

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

• * * * *

In the Matter of:

APPLICATION OF CUMBERLAND FALLS)
HIGHWAY WATER DISTRICT FOR (1) A)
CERTIFICATE OF PUBLIC CONVENIENCE AND)
NECESSITY TO CONSTRUCT EXTENSIONS AS)
DESCRIBED; (2) AUTHORITY TO BORROW) CASE NO. 9451
APPROXIMATELY \$403,000 FROM FARMERS)
HOME ADMINISTRATION; (3) AUTHORITY TO)
REFUND EXISTING FMHA INDEBTEDNESS;)
(4) A RATE INCREASE EFFECTIVE)
NOVEMBER 20, 1985)

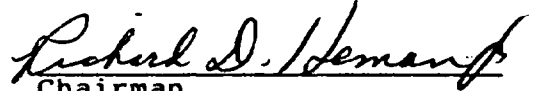
O R D E R

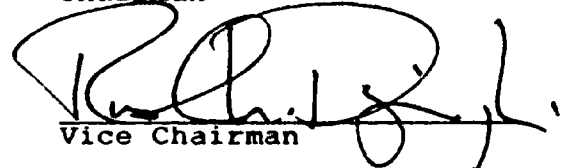
IT IS ORDERED that:

1. The Staff Audit Report for Cumberland Falls Highway Water District ("Cumberland Falls") attached hereto as Appendix A shall be included as a part of the record in this proceeding.
2. Staff will be available for cross-examination at the hearing set for Thursday, March 27, 1986, at 10 A.M., Eastern Standard Time, in the Commission's offices, Frankfort, Kentucky.

Done at Frankfort, Kentucky, this 24th day of March, 1986.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary

APPENDIX A
Report on Limited Audit
of
Cumberland Falls Highway Water District

PREFACE

On October 30, 1985, Cumberland Falls Highway Water District ("Cumberland Falls") filed an application requesting (1) a Certificate of Public Convenience and Necessity to Construct Extensions, (2) Authority to Borrow Approximately \$403,000 from Farmers Home Administration ("FmHA"), (3) Authority to Refund Existing FmHA Indebtedness and (4) a Rate Increase. The proposed number of new customers due to the extension is 130, an increase of approximately 18 percent. These proposed new customers should generate approximately \$33,530 annually from the existing rates. The proposed rates would generate \$65,965 annually in additional revenues.

In order to expedite the processing of the case and substantially reduce the need for written data requests, the Commission staff chose to perform an audit, limited in scope, on the operations of Cumberland Falls. The audit was conducted by Ms. Angela Schweickart and Mr. Isaac Scott of the Division of Rates and Tariffs on March 4-7, 1986, at the offices of Howard K. Bell, Consulting Engineers ("HKB") in Lexington, Kentucky.

SCOPE

The scope of this audit was limited to ascertaining whether the operating expenses for the test period ended July 31, 1985, were accounted for in accordance with the Uniform System of Accounts for Water Utilities ("Uniform System of Accounts") and were properly allocated.

FINDINGS

Cumberland Falls entered into a management agreement with HKB in January, 1984. Under the terms of the contract, HKB is to furnish the following management and supervision activities:

1. Appoint a field manager to supervise and coordinate the day-to-day operations.
2. Maintain proper operating and accounting records.
3. Perform all maintenance services with its forces or by contract.
4. Read customer meters monthly and install new services.
5. Provide and maintain all necessary and proper services required in the billing and collection of monthly water bills.
6. Establish and maintain an office and storage area, as may be required, in Whitley County, Kentucky.

These management and supervision activities have been billed by HKB to Cumberland Falls during the test period under the following provisions:

1. A fixed monthly fee of \$450 for managerial services, \$550 per month beginning January 1, 1986.
2. A fee of \$4.50 per month per customer billed, \$5 per month beginning January 1, 1986.

3. All supplies, labor, equipment, and any other direct and/or indirect costs incurred in performing actual maintenance and construction work at HKB's actual cost.

