

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

IN RE: Proposed Revisions to)
Rules 25-30.020, 25-30.025,)
25-30.030, 25-30.032, 25-30.033,)
25-30.034, 25-30.035, 25-30.036,)
25-30.037, 25-30.060, 25-30.110,)
25-30.111, 25-30.135, 25-30.255,)
25-30.320, 25-30.335, 25-30.360,)
25-30.430, 25-30.436, 25-30.437,)
25-30.443, 25-30.455, 25-30.515,)
25-30.565, NEW RULES 25-22.0407,)
25-30.0408, 25-30.0371,)
25-30.038, 25-30.039, 25-30.090,)
25-30.117, 25-30.432 to)
25-30.435, 25-30.4385, 25-30.4415,)
25-30.456, 25-30.460, 25-30.465,)
25-30.470, AND 25-30.475; AND)
REPEAL OF RULE 25-30.441, F.A.C.)
PERTAINING TO WATER AND)
WASTEWATER REGULATION.)

DOCKET NO. 911082-WS

VOLUME V

Pages 455 through 614

PROCEEDINGS:

HEARING

BEFORE:

CHAIRMAN J. TERRY DEASON
COMMISSIONER THOMAS M. BEARD
COMMISSIONER SUSAN F. CLARK
COMMISSIONER LUIS J. LAUREDO
COMMISSIONER JULIA L. JOHNSON

DATE:

Wednesday, May 26, 1993

TIME:

Commenced at 9:30 a.m.
Concluded at 1:20 p.m.

PLACE:

101 East Gaines Street
Tallahassee, Florida

REPORTED BY:

JANE FAUROT
Notary Public in and for the
State of Florida at Large

ACCURATE STENOGRAPHY REPORTERS, INC.
100 SALEM COURT
TALLAHASSEE, FLORIDA 32301
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1 ALSO PRESENT:

2 CHARLES H. HILL, Director, Division of Water and
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4 BILL LOWE, FPSC Division of Water and Wastewater.

5 BILLIE B. MESSER, FPSC Division of Water and
6 Wastewater.

7 PATRICIA W. MERCHANT, FPSC Division of Water and
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16 Wastewater.

17 PATRICK MAHONEY, FPSC Division of Research &
18 Regulatory Review.

19 ROBERT P. TODD.
20
21
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23
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P R O C E E D I N G S

1
2 COMMISSIONER DEASON: Perhaps now is a good time
3 to discuss scheduling a little bit. There has been
4 some concern expressed that there are three
5 Commissioners that are going to have to be leaving
6 going to a hearing in Fort Myers this afternoon.
7 There are a number of Staff persons here at the
8 Commission who will be attending that hearing. And I
9 understand there is some Staff personnel in Public
10 Counsel's Office who will need to be making travel
11 arrangements to be in attendance at that hearing, also.

12 And there has been some discussion that if we
13 could conclude today's proceedings at a reasonable hour
14 somewhere, it has been suggested noon or 1:00 p.m. My
15 original plans were to try to stop today around 3:00
16 p.m. I have no objection to having a target completion
17 time for today's proceedings somewhere around noon or
18 1:00 p.m. My only concern is that we have set aside --
19 we have been fortunate enough to find three days
20 consecutively in July to conclude these hearings, and
21 that was a minor miracle in and of itself. And we are
22 going to have to conclude the hearings in July. Beyond
23 that it gets more and more difficult. And I think we
24 all would agree that it's time to bring these rules to
25 a closure. So my only request is that the parties keep

1 in mind that we don't have an unlimited supply of time
2 and days to get this concluded, that if we conclude
3 early today we are just going to have to buckle down
4 that much more in the July proceedings. So as long as
5 everyone understands that.

6 I have had a request this morning that after we
7 conclude our discussion of Rule .037, that we go
8 immediately into Rule .433. This would accommodate
9 some out-of-town personnel, and I think that's a
10 reasonable request if there is no objection. And I
11 also had a request that it may be helpful if we could
12 identify those rules, if there are any, and I hope
13 there are, those rules that are essentially
14 noncontroversial or may be just minor comments that we
15 could go ahead and maybe identify those and get those
16 concluded today and get those out of the way, so we
17 could focus on the rules in the July hearing. And that
18 may expedite things. So, just kind of keep those things
19 in mind.

20 Our first order of business today, though, is to
21 conclude Rule .037, and I think that Ms. Dismukes had
22 some final comments in regard to that rule, is that
23 correct?

24 MS. DISMUKES: Yes. Thank you.

25 OPC has proposed a few changes to Subsection

1 (2)(c) of the proposed rule. And, basically, our
2 addition is to require that the utility provide a
3 description of the nature and identity of all parent
4 companies, affiliated companies, and related parties.
5 And, basically, our reasoning is pretty much the same
6 as it was when we discussed this same addition under
7 other certification issues.

8 COMMISSIONER LAUREDO: What was it again? What
9 section? It was too fast. What section?

10 MS. DISMUKES: It's Section (2)(c). In addition,
11 as Florida Waterworks Association brought up yesterday,
12 we added what they're characterizing as clarifications
13 to Subsection (g), which is that the contract for sale
14 shall also include any auxiliary or supplemental
15 agreements. In Florida Waterworks' comments concerning
16 our proposal, they indicated some disagreement with
17 Subsections (1), (2), and (3) of (g), which is where we
18 have proposed that the utility also provide some
19 additional information. And as I understand their
20 concern, it is that that information may not be
21 contained in the agreements that we requested that the
22 utility provide when they filed this application. So
23 compared to what we have in our comments, I would just
24 like to say that we would change it to say, "In
25 addition, the utility shall provide, where applicable,

1 the following." And that is basically the purchased
2 price and terms of payment which was already part of
3 the rule as proposed by Staff.

4 And then our two additions are the dollar amount
5 of the assets purchased. Staff had originally had a
6 list of the assets purchased, and we have just added
7 that the dollar amount should also be included. And,
8 in addition, we would like to know the assets of any
9 nonregulated operations or entities.

10 To that we have also added a Subsection (3), which
11 asks that the utility provide a description of all
12 consideration between the parties, including promised
13 salaries, retainer fees, stock, stock options,
14 assumptions of obligations, et cetera. And, basically,
15 all we are asking is if there are any kind of side
16 deals which were not a function of the agreement, we
17 would like to know about that. If the utility doesn't
18 have it in the agreement, they can provide it as a
19 separate list or a separate item. The only party that
20 commented on that was Florida Cities. If they don't
21 dispute providing this information, then I don't think
22 there is any disagreement between us and Florida Cities
23 or Florida Waterworks Association.

24 We have also proposed a modification to Subsection
25 (2)(k), which is basically the same thing as Subsection

1 (c), which is to include any auxiliary or supplemental
2 agreement. And then, finally, the same change we
3 propose to Subsection (3)(g). And those are basically
4 our suggested changes to the proposed rules.

5 CHAIRMAN DEASON: What do you mean by " auxiliary"
6 and "supplemental agreements"? These are things that
7 are not part of the contract but are part of the
8 transaction?

9 MS. DISMUKES: To be honest with you, I don't know
10 whether or not a situation exists where there is more
11 than one contract. It's just basically if there are
12 additional contracts, we would like to have them file
13 those as well.

14 COMMISSIONER LAUREDO: Just about anything, but we
15 don't want their birth certificates and their
16 citizenship application. My God, I would hate to get
17 into this business.

18 MS. DISMUKES: I was just going to say, I mean, if
19 there are any agreements outside the actual purchase
20 agreement, and it has to do with the transfer, I think
21 that it would be important for all parties to have that
22 at the time they file the application.

23 COMMISSIONER LAUREDO: If it has to do with the
24 transfer?

25 MS. DISMUKES: Correct.

1 COMMISSIONER LAUREDO: But in any agreement
2 between entities that may be parties, may be purchasers
3 but has nothing to do with it -- I mean, there has got
4 to be a stop to how much you want to know about
5 relationships between parties, investors. I was going
6 to ask you why do we need financial statements for --
7 although nobody has objected to it -- for people
8 providing funding?

9 While on (k), all entities -- I hope I'm in the
10 right place, Page 32. And this is not your suggestion,
11 so I shouldn't ask you. People providing funding and
12 financing, they want financial statements and copies.
13 Why would you want a financial statement? If I come up
14 and put up a million dollars, why would you want my
15 financial statements? There must be a logic to wanting
16 all of this stuff.

17 COMMISSIONER BEARD: Commissioner, I think I can
18 remember one specific case where it was a territorial
19 dispute and the owner of the company was proposing that
20 he had the financial ability to serve the area, as an
21 example, and he literally was talking about his home,
22 and this, that, and the other, and it really became
23 pretty ludicrous. And I think the point is that you're
24 looking to see that this entity, whoever it is that
25 proposes to own this, has the financial ability and

1 stability to provide service in the future as opposed
2 to having somebody that is coming in that is on the
3 verge of Chapter 11 trying to buy a water and
4 wastewater.

5 COMMISSIONER LAUREDO: Yes, but this is the people
6 providing the funding to the buyer, not the buyer.
7 This is the backers of the buyer. That's why I was
8 wondering. Let's say a bank or --

9 COMMISSIONER BEARD: I think that's part of it.

10 COMMISSIONER CLARK: Wouldn't you want that if you
11 are relying on their ability to, in fact, provide the
12 funds? Don't you need to know that they have the
13 ability to provide the funds they say they are going to
14 provide to the buyer?

15 COMMISSIONER DEASON: Well, I think the rule would
16 only apply to people who have a 10 percent or greater
17 ownership share, is that correct? It's not like the
18 owner goes to the bank and we are asking a financial
19 statement of the bank. If the bank has a 10 percent
20 ownership share, then we are asking for the bank's
21 financial statement.

22 MR. CRESSE: That was the clarification that I was
23 going to ask about. Exactly what that means is
24 25.303(7)(k), it says, "A list of all entities which
25 have provided or will provide funding to the buyer and

1 an explanation of manner and amount of such funding,
2 which shall include their financial statements and
3 copies of any financial agreements with the utility."
4 Now that seems to me to say if Sun Bank is lending the
5 buyer \$500,000, you have got to provide Sun Bank's
6 financial statements.

7 COMMISSIONER BEARD: Would that be in the form of
8 their annual report?

9 MR. CRESSE: Yes, I guess that would be
10 satisfactory.

11 COMMISSIONER LAUREDO: But it doesn't make sense.

12 CHAIRMAN DEASON: But the next sentence, I think,
13 clarifies that. Or if it doesn't clarify that, I think
14 we need to get it clarified.

15 COMMISSIONER LAUREDO: I'm glad you brought that
16 up, because that was my next question.

17 MR. CRESSE: That's the clarification that I'm
18 seeking. Now, if the next sentence excludes the
19 lender, which says, "This requirement shall not apply
20 to any person or entity holding less than 10 percent
21 ownership interest in the utility," if that's only
22 people that are providing equity --

23 COMMISSIONER LAUREDO: Yes, but that qualifies the
24 buyer. It doesn't qualify the lender. See, that
25 sentence is very confusing. This requirement shall not

1 apply to any person, and let's just say the five of us
2 get together and buy a utility. And I have a 5 percent
3 equity; less than 10 percent, or 8 percent, and all the
4 other partners have more than 10. I have to show all
5 of my financial -- I don't have to show all of my
6 financial backers, you all do. That's what that
7 sentence says to me. So, anybody that backs in any way
8 anybody who has a 10 percent or more equity has to
9 disclose their financial statements. That is the
10 backers, not the buyers or the equityholders. I think
11 it's impractical, and I don't know where it would lead
12 you.

13 COMMISSIONER BEARD: What you could invite -- and
14 I'm no expert in this. You could invite Tom Beard of
15 ABC Company that has 5 percent, and it's a shell. Tom
16 Beard of DEF Company who has 5 percent and it's a
17 shell. And I can build my way up to 20 percent equity,
18 as an example, some way that way and then the rest is
19 debt. I'm just thinking out loud.

20 COMMISSIONER CLARK: Well, if you read the rule, I
21 think the sentence makes it clear, that you don't get
22 it from a bank because that bank is not providing --

23 CHAIRMAN DEASON: Maybe we can get some
24 clarification from Staff. What is the purpose or the
25 intent?

1 MS. CHASE: Commissioners, the purpose of the
2 change was just that, that if they have more than a 10
3 percent ownership, that we do expect to see their
4 financial backing. This same language was put in in
5 .033, which was discussed yesterday. The whole idea is
6 that this could very well be a brand new utility. You
7 know, someone brand new purchasing a utility, and we
8 would look at them the same way we would look at an
9 original certificate. Do they have the financial
10 backing and the financial wherewithal to operate the
11 utility? And Commissioner Beard's point was exactly
12 what this is getting to, that if they have an
13 individual or something that's signing an agreement
14 that they are going to provide \$100,000 backing, we
15 want to know that that person really does have that
16 money readily available where they could provide it.

17 COMMISSIONER CLARK: Well, suppose that person
18 says they are going to provide \$100,000, and it's going
19 to be through a loan from a bank. Does the bank have
20 to provide their statement?

21 MS. CHASE: No, that's not at all the intent of
22 this.

23 COMMISSIONER LAUREDO: Where did you read that?

24 COMMISSIONER CLARK: Because it doesn't apply to
25 any person or entity holding less than a 10 percent

1 ownership; the bank does not have any --

2 COMMISSIONER LAUREDO: No, but, again, we are
3 getting confused. That's qualifying the buyer; it's
4 not qualifying the backer of the buyer. If the equity
5 holder --

6 COMMISSIONER CLARK: Fead it again.

7 COMMISSIONER LAUREDO: My example is if I have 8
8 percent, if I have 8 percent of this new equity group
9 moving in, and I say in the application I am pledging
10 \$100,000 of working capital for this thing, I do not
11 have to turn --

12 COMMISSIONER CLARK: I agree with that.

13 COMMISSIONER LAUREDO: Right. But everybody else
14 who has more than 10 percent has to disclose the
15 financial statements, not of themselves, but of
16 everybody who is lending them money.

17 COMMISSIONER CLARK: Not unless those people
18 have --

19 MR. HOFFMAN: Commissioners, one problem that I
20 see with it that goes along with this line of
21 discussion is if you read that sentence, where it says
22 "This requirement shall not apply to any person or
23 entity holding less than 10 percent ownership," it does
24 seem that the bank, the Sun Bank, in Mr. Cresse's
25 example is excluded. But then if you read on it says,

1 "Unless the bank is also providing other funding," for
2 instance, other than funding to secure an ownership
3 interest to the utility. So if you continue the
4 example, Sun Bank has a \$10,000 line of credit to the
5 utility, they just got thrown into this requirement.

6 CHAIRMAN DEASON: If we were to put a period after
7 the word "utility" on Line 2, would that solve the
8 problem?

9 COMMISSIONER LAUREDO: What after Line 2?

10 CHAIRMAN DEASON: Just strike everything after
11 that.

12 MR. HOFFMAN: Strike beginning with the word
13 "unless" and then thereafter?

14 CHAIRMAN DEASON: Yes.

15 MR. HOFFMAN: Yes, I think that would solve that
16 issue.

17 COMMISSIONER CLARK: Well, do we want to make an
18 exception for savings and loans? If the federal
19 government isn't going to be careful, maybe we need to
20 be.

21 CHAIRMAN DEASON: I think that we are getting into
22 a very slippery slope there, if we try to put
23 additional requirements on a savings and loan versus a
24 bank.

25 MS. CHASE: Commissioners, this language was put

1 in to address Mr. Cresse's concern that he raised. We
2 wouldn't have any problem with a period after
3 "utility," like he said. I would suggest we make the
4 same change, though, back in 25-30.033, where we
5 tracked this language exactly.

6 COMMISSIONER CLARK: Who were you intending to get
7 at when you say, "Unless that person or entity is also
8 providing other funding," other than funding to secure
9 an ownership interest to the utility?

10 MS. CHASE: Honestly, Commissioner, I don't know.
11 This came out of one of the workshops. We were trying
12 to address that problem. I think the language just
13 doesn't do it.

14 COMMISSIONER CLARK: But if you put a period, it
15 will.

16 MS. CHASE: Yes.

17 MS. DISMUKES: You could have a situation -- I
18 think we have one in a small water and sewer case where
19 a brother or something had loaned the money to finance
20 the utility, where you might want to be concerned about
21 his financial wherewithal, as well. I know that gets
22 into Commissioner Lauredo's concern, but that did
23 happen with Jasmine Lakes.

24 CHAIRMAN DEASON: But don't you think that that
25 would show up on the person -- the person that borrowed

1 the money from the brother, that would show up on their
2 financial statement as a note payable to the brother,
3 that may raise a question.

4 MS. DISMUKES: Right. You can always approach it
5 on a case-by-case basis as opposed to requiring it in
6 the application. I was just giving an example that
7 came to mind.

8 MS. CHASE: Commissioner, let me just point out, I
9 think that's true. And if you look at the one above it
10 in (j), that's where they have to provide a statement
11 or, you know, show their financial ability. And that's
12 where we can address those on a case-by-case basis. It
13 gets to whether we approve the application or not, and
14 if they are not willing to provide something that's
15 questionable, then the answer would be, you know, they
16 have to maybe be denied. So we can get at those kind
17 of case-by-case bases in (j).

18 COMMISSIONER BEARD: Let me ask you a question
19 about the word "ownership" here. The "We Five Company"
20 that Commissioner Lauredo was describing, we each put
21 up 5 percent equity. Now, you've got 25 percent of the
22 money. We go to Sun Bank, we borrow the other 75
23 percent of the money. Okay. 75 percent debt, 25
24 percent equity. What portion of the ownership do the
25 five us have? Do we have 5 percent each, or do we have

1 20 percent each for the purpose of this rule?

2 MS. CHASE: You would have 20.

3 COMMISSIONER BEARD: Okay. That makes sense to
4 me.

5 MS. CHASE: Sun Bank is just a loan to back it.

6 COMMISSIONER BEARD: Okay.

7 COMMISSIONER LAUREDO: Oh, no, the lender does not
8 take equity by lending you money. I'm just saying it's
9 just going to be funny to see, going up to Sun Bank and
10 telling them that the Public Service Commission, which
11 is fine, I guess, will be able to get their annual
12 report.

13 COMMISSIONER BEARD: That's not what I read here.
14 The point is there would be five people with 20 percent
15 ownership; those five would have to provide their
16 records. Sun Bank, as I read this, has loaned the
17 money to those five owners; they don't need to provide
18 their records. That's the way I understand this.

