State of Florida

Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

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

DATE: February 17, 2015

TO: Office of Commission Clerk

FROM: Lynn M. Deamer, Chief of Auditing, Office of Auditing and Performance Analysis

RE: Docket No.: 140217-WU
Company Name: Cedar Acres, Inc.
Company Code: WU917
Audit Purpose: Staff-Assisted Rate Case
Audit Control No: 14-343-1-1

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 a response to the Office of Commission Clerk. There is no confidential work papers associated with this audit.

LMD/cp

Attachment: Audit Report

cc: Office of Auditing and Performance Analysis File

State of Florida

Public Service Commission

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

Auditor's Report

Cedar Acres, Inc.
Staff-Assisted Rate Case

Twelve Months Ended September 30, 2014

Docket No. 140217-WU
Audit Control No. 14-343-1-1
January 30, 2015

V. Hymavathi

Hymavathi Vedula
Audit Manager

George Simmons
Audit Staff

Lynn M. Deamer

Lynn M. Deamer
Reviewer

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Purpose

To: Florida Public Service Commission

We have performed the procedures described later in this report to meet the agreed-upon objectives set forth by the Division of Accounting and Finance in its audit service request dated December 9, 2014. We have applied these procedures to the attached schedules prepared by audit staff in support of Cedar Acres, Inc.'s request for a Staff-Assisted Rate Case in Docket No. 140217-WU.

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

Objectives and Procedures

Background

The test year is the historical twelve months ended September 30, 2014.

Cedar Acres, Inc. is a Class C utility in Sumter County. Order PSC-09-0541-FOF-WU, issued August 4, 2009, granted the original certificate and approved initial rates and charges. It also stated that the Utility provides water service to 312 residential customers in the Oakland Hills mobile home subdivision, and that there are an additional 12 lots in the subdivision that have individual wells and are not on the utility system. Rate Base has never been established.

NARUC refers to the National Association of Regulatory Utility Commissioners.

USOA refers to the NARUC Uniform System of Accounts as adopted by Rule 25-30.115, Florida Administrative Code (F.A.C.).

The Utility has a sister company called the J.S.R. Company (Company). They are related through shared owners.

The Utility is a corporation and as such files a Form 1120, Corporate Tax Return.

General

Utility Books and Records

Objectives: The objective was to determine whether the Utility maintains its books and records in conformity with NARUC USOA

Procedures: We reviewed the Utility's books and records by obtaining its general ledger. We determined that the Utility's books and records are not in compliance with the NARUC USOA. See Finding 1.

Rate Base

Utility Plant in Service

Objectives: The objectives were to determine whether Utility Plant in Service (UPIS): 1) Consists of property that exists and is owned by the Utility, 2) Additions are recorded at original cost, 3) Retirements are made when a replacement asset was put in service, and 4) Adjustments required in the Utility's last rate proceeding were recorded in its books and records.

Procedures: Rate base has never been established for Cedar Acres, Inc. The Utility was able to locate a bid that it had received to build the plant in 1985. Audit staff was not able to verify if this was the bid actually accepted at the time. We stratified the amounts on the bid into NARUC account numbers and tried to match the amounts to the 2008 annual report. (There are no annual reports filed prior to 2008.) We also tried to reconcile the bid to the general ledger. We could not successfully reconcile the bid to the general ledger or the annual report. However, audit staff doesn't believe that the bid is sufficient documentation to support original plant in service, so we removed the Utility's original cost of UPIS from our audited balance. The Utility could only support, with sufficient documentation, additions of $57,019 added in 2010, 2011, and 2012. This is the audited balance as of September 30, 2014. See Finding 2.

Land & Land Rights

Objectives: The objectives were to determine whether utility land is: 1) Recorded at original cost, 2) Owned or secured under a long-term lease agreement, and that 3) Adjustments required in the Utility's last rate proceeding were recorded in its books and records.

Procedures: We searched the Sumter County Clerk of the Courts' official records to verify the ownership of the Utility's land. We calculated the land balance using document stamps that were placed on the land deeds. We determined that the land balance for the water system is not recorded at cost by the Utility as of September 30, 2014. See Finding 3.

