to its books and records.

Procedures: We reconciled the beginning balances for CIAC, as of September 30, 2012 from Order No. PSC-13-0320-PAA-WU to the general ledger. We noted that there were no additions

to CIAC since the last rate proceeding. We determined the year-end and simple average balances as of September 30, 2015. No exceptions were noted.

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 reconciled the beginning balances for amortization of CIAC, as of September 30, 2012 from Order PSC-13-0320-PAA-WU to the general ledger. We calculated annual accruals to accumulated amortization of CIAC using the depreciation rates established by Rule 25-30.140(2), F.A.C., from September 30, 2012 to September 30, 2015. We determined the year-end and simple average balances as of September 30, 2015. Finding 4 discusses our recommended adjustment to accumulated amortization of CIAC.

Working Capital

Objectives: The objective was to determine whether the Utility’s working capital balance is properly calculated in compliance with Commission rules.

Procedures: We calculated the Utility’s working capital balance as of September 30, 2015 using one-eighth of operation and maintenance expense as required by Rule 25-30.433 (2), F.A.C. Findings 9 and 10 discuss our recommended adjustment to working capital.

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 determined that the Utility’s capital structure consists of common equity, long-term debt, and customer deposits. We determined the year-end and simple average Capital Structure balance and its weighted average cost as of September 30, 2015. Findings 5, 6, and 7 discuss our recommended adjustments to the capital structure.

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 September 30, 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 also determined the number of miscellaneous service charges by type. We calculated

miscellaneous service charges by multiplying the Commission approved tariff by the number we determined and traced the amounts to the general ledger. Finding 8 discusses our recommended adjustment to operating revenues.

Operation and Maintenance Expense

Objectives: The objectives were to determine whether operation and maintenance expenses (O&M) are: 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 the invoices provided in support of the Utility's O&M expense for the test year. 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. We examined related party transactions with other utilities owned or managed by Mr. Smallridge including the employee salaries from FUS1. We have determined the most recent costs that are common to all the utilities and calculated an allocation percentage based on number of customers. Findings 9, 10, 11, and 12 discuss our recommended adjustments to O&M expense.

Depreciation and Amortization

Objectives: The objectives were to determine whether the Utility's depreciation and CIAC amortization expense is properly calculated using the Commission authorized rates.

Procedures: We compiled a schedule from audited UPIS items and recalculated depreciation based on depreciation rates authorized by Rule 25-30.140, F.A.C. for the test year. We also recalculated amortization of CIAC using Commission approved rates for the test year. Findings 2 and 3 discuss our recommended adjustments to depreciation expense.

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 NARUC USOA.

Procedures: We scheduled TOTI based on documentation provided by the Utility. We included property taxes and regulatory assessment fees (RAF) for the test year and confirmed their utility classification. We recalculated RAFs using the approved RAF rate and the audited revenue balances. In addition we calculated the allocated payroll taxes based on the employee salaries from FSU1 using the Social Security rate and the Medicare rate. Finding 13 discusses our recommended adjustments to TOTI.

Audit Findings

Finding 1: Utility Plant in Service

Audit Analysis: According to the Utility's general ledger, the UPIS balance was \$215,438 as of September 30, 2015. Audit staff determined the UPIS balance to be \$219,677. We noted the following.

1. The simple average plant balances were recorded as the adjustments from Order No. PSC-13-0320-PAA-WU. The test year-end balances should have been recorded.
2. The Utility had recorded the proforma adjustment of \$1,861 although the project had never been completed.
3. The adjustments were recorded as of January 1, 2012 when the end of the test year had been September 30, 2012.

The utility plant is understated by \$4,239 as shown in Table 1-1.