HKB, who also provides management and bookkeeping services for East Knox County Water District ("East Knox"), entered into an agreement with East Knox to provide all the aforementioned services for Cumberland Falls. In addition, HKB keeps the books for East Knox. HKB receives a monthly invoice, reflecting actual charges for services provided for Cumberland Falls, from East Knox with the various costs separated into System Maintenance and Construction Costs - Account No. 008, and General Management Costs - Account No. 006. Each month HKB bills Cumberland Falls at the \$450 monthly fee and the \$4.50 per month per customer billed to cover the charges included in the 006 Accounts and actual charges for the expenses included in the 008 Accounts. Any additional work HKB has performed for Cumberland Falls such as consulting services is also billed monthly to Cumberland Falls as a part of the aforementioned invoices.

When HKB receives Cumberland Falls' invoice from East Knox they record on the books of Cumberland Falls both the 006 and the 008 expenses at the actual amounts billed with a balancing credit entry into Accounts Payable to HKB. During the next month Cumberland Falls generally receives a statement from HKB and proceeds to credit the cash account and debit the HKB Accounts Payable account for the amount of the statement.

This procedure results in a difference in expenses each month since actual costs are recorded in the 006 Accounts

initially and then ultimately paid by Cumberland Falls in the form of a flat monthly fee of \$450 per month and \$4.50 per customer. Since Cumberland Falls records all the expenses from the East Knox invoice at first, an adjustment is made for the prior month to allocate the difference between the accounts payable recorded in the prior month corresponding to the East Knox invoice and the amount actually paid and debited to HKB Accounts Payable. This differential has been prorated by Cumberland Falls to the following four accounts:

HKB Billing		
<u>Account No.</u>	<u>Account No.</u>	<u>Account</u>
006	90901000	Meter Reading Labor
006	90902000	Accounting & Collecting Labor
006	92920000	Administrative Services
008	64640000	Transmission & Distribution Labor

Cumberland Falls decided to prorate the differential to these accounts because they wanted to keep the other expense accounts at "actual". The following accounts per East Knox invoices are classified as 006 expenses:

HKB Billing		
<u>Account No.</u>	<u>Account No.</u>	<u>Account Title</u>
006	901	Meter Reading Expense
006	902	Accounting & Collecting
006	920	Administrative Services
006	926	Employee Benefits
006	933	Transportation Expense

According to the contract, the aforementioned 006 expenses are included in the \$450 monthly fee and \$4.50 per month per customer billed fee.

Both East Knox's and HKB's monthly invoices are generally dated on the last day of the month. Since HKB keeps both East Knox's and Cumberland Falls' books, this adjustment of the prior month's differential is unnecessary and results in some misclassification of expenses. For instance, when HKB performs some additional consulting work, these expenses end up being included in the differential and, therefore, allocated to the four labor accounts (one of which is Transmission and Distribution Labor - 640, which is classified as an 008 expense and, therefore, is passed on at actual from East Knox to HKB to Cumberland Falls).

Since HKB apparently has access to the records of all the parties on a timely basis, the prior month adjustment unnecessarily complicates the accounting process. Therefore, for purposes of this audit, the test period expenses per the HKB and East Knox invoices have been recomputed by matching the months the expenses were incurred. The HKB monthly \$450 fee and \$4.50 fee per month per customer billed have been allocated monthly to all the aforementioned 006 accounts based upon a weighted-average of those 006 expenses on the East Knox invoice for the same month. This method eliminates the need for a monthly adjustment, allocates the 006 expenses to the proper accounts and allows the expenses incurred by Cumberland Falls from HKB for additional consulting services to be properly classified. It is recommended that Cumberland Falls follow this procedure in the future.

In addition to the foregoing restatement of expenses, the audit revealed the following:

Purchased Water - 601

Cumberland Falls reported a test-year purchased water expense of \$62,563. A review of test-year purchased water invoices confirms this amount as being correct and, therefore, no adjustments to this account are necessary.

Power Purchased for Pumping - 622

Cumberland Falls included in this account \$1,597 for electricity for the office. According to the Uniform System of Accounts, this expense is required to be recorded in Office Supplies and Expense Account 921. Therefore, this account has been reduced by \$1,597 to a balance of \$5,648.

Transmission and Distribution-Labor - 640

Cumberland Falls reported \$25,277 test year expense for Transmission and Distribution Labor. This account is classified as an 008 expense, and, therefore, this expense per the East Knox invoice was passed on at actual to Cumberland Falls from HKB. However, this account has been included in Cumberland Falls' allocation of the monthly cost differential previously discussed even though it is not an 006 expense. In addition, the adjusting entry for the months of March through July of the test year were incorrectly recorded in reverse. An entry was made by Cumberland Falls in an attempt to correct the error, however, it was incorrect.