Accumulated Depreciation

Objectives: The objectives were to determine whether accumulated depreciation: 1) Accruals are properly calculated and recorded based on Rule 25-30.140 – Depreciation, F.A.C., 2) Retirements are recorded when an asset was replaced, and 3) Adjustments required in the Utility's last rate proceeding were recorded to its books and records.

Procedures: We calculated depreciation accruals for all supported additions and verified that the correct depreciation rates were used as of September 30, 2014. See Finding 4.

Contributions-in-Aid-of-Construction

Objectives: The objectives were to determine whether Contributions in Aid of Construction (CIAC): 1) Consist of cash or property contributions that exist and are owned by the Utility, 2) Additions are recorded using Commission approved tariffs, 3) Retirements are recorded when a contributed asset was replaced, and 4) Adjustments required in the Utility's last rate proceeding were recorded to its books and records.

Procedures: Audit staff reviewed annual reports and documentation from the Utility, and determined that the Utility has not recorded CIAC. The Utility does have an approved tariff, effective September 18, 2009, that sets the service availability fee to the actual cost. Order PSC-09-0541-FOF-WU, issued August 4, 2009, states that the Utility provides water service to 312 residential customers in the Oakland Hills mobile home subdivision, and that there are an additional 12 lots in the subdivision that have individual wells and are not on the utility system. Audit staff checked with the Utility and this has not changed. Therefore, audit staff could not impute a cost based on the approved tariff for the 312 customers because 1) there is not a defined cost in the tariff, 2) documentation does not exist to determine whether the cost to begin service was passed on to the customer, and 3) audit staff could not determine the original cost of plant and thus impute CIAC pursuant to Rule 25-30.-570 F.A.C. No further work was performed.

Accumulated Amortization of CIAC

Objectives: The objectives were to determine whether Accumulated Amortization of CIAC: 1) Accruals are properly calculated and recorded based on Rule 25-30.140 – Depreciation, F.A.C.,

2) Retirements are recorded when a contributed asset was replaced, and 3) Adjustments required in the Utility's last rate proceeding were recorded to its books and records.

Procedures: Audit staff couldn't verify an amount for CIAC; therefore, accumulated amortization of CIAC was not calculated.

Acquisition Adjustment

Objectives: The objective was to determine whether an acquisition adjustment is recorded on the books and records of the Utility, and if so, whether it has been approved by the Commission.

Procedures: The Utility has not changed owners while under the jurisdiction of the Florida Public Service Commission, therefore, an acquisition adjustment does not and should not exist. No further work done.

Working Capital

Objectives: The objective was to determine the working capital allowance to be included in rate base pursuant to Rule 25-30.433- Rate Proceedings, F.A.C.

Procedures: We calculated the working capital allowance for the test year using one-eighth of Operation and Maintenance (O&M) Expense. See Finding 7.

Capital Structure

Objectives: The objectives were to determine the: 1) Components of the Utility's capital structure, 2) Cost rate for each class of capital, 3) Overall weighted cost of capital, and that 4) Components are properly recorded in compliance with the NARUC USOA.

Procedures: We reviewed the Utility's general ledger and determined that the Utility's capital structure is composed of common equity. We determined the year-end and simple average capital structure balance and its weighted average cost as of September 30, 2014. See Finding 5.

Net Operating Income

Operating Revenue

Objectives: The objectives were to determine whether revenues are: 1) Representative of the Utility's operations for the test year, 2) Calculated using Commission approved tariff rates, and 3) Recorded in compliance with NARUC USOA.

Procedures: We summarized the Utility's gallonage by customer account for the test year using the Utility's billing report. We calculated revenues for water using the number of bills and gallonage. We compared the calculated revenues obtained with water revenues recorded in the general ledger. See Finding 6.

Operation and Maintenance Expense

Objectives: The objectives were to determine whether Operation and Maintenance Expenses (O&M) are: 1) Representative of the Utility's ongoing operations for the test year, 2) Recorded in the appropriate period for the correct amount, 3) Required for the provision of utility services, and 4) Recorded in compliance with the NARUC USOA.

