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Public Service Commission

December 28, 2007

Ann Cole
Office of Commission Clerk
2540 Shumard Oak Blvd.
Tallahassee, Florida 32399-0870

Re: Docket No. 070300, In re: Review of 2007 Electric Infrastructure Storm Hardening Plan filed pursuant to Rule 25-6.0342, F.A.C., submitted by Florida Public Utilities Company

Re: Docket No. 070304-EI, In re: Petition for rate increase by Florida Public Utilities Company.

Dear Ms. Cole:

Attached for filing is an original and 6 copies of the direct testimony of Kathy L. Welch, appearing on behalf of Staff in Docket No. 070304-EI, and the certificate of service.

Yours truly,

Martha C. Brown

Martha C. Brown
Senior Attorney

MCB/tfw

CMP ____
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CTR 1
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OPC ____
RCA ____
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SGA ____
SEC ____
OTH ____

DOCKET NO. 070304-EI: Petition for rate increase by Florida Public Utilities Company

WITNESS: **Direct Testimony Of Kathy L. Welch,** Appearing On Behalf Of Staff

DATE FILED: December 28, 2007

CMP ______
COM 5
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SGA ______
SEC ______
OTH ______

DIRECT TESTIMONY OF KATHY L. WELCH

Q. Please state your name and business address.

A. My name is Kathy L. Welch and my business address is 3625 N.W. 82nd Ave., Suite 400, Miami, Florida, 33166.

Q. By whom are you presently employed and in what capacity?

A. I am employed by the Florida Public Service Commission as a Public Utilities Supervisor in the Division of Regulatory Compliance and Consumer Assistance.

Q. How long have you been employed by the Commission?

A. I have been employed by the Florida Public Service Commission since June, 1979.

Q. Briefly review your educational and professional background.

A. I have a Bachelor of Business Administration degree with a major in accounting from Florida Atlantic University and a Masters of Adult Education and Human Resource Development from Florida International University. I have a Certified Public Manager certificate from Florida State University. I am also a Certified Public Accountant licensed in the State of Florida, and I am a member of the American and Florida Institutes of Certified Public Accountants. I was hired as a Public Utilities Analyst I by the Florida Public Service Commission in June of 1979. I was promoted to Public Utilities Supervisor on June 1, 2001.

Q. Please describe your current responsibilities.

A. Currently, I am a Public Utilities Supervisor with the responsibilities of administering the District Office and reviewing work load and allocating resources to complete field work and issue audit reports when due. I also supervise, plan, and conduct utility audits of manual and automated accounting systems for historical and forecasted financial statements and exhibits.

Q. Have you presented testimony before this Commission or any other regulatory agency?

A. Yes. I have testified in several cases before the Florida Public Service Commission. Exhibit KLW-1 lists these cases.

Q. What is the purpose of your testimony today?

A. The purpose of my testimony is to sponsor the staff audit report of Florida Public Utilities Company (FPUC or Utility) which addresses the Utility's application for increase in electric rates, Audit Control Number 07-262-4-1. This audit report is filed with my testimony and is identified as Exhibit KLW-2.

Q. Did you prepare or cause to be prepared under your supervision, direction, and control this audit report?

A. Yes, I was the supervisor in charge of this audit.

Q. Please describe the work you performed in this audit.

A. For rate base, we reconciled the rate base supporting schedules and traced those to the general ledger and obtained supporting documentation for all adjustments in 2006. We recalculated the adjustments, traced the amounts to the ledgers, and reviewed prior orders. We reviewed the board of directors' minutes, the internal audit reports and the external audit work papers. We sampled plant additions for the period January 1, 2003, through December 31, 2006, for compliance with the audit objectives. We verified that the utility properly recorded retirements when a capital item was removed or replaced. We sampled construction project additions and the corresponding source documentation. We sampled Customer Advance additions for the period January 1, 2003, through December 31, 2006, for compliance with the audit objectives and traced them to contracts. We traced the accumulated depreciation schedules to the corresponding plant in service schedules. We verified that the utility used Commission authorized rates to depreciate its plant accounts by calculating a sample of accumulated depreciation account balances to test for calculation errors. We verified that the utility properly recorded retirements to accumulated depreciation when the corresponding plant was removed or replaced. We recalculated a sample of accumulated depreciation account balances as of December 31, 2006. We traced the working capital accounts to the general ledger, and reviewed any allocations of common accounts. We recalculated the utility's working capital balance as of December 31, 2006.

For net operating income, we reconciled the individual components of net operating income (NOI) balances to the utility's general ledger for the 12-month period ended December 31, 2006. We recalculated the adjustments, traced the components to the ledger and reviewed them with the last rate case. We obtained the December entry for the unbilled calculation and traced the components to source documentation. We sampled Operation and Maintenance (O&M) Expense items from the general ledger based on auditor judgment. We reviewed the sample for the proper utility system, classification, amount, period and recurring nature. We examined invoices and supporting documentation to determine if the audit objectives were met. We obtained the detail for direct and allocated salaries. We reviewed the allocation methodology and recomputed clearing amounts. We compared uncollectible expense to the four year average ratio of uncollectible amounts to revenue. We recalculated regulatory assessment fees and reconciled them to the general ledger. We reviewed the property tax bills and determined whether the amount booked reflects the discount amount. We compared the percent of payroll tax to total salaries for reasonableness. We recalculated depreciation expense for the period using Commission approved rates.

For capital structure, we reconciled the individual components of capital structure to balances in the utility's general ledger as of December 31, 2006. We recalculated the overall weighted cost of capital for the test year ended 2006. We compared actual debt balances and interest rates to the original loan agreements. We compared actual deferred tax balances to the taxes. We reconciled the common equity components and the investment tax credit components and recalculated the investment tax credit rate. We compared actual deposits to the utility records.

Q. Please review the audit findings in the audit report that are you are testifying on.

A. **Audit Finding No. 1**

Audit Finding No. 1 discusses missing invoices. The utility was unable to provide invoices and supporting documentation for several of the sample items. Because the utility was unable to support these items, they should be removed from rate base. The plant 13-month average should be reduced by $900,539.37, to remove these items. The accumulated depreciation 13-month average should be reduced by $125,449.15. The depreciation expense should be reduced $43,391.26.

Audit Finding No. 2

Audit Finding No. 2 discusses trucks transferred from the water division. The utility's Plant in Service includes two trucks transferred from its water company, which was sold in March 2003, a 1999 Ford 150 and a 2000 Ford. The transaction occurred in

September 2006 when the trucks were discovered during the inventory. When the electric company booked the acquisition of the trucks, it recorded the difference between the original cost and the accumulated depreciation as a gain. Since the vehicles were transferred to electric plant, the company applied the electric depreciation rate in calculating the depreciation expense from the time the trucks were purchased to the time they were transferred. I recalculated the depreciation expense using the correct rates and determined a different amount than the company's amount as of December 2006. In order to correct the plant and depreciation balances, I recommend that the plant 13-month average should be increased by $22.30, the accumulated depreciation 13-month average should be reduced by $14,532.41, and depreciation expense should be increased by $4,464.53.

Audit Finding No. 3

Audit Finding No. 3 discusses uncollectible expense. In 2006, the utility expensed $87,415 to electric for uncollectible expense. This amount was increased by $129,249 in the 2008 forecast for increased fuel rates and a projected increase in consumption. Actual write offs in 2006 were $58,025. The actual write offs were much less than the amount actually accrued by the utility. We compared the average of four years of write offs compared to revenue (net of industrial customers and interdepartmental revenue) as a test and found that the average is even less than the actual write offs. If the four year average write off is used, uncollectible expense should be reduced by $33,762.

Audit Finding No. 4

Audit Finding No. 4 discusses public relation expenses. In 2006, the utility paid Curly and Pynn for a multi media campaign, meetings with the key leadership at the utility to assign tasks and duties to educate the public in relation to the fuel increases, and meetings with the entire staff of each division to educate employees about the fuel increases. Account 913.4, Information and Instructional Advertising expense includes invoices totaling $120,405.89. In addition, Account 916, Miscellaneous Sales expense, was credited for an entry made to the 913.4 account of $5,354.38 for each division. The net amount recorded in the 2006 expenses was $109,697.13. In addition $29,808 was added to the 2008 expense for informing the customers about the fuel increase. The total included in the 2008 expenses was $147,205. Since the fuel increase is already in effect and the rate case will go into effect in 2008, the need for public relations may not extend for the four or five years that the rate increase will be in effect.

We annualized actual costs in the account as of September 2007. These amounted to $67,076 which is significantly less than the $147,205 projected. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses. The utility increased this account by 103.4% in 2007 and 103.5% in 2008 for customer growth and inflation.

Audit Finding No. 5

Audit Finding No. 5 discusses legal costs and mailing. Included in account 928, Regulatory Commission expense, were 2006 costs of $34,249.67 paid to Messer, Caparello and Self for work related to obtaining the new fuel contracts and for expanding the territory. The fuel contracts will not be renewed for another ten years. Therefore, these costs may not be recurring. These costs have been trended up by 102.2% in 2007 and 102.3% in 2008.