19 COMMISSIONER LAUREDO: See, I just come with
20 another mentality. I would be a little more worried
21 about their next cash flow. To me, that just means
22 that they have an obligation, that's probably in the
23 scheme of things, more superior. They are going to
24 have to pay Sun Bank. And so if you want to do an
25 analysis of economic viability, I would be more worried

1 about other things. But I can live with it.
2 Semantically, I think, taking that out helps at least
3 to -- but there are people out there. I want you to
4 know that part of the reason I bring this up, besides
5 the fact that I have a great fear of the constant
6 incremental but steady intrusion of government into
7 everybody's lives, generally. It is also talking about
8 disincentives. There are a lot of private capital
9 people, venture capital people, who would be
10 discouraged by this kind of rule.

11 CHAIRMAN DEASON: And that may be good,
12 Commissioner, because we only want those people in the
13 utility business who are forthright and want to make
14 all of their records available, and realize the burden
15 that they are placing on themselves and the public
16 trust that they are taking upon themselves to be a
17 public utility. We are not talking about requirements
18 of people who are in some type of private business.
19 It's a totally different situation when somebody is
20 coming in and offering themselves to become owners of a
21 public utility.

22 COMMISSIONER LAUREDO: But, again, here is where
23 our confusion is. I'm talking about the lender.

24 CHAIRMAN DEASON: There is no requirement --

25 COMMISSIONER LAUREDO: I'm talking about the guy

1 who is willing to back me from California, who is a
2 venture capitalist, who says, "I'm going to fund your
3 investment in this thing, Mr. Lauredo. I am John
4 Smith, venture capitalist." And it shouldn't imply
5 that just because he doesn't want to disclose this
6 stuff, he is less ethical than myself or anybody else.
7 I think that is the wrong conclusion. But for a lot of
8 other competitive reasons, economic and business
9 reasons, a lot of people don't like to have their tax
10 returns on the record, particularly public records.
11 And it doesn't mean that they are dishonest. Why do we
12 need to draw that conclusion? There are a lot of other
13 reasons. It may not be applicable. It's just that
14 it's one of those things. Philosophically, I have a
15 problem, but I know a lot of reputable established
16 venture capital people would stay away from this kind
17 of investment. I guarantee you, because I know some of
18 them, you know. And, by the way, they're risking their
19 capital. That is the ultimate commitment to making
20 this work, that there is no recourse to them. They put
21 up the capital through me, the 10 percent owner. I'm
22 liable to them for that money, and they just, you know,
23 it has a chilling effect.

24 CHAIRMAN DEASON: If that is the case, that
25 venture capitalist has no requirement under this rule,

1 because we're going to -- this rule would look at you
2 and your financial statements. And the only question
3 would come up, if you're relying upon some venture
4 capitalist for your financial stability, well, then
5 that may raise a question later on. But there is no
6 requirement up front that that venture capitalist has
7 got to provide his or her --

8 COMMISSIONER LAUREDO: Sure, if he provides
9 funding. If he has provided or will provide funding,
10 money.

11 COMMISSIONER CLARK: But then it says it doesn't
12 apply to anyone who doesn't also take an equity
13 ownership along with providing that funding.

14 CHAIRMAN DEASON: That is the second sentence.
15 Staff, correct me if I'm misinterpreting this.

16 COMMISSIONER LAUREDO: I don't agree with that,
17 Commissioner Clark.

18 MS. CHASE: No, Commissioner, that's correct.

19 CHAIRMAN DEASON: That is the intent?

20 MS. CHASE: Yes.

21 CHAIRMAN DEASON: We are only getting financial
22 statements and financial information on those entities
23 which have a 10 percent or greater ownership share in
24 the utility.

25 MS. CHASE: That is true.

1 COMMISSIONER LAUREDO: Okay. Now, so in this
2 case, so that it's clear and it's a simple example,
3 that I do have a backer for my investment, and my
4 investment is 8 percent -- I will take it back. I
5 could have a 50 percent. If I have a 50 percent share
6 of this new investment, and my financial backer is XYZ
7 Venture Capital, who has no equity in the enterprise.
8 He is a lender to Luis Lauredo. He does not have to
9 disclose his financial statement?

10 MS. CHASE: That is correct.

11 COMMISSIONER LAUREDO: Oh.

12 CHAIRMAN DEASON: Now, what you have to realize,
13 though, is when Staff makes their review, and they look
14 -- and maybe we ought not to use you as an example --
15 but someone else, an individual who is, basically,
16 being supported by a venture capitalist, and that is
17 the only source of income or financial support they
18 have, Staff may question that, and say, "Look, you have
19 met the requirements, but we have substantial doubt
20 about this individual. Unless you come forth with more
21 information, we have no alternative but to deny the
22 application, because we are not convinced that there is
23 the necessary financial viability and support to
24 support the utility."

25 COMMISSIONER BEARD: But that has nothing to do

1 with venture capitalist. If I borrow X number of
2 dollars, and I use those dollars to buy into the
3 utility, the question becomes do I have the ability,
4 the financial stability to meet my debts, to continue
5 to do that? And that's -- there is a loan agreement
6 that says I have got to pay \$350 a month for 36 months
7 to pay that off. Now, the question is, can I, as the
8 owner, pay that off? Not have they got more money to
9 lend me. I have just got a note out there, a note
10 payable I've got to deal with. It has nothing to do
11 with the lender. It has to do with me, the owner.

12 CHAIRMAN DEASON: Well, I agree with that, but we
13 had the example of -- like some type of a sweetheart
14 loan from a brother to a brother type thing. And I
15 think if there is some question about that, I think
16 that we could -- Staff would have the authority, or the
17 Commission would have the authority to ask further
18 questions that, perhaps, goes beyond the rule. But I
19 think the way the rule is written now is sufficient,
20 and that we would get the necessary information that we
21 would need to make an informed decision. And only in
22 that very limited situation where we would need
23 additional information to assure ourselves would that
24 be necessary. And I think that's probably going to be
25 on a very limited basis. Now, I don't know what

1 Staff's intent is. I think that is the way I read the
2 rule.

3 MS. CHASE: That is right, Commissioner. And when
4 we would use this, often it would not be so such if
5 they had gone out and actually borrowed money to use;
6 it would be if they are going to, like, on an ongoing
7 basis, if I need any additional capital, I'm going to
8 be getting it from my brother-in-law, or whatever it
9 is. That's where we would be concerned. "Well, will
10 he be able to provide that on an on-going basis?" It
11 is not so much for a loan agreement, per se; it's for
12 when they have said they are going to be using this
13 source. If they don't have it themselves and they are
14 going to be relying on some other source on an ongoing
15 basis, that is where we would look at that.

16 COMMISSIONER LAUREDO: Well, we struck that last
17 sentence out. After the period, you suggested?

18 CHAIRMAN DEASON: Right. And without objection --
19 Yes?

20 MR. SHREVE: Mr. Chairman, off of this subject,
21 but back to one of Commissioner Lauredo's earlier
22 questions about nonrelated information that was coming
23 in here, I wonder if I could just mention one of the
24 reasons that we would need that. Although it appears
25 that some of the deals or some of the agreements might

1 appear to be unrelated to a specific transaction, if
2 you take, for instance, when Southern States purchased
3 from Deltona there was an original agreement. But then
4 in addition to that, there was what would appear to be
5 an unrelated agreement in the settlement of a lawsuit
6 between Deltona, and where Southern States actually
7 took over some responsibility from Deltona for
8 furnishing some service that was really a developer's
9 responsibility. We want to know if there is any
10 influence in there anywhere?

11 We've actually had a situation, not concerning
12 Southern States, but where there were either three or
13 four deals made at the same time, which would appear to
14 be separate transactions, some of them out of the State
15 of Florida. But when the company made the deal, it
16 placed an undue burden or a bigger portion of the
17 burden on the Citizens of the State of Florida, while
18 giving a break to an unrelated transaction
19 out-of-state. So, there are some that would appear to
20 be unrelated.

21 COMMISSIONER LAUREDO: But the document related to
22 the actual purchase is not the totality or the
23 reflection of either the, quote, "purchased price or
24 the obligations arising," because there are other --
25 well, that helps explain. And that has happened?

1 MR. SHREVE: Yes, sir, it has.

2 COMMISSIONER LAUREDO: I've got it.

3 MR. SHREVE: That's right.

4 COMMISSIONER LAUREDO: I got it. Good point.

5 CHAIRMAN DEASON: Okay. Rule 25-30.037, I think
6 we have already discussed a few things yesterday.

7 MR. SEIDMAN: Commissioner, could I just reiterate
8 one thing. With regard to .037(2)(c), with regard to
9 description of nature and identity of all parent
10 companies and affiliated companies, we addressed that
11 under 25-30.033(1)(c) yesterday, and our comments are
12 the same on that. And I think you gave direction to
13 the Staff with regard to wording on that.

14 COMMISSIONER CLARK: "Where applicable," is what
15 we are talking about, "where applicable"?

16 CHAIRMAN DEASON: This is in relation to
17 affiliated entities?

18 MR. SEIDMAN: Right, that it had to do with the
19 utility.

20 COMMISSIONER LAUREDO: You're talking about Page
21 31, is that where you're at? (2)(c)?

22 MR. SEIDMAN: Page 31.

23 COMMISSIONER LAUREDO: Let me make sure we are on
24 the same page, "The nature of the buyer's business
25 organization," i.e. --

1 MR. SEIDMAN: Right.

2 COMMISSIONER LAUREDO: All that calls for is a
3 statement that says XYZ is a corporation or XYZ is a
4 partner.

5 MR. SEIDMAN: Well, it asks for a description and
6 identity, and we took issue with that because of the
7 burdensomeness and the irrelevancy of listing hundreds
8 of entities. And you addressed that yesterday already.
9 And all I'm saying is those remarks that were discussed
10 yesterday should carry over to this, because it's the
11 same phrasing.

12 CHAIRMAN DEASON: Yes. And as I recall, the
13 Commission addressed that and decided that there would
14 not be a requirement to list every affiliated entity,
15 unless there was a need to show support from those
16 affiliated entities to prove financial viability, and
17 that burden would be on the person requesting the
18 transfer.

19 MR. SEIDMAN: That's correct. We just want to
20 make sure that the same thing carries through. Thank
21 you.

22 CHAIRMAN DEASON: Am I interpreting that
23 correctly?

24 MS. CHASE: Yes.

25 CHAIRMAN DEASON: Okay.

1 MS. MOORE: The change you just made in .037,
2 striking the last sentence, also needs to be made in
3 .033.

4 CHAIRMAN DEASON: I think we determined that we
5 should do that, without objection. There was a
6 discussion concerning arrangement of proving land
7 ownership, other than with a warranty deed. You were
8 going to incorporate that language into this rule as
9 well as we discussed yesterday, is that correct?

10 And then, Ms. Chase, you made a recommended change
11 to Paragraph (2)(m), and we determined that that needed
12 to be determined in conjunction with our ultimate
13 disposition of Rule .0371.

14 MS. CHASE: That's correct.

15 CHAIRMAN DEASON: And so, really, the only matters
16 that are left to decide at this point would be the
17 additional language suggested by Public Counsel for
18 (2)(g) and for 2(k), is that correct?

19 MS. CHASE: That's correct.

20 CHAIRMAN DEASON: Commissioners, what is your
21 pleasure?

22 COMMISSIONER CLARK: I move the rule with those
23 amendments.

24 CHAIRMAN DEASON: Do I have a second?

25 COMMISSIONER LAUREDO: Whenever we move this,

1 again, to make sure, we are just kind of moving on what
2 I call first reading?

3 CHAIRMAN DEASON: The first reading. It will be
4 incorporated into the final proposal as we suggested
5 here, but we are free to reconsider any of that and
6 change or modify in the final vote, which now appears
7 to be in September.

8 COMMISSIONER LAUREDO: Okay.

9 CHAIRMAN DEASON: Without objection? Hearing
10 none. Staff has sufficient direction then for Rule
11 .037.

12 MR. ARMSTRONG: Mr. Chairman, if I may, just a
13 couple of quick comments on Southern States' position
14 as on the record. We don't have any problem whatsoever
15 with contracts, auxiliary agreements, anything related
16 to the purchase. We have no problem with that. We
17 also have no problem with providing the information
18 about the financial backing of the owner. Obviously,
19 we are wholly-owned by Minnesota Power, which is a
20 publicly traded company. And we concede to filing
21 annual reports every time we file an acquisition, if
22 that's -- I think that would be acceptable, and I just
23 wanted confirmation that that would be acceptable. Is
24 that the kind of information you need from a company
25 like Southern States?

1 MS. CHASE: I'm sorry, what?

2 MR. ARMSTRONG: What we would like to do in terms
3 of the financial backing of the owner -- obviously, we
4 are wholly-owned by Minnesota Power, which is a
5 publicly traded company, and what we saw when we read
6 this is fine. You know, we will hand you down your
7 report, and 10-Qs, but we just want to make sure that's
8 okay.

9 MS. CHASE: That will be fine.

10 MR. ARMSTRONG: Thank you.

11 CHAIRMAN DEASON: Before we move on to Rule .433,
12 which has been requested to be taken out of order, do
13 any of the parties know of noncontroversial rules that
14 we can go ahead and consider at this time, or do you
15 want -- perhaps you just need to be thinking about
16 that, and we can take care of that before the day is
17 over. Whatever your pleasure is.

18 Mr. Scheifelbein?

19 MR. SCHIEFELBEIN: Our pleasure is your pleasure,
20 Mr. Chairman. We were prepared to do that right now.
21 I don't know if the other parties are.

22 CHAIRMAN DEASON: Why don't you go ahead and
23 identify those, and perhaps the parties can take a look
24 at those and inform us whether there is any
25 controversy.

1 MR. SCHIEFELBEIN: According to my notes,
2 25-30.060, which deals with exemptions, the only
3 comments that have been filed on that are by Staff, and
4 we have no controversy with it. And we are not aware
5 of anyone else. 25-30.090, abandonments. Again, the
6 only comments are Staff's. We have no problem with the
7 rule as proposed and are not aware of anyone else's.
8 25-30.111, exemptions for resale, same thing;
9 25-30.135, tariffs, rules and miscellaneous; 25-30.320,
10 refusal and discontinuance of service; 25-30.335,
11 customer bills; 25-30.360, refunds; 25-30.430, test
12 year approval.

13 COMMISSIONER LAUREDO: How about .433? Nevermind,
14 nevermind.

15 MR. SCHIEFELBEIN: One or two small items on that,
16 Commissioner. Things go downhill from there. I don't
17 believe there is any controversy among the parties on
18 25-30.437, rate structure. 25-30.4385, additional
19 information, which, I believe, relates strictly to
20 proposed tariff sheets. 25-30.441, which is repeal,
21 and its replacement 25-30.4415, investment required in
22 public interest, 25-30.443, Class C MFRs.

23 MS. MERCHANT: Excuse me. Is that my proposed
24 changes to 25-30.443? They were very minor.

25 CHAIRMAN DEASON: 25-30.433 or --

1 MS. MERCHANT: 25-30.443. They were very minor to
2 piggyback the Class A and B, that is all.

3 MR. SCHIEFELBEIN: Offhand I have no idea.

4 MS. MERCHANT: You might want to check that.

5 COMMISSIONER LAUREDO: Yes, you keep doing that,
6 and I'm working off -- when I say the rule, I'm working
7 off the rules that I have, notwithstanding your
8 testimony as suggested. You're just another party as
9 far as I'm concerned. Is that the way I should be
10 thinking? You're just suggesting a change, just like
11 they would suggest a change?

12 MS. MERCHANT: That's correct.

13 COMMISSIONER LAUREDO: So, all you're really
14 saying is on .443 you may have a suggestion?

15 COMMISSIONER BEARD: She is simply asking that if
16 there is a conflict with her -- she is saying it's not
17 controversial with her changes included.

18 MS. MERCHANT: That's correct. I am asking if he
19 agrees with my proposed changes. They are very -- what
20 do you call it, housekeeping, very minor.

21 COMMISSIONER LAUREDO: I think you're saying just
22 as it reads, not with your suggestion.

23 COMMISSIONER CLARK: Well, if we can cover the
24 suggestions, we can get rid of it altogether.

25 COMMISSIONER LAUREDO: Okay.

1 MR. SCHIEFELBEIN: Sure. And up to now, my
2 comments have been also to imply on those sections the
3 Staff tweaking of those rules is okay, too, and it
4 doesn't seem to have inspired any great debate, also.
5 And that would apply to .443 as well.

6 MS. MOORE: .437, you've already announced, that
7 also has one Staff change, the comments of Mr. Willis.

8 MR. SCHIEFELBEIN: Yes.

9 CHAIRMAN DEASON: He just stated that if he has no
10 controversy with it, he is accepting the suggestions
11 made by Staff.

12 MR. SEIDMAN: That's correct.

13 MR. SCHIEFELBEIN: What my notes are attempting to
14 do is see if there is any controversy anywhere. I see
15 if we are happy, but other people aren't.

16 COMMISSIONER LAUREDO: And when you say "we," it's
17 the Florida Association?.

18 MR. SCHIEFELBEIN: Yes, sir. 25-30.460,
19 miscellaneous service charges; 25-30.470, rate case
20 expense amortization. We hate the rule, but we need a
21 statutory change. So, we won't waste your time.
22 25-30.475, effective dates. And that's it.

23 CHAIRMAN DEASON: Well, you're to be commended.

24 COMMISSIONER LAUREDO: Yes.

25 CHAIRMAN DEASON: I think we're -- assuming what

1 the other parties have to say, this is refreshing news.

2 COMMISSIONER LAUREDO: Just don't give them a
3 chance to say anything.

4 MR. SCHIEFELBEIN: I probably should leave now.

5 COMMISSIONER CLARK: Ken's getting nervous.

6 CHAIRMAN DEASON: Mr. Hoffman, do you need
7 additional time to evaluate these or can you express
8 your position on these so-called noncontroversial
9 rules?

