

State of Florida



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Public Service Commission

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-M-E-M-O-R-A-N-D-U-M-

DATE: April 17, 2008

TO: Patricia L. Brady, Regulatory Analyst IV, Division of Economic Regulation

FROM: Denise N. Vandiver, Chief of Auditing, Division of Regulatory Compliance & Consumer Assistance

RE: Docket No: 070739-WS; Company Name: Fairways / Mt. Plymouth, Ltd.;
Audit Purpose: Audit Rate Base; Company Code: WS881;
Audit Control No: 08-025-1-1:

Attached is the final audit report for the utility stated above. I am sending the utility a copy of this memo and the audit report. If the utility desires to file a response to the audit report, it should send the response to the Division of Commission Clerk. There are confidential work papers associated with this audit.

DNV:bj
Attachments

Copy: Division of Regulatory Compliance and Consumer Assistance (Hoppe, District Offices, File Folder)
Division of Commission Clerk (2)
Division of Competitive Markets and Enforcement (Harvey)
General Counsel
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FLORIDA PUBLIC SERVICE COMMISSION

DIVISION OF REGULATORY COMPLIANCE AND CONSUMER ASSISTANCE
BUREAU OF AUDITING

Tallahassee District Office

FAIRWAYS/MT. PLYMOUTH, LTD.

ESTABLISHMENT OF RATE BASE AT TRANSFER

AS OF APRIL 30, 2007

DOCKET NO. 070739-WS
AUDIT CONTROL NO. 08-025-1-1

A handwritten signature in black ink, appearing to read "Charleston J. Winston".

Charleston J. Winston, Audit Manager

A handwritten signature in black ink, appearing to read "Donna Brown".

Donna Brown, Audit Staff

A handwritten signature in black ink, appearing to read "Lynn M. Deamer".

Lynn M. Deamer, Audit Supervisor

DOCUMENT NUMBER-DATE

03089 APR 18 08

FPSC-COMMISSION CLERK

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DIVISION OF REGULATORY COMPLIANCE AND CONSUMER ASSISTANCE
AUDITOR'S REPORT

APRIL 9, 2008

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

We have performed the procedures enumerated later in this report to meet the agreed upon objectives set forth by the Division of Economic Regulation in its audit service request. We have applied these procedures to the attached schedules prepared by the audit staff based on the filing by Aqua Utilities Florida, Inc. for a Certificate Transfer, Docket No. 070739-WS, as of April 30, 2008.

This audit was performed following general standards and fieldwork 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. There is confidential information associated with this audit.

OBJECTIVES AND PROCEDURES:

I. RATE BASE:

A. Objective - Plant in Service: To determine that the property exists and is owned by the utility. To determine that additions are authentic, recorded at original cost, and properly classified in compliance with Commission Rules and the NARUC Uniform System of Accounts. To verify that the proper retirements were made when a replacement item was put in service. To determine that the land is owned by the utility and is included in rate base at original cost.

1. Judgmentally sampled plant additions from 2002 to April 30, 2007. We tested the plant additions for the proper amount, period, classification, support documentation, non-utility, reasonableness, nonrecurring and prudent. We reviewed the tax returns for 2000 through 2007 for utility plant being included in cost of goods sold and the utility plant amount. We found that the plant in service did not match the amount on the 2007 tax return. More detail on this may be found in Audit Finding No. 1.
2. We toured the plant in service to verify the plant in service was in agreement with the books and records. We found that some of the land included in the filing was not being used. More detail on this may be found in Audit Finding No. 2.
3. We traced the cost of the land to the deed and Lake County Property Appraiser's and Tax Collector's records.

B. Objective – Contributions in Aid of Construction (CIAC): To determine that the utility CIAC balances are properly stated in the filing.

1. We obtained and reviewed the schedule of CIAC additions. We performed a test of CIAC additions for the proper amount, period, classification and supporting documentation. We reviewed the tax returns from 2000 through 2007. We reviewed the company's HUD – 1 Uniform Settlement Statements. We found that utility connection fees were not included in the filing as CIAC. More detail on this may be found in Audit Finding No. 3.

C. Objective – Accumulated Depreciation: To verify that accumulated depreciation is calculated using the Commission authorized rates and the calculations are correct.

1. We obtained, reviewed and recalculated the schedule of accumulated depreciation prepared by the company. We verified that the company used Commission authorized rates by comparing the rates used by the company to the authorized rates.

D. Objective – Accumulated Amortization of CIAC. To determine that CIAC accumulated amortization balances are properly stated and that annual accruals are reflective of depreciation rates and proper composite rates.