Table 1-1

Account - Description	Utility Balance 9/30/2015	Audit Adjustments	Audit Balance 9/30/2015	Simple Average
301 Organization	\$ -	\$ -	\$ -	\$ -
303 Land	6,500	-	6,500	6,500
304 Structures & Improvements	5,822	(69)	5,753	5,753
307 Wells & Springs	24,869	-	24,869	24,869
309 Supply Mains	3,003	162	3,165	3,165
310 Power Generation Equip.	-	-	-	-
311 Pumping Equip.	11,192	-	11,192	11,192
320 Water Treatment Equip.	4,380	3,750	8,130	8,130
330 Distribution Reservoirs	11,448	1,039	12,487	12,487
331 Transmission and Distribution Mains	100,736	-	100,736	100,736
333 Services	15,363	-	15,363	15,363
334 Meters and Meter Install.	23,681	(643)	23,038	22,897
335 Hydrants	8,444	-	8,444	8,444
339 Other Plant And Misc.	-	-	-	-
Total:	\$ 215,438	\$ 4,239	\$ 219,677	\$ 219,536

The UPIS balances above do not include allocated common plant. See Finding 3.

Effect on the General Ledger: The following entry is needed to correct the general ledger as of September 30, 2015.

NARUC	Description	Debit	Credit
101	304 Structures & Improvements		\$ 69
101	309 Supply Mains	\$ 162	
101	320 Water Treatment Equip.	\$ 3,750	
101	330 Distribution Reservoirs	\$ 1,039	
101	334 Meters and Meter Install.		\$ 643
	TBD Equity		\$ 4,239

Effect on Staff Prepared Exhibits: Audit staff determined UPIS to be \$219,677, and the simple average UPIS to be \$219,536 as of September 30, 2015.

Finding 2: Accumulated Depreciation and Depreciation Expense

Audit Analysis: According to the Utility’s general ledger, the accumulated depreciation balance was \$121,989 as of September 30, 2015 and test year depreciation expense was \$7,168. We noted that accumulated depreciation and depreciation expense only gets recorded once a year at December 31st and nothing has been booked for 2015. Audit staff recalculated accumulated depreciation and depreciation expense using the audited UPIS plant balances and the depreciation rates established by Rule 25-30.140(2), F.A.C. as shown in Table 2-1.

Table 2-1

Account - Description	Audit Balance		Audit Balance
	Accum Dep 9/30/2015	Simple Average	Depreciation 9/30/2015
108/403 304 Structures & Improvements	\$ 5,492	\$ 5,385	\$ 213
108/403 307 Wells & Springs	12,309	11,849	920
108/403 309 Supply Mains	2,456	2,406	99
108/403 310 Power Generation Equip.	-	-	-
108/403 311 Pumping Equip.	11,192	11,192	-
108/403 320 Water Treatment Equip.	2,916	2,677	478
108/403 330 Distribution Reservoirs	10,193	10,004	378
108/403 331 Transmission and Distribution Mains	60,894	59,569	2,649
108/403 333 Services	11,649	11,430	439
108/403 334 Meters and Meter Install.	15,514	14,841	1,346
108/403 335 Hydrants	4,231	4,126	211
108/403 339 Other Plant And Misc.	-	-	-
Total:	\$ 136,846	\$ 133,479	\$ 6,733
Utility balance - 9/30/2015:	121,989		7,168
Audit Adjustment:	\$ 14,857		\$ (435)

The balances above do not include accumulated depreciation and depreciation expense for allocated common plant. See Finding 3.

Effect on the General Ledger: The following entry is needed to correct the general ledger as of September 30, 2015. Since the books are closed, depreciation expense should be booked to retained earnings.

NARUC	Description	Debit	Credit
TBD	Equity	\$ 14,857	
108	Accumulated Depreciation		\$ 14,857

Effect on Staff Prepared Exhibits: Audit staff determined accumulated depreciation and depreciation expense to be \$136,846 and \$6,733, respectively for the test year ended September 30, 2015. We also determined the simple average for accumulated depreciation to be \$133,479.

Finding 3: Allocated Common Plant

Audit Analysis: According to the Utility’s general ledger, allocated plant had been incorrectly recorded using the simple average balance of \$1,589 in Account 354 – Structures and Improvements. Since rates were last established in Docket No. 120269-WU, Mr. Smallridge has increased the number of utilities he owns or manages from six to nine, which has reduced the percent allocated to PCU. Finding 11 discusses the current allocation methodology. In addition, all of the previously approved allocated assets have been retired or replaced. Based on supporting invoices, audit staff has recalculated allocated plant as shown in Table 3-1.