10 MR. HOFFMAN: Mr. Chairman, I think we need a
11 little time to evaluate. Let me just kind of tell you
12 where I think Southern States is at, at this point. I
13 know that we will be presenting comments on the used
14 and useful proposals which are in .432. We'll also be
15 presenting some comments on .433, .434 and .436. Now,
16 apart from that, if we have some time to go back and
17 doublecheck, we may be just fine at this point. We
18 also have some comments from Mr. Cresse on some new
19 proposals by the Office of Public Counsel which address
20 tax loss carryforwards and the treatment of non-utility
21 investments. But those proposals are not part of your
22 rulemaking. Those are something new that Public
23 Counsel has suggested.

24 CHAIRMAN DEASON: Okay. Very well.

25 MR. HOFFMAN: So, at this point, we're at .432,

1 .433 and .434 and .436 and a couple of Public Counsel's
2 suggestions.

3 COMMISSIONER LAUREDO: Well, how did you answer
4 the Chairman's question? I'm sorry, I know you -- are
5 you going to take a few minutes during a break or
6 something and tell us?

7 CHAIRMAN DEASON: He is not aware of any
8 controversy on those rules that Mr. Scheifelbein just
9 identified, but he is requesting an opportunity to make
10 a quick review to confirm that.

11 MR. HOFFMAN: Yes.

12 CHAIRMAN DEASON: Mr. Mann?

13 MR. MANN: Yes, Mr. Chairman. We know for certain
14 that the following we have no controversy and agree
15 with those included in the list of Mr. Scheifelbein,
16 and that is 30.090, .111, .135, .320, .335, and .460.
17 The others, I think there is a good chance that there
18 really is no controversy or very little, perhaps a
19 question or two, or a clarification or two. And we can
20 do the same as Mr. Hoffman, take our first opportunity
21 and go over that list and see if we can increase the
22 list of agreed upon noncontroversial issues.

23 CHAIRMAN DEASON: Okay. That sounds fine. I will
24 just ask the parties perhaps to do that today, so when
25 we conclude the hearing today we will know which of

1 these noncontroversial rules we can dispose of, and we
2 won't have to worry about come July.

3 I believe we're prepared now to address Rule .433.
4 Staff?

5 MS. MERCHANT: Commissioners, Rule .433 deals with
6 rate case proceedings, and there are several sections
7 in this rule that deal with policies. The majority of
8 them are already established Commission policies that
9 we are codifying into rule. And there are several
10 people that are going to address the different
11 sections. So the first one is quality of service, and
12 Mr. Hill will address that for us.

13 MR. HILL: Quality of service merely codifies
14 current Commission practice. We, for many years, had
15 no real standards. We have, over the past four and
16 five years, developed standards. We bring them up in
17 every rate case, and we are just trying to codify
18 current Commission practice.

19 MR. SCHIEFELBEIN: The Florida Waterworks
20 Association does not oppose the rule as written. We
21 agree that it codifies existing policy, long-standing
22 policy. We do take issue with the Public Counsel
23 suggestions on this rule, which indicates that a fine
24 will be imposed if any if the standards are not met.
25 We think that your authority to fine a utility is

1 unquestioned, but we don't think that you need to tie
2 your hands with language that would require a penalty.

3 CHAIRMAN DEASON: Mr. Hoffman?

4 MR. HOFFMAN: We don't have any comments on this
5 section.

6 CHAIRMAN DEASON: Mr. Mann?

7 MR. MANN: Ms. Dismukes will be addressing our
8 comments on these sections.

9 CHAIRMAN DEASON: Right now, I take it we are just
10 addressing Paragraph 1 of .433?

11 COMMISSIONER CLARK: Why don't we do the whole
12 thing?

13 MS. MERCHANT: I think it's simpler to go
14 section-by-section, because each one may be
15 controversial -- some of them are controversial; some
16 of them are not. If we go that way.

17 COMMISSIONER LAUREDO: So, let me -- Southern
18 States not commenting means that they don't have any
19 problem with it?

20 MR. HOFFMAN: We support the comments made by the
21 Association. We don't have anything to add to that.

22 COMMISSIONER LAUREDO: Okay.

23 MS. DISMUKES: The Florida Waterworks Association
24 is somewhat correct in that we propose that if a
25 utility does not meet any one of the Commission

1 standards that an appropriate penalty be imposed. This
2 is -- my understanding is that it's the current
3 Commission practice that they do impose penalties, not
4 perhaps on a routine basis, but they do impose
5 penalties when the utility does not meet the quality of
6 service standards. We are not proposing that it be a
7 fine. It can be any kind of penalty that the
8 Commission wishes to choose that they feel is
9 appropriate. Primarily, our thinking here is that it
10 would provide the utility with an incentive to meet the
11 quality of service standards.

12 COMMISSIONER CLARK: Why do we have to do that? I
13 mean, the law says you can fine for any violation of a
14 rule, order or statute. It's already in the statute.
15 Why would we put it in a rule?

16 MS. DISMUKES: To me it was just a point of
17 clarification that if it was in the rule that the
18 utility would more aptly try and meet the quality of
19 service standards. If it was a new rule where the --
20 Mr. Hill pointed out that you're codifying Commission
21 practice. It's my understanding that the Commission
22 does impose penalties, and so we have just added that
23 to the change that has been proposed by the Staff.
24 Perhaps you were right that if it is in the law, it's
25 not necessary here. It was just, basically, an

1 addition.

2 COMMISSIONER CLARK: To make sure that they knew
3 about it, to remind them?

4 MS. DISMUKES: (Indicating yes.)

5 COMMISSIONER JOHNSON: Are there any other
6 instances in any of the rules where we set out that we
7 can impose a penalty?

8 MR. HILL: No, ma'am.

9 COMMISSIONER JOHNSON: Are there any -- and there
10 are other places in the rule where we could impose a
11 penalty?

12 MR. HILL: Yes, ma'am. And I would guess I would
13 point out that often in the past the Commission, as
14 opposed to a penalty, has ordered the utility to take
15 steps to correct the action. And I guess that is why
16 we wrote it the way we did; that the Commission often
17 does impose a penalty, sometimes a penalty on return on
18 equity. But often it's merely ordering a utility to
19 take certain action to correct the deficiency.

20 COMMISSIONER JOHNSON: And in a way this --
21 language like this might hurt us for purposes of legal
22 argument. If there is one particular section where we
23 state that we can impose a penalty, and then there are
24 other places where we can impose a penalty, but we
25 didn't say that, although it would be an argument where

1 I think we would win, there is an argument that could
2 be made that, "Hey, look, you can't impose a penalty
3 here. Whenever you wanted to impose a penalty, your
4 rule laid that out." I would probably prefer that we
5 didn't -- unless we did it in every instance, I'd
6 prefer that we wouldn't just segregate it out in one
7 instance.

8 CHAIRMAN DEASON: Any objection to Commissioner
9 Johnson's suggestion?

10 COMMISSIONER CLARK: No.

11 CHAIRMAN DEASON: Very well. All right. Next
12 section of the rule.

13 COMMISSIONER CLARK: Before we go on, I have a
14 question on the introductory paragraph. It says, "The
15 following provisions apply, unless for good cause shown
16 they result in an unreasonable burden." I guess my
17 question is are you going to file them unless you show
18 good cause otherwise, or is good cause limited to being
19 an unreasonable burden?

20 MS. MERCHANT: I believe Staff's position would be
21 that you would have to show the burden up front.

22 COMMISSIONER CLARK: I guess my suggestion is that
23 you should say, "Unless the applicant or any intervenor
24 demonstrates that the rules result in an unreasonable
25 burden." I mean, that is your good cause. It's

1 redundant to have --

2 MS. MERCHANT: "Good cause shown," you would take
3 that out?

4 COMMISSIONER CLARK: Take that out.

5 CHAIRMAN DEASON: You would strike the phrase,
6 "for good cause shown"?

7 COMMISSIONER CLARK: Yes.

8 CHAIRMAN DEASON: Any objection to striking the
9 phrase? Very well, strike the phrase.

10 MS. MERCHANT: Are we on to 2?

11 COMMISSIONER LAUREDO: I'm sorry, from line?

12 CHAIRMAN DEASON: This would be on Line 3 and
13 strike the phrase "for good cause shown."

14 COMMISSIONER LAUREDO: Okay.

15 CHAIRMAN DEASON: Paragraph 2.

16 MS. MERCHANT: Commissioners, I would like to
17 combine 2 and 3 together because they relate, and I
18 don't think that we will have any objection from the
19 parties.

20 CHAIRMAN DEASON: Okay.

21 MS. MERCHANT: Section 2 deals with the working
22 capital allowance calculation, and Section 3 deals with
23 debit deferred taxes on income taxes. And then the
24 second part of 3 deals with the debit deferred taxes to
25 be included in addition to working capital. Section 2

1 states that the proposed calculation for working
2 capital would be the formula approach or one-eighth of
3 O&M expenses. We also propose that no allowance for
4 deferred debits be included in addition to that
5 allowance.

6 The current Commission practice -- excuse me, the
7 current rule for filing minimum filing requirements is
8 that the utility use the formula approach with no
9 allowance for deferred debits. And if they use the
10 balance sheet approach, they won't receive recovery of
11 the increased rate case expense in that rate case.

12 The policy that this rule, the current rule is
13 based on was the alternative ratemaking docket where
14 the Commission found that the balance sheet method was
15 the more accurate method, but it was also a lot more
16 expensive for the water and wastewater utilities. And
17 in that order, 21202, the Commission found that the
18 increased benefits for the balance sheet approach did
19 not offset the increased cost.

20 Also, a utility that's losing money most likely is
21 going to show a negative working capital allowance on
22 the balance sheet approach. And in that situation, the
23 Commission would always allow, or in the past the
24 policy of the Commission was to allow a zero working
25 capital allowance. If a utility is in a loss situation

1 you are really -- if you don't -- if you don't give
2 them a return on their working capital allowance, then
3 you could prevent a utility from ever recovering that
4 investment or paying their working capital needs on a
5 timely basis.

6 As far as the allowance, the increased allowance
7 for deferred debits in the working capital, in addition
8 to the formula method, I believe that that's
9 inappropriate. If you get into determining which
10 deferred debits to include in rate base, I think you
11 also have to include any deferred credits, any other
12 deferred credits that might be on the utility's balance
13 sheet at the same time. And once you start deciding
14 which ones should be included, then you're essentially
15 back to the expense incurred by the balance sheet
16 approach. And I think you have offset any of the
17 savings that you chose by using the formula approach.

18 And that concludes my comments on the working
19 capital calculation, but I've also got a proposed
20 correction to the first sentence in Section 3.

21 Section 3 deals with the used and useful -- excuse
22 me. What we were addressing in the first part of
23 Section 3 was that debit deferred taxes associated with
24 CIAC, contributions in aid of construction, should be
25 offset against the credit deferred taxes in the capital

1 structure. I proposed a change to this. This was not
2 in my comments as prefiled. I don't believe any of the
3 parties disagree with the changed wording. And the new
4 proposed wording would read, "Used and useful debit
5 deferred taxes shall be offset against credit deferred"
6 -- excuse me -- "used and useful credit deferred taxes
7 in the capital structure. Any resulting net debit
8 deferred taxes shall be included as a separate line
9 item in the rate base calculation, and the credit would
10 belong into the capital structure." I don't believe
11 that that part is controversial at all. And I just
12 wanted to propose that change. The last line is the
13 section on the other deferred debit in addition to the
14 formula method of working capital.

15 And that concludes my comments.

16 CHAIRMAN DEASON: Thank you.

17 Mr. Schiefelbein?

18 MR. SCHIEFELBEIN: Thank you. Real briefly, you
19 will find behind Tab 7 of Composite Exhibit 1, the
20 comments of the Florida Waterworks Association, which
21 is entirely addressing the treatment, regulatory
22 treatment, of deferred debits. And with yesterday's
23 correction also attached to that by now should be the
24 petition that we have filed with DOAH challenging the
25 rule as initially proposed. Essentially, our position

1 is that the policy represented by the last sentence in
2 Paragraph 3 of .433 is confiscatory and will not give
3 any acknowledgment of investment on a great many items.
4 Ms. Debbie Swain will address this proposal or our
5 position in depth.

6 MS. SWAIN: Good morning, Commissioners. My name
7 is Debbie Swain. I'm representing the Florida
8 Waterworks Association.

9 The Waterworks Association has no objection to the
10 rule as proposed. The comments that I have regarding
11 the method of working capital, of calculating working
12 capital are in response to comments from Public
13 Counsel.

14 The recommendation, as Ms. Merchant described, is
15 that one-eighth O&M or the formula method of working
16 capital be used. And OPC has suggested rather that the
17 balance sheet method be used. Working capital is
18 defined as the amount of investor-supplied cash used to
19 finance operating costs during the time lag before
20 revenues are collected. And another definition, and
21 this is the accounting definition and the one that I am
22 most familiar with, is current assets minus current
23 liabilities. It is that definition that has spawned
24 the concept of using the balance sheet for the
25 calculation of working capital.

1 I would like to go back and give you just a little
2 historical background from my own perspective. I have
3 been filing rate cases for nearly 16 years, and during
4 seven of those years I filed eight rate cases under PSC
5 jurisdiction using the balance sheet method. The time
6 involved in preparing just that section of the minimum
7 filing requirements exceeded any other particular
8 section in the rate case filing. And the reason for
9 that is that in order to determine or measure working
10 capital using the balance sheet, one must go back to
11 the balance sheet and allocate each component to the
12 system being filed for the rate case.

13 And in my own experience, the balance sheet was
14 the balance sheet for the whole company. In one case
15 it was Southern States Utilities and in another case it
16 was Deltona Utilities, where I was employed at the
17 time. And the total company balance sheet included
18 looking at current assets and current liabilities and
19 the cash account for the entire company. That entire
20 company included the water and sewer systems for which
21 I was filing a rate case, as well as nonjurisdictional
22 systems, LP gas, systems that were under jurisdictions
23 of counties, or other systems simply not included in
24 the rate case. And the method of allocation used was
25 different for each small component on the balance

1 sheet. And it became very time-consuming, and it also
2 became very judgmental.

3 The experience that I had is that the balance
4 sheet method is not an exact method. There is a more
5 exact method. It's the lead lag study, and I think all
6 the parties agree that that is far too costly to
7 consider. And no one has brought that up as a
8 possibility. But the balance sheet is not any more
9 exact, in my opinion, than the formula method. And the
10 reason is -- there are three reasons. One is that it
11 measures the working capital that the company has
12 experienced during the test year and not what it
13 actually requires. Because it is simply a test year, a
14 test year view with very rarely any pro form type
15 adjustments made to the balance sheet.

16 And as Ms. Merchant described as well, in the case
17 where a utility is financially troubled, it may have a
18 -- actually have a negative working capital, and no one
19 should think that that means it has no requirement for
20 working capital. It just has not experienced a working
21 capital -- a positive working capital.

22 The second reason why it's not exact, or not any
23 more exact than the formula method, is that it's an
24 allocation. And an allocation, although it may be the
25 only mechanism to measure certain things, it's not the

1 best measurement for working capital.

2 And the last reason is that being from -- looking
3 at it from a management perspective, it is open for
4 manipulation. It puts management in a dilemma of
5 making decisions that may not be in the best interest
6 of the customers nor the utility. And just a very
7 brief example, cash in the bank, where cash in the bank
8 is not available as a component for working capital
9 using the balance sheet method if it is earning
10 interest. And management may be faced with making a
11 decision whether to put that cash in a money market
12 account earning 2-1/2 percent, or to leave it out of
13 the money market account, earn no interest and,
14 therefore, have it available as a working capital
15 component.

16 The formula method measures a 45-day average lag
17 in recovering revenues to finance operating costs
18 allowed in the test year. Sometimes that results in a
19 higher working capital, and sometimes it results in a
20 lower than the balance sheet. But in no case will it
21 result in a negative, or hopefully not a zero. And I
22 think that it averages -- I think that each utility, if
23 looking at its own situation, may find in some cases
24 one is -- one would result in a higher revenue
25 requirement than the other. But overall, it results in

1 an average, fair, positive number.

2 Now, I'm going to go to Section .433(3),
3 specifically, whether or not to also include preferred
4 debits as a separate item of rate base. Less there be
5 any misunderstanding, the Waterworks Association is not
6 suggesting that deferred debits in their entirety be
7 included as a separate item of rate base. And let me
8 read to you, briefly, from my accounting manual, that
9 sometimes have to go back to, the definition of a
10 deferred debit, also called a deferred charge. You
11 will see the terms used synonymously. "A deferred
12 charge is caused by the prepayment of long-term
13 expenses. These expenses have reliably determinable
14 future economic benefits, useful in earning future
15 revenues. On this basis they are viewed as assets
16 until they are used." The only conceptual difference
17 between prepaid expense, which is a type of current
18 asset, and a deferred charge or deferred debit is the
19 length of time over which the deferred amount will be
20 amortized.

21 Giving you a couple of pertinent examples, one is
22 rate case expense. At the time that a rate case is
23 filed, the Company has incurred a large amount in some
24 cases, of rate case expense, and is allowed to recover
25 one-quarter of its rate case expense in current rates.

1 It is amortized over a four-year period, and there is a
2 balance remaining that is not recoverable through any
3 other mechanism. It is an investment made by the
4 utility upfront and an expense and, yet, it is not
5 allowed to recover it all in one year. And the
6 utilities agree that that is fair. It has a benefit of
7 more than one year, and that expense should be
8 recovered over a period of time. Until it's fully
9 recovered, it's an item on a balance sheet. It's not a
10 current asset. Again, the definition, the accounting
11 definition of working capital is current assets minus
12 current liabilities.

13 Another example of a deferred debit is a deferred
14 maintenance cost. For example, a utility has a program
15 of repainting tanks every five years. One-fifth of
16 that expense will be allowed to be recovered in current
17 rates. The remaining fourth-fifths is sitting on the
18 balance sheet as an asset, an investment made by the
19 utility. It's not includable in utility plant in
20 service. It is not includable in working capital,
21 because it is not a current asset. It's not includable
22 in working capital because, using the formula method,
23 only one-eighth of current operating expenses are
24 allowed in working capital. The unamortized balance in
25 some cases represents significant investment made by

1 the utility.

2 COMMISSIONER CLARK: You're saying the unamortized
3 balance of something should earn a return?

4 MS. SWAIN: That's right. A deferred charge is a
5 mid-term asset. It's not a current asset. It's not
6 something that is going to be used up within the
7 current period. And it is not a long-term asset. It's
8 not a tangible utility plant asset, but it represent an
9 investment made by a utility which it will not recover
10 until the amortization period has expired.

