

HARTMAN & ASSOCIATES, INC.

ORIGINAL

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August 5, 1998

HAI#96-459.01

Ms. Blanca S. Bayo
Division of Records & Reporting
Florida Public Service Commission
Capital Circle Office Center
2540 Shumard Oak Blvd.
Tallahassee, Florida 32399-0850

**Subject: Docket No. 980307 - WS - Zellwood Station Co-Op, Inc.
Audit Report - Establish Rate Base - Period Ended December 31, 1998
Audit Control # 98-095-3-1**

Dear Ms. Bayo:

The following are responses and/or clarifications as to the eight (8) Audit Exception's and four (4) Disclosures included in Mr. Brown's report.

**Audit Exception No. 1
Subject: Utility Plant**

Facts: The utility could not provide documents (invoices and checks) supporting the transfer of \$210,781.00 and \$1,989,822.00 of respective water and wastewater plant-in-service.

Zellwood Station Co-Op, Inc. purchased the utility along with the mobile home park on October 1, 1993, from Zellwood Station, LTD., for \$13,600,000.

The \$2,200,603 allocated to the utility was based on a physical improvement inspection report conducted by a public engineer on February 25, 1994. The total amount did not include general plant and was not an original cost study. The allocations in the rate case filing of \$1,156,768 for water and \$1,736,274 for wastewater reflected general and common plant and HAI's best estimate of the original cost of both systems without performing an original cost study:

Opinion/Recommendation: Water and wastewater plant-in-service should be reduced by \$1,097,725.84 and \$1,721,884.97, respectively. Field staff defers to the FPSC engineer and analyst for disposition of the plant valuation at transfer.

ACK _____
AFA 1
APP _____
CAF _____
CMU _____
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EAG _____
LEG 2
LIN 3
OPC _____
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SEC 1
WAS Walker
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ORLANDO FORT MYERS PLANTATION JACKSONVILLE

DOCUMENT NUMBER-DATE

08468 AUG 10 98

FPSC-RECORDS/REPORTING

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MAIL ROOM
AUG 10 1998
FLORIDA PUBLIC SERVICE COMMISSION

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Company Response: The Company feels that in absence of the supporting documents from the previous two owners, it may well be in the best interest of all parties to agree to performing an "original cost study" as part of a supplemental rate filing which would also include metered rates within the next three years, with the requested rates put in place during the interim period.

Audit Exception No. 2
Subject: Depreciation and related Reserve

Facts: The water and wastewater reserve at December 31, 1996, along with test year depreciation, was recalculated per F. A. C. 25-30.140. Accumulated depreciation on the unsupported transferable plant along with associated depreciation expense (Exception No. 1) was excluded from the respective balances at December 31, 1996.

Opinion/Recommendation: It is recommended that accumulated depreciation at December 31, 1996, and water depreciation expense for the test year ended at the same date be reduced by \$239,519.12 and \$81,430.40, respectively; and that wastewater accumulated depreciation and depreciation expense for the same period be reduced by \$294,738.54 and \$88,552.04, respectively.

Company Response: The Company agrees that all water and wastewater assets should be recalculated per F. A. C. 25-30.140 for the test year versus the original depreciation rates and lives that are on the Company's books and records. The depreciation expense is predicated upon the plant in service which is at issue. The depreciation "fall-out" from expense and accumulated depreciation balances will be a by-product of the original cost study proposal to be conducted within the next 3 years.

Audit Exception No. 3
Subject: CIAC and Amortization

Facts: The utility reflected \$250,000 of contributions –in-aid-of-construction (CIAC) at December 31, 1996, via its Commission –submitted rate filing.

A review of the company's records did not support the existence of CIAC. Utility representative informed staff that it has never collected monies from customers for anything other than monthly water and wastewater charges of \$17.50 per customer.

Opinion/Recommendation: It appears that the utility's consultants imputed the CIAC. It is recommended that CIAC be reduced until the Tallahassee analyst and engineer evaluate the transferable plant per Exception No. 1 and determine the associated components. The related accumulated amortization of \$12,513 should be reduced in total.

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Company Response: At the time of this filing, the Company has petitioned the St. Johns River Water Management District for grant money to assist in metering the system. The Company hopes to receive up to \$125,000 in matching grant money. At its August 11 monthly meeting, the SJRMD is expected to consummate a \$50,000 grant agreement. Therefore, the Company believes that a minimum \$50,000 in CIAC from The SJRWMD is appropriate and the fallout adjustments associated therewith.

Audit Exception No. 4
Subject: Utility Pro Forma Adjustments

Facts: The utility was unable to provide field staff with schedules or documentation supporting \$68,111.11 and \$77,369.00 of 1996 water and wastewater proforma's, respectively. Water and wastewater operating and maintenance expenses (O&M), including proforma's, were \$169,841.07 and \$167,421.93, respectively, for the test year ended December 31, 1996.