The utility also included postage and printing costs for mailing a letter regarding increased electric costs in account 923.1, Outside Services, for $6,609.96. This account was trended up using the same factors for a total of $6,911.

The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

Audit Finding No. 6

Audit Finding No. 6 discusses a customer survey. In 2006, the utility charged account 916, Miscellaneous Sales expenses, $25,600 for a customer survey. The costs were split equally between Marianna and Fernandina. The account was trended up using inflation and customer growth of 103.4% in 2007 and 103.5% in 2008 or a total of $27,397. The utility plans to continue doing surveys in the future but they may not be as extensive as this one and may cost less. Continuing surveys may only address one aspect of customer service as opposed to the extensive approach used in this one.

Schedule C-7, Operation and Maintenance Expenses, for 2008 shows less in the account due to a credit that was posted to the wrong account as described in the audit finding on public relations costs.

The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

Audit Finding No. 7

Audit Finding No. 7 discusses Opportunity Florida. Marianna account 930.23, Economic Development expense, includes $5,000 for membership dues to Opportunity Florida. The utility joined this organization for networking opportunities with other industries. The 930.23 account was trended up using inflation and customer growth of 103.4% in 2007 and 103.5% in 2008 or a total of $5,351. If the Commission does not determine that the membership benefits the customers, these costs should be removed.

Audit Finding No. 8

Audit Finding No. 8 discusses office construction. Marianna's account 935, Maintenance of General Plant, includes $2,219 to construct a wall in the office in March 2006. The account was trended up using inflation and customer growth of 103.4% in 2007 and 103.5% in 2008 for a total of $2,375. This amount should be capitalized in

Structures and Improvements and depreciated at 2%. I recommend that expenses in 2008 should be reduced by $2,375, Plant in 2006 should be increased by the average of $1,707, average accumulated depreciation should be increased by $16, and Depreciation expense should be increased by $37.

Audit Finding No. 9

Audit Finding No. 9 discusses travel expenses. Marianna's account 588.2, Other Distribution Expense, includes $677.69 of airline expenses for the wife of its safety contractor. This account was trended up by payroll and customer growth of 106.8% in 2007 and 106.8% in 2008 for a total of $773. Because this is not a utility expense, I recommend that expenses should be reduced by $773 in 2008.

Audit Finding No. 10

Audit Finding No. 10 discusses a transformer pad. Fernandina's account 595.3, Maintenance of Transformers, includes $2,400 to remove a pad and set a new transformer at the Ritz Carlton Hotel in August 2006. The account was trended up using payroll and customer growth of 106.8% in 2007 and 106.8% in 2008 for a total of $2,738. This amount should be capitalized to account 115.1010.368 and depreciated at 4.2%. I recommend that expenses should be reduced by $2,738 in 2008, Plant in 2006 should be increased by the average of $923, average accumulated depreciation should be increased by $10, and Depreciation expense should be increased by $42.

Audit Finding No. 11

Audit Finding No. 11 discusses moving expenses. The utility paid moving expenses for the new Division Manager. A deposit on a rental house and two months rent were paid in January 2006. The total costs for this expense report were $3,734.21. Moving costs may not be recurring. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

Audit Finding No. 12

Audit Finding No. 12 discusses substation maintenance. In its "over and above" expenses included in 2008 projected test year expenses on Schedule C-7, Operation and Maintenance Expenses, the utility included an amount for annual inspection and maintenance of the substations. The utility proposes to implement this program because lack of maintenance has caused failures. We could not determine if some of the expenses found in 2006 may not have occurred if this program had been in effect sooner. The utility did not make any allowance in its "over and above" calculation for a decrease in repairs. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

Audit Finding No. 13

Audit Finding No. 13 discusses storm reserve. Commission Order No. PSC-04-0369-AS-EI allowed for an annual increase to the storm reserve of $121,625 with additional increases if the utility did not spend $22,641, annually, for economic development. In 2006, the amount applied to the storm reserve was $16,758. In its projected expenses for account 924 for 2008, the utility proposed an increase to the annual accrual to the reserve to $203,880, plus the $16,758 of unused economic development costs calculated in 2006. The $16,758 should be removed as it should not be recurring in the future.

The utility has included $5,000 of economic development costs in its 2006 test year which were trended up to $5,351. It has also included an additional $10,350 for economic development in its estimate of over and above expenses on C-7, Operation and Maintenance Expenses, for 2008 for its Fernandina division.

The 2008 forecast should be reduced by the $16,758 for economic development costs. The Commission may put a similar recommendation in this rate order for the new economic development forecast of $15,701, but if the order is worded the same, costs will only go to the storm reserve if they are not expensed as planned in the economic development forecast. The new storm allowance accrual should also be reviewed for reasonableness.

<u>Audit Finding No. 14</u>

Audit Finding No. 14 discusses the medical benefit forecast. In the 2008 projected expenses in C-7 for account 926.2, Employee Benefits, Medical, the utility included an 11.4% increase in its medical benefits for 2008. The utility has received a revised estimate from Cigna Health Care which indicates a 34.78% increase in 2008 insurance expense. This would increase the projection from $543,969 to $650,336 or an increase of $106,367

<u>Audit Finding No. 15</u>

Audit Finding No. 15 discusses overhead. The utility added several salaries in its "over and above" expense increases on C-7, Operation and Maintenance Expenses, for its 2008 expense projection. The salary computations included a 37-38% overhead calculation. This calculation included vacation, holiday and sick leave which do not increase the base pay. Based on 2006 actual costs, we determined the actual 2006 overhead for pension, taxes and insurance to be 30.65%. In order to reduce expenses to the actual level, I recommend that expenses for 2008 should be reduced by $17,735.78.

<u>Audit Finding No. 16</u>

Audit Finding No. 16 discusses the allocation of clearing accounts. The utility puts several expenses in its 1840 clearing accounts. These accounts are not allocated to all divisions but instead are charged to the divisions through the payroll entry. The allocation through payroll does not allocate as much expense to non-regulated operations as the regular allocation process. They are all payroll related costs. Based on the payroll allocation used by the utility in 2006, 26% of payroll relates to propane and merchandising and jobbing. If the payroll allocation is used, expenses allocated to electric would decrease by $204,264.05. Adjusting this amount for the 2007 and 2008 trending used by the utility, I recommend that expenses for 2008 should be reduced by $262,452.31.

Audit Finding No. 17

Audit Finding No. 17 compares actual 2007 costs to the 2007 forecast. We annualized the 2007 expenses as of September 30, 2007 and compared them to the forecast on schedule C-7 (2007), Operation and Maintenance Expenses, of the filing. The actual annualized costs were $488,245.33 less than the filing expenses for 2007. Many of the differences related to accounts that had "over and above" expense adjustments. The "over and above" expenses total $574,896 in 2007. The only over and above amounts that appear to have been substantially incurred were the general liability account 925.2 and the maintenance of underground lines account 594.2. The audit report includes a schedule showing the annualized expenses, by account, compared to the forecast.

Q. Does that conclude your testimony?

A. Yes.

DOCKET NO. 070304-EI: Petition for rate increase by Florida Public Utilities Company

WITNESS: **Direct Testimony Of Kathy L. Welch,** Appearing On Behalf Of Staff

EXHIBIT KLW-1: History of Testimony Provided by Kathy L. Welch

Docket No. 070304-EI
Exhibit KLW-1 (Page 1 of 1)
History of Testimony
Provided by Kathy L. Welch

- In re: Application for approval of rate increase in Lee County by Tamiami Village Utility, Inc., Docket No. 910560-WS

- In re: Application for transfer of territory served by Tamiami Village Utility, Inc. in Lee County to North Fort Myers Utility, Inc., cancellation of Certificate No. 332-S and amendment of Certificate 247-S; and for a limited proceeding to impose current rates, charges, classifications, rules and regulations, and service availability policies, Docket No. 940963-SU

- In re: Application for a rate increase by General Development Utilities, Inc. (Port Malabar Division) in Brevard County, Docket No. 911030-WS

- In re: Dade County Circuit Court referral of certain issues in Case No. 92-11654 (Transcall America, Inc. d/b/a ATC Long Distance vs. Telecommunications Services, Inc., and Telecommunications Services, Inc. vs. Transcall America, Inc. d/b/a ATC Long Distance) that are within the Commission's jurisdiction, Docket No. 951232-TI

- In re: Application for transfer of Certificates Nos. 404-W and 341-S in Orange County from Econ Utilities Corporation to Wedgefield Utilities, Inc., Docket No. 960235-WS

- In re: Application for increase in rates and service availability charges in Lee County by Gulf Utility Company, Docket No. 960329-WS

- In re: Fuel and purchased power cost recovery clause and generating performance incentive factor, Docket No. 010001-EI