Procedures: We reviewed the invoices provided in support of the Utility's O&M expense for the test year. We ensured all expenses were correctly classified, and verified that they were recurring in nature. We verified each expense against the invoice and supporting documentation. See Finding 7.

Depreciation and CIAC Amortization Expense

Objectives: The objective is to determine the Utility's depreciation and CIAC amortization expense for the twelve months ended September 30, 2014 using the Commission authorized rates.

Procedures: We calculated the depreciation for the additions to plant in service that we could trace to sufficient supporting documentation for the twelve months ended September 30, 2014. There is no CIAC amortization expense. See Finding 4.

Taxes Other than Income

Objectives: The objectives were to determine whether taxes other than income (TOTI) is: 1) Representative of the Utility's ongoing operations for the test year, 2) Recorded in the appropriate period for the correct amount, 3) Required for the provision of utility services, and 4) Recorded in compliance with the NARUC USOA.

Procedures: We compiled the Utility's TOTI for the test year using the general ledger and supporting documentation. See Finding 9.

Audit Findings

Finding 1: NARUC Chart of Accounts

Audit Analysis: The Utility's books and records were not maintained in accordance with NARUC USOA procedures. The Utility did not have general ledgers prior to 2012. The Utility did not use the USOA account numbering system in its general ledger for the period January 1, 2012 through October 31, 2014. In the Utility's general ledger, income is recorded when a deposit is made and expenses are recorded when a check is written. There is no accounts payable, and very few journal entries are recorded. At year-end, the Utility's Certified Public Accountant (CPA) prepares the annual report to be filed with this Commission. The CPA prepares the year-end adjusting journal entries in order to reclassify items for reporting purposes, which can be traced to the annual reports.

Effect on the General Ledger: For information purposes only.

Effect on the Staff Prepared Exhibits: None.

Finding 2: Utility Plant in Service

Audit Analysis: We tried to reconcile a bid provided by the Utility for the original cost of plant in or about 1985 to the first annual report filed with the Commission. Audit staff was not able to verify if this was the bid that had been accepted. In the 2008 annual report, UPIS excluding land had a balance of $327,385 and the bid, based on the audit review, provided a balance of $454,789. Audit staff requests the staff engineer to review this documentation. There were no additions or retirements on the annual reports until 2012. The Utility only provided general ledgers for the years 2012, 2013, and as of 10/31/2014. Audit staff attempted to reconcile the annual reports to the general ledger as shown in Table 2-1.

Table 2-1

	Annual Reports	General Ledgers	Variance
2012	$376,149	$360,474	($15,675)
2013	$379,563	$363,888	($15,675)
10/31/2014	N/A	$364,357	N/A

We were not able reconcile these two documents, and the Utility is unable to explain the variance. However, it should be noted that since plant went into service in 1985, it has approximately 30 years of depreciation, which would significantly offset the original cost of plant.

Audit staff traced plant additions to invoices as shown in Table 2-2. We calculated the associated retirements using 75 percent of the cost of any additions that had been replaced based on Commission practice. If the engineer and analyst determine a beginning balance for original costs, then the retirement amounts should be applied to those balances.

Table 2-2

	Plant Additions	Retirements
2010	$3,532	$2,648
2011	$17,434	$13,075
2012	$36,053	$23,247
Total	**$57,019**	**$38,970**

Of the $57,019 of plant additions, audit staff could not directly trace these amounts by plant account to the annual reports or the general ledger. However, we did note plant additions of $52,178 in the 2012 and 2013 annual reports and general ledgers. We also noted plant additions of $1,986 in the 2014 general ledger (as of 10/31/2014).

Audit staff verified additions of $57,019 and depreciated the plant accounts with respect to these balances as shown in Table 2-3 following this finding.

Finding 2 (Cont.)

Effect on the General Ledger: To be determined by the Utility.

Effect on the Staff Prepared Exhibits: We calculated the simple average balance for UPIS to be $57,019 as of September 30, 2014.