Table 3-1

Account - Description	Audit Balance	Simple	Accum Dep	Simple	Depreciation
	9/30/2015	Average	9/30/2015	Average	9/30/2015
340 Office Furniture & Equip.	\$ 1,349	\$ 1,781	\$ (279)	\$ 26	\$ 254
341 Trans. Equip.	20,301	11,651	(2,426)	(1,899)	1,946
343 Tools, Shop and Garage Equip.	120	554	(720)	(245)	41
	<u>\$ 21,770</u>	<u>\$ 13,986</u>	<u>\$ (3,426)</u>	<u>\$ (2,118)</u>	<u>\$ 2,241</u>
Pinecrest Allocation at 6%	1,229	790	(193)	(120)	127
345 Power Operated Equip.	4,000	4,000	(857)	(1,057)	400
Pinecrest Allocation at 100%	<u>\$ 4,000</u>	<u>\$ 4,000</u>	<u>\$ (857)</u>	<u>\$ (1,057)</u>	<u>\$ 400</u>
Total:	<u>\$ 5,229</u>	<u>\$ 4,790</u>	<u>\$ (1,050)</u>	<u>\$ (1,176)</u>	<u>\$ 527</u>
Utility balance - 9/30/2015:	-	-	-	-	-
Audit Adjustment:	<u>\$ 5,229</u>		<u>\$ (1,050)</u>		<u>\$ 527</u>

Effect on the General Ledger: The following entry is needed to correct the general ledger as of September 30, 2015.

NARUC Description	Debit	Credit
101 340 Office Furniture & Equip.	\$ 76	
101 341 Trans. Equip.	\$ 1,146	
101 343 Tools, Shop and Garage Equip.	\$ 7	
101 345 Power Operated Equip.	\$ 4,000	
108 Accumulated Depreciation	\$ 1,050	
403 Depreciation Expense	\$ 527	
TBD Equity		\$ 6,806

Effect on Staff Prepared Exhibits: Audit staff determined UPIS to be \$5,229, and the simple average UPIS to be \$4,790 as of September 30, 2015. We determined accumulated depreciation and depreciation expense to be \$1,050 and \$527, respectively for the test year ended September 30, 2015. We also determined the simple average for accumulated depreciation to be \$4,790.

Finding 4: Accumulated Amortization of CIAC

Audit Analysis: According to the Utility’s general ledger, the accumulated amortization of CIAC balance was \$75,736 as of September 30, 2015. We noted that accumulated amortization of CIAC only gets recorded by the Utility once a year on December 31st. We also noted that the simple average balance for accumulated amortization of CIAC was recorded when the adjustments from Order No. PSC-13-0320-PAA-WU were booked. Audit staff recalculated accumulated amortization of CIAC using the CIAC balances and the depreciation rates established by Rule 25-30.140(2), F.A.C. as shown in Table 4-1.

Table 4-1

Account - Description	Audit Balance	
	Accum Amort 9/30/2015	Simple Average
272 304 Structures & Improvements	\$ 184	\$ 179
272 307 Wells & Springs	3,866	3,781
272 309 Supply Mains	446	438
272 310 Power Generation Equip.	-	-
272 311 Pumping Equip.	2,352	2,278
272 320 Water Treatment Equip.	-	-
272 330 Distribution Reservoirs	-	-
272 331 Transmission and Distribution Mains	57,489	56,531
272 333 Services	12,279	12,060
272 334 Meters and Meter Install.	-	-
272 335 Hydrants	3,328	3,275
272 339 Other Plant And Misc.	-	-
Total:	\$ 79,944	\$ 78,541
Utility balance - 9/30/2015:	75,736	
Audit Adjustment:	\$ 4,208	

Since no additions have been recorded to CIAC, no adjustment to amortization expense was required.

Effect on the General Ledger: The following entry is needed to correct the general ledger as of September 30, 2015.

NARUC	Description	Debit	Credit
272	Accumulated Amortization of CIAC	\$ 4,208	
TBD	Equity		\$ 4,208

Effect on Staff Prepared Exhibits: Audit staff determined accumulated amortization of CIAC to be \$79,944, and the simple average accumulated amortization of CIAC to be \$78,541 as of September 30, 2015.