- In re: Application for staff-assisted rate case in Highlands County by The Woodlands of Lake Placid, L.P., Docket No. 020010-WS

- In re: Application for rate increase in Marion, Orange, Pasco, Pinellas, and Seminole Counties by Utilities, Inc. of Florida, Docket No. 020071-WS

- In re: Petition for issuance of a storm recovery financing order, by Florida Power & Light Company, Docket No. 060038-EI

DOCKET NO. 070304-EI: Petition for rate increase by Florida Public Utilities Company

WITNESS: **Direct Testimony Of Kathy L. Welch,** Appearing On Behalf Of Staff

EXHIBIT KLW-2: Audit Report

FLORIDA PUBLIC SERVICE COMMISSION

DIVISION OF REGULATORY COMPLIANCE & CONSUMER ASSISTANCE
BUREAU OF AUDITING

Miami District Office

FLORIDA PUBLIC UTILITIES COMPANY
ELECTRIC DIVISION

FILE AND SUSPEND RATE CASE INVESTIGATION

AS OF DECEMBER 31, 2006
FORECAST DECEMBER 31, 2008

DOCKET NO. 070304-EI
AUDIT CONTROL NO. 07-262-4-1

Yen Ngo, Audit Manager

Iliana Piedra, Audit Staff

Daniel Acheampong, Audit Staff

Kathy L. Welch, Public Utilities Supervisor

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DIVISION OF REGULATORY COMPLIANCE & CONSUMER ASSISTANCE AUDITOR'S REPORT

December 12, 2007

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

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 September 18, 2007. We have applied these procedures to the 2006 actual and 2008 projected costs on the attached schedules which were prepared by Florida Public Utilities Company-Electric Division in support of its filing for rate relief in Docket No. 070304-EI.

This audit was performed following general standards and field work standards found in the AICPA Statements on Standards for Attestation Engagements. This report is based on agreed upon procedures which are only for internal Commission use.

OBJECTIVES AND PROCEDURES

RATE BASE

General

Objective: To determine that the utility's filing represents its recorded results from continuing operations. To verify, for the historical year, that all adjustments are consistent with the prior rate cases and calculated correctly.

Procedures: We reconciled the rate base supporting schedules and traced those to the general ledger. We obtained supporting documentation for all adjustments in 2006, recalculated the adjustments, traced amounts to the ledgers, and reviewed prior orders. We reviewed the board of directors' minutes, the internal audit reports and the external audit workpapers.

Utility Plant

Objective: To verify plant additions, retirements and adjustments from the last historic year through December 31, 2006 and obtain supporting documentation for the plant forecast for 2007 and 2008. To review the utility continuing property records and determine if they are in compliance with Commission Rule 25-6.014(3), Florida Administrative Code.

Procedures: We sampled plant additions for the period January 1, 2003 through December 31, 2006 for compliance with the stated objectives above. We verified that the utility properly recorded retirements when a capital item was removed or replaced. We sampled construction project additions and the corresponding source documentation. We obtained the supporting documentation for the forecast plant but no audit was completed of the data due to time constraints.

Customer Advances

Objective: To determine that additions to Customer Advances from 2003 to 2006 are properly recorded.

Procedures: We sampled Customer Advance additions for the period January 1, 2003 through December 31, 2006 for compliance with the stated objectives above and traced them to contracts.

Accumulated Depreciation

Objective: To determine that accruals to accumulated depreciation in 2006 are properly recorded in compliance with the NARUC Uniform System of Accounts. To verify that depreciation expense accruals are calculated using the Commission authorized rates and that retirements are properly recorded.

Procedures: We traced the accumulated depreciation schedules to the corresponding plant in service schedules. We verified that the utility used Commission authorized rates to depreciate its plant accounts by calculating a sample of accumulated depreciation account balances to test for calculation errors. We verified that the utility properly recorded retirements to accumulated depreciation when the corresponding plant was removed or replaced. We recalculated a sample of accumulated depreciation account balances as of December 31, 2006.

Working Capital

Objective: To determine that the utility's working capital balance is properly calculated and consistent with the last order. Also, to determine if any interest earning or bearing accounts or any non-utility items were included in the calculation.

Procedures: We traced the working capital accounts to the general ledger, and reviewed any allocations of common accounts. We recalculated the utility's working capital balance as of December 31, 2006.

NET OPERATING INCOME

General

Objective: To determine that the utility's filing represents its results from continuing operations. To determine that the adjustments to the filing were properly calculated, and consistent with prior orders.

Procedures: We reconciled the following individual components of projected net operating income (NOI) balances to the utility's general ledger for the 12-month period ended December 31, 2006. We recalculated the adjustments, traced the components to the ledger and reviewed them with the last rate case.

Revenues

Objective: To determine that revenues in 2006 are properly recorded in compliance with Commission rules and are based on the utility's Commission approved tariff rates. To verify the calculation of unbilled revenues.

Procedures: We traced revenues to the general ledger and utility billing registers and selected a sample of customer bills from each customer rate class on a random basis, and recalculated the bills using the Commission approved tariff rates. We obtained the December entry for the unbilled calculation and traced the components to source documentation.

Operation and Maintenance Expenses (O&M)

Objective: To determine that operation and maintenance expenses in 2006 are properly recorded in compliance with Commission rules and were reasonable and prudent for ongoing utility operations. To determine if any costs related to non-regulated operations were included. To determine if any costs were out of period or non-recurring. To determine if corporate costs allocated related to electric operations. To determine if advertisements included are image enhancing or relate to conservation or fuel. To determine if refunds were properly recorded.

Procedures: We sampled O&M expense items from the general ledger based on auditor judgment. We reviewed the sample for the proper utility system, classification, amount, period and recurring nature. We examined invoices and supporting documentation to determine if the above objectives were met. We obtained the detail for direct and allocated salaries. We reviewed the allocation methodology and recomputed clearing amounts. We compared uncollectible expense to the four year average ratio of uncollectible amounts to revenue.

Taxes-Other-Than-Income

Objective: To determine that taxes other than income tax expense in 2006 is properly recorded and reasonable and prudent for ongoing utility operations.

Procedures: We recalculated regulatory assessment fees and reconciled them to the general ledger. We reviewed the property tax bills and determined whether the amount booked reflects the discount amount. We compared the percent of payroll tax to total salaries for reasonableness.

Depreciation Expense

Objective: To determine that depreciation expense is properly recorded in compliance with Commission rules and that it accurately represents the depreciation of plant assets.

Procedures: We recalculated depreciation expense for the period using Commission approved rates.

CAPITAL STRUCTURE

General

Objective: 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 properly recorded and that the components accurately represent the ongoing utility operations. To verify that non-utility assets, supported by the utility's capital structure, are removed from the capital structure, in the rate base/capital structure reconciliation. To verify that the non-utility investments are removed from equity, prior to the determination of debt/equity ratios. To verify that the cost rates are appropriate. To determine how the rate base adjustments are adjusted in the capital structure.

Procedures: We reconciled the following individual components of capital structure to balances in the utility's general ledger as of December 31, 2006. We recalculated the overall weighted cost of capital for the test year ended 2006.

Long-Term-Debt

Objective: To determine that long-term debt balances represent actual obligations of the utility's parent and that they are properly recorded.

Procedures: We compared actual debt balances and interest rates to the original loan agreements.

Short-Term-Debt

Objective: To determine that short-term debt balances represent actual obligations of the utility's parent and that they are properly recorded.

Procedures: We compared actual debt balances and interest rates to the original loan agreements.

Accumulated Deferred Income Taxes

Objective: To determine that accumulated deferred income taxes are properly stated and calculated based on the recorded differences between utility book and taxable income.

Procedures: We compared actual deferred tax balances to the taxes. We reconciled the common equity components and the investment tax credit components and recalculated the investment tax credit rate.

Customer Deposits

Objective: To determine that customer deposit balances represent actual obligations of the utility and are properly recorded.

Procedures: We compared actual deposits to the utility's records.

AUDIT FINDING NO. 1

SUBJECT: MISSING INVOICES

AUDIT ANALYSIS: The utility was unable to provide invoices and supporting documentation for the following sample items. Because the utility was unable to support these items, they should be removed from rate base.

