

ORIGINAL

M E M O R A N D U M

July 1, 1998

TO: DIVISION OF RECORDS AND REPORTING
FROM: DIVISION OF AUDITING AND FINANCIAL ANALYSIS (VANDIVER) *OV*
RE: DOCKET NO. 980441-WS -- ORCHID SPRINGS DEVELOPMENT CORPORATION
AUDIT REPORT - STAFF-ASSISTED RATE CASE
AUDIT CONTROL NO. 98-119-3-1

The above-referenced audit report is forwarded. Audit exceptions document deviations from the Uniform System of Accounts, Commission rule or order, Staff Accounting Bulletin and generally accepted accounting principles. Audit disclosures show information that may influence the decision process.

The audit was prepared using a micro computer and has been recorded on one diskette. The diskette may be reviewed using IBM compatible equipment and LOTUS 1-2-3 software. There are no confidential working papers associated with this audit.

Please forward a complete copy of this audit report to:

Orchid Springs Development Corporation
Carol C. Rhinehart
710 Overlook Drive
Winter Haven, FL 33884-1669

DNV/sp

Attachment

cc: Chairman Johnson
Commissioner Clark
Commissioner Deason
Commissioner Garcia
Commissioner Jacobs
Mary Andrews Bane, Deputy Executive Director/Technical
Legal Services
Division of Auditing and Financial Analysis (Devlin/Causeaux/
File Folder)
Division of Water and Wastewater (Okome)
Orlando District Office (Forbes)

Research and Regulatory Review (Harvey)
Office of Public Counsel

DOCUMENT NUMBER-DATE

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FPSP-RECORDS/REPORTING



ORIGINAL

FLORIDA PUBLIC SERVICE COMMISSION

*DIVISION OF AUDITING AND FINANCIAL ANALYSIS
BUREAU OF AUDITING*

ORLANDO DISTRICT OFFICE

ORCHID SPRINGS DEVELOPMENT CORPORATION

STAFF-ASSISTED RATE CASE

HISTORICAL YEAR ENDED MARCH 31, 1998

DOCKET NO. 980441-WS

AUDIT CONTROL NO. 98-119-3-1

A handwritten signature in cursive script, appearing to read "Simon Ojada", written over a horizontal line.

Simon Ojada, Audit Manager

A handwritten signature in cursive script, appearing to read "Ian J. Forbes", written over a horizontal line.

Ian J. Forbes, Audit Supervisor

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**DIVISION OF AUDITING AND FINANCIAL ANALYSIS
AUDITOR'S REPORT**

JUNE 18, 1998

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

We have applied the procedures described later in this report to prepare the accompanying schedules of Rate Base, Net Operating Income, and Capital Structure for the historical 12-month period ended March 31, 1998, for Orchid Springs Development Corporation. These schedules were prepared by the auditor as part of the utility's petition for a Staff-Assisted Rate Case in Docket No. 980441-WS. There is no confidential information associated with this audit, and there are no audit staff minority opinions.

This is an internal accounting report prepared after performing a limited scope audit. Accordingly, this document must not be relied upon for any purpose except to assist the Commission staff in the performance of their duties. Substantial additional work would have to be performed to satisfy generally accepted auditing standards and produce audited financial statements for public use.

In our opinion, the schedules referred to above, except Rate Base, present fairly, in all material respects, the utility's books and records not maintained in conformity with accounting practices prescribed by the Florida Public Service Commission. The expressed opinion extends only to the scope of work described in this report. The attached findings discuss all differences and other matters which were noted during our examination.

SUMMARY OF SIGNIFICANT FINDINGS:

Orchid Springs Development Corporation could not provide documentation to support plant-in-service.

The utility collects a \$50.00 deposit from its residential rental customers and makes a refund only when the rental customer vacates the apartment. Homeowners are not charged a deposit. The utility does not pay interest on customer deposits.

The utility failed to record its revenues and expense on the accrual basis.

Orchid Springs collects an unauthorized 2.5 percent utility tax from its customers.