1. We obtained, reviewed and recalculated the schedule of accumulated amortization of CIAC prepared by the company. We found that the company was not using the proper amortization rates. More detail on this may be found in Audit Finding No. 3.

E. Objective – Acquisition Adjustment. To determine if an acquisition adjustment is applicable per FPSC Rule 25-30.0371.

1. We obtained and reviewed the purchase price for the utilities. We reviewed the filing for the transfer of assets. We established the rate base amounts at the time of transfer. We reviewed FPSC Rule 25-30.0371 and found that an acquisition adjustment is applicable. More detail on this may be found in Audit Finding No. 6.

II. REVENUES AND EXPENSES

A. Objective – Revenues: To determined the company's revenues from inception to December 31, 2007.

1. We obtained and reviewed the company's general ledgers and billing registers. We scheduled revenues from May 2003 through December 31, 2007. We found that the company did not have approved Commission tariffs. More details on this may be found in Audit Finding No. 4.

B. Objective – Expenses: To determine the company's expenses for 2006 and 2007.

1. We obtained and reviewed the company's general ledgers and invoices for 2006 and 2007. We judgmentally selected expenses and reviewed invoices for the proper amount, period, classification, support documentation, non-utility, reasonableness and prudent. Details of the expenses recorded may be found in Audit Finding No. 5.

AUDIT FINDING NO. 1

SUBJECT: TAX RETURN - PLANT IN SERVICE

STATEMENT OF FACT: Fairways/Mt. Plymouth, Ltd., sold its water and wastewater utilities to Aqua Utilities Florida, Inc. on April 30, 2007.

The 2007 tax return and the general ledger of Fairways/Mt. Plymouth, Ltd., showed the Plant in Service for the utilities to be \$756,879.

Aqua Utilities Florida, Inc., in its Certificate of Transfer filing, restated the Plant in Service of the utilities to be \$2,481,465. Aqua Utilities Florida, Inc. stated that mainly the difference of \$1,724,586 (\$2,481,465 - \$756,879) was because Fairways/Mt. Plymouth, Ltd., did not record the proper amount of Plant in Service on its books. Our audit sampled plant additions and found the balance recorded by Aqua Utilities Florida, Inc. to be correct.

EFFECT ON GENERAL LEDGER IF FINDING IS ACCEPTED: No effect on the general ledger. This Audit Finding is provided for informational purposes only.

EFFECT ON FILING IF FINDING IS ACCEPTED: No effect on the Certificate of Transfer filing. This Audit Finding is provided for informational purposes only.

AUDIT FINDING NO. 2

SUBJECT: LAND

STATEMENT OF FACT: Fairways/Mt. Plymouth, Ltd., sold the water and wastewater utilities to Aqua Utilities Florida, Inc. on April 30, 2007.

Fairways/Mt. Plymouth, Ltd., did not record any amount in the book or and on its tax return for the cost of the land. Aqua Utilities Florida, Inc., determined the land values to be \$8,560 as shown below. Aqua Utilities Florida, Inc., derived the amounts from the Lake County Tax Collector's Office.

System	Account Number	Land Use	2006 Assessed Value	Site No.	Plant Use during Audit Staff Plant Tour
(a) Fairways	3219280003-000-00700	Use unknown	\$ 1,560	1314119	Vacant Lot
(b) Fairways	3219280600-00B-00000	Water plant site	\$ 2,000	3806491	Water plant site and Wells
(c) Fairways	3219280600-00D-00000	Use unknown	\$ 1,000	3806492	Vacant Lot
(d) Fairways	3219280600-00E-00000	WW treatment plant	\$ 1,000	3806493	WW treatment plant
(e) Fairways	3219280600-00F-00000	Use unknown	\$ 1,000	3806494	Vacant Wooded Area
(f) Fairways	3219280600-00G-00000	Lift station	\$ 2,000	3806495	Lift station
Total:			<u>\$ 8,560</u>		

Land Allocations Per Company		Water	Wastewater
Land - Well Sites	(a) + (c)	\$ 2,560	
Land - Water Treatment Plant	(b)	\$ 2,000	
Land - Lift Stations	(f)		\$ 2,000
Land - Treatment & Disposal Plant	(d) + (e)		\$ 2,000
Total:		<u>\$ 4,560</u>	<u>\$ 4,000</u>

Land Allocations Per Audit		Water	Wastewater
Land - Water Treatment Plant and Wells	(b)	\$ 2,000	
Land - Lift Stations	(f)		\$ 2,000
Land - Treatment & Disposal Plant	(d)		\$ 1,000
Total:		<u>\$ 2,000</u>	<u>\$ 3,000</u>

Difference:	<u>\$ 2,560</u>	<u>\$ 1,000</u>
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The audit staff toured the plant sites on March 12 and 27, 2008.