Acct. No.	Period	Description	Date	JE	Amount	Plant Allocation 2006
2003						
	2003					
100.1070.39˙	Jul-03	Kubra Data T	8/12/2003		10,000.00	2,900.00
100.1070.397	May-03	Sprint	6/6/2003		46,000.00	13,800.00
114.1070.366	Nov-03	PS & S Elect	12/9/2003		2,650.00	2,650.00
115.1070.366	Aug-03	Sea Coast Gı	9/9/2003		4,900.00	4,900.00
115.1070.366	Aug-03	Oldcastle Pre	9/10/2003		4,177.68	4,177.68
115.1070.368	Sep-03	Hughs Suppl·	10/8/2003		17,604.71	17,604.71
115.1070.368	Sep-03	Cooper Powe	10/9/2003		54,154.00	54,154.00
		Total Depreciation Expense			139,486.39	100,186.39
2004	2004					
100.1070.376	Dec-04	Several Inv A	1/18/2005	33	111,496.44	33,448.93
114.1070.362	Dec-04	PPO	1/11/2005	33	44,255.60	44,255.60
114.1070.364	Aug-04	Utilicon Servi	9/10/2004		5,206.89	5,206.89
114.1070.364	Aug-04	P Local Non-	8/31/2004	9	3,970.00	3,970.00
114.1070.365	Dec-04	Transfer Cha	1/27/2005	5.33	30,863.16	30,863.16
114.1070.392	Jan-04	Altec Industri	2/11/2004		194,165.98	194,165.98
115.1070.362	Feb-04	Siemens Pov	3/10/2004		149,734.56	149,734.56
115.1070.362	Apr-04	Siemens Pov	5/10/2004		142,325.88	142,325.88
115.1070.362	May-04	Southern Sta	6/8/2004		106,006.49	106,006.49
115.1070.364	Dec-04	Pike Electric	1/11/2005	33	2,027.94	2,027.94
115.1070.365	Dec-04	Zero Vouche	1/18/2005		14,049.23	14,049.23
115.1070.366	May-04	Gateway to A	5/31/2004	3	12,099.00	12,099.00
115.1070.366	Nov-04	David Miller	12/8/2004		30,631.00	30,631.00
115.1070.368	Feb-04	Hughes Supp	3/10/2004		11,945.92	11,945.92
		Total Depreciation Expense			858,778.09	780,730.58
2005	2005					
115.1070.365	Aug-05	Pike Electric	9/12/2005		5,584.00	5,584.00
115.1070.370	Mar-05	GE Supply	4/11/2005		11,008.16	11,008.16
115.1070.370	Nov-05	GE Supply	12/13/2005		3,030.24	3,030.24
		Total Depreciation Expense			19,622.40	19,622.40
		Total 2006 Adjustment			1,017,886.88	900,539.37

The depreciation was calculated as follows:

Acct. No.	Period	JE	Plant Allocation 2003	2004	2005	2006	Depreciation Expense 2003	2004	2005	2006	Accumulated Depreciation Total
2003											
	2003										
100.1070.3913	Jul-03		32%	31%	32%	29%	320.00	620.00	640.00	580.00	2,160.00
100.1070.397	May-03		27%	31%	30%	30%	1,656.00	2,852.00	2,760.00	2,760.00	10,028.00
114.1070.3662	Nov-03						8.83	53.00	53.00	53.00	167.83
115.1070.3662	Aug-03						40.83	98.00	98.00	98.00	334.83
115.1070.3663	Aug-03						34.81	83.55	83.55	83.55	285.47
115.1070.3681	Sep-03						246.47	739.40	739.40	739.40	2,464.66
115.1070.3683	Sep-03						758.16	2,274.47	2,274.47	2,274.47	7,581.56
Total Depreciation Expense							3,065.10	6,720.42	6,648.42	6,588.42	23,022.36
2004											
100.1070.376	Dec-04	33	27%	31%	30%	30%		72.01	836.22	836.22	1,744.45
114.1070.362	Dec-04	33						110.64	1,327.67	1,327.67	2,765.98
114.1070.364.6	Aug-04							91.12	218.69	218.69	528.50
114.1070.3647	Aug-04	9						69.48	166.74	166.74	402.96
114.1070.3657	Dec-04	5.33						97.73	1,172.80	1,172.80	2,443.33
114.1070.3923	Jan-04							18,445.77	18,445.77	18,445.77	55,337.30
115.1070.362	Feb-04							4,117.70	4,492.04	4,492.04	13,101.77
115.1070.362	Apr-04							3,202.33	4,269.78	4,269.78	11,741.89
115.1070.362	May-04							2,120.13	3,180.19	3,180.19	8,480.52
115.1070.3648	Dec-04	33						7.10	85.17	85.17	177.44
115.1070.3656	Dec-04							44.49	533.87	533.87	1,112.23
115.1070.3662	May-04	3						161.32	241.98	241.98	645.28
115.1070.3662	Nov-04							102.10	612.62	612.62	1,327.34
115.1070.3681	Feb-04							459.92	501.73	501.73	1,463.38
Total Depreciation Expense								29,101.83	36,085.27	36,085.27	101,272.37
2005											
115.1070.3657	Aug-05								88.41	212.19	300.61
115.1070.370	Mar-05								330.24	396.29	726.54
115.1070.370	Nov-05								18.18	109.09	127.27
Total Depreciation Expense									436.84	717.57	1,154.41
Total										43,391.26	125,449.15

EFFECT ON THE GENERAL LEDGER: The following journal entry should be made to correct the utility's general ledger balances.

Accumulated Depreciation	125,449.15	
Retained Earnings	818,481.48	
Plant		900,539.34
Depreciation Expense		43,391.26

EFFECT ON THE FILING: The plant 13-month average should be reduced by $900,539.37. The accumulated depreciation 13-month average should be reduced by $125,449.15. The depreciation expense should be reduced $43,391.26.

AUDIT FINDING NO. 2

SUBJECT: TRUCKS TRANSFERRED FROM WATER

AUDIT ANALYSIS: The utility's Plant in Service includes two trucks transferred from its water company, which was sold in March 2003, a 1999 Ford 150 and a 2000 Ford. The transaction occurred in September 2006 when the trucks were discovered during the inventory.

When the electric company booked the acquisition of the trucks, it recorded the difference between the original cost and the accumulated depreciation as a gain. Since the vehicles were transferred to electric plant, the company applied the electric depreciation rate in calculating the depreciation expense from the time the trucks were purchased to the time they were transferred.

The audit recalculation of the depreciation expense revealed a different amount than the company's amount as of December 2006. Below is staff's recalculation of the depreciation expense for the trucks.

1999 Ford Truck (Truck 1)

	1999	2002
Depreciation Rate	4.70%	11.30%
Actual cost	19,410.51	

Date	Depreciation Base	Depreciation Rate	Yearly Depreciation	Book Value
Jul-99	19,410.51	4.70%	456.15	18,954.36
Dec-00	19,410.51	4.70%	912.29	18,042.07
Dec-01	19,410.51	4.70%	912.29	17,129.78
Dec-02	19,410.51	11.30%	2,193.39	14,936.39
Dec-03	19,410.51	11.30%	2,193.39	12,743.00
Dec-04	19,410.51	11.30%	2,193.39	10,549.61
Dec-05	19,410.51	11.30%	2,193.39	8,356.22
Dec-06	19,410.51	11.30%	2,193.39	6,162.84
Total Accumulated Dep.			13,247.67	

2000 Ford Truck (Truck 2)

	1999	2002
Depreciation Rate	4.70%	11.30%
Actual cost	20,098.60	

Date	Depreciation Base	Depreciation Rate	Yearly Depreciation	Book Value
Jul-00	20,098.60	4.70%	472.32	(472.27)
Dec-01	20,098.60	4.70%	944.63	(1,416.90)
Dec-02	20,098.60	11.30%	2,271.14	(3,688.05)
Dec-03	20,098.60	11.30%	2,271.14	(5,959.19)
Dec-04	20,098.60	11.30%	2,271.14	(8,230.33)
Dec-05	20,098.60	11.30%	2,271.14	(10,501.47)
Dec-06	20,098.60	11.30%	2,271.14	(12,772.61)
Total Accumulated Depr.			12,772.66	

Recalculated Accumulated Depr.	Truck 1 Above	13,247.67
	Truck 2 Above	12,772.66
		26,020.33
Company's Accumulated Depr.	Truck 1	(15,897.02)
	Truck 2	(14,183.23)
		(30,080.25)
Difference		(4,059.92)

EFFECT ON THE GENERAL LEDGER: The following journal entries should be made to correct the utility's general ledger balances. (See the differences on page 8 for explanation.)

Truck 1		
Plant	6.15	
Depreciation Expense	2,193.39	
Accumulated Depreciation	2,649.35	
Retained Earnings		4,848.89
Truck 2		
Plant	16.15	
Depreciation Expense	2,271.14	
Accumulated Depreciation	1,410.57	
Retained Earnings		3,697.86

EFFECT ON THE FILING: The plant 13-month average should be increased by \$22.30. The accumulated depreciation 13-month average should be reduced by \$14,532.41 (7,259.59 + 7273.02). Depreciation expense should be increased by \$4,464.53. See attached schedule for the calculation of these adjustments.

