

State of Florida



Public Service Commission

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

DATE: August 14, 2000
 TO: Division of Economic Regulation (Merta)
 FROM: Division of Regulatory Oversight (Vandiver) W
 RE: 000108-GU; Chesapeake Utilities Corporation
 Audit Report; Rate Case
 Historical 12-Month Period Ended December 31, 1999
 Audit Control No. 00-159-3-1

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, they should send it to the Division of Records and Reporting. There are no confidential work papers associated with this audit.

DNV/sp

Attachment

cc: Division of Regulatory Oversight (Hoppe/Harvey/File Folder)
 Orlando District Office (Winston)
 ✓ Division of Records and Reporting
 Division of Legal Services

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FLORIDA PUBLIC SERVICE COMMISSION
DIVISION OF REGULATORY OVERSIGHT
BUREAU OF AUDITING SERVICES

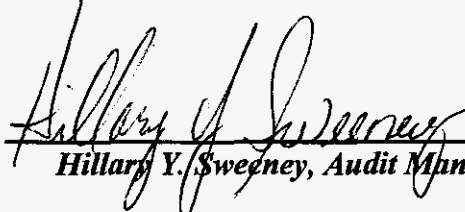
Orlando District Office

**FLORIDA DIVISION OF
CHESAPEAKE UTILITIES CORPORATION**


RATE CASE AUDIT

HISTORICAL 12-MONTH PERIOD ENDED DECEMBER 31, 1999

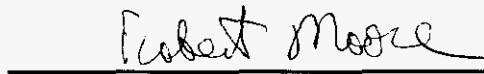
DOCKET NO. 000108-GU
AUDIT CONTROL NO. 00-159-3-1



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**DIVISION OF REGULATORY OVERSIGHT
AUDITOR'S REPORT**

AUGUST 7, 2000

TO: FLORIDA PUBLIC SERVICE COMMISSION AND OTHER INTERESTED PARTIES

We have applied the procedures described later in this report to audit the accompanying Rate Base, Net Operating Income and Capital Structure schedules for the historical 12-month period ended December 31, 1999, for the Florida Division of Chesapeake Utilities Corporation. These schedules were prepared by the company as part of its petition for rate relief in Docket No. 000108-GU.

This is an internal accounting report prepared after performing a limited scope audit. Accordingly, this report should 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.

SUMMARY OF SIGNIFICANT FINDINGS

The utility did not make the adjustment per Commission Order No. 23166, issued July 10, 1990, to disallow \$509,422 in acquisition adjustment.

The utility did not remove purchased gas adjustment (PGA) revenues, PGA expenses, and PGA taxes by \$5,790,925, \$5,791,942, and \$28,983, respectively, for 2001 from its Minimum Filing Requirements (MFRs) filing.

The utility understated Account No. 242.8, Flex-Rate Liability by \$10,305.

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 the 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.

Verify - The item was tested for accuracy and compared to the substantiating documentation.

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.

Examined - The exhibit amounts were reconciled with the general ledger. The general ledger account balances were traced to subsidiary ledgers. Selective analytical review procedures were applied, and account balances were tested to the extent further described.

Confirmed - Evidential matter supporting an account balance, transaction, or other information was obtained directly from an independent third party.

RATE BASE: Examined account balances for utility-plant-in-service (UPIS), contributions-in-aid-of-construction (CIAC), accumulated depreciation, and accumulated amortization of CIAC from June 30, 1989. Reconciled rate base balances authorized in Commission Order No. 23166, issued July 10, 1990, to the June 30, 1989 general ledger balance. Tested plant account balances using stratified sample methods. Examined supporting documentation for sample CIAC additions selected using auditor judgment and agreed to FPSC-approved tariff amounts. Compiled working capital accounts. Tested additions to accumulated depreciation and accumulated amortization for proper rates and calculations. Tested working capital for interest-bearing amounts, unfunded reserves, and non-utility transactions using auditor judgment.