Since this is an 008 expense and it is passed through to Cumberland Falls at actual cost from East Knox, it has not been included in the revised allocation of the 006 expenses. The

Transmission and Distribution Labor expense per the East Knox invoices for the test year totals \$25,547. Therefore, this expense has been increased by \$270.

Transmission and Distribution-Supplies and Expenses - 641

Cumberland Falls reported a test year expense of \$1,307 for Transmission and Distribution-Supplies and Expenses. However, a review of the cash disbursements ledger revealed a duplicate payment of an invoice to W. D. Bryant and Sons of \$51. In addition, two communication expenses totaling \$256 were incorrectly expensed to this account instead of Miscellaneous-General Expenses - 930. Therefore, this account has been reduced by \$307 to reflect the proper test year expense.

Maintenance of Mains - 651

The maintenance of mains expense reported by Cumberland Falls for the test year was \$1,498. However, this included credits of \$1,134 due to customers paying for a part of the service being performed. This revenue should have been recorded in Account No. 474 - Other Water Revenues and not netted against the maintenance of mains expense. Therefore, this expense has been increased to \$2,632 in accordance with the Uniform System of Accounts.

Maintenance of Services - 652

Cumberland Falls reported for the test year a maintenance of services expense of \$1,429. Due to the recomputation of expenses from East Knox through HKB to Cumberland Falls, a slight discrepancy of \$6 occurred. Since the recomputation is based on the actual expenses incurred during a month and avoids a timing

problem, the recomputation is considered correct and the expense has been reduced to \$1,423.

Maintenance of Meters - 653

The maintenance of meters expense reported by Cumberland Falls for the test year was \$6,470. However, a review of invoices disclosed that \$7,786 was improperly expensed. In addition, a review of the General Journal revealed that \$1,500 was improperly credited to this account.

Cumberland Falls expensed during the test year two master meter relocations totaling \$6,874. In accordance with the Uniform System of Accounts, these expenses have been capitalized in Account No. 101-343 - Transmission and Distribution Lines and depreciated over 35 years using the straight-line depreciation method.

The cost of the Brush Harbor master meter relocation was computed on work order no. 85-31. East Knox prepared the work order and performed the work. The work order stated that a 4-inch tapping valve costing \$265 was supplied at no charge. Cumberland Falls, however, included this expense in the Maintenance of Meters Account for the test year. Since this item was provided at "no charge" it has been capitalized in Account No. 101-343 - Transmission and Distribution Lines and included in Account No. 271 - Contribution in Aid of Construction.

Tri County Assemblies, Inc., ("Tri County") is an industrial customer that needed the Brush Harbor master meter relocation to insure a proper level of pressure. Tri County agreed to contribute \$1,500 towards the cost of the master meter relocation.

Cumberland Falls credited this revenue to the Maintenance of Meters Account. According to the Uniform System of Accounts, this revenue is required to be recorded in Account No. 271 - Contributions in Aid of Construction instead of being credited to the expense account.

Cumberland Falls installed a new 2-inch meter at Tri County. The total cost was \$647 and was incorrectly expensed. The meter costing \$349 is required to be recorded in Account No. 101-346 - Meters while the \$298 installation charge is required to be recorded in Account No. 101-347 - Meter Installations-Services.

Due to the capitalization of the aforementioned items and the reclassification of the revenue from Tri County, the maintenance of meters expense has been reduced to \$184.

Extraordinary Repairs and Maintenance - 656

Cumberland Falls reported \$211 of extraordinary repairs and maintenance expense for the test year. The \$211 expense was incurred for having a pump motor installed, which was held in stock. According to the Uniform System of Accounts, this expense should be capitalized and recorded in Account No. 101-325 - Pumping Plant Structures and Equipment. This item has, therefore, been reclassified and depreciated over 10 years using the straight-line depreciation method.