Finding 5: Common Equity

Audit Analysis: According to the Utility's general ledger, common equity was a debit balance of \$26,442 (\$9,900 + \$16,541) as of September 30, 2015. Account 218 – Proprietary Capital had a debit balance of \$9,900, which consisted of the journal entries to record the adjustments to the transfer balances approved in Order No. PSC-12-0475-PAA-WU, Docket No. 110311-WU, issued September 18, 2012 when Mr. Smallridge originally purchased PCU. Account 32000 – Members Equity had a debit balance of \$16,541, which consisted of year-end closing entries as well as the journal entries to record the adjustments approved in Order No. PSC-13-0320-PAA-WU. These journal entries were recorded incorrectly because rate base was adjusted to the simple average balances instead of the test year-end balances as of September 30, 2012 including an adjustment for working capital.

Since including negative equity in the capital structure would penalize the Utility by understating the overall rate of return, the negative equity was adjusted to zero.

Effect on the General Ledger: The Utility should determine the effect on the general ledger.

Effect on Staff Prepared Exhibits: Audit staff determined that the year-end and the simple average common equity balances were adjusted to zero as of September 30, 2015.

Finding 6: Long-Term Debt

Audit Analysis: According to the Utility’s general ledger, the long-term debt balance was \$45,424 as of September 30, 2015. Based on the loan amortization schedules, audit staff determined the long-term debt balance to be \$44,580 as shown in Table 6-1.

Table 6-1

Account - Description	Audit Balance 9/30/2014	Audit Balance 9/30/2015	Simple Average
224.1 LTD - Center State Bank Loan	\$ (38,580)	\$ (33,196)	\$ (35,888)
224.3 LTD - Old FL National	\$ (3,863)	\$ (577)	\$ (2,220)
224.4 LTD - Mike Smallride	\$ (13,763)	\$ (10,807)	\$ (12,285)
Total Per Audit:	\$ (56,206)	\$ (44,580)	\$ (50,393)
Utility Balance:	\$ (56,206)	\$ (45,424)	\$ (50,815)
Audit Adjustment:	\$ -	\$ 844	\$ 422

Effect on the General Ledger: The Utility should determine the effect on the general ledger.

Effect on Staff Prepared Exhibits: Audit staff determined long-term debt to be \$44,580, and the simple average long-term debt to be \$50,393 as of September 30, 2015.

Finding 7: Customer Deposits

Audit Analysis: According to the Utility's general ledger, the customer deposit balance was \$1,628 as of September 30, 2015. Audit staff determined customer deposits to be \$2,959 by reviewing the deposit log. We noted that the Utility pays two percent interest on deposits when a refund check is issued. We also noted that the Utility refunds the deposits within the time frame allotted by Rule 25-30.311, F.A.C.

The Utility's customer deposits' are understated by \$1,331 as shown in Table 7-1.

Table 7-1

<u>Account - Description</u>	<u>Audit Balance</u> <u>9/30/2014</u>	<u>Audit Balance</u> <u>9/30/2015</u>	<u>Simple</u> <u>Average</u>
235 - Customer Deposits	\$ (1,792)	\$ (2,959)	\$ (2,376)
Total:	\$ (1,792)	\$ (2,959)	\$ (2,376)
Utility Balance:	\$ (1,804)	\$ (1,628)	\$ (1,716)
Audit Adjustment:	\$ 12	\$ (1,331)	\$ (660)

Audit staff noted that the Utility is still collecting initial deposits of \$64. However, the current tariff rate is \$67, which went into effect August 13, 2013.

Effect on the General Ledger: The Utility should determine the effect on the general ledger.

Effect on Staff Prepared Exhibits: Audit staff determined customer deposits to be \$2,959, and the simple average customer deposits to be \$2,376 as of September 30, 2015.

Finding 8: Operating Revenue

Audit Analysis: The Utility's operating revenue amount was \$57,811 for the twelve months ended September 30, 2015. However, audit staff recalculated revenue by determining the number of bills and gallons consumed from the billing register as well as the number of miscellaneous service charges times the Commission approved tariff rates. The Utility correctly applied the tariffs for miscellaneous service charges. Audit Staff determined operating revenue to be \$57,327 as shown in Table 8-1.