EFFECT ON GENERAL LEDGER IF FINDING IS ACCEPTED: Land should be reflected on the general ledger at \$2,000 for the water system and \$3,000 for the wastewater system.

EFFECT ON FILING IF FINDING IS ACCEPTED: Reduce Aqua Utilities Florida, Inc., transfer filing by \$2,560 (\$4,560 - \$2,000) for water and by \$1,000 (\$4,000 - \$3,000) for wastewater.

AUDIT FINDING NO. 3

SUBJECT: CIAC AND ACCUMULATED AMORTIZATION OF CIAC

STATEMENT OF FACT: Fairways/Mt. Plymouth, Ltd., sold its water and wastewater utilities to Aqua Utilities Florida, Inc. on April 30, 2007.

Fairways/Mt. Plymouth, Ltd., did not record any CIAC on its books. Per the company's HUD – 1 Uniform Settlement Statement, it received a Utility Contribution of \$4,000 and a Meter Fee of \$260 per lot. As of April 30, 2007 there were 243 lots sold.

Aqua Utilities Florida, Inc. in its filing for a certificate for the utilities shows CIAC of \$131,220 (243 x \$270 x 2) for water and irrigation meters. The \$270 includes \$260 for the meter fee plus a \$10 connection charge for each water and each irrigation meter. No CIAC was recorded for wastewater.

The audit staff determined that CIAC should be \$1,035,180 as shown below. The \$10 connection charge should have been recorded as revenues and is included in Audit Finding No. 4.

	Contribution Amount (A)	Customers	Total
Water Contribution	\$ 2,000	243	\$ 486,000
Meter Fees	\$ 260	243	\$ 63,180
Wastewater Contribution	\$ 2,000	243	\$ 486,000
Total:	<u>\$ 4,260</u>		<u>\$ 1,035,180</u>

(A) \$4,000 split evenly between water and wastewater

The amount of Accumulated Amortization of CIAC included in the certificate filing was \$13,688.

Per NARUC, Account 272 – Accumulated Amortization of Contributions in Aid of Construction, B.:

“Specifically, balances in account 271 which represent contributions of depreciable plant shall be amortized by charges to this account over a period equal to the estimated service life of the related contributed asset. A group or overall composite rate may be used for contributed balances that cannot be directly related to a plant asset.”

The audit staff determined that Accumulated Amortization of CIAC should be \$53,940 for water (\$8,587 for meters + 45,353 for other water components) and \$45,353 for wastewater.

EFFECT ON GENERAL LEDGER IF FINDING IS ACCEPTED: CIAC should be reflected on the general ledger at \$549,180 for the water system and \$486,000 for the wastewater system. Accumulated Amortization of CIAC should be reflected on the general ledger at \$53,940 for the water system and \$45,353 for the wastewater system.

EFFECT ON FILING IF FINDING IS ACCEPTED: Water CIAC should be increased by \$417,960 ($\$486,000 + \$63,180 - \$131,220$). Water Accumulated Amortization of CIAC should be increased by \$40,252 ($\$53,940 - \$13,688$).

Wastewater CIAC should be increased by \$486,000. Wastewater Accumulated Amortization of CIAC should be increased by \$45,353.

AUDIT FINDING NO. 4

SUBJECT: REVENUES

STATEMENT OF FACT: Fairways/Mt. Plymouth, Ltd., sold its water and wastewater utilities to Aqua Utilities Florida, Inc. on April 30, 2007.

Fairways/Mt. Plymouth, Ltd., did not file for certification with the Florida Public Service Commission during its ownership of the utilities. Fairways/Mt. Plymouth, Ltd. provided the following explanation:

Between 2001 and the date Fairways/Mt. Plymouth became operational in 2002, FWSC (Florida Water Service Corp.) decided to sell its utility systems in Florida and terminated discussions to purchase the water and wastewater systems of Fairways/Mt. Plymouth.

At the time FWSC terminated discussions, it was Fairways/Mt. Plymouth's belief that until it reached 100 customers it would not be regulated and it was its intent to sell the system at that point in time. Fairways/Mt. Plymouth did not monitor the customer connections and its requirement to be certificated by the PSC was overlooked as development progressed.