NET OPERATING INCOME: Compiled and reviewed utility revenue and operating and maintenance accounts for the year ended December 31, 1999. Chose a judgmental sample of customer bills and recalculated using FPSC-approved rates. Verified a judgmental sample of operation and maintenance expenses and examined the invoices and other supporting documentation. Tested the calculation of depreciation expense. Examined support for taxes other than income and income taxes

CAPITAL STRUCTURE: Compiled components of the capital structure for the year ended December 31, 1999. Agreed interest expense to the terms of the notes and bonds. Confirmed note balances at December 31, 1999.

Exception No. 1

Subject: Capitalized Sales Tax on Plant Additions

Statement of Fact: The utility reported 1999 year-end balances of \$4,000,202 and \$1,053,519 for Accounts 376, Mains (Plastic), and 381, Meters, respectively.

Recommendation:

Account 376 Mains (Plastic)

The 1999 ending balance is overstated by \$2,324. The utility charged additional sales tax of \$1,114 ($\$18,571 * .06$) and \$1,210 ($\$20,161 * .06$) on the total amount of two invoices. The utility should reduce Account 376 by \$2,324 ($\$1,114 + \$1,210$).

Account 381 Meters

The utility charged additional sales tax of \$575 ($\$9,582.07 * .06$) on the total amount of an invoice. The utility should reduce Account 381 by \$575.

Exception No. 2

Subject: Acquisition Adjustment

Statement of Fact: In Commission Order No. 23166, issued July 10, 1990, the Commission disallowed \$509,422 in acquisition adjustment. The utility reported a 1999 year-end acquisition adjustment balance of \$509,422 in its general ledger. The utility did not make the Commission-ordered adjustment to its books. However, it did remove this amount in its MFRs filing.

Recommendation: Per Commission Order No. 23166, the utility should remove \$509,422 from Account 114.1, Excess Cost of Acquisition-New-CFG Adjustments.

Exception No. 3

Subject: PGA Revenues, PGA Expenses, and PGA Taxes

Statement of Fact: The utility included the following PGA revenues, PGA expenses, and PGA taxes in its MFRs.

	<u>1999</u>	<u>2000</u>	<u>2001</u>
PGA revenues	\$7,806,424	\$7,195,543	\$5,790,925
PGA expenses	\$7,665,881	\$7,159,530	\$5,761,942
PGA-related taxes	\$39,070	\$36,013	\$28,983

In accordance with Commission Order No. PSC-92-0924-FOF-GU, issued September 3, 1992, it is appropriate to remove PGA-related items that are recoverable through the PGA Cost Recovery Clause.

The projected amounts for the years 2000 and 2001 assume no over/under recovery.

Recommendation: The above amounts should be removed from the MFRs as shown above.

Exception No. 4

Subject: Common Equity

Statement of Fact: The utility reported a 1999 year-end common equity balance of \$11,216,456 in its general ledger. The MFRs reported a 1999 year-end common equity balance of \$11,809,982.

The utility's general ledger reports a 1999 ending balance of \$11,216,456 and a 2000 beginning balance of \$11,809,982. The utility does not record closing journal entries for the expense and revenue summary accounts. However, it does reflect the net effect in the beginning balance of the next year. The difference, \$593,526 ($\$11,809,982 - \$11,216,456$), is net income.

Recommendation: The 2000 opening balance of common equity reflects an adjustment to include net income. The utility should be required to make these journal entries to the general ledger accounts as part of its end of year closing entries. Closing and adjusting entries posted for the purpose of recording net operating income should be visible in the utility's general ledger accounts.

Exception No. 5

Subject: Misstated Flex-Rate Liability

Statement of Fact: The utility reported a 13-month average balance for flex-rate liability of (\$46,880).