13-Month Average Effect 2006

	Truck 1			Truck 2		
	Per Staff	Per Company	Diff.	Per Staff	Per Company	Diff.
Beginning Balance	11,054.29		11,054.29	10,501.52		10,501.52
Jan-06	11,237.07		11,237.07	10,690.78		10,690.78
Feb-06	11,419.85		11,419.85	10,880.04		10,880.04
Mar-06	11,602.63		11,602.63	11,069.30		11,069.30
Apr-06	11,785.41		11,785.41	11,258.57		11,258.57
May-06	11,968.20		11,968.20	11,447.83		11,447.83
Jun-06	12,150.98		12,150.98	11,637.09		11,637.09
Jul-06	12,333.76		12,333.76	11,826.35		11,826.35
Aug-06	12,516.54		12,516.54	12,015.61		12,015.61
Sep-06	12,699.33	15,897.02	(3,197.69)	12,204.87	14,183.23	(1,978.36)
Oct-06	12,882.11	15,897.02	(3,014.91)	12,394.14	14,183.23	(1,789.09)
Nov-06	13,064.89	15,897.02	(2,832.13)	12,583.40	14,183.23	(1,599.83)
Dec-06	13,247.67	15,897.02	(2,649.35)	12,772.66	14,183.23	(1,410.57)
13-Month Average	12,150.98	4,891.39	7,259.59	11,637.09	4,364.07	7,273.02

Truck 1				
Per Company				
Plant		19,404.36		
	Accumulated Depreciation		15,897.02	
	Gain		3,507.34	
Per Staff				
Plant		19,410.51		
Dep Exp		2,193.39		
	Accumulated Depreciation		13,247.67	p.8
	Retained Earnings		8,356.23	
Adjustments p.9				
Plant		6.15		
Dep Exp		2,193.39		
	Accu Dep	2,649.35		
	Retained Earnings		4,848.89	
Truck 2				
Per Company				
Plant		20,082.45		
	Accumulated Depreciation		14,183.23	
	Gain		5,899.22	
Per Staff				
Plant		20,098.60		
Dep Exp		2,271.14		
	Accumulated Depreciation		12,772.66	p.8
	Retained Earnings		9,597.08	
Adjustments p.9				
Plant		16.15		
Dep Exp		2,271.14		
	Accumulated Depreciation	1,410.57		
	Retained Earnings		3,697.86	
Total Adjustments				
Plant		22.30	p. 9	
Depreciation Expense		4,464.53	p. 9	
	Accumulated Depreciation	4,059.92	p. 8	

AUDIT FINDING NO. 3

SUBJECT: UNCOLLECTIBLE EXPENSE

AUDIT ANALYSIS: In 2006, the utility expensed $87,415 to electric operations for uncollectible expense. This amount was increased by $129,249 in the 2008 forecast for increased fuel rates and a projected increase in consumption. The $87,415 was determined as follows:

	Marianna	Fernandina	Total
Accounts due over 90 days 12/31/06	59,984.92	62,074.74	122,059.66
Less estimated to be collected by Div. managers		(27,028.15)	(27,028.15)
	59,984.92	35,046.59	95,031.51
Accounts due under 90 days	1,478,790.40	1,608,446.60	3,087,237.00
Percent estimated to be lost	0.22000%	0.90000%	
	3,253.34	14,476.02	17,729.36
Total estimated over and under 90 days	63,238.26	49,522.61	112,760.87
Less beginning balance uncollectible	18,806.00	5,121.00	23,927.00
Net to be accrued	44,432.26	44,401.61	88,833.87
Less propane and merchandising and jobbing			(1,418.87)
			87,415.00

Actual write offs in 2006 were $58,025 or .184% in Marianna and .101% in Fernandina. The actual write offs were much less than the amount actually accrued by the utility. The average rate of four years of write offs compared to revenue net of industrial customers and interdepartmental revenue is .182% for Marianna and .084% for Fernandina. The average is even less than the actual write offs. If the four year average write off of .00136 is used, uncollectible expense would be reduced by $33,762. ($39,450,684 revenue 2006 x average rate .00136=$53,653; difference between $53,653-$84,415 booked above=$33,762)

EFFECT ON THE LEDGER: This entry would be made for the filing only.

EFFECT ON THE FILING: Expenses would be reduced by $33,762.

AUDIT FINDING NO. 4

SUBJECT: PUBLIC RELATION EXPENSES

AUDIT ANALYSIS: In 2006, the utility paid Curly and Pynn for the following:

1. Developed and integrated a multi media campaign, to educate FPUC customers, which included home energy makeover events, public speaking engagements, letters to the editor of the local newspapers, talking points for employees, etc.

2. Scheduled and organized meetings with the key leadership in both divisions and worked with the division management to assign certain tasks and duties of the team to address the need to educate the public in relation to the fuel increases.

3. Scheduled and organized meetings with the entire staff of each division to educate employees about the fuel increases.

Account 913.4, Information and Instructional Advertising expense includes invoices for Curley and Pynn of $60,202.52 in Marianna and $60,203.37 in Fernandina for a total of $120,405.89. Account 916, Miscellaneous Sales Expense, was credited for an entry made to the 913.4 account of $5,354.38 for each division. The net amount recorded in the 2006 expenses was $109,697.13.

The utility increased this amount by 103.4% in 2007 and 103.5% in 2008 for customer growth and inflation. In addition $29,808 was added for informing the customers about the fuel increase. The total included in the 2008 expenses was $147,205.

Since the fuel increase is already in effect and the rate case will go into effect in 2008, the need for public relations may not extend for the four or five years that the rate increase will be in effect. We annualized actual costs in account 913.4 as of September 2007. This resulted in an amount of $67,076 which is significantly less than the $147,205 projected.

The utility should provide support that establishes the need for these costs to continue during the next four years.

EFFECT ON THE GENERAL LEDGER: This finding is provided for informational purposes only.

EFFECT ON THE FILING: This finding is provided for informational purposes only. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

AUDIT FINDING NO. 5

SUBJECT: LEGAL AND MAILING

AUDIT ANALYSIS: Included in account 928, Regulatory Commission expense, were costs paid to Messer, Caparello and Self for costs related to obtaining the new fuel contracts of $16,301.71 for each Marianna and Fernandina and $1,646.25 for expanding the territory for a total of $34,249.67 in 2006. The fuel contracts will not be renewed for another ten years. Therefore, these costs may not be recurring. These costs have been trended up by 102.2% in 2007 and 102.3% in 2008.

The utility also included postage and printing costs for mailing a letter regarding increased electric costs in account 923.1, Outside Services, for $6,609.96. This account was trended up by inflation of 102.2% in 2007 and 102.3% in 2008 for a total of $6,911.

EFFECT ON THE GENERAL LEDGER: This finding is provided for informational purposes only.

EFFECT ON THE FILING: This finding is provided for informational purposes only. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

AUDIT FINDING NO. 6

SUBJECT: CUSTOMER SURVEY

AUDIT ANALYSIS: In 2006, the utility charged to account 916, Miscellaneous Sales expense, $25,600 for a customer survey. The costs were split equally between Marianna and Fernandina. The 916 account was trended up using inflation and customer growth of 103.4% in 2007 and 103.5% in 2008 for a total of $27,397. The utility plans to continue doing surveys in the future but they may not be as extensive as this one and may cost less. Continuing surveys may only address one aspect of customer service as opposed to the extensive approach used in this one.

Schedule C-7, Operation and Maintenance Expenses, for 2008 shows less in the account due to a credit that was posted to the wrong account as described in the audit finding on public relations costs.

EFFECT ON THE GENERAL LEDGER: This finding is provided for informational purposes only.

EFFECT ON THE FILING: This finding is provided for informational purposes only. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

AUDIT FINDING NO. 7

SUBJECT: MEMBERSHIP OPPORTUNITY FLORIDA

AUDIT ANALYSIS: Marianna account 930.23, Economic Development includes $5,000 for membership dues to Opportunity Florida. The utility joined this organization for networking opportunities with other industries.

The 930.23 account was trended up using inflation and customer growth of 103.4% in 2007 and 103.5% in 2008 or a total of $5,351.

If the Commission does not determine that the membership benefits the customers, these costs should be removed.

EFFECT ON THE GENERAL LEDGER: This finding is provided for informational purposes only.

EFFECT ON THE FILING: If the Commission does not believe the membership benefits the customers, $5,351 should be removed from 2008 expenses.

AUDIT FINDING NO. 9

SUBJECT: TRAVEL

AUDIT ANALYSIS: Marianna's account 588.2, Other Distribution Expense, includes $677.69 of airline expenses for the wife of its safety contractor. This account was trended up by payroll and customer growth of 106.8% in 2007 and 106.8% in 2008 for a total of $773.

EFFECT ON THE GENERAL LEDGER: This finding has no effect on balance sheet accounts in 2006 so no adjustment is necessary to the ledger.

EFFECT ON THE FILING: Expenses should be reduced by $773 in 2008.