SUMMARY OF SIGNIFICANT PROCEDURES

Our audit was performed by examining, on a test basis, certain transactions and account balances which we believe are sufficient to base our opinion. Our examination did not entail a complete review of all financial transactions of the company. Our more important audit procedures are summarized below. The following definitions apply when used in this report:

Compiled - The exhibit amounts were reconciled with the general ledger, and accounts were scanned for error or inconsistency.

Reviewed - The exhibit amounts were reconciled with the general ledger. The general ledger account balances were traced to subsidiary ledgers, and selective analytical review procedures were applied.

Verify - The item was tested for accuracy, and substantiating documentation was examined.

RATE BASE: Polk County established a rate base in 1993 without a breakdown of plant accounts. PSC engineer will do an original cost study including a determination of accumulated depreciation. Scheduled documented additions from April 1993 to March 1998. Verified date utility land was dedicated to public service. Reviewed books and records for evidence of contributions-in-aid-of-construction.

NET OPERATING INCOME: Compiled utility revenue and operation and maintenance accounts for the fiscal year ended March 31, 1998. Chose a judgmental sample of customer bills and recalculated using Polk County-approved rates. Reviewed operation and maintenance expenses and examined invoices and supporting documentation.

CAPITAL STRUCTURE: Compiled components of the parent capital structures for the fiscal year ended March 31, 1998.

EXCEPTIONS

Exception No. 1

Subject: NARUC Chart of Accounts

Statement of Fact: Florida Administrative Code No. 25-30.115 states that “water and wastewater utilities shall, effective January 1, 1998, maintain their accounts and records in conformity with the 1996 NARUC Uniform Systems of Accounts”

The Uniform System of Accounts, Accounting Instruction 2, requires the books of accounts of all water and wastewater utilities shall be kept by the double entry method, on an accrual basis. It further states that “All books of accounts, together with records and memoranda supporting the entries therein, shall be kept in such a manner as to support fully the facts pertaining to such entries.”

The utility does not utilize the account numbering system delineated by NARUC and maintains its records on a cash basis. The utility is commingling its accounting with the developer’s operations.

Records supporting original cost for land and plant-in-service were not available.

Recommendation: The utility should be required to maintain its records in conformity with the NARUC Uniform Systems of Account as prescribed by Rule 25-30.115, F.A.C., regarding record keeping of water and wastewater utilities.

Exception No. 2

Subject: Plant-in-Service

Statement of Fact: Orchid Springs Development Corporation's water and wastewater service plants were built around 1975 and 1976. The original costs of the systems are unknown. The utility general ledger has \$139,377 for water plant and \$216,888 for wastewater as of March 31, 1998.

Polk County established a rate base of \$79,132 for water and \$141,325 for wastewater effective October 1993. Utility did not have the various accounts broken down by plant account for Polk County.

For the period April 1992 to March 1998, the utility recorded plant additions of \$19,905 for water and \$1,500 for wastewater.

Recommendation: The utility did not maintain proper records of installation and installed costs of plant-in-service. The estimated costs of plant for water and wastewater of \$139,377 and \$216,888 should be removed from the company's books. An original cost study is to be established by the Division of Water and Wastewater engineer to determine the proper value of plant-in-service.

Exception No. 3

Subject: Customer Deposits

Statement of Fact: The utility collects a \$50.00 deposit from its residential rental customers and makes a refund only when the rental customer vacates the apartment. The utility does not pay interest on customer deposits.

Homeowners are not charged a deposit. The utility tariff does not provide for customer deposits.

Florida Administrative Code 25-30.311 (5) states,

After a customer has established a satisfactory payment record and continuous service for a period of 23 months, the utility shall refund the residential customer's deposits, provided the customer has not, in the preceding 12 months, (a) made more than one late payment of a bill, (b) made payment with a check refused by bank, (c) been disconnected for nonpayment at any time,

Florida Administrative Code No. 25-30.311(4) states,

(a) Each public utility which requires deposits to be made by its customers shall pay a minimum interest on such deposits of 6 percent per annum (b) The deposit interest shall be simple interest in all cases and settlement shall be made annually, either in cash or by credit on the current bill. This does not prohibit any public utility paying a higher rate of interest than required by this rule.

