

State of Florida



# Public Service Commission

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CLERK

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**DATE:** August 12, 2011  
**TO:** Office of Commission Clerk  
**FROM:** Clarence J. Prestwood, Chief of Auditing, Office of Auditing and Performance Analysis *CJP*  
**RE:** Docket No.: 110130-WS  
Company Name: Shangri-La by the Lake Utilities, Inc.  
Company Code: WS728  
Audit Purpose: Staff Assitsted Rate Case  
Audit Control No: 11-153-1-2

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Attached is the final audit report for the Utility stated above. I am sending the Utility a copy of this memo and the audit report. If the Utility desires to file a response to the audit report, it should send a response to the Office of Commission Clerk. There were no confidential work papers associated with this audit.

CJP/kby

Attachment: Audit Report

cc: Office of Auditing and Performance Analysis File

DOCUMENT NUMBER-DATE

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FPSC-COMMISSION CLERK

State of Florida



**Public Service Commission**

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

**Auditor's Report**

Shangri-La by the Lake Utilities, Inc.  
Staff Assisted Rate Case

**Twelve Months Ended March 31, 2011**

Docket No. 110130-WS  
Audit Control No. 11-153-1-2  
**August 18, 2011**

Handwritten signature of Intesar Terkawi in black ink.

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Intesar Terkawi  
Audit Manager

Handwritten signature of Lynn M. Deamer in black ink.

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Lynn M. Deamer  
Reviewer

DOCUMENT NUMBER - DATE

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## Table of Contents

Purpose.....	1
Objectives and Procedures.....	2
Audit Findings	
1: Utility Books and Records.....	6
2: Utility Plant in Service.....	7
3: Accumulated Depreciation.....	12
4: Contributions-in-Aid-of-Construction .....	14
5: Accumulated Amortization of CIAC .....	15
7: Operating Revenue.....	17
8: Operations and Maintenance Expense .....	18
9: Taxes Other than Income .....	21
Exhibits	
1: Rate Base .....	22
2: Net Operating Income.....	23
3: Capital Structure .....	24

## Purpose

To: Florida Public Service Commission

We have performed the procedures described later in this report to meet the agreed-upon objectives set forth by the Division of Economic Regulation in its audit service request dated June 2, 2011. We have applied these procedures to the attached exhibits prepared by the audit staff in support of Shangri-La by the Lake Utilities, Inc.'s request for a Staff Assisted Rate Case in Docket No. 110130-WS.

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

## Objectives and Procedures

### **GENERAL**

#### Definitions

The term "Utility" used within this report refers to Shangri-La by the Lake, Inc.

The test year is the twelve months ended March 31, 2011.

#### Last Case

Order No. PSC-96-0062-FOF-WS, which was issued January 12, 1996, in Docket No. 940653-WS, established the balances for Plant in Service and Accumulated Depreciation as of June 30, 1994. The Utility's customers subsequently filed a complaint regarding these stated balances. In response to the complaint, the Commission issued Order No. PSC-00-0259-PAA-WS, in Docket No. 990080-WS, on February 8, 2000. This order established new balances for Plant in Service and Accumulated Depreciation as of June 30, 1994.

#### Utility Books and Records

**Objective:** The objective was to determine that the Utility maintains its accounts and records in conformity with the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts (USOA) as adopted by the Florida Public Service Commission.

**Procedures:** We reviewed the Utility's accounting systems. Audit Finding 1 discusses our findings and recommendations for the Utility's accounting system.

### **Rate Base**

#### Utility Plant in Service

**Objectives:** The objectives were 1) to determine that property exists and is owned by the Utility, 2) to determine that additions to Utility Plant in Service (UPIS) are authentic, recorded at original cost, and classified in compliance with Commission rules and the NARUC USOA, and 3) to verify that proper retirements of UPIS are made when a replacement item was placed in service.

**Procedures:** We determined the Utility's water and wastewater UPIS balances as of June 30, 1994 that were established in Docket No. 990080-WS. We compiled UPIS additions for the period July 1, 1994 through March 31, 2011 to determine the UPIS balances for this proceeding. We scheduled retirements to UPIS when a capital item was removed or replaced. We toured the Utility plant sites to observe whether asset additions were completed and to ascertain if asset retirements were needed. Audit Finding 2 discusses our findings and recommended UPIS balance as of March 31, 2011.

### Land and Land Rights

**Objectives:** The objectives were to determine that the Utility's land is recorded at original cost and is owned or secured under a long-term lease.