Meter Reading Labor - 901

Cumberland Falls reported a test-year meter reading labor expense of \$12,950. Due to the recomputation of expenses from East Knox through HKB to Cumberland Falls a slight discrepancy of \$7 occurred. Since the recomputation is based on the actual

expenses incurred during a month and avoids a timing problem, the recomputation is considered correct and the expense has been restated at \$12,957.

Accounting and Collecting Labor - 902 and Administrative Services
- 920

The reported test year expense for accounting and collecting labor was \$22,310. The reported test year expense for administrative services is \$1,619. Due to the allocation method Cumberland Falls used and a problem of Cumberland Falls recording the monthly adjusting entry in reverse for the last 5 months of the test year and then making an incorrect correcting entry, a discrepancy arose between the amounts reported per the application and the amounts from the recomputation of the monthly expenses actually incurred. Since the recomputation is based on the actual expenses incurred during a month and avoids a timing problem and avoids the "incorrect" adjusting entries made for the last 5 months of the test year, the recomputation is considered correct. Therefore, the accounting and collecting labor expense has been increased by \$1,956 due to the discrepancy while the administrative services expense has been reduced by \$330.

Office Supplies and Expense - 921

Cumberland Falls reported a test-year office supplies and expense of \$640. This expense has been increased by \$1,597 due to the reclassification of the power expense for the office from Account No. 622 - Power Purchased for Pumping.

Outside Services-Engineering - 923

Cumberland Falls reported for the test year outside services-engineering expenses of \$2,500. Vaughn and Melton Consulting Engineers prepared a preliminary engineering report for the proposed expansion project for \$2,500. Pursuant to the Uniform System of Accounts and Generally Accepted Accounting Principles, expenses associated with the preparation of a case before the Commission should be charged to Account No. 186 - Miscellaneous Deferred Debits and amortized over 3 years in the Regulatory Commission Expense - Account No. 928. Therefore, this expense has been reclassified reducing the outside services-engineering expense to \$0.

Employee Benefits - 926

East Knox hired three full-time employees to perform duties only for Cumberland Falls. When one of these employees takes a sick or vacation day, their hours are charged to Employee Benefit Account 926. Of the three employees, one works under Accounting Labor and Administrative Services while the other two work under Meter Reading Labor and Transmission and Distribution Labor. The employee benefits expense is classified as an 006 expense and, therefore, is included in the monthly fee and the \$4.50 per month per customer billed fee of HKB to Cumberland Falls. Since these expenses for vacation and sick leave are not considered actual employee benefits, such as health insurance, these expenses should be charged in the future to the various labor accounts which that employee's labor would have been charged for that day. This accounting method should be followed since the transmission and

distribution labor expense is an 008 expense and, as such, is passed on as actual to Cumberland Falls and should not be subject to the allocation of the HKB monthly fees. In addition, this method would provide a more accurate classification of expenses.

Due to time constraints and the limited scope of this audit, the aforementioned reclassification of Employee Benefits was not made for the test year. However, since Employee Benefits is classified as an 006 expense, it is subject to the allocation of the monthly fees. Cumberland Falls did not use this account when allocating the monthly adjustment. In addition, Cumberland Falls misclassified this expense for October through December during the test year by including it in General Miscellaneous Expense Account 930, instead of the Employee Benefits Account.

Due to the aforementioned items and the recomputation of the monthly expenses, a discrepancy has appeared. Since the recomputation is based on the actual expenses incurred for a month prorated from the HKB monthly fees, it is considered correct. Therefore, the employee benefits expense has been increased by \$1,770.

Regulatory Commission Expense - 928

Cumberland Falls included in this account the Public Service Commission annual assessment of \$218. This expense is required by the Uniform System of Accounts to be recorded in Account No. 408 - Taxes Other Than Income. The expenses associated with preparing and presenting a case to the Commission should be accounted for in Account No. 186 - Miscellaneous

Deferred Debits and amortized through the Regulatory Commission Expense Account 928.