Recommendation: The company should be required to treat all customers equally. The utility should be required to refund customer deposits with appropriate accrued interest to customers that have established good credit for 23 months. Also, the utility should be required to pay 6 percent annual interest on customer deposits.

Exception No. 4

Subject: Unauthorized Utility Tax

Statement of Fact: Orchid Springs Development Corporation charges its customers a 2½ percent utility tax. The utility tax was authorized by Polk County when the county regulated water and wastewater operations.

Recommendation: Orchid Springs Development Corp. should be required to stop collecting the utility tax since the utility is no longer regulated by Polk County.

Exception No. 5

Subject: Expense

Statement of Fact: Orchid Springs Development Corporation charged all office telephone and electricity bills to the utility account. The office is used by the owner for his other nonutility businesses.

The utility spent \$14, 862 for legal services for the 12-month period ended March 31, 1998, due to drainage problem caused by the Baytree Golf Course and proceedings with the Garden Grove Water Company.

The utility allocates all expenses between water and wastewater on a 50/50 basis except for some expenses that are identifiable to only water or wastewater.

The utility also misclassified some of its expenses for the test period as shown below.

Recommendation: Staff recommends that the telephone and electricity bills be split on a 50/50 basis since the office is used for other nonutility businesses. The owner agreed to allocate the telephone and the electricity bills on a 50/50 basis in the future.

The following adjustments were made by staff to correct all misclassifications made to water and wastewater operating expense accounts.

WATER - Operating Expense

Out-of-period expense (utility billing software)	(3,042)
Telephone expense (50% allocation)	(548)
Office electricity expense (50% allocation)	(272)
Amount traced to purchased power (misclassified)	1,539
Unrecorded gas bill	37
No supporting documentation (no invoice)	(592)
Nonutility expense	(1,493)
Utility tax collected	<u>1,298</u>
Total	<u>(3,073)</u>

Exception No. 5, contd.

WASTEWATER - Operating Expense

Out-of-period expense (utility billing software)	(3,042)
Telephone expense (50% allocation)	(548)
Office electricity expense (50% allocation)	(208)
Amount not traced to purchased power (misclass)	(1,120)
No supporting documentation (no invoice)	(370)
Nonutility expense	(2,025)
Utility tax collected	<u>1,298</u>
Total	<u>(6,015)</u>

DISCLOSURES

Disclosure No. 1

Subject: Land

Statement of Fact: Orchid Spring Development Corporation provided a 99-year lease for the utility land at a rate of \$15,000 per year.

Recommendation: Staff defers to the analyst as to the reasonableness of the cost.

Disclosure No. 2

Subject: Proposed Capital Improvements and 1998 Major Expenses

Statement of Fact: Orchid Springs Development Corporation submitted an estimated cost of water and wastewater plant capital improvements of \$29,121.06 and \$80,829.16, respectively.

In April 1998 the utility spent \$4,227.50 to survey the boundary of the wastewater treatment plant and two well sites. Also, in May 1998 the utility spent \$11,244.00 to fix the drainage around the large retention pond. These are the only costs incurred for capital improvement in 1998 as of the end of field work, June 1998.

Recommendation: Staff defers to the Division of Water and Wastewater as to whether the capital improvements are prudent expenditures.

The 1998 expenditure is an information item for the analyst.

Disclosure No. 3

Subject: Requested Increase in Management and Maintenance Contract Fees

Statement of Fact: Cassidy Organization, Inc. (the parent company) currently charges the utility a monthly management fee of \$1,183.00 for each system, water and wastewater, for a total of \$2,366.00 a month. The Cassidy Organization, Inc. is requesting a combined management fee of \$4,784.00, an increase of \$2,418.00 a month.

The maintenance contractor currently charges \$1,161.60 a month and has requested an increase of \$485.40 a month.

Recommendation: The proposed increase in management and contractual fees are information items for the analyst.

Disclosure No. 4

Subject: Unbilled Revenue

Statement of Fact: The owners of the utility own a swimming pool and a clubhouse that receive water and wastewater services from the utility. These facilities were not metered and not billed for the services received for the test period.