<u>Account</u>	<u>Account Title</u>	<u>13 Month Average</u>
242.8	Flex Rate Liability - 10/94 - 9/95	\$23,490
242.81	Flex Rate Liability - 10/95 -9/96	<u>\$23,390</u>
	Total Flex Rate Liability	<u>\$46,880</u>

Working Capital

In MFRs Schedule B-13, the utility reported an adjustment of (\$46,880) to miscellaneous current liabilities to reflect the flex-rate liability 13-month average balance.

Cost of Capital

In MFRs Schedule D-1, the utility reported an adjustment of \$46,880 to reflect the flex-rate liability 13-month average balance. The average balance should be increased by \$10,305 to account for an amount, \$66,981, included in the calculation as a debit rather than a credit entry to the account.

Recommendation: The 13-month average balance for flex rate liability should be as scheduled below:

<u>Account</u>	<u>Account Title</u>	<u>13-Month Average per Company</u>	<u>Adjustment</u>	<u>13-Month Average per Audit</u>
242.8	Flex Rate Liability - 10/94 - 9/95	\$23,490	\$10,305	\$33,795
242.81	Flex Rate Liability - 10/95 -9/96	<u>\$23,390</u>	_____	<u>\$23,390</u>
	Total Flex Rate Liability	<u>\$46,880</u>	<u>\$10,305</u>	<u>\$57,185</u>

Working Capital

An additional \$10,305 should be removed from the current liabilities section of working capital. This adjustment reflects an amount, \$66,981, included in the 13-month average as a debit instead of a credit amount. This change will have the effect of increasing the 13-month average balance of working capital from \$498,227 to \$508,532.

Cost of Capital

The flex-rate liability, a zero-cost component of the capital structure, should be increased by \$10,305. This will not change the weighted average cost of capital, 8.26 percent, because of its small size.

SCHEDULE G-1

CALCULATION OF THE PROJECTED TEST YEAR RATE BASE

PAGE 1 OF 28

FLORIDA PUBLIC SERVICE COMMISSION

EXPLANATION: PROVIDE A SCHEDULE CALCULATING A 13-MONTH AVERAGE RATE BASE FOR THE HISTORIC BASE YEAR, THE HISTORIC BASE YEAR PLUS ONE, AND THE PROJECTED TEST YEAR.

TYPE OF DATA SHOWN:
HISTORIC BASE YEAR DATA: 12/31/99
HISTORIC BASE YR + 1: 12/31/00
PROJECTED TEST YEAR: 12/31/01
WITNESS: WILLIAMS

COMPANY: FLORIDA DIVISION OF CHESAPEAKE UTILITIES CORP.