**Procedures:** We determined the water and wastewater land balances as of June 30, 1994 that were established in Docket No. 990080-WS. We reconciled the Utility's water and wastewater land balances for this proceeding to the balances established in Order No. PSC-00-0259-PAA-WS. There were no changes to utility land since the transfer proceeding.

### Contributions-in-Aid-of-Construction

**Objectives:** The objectives were 1) to determine that additions to Contributions-in-Aid-of-Construction (CIAC) were recorded in compliance with Commission rules and the NARUC USOA, and 2) to determine that all donated property is properly accounted for and recorded as CIAC.

**Procedures:** We determined the Utility's CIAC balances as of June 30, 1994 that were established in Docket No. 990080-WS. We compiled additions to CIAC for the period July 1, 1994 through March 31, 2011 to determine the Utility's CIAC balance for this rate case proceeding. We reviewed the Utility's 2005 through 2010 Federal Income Tax returns for unrecorded cash and property contributions. Audit Finding 4 discusses our finding and the CIAC balance as of March 31, 2011.

### Accumulated Depreciation

**Objectives:** The objectives were 1) to determine that accruals to accumulated depreciation are recorded in compliance with Commission rules and the NARUC USOA, 2) to verify that depreciation accruals are calculated using the Commission's authorized rates, and 3) to verify that retirements are properly scheduled.

**Procedures:** We determined the Utility's accumulated depreciation balances as of June 30, 1994 that were established in Docket No. 990080-WS. We compiled accumulated depreciation accruals for the period July 1, 1994 through March 31, 2011 to determine the Utility's accumulated depreciation balances for this proceeding. We scheduled retirements to accumulated depreciation when a capital item was removed or replaced. Audit Finding 3 discusses our findings and recommended balances for accumulated depreciation as of March 31, 2011.

### Accumulated Amortization of CIAC

**Objective:** The objective was to determine that accruals to accumulated amortization of CIAC were recorded in compliance with the NARUC USOA, and the Commission rules.

**Procedures:** We determined the Utility's accumulated amortization of CIAC balances as of June 30, 1994 that were established in Docket No. 990080-WS. We compiled accumulated amortization of CIAC accruals for the period July 1, 1994 through March 31, 2011 to determine the Utility's accumulated amortization of CIAC balances for this proceeding. Audit Finding 5

discusses our findings and recommended balances for accumulated amortization of CIAC as of March 31, 2011.

### Working Capital

**Objective:** The objective was to calculate the working capital allowance in compliance with Commission rules.

**Procedures:** We calculated the Utility's working capital allowance for the test year using one-eighth of operation and maintenance expense as required by Commission Rule 30.433(2), Florida Administrative Code (FAC).

## **Net Operating Income**

### Revenues

**Objective:** The objective was to determine that revenues were recorded in compliance with Commission rules and are based on the Commission approved tariff rates.

**Procedures:** We compiled Utility revenues for the test year from the Utility's general ledger and billing register. We traced the customer bills to the tariff. Audit Finding 7 discusses our findings and recommended revenue.

### Operation and Maintenance Expense

**Objective:** The objective was to determine that operation and maintenance expenses (O&M) were representative of ongoing Utility's operations, and were recorded in compliance with the NARUC USOA, and the Commission rules.

**Procedures:** We compiled operation and maintenance expense items from the Utility's general ledger and vendor invoice file. We reviewed all Utility invoices for proper amount, period, classification, NARUC account, and recurring nature. Audit Finding 8 discusses our findings and the recommended operation and maintenance expense for the test year.

### Federal Income Tax

**Objective:** The objectives were 1) to determine that the Federal income taxes were correctly calculated, and 2) to determine that the taxes due were paid to the Internal Revenue Service (IRS).

**Procedures:** We traced the revenue recorded on the Tax Form 1120S to the Utility's annual reports for the last five years. We were not able to verify that the Federal Income Taxes due were paid to the Federal authorities because the Utility's status is an S-Corporation and net income or loss passes through to the individual shareholders. Therefore, no tax expense was calculated or paid at the corporate level.

### Taxes Other than Income

**Objective:** The objective was to determine that Taxes Other Than Income (TOTI) tax expense was recorded in compliance with NARUC USOA, and the Commission rules.

**Procedures:** We compiled TOTI expense items from the Utility's general ledger and vendor invoice file. We reviewed all Utility tax invoices for proper amount, period, classification, NARUC account, and recurring nature. Audit Finding 9 discusses our findings and recommended TOTI expense for the test year.

### Depreciation and Amortization Expenses

**Objectives:** The objectives were 1) to determine that depreciation expense and amortization expense were recorded in compliance with Commission rules and 2) to determine that they accurately represent the depreciation of UPIS and the amortization of CIAC from ongoing utility operations.