AUDIT FINDING NO. 10

SUBJECT: TRANSFORMER PAD

AUDIT ANALYSIS: Fernandina's account 595.3, Maintenance of Transformers, included \$2,400 to remove a pad and set a new transformer at the Ritz Carlton Hotel in August 2006. The account was trended up using payroll and customer growth of 106.8% in 2007 and 106.8% in 2008 for a total of \$2,738. This amount should be capitalized to account 115.1010.368 and depreciated at 4.2%.

Month	Plant	Depreciation Expense	Accumulated Depreciation
August	2,400.00	8.40	8.40
September	2,400.00	8.40	16.80
October	2,400.00	8.40	25.20
November	2,400.00	8.40	33.60
December	2,400.00	8.40	42.00
Total	12,000.00	42.00	
13-month average	923.08	3.23	9.69

EFFECT ON THE GENERAL LEDGER: The following entry should be made:

	DEBIT	CREDIT
Depreciation Expense	42	
Plant	2,400	
Accumulated Depreciation		42
Retained Earnings		2,400

EFFECT ON THE FILING: Expenses should be reduced by \$2,738 in 2008. Plant in 2006 should be increased by the average of \$923. Average accumulated depreciation should be increased by \$10. Depreciation expense should be increased by \$42.

AUDIT FINDING NO. 11

SUBJECT: MOVING EXPENSES

AUDIT ANALYSIS: The utility paid moving expenses for the new Division Manager. A deposit on a rental house and two months rent were paid in January 2006. The total costs for this expense report were $3,734.21 and were allocated to the following accounts:

		2006	2007	2008
115.4010.580	Fernandina Operation Supervision	1,172.81	1,237.31	1,305.37
115.4010.901	Fernandina Customer Account Supervision	1,136.16	1,198.65	1,264.57
115.4020.590	Fernandina Distribution Maintenance	1,136.16	1,198.65	1,264.57
995.4010.901	Propane	219.91		
115.1430.1	Fernandina	69.17		
		3,734.21	3,634.61	3,834.52

Moving costs may not be recurring. The utility should provide support that establishes the need for these costs to continue during the next four years.

EFFECT ON THE GENERAL LEDGER: This finding is provided for informational purposes only.

EFFECT ON THE FILING: This finding is provided for informational purposes only. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

AUDIT FINDING NO. 12

SUBJECT: SUBSTATION MAINTENANCE

AUDIT ANALYSIS: In it's "over and above" expenses included in 2008 projected test year expenses on filing C-7, Operation and Maintenance Expenses, the utility included an amount for annual inspection and maintenance of the substations. The utility proposes to implement this program because lack of maintenance has caused failures. We could not determine if some of the expenses found in 2006 may not have occurred if this program had been in effect sooner. The utility did not make any allowance in it's "over and above" calculation for a decrease in repairs. Some of the higher costs in 2006 are:

Account	Date	Vendor	Description	Amount
115.4020.570	4/7/2006	Megaway	Eng. Serv. For Stepdown Station	2,400.00
115.4020.570	7/7/2006	Tempaco		4,675.02
115.4020.570	6/23/2006	Hughes Supply		4,152.46
115.4020.592	5/3/2006	Industrial Electronics	Breaker and Relay testing for outage	3,483.90
115.4020.592	3/1/2006	GE International	AIP Substation Transformer failed	9,416.00
				24,127.38

Engineering staff needs to determine if these costs will be recurring if an inspection and testing maintenance program is implemented.

The utility should provide support that establishes the need for these costs to continue during the next four years.

EFFECT ON THE GENERAL LEDGER: This finding is provided for informational purposes only.

EFFECT ON THE FILING: This finding is provided for informational purposes only. The Commission may decide to amortize costs that are not recurring over the estimated period the new rates will be in effect which would reduce expenses.

AUDIT FINDING NO. 13

SUBJECT: STORM RESERVE

AUDIT ANALYSIS: Commission Order PSC-04-0369-AS-EI allowed for an annual increase to the storm reserve of $121,625 with additional increases if the utility did not spend the $22,641 projected for economic development. In 2006, the amount applied to the storm reserve for economic development was $16,758. In its projected expenses for account 924 for 2008, the utility proposed an increase to the annual accrual to the reserve to $203,880 plus the $16,758 of unused economic development costs calculated in 2006. The $16,745 should be removed as it should not be recurring in the future.

The utility has included $5,000 of economic development costs in its 2006 test year which were trended up to $5,351. It has also included an additional $10,350 for economic development in its estimate of over and above expenses on C-7, Operations and Maintenance Expenses, for 2008 for its Fernandina division.

EFFECT ON THE GENERAL LEDGER: There is no effect on the general ledger since these expenses are forecast.

EFFECT ON THE FILING: The 2008 forecast should be reduced by the $16,758 for economic development costs. The Commission may put a similar recommendation in this rate order for the new economic development forecast of $15,701, but if the order is worded the same, costs will only go to the storm reserve if they are not expensed as planned in the economic development forecast. The new storm allowance accruals should also be reviewed for reasonableness by staff engineers.

AUDIT FINDING NO. 14

SUBJECT: MEDICAL BENEFIT FORECAST

AUDIT ANALYSIS: In the 2008 projected expenses in C-7, Operation and Maintenance Expenses, for account 926.2, Employee Benefits, Medical, the utility included an 11.4% increase in its medical benefits for 2008. The utility has received a revised estimate from Cigna Health Care which indicates a 34.78% increase in 2008 insurance expense. This would increase the projection from \$543,969 to \$650,336 or an increase of \$106,367 computed as follows. The utility has not re-filed this schedule.

2006 Expense	438,333.00
Increase 2007	110.0800%
2007 Projection	482,516.97
New 2008 Increase	134.78%
New 2008 Projection	650,336.37
Projection in Filing	543,969.00
Difference	106,367.37

EFFECT ON THE GENERAL LEDGER: This finding is for informational purposes only.

EFFECT ON THE FILING: This finding is for informational purposes only.

AUDIT FINDING NO. 15

SUBJECT: OVERHEAD IN OVER AND ABOVE FORECAST

AUDIT ANALYSIS: The utility added several salaries in it's "over and above" expense increases on C-7, Operation and Maintenance Expenses, for its 2008 expense projection for new positions and wage increases. The salary computations included a 37-38% overhead calculation. This calculation included vacation, holiday and sick leave which do not increase the base pay. Based on actual 2006 costs, we determined the actual 2006 overhead for pension, taxes and insurance to be 30.65%.

The following is a schedule of the salaries included and the overhead that were provided in supporting documentation for its "over and above" expenses in its 2008 forecast:

	A	B	C	D	E	F	G	H	
	Direct		Corporate Costs Allocated					Note A	
Account	Marianna	Fernandina	Corporate	Divided by 1.37	Benefits	Allocation	Amount Electric Used	Difference Staff/Utility Corporate	Total All
4010.580	56,497.00								
4020.5932		5,949.00							
4020.5942		6,163.00							
4010.5931	38,304.50	38,304.50							
4010.5881	10,454.50	10,454.50							
4010.928	9,995.50	9,995.50							
4010.920			51,531.00	37,613.87	13,917.13	40.00%	5,566.85	(955.39)	
4010.903			56,992.00	41,600.00	15,392.00	35.00%	5,387.20	(924.56)	
4010.920			82,200.00	60,000.00	22,200.00	40.00%	8,880.00	(1,524.00)	
4010.92			95,066.00	69,391.24	25,674.76	40.00%	10,269.90	(1,762.54)	
4010.9251			33,280.00	24,291.97	8,988.03	32.00%	2,876.17	(493.61)	
Salary Survey	21,691.00	21,691.00							
	136,942.50	92,557.50							
Divided by 1.38	99,233.70	67,070.65							
Benefits Utility	37,708.80	25,486.85							
Benefits Staff	30,415.13	20,557.15	Note B						
Difference	7,293.68	4,929.69						5,660.10	17,883.47

Note A: Column (D (payroll without overhead) x.3065 overhead rate staff x Column F (allocation rate corporate))-Column G (used by company)
Note B: Amount above without benefits x .3065 overhead rate staff

EFFECT ON THE GENERAL LEDGER: There is no effect on the general ledger.

EFFECT ON THE FILING: Expenses for 2008 should be reduced by $17,883.47.

AUDIT FINDING NO. 16

SUBJECT: ALLOCATION OF CLEARING

AUDIT ANALYSIS: The utility puts several expenses in its 1840 clearing accounts. These accounts are not allocated to all divisions but instead are charged to the divisions through the payroll entry. The allocation through payroll does not allocate as much expense to non-regulated operations as the regular allocation process. The accounts are all payroll related costs. Based on the payroll allocation used by the utility in 2006, 26% of payroll relates to propane and merchandising and jobbing. The following schedule shows how much of the costs were removed using the payroll entry instead of allocating the expenses using payroll and how it effects the electric allocation. The amounts shown below as removed were credits to the clearing accounts from the payroll journal entries. The total costs are the costs charged to the clearing accounts. The amounts charged to the electric division are the net of the first two amounts times the rates used by the utility. Staff used the total costs times the payroll allocation rate to determine what it would have charged and compared it to the amount that did get charged to electric. We then trended up the difference using the trend factors for the individual accounts.