11 CHAIRMAN DEASON: Wouldn't you agree that a
12 properly applied balance sheet approach would consider
13 all the deferred debits which are utility related and
14 prudently invested in and would earn a return under
15 that approach?

16 MS. SWAIN: No, I don't agree with that. And the
17 reason is that the balance sheet method of working
18 capital should only consider current assets and current
19 liabilities. And I am speaking of an asset that is not
20 a current asset. It has perhaps many years ago been
21 grouped on a schedule that we use here at the Florida
22 Public Service Commission with working capital, but
23 it's not truly a component of working capital. It's
24 not a current asset. It's something else. Just as
25 Patricia Merchant described, deferred credits are not

1 includable -- are not otherwise includable in -- by
2 looking at capital components and CIAC, somewhere or
3 other there is some deferred credits that may be --
4 also need to be considered. And the Waterworks
5 Association has no objection to that as well. But, we
6 need to separate the concept of working capital from
7 another type of asset that's not included in the
8 current assets.

9 And I don't think that a balance sheet -- the
10 balance sheet method is going to solve that problem. I
11 think that while you're looking at a balance sheet,
12 doing a working capital calculation, that it was
13 logical to then also look at other things that were not
14 included in current assets and perhaps lump them all
15 together. But I don't think it was ever intended, and
16 it certainly is not in -- deferred debits don't fall
17 within either definition, either the current asset
18 minus current liability nor the lag between the time
19 that expenses are incurred and revenues are recovered.
20 It doesn't fall within either one of those.

21 In the past, the way that they were treated, even
22 at a time when one-eighth O&M was used prior to the
23 early 1980s, the Staff would look on a case-by-case
24 basis, and it often had to be brought up by the utility
25 and often -- not always did they bring it up. But a

1 portion of that deferred asset, deferred rate case
2 expense was includable as a rate base component, in
3 addition to working capital. And the way that was done
4 is that an average balance would be used. We recognize
5 that because it's a deferred debit, and it is being
6 amortized, that balance is continually decreasing. And
7 perhaps 100 percent of that should not be included, but
8 some portion of it should. At least the average
9 balance that is going to be there during the time the
10 rates are in effect. And not all deferred debits
11 should be considered. And I don't think that that
12 would be a tremendously costly or expensive endeavor.
13 I think the utilities would want to see that they are
14 going to recover the investment they have made in rate
15 case expense, and the investment that they have made in
16 expenses that they were required to defer and amortize.

17 If they painted a tank during the test year, and
18 were only allowed to recover one-fifth of that or
19 one-fourth of that, then the remainder is not recovered
20 through rates in the current period unless somehow or
21 the other they can recover a return on it by
22 identifying it separately on rate base.

23 And there are other types of deferred debits that
24 clearly should not be included. And I don't think it
25 needs to be looked at in any great depth. For example,

1 there is some preliminary survey and investigation type
2 accounts that are described in the NARUC chart of
3 accounts that fall within deferred debits. And they
4 relate to projects that may be in construction work in
5 progress. And where that construction is not included,
6 well, neither should preliminary survey investigations.
7 I'm speaking specifically of those things that are
8 includable as operating expenses during one brief
9 period of time, the test year, and the unamortized
10 balance then should be separately included.

11 The rule that Ms. Merchant quoted, or described,
12 was stated in Order No. 21202 in May of 1989. There
13 are six witnesses quoted in that order under the
14 section of working capital. And all six witnesses that
15 are quoted stated that deferred charges should be a
16 separate line item in rate base. And I have not
17 reviewed the transcripts. I was aware of the hearings
18 going on at that time, but each one of the witnesses
19 that testified related to working capital described
20 something similar to what I'm describing to you today.

21 Now, what ended up happening is an order was
22 issued that says that we believe it's appropriate to
23 strike a compromise between the established superiority
24 of the balance sheet approach as the most accurate
25 reflection of the utility's working capital and the

1 witnesses' persuasive arguments for the formula
2 approach and an allowance for deferred debits. I
3 believe that what happened was that to switch to using
4 a formula method, which the witnesses in that case
5 demonstrated was less expensive, that they had to give
6 up something. And what they gave up was deferred
7 debit. To my knowledge there is no testimony in that
8 case to the contrary of what is stated in the order.
9 Their testimony being that deferred debits or deferred
10 charges should be included.

11 I also, although the order states that it's a more
12 exact method, have described to you the reasons why I
13 believe that it is a more exact method. I think that
14 we need to somehow separate this concept, separate the
15 concept of working capital, which is specifically
16 looking at current operations from mid-term assets, and
17 give the utility an opportunity to earn on what could
18 be a significant investment that it has made.

19 The concludes my comments on working capital and
20 deferred debits.

21 The first sentence in .433(3), related to netting
22 deferred tax debits and deferred tax credits on the
23 capital structure is an acceptable alternative to what
24 I think is a better mechanism. And just to spend a
25 couple of moments on it, the most common cause for

1 deferred tax debits are the payment of taxes on CIAC.
2 And I think that it would be more accurate and more
3 simple to simply offset CIAC by the taxes paid on it.
4 And there has been resistance by the Staff to doing
5 that. And, personally I think that it's simpler, it's
6 cleaner, it's clearer, and it may have the same effect
7 as what Staff is recommending in this change. And,
8 again, as I said, this is an acceptable alternative. I
9 had rather see it be a direct offset to the transaction
10 that caused the tax, but if that were not possible,
11 then this would be fine.

12 I would like to also clarify -- and I have spoken
13 to Staff, and I believe that they agree -- that what
14 this is intended to do, their proposed change is
15 intended to do is to make sure that all deferred taxes
16 associated with any transaction that is going to affect
17 rate base be somehow included. And my particular
18 concern was where there may be a prepaid CIAC that is
19 non-used and useful, may be found to be for some
20 reason, an appropriate reduction to rate base. I want
21 to make sure that those deferred debits or the taxes
22 paid on that CIAC, even though that CIAC is prepaid, is
23 used to offset the deferred credits and the capital
24 structure.

25 That concludes my comments. Thank you.

1 CHAIRMAN DEASON: Mr. Hoffman?

2 MR. CRESSE: Mr. Chairman, my comments will be
3 fairly brief. I have filed written comments on two
4 issues. The part that I am suggesting as it relates to
5 the removal of the sentence in Paragraph 3 that says,
6 "No other deferred debit shall be considered in rate
7 base when the formula method of working capital is
8 used." I think, simply, what you have just heard is
9 about as good an explanation about that problem as I
10 have ever heard. But the fact remains that if you just
11 take a very simple example of the way you treat
12 nonrecurring expenses for ratemaking purposes, on the
13 next page you say you're going to amortize that over a
14 five-year period. Actually, you ought to change that
15 to a four-year period to make it consistent with the
16 other amortizations of rate case expense and other
17 things. Because, typically, if a utility can stay out
18 of a rate case for four years, absent other external
19 factors effecting them, they are doing pretty good.
20 Particularly a water and sewer company is doing pretty
21 good with all the external factors placed on them.

22 So, the question is whether or not on deferred
23 expenses you're going to allow a rate of return on that
24 which they have invested but haven't recovered. You
25 haven't allowed recovery of it. And simply put, I

1 think if you're going to abide by the principle that
2 the utility has the opportunity to earn, not a
3 guarantee, but the opportunity to earn a fair rate of
4 return on their prudent investment, then you will allow
5 them to earn a fair rate of return on any unamortized
6 expenses that are reflected on their books and records.
7 If you eliminate that, you're violating the basic
8 principle of giving the opportunity to earn a fair rate
9 of return on the money that you have spent, on the
10 investment that you've made. Because, basically, on
11 deferred expenses what you're doing is treating a
12 portion of that cost as an asset until you're allowed
13 to recover.

14 It is really no different than saying, "We have
15 invested in a four-year asset, and we are going to
16 depreciate it over four years." And when you say to a
17 utility, "You're not going to be allowed to earn a rate
18 of return on that investment, even though it has a life
19 of only four years," you're saying to them directly,
20 "We are not going to allow you to earn a fair rate of
21 return on the prudently incurred cost, or give you the
22 opportunity to do it." Strike that sentence, and it
23 can be an issue in the rate case, that the people can
24 jump up on each side and argue how much should be
25 allowed. When you incorporate it in your rule, you

1 have just about foregone, you know, the opportunity to
2 really argue it. I realize that the front of this
3 paragraph says, "Unless for good cause shown," but
4 things have a way of saying, "Well, the first time we
5 have decided that --" you know, we do rate case expense
6 standardly.

7 COMMISSIONER CLARK: Do we currently -- take rate
8 case expense, do we currently treat it as an asset on
9 which a return can be earned?

10 MR. CRESSE: You should. I, frankly, don't know.
11 I don't know the answer to that question, but it
12 should. If you amortize it over a four-year period,
13 obviously, people have got money invested in rate case
14 expense until they recover it. And it takes four
15 years, yes, they are entitled to a rate of return on
16 it.

17 COMMISSIONER CLARK: You're not allowing them to
18 pay you over four years?

19 MR. CRESSE: Pardon?

20 CHAIRMAN DEASON: Commissioner, the amortization
21 is allowed over a four-year period. The utility
22 recovers dollar-for-dollar the money spent. The
23 question is the carrying costs of those funds, they
24 have to expend the funds, pay the attorneys and the
25 consultants upfront, and so they have an investment, so

1 to speak, that has not been recovered.

2 MR. CRESSE: They can't survive if they pay me an
3 amount over four years. I like to have it upon the
4 completion of service.

5 CHAIRMAN DEASON: I think there has also been, in
6 some cases, I don't know if it is to the point of
7 whether it is a policy or not, it may very well be, but
8 in some case it has been determined that the
9 unamortized rate case expense has been excluded from
10 rate base for the specific reason that the utility
11 would be allowed to recover the expenditures, but would
12 not be able to -- allowed to earn a return on that as
13 an incentive to the company to minimize rate case
14 expense to put them at jeopardy to some limited extent
15 to keep rate case expense at a very minimum. Now, I
16 don't know if that is a policy or not. I think that
17 rationale has been utilized in some cases. Maybe Staff
18 can enlighten us further.

19 MS. MERCHANT: I think back when we used the
20 balance sheet approach. I know back when we used the
21 balance sheet approach, we did include the unamortized
22 balance of rate case expense, but we calculated the
23 average unamortized balance over the remaining period.
24 That was the Commission practice at that time. And I
25 am not aware of a water and wastewater case that we

1 have handled that we have made any type of an
2 adjustment to disallow the unamortized portion using
3 the balance sheet approach. But the Commission
4 practice using the formula approach, we have not
5 included any unamortized rate case expense in rate
6 base.

7 COMMISSIONER CLARK: And it is because it's a
8 trade-off.

9 MS. MERCHANT: That is our opinion. That in the
10 balance sheet approach, I don't think the Commission
11 ever distinguished between the current assets and the
12 current liabilities. It was always built into the
13 calculation that deferred debits would go in, and the
14 deferred credits would go in, if they were appropriate
15 to be included in the balance sheet approach. And we
16 did not separate out that portion which was current
17 assets and current liabilities. And the same thing
18 with the loss, the deferred charges or like deferred
19 painting charges. We would use the average unamortized
20 balance as a debit to the balance sheet approach. And
21 any other credit items would offset that. So, it's all
22 one calculation. It wasn't separated between current
23 and deferred portions.

24 MR. CRESSE: I think you took some gains. You
25 take gains and you amortize gains sometimes over,

1 disposition of the property, amortize those over a four
2 or five-year period. Obviously, unamortized gains
3 offset the unamortized expenses. I'm not arguing that
4 point at all, because those gains should offset. But
5 what your rule does is really, essentially, prohibits
6 that evidence from being submitted. And I think you
7 ought to strike that out of the rule, and then people
8 can come in if they have other deferred debits that are
9 not offset by other deferred credits, you can look at
10 them and evaluate them and say, "Should you earn a fair
11 rate of return on that, or should you not?"

12 COMMISSIONER CLARK: Shouldn't we just strike all
13 of 3 in that case, because the deferred taxes --

14 MR. CRESSE: Well, I think what -- my
15 understanding of what deferred taxes does, it says they
16 offset one another. And --

17 COMMISSIONER CLARK: But they fall into the same
18 category as a deferred expense.

19 MR. CRESSE: No. It says it will be in a separate
20 line, and that they offset one another. Now, the Staff
21 can explain that better than I. It's not a part of
22 working capital.

23 COMMISSIONER CLARK: What I am saying is if we are
24 just going to look at types of expenses that are
25 deferred over a period of time and types of credits

1 that are deferred over a period of time, such as gain
2 on sale, taxes fall into those -- taxes and expense,
3 and you may have to pay it upfront and get it back over
4 a period of time, or you may get to pay a little bit
5 and collect it over a period of time. What I am saying
6 is why we have 3 is because you're making an exception
7 for a certain type of deferred credit and deferred
8 debit. If you were just going to open the whole thing
9 up with respect to all deferred credits and all
10 deferred debits, then you can take out 3 completely.

11 MR. CRESSE: I would rather let Staff explain
12 their proposed rule, and why. I feel a little
13 inadequate on that subject, and I will admit it and
14 confess guilt. But I think there's a good reason, from
15 what I understand there is a good reason to treat that
16 in the way it's written there.

17 MS. MERCHANT: I think with the deferred tax
18 credits and debits, you have got the deferred tax
19 credits in the capital structure, that has been
20 Commission practice as long as I have been here. But
21 until the CIAC became taxable, that is when the debit
22 deferred taxes really came into play. And then you've
23 got the question of what to do with them. We always
24 netted the two, the debit and the credits. And,
25 generally, the debits were a lot lower than the

1 credits, so the net balance went into the capital
2 structure. But now we have a situation with water and
3 wastewater utilities that is reverted to a net debit
4 balance because of the taxability of CIAC. So, I think
5 we really need to keep those two together as a package
6 and -- Ms. Causseaux can answer it in more detail for
7 us on deferred taxes.

8 COMMISSIONER CLARK: Just from the standpoint that
9 one is a deferred expense, and the other is a deferred
10 credit, taxes are an expense like anything else. What
11 I'm saying is they fall within the big category of
12 deferred debit or credit just like unamortized rate
13 case expense does.

14 MS. MERCHANT: I think they are a lot longer term,
15 though, than the other items that we are discussing.

16 COMMISSIONER CLARK: But the reason you need 3 now
17 is because you're making an exception for a certain
18 type of deferred taxes, and the other ones you're not
19 going to look at. If you're just going to leave it
20 open to discussion in the rate case, you can do away
21 with all of No. 3.

22 MS. MERCHANT: I think that kind of defeats the
23 purpose of going to -- going from the balance sheet
24 approach, because immediately you're going to have the
25 cost, the increased cost to decide which ones are more,

1 you know, which ones should be included. And I just
2 think you have defeated the purpose right there. And
3 you're always going to -- if you leave the other
4 deferred debit portion in the rule, I mean, if you
5 allow that, then you're opening that up to every rate
6 case to be litigated. And I think our goal is to
7 reduce the cost and to get a standard practice.

8 MR. CRESSE: Commissioner Clark, let me add, I
9 think the reason it's handled separately, from my
10 perspective, is all of these deferred taxes have zero
11 cost of capital and are treated as a source of funds in
12 the capital structure. That makes it separate, and I
13 think it ought to stay that way. If you look at it
14 long enough and see the impact of it, you will find
15 that's really in the best interest of the ratepayers to
16 handle it that way. I won't go any further.

17 MR. ARMSTRONG: Also, Commissioners, if I could, I
18 don't want to, you know, I don't want to overstate how
19 difficult this would be in a rate to do, too. Because
20 I think what the company is looking at is things like
21 mandated costs, like testing costs. That is certainly
22 one thing that we have to do. Renewal of permits,
23 those costs, we are required to amortize them. We
24 don't get a return on the dollars. Which, with the
25 testing requirements going up and up every year, the

1 dollars are becoming more significant. Another thing
2 would be reasonably incurred costs, which for some
3 reason or another, it's decided during a rate case that
4 they be amortized. I mean, I think those are pretty
5 specifically identified and easily identified in rate
6 cases.

7 COMMISSIONER CLARK: Let me be sure. Is this a
8 working capital argument, or is this simply a rate base
9 argument? I realize working capital goes --

10 COMMISSIONER CRESSE: It's a rate base argument.

11 MS. MERCHANT: I would disagree with that. I
12 would think it's a working capital argument. I think
13 that you can't separate them out.

14 COMMISSIONER CLARK: Well, let me ask this
15 question: Is working capital generally thought to be a
16 current look?

17 MS. MERCHANT: I think for accounting purposes
18 working capital is current assets minus current
19 liabilities. I think what we have is a ratemaking
20 balance sheet approach. I don't think that it's
21 actually just the current assets. It has never been,
22 since I've done a balance sheet calculation, it has
23 been anything on the debit side that was appropriate to
24 be included, and anything on the credit side,
25 irregardless of current or mid-term life.

1 COMMISSIONER CLARK: Let me ask you a question.
2 How would rate case expense or other expenses be
3 different than, say, if you were getting ready to build
4 a plant and you had to expend money for site
5 preparation and plants?

6 MS. MERCHANT: Construction work in progress?

7 COMMISSIONER CLARK: Right. You put it into
8 construction work in progress --

9 MS. MERCHANT: Correct.

10 COMMISSIONER CLARK: -- and that becomes part of
11 rate base.

12 MS. MERCHANT: Not necessarily. Only when the
13 utility can show that it has a financial -- I can't
14 think of the right word here. The financial condition
15 will suffer if the construction work in progress is not
16 included. Generally what is done, is CWIP is
17 disallowed for water and wastewater utilities. And
18 they are allowed to earn an allowance for funds used
19 during construction, AFUDC.

20 COMMISSIONER CLARK: All right. But what I am
21 saying is they just don't get it back
22 dollar-for-dollar. They get a return on it.

23 MS. MERCHANT: They get a return on it; that's
24 correct.

25 COMMISSIONER CLARK: Why would rate case expense,

1 which is an investment they have to make, that they can
2 only recover over a four-year period be any different?
3 What is the rationale for it being different?

4 MS. MERCHANT: I'm saying that that is implicit in
5 the formula calculation for working capital. It's
6 one-eighth of O&M expenses. That is the alternative
7 to the amount of working capital that you would get on
8 the balance sheet approach. I don't think that you can
9 separate the two out. Another --

10 CHAIRMAN DEASON: Let me take a crack at this for
11 just a moment. Maybe we need to go to ratemaking 101
12 here for just a moment.