**Procedures:** We calculated depreciation expense and amortization expense using the UPIS and CIAC balances determined in Audit Findings 2 and 4 and the approved depreciation rates. Audit Findings 2 and 5 discuss our findings and recommended depreciation expense as well as the recommended amortization expense for the test year.

## **Capital Structure**

### General

**Objective:** The objective was to determine that the components of the Utility's capital structure and the respective cost rates used to arrive at the overall weighted cost of capital are recorded in compliance with Commission rules.

**Procedures:** We determined that the Utility's capital structure has long-term debt and equity. Audit Finding 6 discusses our findings and recommended capital structure.

## Audit Findings

### **Finding 1: Utility Books and Records**

**Audit Analysis:** Order No. PSC-96-0062-FOF-WS required the Utility to maintain its books in accordance with the NARUC USOA as required by the Commission Rule.

The Utility does not follow the NARUC system. Accounts are neither classified nor numbered according to the NARUC system. The Utility uses the cash basis of accounting method. The owner and his wife maintain the daily bookkeeping for the Utility, and an outside accountant prepares the federal and state tax returns and the annual reports on annual basis.

We recommend that the Utility maintain its books in accordance with the NARUC USOA and be required to convert to the accrual basis method of accounting for all future reporting periods.

**Effect on the General Ledger:** For informational purposes only.

## **Finding 2: Utility Plant in Service**

**Audit Analysis:** The Utility's General Ledger reflects water and wastewater UPIS balances of \$177,932 and \$301,374, respectively as of March 31, 2011.

Order No. PSC-00-0259-PAA-WS established water and wastewater balances of \$79,128 and \$86,332, respectively, as of June 30, 1994. The Utility did not adjust water and wastewater UPIS balances to the Commission Order.

Based on our adjustments and findings discussed below, the Utility's UPIS are \$134,537 for water and \$144,800 for wastewater, as of March 31, 2011. The simple average water and wastewater UPIS balances for the test year are \$134,259 and \$144,800 respectively.

We compiled UPIS additions from July 1, 1994 through March 31, 2011 for water and wastewater. We started with the UPIS balances established in the Utility's last rate case proceeding. We then posted additions and retirements to UPIS in succeeding years when capital items were added or replaced. We reclassified plant additions to the correct NARUC USOA account when necessary. We toured the Utility's water and wastewater plant sites and lift stations to observe and ascertain the condition and existence of the Utility's assets.

Our analysis for the adjustments stated in Table 1 and Table 2 are below.

- 1) Account 301 – Organization is increased by \$750, as the Utility did not adjust to the Commission's last order in Docket 990080-WS.
- 2) Account 307 – Wells & Springs is decreased by \$4,500, as the Utility did not adjust to the Commission's last order in Docket 990080-WS.
- 3) Account 309 – Supply Mains is increased by \$300, as the Utility did not adjust to the Commission's last order in Docket 990080-WS.
- 4) Account 311 – Pumping Equipment is decreased by \$14,680 based on the following adjustments.
  - a. We have decreased the account by \$13,501, as the Utility did not adjust to the Commission's last order in Docket 990080-WS.
  - b. We have decreased the account by \$1,179, which represents the retirement for a replacement of a reducer in 2005.
- 5) Account 320 – Water Treatment Equipment is increased by \$8,906, as the Utility did not adjust to the Commission's last order in Docket 990080-WS.
- 6) Account 330 – Distribution Reservoirs & Standpipes is increased by \$1,500, as the Utility did not adjust to the Commission's last order in Docket 990080-WS.

- 7) Account 331 – Transmission & Distribution Lines is decreased by \$35,207 based on the following adjustments.
  - a. We have decreased the account by \$40,502, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
  - b. We have increased the account by \$4,738, which represents the difference between the audit plant additions of \$12,088 to the Utility’s Plant additions of \$7,350 in 2005.
  - c. We have reclassified \$557, which represents a 2011 motor pump from the O&M expenses to the Plant in Service Account.
- 8) Account 333 – Services is increased by \$7,675, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 9) Account 334 – Meters & Meter Installation is increased by \$5,257 due to the following adjustments.
  - a. We have increased the account by \$17,500, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
  - b. We have decreased the account by \$12,243, which represents the difference of \$23,523 recorded by the Utility, and the audited amount of \$11,280.
- 10) Account 339 – Other Plant & Miscellaneous Equipment is decreased by \$13,396 due to the following adjustments.
  - a. We have reclassified \$11,185, which represents the costs of cleaning and painting the Aerator tank in 2010 to the O&M expense.
  - b. We have reclassified \$348, which represents the water portion of the 2007 annual service of accounting software to the O&M expense.
  - c. We have decreased the account by \$1,863, as the Utility did not provide the required support.
- 11) Account 351 – Organization is increased by \$750, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 12) Account 354 – Structure & Improvement is increased by \$6,080, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 13) Account 360 – Collection Sewers - Force is increased by \$3,138, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 14) Account 361 – Collection Sewers-Gravity is decreased by \$144,017, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 15) Account 362 – Special Collecting Structures is increased by \$200, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.