Table 8-1

NARUC	Description	Utility Balance 9/30/2015	Audit Adjustments	Audit Balance 9/30/2015
461.1	Residential Revenues	\$ 53,438	(1,189)	\$ 52,249
461.2	Commercial Revenues	\$ -	337	\$ 337
		\$ 53,438	\$ (852)	\$ 52,585
474.1	Late Fees	\$ 2,332	(88)	\$ 2,244
474.3	Reconnection Fees	\$ 741	54	\$ 795
474.4	Connection Fees	\$ -	420	\$ 420
474.5	Credit Card Fees	\$ 1,300	(17)	\$ 1,283
		\$ 4,373	\$ 369	\$ 4,742
Grand Total		\$ 57,811	\$ (484)	\$ 57,327

Note: Acct 474.3 - Reconnection Fees include premise visits

Effect on the General Ledger: The Utility should determine the effect on the general ledger.

Effect on Staff Prepared Exhibits: Audit staff determined the operating revenues to be \$57,327 for the test year ended September 30, 2015.

Finding 9: Operations and Maintenance Expense

Audit Analysis: The Utility's direct O&M expense amount was \$25,396 for the twelve months ended September 30, 2015. However, audit staff reviewed all expenses to determine if the transactions were made in the proper period, amount, classification, and whether the expenses were utility related. Audit staff determined direct O&M expenses to be \$18,614 as shown in Table 9-1.

Table 9-1

Direct Costs		Per Utility		Per Audit
Acct. Nos.	Acct. Description	9/30/2015	Adjustment	9/30/2015
615	Purchased Power	\$ 2,307	\$ (40)	\$ 2,267
618	Chemicals	1,810	-	1,810
620	Materials & Supplies	39	-	39
631	Contractual Services - Professional	4,093	-	4,093
635	Contractual Services - Testing	4,387	(1,400)	2,987
636	Contractual Services - Other	688	-	688
655	Insurance Expense	4,616	(557)	4,059
665	Reg. Commission Expense	2,752	(2,752)	-
670	Bad Debt Expense	451	-	451
675	Miscellaneous Expense	4,253	(2,032)	2,220
Total		\$ 25,396	\$ (6,782)	\$ 18,614
Working Capital Adjustment		\$ 3,175	\$ (848)	\$ 2,327

Based on the review of supporting documentation, the adjustments that follow were made to the test year expenses.

1. We removed late fees of \$40 from Account 615 – Purchased Power to Account 426 – Non-utility expenses.
2. Account 635 – Contractual Services – Testing included \$2,100 for testing of drinking water facilities. Since these tests are required every three years, this amount should be amortized over this time period at an amount of \$700 per year. Therefore, \$1,400 (\$700 x 2 years) was removed and transferred to a deferred account.
3. For Account 655 – Insurance Expense, we reclassified \$326 to Account 604 – Employee Benefits for health insurance premiums. We also removed a 2014 year-end adjusting journal entry debit of \$231 because a portion of the adjustment was for out of period items.
4. For Account 665 – Regulatory Commission Expense, we reclassified \$139 to Account 675 – Miscellaneous Expense for the 2015 Annual Report to the Florida Department of State and Regulatory Assessment Fees of \$2,613 to Account 408 – TOTI.
5. For Account 675 – Miscellaneous Expenses, we removed \$403 for unsupported items and reclassified them to Account 426 – Non-utility expenses. We increased the account by \$139 from Account 665 – Regulatory Commission Expense. We increased credit card fees by \$62 for an unrecorded expense item. We removed \$1,830 and reclassified it to

Account 427 – Interest Expense. This represents a decrease of \$2,032 ($-\$403 + \$139 + 62 - \$1,830$) to Account 675.

Effect on the General Ledger: Since the books are already closed, there is no effect on the general ledger.

Effect on Staff Prepared Exhibits: Audit staff determined that direct O&M expense to be \$18,614 and working capital to be \$2,327 for the test year ended September 30, 2015.