Although customers were connected to the water and wastewater system in 2002, Fairways/Mt. Plymouth did not begin billing customers until May of 2003.

Per Aqua Utilities Florida Inc., the following is their residential customers proposed tariff :

	Base Rate	Gallons Charged Per 1,000
Water	\$7.50	\$1.75
Irrigation	\$7.50	\$1.75
Wastewater	\$7.50	\$3.75

Using the billing registers and generals ledgers of Fairways/Mt. Plymouth, Ltd., and Aqua Utilities Florida, Inc., the audit staff determined the revenues for May 2003 through Dec. 31, 2007 as shown on the schedule below.

	2003	2004	2005	2006	2007
Water	12,447	26,939	189,484	42,917	95,011
Wastewater	20,406	51,692	62,641	76,628	82,373
Irrigation	26,258	63,035	82,240	144,923	71,565
Misc. (A)	(1,116)	14,526	12,574	11,448	2,400
Total Revenues	<u>57,995</u>	<u>156,193</u>	<u>346,940</u>	<u>275,916</u>	<u>251,350</u>

(A). Miscellaneous revenues also contain billing adjustments.

Fairways/Mt. Plymouth, Ltd., did not pay any Regulatory Assessment Fees (RAFs) during its ownership of the utilities.

EFFECT ON GENERAL LEDGER IF FINDING IS ACCEPTED: No effect on the general ledger. This Audit Finding is provided for informational purposes only.

EFFECT ON FILING IF FINDING IS ACCEPTED: No effect on the filing. This Audit Finding is provided for informational purposes only.

AUDIT FINDING NO. 5

SUBJECT: EXPENSES

STATEMENT OF FACT: Fairways/Mt. Plymouth, Ltd., sold its water and wastewater utilities to Aqua Utilities Florida, Inc. on April 30, 2007.

Fairways/Mt. Plymouth, Ltd., did not record its expenses using the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts

Using invoices and generals ledgers of Fairways/Mt. Plymouth, Ltd., and Aqua Utilities Florida, Inc., the audit staff determined the expenses for 2006 and 2007 as shown on the schedules below:

Fairways/Mt. Plymouth, Ltd., 2006 expenses were combined for water and wastewater in its general ledger. The Audit Staff sampled the expenses and split the total evenly between water and wastewater.

Water		
Expenses:		
ACCOUNT	2006 DESCRIPTION	Total
615	Purchased Power	8,618
636	Contractual Services - Other	38,495
675	Misc. Expenses	7,716
	Total:	<u>54,829</u>

Wastewater		
Expenses:		
	2006	
711	Sludge Removal Expense	32,732
715	Purchased Power	8,618
736	Contractual Services - Other	5,763
775	Misc. Expenses	7,716
	Total:	<u>54,829</u>

Water**Expenses:** 2007

ACCOUNT NO.	DESCRIPTION	Total
601	Salaries and Wages - Employees	7,550
604	Employee Pensions and Benefit	(18)
615	Purchased Power	11,084
618	Chemicals	2,060
620	Materials and Supplies	684
631	Contractual Services - Engineering	1,553
633	Contractual Services - Legal	7,610
635	Contractual Services - Testing	1,692
636	Contractual Services - Other	28,194
670	Bad Debt Expense	4,806
675	Misc. Expenses	9,294
	Total Water Expenses:	<u><u>74,507</u></u>

Wastewater**Expenses:** 2007

ACCOUNT NO.	DESCRIPTION	Total
701	Salaries and Wages - Employees	11,585
704	Employee Pensions and Benefits	(484)
711	Sludge Removal Expense	11,436
715	Purchased Power	7,816
718	Chemicals	3,152
720	Materials and Supplies	1,327
731	Contractual Services - Engineering	903
733	Contractual Services - Legal	7,610
735	Contractual Services - Testing	2,265
736	Contractual Services - Other	28,206
770	Bad Debt Expense	118
775	Misc. Expense	9,299
	Total Wastewater Expenses:	<u><u>83,233</u></u>

EFFECT ON GENERAL LEDGER IF FINDING IS ACCEPTED: No effect on the general ledger. This Audit Finding is provided for informational purposes only.

EFFECT ON FILING IF FINDING IS ACCEPTED: No effect on the filing. This Audit Finding is provided for informational purposes only.

AUDIT FINDING NO. 6

SUBJECT: NEGATIVE ACQUISITION ADJUSTMENT

STATEMENT OF FACT: Fairways/Mt. Plymouth, Ltd., sold its water and wastewater utilities to Aqua Utilities Florida, Inc. on April 30, 2007 for \$449,973. Aqua Utilities Florida, Inc., is requesting a water and wastewater rate base value of \$1,911,911.