- 16) Account 363 – Services to Customers is increased by \$5,145, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 17) Account 364 – Flow Measuring Devices is increased by \$2,474, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 18) Account 365 – Flow Measuring Installations is increased by \$2,540, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 19) Account 370 – Receiving Wells is increased by \$16,000, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
- 20) Account 371 – Pumping Equipment is decreased by \$32,258 due to the following adjustments.
  - a. We have decreased the account by \$25,580, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
  - b. We have decreased \$7,902, which represents the Utility Plant additions in 2005 that lacked the support.
  - c. We have increased the account by \$1,224, which represents the difference between the invoice amount of \$4,897, for the unrecorded 1997 pump replacement and the retirement of \$3,673 that we calculated.
- 21) Account 380 – Treatment and Disposal Equipment is decreased by \$3,694 due to the following adjustments.
  - a. We have increased the account by \$3,399, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.
  - b. We have increased the account by \$61, which represents the difference between the invoice amount of \$244, for the unrecorded 1997 backflow preventer replacement, and the retirement of \$183 that we calculated.
  - c. We have increased the account by \$234, which represents the unrecorded cost of the Air Compressor.
- 22) Account 389 – Other Plant & Misc. Equipment is decreased by \$1,661 due to the following adjustments.
  - a. We have decreased the account by \$959, which represents the retirement of a PVC Air Line replacement in 2004.
  - b. We have reclassified \$348 to O&M expense, which represents wastewater portion of the 2007 annual service of accounting software.
  - c. We have decreased the account by \$354, as the Utility did not provide the required support.
- 23) Account 390 – Office Furniture & Equipment is decreased by \$1,500, as the Utility did not provide the required support.
- 24) Account 395 – Tools Shop & Garage Equipment is increased by \$203, as the Utility did not adjust to the Commission’s last order in Docket 990080-WS.

25) Account 398 – Other Tangible Plant is decreased by \$17,362 due to the following adjustments.

- a. We have decreased the account by \$9,562, as the Utility did not adjust to the Commission's last order in Docket 990080-WS.
- b. We have decreased the account by \$7,800, as the Utility did not provide the required support.

**Table 1**  
**Water Plant Balance**  
**As of March 31, 2011**

Acct No.	Account Description	Balance Per Utility	Adjustment	Balance Per Audit
301	Organization	-	\$750	\$750
304	Structure and Improvement	\$5,000	-	5,000
307	Wells & Springs	36,412	(4,500)	31,912
309	Supply Mains	-	300	300
311	Pumping Equipments	21,750	(14,680)	7,070
320	Water Treatment Equipment	-	8,906	8,906
330	Distribution Reservoirs & Standpipes	-	1,500	1,500
331	Transmission & Distribution Mains	74,350	(35,207)	39,143
333	Services	-	7,675	7,675
334	Meter & Meter Installation	23,523	5,257	28,780
339	Other Plant & Miscellaneous Equipment	16,897	(13,396)	3,501
	<b>Total UPIS</b>	<b>\$177,932</b>	<b>(\$43,395)</b>	<b>\$134,537</b>

**Table 2**  
**Wastewater Plant Balance**  
**As of March 31, 2011**

Acct No.	Account Description	Balance Per Utility	Adjustment	Balance Per Audit
351	Organization	-	\$750	\$750
354	Structure & Improvement	-	6,080	6,080
360	Collection Sewers – Force	-	3,138	3,138
361	Collection Sewers – Gravity	\$218,000	(144,017)	73,983
362	Special Collecting Structures	-	200	200
363	Services to Customers	-	5,145	5,145
364	Flow Measuring Devices	-	2,474	2,474
365	Flow Measuring Installation	-	2,540	2,540
370	Receiving Wells	-	16,000	16,000
371	Pumping Equipment	33,902	(32,258)	1,644
380	Treatment & Disposal Equipment	26,000	3,694	29,694
389	Other Plant & Misc. Equipment	4,610	(1,661)	2,949
390	Office Furniture & Equipment	1,500	(1,500)	-
395	Tools, Shop, Garage Equipment	-	203	203
398	Other Tangible Plant	17,362	(17,362)	-
	<b>Total UPIS</b>	<b>\$301,374</b>	<b>(\$156,574)</b>	<b>\$144,800</b>

**Effect on the General Ledger:** The UPIS balance for water should be decreased by \$43,395 and the UPIS balance for wastewater should be decreased by \$156,547 as of March 31, 2011.