Recommendation: The utility has now installed water meters on the swimming pool and the clubhouse. Staff recommends that the utility starts billing for the swimming pool and the clubhouse.

According to the maintenance contractor, the swimming pool uses about one thousand gallons of water a day.

SCHEDULES FOR STAFF ASSISTED RATE BASE
 ORCHID SPRINGS DEVELOPMENT CORPORATION
 DOCKET NO. 980441-WS
 RATE BASE - WATER
 TEST YEAR ENDED 03/31/98

EXHIBIT I

(a) DESCRIPTION	(b) PER POLK COUNTY 10/31/93	(c) PER PER BOOKS 03/31/98	(d) DIFF.	(e) ADDITION PER AUDIT 03/31/98
UTILITY PLANT IN SERVICE	79,132	140,878	(61,746)	19,905
LAND	0	0		0
PLANT HELD FOR FUTURE USE	0	0		0
CIAC	0	0		0
AMORTIZATION OF CIAC	0	0		0
ACCUMULATED DEPRECIATION	0	0		0
WORKING CAPITAL	0	9,175		8,971
TOTAL	79,132	150,053		28,876

1. Unable to determine plant in service. Water and wastewater engineer to do original cost study to determine cost of plant in service including the accumulated depreciation.
2. Working Capital Formula: 1/8 Operating and Maintenance Expense.
3. All amounts rounded to the nearest whole dollar.

SCHEDULES FOR STAFF ASSISTED RATE BASE
ORCHID SPRINGS DEVELOPMENT CORPORATION
DOCKET NO. 980441-WS
RATE BASE - WASTEWATER
TEST YEAR ENDED 03/31/98

EXHIBIT II

(a) DESCRIPTION	(b) PER POLK COUNTY 10/31/93	(c) PER PER BOOKS 10/31/98	(d) DIFF.	(e) ADDITION PER AUDIT 03/31/98
<u>UTILITY PLANT IN SERVICE</u>	141,325	215,388	(74,063)	1,500
<u>LAND</u>	0	0		0
<u>PLANT HELD FOR FUTURE USE</u>	0	0		0
<u>CIAC</u>	0	0		0
<u>AMORTIZATION OF CIAC</u>	0	0		0
<u>ACCUMULATED DEPRECIATION</u>	0	0		0
<u>WORKING CAPITAL</u>	0	12,838		12,086
<u>TOTAL</u>	<u>141,325</u>	<u>228,226</u>		<u>13,586</u>

1. Unable to determine plant in service. Water and wastewater engineer to do original cost study to determine cost of plant in service including the accumulated depreciation.
2. Working Capital Formula: 1/8 Operating and Maintenance Expense.
3. All amounts rounded to the nearest whole dollar.

SCHEDULES FOR STAFF ASSISTED RATE BASE
 ORCHID SPRINGS DEVELOPMENT CORPORATION
 DOCKET NO. 980441-WS
 NET OPERATING INCOME - WATER
 TEST YEAR ENDED 03/31/98

EXHIBIT IV

DESCRIPTION	(1) BALANCE PER BOOKS 03/31/98	(2) AUDIT DISCLOSURES ADJUST	(3) Refer to	(4) AUDITED BALANCE
OPERATING REVENUES	45,257	0		45,257
OTHER REVENUES - UTILITY TAX		1,131		1,131
<hr/>				
OPERATING EXPENSES				
OPERATION AND MAINTENANCE EXPENSE	73,404	3,073	E-5	70,331
DEPRECIATION EXPENSE	0	0		0
AMORTIZATION EXPENSE	0	0		0
TAXES OTHER THAN INCOME	0	0		0
TOTAL OPERATING EXPENSES	73,404	3,073		70,331
<hr/>				
NET OPERATING INCOME/LOSS	(28,147)	(3,073)		(23,943)

Note: Unable to determine depreciation expense
 Engineer to do original cost study
 to determine original cost of plant in service.