13 What you've got is you've got a balance sheet.
14 That's the whole basis upon which regulation is based.
15 You start with the balance sheet. You look at all of
16 the assets, and you look at all of the sources of
17 capital. If a utility were 100 percent jurisdictional.
18 If it were -- you're confident that it was 100 percent
19 -- all the assets were prudently invested in, and they
20 were all used and useful; and you didn't have to worry
21 about all of these other ratemaking adjustments and
22 concerns that we have, it would be a simple matter.
23 You take total assets; that would be your rate base.
24 And you would look at the credit side, and you would
25 identify all of the sources of capital and those things

1 which had a cost to them; that would be your capital
2 structure. And those that didn't have a cost, you
3 would put those in the capital structure as zero cost.
4 You'd get a composite rate of return. You'd multiply
5 that composite rate of return times your total assets,
6 and you'd get your revenue requirement. Of course,
7 you'd have to add in your expenses, but that is the
8 income statement. Right now we are talking about
9 balance sheet. But we don't -- we can't do that.
10 That's too simple. We do have all of these concerns
11 about what is jurisdictional and what is not. We just
12 had the example that some utilities invest in propane
13 gas operations. We can't allow a return on that. In
14 the electrics we have FERC jurisdiction versus state
15 jurisdiction we have to allocate, so we can't use the
16 balance sheet for that.

17 But I did a study one time, and I think I
18 calculated that 99 percent of the rate base that we
19 allow comes straight from the balance sheet. And what
20 is it? Well, it's your long-term plant. It's the land
21 the plant is built on. It's the plant. It's all the
22 infrastructure upon which the utility -- it's the
23 materials and the supplies, fuel inventory, in the case
24 of electric utilities, which is a large component. All
25 of that comes straight from the balance sheet. And we

1 say, "Fine, that's great. Let's use the balance
2 sheet." And then you've got this 1 percent that you
3 don't know what to do with. And you've got people out
4 there saying, "Well, we can't use the balance sheet to
5 determine working capital. We've got to use a formula,
6 because it's simpler." And it is simpler. There is no
7 doubt it's simpler.

8 When we go and we calculate working capital, what
9 we are saying is -- the way I've always interpreted
10 working capital, it's not simply just current assets
11 and current liabilities. It's everything on the asset
12 side, on the debit side of the balance sheet, that's
13 not already in rate base we have got to look at in
14 determining if it is in or out or not. And what you do
15 on the credit side, is everything on their credit side
16 that's not already in the capital structure, and you've
17 got to determine whether that's utility related and how
18 that's to be determined. You net the two against each
19 other, and usually you come up with a positive amount
20 that goes into rate base and earns the composite rate
21 of return.

22 So, you cannot simply look at working capital and
23 say it's current assets minus current liability, not in
24 the ratemaking sense. It's all assets which would
25 include your deferred debits. But in making that

1 determination on the balance sheet, you would also look
2 at deferred credits and see if the two offset each
3 other. And sometimes they would, and sometimes they
4 won't. And it may depend on what industry you're
5 working in as to what the results are going to be.

6 What we are hearing here is for the water and
7 sewer industry that with the CIAC being such a large
8 component, that it's very possible that your deferred
9 debits are going to exceed your deferred credits; which
10 then means if you're going to have a net debit there,
11 that is a component that gets added into rate base. If
12 you strictly follow the balance sheet, all of that will
13 be taken care of. But what we have here is we have an
14 argument that says it's too costly and time-consuming
15 for a small water and sewer company to do a thorough
16 and accurate balance sheet. What is the answer? Well,
17 let's do one-eighth of O&M. And what the utility is
18 saying is, "Well, that's all right for the current
19 assets and current liabilities, one-eighth is the
20 proper surrogate." And what you have Staff saying is
21 that, "Well, we are going to do working capital in the
22 broader definition with the formula or we are not."
23 And what they are saying is you can't mix apples and
24 oranges. You can't take the one-eighth of O&M and then
25 start adding in deferred debits on top of that, because

1 in the broader definition of working capital, the
2 one-eighth they are supposed to already take that into
3 consideration. That is the issue, and I hope I have
4 described it.

5 COMMISSIONER LAUREDO: Would you put that in
6 writing?

7 CHAIRMAN DEASON: I have before.

8 COMMISSIONER CLARK: He is the reason we do
9 balance sheet.

10 CHAIRMAN DEASON: All right. Mr. Mann.

11 MR. CRESSE: Mr. Chairman, I had one other comment
12 about the Public Counsel's proposal, but I would like
13 for them to explain it first. But I just didn't want
14 you to think I was through.

15 CHAIRMAN DEASON: Okay.

16 MS. DISMUKES: OPC is the odd man out. We are
17 proposing the Commission switch back to the balance
18 sheet approach for determination of working capital. I
19 think the real issue here is, is it more expensive to
20 do the balance sheet approach? I think the Commission
21 has determined that, in Order 21202, that the balance
22 sheet approach was the most appropriate and accurate
23 reflection of a utility's investment in working
24 capital. It's my current understanding that they use
25 that approach in electric and telephone. If I am

1 wrong, I wish somebody would correct me.

2 So, I think what we really need to get down to, if
3 we are going to debate about the balance sheet approach
4 versus the one-eighth O&M is, is it really more costly
5 to do the working capital approach to the extent that
6 it outweighs the benefit of the accuracy.

7 In the order where that Commission decided to
8 change its past policy of using the balance sheet
9 approach and switch to the one-eighth O&M approach,
10 that was basically the decision, or the basis for
11 making the change, that it was more costly; that the
12 balance sheet approach cost more than the impact on
13 rate base or the revenue requirement.

14 And I'd just like to talk about that for a minute.
15 That order was, I believe, issued back in 1988. That
16 was several years ago. I think many utilities have
17 come further in terms of their computer capabilities.
18 I think that it was more difficult to add up 13 numbers
19 by hand or on a calculator than it is on a computer
20 today.

21 I think if the Commission could establish a
22 methodology under the balance sheet approach that
23 reduced the areas of conflict that come up in the rate
24 cases, that would eliminate some of the litigation
25 expenses. I think of a lot -- as I recall, reading the

1 order, there were consulting expenses and attorney's
2 fees associated with working capital as it was set out.
3 Or this may have been in something that was received in
4 the public documents request, I'm not real sure. And
5 it wasn't, it didn't distinguish between how much of it
6 was the effort to add up the numbers versus the dollars
7 associated with litigating the issue. And I think that
8 if you had an approach that, for which we could not
9 argue about; it was set in stone, then you would
10 eliminate the litigation aspect of it.

11 So, in my mind when we are talking about working
12 capital, we are coming down to: Is it more cost
13 beneficial? I would like to address a couple of the
14 other points that have been raised so far that are
15 really outside the cost versus benefits.

16 COMMISSIONER CLARK: Well, let me ask you a
17 question. Do you think the costs of doing that balance
18 sheet outweigh the benefits? Do you think so?

19 MS. DISMUKES: I've done the balance sheet
20 approach for two small -- since I have been at OPC --
21 two small water and sewer companies, and it took me,
22 literally, less than 30 minutes.

23 So, we didn't litigate it. I mean, I did -- the
24 attorney asked me five questions. I think what it was
25 is the utility knew that the Commission was going to go

1 with one-eighth, given that that was their policy. So,
2 it wasn't worth getting into the nitty-gritty of it.
3 That is my personal opinion. In that instance, we came
4 up with a negative working capital. The utility, I
5 don't recall what they wanted. So, we put in the rate
6 base zero. You get into a case like Florida Cities or
7 Southern States, it does get quite a bit more complex,
8 primarily because of the deferred debits and credits.

9 In the Marco Island case, for example, the
10 utility did do a balance sheet approach. It was
11 included on a diskette that they gave us. They did not
12 present it to the Commission, but it was just -- I
13 won't say hundreds, but 10, 20, 30 deferred debit
14 accounts that they were listing. They didn't
15 distinguish; they put it all in for purposes of
16 determining their working capital in this diskette that
17 we got. You get into a company like that, it does get
18 somewhat cumbersome. But it's primarily due to the
19 deferred debit and credits that we've been talking
20 about that we want to add in with the one-eighth O&M
21 approach now.

22 So, I don't know if we go that route if we are
23 going to accomplish anything in terms of saving costs
24 by using the one-eighth approach. That is my personal
25 experience since being with the Office of Public

1 Counsel. I've done it a lot of times in electric and
2 telephone cases outside of this state, and you don't
3 have the rate case expense problem in those situations.

4 COMMISSIONER CLARK: So, what you're saying is in
5 order to realize a benefit from simplicity with the
6 one-eighth, you have to also eliminate taking into
7 account deferred debits and deferred credits, because
8 that's where the real cost is involved? And if you use
9 the one-eighth and also allow that, you haven't gained
10 anything by scuttling the balance sheet approach?

11 MS. DISMUKES: That is my personal opinion, yes.

12 COMMISSIONER CLARK: Okay.

13 MS. DISMUKES: I think Patricia Merchant brought
14 up the concept that the, and I believe that Florida
15 Waterworks Association agrees with that, that the
16 balance sheet approach is not representative of the
17 working capital needs of a utility that is perhaps not
18 earning compensatory rates. I've never seen anybody
19 prove that. I personally have not done a study. I've
20 thought about going back and looking at a utility that
21 -- what their balance sheet looks like before and after
22 they get a rate increase or after a rate increase has
23 been in effect for awhile. It has some intuitive
24 appeal in my mind that the working capital needs might
25 tend to appear to be less when a utility is earning

1 less than its authorized rate of return, because they
2 would sit there and, perhaps -- and I've never seen
3 anybody show it, the extent of their payables, so it
4 would increase the liability side of the equation.

5 One point that Mr. Shreve has brought to my
6 attention is that if we had implemented this rule four
7 years ago, we would be looking at the balance sheet
8 approach for the water and wastewater industry, four or
9 five years ago whenever that order came out. And so
10 it's somewhat a matter of timing. And we would have
11 liked to have seen the balance sheet approach be in a
12 rule, and then we wouldn't be here today.

13 The other point is that -- I don't know if it
14 could be done, but something that we have thought about
15 is, is there some kind of something in between the
16 balance sheet approach and the one-eighth. I haven't
17 done it, I've never seen it done, but is there any kind
18 of study on a generic basis or the sample of utilities,
19 water and wastewater specific, that would get us to
20 something more accurate than the one-eighth? For
21 example, is it one-sixteenth? Is that really the true
22 working capital needs for a water and wastewater?

23 COMMISSIONER CLARK: Why was one-eighth chosen?

24 MS. DISMUKES: I believe the one-eighth came from
25 the FERC many, many, many years ago. I think it was

1 back in the 1920s or '40s, or something like that. And
2 it is based upon, I believe, a 45-day lag. But my
3 knowledge of it is, is it started out at the FERC.

4 COMMISSIONER CLARK: But why 45 days?

5 MS. DISMUKES: The utility takes 30 -- there is a
6 30-day billing lag for the -- there isn't that
7 situation with telephone companies, which is, you know,
8 vehemently argued. But in this situation it's -- they
9 bill in arrears.

10 MR. CRESSE: Commissioner, let me add to that that
11 the one-eighth substituted, I think some time 15 years
12 ago, for what they called lead/lag studies. And people
13 actually made a living going into a utility and
14 studying what their working capital needs were on
15 lead/lag studies. And this Commission announced that
16 we thought any money spent on lead/lag studies was
17 imprudently incurred.

18 CHAIRMAN DEASON: So, that's the reason the people
19 that did lead/lag studies didn't like the balance
20 sheet, Mr. Cresse.

21 MR. CRESSE: And the people -- they invited us to
22 Washington to talk about lead/lag studies. And we told
23 them the same thing in Washington. And I don't think
24 there has been a lead/lag study done in Florida since
25 then. But lead/lag studies is the origin of the --

1 COMMISSIONER CLARK: 45 days?

2 MR. CRESSE: For the 45 days, and that is kind of
3 the origin of the one-eighth. But, actually, people
4 went around and looked at all of that stuff in the
5 past: How long does it take you -- how much money do
6 you have to put up that's in your current deal that is
7 not in your plant? And, you know, you have to pay
8 bills in advance of getting your revenue.

9 CHAIRMAN DEASON: At one time the Florida
10 Commission put a refinement on the formula and had what
11 they referred to as the 20 percent income tax lag.
12 What they did was they calculated the one-eighth of
13 O&M, and then they said whatever -- and they took 20
14 percent of your income taxes payable and said, "Well,
15 that is an amount that works in the opposite
16 direction," and they offset the two. And you could
17 debate whether that was a good refinement or not. But
18 you can see there are all kinds of variations to the
19 straight one-eighth.

20 MS. SWAIN: Commissioners, just a moment ago on
21 the 45 days --

22 MS. DISMUKES: I haven't finish my comments yet.

23 MS. SWAIN: Okay.

24 MS. DISMUKES: I lost my train of thought.

25 COMMISSIONER CLARK: You were talking about

1 one-sixteenth maybe being more accurate than
2 one-eighth.

3 MS. DISMUKES: Well, I was saying it could be more
4 accurate. We just don't know. The one-eighth is,
5 according to Mr. Cresse, based upon the lead/lag
6 analysis, the way it was done. My understanding is
7 that did come directly from the FERC and doesn't have
8 anything to do with water and wastewater utilities.

9 I had one other point that escapes me.

10 COMMISSIONER LAUREDO: It will come back.

11 MS. DISMUKES: Okay. I reserve the right, if it
12 comes back in a few minutes, after the other comments
13 come in, I'd like to say it.

14 MR. HOFFMAN: Mr. Chairman, I think she was
15 mentioning Mr. Shreve's support of the formula method.

16 MS. DISMUKES: I remember.

17 CHAIRMAN DEASON: Well, was that the negative
18 one-eighth formula?

19 COMMISSIONER CLARK: Let me ask a question. On
20 the -- it doesn't make sense to distinguish the size of
21 the utility with whether or not you use one-eighth.

22 For instance, it seems to me that we are most
23 concerned with rate case expense the smaller the
24 utility because it becomes a greater portion of what
25 needs to be visited on the ratepayers. Does it make

1 sense to adopt a rule that uses the one-eighth for C
2 and D utilities, and not for A and Bs? But I gather,
3 from what you said, it's really -- the problem is
4 really the A and B where you find the expense exceeds
5 the benefits.

6 CHAIRMAN DEASON: Think about that question,
7 because we are going to take a break.

8 (Brief recess.)

9 CHAIRMAN DEASON: I think we had a question
10 pending.

11 MS. DISMUKES: Did we have a question pending?

12 COMMISSIONER LAUREDO: A thought; a thought
13 pending.

14 COMMISSIONER JOHNSON: We had a thought pending,
15 that's right.

16 CHAIRMAN DEASON: A thought pending.

17 MS. DISMUKES: I just have one final point I
18 wanted to make. And that was in Order 210122 (sic),
19 which is the order that basically switched the
20 Commission's practice from the balance sheet approach
21 to the one-eighth O&M, my recollection of reading the
22 order, which was not that long ago, a day or two ago,
23 was that OPC did not present a witness in that case.
24 We did participate in the case through cross
25 examination, but you did not have an OPC witness there

1 discussing or recommending the balance sheet approach.
2 The parties that were addressed in the order were six
3 or seven of the utilities, and I believe there may have
4 been a Staff witness. That was my final point. Thank
5 you.

6 CHAIRMAN DEASON: Mr. Hoffman, you said you had
7 some questions. You had some comments after --

8 MR. HOFFMAN: I think Mr. Cresse had some comments
9 he wanted to make.

10 MR. CRESSE: My comments was on Paragraph 5. If
11 we are still on 3, then I can wait until we get to
12 Paragraph 5.

13 CHAIRMAN DEASON: Right now we are still on
14 Paragraphs 2 and 3.

15 MR. CRESSE: All right, sir.

16 MS. SWAIN: I have some additional comments on 2
17 and 3.

18 CHAIRMAN DEASON: Okay.

19 COMMISSIONER LAUREDO: Mr. Chairman, do we have an
20 idea what we are going to do today? Because I was
21 going to try to -- I did change my plane, but I guess
22 we are not going to make it, huh?

23 CHAIRMAN DEASON: Well, I've had a request that
24 once we finish the working capital discussion that we
25 move into the next rule, which hopefully won't take a

1 long time, so that Ms. Swain will not have to come back
2 in July. And if we can -- let me ask: What time is
3 your plane?

4 COMMISSIONER LAUREDO: 1:45.

5 CHAIRMAN DEASON: We will give it our best shot,
6 and if we get to the point to where we feel like we
7 have to go, we'll just have to go.

8 MS. SWAIN: Okay.

9 CHAIRMAN DEASON: Maybe Ms. Swain will be fast.

10 MS. SWAIN: I'm sure I will.

11 One point, again, is that working capital is a
12 mechanism the utility has to recover an investment in
13 -- a 45-day investment. It's only a 45 day-investment.
14 That is what the one-eighth O&M, that's what we were
15 talking about before.

16 Deferred debits are, in many cases, investments in
17 three, four, five, seven-year assets. They are not a
18 45-day asset as working capital is. And that is, I
19 think, the bridge and the distinction. We are not
20 asking, again, for all the deferred debit. What we are
21 specifically looking for is those expenses that have
22 been prudently incurred and are allowed in a rate case.
23 And we have been required to amortize them over a
24 period of time rather than recovering them in a current
25 year. We are not talking about putting out a wish list

1 of deferred debit. We are talking about specifically
2 where prudent rate case expense is being allowed to be
3 recovered over a four-year period, that the remaining
4 balance be recoverable, that permitting costs that have
5 been allowed to be recovered over a five-year period or
6 a seven-year period, whatever is pertinent, that the
7 remaining balance be recoverable. That testing fees
8 that have to be done periodically and only one-third or
9 one-fourth of them are allowed as a current operating
10 expense, that the remaining balance be recoverable, and
11 that any other expense in a rate case that is found to
12 be recoverable over a period of time in excess of one
13 year.

14 And, again, I'm not talking about a wish list of
15 deferred debits; I'm talking specifically about
16 expenses that are being allowed in a rate case, but we
17 are now not allowed to recover them in just a one-year
18 period. To me this is no different when you're
19 speaking of a five-year asset than a vehicle that's
20 used entirely for water utility operations that is
21 being depreciated over five years. It's the same
22 thing. It's just not tangible.