During the test year Cumberland Falls incurred the following expenses associated with the case performed by HKB:

<u>Date of Invoice</u>	<u>Description</u>	<u>Amount</u>
1/31/85	Proposed Water Line Extension Project	\$3,587.50
6/30/85	Consulting Services as Requested - Water Line Extension Project	273.22
7/31/85	Consulting Services as Requested - Water Line Extension Project	<u>261.27</u>
	TOTAL	<u>\$4,121.99</u>

Due to Cumberland Falls' practice of the monthly allocation of the difference between the accounts payable recorded in the prior month and the accounts payable amount actually paid in the current month, these expenses associated with the case were not separated out but allocated to the four labor accounts Cumberland Falls has chosen to use for the monthly adjustment. Since a recomputation of the monthly expenses has been done, the expenses associated with the preparation of the case have been reclassified into Account No. 186 - Miscellaneous Deferred Debits and amortized over 3 years through the Regulatory Commission Expense Account. The \$2,500 preliminary engineering report has also been reclassified into the appropriate accounts.

The total for Account No. 186 - Miscellaneous Deferred Debits is \$6,622. Since this is to be amortized over 3 years, the Regulatory Commission Expense Account 928 is \$2,207 for the test year.

Miscellaneous General Expenses - 930

Cumberland Falls reported test-year miscellaneous general expenses of \$2,992. However, the communication expenses of \$256 incorrectly recorded in Account No. 641 - Transmission and Distribution-Supplies and Expenses has been reclassified to the Miscellaneous General Expenses. In addition, the employee benefits expense for October, November and December of the test year had been incorrectly recorded in the Miscellaneous General Expenses. The Employee Benefit expense totaling \$1,674 has been reclassified to Account No. 926 - Employee Benefits.

A review of the General Journal disclosed a credit to the Miscellaneous General Expense Account of \$58 originating from the cash receipts journal. According to the Uniform System of Accounts, revenues received should not be credited to the associated expense account. Therefore, this revenue item has been excluded from the Miscellaneous General Expense Account and included in Account No. 474 - Other Water Revenue.

The cumulative total of the aforementioned items results in reducing the miscellaneous general expense by \$1,360 to a balance of \$1,632.

Transportation Expense - 933

Cumberland Falls reported a test-year transportation expense of \$8,055. This account includes expenses incurred from HKB's monthly fees, actual other expenses, and lease payments on a truck. The transportation expense per East Knox invoices is classified as an 006 expense and, therefore, is included in HKB's monthly fees to Cumberland Falls. Cumberland Falls did not

include the transportation expense in its monthly adjustment of the allocation of the difference of the accounts payable recorded in the prior month and the accounts payable amount actually paid during the current month.

Since the transportation expense is classified as an 006 expense, it is subject to the allocation of HKB's monthly fees based upon the weighted average of all the 006 expenses per each month. The recomputation of the monthly expenses incurred results in a different amount charged to the transportation expense than under Cumberland Falls' method of monthly adjustments. Since the recomputation amount is determined on actual expenses incurred in the current month and avoids any timing problems and requires no monthly adjustment, it is considered correct.

Cumberland Falls included in the transportation expense a \$350 deposit for the lease of a truck. This deposit is not an expense since it is subject to refund under the lease agreement. The deposit should be classified in Account No. 134 - Other Special Deposits.

During the test year, Cumberland Falls had a transmission overhaul performed on another truck. This expense totaled \$385 and should have been capitalized in Account No. 392 - Transportation Equipment. This expense has been reclassified and is being depreciated over 5 years using the straight-line method of depreciation.

The cumulative total adjustments to this expense due to the aforementioned items is \$<505>. Therefore, this expense has been reduced to \$7,550.

Improvements to Corbin and Bee Creek Pumping Stations

During the test year HKB provided engineering services to help determine how to improve the Corbin and Bee Creek Pumping Stations. The total expense for these services during the test year was \$7,052. Due to Cumberland Falls' method of allocating the difference in the Accounts Payable recorded for the prior month and the Accounts Payable actually paid in the current month, this expense has been allocated to the four labor expense accounts. Since these improvements will eventually improve the stations and the benefit derived will extend over one period, these expenses have been capitalized in Account No. 101-321 - Pumping Plant-Structure and Improvements and depreciated over 10 years using the straight-line depreciation method.

Meter Reclassification

In July 1985, the cost of a meter was incorrectly capitalized in Account No. 101-347 - Meter Installations. Therefore, the meter expense of \$308 has been reclassified to Account No. 101-346 - Meters.