### Finding 3: Accumulated Depreciation

**Audit Analysis:** The Utility’s General Ledger reflects water and wastewater accumulated depreciation balances of \$49,591 and \$152,156, respectively as of March 31, 2011. The Utility reported water depreciation expense of \$4,649 and wastewater depreciation expense of \$13,509 for the test year ended March 31, 2011.

We determined the audit balance of Accumulated Depreciation to be \$95,106 for water and \$80,944 for wastewater, as of March 31, 2011. The simple average water and wastewater Accumulated Depreciation balances are \$92,696 and \$79,782. The depreciation expense for water and wastewater are \$4,821 and \$2,324. The water and wastewater adjustments of \$45,515 (\$26,136 + \$19,379), and (\$71,211) ((\$41,350 + (\$112,561))) includes \$26,136, and \$41,350 adjustments to the Commission Order No. PSC-00-0259-PAA-WS. The adjustments of \$19,379 and (\$112,561) are due to our Plant in Service adjustments explained in Audit Finding. 2, and due to using the depreciation rates prescribed in Commission Rule 25-30-140, F.A.C.

**Table 1**  
**Water Accumulated Depreciation**  
**As of March 31, 2011**

Acct No.	Account Description	Balance per Utility	Adjustment	Balance Per Audit
301.	Organization	-	\$333	\$333
304.	Structure & Improvement	\$1,150	1,026	2,176
307.	Wells & Springs	9,395	12,918	22,313
309.	Supply Mains	-	166	166
311.	Pumping Equipments	6,885	(3,991)	2,894
311.1	Pumping Equipments	-	2,335	2,335
320.	Water Treatment Equipment	-	7,800	7,800
320.1	Water Treatment Equipment	-	1,469	1,469
330.	Distribution Reservoirs & Standpipes	-	1,500	1,500
331.	Transmission & Distribution Mains	20,239	1,762	22,001
333.	Services	-	6,522	6,522
334.	Meter & Meter Installation	6,384	18,158	24,542
339.	Other Plant & Miscellaneous Equipment	5,538	(4,483)	1,055
	<b>Total</b>	<b>\$49,591</b>	<b>\$45,515</b>	<b>\$95,106</b>

**Table 2**  
**Wastewater Accumulated Depreciation**  
**As of March 31, 2011**

Acct No.	Account Description	Balance per Utility	Adjustment	Balance Per Audit
351.	Organization	-	\$333	\$333
354.	Structure & Improvement	-	6,080	6,080
360.	Collection Sewers - Force	-	3,138	3,138
361.	Collection Sewers - Gravity	\$103,133	(88,935)	14,198
361.1	Collection Sewers - Gravity	-	4,500	4,500
362.	Special Collecting Structures	-	98	98
363.	Services to Customers	-	4,433	4,433
364.	Flow Measuring Devices	-	2,474	2,474
365.	Flow Measuring Installation	-	1,325	1,325
370.	Receiving Wells	-	16,000	16,000
371.	Pumping Equipment	17,076	(18,822)	(1,746)
380.	Treatment & Disposal Equipment	16,514	12,281	28,795
380.1	Treatment & Disposal Equipment	-	899	899
389.	Other Plant & Misc. Equipment	3,723	(3,507)	216
390.	Office Furniture & Equipment	1,500	(1,500)	-
395.	Tools, Shop, Garage Equipment	-	203	203
398.	Other Tangible Plant	10,209	(10,209)	-
	<b>Total</b>	<b>\$152,155</b>	<b>\$(71,211)</b>	<b>\$80,944</b>

**Effect on the General Ledger:** The Utility should adjust its general ledger to the audited accumulated depreciation balances determined above. The accumulated depreciation balance for water should be increased by \$45,515 and the accumulated depreciation balance for wastewater should be decreased be \$71,211 as of March 31, 2011. We also determined that water depreciation expense should be increased by \$172 and wastewater depreciation expense should be decreased by \$11,185.

#### **Finding 4: Contributions-in-Aid-of-Construction**

**Audit Analysis:** The Utility's General Ledger reflects CIAC balances of \$9,131 and \$18,257 for water and wastewater, respectively as of March 31, 2011.