Finding 10: Allocated Common Operations and Maintenance Expense

Audit Analysis: The Utility's allocated O&M expense amount was \$23,824 for the twelve months ended September 30, 2015. Audit staff reviewed all expenses to determine if the transactions were made in the proper period, amount, classification, and whether the expenses were utility related. We also reviewed how the expenses were allocated from FUS1. Finding 11 discusses the applied allocation method. Audit staff determined allocated O&M expenses to be \$23,066 as shown in Table 10-1.

Table 10-1

Acct. Nos.	Acct. Description	Per Utility 9/30/2015	Audit Adjustment	Per Audit 9/30/2015
601	Salaries & Wages - Employees	\$ 9,153	\$ -	\$ 9,153
603	Salaries & Wages - Officers	4,890	-	4,890
604	Employee Pension & Benefits	1,472	-	1,472
620	Materials & Supplies	3,166	(1,046)	2,120
636	Contractual Services - Other	2,621	(2,579)	43
640	Rent	(5,082)	6,031	949
650	Transportation Expense	2,608	(630)	1,978
675	Miscellaneous Expense	4,995	(2,534)	2,461
Total		\$ 23,824	\$ (758)	\$ 23,066
Working Capital Adjustment		\$ 2,978	\$ (95)	\$ 2,883

Based on the review of FUS1's allocation methodology and supporting documentation, the adjustments that follow were made to the test year expenses.

1. For Account 620 – Material & Supplies, we removed \$463 because this amount consisted of transportation, office supplies and postage. We reclassified \$164 to Account 650 – Transportation and the balance of \$299 to Account 675 – Miscellaneous Expenses. We noted that in March 2015, FUS1 was allocating the cost of repairs across all of the utilities owned or managed by Mr. Smallridge. We reviewed the supporting invoices and removed \$583 from Account 620 – Materials and Supplies for items that were not related to PCU. This represents a decrease of \$1,046 (\$463 + \$583) to Account 620 – Material & Supplies.
2. For Account 636 – Contractual Services - we removed a 2014 year-end adjusting journal entry debit of \$779 because a portion of the adjustment was for out of period items. We also removed the mowing allowance of \$1,800 since Mr. Smallridge does the mowing and his salary is already reflected with the allocated expenses from the common office. This represents a decrease of \$2,579 (\$779 + \$1,800) to Account 636 – Contractual Services.
3. In 2014, all the allocated common office expense was recorded in Account 640 – Rent. In December, a year-end adjusting journal entry was recorded to reclassify the expenses to the proper accounts. We removed the 2014 year-end adjusting journal entry credit of \$5,846 because a portion of the adjustment was for out of period items. We then

increased rent expense by \$185 based on the rental agreement for the new office that FUS1 moved into during January 2015. This represents an increase of \$6,031 (\$5,846 + \$185) to Account 640 - Rent.

4. For Account 650 – Transportation expense, we removed a 2014 year-end adjusting journal entry debit of \$1,323 because a portion of the adjustment was for out of period items. We reclassified \$431 from Account 640 – Rent. We reclassified \$164 from Account 620 – Materials & Supplies. We removed \$186 because FUS1 had been allocating a truck loan payment to all of the utilities owned or managed by Mr. Smallridge. We increased transportation expense by \$284, which reflects the allocated portion of the vehicle insurance on the two trucks owned by FUS1. The net effect of these adjustments is a decrease of \$630 ($-\$1,323 + \$431 + \$164 - \$186 + \284).
5. For Account 675 – Miscellaneous Expenses, we removed a 2014 year-end adjusting journal entry debit of \$2,587 because a portion of the adjustment was for out of period items. We increased this account by \$299, which had originally been recorded in Account 620 – Materials and Supplies. We removed \$28 because this amount represented expense that should have only been allocated to East Marion. This account also included allocating the cost of employees’ working lunches to all of the utilities owned or managed by Mr. Smallridge. We removed \$90 and reclassified it to Account 426 – Non-utility expenses. We removed the \$128 expense of rental equipment because it wasn’t used at PCU. The net effect of these adjustments is a decrease of \$2,534 ($-\$2,587 + \$299 - \$28 - \$90 - \128).

Effect on the General Ledger: Since the books are already closed, there is no effect on the general ledger.