Depreciation Expense - 300

Cumberland Falls reported test-year depreciation expense of \$19,407. Due to the limited audit several items have been capitalized, therefore, increasing test year depreciation. The following schedule recaps the capitalization adjustments with the applicable depreciation expense:

<u>Account No.</u>	<u>Title of Account</u>	<u>Depreciation Expense</u>	<u>Explanation</u>
101-392	Transportation Equipment	\$ 77	Transmission over-haul, S/L 5 years; \$385
101-343	Transmission & Distribution Lines	204	2 master meter relocations; S/L 35 years; \$7,139
101-321	Pumping Plant - Structure and Improvements	705	Improvements to Corbin & Bee Creek Pumping Stations; S/L 10 years; \$7,052
101-325	Pumping Plant - Electric Structure & Equipment	21	Labor to install pump held in stock; S/L 10 years; \$211.01
101-347	Meter Installations	-0-	April, 1985 - Tri County Meter Installation; \$298; July, 1985 meter reclassified in Meter Account \$<308>; S/L 35 yrs.
101-346	Meters	46	April 1985/Meters \$349; May 1985/Meters \$955; July 1985/Meter reclassified from Meter Installation Acct. 308; S/L 35 yrs.

\$1,053

Because of the limited scope of this audit, the staff has not determined the validity of Cumberland Falls reported plant in service; therefore, except for the increase in depreciation expense due to the aforementioned capitalized items, the staff has made no attempt to verify Cumberland Falls' depreciation expense. The adjusted depreciation expense for the test year is \$20,460.

Taxes Other Than Income - 408

Cumberland Falls recorded the annual Public Service Commission assessment in Account No. 928 - Regulatory Commission Expense. Pursuant to the Uniform System of Accounts, this expense is required to be included in Account No. 408 - Taxes Other Than Income. Therefore, this expense has been reclassified to Account No. 408 - Taxes Other Than Income.

Other Water Revenues - 474

The Uniform System of Accounts requires miscellaneous operating revenues received to be recorded in Account No. 474 - Other Water Revenues. Per the cash receipts and sales journals, several credits to the Maintenance of Mains Account 651 and to the Miscellaneous General Expense Account 930 were made incorrectly. These credits are required to be recorded in the Other Water Revenues Account 474. These credits total \$1,192 and have been classified to Account No. 474 - Other Water Revenues.

SUMMARY

The following is a summary of the effect of these adjustments on Cumberland Falls' test-year operating statement:

Acct. <u>No.</u>	<u>Account Name</u>	<u>Test Year Reported</u>	<u>Staff Adjustments</u>	<u>Test Year Adjusted</u>
<u>Revenues</u>				
461	Sales-Gen. Customers	\$182,459		\$182,459
464	Sales-Public Utilities	2,796		2,796
471	Misc. Serv. Revenues	4,252		4,252
474	Other Water Revenues	-0-	\$ 1,192	\$ 1,192
		<u>\$189,507</u>	<u>\$ 1,192</u>	<u>\$190,699</u>
<u>Operating Expenses</u>				
601-1	Purchased Water - Corbin	\$ 44,992	-0-	\$ 44,992
601-2	Purchased Water - Williamsburg	16,772	-0-	16,772
601-3	Purchased Water - W. Laurel	799	-0-	799
622	Power Purchased for Pumping	7,245	<1,597>	5,648
623	Pumping-Supplies & Expenses	34	-0-	34
625	Maintenance of Pumping Plant	599	-0-	599
632	Water Treatment & Expense	150	-0-	150
640	Trans. & Dist. Labor	25,277	270	25,547
641	Trans. & Dist. Sup. & Exp.	1,307	<307>	1,000
651	Maintenance of Mains	1,498	1,134	2,632
652	Maintenance of Services	1,429	<6>	1,423
653	Maintenance of Meters	6,470	<6,286>	184
654	Maintenance of Hydrants	166	-0-	166
656	Extraordinary Repairs & Maintenance	211	<211>	-0-
901	Meter Reading Labor	12,950	7	12,957
902	Acct. & Collecting Labor	22,310	1,956	24,266
903	Customer Accounts-Supplies & Expenses	3,868	-0-	3,868
904	Uncollectible Accounts	2,555	-0-	2,555
920	Administrative Services	1,619	<330>	1,289
921	Office Supplies & Expenses	640	1,597	2,237
923-1	Outside Serv.-Engineering	2,500	<2,500>	-0-
923-2	Outside Services-Legal	835	-0-	835
923-3	Outside Serv.-Accounting	3,865	-0-	3,865
924-1	Liability & Property Ins.	282	-0-	282
924-3	Insurance-Truck	989	-0-	989
924-4	Insurance-Fidelity Bonds	110	-0-	110
926	Employee Benefits	1,210	1,770	2,980
928	Regulatory Commission Exp.	218	1,989	2,207
930	Miscellaneous Gen. Expense	2,992	<1,360>	1,632
933	Transportation Expense	8,055	<505>	7,550
		<u>\$171,947</u>	<u>\$<4,379></u>	<u>\$167,568</u>