Order No. PSC-00-0259-PAA-WS established water CIAC balance of \$4,520 as of June 30, 1994. The Utility did not adjust the water CIAC balance to the Commission Order.

We compiled CIAC additions for the period June 30, 1994, through March 31, 2011, to determine the Utility's CIAC balance as of March 31, 2011. We used information from the Utility's 1996-2010 annual reports, and from its authorized service availability tariff, and revenue to determine the CIAC additions since its last rate proceedings.

Our adjustment of \$4,645 consists of \$4,520 adjustment to the above stated Commission Order, and \$125 reclassification of revenue explained in Audit Finding 7. Simple average CIAC for water and wastewater are \$13,714 and \$18,257.

**Effect on the General Ledger:** The Utility should increase its water CIAC balance by \$4,645 as of March 31, 2011.

## **Finding 5: Accumulated Amortization of CIAC**

**Audit Analysis:** The Utility's annual reports and general ledger reported zero balances for both water and wastewater Accumulated Amortization of CIAC as of March 31, 2011.

Order No. PSC-00-0259-PAA-WS established water Accumulated Amortization of CIAC of \$363 as of June 30, 1994.

We calculated water and wastewater accumulated amortization of CIAC to be \$5,007 and \$1,644 as of March 31, 2011. The Amortization of CIAC for water and wastewater are \$493 and \$292.

**Effect on the General Ledger:** The Utility should increase water and wastewater Accumulated Amortization of CIAC by \$5,007 and \$1,644, respectively as of March 31, 2011. In addition, water and wastewater CIAC amortization expense should be increased \$493 and \$292 for water and wastewater, respectively.

## **Finding 6: Capital Structure**

**Audit Analysis:** The Utility reported in the Annual Report and General Ledger long-term liabilities of \$386,087, short-term liabilities of \$77,206, Retained Earnings of (\$439,857), and Common Stock of \$100.

We compiled all eleven long-term debts. They are related parties loans with an average interest rate of 6.36%, for a total of \$465,293. We have set the common equity to zero because the Utility's general ledger reflects a negative equity balance for the test year ended March 31, 2011. The Utility does not charge customer deposits.

**Effect on the General Ledger:** None

## **Finding 7: Operating Revenue**

**Audit Analysis:** The Utility uses only 5/8" meters and services 185 residential water customers, one general water customer, and 179 wastewater residential customers.

We re-calculated the water and wastewater revenue based on the usage from the billing register. The billing register was accepted for water, as there were no significant variances. However, the amount of wastewater revenues did not match our recalculated revenues. The Utility did not use the correct tariff gallonage charge of \$2.92 (Per 1,000). The Utility was using \$2.43 (Per 1,000) gallonage charge instead. The total wastewater gallonage used is 4,547,000, for a total amount of \$11,049  $(4,547,000/1000) * \$2.43$ . Our calculation using the correct gallonage charge is \$13,277  $(4,547,000/1000) * \$2.92$ . Wastewater revenue should be increased by \$2,228  $(\$13,277 - \$11,049)$ .

Other revenue of \$62.50 for each of water and wastewater for a total of \$125, which is the cost of a meter installation, should be reclassified to water CIAC.

**Effect on the General Ledger:** Decrease other water revenue by \$62.50, other wastewater revenue by \$62.50, and increase wastewater revenue by \$2,228.

## **Finding 8: Operations and Maintenance Expense**

**Audit Analysis:** The Utility's general ledger shows water and wastewater operation and maintenance (O&M) expense balances of \$31,205 and \$36,925, respectively for the test year.

We calculated the O & M expenses to be \$30,199 and \$33,187 respectively, for water and wastewater. The calculations and our analysis of these overstatements are explained in the following adjustments and shown in the tables below.