Account	Type	Removed Non-Reg and Cons.	Total Costs	Charged Electric Co. Methodology	Charged Electric 25% Payroll Alloc.	Difference	Trend Factors	2008 Difference
925.2	Gen. Liab.	87,770.00	574,386.04	189,736.02	143,596.51	46,139.51	106.8/106.8	52,627.83
926.1	Pension	181,835.00	1,396,952.00	425,290.95	349,238.00	76,052.95	105.8/110	88,510.42
926.2	Medical	232,370.00	1,625,883.63	487,688.07	406,470.91	81,217.16	110.08/134.78	120,339.47
926.4	401K	2,490.00	17,259.28	5,169.25	4,314.82	854.43	106.8/106.8	974.58
		504,465.00	3,614,480.95	1,107,884.29	903,620.24	204,264.05		262,452.31

Expenses allocated to electric would decrease by $204,264.05 if the utility allocated the total account based on the payroll allocated.

EFFECT ON THE GENERAL LEDGER: If this methodology is accepted, the utility method would change going forward but 2006 would not be affected.

EFFECT ON THE FILING: If this methodology is accepted, expenses for 2008 should be reduced by $262,452.31.

AUDIT FINDING NO. 17

SUBJECT: COMPARISON OF 2007 TO FORECAST

AUDIT ANALYSIS: The 2007 expenses as of September 30, 2007 were annualized and compared to the forecast on schedule C-7 (2007), Operation and Maintenance Expenses, of the filing. The actual annualized costs were $488,245.33 less than the filing expenses for 2007. Many of the differences related to accounts that had "over and above" expenses. The "over and above" expenses total $574,896 in 2007. The only over and above amounts that appear to have been substantially incurred were the general liability account 925.2 and the maintenance of underground lines account 594.2. A schedule showing the computation follows.

EFFECT ON THE GENERAL LEDGER: This finding is for informational purposes only and does not affect booked expenses in 2006.

EFFECT ON THE FILING: This finding is for informational purposes only.

ACCOUNT	114-Marianna AMOUNT Sep-07	115-Fernandina AMOUNT Sep-07	TOTAL Sep-07	ANNUALIZED	PER C-7 2007	DIFFERENCE	OVER AND ABOVE
4010 562		4,756.00	4,756.00	6,341.33	42,501.00	(36,159.67)	25,000.00
4010 566		119.00	119.00	158.67	12,116.00	(11,957.33)	12,000.00
4010 580	98,455.00	119,760.00	218,215.00	290,953.33	380,422.00	(89,468.67)	56,408.00
4010 582	8,818.00	36,581.00	45,399.00	60,532.00	94,672.00	(34,140.00)	45,000.00
4010 5831	39,118.00	24,084.00	63,202.00	84,269.33	54,913.00	29,356.33	
4010 5832	27,502.00	9,613.00	37,115.00	49,486.67	65,562.00	(16,075.33)	
4010 5841	446.00	8,853.00	9,299.00	12,398.67	3,723.00	8,675.67	
4010 5842		22,821.00	22,821.00	30,428.00	27,504.00	2,924.00	
4010 585	8,989.00	1,556.00	10,545.00	14,060.00	12,770.00	1,290.00	
4010 586	121,401.00	73,266.00	194,667.00	259,556.00	273,056.00	(13,500.00)	
4010 5871	33,686.00	6,523.00	40,209.00	53,612.00	55,585.00	(1,973.00)	
4010 5872	6,761.00	24,352.00	31,113.00	41,484.00	44,010.00	(2,526.00)	
4010 5881	48,757.00	36,792.00	85,549.00	114,065.33	105,926.00	8,139.33	
4010 5882	23,191.00	67,550.00	90,741.00	120,988.00	155,533.00	(34,545.00)	50,800.00
4010 5883	1,937.00	3,015.00	4,952.00	6,602.67	11,129.00	(4,526.33)	
4010 589	784.00		784.00	1,045.33	1,053.00	(7.67)	
4010 901	23,942.00	36,282.00	60,224.00	80,298.67	73,765.00	6,533.67	1,428.00
4010 9011	14,189.00	16,197.00	30,386.00	40,514.67	49,056.00	(8,541.33)	
4010 902	109,682.00	101,161.00	210,843.00	281,124.00	295,709.00	(14,585.00)	
4010 903	194,643.00	221,881.00	416,524.00	555,365.33	524,917.00	30,448.33	
4010 9031	89,511.00	102,227.00	191,738.00	255,650.67	275,807.00	(20,156.33)	1,349.00
4010 904	17,038.00	15,277.00	32,315.00	43,086.67	87,590.00	(44,503.33)	175.00
4010 905	31,979.00	17,418.00	49,397.00	65,862.67	80,765.00	(14,902.33)	
4010 9051	5,644.00	6,445.00	12,089.00	16,118.67	16,804.00	(685.33)	
4010 9131	300.00		300.00	400.00		400.00	
4010 9132	3,620.00		3,620.00	4,826.67	1,589.00	3,237.67	
4010 9133	2,657.00	2,552.00	5,209.00	6,945.33	8,504.00	(1,558.67)	
4010 9134	50,307.00	50,169.00	100,476.00	133,968.00	154,148.00	(20,180.00)	28,800.00
4010 916		571.00	571.00	761.33	13,699.00	(12,937.67)	
4010 920	321,766.00	435,331.00	757,097.00	1,009,462.67	1,071,369.00	(61,906.33)	58,302.00
4010 9211	4,248.00	4,280.00	8,528.00	11,370.67	10,867.00	503.67	
4010 9212	2,382.00	2,404.00	4,786.00	6,381.33	7,111.00	(729.67)	
4010 9213	3,377.00	3,388.00	6,765.00	9,020.00	8,113.00	907.00	
4010 9214	27,347.00	24,363.00	51,710.00	68,946.67	34,425.00	34,521.67	
4010 9215	40,259.00	40,579.00	80,838.00	107,784.00	93,308.00	14,476.00	
4010 9216	1,088.00	2,690.00	3,778.00	5,037.33	6,913.00	(1,875.67)	5,200.00
4010 8231	4,215.00	7,049.00	11,264.00	15,018.67	18,306.00	(3,287.33)	
4010 9232	8,323.00	8,839.00	17,162.00	22,882.67	40,283.00	(17,400.33)	
4010 9233	74,022.00	78,440.00	152,462.00	203,282.67	226,660.00	(23,377.33)	82,150.00
4010 924	87,462.00	33,430.00	120,892.00	161,189.33	181,238.00	(20,048.67)	
4010 9251	43,976.00	51,421.00	95,397.00	127,196.00	114,957.00	12,239.00	632.00
4010 9252	230,710.00	227,879.00	458,589.00	611,452.00	475,595.00	135,857.00	133,000.00
4010 9261	146,372.00	151,861.00	298,233.00	397,644.00	365,497.00	32,147.00	
4010 9262	164,069.00	171,618.00	335,687.00	447,582.67	488,303.00 •	(40,720.33)	
4010 9263	19,503.00	20,997.00	40,500.00	54,000.00	54,000.00	0.00	
4010 9264	6,463.00	6,693.00	13,156.00	17,541.33	6,157.00	11,384.33	

ACCOUNT	114-Marianna AMOUNT Sep-07	115-Fernandina AMOUNT Sep-07	TOTAL Sep-07	ANNUALIZED	PER C-7 2007	DIFFERENCE	OVER AND ABOVE
4010 928	56,323.00	60,226.00	116,549.00	155,398.67	133,967.00	21,431.67	
4010 9302	29,746.00	28,334.00	58,080.00	77,440.00	79,227.00	(1,787.00)	
4010 93022	3,189.00	2,246.00	5,435.00	7,246.67	4,539.00	2,707.67	
4010 93023	5,000.00		5,000.00	6,666.67	15,170.00	(8,503.33)	10,000.00
4010 931	4,299.00	4,333.00	8,632.00	11,509.33	8,490.00	3,019.33	
4020 570		61,912.00	61,912.00	82,549.33	102,430.00	(19,880.67)	
4020 571		24,152.00	24,152.00	32,202.67	80,603.00	(48,400.33)	
4020 573		0.00	0.00	0.00	461.00	(461.00)	
4020 590	26,242.00	69,337.00	95,579.00	127,438.67	146,674.00	(19,235.33)	2,856.00
4020 591		1,962.00	1,962.00	2,616.00	10,411.00	(7,795.00)	
4020 592	6,803.00	22,070.00	28,873.00	38,497.33	75,455.00	(36,957.67)	
4020 5931	2,153.00	12,206.00	14,359.00	19,145.33	46,044.00	(26,898.67)	
4020 5932	449,993.00	224,682.00	674,675.00	899,566.67	1,032,586.00	(133,019.33)	53,248.00
4020 5933	73,662.00	19,777.00	93,439.00	124,585.33	137,755.00	(13,169.67)	
4020 5941	10,051.00	6,492.00	16,543.00	22,057.33	7,968.00	14,089.33	
4020 5942	248.00	166,223.00	166,471.00	221,961.33	143,039.00	78,922.33	5,748.00
4020 5951	33,720.00	8,043.00	41,763.00	55,684.00	68,893.00	(13,209.00)	
4020 5952	7,949.00	10,669.00	18,618.00	24,824.00	7,451.00	17,373.00	
4020 5953		37,099.00	37,099.00	49,465.33	58,267.00	(8,801.67)	
4020 596	8,113.00	24,741.00	32,854.00	43,805.33	52,438.00	(8,632.67)	
4020 597	14,305.00	17,186.00	31,491.00	41,988.00	37,647.00	4,341.00	
4020 598	34,525.00	22,538.00	57,063.00	76,084.00	73,927.00	2,157.00	
4020 935	31,710.00	44,513.00	76,223.00	101,630.67	167,932.00	(66,301.33)	2,800.00
	2,946,970.00	3,149,824.00	6,096,794.00	8,129,058.67	8,617,304.00	(488,245.33)	574,896.00