Table 2-3

	12/31/09	Adds	12/31/10	Adds	12/31/11	Adds	12/31/12	Adds	12/31/13	Adds	9/30/14
307 Wells	-	$3,532	$3,532	17,434	$20,966	$11,192	$32,158	-	$32,158	-	$32,158
310 Power Eq.	-	-	-	-	-	$23,971	$23,971	-	$23,971	-	$23,971
311 Pump Eq.	-	-	-	-	-	$890	$890	-	$890	-	$890
Total	-	**$3,532**	**$3,532**	**$17,434**	**$20,966**	**$36,053**	**$57,019**	-	**$57,019**	-	**$57,019**

Finding 3: Land and Land Rights

Audit Analysis: NARUC USOA, Definition 9, defines "Original Cost", as applied to utility plant, to mean the cost of such property to the person first devoting it to public service.

The Utility's land balance in the general ledger is $47,740 as of September 30, 2014. Audit staff calculates it to be $4,440 based on our findings discussed below.

Cedar Acres, Inc. purchased 217 acres of land on June 10, 1983, of which 4.34 acres was dedicated to public service for use by the Utility. Audit staff determined a purchase price of $222,000 based on the documentary stamps affixed on the deed, which equates to approximately $1,023 per acre. Therefore, audit staff calculates land to be $4,440 (4.34 acres x $1,023) as shown in Table 3-1.

Table 3-1

	Balance per Utility	Audit Adj.	Balance per Audit
Land	$47,740	($43,300)	$4,440
Total	**$47,740**	**($43,300)**	**$4,440**

The 4.34 acres is divided into two non-contiguous parcels, each having a well. One of the parcels also has the water treatment facility on it. The Utility stated that it only uses one of the parcels. The other parcel has a non-working well on it. We did not verify this and request that the staff engineer review this issue and make adjustments, if any, to the value of land that we calculated.

Effect on the General Ledger: To be determined by the Utility.

Effect on the Staff Prepared Exhibits: We calculated the simple average balance for land to be $4,440 as of September 30, 2014.

Finding 4: Accumulated Depreciation and Depreciation Expense

Audit Analysis: In the general ledger, the Utility has a balance of $275,116 for accumulated depreciation as of September 30, 2014. The Utility did not record depreciation for the test year. The Utility only provided general ledgers for the years 2012, 2013, and as of 10/31/2014. Audit staff attempted to reconcile the annual reports to the general ledger as shown in Table 4-1.

Table 4-1

	Annual Reports	General Ledgers	Variance
2012	$281,823	$275,116	($6,707)
2013	$288,940	$275,116	($13,824)
10/31/2014	N/A	$275,116	N/A

As of September 30, 2014, audit staff calculated a balance of $8,199 for accumulated depreciation and a balance of $2,648 ($663 + $1,985) for depreciation expense based on the supported plant additions and using the rates prescribed in Rule 25-30.140, F.A.C. as shown in Table 4-2 following the finding.

Effect on the General Ledger: To be determined by the Utility.

Effect on the Staff Prepared Exhibits: We calculated the simple average balance for accumulated depreciation to be $6,836 as of September 30, 2014. We calculated depreciation to be $2,648 for the test year ended September 30, 2014.

Table 4-2

	A/D 12/31/2010	Dep. Exp (12 mos)	A/D 12/31/2011	Dep Exp (12 mos)	A/D 12/31/2012	Dep. Exp (9 mos)	Dep Exp (3 mos)	A/D 12/31/2013	Dep. Exp (9 mos)	A/D 9/30/2014
307	($131)	($776)	($907)	($1,191)	($2,098)	($893)	($298)	($3,289)	($891)	($4,180)
310	-	-	-	($1,410)	($1,410)	($1,058)	($352)	($2,820)	($1,055)	($3,875)
311	-	-	-	($52)	($52)	($40)	($13)	($105)	($39)	($144)
Total	**($131)**	**($776)**	**($907)**	**($2,653)**	**($3,561)**	**($1,991)**	**($663)**	**($6,214)**	**($1,985)**	**($8,199)**

Finding 5: Capital Structure

Audit Analysis: Audit staff reviewed the Utility's annual reports from 2008 through 2013 for the capital structure components. We noted that the 2013 annual report had a balance of $9,500 for common equity, a balance of ($118,986) for retained earnings (deficit), and a balance of $217,550 for notes payable to associated companies. We tried to trace the amounts noted above to the 2013 general ledger and tax return, but were unable to do so. We did not include these balances in calculating the capital structure. The Utility does not collect customer deposits.