23 That is the extent of my comments.

24 CHAIRMAN DEASON: Questions, Commissioners? Final
25 comments?

1 MS. MERCHANT: Commissioners, I just wanted to add
2 one more point about using the balance sheet approach.
3 If we were to go to the balance sheet approach, I think
4 that one thing the parties have not mentioned was the
5 amount of time that Staff would have to expend on that.
6 And you are talking -- a majority of the rate case
7 applications would be, you know, a lot of the small
8 staff-assisted rate cases where that would not involve
9 any litigation expense, but a lot of Staff time. And,
10 also, even with the Class A and B utilities when you
11 start doing the balance sheet calculation, I have found
12 in my experience the bigger they are the more
13 allocations they have, the more complex the calculation
14 is going to be and the more time it's going to take
15 from Staff, from the utilities and litigation at a
16 hearing. And I just really believe that the balance
17 sheet approach is too expensive, because rate case
18 expense for water and wastewater utilities, whether
19 it's a small Class C company or an A or B, rate case
20 expense is very material compared to the revenue
21 requirement. Whereas, an electric, a telephone -- I'm
22 not sure about gas companies, but I know electric and
23 telephone, the rate case expense is not near as
24 material compared to that of a water and wastewater
25 utility.

1 CHAIRMAN DEASON: Let me clarify something. When
2 I mentioned earlier about a policy not allowing
3 unamortized rate case expense in rate base as an
4 incentive to minimize rate case expense, I was
5 confused. It was not the water and wastewater
6 industry; it was in the electric industry and maybe
7 telephone industry.

8 MS. MERCHANT: Those are all my points that I
9 would like to make.

10 MR. WILLIS: Commissioners, I would like to throw
11 something in, too. I worked a lot on that prior docket
12 in which the Commission went to the one-eighth formula
13 on. And parties here are mixing a lot of things and
14 trying to take components apart.

15 The industry wants to take in deferred debit and
16 look at just those certain components instead of using
17 the one-eighth.

18 And I think in this case Staff is going to have to
19 support Ms. Dismukes in this because the real reason
20 this Commission went to the one-eighth formula was to
21 use it as a surrogate to the balance sheet approach.

22 And Ms. Merchant is completely correct when she
23 says that the balance sheet approach contains
24 everything including your current assets and
25 liabilities, but also there is intermediate assets and

1 liabilities, your deferred debits and credits. It has
2 always been that way, and that is the way it is done in
3 the other industries, too.

4 As far as my experience goes, the major issues
5 that arose in the cases in the past came from the
6 deferred debits and credits. It never really had that
7 much of an issue on the current assets and liabilities.
8 Those were always, is it interest-earning or not
9 interest earning? How much should be thrown in? But
10 the real emphasis and the cost went to the deferred
11 debits and credits. And that is one of the major
12 reasons that the Commission said, "We will just use the
13 one-eighth formula as a surrogate." I don't think the
14 Commission was looking at saying one-eighth per our
15 definition here is current assets and current
16 liabilities. I think when they passed that rule or,
17 basically in that order, they were saying that the
18 one-eighth formula is a surrogate to the entire balance
19 sheet approach.

20 CHAIRMAN DEASON: Let me ask you a question. I
21 gather that the comments from the industry have
22 basically been that there is a concern that the
23 deferred debits, those items which the Commission
24 recognizes as a legitimate expense, but for policy
25 purposes have those expenses capitalized and amortized

1 over a period of time to even out the expense. We had
2 an example of a rate case expense is a prime example.
3 But we've also had other examples, such as, I don't
4 know, painting a water tower or things of that nature.
5 If the Commission were inclined to have a policy that
6 says something to the effect that, if the Commission
7 recognizes an expense as a legitimate and prudently
8 incurred expense for utility purposes and should be
9 recovered, and allows that expense to be amortized,
10 that the unamortized balance under some type of an
11 averaging method would be allowed in the rate base. If
12 we were to do that, then what, in your opinion, should
13 we do with the one-eighth? Should we say reduce that
14 to one-tenth or one-twelfth?

15 What I'm hearing the industry say is their concern
16 is that there is going to be more and more of these
17 types of expenses that are going to be incurred and are
18 going to be set up in an amortization schedule. I
19 think there was mention of the fact that some of the
20 costs for testing, which are going to become more and
21 more material may be treated that way. And that the
22 deferred debits are going to become more and more
23 significant in the overall scheme of things.

24 And I think the ultimate goal we are all trying to
25 reach here is how can we allow a reasonable return on

1 prudently incurred costs, and not spend a great amount
2 of time and expense, both time and expense of the
3 consultants and time and expense of Staff to determine
4 what the precise number is. I think we all would like
5 to have the precise number, but we are trying to, in a
6 reasonable way, offset that.

7 And my question is if we were to allow, if the
8 Commission enters an order and says, "This expense is
9 legitimate, amortize it over four years." And we take
10 some average of that and put that in the rate base,
11 what does that do to the one-eighth? Do you have any
12 idea?

13 MR. WILLIS: Since it's a surrogate you will have
14 to reduce it, because it did take into account, as far
15 as I'm concerned, in my opinion, it took into account
16 the deferred debits and credits. But if you are also
17 going to say, "Let's go ahead and include those
18 deferred debits," then I think you have got to also say
19 anything that the Commission decides is a prudently
20 incurred or a prudent deferred credit should also be
21 recognized on the offset.

22 CHAIRMAN DEASON: Well, I agree with that.
23 Nothing comes to mind right away, but I'm sure there is
24 something.

25 MR. ARMSTRONG: Can I make just two comments in

1 response? And that would be the one-eighth, we have
2 discussed why the one-eighth came about, the 45-day
3 lag. I don't know how you can reduce the one-eighth.
4 I mean, down to something else unless we can say the
5 Company will recover those dollars sooner than 45 days.
6 And I don't know that that can be said.

7 The second thing, though, is when we talk about
8 balance sheet or any other method, these costs we are
9 talking about, rate case expense and costs prudently
10 incurred but determine by the Commission, for some
11 reason, that they should be recovered over a period of
12 time, sometimes being three, four and five years. We
13 don't know all those things -- we don't know all those
14 items until we actually get to that rate case and get
15 through that rate case. So, you know, I don't know how
16 you can say that those things are considered as part of
17 the one-eighth O&M at this point either, when we don't
18 know what those numbers are going be. So, I don't know
19 how we can say it was contemplated within the --

20 CHAIRMAN DEASON: Well, see, that's just it. The
21 one-eighth is just a rule of thumb. And nobody can sit
22 here with any accuracy and say what is or is not
23 contemplated in the one-eighth. We don't know.

24 What I'm hearing is there is concern that deferred
25 debits are going to become more and more significant,

1 and that if we don't recognize them somehow, that we
2 are probably going to be putting ourselves in a
3 situation where we are going to be doing time-consuming
4 and expensive analysis when perhaps it's not necessary.
5 And that is what my concern is. That is the whole
6 purpose of these rules is to try to cut down on the
7 amount of time and expense and still come up with a
8 reasonable result.

9 And what I'm hearing Staff saying is that if we're
10 under the present scheme of things, if we're going to
11 give a lot of detailed analysis to deferred debits and
12 deferred credits, we have might as well do it for the
13 whole shooting match, and just have a policy of balance
14 sheet, which doesn't really bother me what that much to
15 be honest with you. But I'm trying to reach some
16 accommodation here.

17 MR. ARMSTRONG: You know, I think we made clear
18 that it's just those four items, and I don't know what
19 kind of detailed analysis we need. I know in the giga
20 case that we have spoken about frequently, the company
21 is not allowed to earn a recovery of all of those
22 dollars that are easily identifiable that were
23 prudently incurred, but amortized over a period of
24 time. Permitting costs, easily identifiable; testing
25 costs, easily identifiable; rate case expense,

1 certainly identifiable, because we are providing
2 updates, you know, three and four times during the
3 case, so I don't know.

4 CHAIRMAN DEASON: And that is what I'm saying. If
5 we can identify those, and we have an order or a policy
6 that says those are legitimate expenses, we're going to
7 amortize them. Basically, I'm asking you how much on
8 the one-eighth are you willing to give up, are you
9 willing to go to one-tenth, one-twelfth, or are you not
10 budging?

11 MR. ARMSTRONG: But I think what the thing is on
12 the one-eighth, the reason we have the one-eighth is
13 because there are these expenses out there that we are
14 incurring that we can't recapture in 45 days.

15 CHAIRMAN DEASON: You're saying the 45 days is
16 carved in stone and there is no deviation from that. I
17 just told you the Commission earlier had a policy where
18 we offset that with 20 percent of the income tax lag.
19 A fifth of it, because it was determined that on
20 average that you've got about a fifth of a year lag in
21 the payment of income taxes. You had the use of those
22 funds until you actually have to write that check to
23 the IRS on June 30th, or whenever corporations have to
24 pay their taxes. Now I know all water and wastewater
25 companies don't actually have to pay taxes to the IRS,

1 but in some instances you do. And the one-eighth
2 doesn't -- some people would argue that the one-eighth
3 doesn't contemplate that. Some people would argue that
4 one-eighth doesn't contemplate the delay in paying
5 interest payments on debts. That is not -- some people
6 would say it is and some people wouldn't. And the only
7 way you would know is to do an expensive lead/lag
8 study, which nobody is proposing be done.

9 MR. SEIDMAN: Commissioners, I guess my problem is
10 that the one-eighth, yes, it is an estimate and a
11 guideline. But it was always meant to be an estimate
12 of the cash working capital portion, not for the
13 portions that had to do with medium-term assets. And
14 when -- historically, when it was used under FERC and
15 before that the Federal Power Commission, and when they
16 started considering whether or not they should use that
17 or the balance sheet approach, it was for the purpose
18 of determining the cash working capital portion of it,
19 not as a surrogate for everything except long-term
20 assets. I think that is what our problem is here.

21 COMMISSIONER CLARK: Doesn't the balance sheet
22 take it into account, though? The balance sheet takes
23 deferred assets and credits into account. I mean, the
24 argument here is do we -- is the one-eighth going to
25 get us anything if we also allow you to include

1 deferred assets and deferred credits. And it seems
2 what I'm hearing is it's not going to get us much if we
3 allow that also, and we might as well use the balance
4 sheet approach.

5 MS. SWAIN: I would like to give a mathematical
6 example, and maybe that will help crystallize it a
7 little bit. Assuming you paint a storage tank, and it
8 cost \$4,000, and you are going to amortize it over four
9 years. It's \$1,000 that is allowed in current
10 expenses. Using one-eighth O&M for working capital,
11 you're allowed to recover your investment on one-eighth
12 of \$1,000. And, yet, there is \$3,000 that the company
13 has already invested in that's sitting in an
14 unamortized balance, an asset on the balance sheet for
15 which it's not recovering any carrying cost. And what
16 we are asking is that we recover at least an average of
17 that. If it is going to decline, it's going to be
18 \$3,000 today. It's going to be 2,000 and then \$1,000,
19 and then it's going to hit zero. We want to recover an
20 average of that. But under the formula method, you're
21 only recovering one-eighth of \$1,000. Now under the
22 balance sheet method we would have recovered the 45-day
23 lag for the entire cost, except that one portion of it
24 is sitting in a deferred debit account. Only the
25 portion that was in current assets, which is the

1 current portion, that you would recover through the
2 balance sheet. The deferred debit was somewhere else.
3 And that needs to be separately considered. It's still
4 separate. It always was a deferred asset. It always
5 was on the balance sheet as a deferred asset. Simply
6 because we used one-eighth O&M for the current expenses
7 doesn't mean that that \$3,000 sitting on an asset has
8 disappeared somewhere.

9 COMMISSIONER CLARK: But I think you're still
10 missing the point. The point here is do we gain
11 anything in terms of cost of using your approach, of
12 using one-eighth, and then also looking at the deferred
13 debits and credits, when we have had testimony that
14 that is where the real rub is. And we are not gaining
15 anything.

16 MS. SWAIN: But we're not -- we don't want to make
17 that the real rub. We only want to address those four
18 things that are already considered in a rate case. It
19 would not require a separate consideration. You are
20 already considering rate case expense. You're already
21 determining how much is a prudent rate case expense and
22 allowing us one-quarter of that in current expenses.
23 You're already disallowing some portion of a tank
24 painting that took place in the current year, saying
25 that it had a benefit in excess of the current period.

1 You're already disallowing some portion of our
2 permitting cost this year, because it has a benefit of
3 something other than just the current year. You're
4 allowing us to only amortize that maybe seven years.
5 There's some testing or some permitting that needs to
6 be done, it's significant in cost every seven years.
7 There is testing.

8 COMMISSIONER CLARK: Do you disagree with the
9 notion that you should reduce the one-eighth in some
10 way?

11 MS. SWAIN: I think there is certainly argument
12 that there may be a mechanical opportunity to reduce
13 the one-eighth. But the only portion in the one-eighth
14 is one-eighth of one year; that's all that's in there
15 right now. We are talking about the other three years
16 or five years or six years of the expense. The only
17 amount in there is one-eighth of one year.

18 CHAIRMAN DEASON: Commissioners, what is your
19 pleasure?

20 COMMISSIONER CLARK: Are we through with that?

21 CHAIRMAN DEASON: Yes. As far as I'm concerned we
22 have had adequate discussion.

23 COMMISSIONER LAUREDO: On the whole --

24 CHAIRMAN DEASON: No. This would be on Paragraphs
25 2 and 3 of Rule .433.

1 COMMISSIONER CLARK: I'd just leave it pending.

2 CHAIRMAN DEASON: Leave it pending. Okay.

3 Mr. Hill.

4 MR. HILL: Mr. Chairman, I did want to point out,
5 and I think everything has been covered, but at the
6 March 5th agenda we did have several options on this.
7 And I do want to remind you that you voted one
8 particular option because you needed to to go to
9 hearing with it. And that is what the debate has been
10 about this morning. There were options that included
11 the balance sheet approach for the Class A utilities
12 and the formula for the B's and C's. The balance sheet
13 for the A's and B's and the formula for the C's and one
14 or two other options. And I did just want to make sure
15 that you understood that there is still those options
16 available to you.

17 CHAIRMAN DEASON: Yes, I remember that. I
18 appreciate you reminding me. I think what the
19 Commission is going to do is, at this point, is to
20 instruct Staff to incorporate this same language in the
21 proposal we will be voting on later, and if
22 appropriate, you may want to suggest some of the
23 alternatives. We are still -- we are not giving any
24 additional direction to Staff. We are basically right
25 on the fence on this one, and we'll have to make a

1 decision when we -- we'll make a decision when we have
2 to.

3 COMMISSIONER CLARK: But Staff can change their
4 minds if they want to and make a different
5 recommendation.

6 CHAIRMAN DEASON: Oh, I don't have any problem
7 with that. We are not giving you any direction
8 different from what is before us right now. If you
9 feel inclined to change that, I have no problem with
10 that. I assume that is in agreement with the other
11 Commissioners.

12 COMMISSIONER LAUREDO: Yes, sir.

13 CHAIRMAN DEASON: Let's see if we can dispose of
14 .434. Staff?

15 MS. MERCHANT: Okay. Commissioner, Section .434
16 deals with the allowance for funds prudently invested
17 charge, which is referred to as AFPI, and not to be
18 confused with allowance for fund used during
19 construction, which is AFUDC.

20 What this charge basically does -- it has been
21 Commission practice for about, probably five to eight
22 years. This charge allows the utility the opportunity
23 to earn a rate of return on prudently constructed plant
24 to be collected from those customers that will connect
25 onto the system at a future date. So, it's the cost of

1 holding that plant that was prudently constructed. It
2 would be a charge in addition to the service
3 availability charge that they pay at connection.

4 What the rule does, is it lists out the filing
5 requirements, the notice requirements, the effective
6 date that Staff is proposing, and that the accrual
7 period be five years for prudently -- that the time
8 frame for prudently constructed plant would be five
9 years, unless it is otherwise approved in the case.

10 The only controversial area of this rule that I
11 believe exists is the requirement in Section (3)(f),
12 that net plant be used to establish a charge which is
13 plant less the accumulated depreciation, instead of
14 gross plant which would just be plant.

15 Basically, what the Staff -- and this is
16 Commission practice, to use net plant. It's been
17 addressing -- it has been used for several years since
18 it was established, since the charge was established,
19 it was net plant. Only recently, in the last two
20 years has this become an issue, to use gross plant.
21 Staff believes that what this charge does is separate
22 the used and useful revenue requirement from the
23 nonused and useful revenue requirement. The used and
24 useful revenue requirement is what you establish
25 customer rates on. And, basically, in that situation

1 you take your rate base, which includes your used and
2 useful plant, minus used and useful accumulated
3 depreciation. So, you can't just take out the used and
4 useful plant portion, you have to -- it would be unfair
5 to the utilities if you only removed the plant and not
6 the accumulated depreciation, which is a reduction.

7 And the way that we flow that through to the AFPI
8 charge is you just take those two amounts, the non-used
9 and useful plant amount and accumulated depreciation
10 and flow that amount directly over to the AFPI charge.
11 Then you allow depreciation expense on that nonused and
12 useful portion for the AFPI charge. You would have any
13 property taxes that were removed from the rate case,
14 from used and useful, that would flow over to AFPI.
15 You would make a revenue requirement on that. If they
16 had income taxes, you would get the income taxes.
17 They'd get the regulatory assessment fees on that
18 amount. And you basically work up a charging that
19 increases by year and is broken out by month, but it
20 actually increases by year, so that the time value of
21 money is included on that return.

22 The utilities argue that they are not going to
23 receive 100 percent recovery of the depreciation
24 expense if we use only net plant instead of gross
25 plant; that the future customers aren't going to pay

1 their full share. I believe that it's the burden on
2 the utility, if they wish to receive 100 percent
3 recovery of that depreciation expense, they should come
4 in at an earlier date and get their AFPI charge
5 established, so that they can recover that cost
6 upfront. Otherwise, if you don't do that, what you
7 have is a situation where you have plant that is
8 already physically deteriorated, and you are charging
9 those future customers something that has already
10 actually been depreciated. So, that is the basis
11 behind Staff's recommendation that you use net plant
12 instead of gross plant.