Effect on Staff Prepared Exhibits: Audit staff determined that allocated O&M expense to be \$23,066 and working capital to be \$2,883 for the test year ended September 30, 2015.

Finding 11: Allocation Methodology

Audit Analysis: During the review of FUS1’s allocation schedules, audit staff noted that there were inconsistencies in the allocation method applied from month to month. We obtained the customer counts for each of the utilities that are owned or managed by Mr. Smallridge as of September 30, 2015. We compiled the allocation percentages used by the Utility in Table 11-1.

Table 11-1

Utility	Salary allocations -9/30/2015		Rent allocations - 9/30/2015	
	Number of Customers	All Employees	Number of Customers	Allocated Expenses
Holiday Gardens	446	20%	446	20%
Crestridge	597	26%	597	26%
West Lakeland	307	14%	307	14%
Pinecrest Utilities	128	6%	128	6%
Lake Forest Utilities	61	3%	61	3%
Charlie Creek Utilities	152	7%	152	7%
East Marion Utilites	103	5%	103	5%
Four Points Utilities	276	12%	276	12%
Bimini Bay Utilities	197	9%	197	9%
	2267	100%	2267	100%

Audit staff reviewed all of the transactions that were ultimately allocated to all nine utilities. Based on supporting documentation and using the six percent for PCU, we made adjustments to allocated expenses as reported in Finding 10.

We also performed an analysis to determine whether using Equivalent Residential Connections (ERCs) as an allocation methodology would be more useful as more systems are acquired. As Mr. Smallridge purchases more systems, we believe that the use of ERCs as the primary factor in allocating costs would be spread more equitably across the Utilities.

However, audit staff used the customer counts in this proceeding.

Effect on the General Ledger: This is for informational purposes only.

Effect on Staff Prepared Exhibits: This is for informational purposes only.

Finding 12: Bad Debt Expense

Audit Analysis: According to the Utility's most recent accounts receivable aging report, the accounts over 120 days past due balance was \$4,742 or 46 percent of the accounts receivable balance. The Utility's tariff does allow for the offset of a past due balance with a customer's deposit. During the review of the Utility's billing register, audit staff noted rather large outstanding balances which date back to 2011 to 2013.

Customer deposits were \$2,959 as of September 30, 2015, which is not adequate to cover the Utility's past due balance on an ongoing basis. The Utility's current bad debt policy is to write-off the remaining balance of an account after the deposit has been applied and recorded \$451 of bad debt expense during the test year.

We did not adjust the \$451 of bad debt expense included in the direct O&M expenses and we defer this issue to the analyst.

Effect on the General Ledger: None.

Effect on Staff Prepared Exhibits: We defer this issue to the analyst.

Finding 13: Taxes Other than Income

Audit Analysis: According to the Utility’s general ledger, the TOTI balance was \$41 as of September 30, 2015. Audit staff determined that the TOTI balance was \$3,599 as shown in Table 13-1.

Table 13-1

Acct. Nos.	Acct. Description	Per Utility		Per Audit
		9/30/2015	Adjustment	9/30/2015
408.1	Taxes - Other - Public Service tax	\$ 41	\$ (41)	\$ -
408.2	Payroll Taxes	-	1,019	1,019
408.3	Regulatory Assessment Fee	-	2,580	2,580
Total		\$ 41	\$ 3,558	\$ 3,599

Based on the review of supporting documentation, the adjustments that follow were made to the test year expenses.

1. We removed \$41 from Account 408.1 – Taxes-Other because this amount was the PCU allocated portion from FUS1 relating to a loan’s closing costs, a campaign contribution, and a vehicle registration renewal. We removed the first two items because they cannot be passed on to the ratepayers and we reclassified the vehicle registration to allocated transportation expense.
2. We increased Account 408.2 – Payroll Taxes by \$1,019 because this amount was originally recorded with the allocated salary expense.
3. We increased Account 408.3 – Regulatory Assessment Fees by \$2,580 (\$2,613 - \$33). The Utility had incorrectly recorded RAF of \$2,613 in Account 665 – Regulatory Commission Expense. We then adjusted RAF by \$33 based on the audited test year revenues.
4. PCU does not pay any property taxes. We obtained documentation from Polk County Property Appraiser’s website, which verified that no taxes were assessed.