The 1997 unaudited water and wastewater O&M expenses per the utility's general ledger were \$125,197.07 and 156,770.82, respectively.

Opinion/Recommendation: Staff recommends that 1996 water and wastewater operating expenses be reduced by \$68,111.11 and \$77,369.00 and net operating income be increased by the same.

Company Response: The Company respectfully apologizes to staff for not providing the support schedules and documentation apparently needed (please see Attachment No. 1). The Company has projected the additional operations and maintenance (including administrative & general) expense increases associated from transcending the utility from a non regulated mom and pop operation to a highly disciplined regulated water and wastewater utility. The Company is in a "catch 22" where as it is in dire need of rate relief before it can actually implement the requested pro forma expense request because of its financial condition.

Audit Exception No. 5
Subject: Filing/Per Books Reconciliation

Facts: The following differences in O&M accounts were noted between the utility's Commission rate filing and its books (general ledger).

Opinion/Recommendation: Staff recommends that water operating and maintenance expense be reduced by \$2,323.27 and wastewater be increased by \$14,712.48.

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Company Response: The Company agrees with staff, except that the dollars associated with accounts 631, 633 and 731 were pulled out of O&M and reassigned to rate case expense. The majority of the other differences occurred because of account classification differences. A/C 601 was a transposition error and A/C 711 test year number was in the pro forma column.

Audit Exception No. 6
Subject: Consumptive Use Permit

Facts: The utility charged Account 631, Contractual Services-Engineering for \$3,564.80 during the test year ended December 31, 1996.

The \$3,564.80 billed to Zellwood Station Co-Op, Inc. by Excel Engineering Consultants was for services provided in processing the utility's application for its consumptive use permit (CUP).

The permit issuer, St. Johns River Water Management District, establish a five-year CUP life.

Opinion/Recommendation: Field staff recommends that the \$3,564.80 charged to Contractual Services-Engineering be reduced to \$2,851.84 to reflect a five-year amortization period.

Company Response: The Company has reflected this expense as a part of its rate case expense using a four-year amortization. The company agrees that this expense should carry a amortization period that parallels the CUP life.

Audit Exception No. 7
Subject: Utility Expensed Plant Additions

Facts: The following capital expenditures were charged to operations during the test year ended December 31, 1996.

Opinion/Recommendation: Staff makes the following recommendations: that water and wastewater operating expenses be reduced by respective \$175.92 and 587.57; that water and wastewater utility plant be increased by the same; and that water and wastewater test year depreciation expense and the associated reserve at December 31, 1996, be increased by \$7.33 and \$16.43.

Company Response: The Company agrees.

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Audit Exception No. 8
Subject: Capital Structure

Facts: The utility purchased the mobile home park along with the utility for \$13,600,000 on October 1, 1993.

The seller, Zellwood Station, LTD., agreed to finance \$1,500,000 of the purchase price at 7 percent and received the balance in cash.

The utility reflected a 7.95 percent cost rate via its submitted filing applicable to the financing of the said loan.

Opinion/Recommendation: Long-term debt for the utility should be reflected at a 7 percent rate and the remaining investment equity.

Company Response: The Company agrees.

Audit Exception No. 9
Subject: Working Capital Allowance

Facts: The working capital allowance has been computed based on the 1/8 formula method to comply with Commission rule 25-30.433(2), Florida Administrative Code.

The respective water and wastewater working capital allowance was computed as \$12,047.37 and \$213,022.23 based upon staff adjusted operation and maintenance expenses of \$96,378.93 and \$104,177.84.

Opinion/Recommendation: Staff recommends that water and wastewater rate base be increased by \$12,047.37 and \$13,022.23, respectively.

Company Response: The Company agrees that the working capital method per Commission rule 25.30.433(2) is the 1/8 O&M method. It does not agree with the staff's level of adjusted water and wastewater O&M expenses.

Disclosure No. 1

Subject : Pro Forma Plant

Facts: The utility reflected a pro forma adjustment of \$234,678 for meters during 1997, via its submitted Commission rate filing.

The utility acquired \$98,383.39 and \$49,448.11 of respective water and wastewater additions from the end of the test year at December 31, 1996 through May 31, 1998.

Meters and associated costs represented \$59,682.54 of the \$147,832.00 plant additions obtained since December 31, 1996.

Opinion/Recommendation: Staff reflected rate base as of December 31, 1996, exclusive of the meter pro forma. Staff traced \$96,959.27 of the \$147,932.00 to supporting documentation. Staff defers to Tallahassee analyst for disposition of this matter.