- 1) Account 632 – Contractual Services-Accounting is overstated by \$1,265. The Utility included the tax preparation and annual report preparation costs for the years 2009 and 2010 in the test year O&M expenses. The 2009 tax preparation and Annual Report preparation of \$2,530 is allocated between water and wastewater. We removed \$1,265 that represents the amount applicable to wastewater.
- 2) Account 635 – Contractual Services-Testing is understated by \$2,026. We compiled all of the twelve months invoices for testing and bacterial analysis services for water and wastewater and allocated them according to the service provided. The amount exceeded the general ledger by \$2,026.
- 3) Account 636 – Contractual Services-Other is understated by \$725(\$5,417 - \$4,692). The total of all the invoices from contractual services is \$3,180. We reclassified the amount of \$11,185 for painting and cleaning the Aerator tank from water plant in service to O&M expenses, and amortized the amount over 5 years (\$11,185/5). We added one-year amortization expense of \$2,237 to the test year O&M expenses and deferred amortization expense of \$8,948 (\$11,185 - \$2,237) to the next four years. We reclassified \$557 that represents the cost of electric pump motor from O & M Expenses to plant in service. The amount exceeded the general ledger by \$725.
- 4) Account 665 – Regulatory Commission Expense is overstated by \$1,972, which represents 2010 Regulatory Assessment Fee that should be removed from O & M expenses and reclassified to Taxes Other Than Income.
- 5) Tax expense in the amount of \$520 that represents 2010 payroll taxes that should be removed from O & M expenses and reclassified to Taxes Other Than Income.
- 6) Account 731 – Contractual Services-Professional is overstated by \$7,369. We compiled all the invoices of consulting services from Wick's Consulting Services Inc, and reclassified the amount of \$7,369 to Account 735 - Contractual Services-Testing.
- 7) Account 732 – Contractual Services-Accounting is overstated by \$1,265. The Utility included the tax preparation and annual report preparation costs for the years 2009 and 2010 in the test year O&M expenses. The 2009 tax preparation of \$2,530 is allocated between water and wastewater. We removed \$1,265 that represents the amount applicable to water.
- 8) Account 735 – Contractual Services-Testing is understated by \$8,805. We compiled the twelve months invoices for testing and bacterial analysis services for water and wastewater

and allocated them according to the service provided for each. Included in this amount is the reclassification of \$7,369 from Account 731.

- 9) Account 736 – Contractual Services-Other is overstated by \$1,922. We compiled the invoices of other contractual services. Based on our audited amounts we decreased the amount of Contractual Services-Others by \$1,922.
- 10) Account 765 – Regulatory Commission Expense, is overstated by \$1,446, which represents 2010 Regulatory Assessment Fee that should be removed from O & M expenses and reclassified to Taxes Other Than Income.
- 11) Tax expense for \$541, which represents 2010 payroll taxes, should be removed from O & M expenses and reclassified to Taxes Other Than Income.

The working capital for water and wastewater is \$3,775 and \$4,148.

**Table 1**  
**Water Expenses**  
**For the Year Ended March 31, 2011**

Acct. No.	Per Utility Balance	Audit Adjustment	Audited Amounts
603.00	\$5,932	-	\$5,933
615.00	2,883	-	2,883
632.00	2,502	(\$1,265)	1,238
635.00	6,709	2,026	8,735
636.00	4,692	725	5,417
640.00	4,200	-	4,200
665.00	1,972	(1,972)	-
Taxes	520	( 520)	-
675.00	1,794	-	1,794
<b>Total</b>	<b>\$31,205</b>	<b>(\$1,006)</b>	<b>\$30,199</b>

**Table 2**  
**Wastewater Expenses**  
**For the Year Ended March 31, 2011**

Acct. No.	Per Utility Balance	Audit Adjustment	Audited Amounts
703.00	\$5,932	-	\$5,933
711.00	2,982	-	2,982
715.00	5,485	-	5,485
731.00	9,341	(\$7,369)	1,972
732.00	2,503	(1,265)	1,238
735.00	-	8,805	8,805
736.00	3,964	(1,922)	2,043
740.00	4,200	-	4,200
765.00	1,446	(1,446)	-
Taxes	541	(541)	-
775.00	530	-	530
<b>Total</b>	<b>\$36,925</b>	<b>(\$3,738)</b>	<b>\$33,187</b>

**Effect on the General Ledger:** Decrease water and wastewater expenses by \$1,006 and \$3,738, respectively.

## **Finding 9: Taxes Other than Income**

**Audit Analysis:** The Utility reported payroll taxes of \$520 and \$541 for water and wastewater and Regulatory Assessment Fee of \$1,975 and \$1,446 for water and wastewater, respectively in the O & M expenses for the test year ended March 31, 2011. The Utility does not pay Tangible Taxes or Property Taxes. We reclassified and recalculated the payroll taxes and the Regulatory Assessment Fees. We increased wastewater Regulatory Assessment Fees by \$100 (\$2,228 \* 4.5%) to reflect the audited revenue balance.

Our calculation of the payroll taxes and Regulatory Assessment Fees are displayed in the following schedules.