DOCKET NO.: 000108-GU

LINE NO.	DESCRIPTION	BASE YEAR		BASE YEAR	BASE YR + 1	PROJECTED	PROJECTED	PROJECTED TEST YEAR AS ADJUSTED
		12/31/99 (PER BOOKS)	COMPANY ADJUSTMENT	ADJUSTED AVERAGE YEAR	AVERAGE YEAR	TEST YEAR UNADJUSTED AVERAGE YR.	TEST YEAR ADJUSTMENTS	
<u>UTILITY PLANT</u>								
1	PLANT IN SERVICE	\$25,289,618	(\$23,702)	\$25,265,914	\$26,589,098	\$31,990,292	(\$23,702)	\$31,956,590
2	CONSTRUCTION WORK IN PROGRESS	\$927,693	\$0	\$927,693	\$1,822,064	\$1,822,064	(\$1,822,064)	\$0
3	ACQUISITION ADJUSTMENT	\$775,529	(\$775,529)	(\$0)	\$632,831	\$632,831	(\$632,831)	\$0
4	COMMON PLANT ALLOCATED	\$0	(\$87,328)	(\$87,328)	\$0	\$0	(\$108,135)	(\$108,135)
5	PLANT HELD FOR FUTURE USE	\$0	\$0	\$0	\$0	\$0	\$0	\$0
6	TOTAL	\$26,992,839	(\$896,557)	\$26,106,282	\$31,043,993	\$34,435,187	(\$2,586,732)	\$31,848,455
<u>DEDUCTIONS</u>								
7	ACCUM PROV-DEPR & AMORT	(\$4,069,092)	\$741,557	(\$3,327,535)	(\$9,934,813)	(\$11,319,815)	\$707,832	(\$10,612,182)
8	CUSTOMER ADVANCES FOR CONSTRUCTION	(\$196,399)	\$0	(\$196,399)	(\$297,829)	(\$267,828)	\$0	(\$267,828)
9	TOTAL DEDUCTIONS	(\$4,265,491)	\$741,557	(\$3,523,934)	(\$10,202,641)	(\$11,587,643)	\$707,832	(\$10,880,010)
10	PLANT NET	\$17,927,347	(\$146,000)	\$17,781,347	\$20,841,352	\$22,847,544	(\$1,879,100)	\$20,968,445
<u>ALLOWANCE FOR WORKING CAPITAL</u>								
11	BALANCE SHEET METHOD	(\$6,591,010)	\$7,069,237	\$498,227	(\$8,196,574)	(\$10,662,111)	\$11,015,367	\$353,256
12	TOTAL RATE BASE	\$11,336,337	\$6,944,237	\$18,280,574	\$11,641,778	\$12,185,434	\$9,136,267	\$21,321,700
13	NET OPERATING INCOME	\$1,187,828	(\$116,167)	\$1,041,661	\$341,870	\$585,651	\$221,368	\$807,219
14	RATE OF RETURN	10.21%		5.70%		4.81%		3.79%

SUPPORTING SCHEDULES: G-1 p.4-6, G-1 p.15, G-2, p.18, G-2 p.21
G-2 p.22, G-2 p.1-3, G-4 p.1-2

SCHEDULE G-3

CALCULATION OF THE PROJECTED TEST YEAR - COST OF CAPITAL

PAGE 2 OF 11

FLORIDA PUBLIC SERVICE COMMISSION

EXPLANATION: PROVIDE A SCHEDULE CALCULATING A 13 MONTH AVERAGE COST OF CAPITAL FOR THE PROJECTED TEST YEAR

TYPE OF DATA SHOWN:
PROJECTED TEST YEAR 12/31/01
WITNESS: WILLIAMS

COMPANY: FLORIDA DIVISION OF CHESAPEAKE UTILITIES CORP.

DOCKET NO.: 000108-GU

LINE NO.	DESCRIPTION	ADJUSTMENTS			RATIO	COST RATE	WEIGHTED COST	
		PER BOOKS	SPECIFIC	PRO RATA ADJUSTED				
1	COMMON EQUITY	11,822,978	(1,533,682)	0	10,289,296	48.28%	12.00%	5.79%
2	LONG TERM DEBT	0	6,377,973	0	6,377,973	29.91%	7.52%	2.25%
3	SHORT TERM DEBT	0	2,119,103	0	2,119,103	9.94%	6.03%	0.60%
4	CUSTOMER DEPOSITS	789,257	0	0	789,257	3.70%	6.44%	0.24%
5	DEFERRED TAXES	1,392,213	0	0	1,392,213	6.53%	0.00%	0.00%
6	FLEX RATE LIABILITY	0	46,880	0	46,880	0.22%	6.30%	0.01%
7	TAX CREDIT	306,978	0	0	306,978	1.44%	0.00%	0.00%
8	TOTAL	14,311,426	7,010,274	0	21,321,700	100.00%		8.89%

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SCHEDULE G-2

CALCULATION OF THE PROJECTED TEST YEAR - NOI - SUMMARY

FLORIDA PUBLIC SERVICE COMMISSION

EXPLANATION: PROVIDE THE CALCULATION OF NET OPERATING INCOME PER BOOKS FOR THE HISTORIC BASE YEAR, THE PROJECTED NET OPERATING INCOME FOR THE HISTORIC BASE YEAR + 1, AND THE PROJECTED TEST YEAR.