Company Response: The Company feels strongly that the \$234,678 is an accurate estimate of the cost of purchasing and installing the meters for existing customers. It was originally thought that SJRWMD would reimburse the Company approximately \$250,000 through a grant, but the grant will be in an amount no less than \$50,000 and no more than \$125,000. It is critical that all meter installation expenditures are reflected in the proposed water rates.

Disclosure No. 2

Subject: Nonrecurring Expenses

Facts: The utility charged Account 633, Contractual Services-Legal for \$24,306.30 during the test year ended December 31, 1996.

The \$24,306.30 represents legal services provided by Gray, Harris & Robinson for utility-related matters.

Field staff was unable to categorize legal expense as some were inadequately descriptive. However, all costs appear to be specifically related to the FPSC rate filing, processing of the consumptive use permit, and the purchase of the utility.

Opinion/Recommendation: The legal costs should be amortized over a period as deemed reasonable by the FPSC analyst. A copy of the invoices totaling \$24,306.30 has been included in the audit work papers to assist the analyst in disposition of this matter.

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Company Response: The Company has included these legal expenses as a part of its requested rate case expense, of which it is requesting a four-year amortization. The Company will assist the FPSC analyst in any way it can as it pertains to rate case expense documentation. The \$24,306.30 of legal expenses does not reflect any cost associated with processing of the consumptive use permit, and the purchase of the utility. It pertains to the original certificate application only.

Disclosure No. 3

Subject: Water Conservation

Facts: The St. Johns River Water Management District's issuance of Zellwood Station Co-Op, Inc.'s consumptive use permit was conditional upon the utility implementing certain water conservation measures. One condition was requiring water meters on all new construction and retrofitting such on existing residences. The retrofit program is required to be completed by the end of 1998.

Opinion/Recommendation: As of May 31, 1998, 690 of the 995 developed lots have been metered. In order to comply with the conditions, the remaining 305 need to be installed by December 31, 1998.

Company Response: The Company will, in good faith, attempt to meet this deadline. As of July 31, 1998, it has 730 meters installed.

Disclosure No. 4

Subject: Allocations

Facts: Operating expenses with the exception of salaries and wages, were distributed equally between water and wastewater, if not specifically identifiable with either operation.

Opinion/Recommendation: Utility representative informed staff that the allocation methodology was based on revenue at a flat rate of \$8.75 for water and \$8.75 for wastewater.

Company Response: The Company believes this is the correct allocation methodology because of the flat rates (revenues). In addition, there are an equal amount of water and wastewater customers.

Ms. Blanca S. Bayo

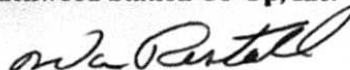
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This filing contains an original and four copies of the service availability policy tariff sheets, and an original and five copies of the remaining information that you requested. Please feel free to call Mr. Chuck Lewis at (407) 839-3955 ext. 203 if you have any questions.

Very truly yours,

Zellwood Station Co-Op, Inc.



W. A. Restall
Utilities Director

cc: Irving Perkins
T. A. Cloud
G. C. Hartman
Julian Coto
Chuck Lewis

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Zellwood Station: W-WWTF Feasibility Study
Docket No. 980307-WS
Pro Forma Reconciliation
Audit Report

Item	Description	Hourly Rate (1)	Overhead Factor (2)	Factored Rate	Annual Hours	Annual Salary
1	Manager/Operator	\$22.00	130.00%	\$28.60	2,080	\$59,488.00
2	Labor/Operator	\$10.00	130.00%	\$13.00	2,080	\$27,040.00
3	Labor	\$8.00	130.00%	\$10.40	2,080	\$21,632.00
4	Clerical	\$10.00	130.00%	\$13.00	2,080	\$27,040.00
						\$135,200.00
Water Allocation						\$67,600.00
Less 1996 Booked Water Wages & Salaries						\$44,395.17 Incorrect Booked Number
Pro Forma						\$23,204.83 A/C: 601
Water Allocation						\$67,600.00 A/C 601
Less 1996 Booked Water Wages & Salaries						\$14,395.17 A/C 601
Pro Forma						\$53,204.83 A/C 601
Wastewater Allocation						\$67,600.00 A/C 701
Less 1996 Booked Water Wages & Salaries						\$43,187.11 A/C 701
Pro Forma						\$24,412.89 A/C 701

Water Expense	Pro Forma	Account	Allocation
Chemicals (3)	\$5,450.00	A/C 618	
Inspections (4)	\$0.00	A/C 635	
Laboratory Testing (5)	\$3,250.00	A/C 635	50/50 Split
Supplies & Cleaning (6)	\$1,500.00	A/C 620	50/50 Split
	\$10,200.00		