### **Water TOTI For the period ended March 31, 2011**

<b>Tax Description</b>	<b>Per Company</b>	<b>Adjustments</b>	<b>Per Audit</b>
<b>Payroll Tax</b>	-	\$520	\$520
<b>Regulatory Assessment Fees</b>	-	1,975	1,975
<b>Total</b>	-	\$2,495	\$2,495

### **Wastewater TOTI For the period ended March 31, 2011**

<b>Tax Description</b>	<b>Per Company</b>	<b>Adjustments</b>	<b>Per Audit</b>
<b>Payroll Tax</b>	-	\$541	\$541
<b>Regulatory Assessment Fees</b>	-	1,546	1,546
<b>Total</b>	-	\$2,087	\$2,087

**Effect on the General Ledger:** Increase water and wastewater TOTI by \$2,495, and \$2,087, respectively.

## Exhibits

### Exhibit 1: Rate Base

#### Water Rate Base

DESCRIPTION	SIMPLE AVERAGE PER UTILITY	ADJUSTMENT	REFER TO	SIMPLE AVERAGE PER AUDIT
UTILITY PLANT IN SERVICE	\$177,932	(\$43,673)	F 2	\$134,259
LAND AND LAND RIGHTS	0	0		0
CONTRIBUTION IN-AID-OF- CONSTRUCTION (CIAC)	(9,131)	(4,583)	F 4	(13,714)
ACCUMULATED DEPRECIATION	(49,591)	(43,105)	F 3	(92,696)
ACCUMULATED AMORTIZATION OF CIAC	0	4,761	F 5	4,761
WORKING CAPITAL		\$2,876	F 8	\$3,775
<b>TOTAL</b>	<b>\$119,210</b>	<b>(\$82,825)</b>		<b>\$36,385</b>

#### Wastewater Rate Base

DESCRIPTION	SIMPLE AVERAGE PER UTILITY	ADJUSTMENT	REFER TO	SIMPLE AVERAGE PER AUDIT
UTILITY PLANT IN SERVICE	\$301,374	(\$156,574)	F 2	\$144,800
LAND AND LAND RIGHTS	0	0		0
CONTRIBUTION IN-AID-OF-CONSTRUCTION (CIAC)	(18,257)	0	F 4	(18,257)
ACCUMULATED DEPRECIATION	(152,155)	72,373	F 3	(79,782)
ACCUMULATED AMORTIZATION OF CIAC	0	1,498	F 5	1,498
WORKING CAPITAL		\$2,876	F 8	\$4,148
<b>TOTAL</b>	<b>\$130,962</b>	<b>(\$78,555)</b>		<b>\$52,407</b>

## Exhibit 2: Net Operating Income

### Water Net Operating Income

DESCRIPTION	PER UTILITY	ADJUSTMENT	REFER TO	PER AUDIT
OPERATING REVENUES	\$43,961	(\$63)	F 7	\$43,898
OPERATING EXPENSES:				
O & M EXPENSE	31,205	(1,006)	F 8	30,199
DEPRECIATION EXPENSE	4,649	172	F 2	4,821
CIAC AMORTIZATION	0	493	F 4	493
TAXES OTHER THAN INCOME	0	2,495	F 9	2,495
TOTAL OPERATING EXPENSES	\$35,854	\$2,154		\$38,008
NET OPERATING INCOME (LOSS)	\$8,107	(\$2,217)		\$5,890

### Wastewater Net Operating Income Taxes

DESCRIPTION	PER UTILITY	ADJUSTMENT	REFER TO	PER AUDIT
OPERATING REVENUES	\$32,224	\$2,166	F 7	\$34,390
OPERATING EXPENSES:				
O & M EXPENSE	36,925	(3,738)	F 8	33,187
DEPRECIATION EXPENSE	13,509	(11,185)	F 2	2,324
CIAC AMORTIZATION	0	292	F 5	292
TAXES OTHER THAN INCOME	0	2,087	F 9	2,087
TOTAL OPERATING EXPENSES	\$50,434	(\$12,544)		\$37,890
NET OPERATING INCOME (LOSS)	(\$18,210)	\$14,710		(\$3,500)

**Exhibit 3: Capital Structure**

**Water and Wastewater Combined**

Class of Capital	Simple Average Per Utility	Simple Average Per Audit	Audit Adjustment	Ratio	Cost Rate	Weighted Cost
LONG TERM LIABILITY	\$386,087	\$465,293	\$79,206	99.98%	6.36%	6.36%
COMMON STOCK	\$100	\$100	\$0	0.02%	10.85%	0.00%
RETAINED EARNINGS	(\$439,857)	\$0	\$439,857	0.00%	10.85%	0.00%
TOTAL CAPITAL	(\$53,670)	\$465,393	\$519,063	100.00%		6.36%