EXHIBITS

FLORIDA PUBLIC SERVICE COMMISSION

COMPANY: FLORIDA PUBLIC UTILITIES
Consolidated Electric Division
DOCKET NO. 070304-EI

EXPLANATION: Provide a schedule of the 13-month average adjusted rate base for the test year, the prior year and the most recent historical year. Provide the details of all adjustments on Schedule B-2.

Type of Data Shown:
Historic Year Ended 12/31/2006
Witness: Jim Mesite, Cheryl Martin

Line No.		(1) Plant in Service	(2)* Accumulated Provision for Depreciation and Amortization	(3) Net Plant in Service (1 - 2)	(4) CWIP - No AFUDC	(5) Plant Held For Future Use	(6) Nuclear Fuel - No AFUDC (Net)	(7) Net Utility Plant	(8) Working Capital Allowance	(9) Other Rate Base Items	(10) Total Rate Base
1	System Per Books (B-3)	72,376,983	(32,199,482)	40,177,500	1,461,603	-	-	41,639,104	(1,682,506)	-	39,956,598
2	Jurisdictional Factors	100%	100%	100%	100%	100%	100%		100%	100%	
3	Jurisdictional Per Books	72,376,983	(32,199,482)	40,177,500	1,461,603	-	-	41,639,104	(1,682,506)	-	39,956,598
4	Adjustments:										
5	Non-regulated Propane Operations	(67,783)	33,370	(34,413)	(7,343)	-	-	(41,756)		-	(41,756)
6	Eliminate Interest Bearing Cash Per 2003 Rate Case Proceeding								(24,312)		(24,312)
7	Eliminate 1/2 Deferred Rate Case Expense Per 2003 Rate Case Proceeding								(116,540)		(116,540)
8	Eliminate Fuel Under-Recovery Per 2003 Rate Case Proceeding								(1,716,749)		(1,716,749)
9											
10											
11											
12											
13	Total Adjustments	$ (67,783)	$ 33,370	$ (34,413)	$ (7,343)	$ -	$ -	$ (41,756)	$ (1,857,601)	$ -	$ (1,899,357)
14											
15	Adjusted Jurisdictional	$ 72,309,200	$ (32,166,112)	$ 40,143,087	$ 1,454,260	$ -	$ -	$ 41,597,348	$ (3,540,107)	$ -	$ 38,057,241
16											
17	* Includes Account 2520 - Customer Advances for Construction										

Supporting Schedules: B-2 (2006), B-3 (2006), B-7 (2006), B-9 (2006)

Recap Schedules: B-2 (2006)

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ADJUSTED JURISDICTIONAL NET OPERATING INCOME

FLORIDA PUBLIC SERVICE COMMISSION

COMPANY:FLORIDA PUBLIC UTILITIES
Consolidated Electric Division
DOCKET NO.: 070304-EI

EXPLANATION: Provide the calculation of jurisdictional net operating income for the test year, the prior year and the most recent historical year.

Type of Data Shown:
Historic Year Ended 12/31/2006
Witness: Mehrdad Khojasteh, Cheryl Martin

Line No.		(1) Total Company Per Books	(2) Non-Electric Utility	(3) Total Electric (1)-(2)	(4) Jurisdictional Factor	(5) Jurisdictional Amount (3)x(4)	(6) Jurisdictional Adjustments (Schedule C-2)	(7) Adjusted Jurisdictional Amount (5)+(6)
1	Operating Revenues:							
2	Sales of Electricity	47,452,526		47,452,526	100%	47,452,526	(30,359,021)	17,093,505
3	Other Operating Revenues	1,074,705		1,074,705	100%	1,074,705	(759,903)	314,802
4	Total Operating Revenues	48,527,231		48,527,231	100%	48,527,231	(31,118,924)	17,408,307
5								
6	Operating Expenses:							
7	Operation & Maintenance:							
8	Fuel			-	100%	-	-	-
9	Purchased Power	30,606,436		30,606,436	100%	30,606,436	(30,606,436)	-
10	Other	8,163,711		8,163,711	100%	8,163,711	(456,411)	7,707,300
11	Depreciation & Amortization	2,722,498		2,722,498	100%	2,722,498	(11,398)	2,711,100
12	Decommissioning Expense			-	100%	-	-	-
13	Taxes Other Than Income Taxes	3,982,172		3,982,172	100%	3,982,172	(22,079)	3,960,093
14	Income Taxes	772,895		772,895	100%	772,895	8,498	781,393
15	Deferred Income Taxes-Net	(195,788)		(195,788)	100%	(195,788)	-	(195,788)
16	Investment Tax Credit-Net	(32,322)		(32,322)	100%	(32,322)	-	(32,322)
17	(Gain)/Loss on Disposal of Plant			-	100%	-	-	-
18	Total Operating Expenses	46,019,602		46,019,602	100%	46,019,602	(31,087,826)	14,931,776
19								
20	Net Operating Income	2,507,629		2,507,629	100%	2,507,629	(31,098)	2,476,531

Supporting Schedules: C-2, C-4, C-5, C-7

Recap Schedules:

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FLORIDA PUBLIC SERVICE COMMISSION

COMPANY: FLORIDA PUBLIC UTILITIES
Consolidated Electric Division
DOCKET NO.: 070304-EI

EXPLANATION: Provide the company's 13-month average cost of capital for the test year, the prior year, and historical base year.

Type of Data Shown:
Historic Year Ended 12/31/06
Witness: Doreen Cox, Robert Camfield

Line No.	Class of Capital	(A) Company Total Per Books	(B) Specific Adjustments	(C) Pro Rata Adjustments	(D) System Adjusted	(E) Jurisdictional Factor	(F) Jurisdictional Capital Structure	(G) Ratio	(H) Cost Rate	(I) Weighted Cost Rate	(J) Interest Expense
	Regulatory Capital Structure, 2006										
1.	Long Term Debt	50,443,237			50,443,237	31.33%	15,801,612	0.4152	8.03%	3.33%	1,268,418
2.	Short Term Debt	3,309,077			3,309,077	31.33%	1,036,586	0.0272	7.29%	0.20%	75,536
3.	Preferred Stock	600,000			600,000	31.33%	187,953	0.0049	4.75%	0.02%	
4.	Common Equity	44,943,721			44,943,721	31.33%	14,078,859	0.3699	11.50%	4.25%	
5.	Customer Deposits	2,136,661			2,136,661		2,136,661	0.0561	6.07%	0.34%	129,626
6.	Deferred Income Taxes	4,674,449			4,674,449		4,674,449	0.1228	0.00%	0.00%	
7.	Tax Credits-Zero Cost	0			0		0	0.0000	0.00%	0.00%	
8.	Tax Credits-Weighted Cost	141,120			141,120		141,120	0.0037	9.55%	0.04%	
9.	TOTAL	106,248,266			106,248,266		38,057,241	1.0000		8.18%	1,473,580

	Class of Capital	Company Total Per Books	Ratio	Cost Rate	Weighted Cost Rate
	Conventional Capital Structure, 2006				
10.	Long Term Debt	50,443,237	0.5080	8.03%	4.08%
11.	Short Term Debt	3,309,077	0.0333	7.29%	0.24%
12.	Preferred Stock	600,000	0.0060	4.75%	0.03%
13.	Common Equity	44,943,721	0.4526	11.50%	5.21%
14.	TOTAL	99,296,036	1.0000		9.55%

Rate Base	$38,057,241
Direct Components	$6,952,231
	$31,105,010
Jurisdictional Factor	31.33%

Common Equity excludes Flo-Gas

Supporting Schedules: B-1 (2006), B-3 (2006), D-3, D-4a, D-5, D-6

Recap Schedules:

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