The Utility provided a promissory note for a line of credit with J.S.R. Company, a related party, in the principal sum of $325,000. Interest accrues at five percent (5%) per annum. However, based on Commission practice, the line of credit from a related party should be treated as equity since no principal or interest payments had been made as of September 30, 2014.

The Utility also provided a schedule of cash deposits from the line of credit, and we were able to trace the amounts to the 2012 and 2013 general ledgers. Audit staff was able to determine the balances as of September 30, 2013 to be $206,750 and September 30, 2014 to be $258,139. We calculated a simple average balance of $232,445, which is 100 percent equity. Based on the leverage formula from Order PSC-14-0272-PAA-WS, issued May 29, 2014, the return on equity is 8.74 percent. See Exhibit 2.

Effect on the General Ledger: None.

Effect on the Staff Prepared Exhibits: The return on equity should be 8.74 percent.

Finding 6: Operating Revenue

Audit Analysis: The Utility records revenues at the end of the calendar year. The Utility recorded total revenues of $28,638 for 2013 in the general ledger. The Utility did not book 2014 revenues in the general ledger as of September 30, 2014. Based on the billing registers, audit staff calculated test year revenues to be $35,402.

We multiplied the number of 1,000 gallons billed for residential and general service customers by current Commission approved rates to arrive at test year revenues.

Table 6-1

Revenue Adjustment Increase (Decrease)			
Service Type	**Test Year Revenues Per Audit**	**Per General Ledger**	**Difference**
Residential Revenues	$35,402	$28,638	$6,764
Total	**$35,402**	**$28,638**	**$6,764**

Effect on the General Ledger: There is no effect on the general ledger.

Effect on the Staff Prepared Exhibits: We calculated operating revenues to be $35,402 for the test year ended September 30, 2014.

Finding 7: Operations and Maintenance Expense

Audit Analysis: The Utility recorded $93,343 of O&M expenses for the test year. We reviewed all the test year O&M expenses and made adjustments that decrease O&M expense by $5,340 as shown in Table 7-1.

Table 7-1

Test Year O&M Adjustments					
Account	**Description**	**Per Utility**	**Per Audit**	**Difference**	
601	Salaries & Wages – Employees	$50,837	$51,923	$1,086	**(1)**
615	Purchased Power	$3,764	$3,223	($541)	**(2)**
616	Fuel for Power Purchased	-	$315	$315	**(2)**
618	Chemicals	$13,539	$1,477	($12,062)	**(3)**
630	Contractual Services – Billing	-	$12,062	$12,062	**(3)**
631	Contractual Services – Professional	$11,568	$5,980	($5,588)	**(4)**
635	Contractual Services – Testing	$7,265	$6,670	($595)	**(5)**
675	Miscellaneous Expenses	$6,371	$6,353	($18)	**(6)**
	Total	**$93,343**	**$88,003**	**($5,340)**	

The audit adjustments were made for the following reasons.

1. Account 601 - Salaries & Wages - Employees should be increased by $1,086 based on the employee's 2014 W-2.
2. Account 615 – Purchased Power should be decreased by $541 ($226 + $315). We removed $226 for electric service for a lighted sign indicating the subdivision and not the Utility. We also reclassified $315 to Account 616 – Fuel for Power Purchased.
3. Account 618 – Chemicals should be decreased by $12,062, and that amount should be reclassified to Account 630 – Contractual Services-Billing.
4. Account 631 – Contractual Services-Professional should be decreased by $5,588 due to insufficiently supported expenses. $3,488 was removed for temporary office help that is non-recurring and $2,100 was removed because it was out of period and non-utility.
5. Account 635 – Contractual Services-Testing should be decreased $595 due to an invoice that was paid twice.
6. Account 675 – Miscellaneous Expenses should be decreased by $18 due to lack of support and the Utility did not provide an explanation.

Working capital allowance is calculated to be $11,000 ($88,003 x 1/8).