Rule 25-30.0371, Florida Administrative Code states the following:

(1) Definition. For the purpose of this rule, an acquisition adjustment is defined as the difference between the purchase price of utility system assets to an acquiring utility and the net book value of the utility assets. A positive acquisition adjustment exists when the purchase price is greater than the net book value. A negative acquisition adjustment exists when the purchase price is less than the net book value.

(3) Negative Acquisition Adjustments. A negative acquisition adjustment shall not be included in rate base unless there is proof of extraordinary circumstances or where the purchase price is less than 80 percent of net book value. If the purchase price is less than 80 percent of net book value then the inclusion of a negative acquisition adjustment shall be calculated pursuant to paragraph (b) below.

(a) Contested. Any entity that believes a full or partial negative acquisition adjustment should be made has the burden to prove the existence of extraordinary circumstances. Under no circumstance, however, shall the purchaser be required to record on its books more than 70 percent of a negative acquisition adjustment. In determining whether extraordinary circumstances have been demonstrated, the Commission shall consider evidence provided to the Commission such as the anticipated retirement of the acquired assets and the condition of the assets acquired.

(b) Uncontested. If the purchase price is less than 80 percent of net book value, then the amount of the difference in excess of 20 percent of net book value shall be recognized for ratemaking purposes as a negative acquisition adjustment. The negative acquisition adjustment shall not be recorded on the books for ratemaking purposes or used for any earnings review unless the purchaser files for a rate increase pursuant to Section 367.081(2), 367.0814, 367.0817 or 367.0822, F.S., that will be effective during the amortization period. The negative acquisition adjustment shall be amortized over a 5-year period from the date of issuance of the order approving the transfer of assets.

The audit staff determined that a negative acquisition adjustment of \$425,223 should be recognized for ratemaking purposes as shown below:

	Water	Wastewater	Total
Rate Base per audit @ April 30, 2007	\$ 137,605	\$ 956,390	\$ 1,093,995
80% of Rate Base			\$ 875,196
Purchase Price			\$ 449,973
Negative Acquisition Adjustment per Audit			<u>\$ 425,223</u>

EFFECT ON GENERAL LEDGER IF FINDING IS ACCEPTED: A negative acquisition adjustment should be recorded on the general ledger in the amount of \$425,223.

EFFECT ON FILING IF FINDING IS ACCEPTED: Total rate base would be decreased by \$425,223.

EXHIBIT I - WATER

FAIRWAYS/MT. PLYMOUTH, LTD.
DOCKET NO. 070739-WS
ESTABLISH RATE BASE AT TRANSFER
AS OF APRIL 30, 2007

DESCRIPTION	AMOUNT PER FILING	AUDIT ADJUSTMENT	AUDIT FINDING	AMOUNT PER AUDIT
UTILITY PLANT IN SERVICE	\$ 778,681			\$ 778,681
LAND	\$ 4,560	\$ (2,560)	2	\$ 2,000
CONTRIBUTIONS IN AID OF CONSTRUCTION (CIAC)	\$ (131,220)	\$ (417,960)	3	\$ (549,180)
ACCUMULATED DEPRECIATION	\$ (147,836)			\$ (147,836)
ACCUMULATED AMORTIZATION OF CIAC	\$ 13,688	\$ 40,252	3	\$ 53,940
TOTAL:	\$ 517,873	\$ (380,268)		\$ 137,605

EXHIBIT II - WASTEWATER

FAIRWAYS/MT. PLYMOUTH, LTD.
DOCKET NO. 070739-WS
ESTABLISH RATE BASE AT TRANSFER
AS OF APRIL 30, 2007

DESCRIPTION	AMOUNT PER FILING	AUDIT ADJUSTMENT	AUDIT FINDING	AMOUNT PER AUDIT
UTILITY PLANT IN SERVICE	\$ 1,694,224			\$ 1,694,224
LAND	\$ 4,000	\$ (1,000)	2	\$ 3,000
CONTRIBUTIONS IN AID OF CONSTRUCTION (CIAC)	\$ -	\$ (486,000)	3	\$ (486,000)
ACCUMULATED DEPRECIATION	\$ (304,187)			\$ (304,187)
ACCUMULATED AMORTIZATION OF CIAC	\$ -	\$ 45,353	3	\$ 45,353
TOTAL:	\$ 1,394,037	\$ (441,647)		\$ 952,390