Effect on the General Ledger: Since the books are already closed, there is no effect on the general ledger.

Effect on Staff Prepared Exhibits: Audit staff determined the TOTI to be \$3,599 for the test year ended September 30, 2015.

Exhibits

Exhibit 1: Rate Base

PINECREST UTILITIES LLC
STAFF-ASSISTED RATE CASE
DOCKET NO. 150224-WU; ACN 15-320-1-1
SCHEDULE OF WATER RATE BASE
AS OF SEPTEMBER 30, 2015

Description	Balance Per Utility as of September 30, 2015	Audit Adjustment	Audit Finding	Balance Per Audit as of September 30, 2015	Test Year Average
Utility Plant in Service	\$ 208,938	\$ 4,239	1	\$ 213,177	\$ 213,036
Utility Plant in Service - Allocated	\$ -	\$ 5,229	3	\$ 5,229	\$ 4,790
Land & Land Rights	\$ 6,500	\$ -		\$ 6,500	\$ 6,500
Accumulated Depreciation	\$ (121,989)	\$ (14,857)	2	\$ (136,846)	\$ (133,479)
Accumulated Depreciation - Allocated	\$ -	\$ 1,050	3	\$ 1,050	\$ 1,176
Contributions in Aid of Construction	\$ (100,352)	\$ -		\$ (100,352)	\$ (100,352)
Accumulated Amortization of CIAC	\$ 75,736	\$ 4,208	4	\$ 79,944	\$ 78,541
Working Capital Allowance	\$ 3,175	\$ (848)	9	\$ 2,327	\$ 2,327
Working Capital Allowance - Allocated	\$ 2,978	\$ (95)	10	\$ 2,883	\$ 2,883
Total Rate Base	\$ 74,986	\$ (979)		\$ 73,912	\$ 75,422

Exhibit 2: Capital Structure

PINECREST UTILITIES LLC
STAFF-ASSISTED RATE CASE
DOCKET NO. 150224-WU; ACN 15-320-1-1
SCHEDULE OF CAPITAL STRUCTURE
AS OF SEPTEMBER 30, 2015

Capital Components	Test Year Avg.	Audit Adjs.	Audit Finding	Audit Adj. Balance	% of Components	Rate Base	% of Rate Base	Rate	Composite Rate
Long Term Debt	\$ 50,815	\$ (422)	6	\$ 50,393	100.00%	\$ 73,046	96.85%	6.77%	6.56%
Equity	\$ (24,447)	\$ 24,447	5	\$ -	0.00%	\$ -	0.00%	11.16%	0.00%
Total Equity and Debt	\$ 26,368	\$ 24,025		\$ 50,393	100.00%	\$ 73,046			
Customer Deposits	\$ 1,716	\$ 660	7	\$ 2,376		\$ 2,376	3.15%	2%	0.06%
Total	\$ 28,084	\$ 24,685		\$ 52,769		\$ 75,422	100.00%		6.62%

Exhibit 3: Net Operating Income

**PINECREST UTILITIES LLC
 STAFF-ASSISTED RATE CASE
 DOCKET NO. 150224-WU; ACN 15-320-1-1
 SCHEDULE OF WATER NET OPERATING INCOME
 FOR TEST YEAR ENDED SEPTEMBER 30, 2015**

Description	Balance per Utilitiy 9/30/2015	Audit Adjustments	Audit Finding	Balance per Audit 9/30/2015
Operating Revenues	\$ 57,811	\$ (484)	8	\$57,327
O&M Expenses	25,396	(6,782)	9	18,614
O&M Expenses - Allocated	23,824	(758)	10	23,066
Depreciation Expense	7,168	(435)	2	6,733
Depreciation Expense - Allocated	-	527	3	527
Amoritization Expense	(2,806)	-		(2,806)
Taxes Other than Income	41	3,558	13	3,599
Income Tax Expense	-	-		-
Total Operating Expenses:	\$ 53,623	\$ (3,890)		\$ 49,733
Net Operating Income (Loss)	\$ 4,188	\$ 3,407		\$ 7,595