Effect on the General Ledger: To be determined by the Utility.

Effect on the Staff Prepared Exhibits: We calculated O&M expenses to be $88,003 for the test year ended September 30, 2014 and calculated the working capital allowance to be $11,000.

Finding 8: Proforma Adjustments

Audit Analysis: The Utility shares office space with the J.S.R. Company, a related party, and does not pay rent to the Company. The Utility stated that ¼ of the office space is used by the Utility. The total monthly rent is $3,048, and the Utility's portion is calculated to be $762. The Utility also states that it should also be allocated an estimated $250 a month for office supplies and equipment usage.

The Utility has no liability or property/casualty damage insurance for their plant or equipment and has not provided an estimate for this amount.

Effect on the General Ledger: No effect on the general ledger.

Effect on the Filing: The analyst needs to determine whether these costs should be included in the test year.

Finding 9: Taxes Other than Income

Audit Analysis: We reviewed all test year TOTI and made adjustments based on the following.

1) Audit staff calculated regulatory assessment fees (RAF) to be $1,593 for the test year based on test year revenues. We reviewed the 2013 RAF form and determined that the Utility had underpaid RAF by $296. The Utility filed an amended RAF form on January 13, 2015 and paid $296.
2) Audit staff determined payroll taxes to be $1,030 based on the Utility's one employee's salary.
3) Audit staff determined property taxes to be $22.66 based on the 2014 tax bill from the county. However, depending on what the Commission staff engineer determines with land, this may change.

The adjustments are shown in Table 9-1.

Table 9-1

Total TOTI Adjustments			
Increase (Decrease)			
	Per Utility	Per Audit	Difference
Regulatory Assessment Fees	$1,289	$1,593	$304
Payroll Taxes	$1,030	$1,030	-
Property Taxes	$23	$23	-
Total	**$2,342**	**$2,646**	**$304**

Effect on the General Ledger: No effect on the general ledger.

Effect on the Filing: We calculated TOTI to be $2,646 for the test year ended September 30, 2014.

Exhibits

Exhibit 1: Rate Base

Cedar Acres, Inc.
Schedule of Rate Base
As of September 30, 2014

	Balance per Utility 9/30/2014	Audit Adjustments	Balance per Audit 9/30/2014	Simple Average
Plant in Service	$364,356	($307,337)	$57,019	$57,019
Land	$47,740	($43,300)	$4,440	$4,440
Accumulated Depreciation	($275,116)	$266,917	($8,199)	($6,836)
CIAC	-	-	-	-
A.A. of CIAC	-	-	-	-
Working Capital	-	$11,000	$11,000	$11,000
Total Rate Base	**136,980**	**($72,720)**	**$64,260**	**$65,623**

Note: The audited balance contains only the amounts that audit staff could support by invoices. The beginning balances are unknown, and the staff engineer and analyst need to determine the disposition.

Exhibit 2: Capital Structure

Cedar Acres, Inc.
Schedule of Cost of Capital
As of September 30, 2014

Class of Capital		**Balance 9/30/2013**		**Balance 9/30/2014**		**Simple Average**		**% of Total**
Long Term Debt		-		-		-		0.00%
Short Term Debt		-		-		-		0.00%
Common Equity		$206,750		$258,139		$232,445		100.00%
Total		**$206,750**		**$258,139**		**$232,445**		100.00%

Equity Formula using Order PSC 14-0272-PAA-WS

Return = 7.13 + (1.610/equity ratio)
Return = 7.13 + (1.610/1)
Return = 8.74%

Exhibit 3: Net Operating Income

Cedar Acres, Inc.

Schedule of Net Operating Income

Test Year Ended September 30, 2014

	Balance per Utility 9/30/2014	Audit Adjustments	Balance per Audit 9/30/2014
Revenues	$28,638	$6,764	$35,402
Operation and Maintenance Expenses	$93,343	($5,340)	$88,003
Depreciation Expenses	-	$2,648	$2,648
Amortization Expense	-	-	-
Taxes Other Than Income Taxes	$2,342	$304	$2,646
Total Net Operating Income	**($67,047)**	**$9,152**	**($57,895)**