Sewer Expense	Pro Forma	Account	Allocation
Chemicals (7)	\$0.00	A/C 718	
Inspections (8)	\$500.00	A/C 735	
Laboratory Testing (9)	\$3,250.00	A/C 735	50/50 Split
Sludge Removal (10)	\$13,500.00	A/C 711	
Supplies & Cleaning (11)	\$1,500.00	A/C 720	50/50 Split
	\$18,750.00		

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General Expenses			
Water and Sewer	Pro Forma	Account	Allocation
General Administration (12)	\$3,000.00	A/C 620	50/50 Split
Regulatory Licenses (.3)	\$500.00	A/C 675	50/50 Split
Repair of Equipment (14)	\$7,500.00	A/C 620	50/50 Split
State & County Permits (15)	\$0.00	N/A	50/50 Split
Utility (16)	\$0.00	N/A	50/50 Split
Misc. Expenses (17)	\$1,200.00	A/C 675	50/50 Split
	<u>\$12,200.00</u>		

Office Expenses			
Water and Sewer	Pro Forma	Account	Allocation
Office Trailer (18)	\$4,500.00	A/C 641	50/50 Split
Supplies (19)	\$1,000.00	A/C 620	50/50 Split
Electricity (20)	\$2,400.00	A/C 615	50/50 Split
Computer (21)	\$4,500.00	A/C 642	50/50 Split
Software (22)	\$2,500.00	A/C 642	50/50 Split
Telephone (23)	\$600.00	A/C 620	50/50 Split
Travel (24)	\$3,000.00	A/C 620	50/50 Split
	<u>\$18,500.00</u>		

Footnotes:

- (1) - These are the applicable hourly rates for the various labor categories in the Orlando Area.
- (2) - This factor includes Zellwood Station Coop, Inc. applicable local, state and federal payroll taxes and fringe benefits
- (3) - Higher chemical costs are anticipated in the test year because of market conditions along this is estimated to be approximately equal to a compounded inflation allowance of 7% between the test year 1996 and the rate year 1999.
- (4) - N/A
- (5) - This item includes water quality testing required by the FDEP. It should be noted that water quality testing is performed over a 3 year cycle. Therefore, the costs for each year is not homogeneous and varies significantly between one year and the next. During the cycle year where volatile organics and radionuclides are tested the analytical expenses can be greater than \$3,000 for these parameters. Staff found test year amount to be 1,230.00.
- (6) - Supplies and cleaning includes miscellaneous chemical and cleaning supplies used to maintain the operations of the water facilities. There was no accounting entry for this expense in the test year.
- (7) - N/A
- (8) - The wastewater treatment facility is inspected 4 times per year by Orange County. The County charges Zellwood \$250.00 per inspection. Orange County also takes additional effluent water quality samples and charges the utility for these as well. The additional water quality Analysis are included in Laboratory testing.
- (9) - This item includes influent and effluent water quality testing required by the FDEP and Orange County. It should be noted that the new wwtf operating

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- permit required both influent and effluent water quality testing. The additional influent samples are required as a condition of the new permit and the additional costs may not have been included in the test year.
- (10) - The costs for sludge hauling has increased by approximately 100% due to market conditions and regulatory constraints. Therefore, the amount declared for the test year should be doubled in the pro-forma.
 - (11) - Supplies and cleaning includes miscellaneous chemical and cleaning supplies used to maintain the operations of the wastewater facilities. There was no accounting entry for this expense in the test year.
 - (12) - General Administrative expenses includes administrative charges payable to Zellwood for the use of office space, accounting, managerial and other administrative expenses.
 - (13) - Regulatory licenses includes business licenses required by the County and the State.
 - (14) - Repair of equipment includes general repair to water and wastewater equipment such as belts, air filters, pump bearings, etc.
 - (15) - N/A
 - (16) - N/A
 - (17) - Other miscellaneous expenses associated with additional employees, record keeping and administrative functions.
 - (18) - The rental cost of the office trailer was obtained from SpaceMasters Manufacturing, Inc. The total cost includes installation, maintenance, delivery, insurance, monthly rental fee and miscellaneous charges.
 - (19) - Office supplies include postage, paper, printing, copier products, etc. This amount was estimated based on previous experience.
 - (20) - The office trailer will require electricity to operate the HVAC system as well as the office equipment. An average bill of \$200.00 per month was assumed.
 - (21) - This item includes the cost to purchase a complete computer system including a printer.
 - (22) - This item includes the cost to purchase computer software specific to the utility and general administrative functions.
 - (23) - A \$50.00 per month telephone charge was assumed based on previous experience.
 - (24) - This item includes basic travel expenses required in operating the utility. This cost includes the costs of attending regulatory seminars.