13 Other than that, I don't think anybody has
14 disagreed with any other components of the rule, and it
15 has never been very controversial in a rate. The only
16 thing controversial about AFPI is this net plant versus
17 gross plant.

18 And that concludes my comments.

19 CHAIRMAN DEASON: Ms. Swain?

20 MS. SWAIN: Thank you. Commissioners, until about
21 eight years ago, utilities did not have an opportunity
22 to earn a return on nonused and useful plant, nor did
23 it have an opportunity to recover expenses associated
24 with nonused and useful plant. And the Commission
25 developed, during a rate case some eight years ago, a

1 mechanism for utilities to recover that investment and
2 those disallowed expenses at the time a customer
3 connects. And they developed a calculation that, after
4 eight years of reviewing it, I think has been fair.

5 Until a few years ago, the utilities, quite
6 honestly looked at the AFPI as a source of revenues
7 that was unexpected and depreciated and did not look
8 behind the calculation and contradict, perhaps, the
9 calculation or fine-tune the calculation.

10 In the last several years, I've had the
11 opportunity to file applications that included a
12 request for AFPI charges using the calculation and
13 mechanism developed by the Staff some number of years
14 ago. And rather than simply putting numbers on a
15 computer model and seeing what came out, I started
16 looking at what was behind it. Until a utility
17 recovers its first AFPI charge, it has never had the
18 opportunity to recover depreciation on nonused and
19 useful plant. Until the day that it recovers its first
20 revenue from a new customer, that depreciation expense
21 associated with that, perhaps, deteriorated plant has
22 never been recovered through current customer rates nor
23 any other mechanism. It has been utility practice, and
24 there are utilities that do not depreciate certain
25 components of nonused and useful plant, because the

1 physical deterioration is at a much lesser pace than
2 the depreciation rule would allow using average life
3 methods. For example, transmission and distribution
4 plant, which may have a life of 50 years, and yet for
5 some portion of that it's nonused and useful.

6 At the time an AFPI charge is requested, there is
7 a determination of what assets are qualifying. And
8 very simply those are nonused and useful assets, assets
9 which have been disallowed from recovery from current
10 customers. There is a reduction in the accumulated
11 depreciation that is used to offset used and useful
12 plant, if there is such an accumulated depreciation on
13 the book of the utility -- on the books of the utility.
14 Using the matching principle in accounting, which we
15 are required to follow because of not only accounting
16 practice, but also our regulations, we do not record
17 expenses on our books until they have been allowed by
18 the Commission. And as an example, depreciation, very
19 pertinent. At the time the depreciation is
20 established, a life is established or there is a change
21 made, the utility is required by its regulator to not
22 record that on its books until it starts recovering the
23 revenues associated with that new depreciation life.

24 CHAIRMAN DEASON: You just lost me there. I'm
25 sorry.

1 MS. SWAIN: For example, for many years utilities
2 used a composite rate of, say, 2-1/2 percent for all
3 utility assets. And then in the mid-1980s new rules
4 were established identifying average lives for
5 different components of the plant. When a utility
6 filed a rate case for the first time under that rule,
7 it was required to then adopt the depreciation lives
8 required by that rule. And the test year would be
9 adjusted to reflect the new depreciation lives, the
10 expense with that new depreciation, not the 2-1/2
11 percent. Yet, the accumulated depreciation reflected
12 years of depreciation at a different rate. There was
13 not an adjustment made to accumulated depreciation to
14 change that or to restate that using the new rule.
15 And, in fact, the utility on its books is not to go
16 back and make an adjustment even in its test year to
17 reflect, assuming it was a historical test year, using
18 those new depreciation lives. As a matter of fact,
19 it's not to book those new lives until it begins
20 recovering revenues using those lives in its rates.
21 So, we found ourselves filing rate cases in March of
22 '93 using a '92 historical test year, adjusting our
23 current year depreciation expense using the new lives,
24 not adjusting accumulated depreciation historically,
25 prior to the test year of 1992. Being allowed to

1 recover revenues starting, perhaps interim rates,
2 perhaps eight months later, say, October of 1993, that
3 first month where revenues were recovered using the new
4 rates is the month that we are to put -- start
5 recording depreciation at those new lives.

6 If I were to file a rate case using a '93 test
7 year, there would not be an attempt by the Commission
8 Staff to go back and adjust 1992, which was my prior
9 test period for those new depreciation lives. We have
10 been instructed that those go into effect on our books
11 at the time we begin to recover the revenues. And very
12 interestingly, the matching concept is so closely held
13 on this single issue, and yet on AFPI, even though the
14 utility has never had the opportunity to recover the
15 expense associated with nonused and useful assets, it
16 is being required to reduce the assets on which it may
17 earn a return for the purpose of that calculation by
18 depreciation, although it has never recovered it.

19 It's very easy to say that the utility should go
20 ahead and ask for an AFPI at the time that it puts new
21 plant in service and do it at that time. But many of
22 us are facing utility facilities that have been in
23 place for 20 or 30 years today, or eight years ago when
24 AFPI was first conceived, and I can't go back and
25 change that situation. All I can do is look back and

1 see that I've never recovered depreciation expense, why
2 should I further reduce my opportunity to earn a return
3 on those assets by reducing them by accumulated
4 depreciation? There is going to be a point in time
5 when I can recover that depreciation. It's the point
6 when I first begin collecting the revenues under an
7 AFPI charge, when the first customer connects. And at
8 that point I've recovered depreciation expense, it
9 should be accumulated and used to reduce future returns
10 on nonused and useful plant. If that were to then
11 become used and useful plant, I have got an
12 accumulation now of depreciation expense that I have
13 recovered. And that should be used to offset my return
14 from current customers in the future. It should go
15 with it, but not until the moment I begin to recover
16 it. If I've not had the opportunity to recover it, it
17 should not be first accumulated. It should not be used
18 to reduce what I may earn a return on.

19 COMMISSIONER CLARK: And your rationale for that
20 is the way we treated a change from one depreciation
21 rate to a new depreciation rate in terms of how you
22 book that after a rate case. Is that your rationale
23 for doing it?

24 MS. SWAIN: I do not mean for that to be a
25 rationale. I mean for that to be a demonstration of

1 the Commission's policy of matching revenues,
2 particularly --

3 COMMISSIONER CLARK: But that's not really a
4 matching principle with respect to depreciation. I
5 mean, you would book and accumulate, as I understand
6 depreciation, from the time you put it in service. And
7 that is sort of separate from the ratemaking. You do
8 that, and you have to come in and get your rates
9 adjusted so you do collect it. I don't recall in any
10 industry that we go back and say, "You know, you didn't
11 collect this, and we are going to start -- we will not
12 depreciate it until you can start collecting it in
13 rates." And that's in that instance where you were
14 changing from one rate to another.

15 MS. SWAIN: There is going to be a point in time
16 when revenues are collected and plant is deteriorating.
17 When a utility serves its first customer, it is
18 collecting rates and its plant is deteriorating. But
19 the nonused and useful portion -- and another -- you
20 know, again, the example of transmission and
21 distribution lines in the case of developer-owned
22 utilities where lines are extended and were not
23 contributed by -- at the time that they were installed,
24 those facilities are not necessarily depreciated on the
25 books of the utility until they become used and useful.

1 In the meantime, if I have an AFPI charge allowed on
2 that nonused and useful portion, I have not recovered
3 the depreciation expense on that until it does become
4 used and useful and I collect that from current
5 customers.

6 I agree that the putting -- booking of
7 depreciation expenses in the case of a change in
8 depreciation life is an extreme example of the matching
9 principle. But what I am saying is that just logically
10 standing back and looking at earning a return on
11 nonused and useful plant, why should I not be able to
12 recover 100 percent of nonused and useful plant from
13 future customers? Why must I reduce it by a
14 depreciation I have never recovered?

15 CHAIRMAN DEASON: Did you book the depreciation?

16 MS. SWAIN: In some cases it was booked; in some
17 cases it was not booked.

18 CHAIRMAN DEASON: In the situation where it was
19 not booked, then are you denied recovery of that
20 expense through the AFPI?

21 MS. SWAIN: I'm trying to think of some of the
22 cases very frequently that we found with the Deltona
23 Systems where we did not depreciate. There was not an
24 accumulated depreciation on the books. There was not a
25 disallowance of accumulated depreciation from used and

1 useful, because it wasn't there to begin with. It
2 wasn't requested to begin with. So, what went was
3 intact the gross plant for transmission and
4 distribution. Because there was nothing on the books,
5 there wasn't a disallowance. It didn't come up. So,
6 no, we did not have, in those cases, we did not have a
7 reduction for accumulated depreciation on plant that
8 was not booked. The only distinction here, then, is
9 whether it was booked or not. And why, if I have not
10 recovered it, why should I have a reduction?

11 CHAIRMAN DEASON: Let me make an analogy here and
12 see if the rationale holds. And I don't know if it
13 does or does not. Let's take an example of a developer
14 utility who, for reasons of the development, keeps
15 rates artificially low, not even enough to cover all of
16 the expenses of operating the utility. And one of
17 those expenses could be argued to be depreciation
18 expense, even though the utility is required to book
19 depreciation. Under your rationale, could you then
20 come and say, "Well, in those prior years when I was
21 selling all of these lots in this development I didn't
22 recover all the depreciation expense that I booked
23 because my rates were too low. Now I want to reverse
24 that depreciation and now set compensatory rates upon
25 an undepreciated base."

1 MS. SWAIN: No, I don't think that a practice like
2 that should allow a developer-owned utility to
3 accumulate its cost and hold them for some future date.
4 I don't agree with that.

5 CHAIRMAN DEASON: Well, explain how this is
6 different, then? If you book depreciation expense for
7 prior periods, but now you are saying, "Now that I have
8 an AFPI charge, I should be able to ignore the prior
9 period depreciation that was booked so that I can
10 recover that through the AFPI on a going-forward
11 basis."

12 MS. SWAIN: Because I'm looking specifically at an
13 opportunity to earn a return on a facility that is
14 being held for future customers. And at some point in
15 time it's going to shift from nonused to used, and I am
16 going to be able to recover depreciation expense from
17 current customers. But in the interim period, I have
18 an investment with a -- and it's a true expense that
19 I've not ever been allowed to recover. It's not that I
20 have chosen to be negligent and not asked to recover it
21 or seek to recover it; I've never been given that
22 opportunity, and this is my first time. I've built a
23 new plant. I'm filing a rate case two years later.
24 I'm asking that the used and useful portion be
25 recoverable. And I'm also asking that that AFPI

1 include a return on all of my investment from future
2 customers.

3 There was a time that it was acceptable practice
4 to take all the costs associated with nonused and
5 useful plant and capitalize them. Maintenance of mains
6 that were not used and useful were capitalized,
7 depreciation expense was capitalized by not
8 depreciating it all. We are not doing that any longer.
9 We are not continuing to accumulate all costs and hold
10 them there for future customers. But we are
11 recognizing that there is a future economic and
12 physical benefit to future customers of having
13 installed nonused and useful plant, and it has been
14 found to be prudently invested, prudently incurred.
15 I've put that money out, and I'm waiting for my future
16 customers to connect. And when they connect, I want
17 them to then begin to pay the depreciation expense, and
18 not until they connect.

19 CHAIRMAN DEASON: Now, let me make sure I have my
20 mechanics correct. If you request an AFPI charge
21 simultaneously when a new plant is close to plant in
22 service, is there any problem with nonrecovery of
23 depreciation expense?

24 MS. SWAIN: If it was put in in a -- if I'm filing
25 a historical rate case, I'm still lagging a year. I've

1 still got plant in service for one year. I'm filing a
2 historical rate case. My average plant is equal to the
3 actual construction cost. I've got a half a year of
4 depreciation on average on the total plant.

5 CHAIRMAN DEASON: If you file a projected test
6 year, and you're anticipating --

7 MS. SWAIN: Then I'm fine. Then I'm fine. And I
8 can't always do that because I've got plant already in
9 the ground. I can't file a rate case every year to
10 make sure I pick up all of my plant.

11 CHAIRMAN DEASON: Okay.

12 MS. SWAIN: Thank you.

13 CHAIRMAN DEASON: You've finished. Okay.

14 Mr. Hoffman? Mr. Cresse?

15 MR. CRESSE: Mr. Chairman, let me just make a very
16 short observation if I can. The proposal in total
17 talks about the capitalization of property taxes. That
18 is in the proposal by the Public Counsel, and it is
19 also in the Staff's proposal on Page 126, contemplates
20 all other costs such as nonused and useful property
21 taxes.

22 CHAIRMAN DEASON: Mr. Cresse, what is the
23 paragraph reference?

24 MR. CRESSE: That's Paragraph M on Page 126 of
25 what I have.

1 MS. MERCHANT: Is that in .433?

2 CHAIRMAN DEASON: I think it's on Page 103 in my
3 version.

4 MS. MERCHANT: That's in AFPI?

5 MR. CRESSE: AFPI.

6 MS. MERCHANT: Okay. Excuse me.

7 MR. CRESSE: .434, I think.

8 CHAIRMAN DEASON: Right.

9 MR. CRESSE: There are so many multiple ways which
10 tax assessors use in this state to determine the value
11 of property that it's somewhat amazing. But for us to
12 -- for you to adopt a concept that somehow you're going
13 to capitalize property taxes and recover that sometime
14 in the future, assumes that property taxes is not a
15 recurring expenses. And if there is anything that is a
16 recurring annual expense, it is property taxes. I see
17 great benefit in encouraging people to take the long
18 view in the construction of water and sewer plant, and
19 that is what AFPI was designed to do, was to encourage
20 them to do the least cost type of planning and
21 implementation over the long run. And with that comes
22 sort of a regulatory contract or compact that if you
23 are prudent, if you make prudent investments, if you
24 look at the long-term, you're going to have the
25 opportunity to earn a fair rate of return on that

1 entire investment. Some of it, which we put in rate
2 base, we will allow to be recovered from current
3 customers. That which we do not put in rate base and
4 be allowed to recover from current customers, we will
5 allow you to capitalize an amount on that investment
6 and recover that in the future. And I think that is
7 the concept of AFPI, basically.

8 And I am not sure that this rule does that. It
9 doesn't make it real clear, as it should in my opinion,
10 that you're going to look at the prudent investment of
11 the company and that which is not allowed in rate base
12 to be recovered from current ratepayers, they can earn
13 a rate of return on it and capitalize it. If you have
14 got a five-year deal in here that says you've got to
15 stop after five years. What happens to the investment
16 that's made, was prudently incurred, everybody agrees
17 that was a good thing to do at the end of five years.
18 Do you take that amount, and do you put it in rate base
19 then? Or do you say, no; you've got to wait and
20 collect it from future customers, if they ever show up.
21 And it is probably -- if there is one thing that water
22 and sewer is treated differently in than telephone and
23 electric, it's in used and useful and what is allowed
24 in current rate base and what is put off to be
25 collected from future customers. No utility in the

1 state, except water and sewer companies, faces the
2 problem of vacant lots. You've got a piece of pipe
3 running through a vacant lot, you say it is not used
4 and useful. It's absolutely used and useful to get
5 water to the guy that's beyond that vacant lot. So,
6 this whole concept, you ought to make it real clear
7 that you're starting off with looking at the prudent
8 investment, and you are going to give the utility an
9 opportunity to earn a rate of return on that or they
10 are going to be able to capitalize that which you don't
11 put in rate base. And that basic policy ought to be
12 enunciated in these rules. And I don't think they do
13 that. I think there is threats there. I think there
14 are concerns of what is going to happen after five
15 years.

16 Let me give you an example. If a utility comes in
17 and builds a water treatment plant, and 500,000 gallons
18 of water would serve their existing customers, and they
19 don't plan long-range. But if they think -- and
20 supposing they spent half a million dollars on it. For
21 another \$100,000 they can double that capacity. And if
22 their projection shows that that is the cheapest thing
23 to do, to go ahead and build the million gallon
24 capacity today for an extra 100,000 or wait four years
25 and build another 500,000 gallon at another \$500,000,

1 obviously, this Commission would say, "Spend the
2 600,000 now, and we'll allow you to earn a rate of
3 return on that amount, which we don't allow to be
4 recovered in current rates." That, I think, would be
5 your decision. And I think you ought to make these
6 rules clear.

7 Now, what happens if at the end of five years the
8 best projections don't come true, those customers don't
9 show up that you expect, that you built -- you spent
10 the \$100,000 for? These rules say the utility has got
11 to eat it, as I understand that. But I think that's
12 wrong. I think if you say they have got to eat it that
13 means you're holding them to a standard of projection,
14 of perfection that you don't hold anybody else to. And
15 if anybody is going to make projections and be held to
16 a standard of being 100 percent accurate, I don't know
17 that person. I never met that person that could
18 project five years in advance and be accurate. We know
19 that the nice thing about projections are they are all
20 going to be wrong.

21 So, I think somewhere in these rules, and this may
22 be the place, you ought to make it clear that the
23 utilities are going to be encouraged to do long-range
24 planning and implementation of those long-range plans.
25 And that after accumulating AFPI for a period of five

1 years, any amount that has not been recovered will be
2 allowed to be recovered in future rates. Thank you.

3 COMMISSIONER CLARK: Mr. Cresse, how does that
4 jibe with the Legislature's direction? I mean, it's
5 not the Commission necessarily that chose to treat
6 water and sewer differently. It's the statute that
7 speaks in terms of used and useful.

8 MR. CRESSE: I don't know that there is anything
9 in the statute that is any different on used and
10 useful. Used and useful is a concept that has been
11 applied to telephone service, it has been applied to
12 electric service from the beginning. And there are
13 court cases on what is used and useful. And let me
14 respond. In an electric case the same principles
15 apply, that plant which is used and useful in utility
16 service. And there are court cases on it that says,
17 because they have been challenged, we have put
18 construction work in progress in rate base to be
19 recovered in current rates. This Commission has done
20 that.

21 COMMISSIONER CLARK: But not in water and sewer.

22 MR. CRESSE: I understand that. But the
23 principles of which those laws are based on are all the
24 same. And that was carried to court. It was
25 challenged, and the Supreme Court of the State of

1 Florida said, "Yes, you can put construction work in
2 progress in rate base." Now, I don't know if they told
3 Mr. Shreve that or they told somebody else that, but
4 the Commission's action in that was upheld.

5 COMMISSIONER CLARK: Mr. Cresse, but it seems to
6 me the statutory language is different for water and
7 sewer indicating a desire by the Legislature to treat
8 it differently. That's my -- that's the dilemma we
9 face, I think.