SCHEDULES FOR STAFF ASSISTED RATE BASE
 ORCHID SPRINGS DEVELOPMENT CORPORATION
 DOCKET NO. 980441-WS
 NET OPERATING INCOME - WASTEWATER
 TEST YEAR ENDED 03/31/98

EXHIBIT III

DESCRIPTION	(1) BALANCE PER BOOKS 03/31/98	(2) AUDIT DISCLOSURES ADJUST	(3) Refer to	(4) AUDITED BALANCE
OPERATING REVENUES	92,849	0		92,849
OTHER REVENUES - UTILITY TAX		2,321		2,321
<hr/>				
OPERATING EXPENSES				
OPERATION AND MAINTENANCE EXPENSE	102,705	6,015	E - 5	96,690
DEPRECIATION EXPENSE	0	0		0
AMORTIZATION EXPENSE	0	0		0
TAXES OTHER THAN INCOME	0	0		0
TOTAL OPERATING EXPENSES	102,705	6,015		96,690
<hr/>				
NET OPERATING INCOME/LOSS	(9,856)	(6,015)		(1,520)

Note: Unable to determine depreciation expense
 Engineer to do original cost study
 to determine original cost of plant in service.

ORCHID SPRINGS DEVELOPMENT CORP.
DOCKET 980441-WS
CAPITAL STRUCTURE
AS OF MARCH 31, 1998

EXHIBIT V

DESCRIPTION	(a) BALANCE PER T/B @03/31/97	(b) BALANCE PER T/B @03/31/98	(c) SIMPLE AVERAGE PER T/B	(d) AUDIT ADJUST- MENTS REF	(e) BALANCE PER AUDIT @03/31/98	(f) SIMPLE AVERAGE PER AUDIT	(g) RATIO	(h) COST RATE	(i) WEIGHTED COST OF CAPITAL
(COMMON EQUITY (A)	243,979	242,520	243,250	0	242,520	243,250	82.17%	14.50%	11.91%
COMMON STOCK	5,100	5,100	5,100		5,100	5,100			
RETAINED EARN.	210,942	209,483	210,213		209,483	210,213			
PD IN CAPITAL	27,937	27,937	27,937	0	27,937	27,937			
L/T DEBT-	7,824	6,503	7,164		6,503	7,164	2.42%	9.50%	0.23%
L/T DEBT-	23,178	19,794	21,486	0	19,794	21,486	7.26%	9.50%	0.69%
L/T DEBT-	18,028	14,771	16,400		14,771	16,400	5.54%	9.50%	0.53%
L/T DEBT-	6,159	4,935	5,547	0	4,935	5,547	1.87%	10.00%	0.19%
(CUSTOMER DEPOSITS	1,862	2,527	2,195		2,527	2,195	0.74%	6.00%	0.04%
OTHER					0	0	0.00%	0.00%	0.00%
TOTAL	301,030	291,050	296,040	0	291,050	296,040	100.00%		13.59%

Required Footnotes:

- (1) Cost of capital is based on utility parent capital structure
- (2) Audit adjustments do not include audit disclosures.
- (3) Equity cost based FPSC Order 23567, issued 7/23/85.

STATE OF FLORIDA

Commissioners:
JULIA L. JOHNSON, CHAIRMAN
J. TERRY DEASON
SUSAN F. CLARK
JOE GARCIA
E. LEON JACOBS, JR.



DIVISION OF RECORDS & REPORTING
BLANCA S. BAYÓ
DIRECTOR
(850) 413-6770

Public Service Commission

July 2, 1998

Carol C. Rhinehart, Secretary/Treasurer
Orchid Springs Development Corporation
710 Overlook Drive
Winter Haven, Florida 33884-1669

Re: Docket No. 980441 - WS - Orchid Springs Development Corporation
Audit Report - Staff-assisted Rate Case - Historical Year Ended March 31, 1998
Audit Control # 98-119-3-1

Dear Ms. Rhinehart:

The enclosed audit report is forwarded for your review. Any company response filed with this office within ten (10) work days of the above case will be forwarded for consideration by the staff analyst in the preparation of a recommendation for this case.

Thank you for your cooperation.

Sincerely,

A handwritten signature in cursive script that reads "Kay Flynn".

Kay Flynn

KF/ABF

Enclosure

cc: Public Counsel
Division of Audit and Financial Analysis
Martin Friedman