<u>Acct. No.</u>	<u>Account Name</u>	<u>Test Year Reported</u>	<u>Staff Adjustments</u>	<u>Test Year Adjusted</u>
403	Depreciation Expense	\$ 19,407	\$1,053	\$ 20,460
408	Taxes Other Than Income	-0-	218	218
<u>Other Income</u>				
419	Interest Income	\$ 3,145	\$ -0-	\$ 3,145
<u>Other Deductions</u>				
427	Interest on Long-Term Debt	\$ 13,917	\$ -0-	\$ 13,917
431	Interest Expense	<u>1,458</u>	<u>-0-</u>	<u>1,458</u>
	NET INCOME (LOSS)	<u>\$ <14,077></u>	<u>\$4,300</u>	<u>\$ <9,777></u>

CONCLUSIONS AND RECOMMENDATIONS

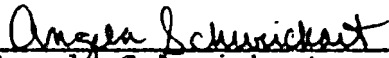
Cloyd Hamilton and Company ("Cloyd") issued a qualified opinion for the year 1982 due to inadequacies of the accounting records. Since Cumberland Falls has contracted for outside accounting services (Peggy Brown of Woodcreek Water District for 1983 and HKB for 1984 to the present), Cloyd has issued unqualified opinions for the calendar years 1983, 1984, and 1985. It is apparent that the records are in a better condition. However, the accounting method initiated by HKB for Cumberland Falls concerning the monthly adjusting entry is more complex than needed, as previously stated.

It is recommended that the months in which the expenses are actually incurred by Cumberland Falls from both HKB and East Knox be "matched". Therefore, the HKB current monthly fees can be properly allocated to all the 006 accounts for Cumberland Falls' records based upon the 006 expenses per the East Knox invoice for

the same month using a weighted average. As previously stated, this method would eliminate the need for a monthly adjusting entry, simplifying the accounting method, in addition to allocating the 006 expenses correctly and properly classifying the additional consulting work performed by HKB for Cumberland Falls.

Cumberland Falls should reclassify the expenses recorded in Account No. 926 - Employee Benefits into the applicable labor accounts in the future, as stated previously. This reclassification would provide a more accurate picture of the applicable labor accounts.

Due to the limited scope of the audit, the staff did not attempt to determine the accuracy of Cumberland Falls's plant in service and did not verify test-year depreciation expense. However, the aforementioned items which were capitalized and depreciated or amortized, should be reclassified on Cumberland Falls's books.

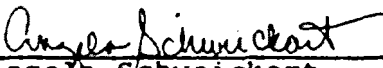


Angela Schweickart
Public Utilities Financial Analyst
Senior
Public Service Commission
Division of Rates and Tariffs
Revenue Requirements Section

the same month using a weighted average. As previously stated, this method would eliminate the need for a monthly adjusting entry, simplifying the accounting method, in addition to allocating the 006 expenses correctly and properly classifying the additional consulting work performed by HKB for Cumberland Falls.

Cumberland Falls should reclassify the expenses recorded in Account No. 926 - Employee Benefits into the applicable labor accounts in the future, as stated previously. This reclassification would provide a more accurate picture of the applicable labor accounts.

Due to the limited scope of the audit, the staff did not attempt to determine the accuracy of Cumberland Falls's plant in service and did not verify test-year depreciation expense. However, the aforementioned items which were capitalized and depreciated or amortized, should be reclassified on Cumberland Falls's books.



Angela Schweickart
Public Utilities Financial Analyst
Senior
Public Service Commission
Division of Rates and Tariffs
Revenue Requirements Section