TYPE OF DATA SHOWN:
 HISTORIC BASE YEAR DATA: 12/31/99
 HISTORIC BASE YEAR + 1: 12/31/00
 PROJECTED TEST YEAR: 12/31/01
 WITNESS: WILLIAMS

COMPANY: FLORIDA DIVISION OF CHESAPEAKE UTILITIES CORP.

DOCKET NO.: 000108-GU

LINE NO.	HISTORIC BASE YEAR PER BOOKS	COMPANY ADJUSTMENTS	HISTORIC BASE YEAR ADJUSTED	HISTORIC BASE YEAR + 1 2000	PROJECTED TEST YEAR 2001	PROJECTED TEST YEAR ADJUSTMENTS	PROJECTED TEST YEAR AS ADJUSTED
OPERATING REVENUE:							
1	OPERATING REVENUES						
	\$17,293,932	(\$738,010)	\$16,555,922	\$14,238,052	\$13,481,994	\$0	\$13,481,994
2	REVENUE RELIEF	\$0	\$0	\$0	\$0	\$0	\$0
3	CHANGE IN UNBILLED REVENUES	\$0	\$0	\$0	\$0	\$0	\$0
4	REVENUES DUE TO GROWTH	\$0	\$0	\$0	\$0	\$0	\$0
5	TOTAL REVENUES	(\$738,010)	\$16,555,922	\$14,238,052	\$13,481,994	\$0	\$13,481,994
OPERATING EXPENSES:							
6	COST OF GAS	\$0	\$9,150,224	\$7,105,543	\$5,790,925	\$0	\$5,790,925
7	OPERATION & MAINTENANCE	(\$478,588)	\$3,835,428	\$4,228,460	\$4,617,575	\$0	\$4,617,575
8	DEPRECIATION & AMORTIZATION	(\$36,715)	\$1,099,938	\$1,271,558	\$1,377,195	(\$4,047)	\$1,373,148
9	AMORTIZATION - OTHER	\$0	\$0	\$0	\$0	\$0	\$0
10	TAXES OTHER THAN INCOME	(\$312)	\$1,157,103	\$1,207,458	\$1,155,218	\$0	\$1,155,218
11	TAXES OTHER THAN INCOME - GRWTH	\$0	\$0	\$0	\$0	\$0	\$0
12	INCOME TAXES FEDERAL	(\$89,099)	\$222,081	(\$18,118)	(\$52,512)	\$0	(\$62,512)
13	INCOME TAXES - STATE	(\$14,829)	\$37,345	(\$6,259)	(\$11,978)	\$0	(\$11,978)
14	INCOME TAXES - GROWTH - FEDERAL	\$0	\$0	\$0	\$0	\$0	\$0
15	INCOME TAXES - GROWTH - STATE	\$0	\$0	\$0	\$0	\$0	\$0
16	INTEREST SYNCHRONIZATION	\$0	\$0	\$0	\$0	(\$217,321)	(\$217,321)
17	DEFERRED TAXES - FEDERAL	\$12,234	\$12,234	\$39,254	\$39,244	\$0	\$39,244
18	DEFERRED TAXES - STATE	\$0	\$0	\$0	\$0	\$0	\$0
19	INVESTMENT TAX CREDITS	\$0	\$0	(\$19,523)	(\$19,523)	\$0	(\$19,523)
20	TOTAL OPERATING EXPENSES	(\$621,843)	\$15,514,261	\$13,888,382	\$12,898,143	(\$221,388)	\$12,676,755
21	OPERATING INCOME	(\$116,167)	\$1,041,661	\$341,670	\$585,851	\$221,388	\$807,219

SUPPORTING SCHEDULES: G-2, p.2-4, G-4 p.2-3

RECAP SCHEDULES: A-1, A-4