10 MR. CRESSE: Do you think the statutory language
11 prohibits you from allowing the amount of prudent
12 investment to be -- earn a fair rate of return?

13 COMMISSIONER CLARK: Well, I think the standard
14 for what can be -- what is determined to be prudent may
15 be different for the two, given the fact that -- in the
16 one instance the statute specifically mentions used and
17 useful. And I am not even sure that the statute
18 doesn't say we can't allow construction work in
19 progress for water and wastewater, but it's different
20 than the statute.

21 MR. CRESSE: If you can't allow construction work
22 in progress under the water and sewer rules, and if you
23 can't have AFPI cover an allowance on AFPI for that
24 which is prudently invested but not included in current
25 rates, then, Commissioner, you ought to be over there

1 recommending a change in the law, because that violates
2 the constitutional requirements that a utility has the
3 opportunity, and only the opportunity, to earn a fair
4 rate of return on their prudent investment. Now, if we
5 have got a law in Florida that says that can't happen
6 here because of legislative law, then, one, I think
7 that law is probably unconstitutional; and, two, I
8 think this Commission, if they believed in that
9 principle, ought to be over there telling the
10 Legislature to change the law. They have messed up
11 again. That is the reason they meet every year, is to
12 correct the prior year's mistakes, one of the reasons.

13 MR. SEIDMAN: Commissioners, I don't think that
14 violates .367. .367 says the Commission shall consider
15 the investment of the utility in land acquired or
16 facilities constructed or to be constructed in the
17 public interest within a reasonable time in the future.
18 And I think you do that. You do include work in
19 progress many times in water and sewer rate cases,
20 especially when you're doing a future test year. You
21 handle it differently than you do for electric and
22 telephone, but you still use it.

23 MR. CRESSE: Well, actually in electric and
24 telephone, construction work in progress that is going
25 to be completed within a year, it's included in current

1 rates. It's not held out. It's put right in if it is
2 going to be completed in a year. And most water and
3 sewer construction, from what Chuck Hill has taught me
4 from time to time, is really completed within a year.
5 So, it probably all ought to be recovered in current
6 rates; if you are going to apply the same fair,
7 equitable and just principles to water and sewer that
8 you apply to electric and telephone.

9 CHAIRMAN DEASON: That means we shouldn't allow a
10 return on unamortized rate case expense, then?

11 MR. CRESSE: You should --

12 CHAIRMAN DEASON: It's not rare -- I mean, it's
13 rare that I can catch you, Mr. Cresse. I just couldn't
14 resist.

15 MR. CRESSE: I guess if you looked at it in terms
16 of a tradeoff, and how badly they are treated on their
17 investment in terms of used and useful calculations, I
18 think that would be a fair tradeoff, Mr. Chairman, if
19 you trade them off equally.

20 MS. MERCHANT: I don't know if there is a
21 confusion, or maybe I am misunderstanding the
22 conversation. But I don't think that there is a rule
23 or -- the statute says that you can't earn a return on
24 construction work in progress in water and wastewater.
25 And we didn't want to establish a rule on that, because

1 we -- in certain circumstances, it's appropriate. It's
2 not in every single case that we allow construction
3 work in progress, but we would employ a projected test
4 year, and that would include real construction work in
5 progress that for that test year has been capitalized
6 as plant in service.

7 CHAIRMAN DEASON: Mr. Cresse, I guess -- what
8 specific changes are you recommending to this proposed
9 rule?

10 MR. CRESSE: I would like to have the prerogative
11 of getting back on that, sir. I have one on another
12 section of it, and it may need to be changed here. But
13 I would like to have the opportunity to draw a
14 paragraph and get it back to you at the next July, or
15 whenever it is. And as soon as I can get it written, I
16 will provide it to everybody. I think it can be
17 clarified, and I am just seeking clarification. I
18 think you ought to make it clear.

19 MR. TODD: Chairman Deason, Ms. Swain was also
20 talking about AFPI when it applied to plant that has
21 been built in the past. But it can also be used in a
22 projected rate setting basis, like for a new utility,
23 as was ours. What happens in that case is the utility
24 is still expensing the appropriate amount of the
25 depreciation expense every single year on gross assets.

1 But when you're doing a projected test case, the
2 nonused and useful portion of that amount is disallowed
3 in depreciation expense. So, you're accumulated
4 depreciation balance, if you're doing it the way we're
5 doing it, is 100 percent of the annual amount that
6 should be per the composite rate times the plant asset
7 balance.

8 CHAIRMAN DEASON: But doesn't the AFPI --

9 MR. TODD: Only on the net balance. In other
10 words, they give you the net plant balance in the
11 future, which is the AFPI and the total accumulated
12 depreciation. So in other words, you've lost the
13 amount between the used and useful portion of the
14 depreciation and what --

15 CHAIRMAN DEASON: What you're saying is the AFPI is
16 calculated on the net balance --

17 MR. TODD: That's correct.

18 CHAIRMAN DEASON: -- each year, so that as
19 depreciation expense is booked, the amount -- the base
20 upon which the AFPI is calculated --

21 MR. TODD: Is 100 percent of the depreciation
22 versus just the used and useful portion of the
23 depreciation. And that is a mismatching of funds.
24 You're not allowed the nonused -- a return through AFPI
25 on the nonused and useful portion of depreciation in

1 the current period.

2 MS. MERCHANT: If I may comment on that, the AFPI
3 charge allows the full nonused and useful depreciation
4 expense for each year. And then it's the net return,
5 the return is only on that net portion. The second
6 year the first year's depreciation is added into the
7 net balance. The third year, two year's of accumulated
8 depreciation are added into that balance. And that is
9 what the return is calculated on, but the expense
10 allows --

11 (Simultaneous conversation.)

12 CHAIRMAN DEASON: The issue is the carrying cost.

13 MS. MERCHANT: That's right.

14 MR. TODD: That's the issue.

15 COMMISSIONER CLARK: Do you understand this?

16 CHAIRMAN DEASON: Yes.

17 COMMISSIONER CLARK: Okay.

18 CHAIRMAN DEASON: Mr. Shreve? Mr. Gatlin?

19 MR. GATLIN: Thank you, Commissioners. Sam Gatlin
20 with the Office of Public Counsel. I just have a
21 couple of points of clarification.

22 One of the rules that we haven't discussed yet,
23 25-30.4335 concerns property taxes. And to be
24 consistent with what we are proposing in that rule, we
25 were proposing that property taxes be added to the AFPI

1 calculation. We agree with Staff's basic mechanics of
2 the AFPI calculation. I do have a question for
3 Patricia Merchant on her testimony, if I can ask her
4 about it.

5 CHAIRMAN DEASON: Before you do that, are you
6 saying you're in agreement with Staff's position on
7 property taxes?

8 MR. GATLIN: With the mechanics and the way they
9 compute AFPI. And just for clarification, one of the
10 proposals that we are making to 30.4335, we're
11 including nonused and useful property taxes in the AFPI
12 calculation. That is all I was clarifying there.

13 CHAIRMAN DEASON: Okay.

14 MR. GATLIN: Patricia, on Page 17 of your
15 testimony, starting on Line 17.

16 MS. MERCHANT: Okay.

17 MR. GATLIN: You state that the AFPI charge begins
18 the month following the end of the test year used to
19 establish the charge.

20 MS. MERCHANT: That's correct.

21 MR. GATLIN: We don't agree with margin reserve,
22 as you know. But if a margin reserve is allowed,
23 doesn't the margin reserve start at the end of the test
24 year?

25 MS. MERCHANT: That's true. But the margin

1 reserve was included in the used and useful portion.
2 The nonused and useful portion is what the AFPI --
3 okay. Does that answer your question. I don't know if
4 -- what I am saying here is that the charge starts
5 accumulating at that point in time, so that if they
6 don't actually implement the charge, or if it's not
7 approved by the Commission until, say, three or four
8 months later, then they would only be able to collect
9 the third month charge. They wouldn't collect -- they
10 wouldn't start collecting the first month charge. They
11 would collect the third month charge. That is what I'm
12 -- that's what the proposed rule does.

13 MR. GATLIN: The rule just seemed a little bit
14 confusing. That Paragraph 4 that you reference.

15 MS. MERCHANT: Okay.

16 MR. GATLIN: It does say at the end of the nonused
17 and useful period -- or, I'm sorry, at the end of the
18 used and useful period. It's on Page 127 of the rules,
19 Paragraph 4.

20 MS. MERCHANT: That's correct.

21 MR. GATLIN: I guess I don't understand the last
22 sentence there. "If any connection have been made
23 between the beginning date and the effective date of
24 the charge," what is that?

25 MS. MERCHANT: Okay. That is like I'm saying if

1 the test year were June 30th for AFPI, then -- and the
2 charge, obviously -- well, say, the Commission were to
3 make it's decision on July 30th, okay. The charge
4 would start accumulating July 1, and you could have
5 customers adding on between that month, but they
6 wouldn't -- there would be no charge in effect at that
7 point in time, so they couldn't be charged an AFPI
8 charge. What happens is when they do -- when the
9 charge becomes effective, and whatever date that
10 customer comes on, they pay that charge as it's
11 accumulated at that date. So, it would be one month
12 accumulated for that customer.

13 MR. GATLIN: That's all I have. Mr. Shreve wants
14 to add some comments.

15 MR. SHREVE: One second.

16 COMMISSIONER CLARK: Just so I am clear -- while
17 they're conferring, Mr. Cresse, your point is property
18 taxes should be treated differently and collected from
19 -- as if it was all attributable to used and useful
20 property?

21 MR. CRESSE: Yes, ma'am. And let me expand that
22 just a moment. Some property -- there is all kinds of
23 ways to assess property.

24 COMMISSIONER CLARK: I think we found out it's not
25 clear how they -- the thought process in figuring that

1 out.

2 MR. CRESSE: Well, some of the lawyers that deal
3 in property tax that I have talked to say that there
4 are eight basic principles that, if followed, the
5 property tax appraiser is correct. And all he has to
6 do is to justify his appraisal on the basis of one of
7 the eight. So, if he uses an income method, then using
8 the income method he might go in and, you know, if you
9 had -- then, obviously, he wouldn't be putting any
10 property tax on property that was not in rate base.
11 Because if he used the income method and looks at the
12 books and records of the utility, they don't have any
13 income for property that is not used and useful, so he
14 would probably assess it. The other thing,
15 if the assessment is not in excess of what you allow in
16 rate base, did he tax the property that wasn't included
17 in the rate base.

18 I think most significantly is the property taxes
19 are an annual recurring expense. And you don't know
20 the basis which the property taxer used. If he used
21 the right method, obviously, he probably is not taxing
22 any more than what you allowed in rate base. And to
23 capitalize that in a mortgage in the future, with
24 property taxes, is mortgaging the future of recurring
25 expenses. There is no way a utility has truly any way

1 to control what they pay in property taxes. They can
2 go down and argue, and I am sure some of them do. Most
3 of them might, I don't know. But ultimately they have
4 no control over the assessment and the level of that
5 expense, and they ought to be allowed to recover it.

6 MS. MERCHANT: I would like to respond, unless
7 somebody --

8 CHAIRMAN DEASON: Okay. Go ahead.

9 MS. MERCHANT: Addressing Mr. Gatlin's concern
10 about property taxes, that is in Rule .433. Public
11 Counsel has requested that all nonused and useful
12 property taxes be recovered in the AFPI calculation.
13 And in that rule, I had recommended that you not
14 establish a rule on property taxes because of the
15 circumstances where they are so different, in every
16 different county, as Mr. Cresse said. So, for that
17 reason, Staff recommended that no rule on property
18 taxes be made. What the AFPI rule contemplates is if
19 there is any expense where there is property taxes or
20 O&M expenses, or anything, if they were adjusted to be
21 nonused and useful, then it would be appropriate to
22 include that in the AFPI charge. We were not actually
23 making an assumption in the AFPI rule that there will
24 be an adjustment in every case.

25 And I also wanted to point out a comment that Mr.

1 Cresse made that the charge stops at five years. That
2 could be changed on a case-by-case basis, but that was
3 just the rule of thumb that we put in there. Also the
4 charge stops accruing at five years. They can collect
5 it until all the customers have connected. So, what
6 happens if you're five-year time is up and you have got
7 100 more customers? They just pay that capped charge
8 until all the customers have connected. So, it stops
9 increasing, but they still get to collect it until all
10 the customers connect. And there is the problem that
11 all those customers may not connect. But I don't
12 believe that that's something that the AFPI rule
13 contemplates. And, you know, that could be a developer
14 problem.

15 COMMISSIONER CLARK: What happens then?

16 MS. MERCHANT: They don't collect it. I mean, if
17 they didn't --

18 MR. CRESSE: Translated, does that mean they don't
19 earn a fair rate of return on that prudent investment?

20 MS. MERCHANT: On that portion that's nonused and
21 useful and customers never connect on.

22 COMMISSIONER CLARK: Well, is it even more
23 reaching in the sense that they don't earn a return on
24 or a return of their investment?

25 MS. MERCHANT: That's true. But I think the

1 question then would go back to say, "Was it really
2 prudent if" -- you know, I mean, you're getting into a
3 big "what if" situation. Because if they built this
4 big plant and then all of a sudden growth stopped
5 dramatically, and they could never fill those
6 customers, then you're talking about a bigger problem.

7 COMMISSIONER CLARK: Do we make that assessment at
8 the beginning? Do we look at what they've built for in
9 their plans and the demographics and projected
10 demographics of the area and say, yes, it looks like a
11 good plan? So, what would change it -- I mean, the
12 question is, not does it look prudent five years after
13 you have made the decision, did it look prudent under
14 those circumstances at the time you made it. So, it's
15 not going to change at five years.

16 MS. MERCHANT: That is how we base our
17 determination at that point. That's all the
18 information we have available to us. We can't read the
19 future.

20 COMMISSIONER CLARK: Nor can they.

21 MR. MERCHANT: That's correct.

22 MR. TODD: And I can address that and say that you
23 have addressed that in both of our initial
24 certifications saying that the rates and charges -- we
25 had a lot of questions at hearing upon what are these

1 growth projections? We put on professional witnesses
2 in land planning and growth management. So, I would
3 say yes.

4 MR. WILLIS: Commissioners, there is one thing
5 that has been sort of left out here in all of these
6 discussions, and that is there is a distinct difference
7 between water and wastewater companies and electric,
8 telephone and gas companies. And that is that the
9 majority of these companies were really placed there
10 because a developer wanted to develop lots, not because
11 he wanted to build a water and wastewater company.
12 That is just something that had to be done to do the
13 development.

14 Now the way a AFPI concept came about, and I'm
15 sure Mr. Cresse remembers this, is that we capped the
16 whole process at five years, because there was a
17 thinking at the time that you needed to sort of cover
18 the utility cost for what was considered a prudent
19 period. But if that growth never came about, then it
20 needed to be shifted over to the developer.

21 In other words, there was never a desire in the
22 AFPI process, this AFPI application, to reward a
23 developer or cover the responsibility of a developer in
24 his desire to develop property by covering his cost.
25 And a developer does it at his own risk. And if we

1 covered the entire asset out there, and he figured it
2 would be developed within five years and just the
3 economy fell apart, and it took 15 years, and this
4 Commission went ahead and allowed AFPI for 15 years on
5 that project, what you're doing at that point is
6 covering the developer's risk and not the risk of the
7 utility company. Because the real reason it was put
8 there was because the developer wanted to develop the
9 property.

10 COMMISSIONER CLARK: But we do have to be careful
11 that we don't want to make it so that he is unwilling
12 to take any risk at all in the sense that if he wants
13 to avoid any risk, he puts in a well and septic tank on
14 every lot.

15 MR. WILLIS: Right.

16 COMMISSIONER CLARK: And that is not what we want.
17 We want some economies of scale. So, you have to
18 balance that. I mean, you have to -- I think you have
19 to evaluate who you are dealing with and the
20 reasonableness of the projections.

21 MR. WILLIS: That's exactly right. I agree fully
22 with that. I'm a firm believer in economy of scale and
23 that's rewarding utilities for economies of scale.

24 CHAIRMAN DEASON: And doesn't the rule state that
25 for good cause shown, or something to that effect, that

1 the five years can be extended?

2 MR. WILLIS: Yes, it does.

3 MS. MERCHANT: That's correct. And we have
4 several AFPI applications that have gone seven years.
5 I can't think of any that have gone longer. But
6 several times we have done things on seven years. Five
7 years is not a scientific number, but, you know, if the
8 utility can show, then Staff and the Commission has
9 approved a longer period of time.

10 MR. CRESSE: Commissioners, the thing that I am
11 pointing out, I think, is -- of course, it gets back to
12 the used and useful and how you calculate that, and how
13 you calculate what you allow AFPI on. But the fact is,
14 after a period of time, if that's a prudent investment,
15 and if the customers that are contemplated don't show
16 up, and if there are still some vacant lots in that
17 subdivision, the entire amount should be recovered
18 through current rates. Somewhere you have to stop it.

19 CHAIRMAN DEASON: Well, that raises an interesting
20 question about growth being projected and it doesn't
21 materialize. I mean, the Commission has made decisions
22 in electric cases where there has been anticipated
23 growth in demand for electricity. And when that's not
24 materialized, we have told the utility to take some of
25 the plant out of rate base and market it on the market

1 for electric -- I mean, there are risks and the
2 Commission has the ultimate responsibility to assign
3 those risks in a fair and equitable manner. And it is
4 just -- you cannot say that a utility should be 100
5 percent insulated from any risk from demand that has
6 been projected that doesn't materialize. They
7 shouldn't have to bear 100 percent of the risk, either.
8 We have got to make a determination of what is fair and
9 in the best interest of the ratepayer and the utility.

10 And what I'm hearing you say is that if they build
11 it, they need to earn on it. And I don't think that is
12 what you mean to say.

13 MR. CRESSE: Mr. Chairman, I think one of the
14 things I'm trying to say is you ought to treat water
15 and sewer companies different than you do telephone
16 companies and electric companies. And let me give you
17 an example. If I went out and developed a 160-acre
18 lot, 160 acres of land, and I put 160 lots on it, I get
19 telephone service and I get electric service. And if I
20 was fortunate enough to get somebody to put in water
21 and sewer, I get water and sewer service. If all of
22 those three utilities come before you a year later,
23 there wouldn't be any question as to whether the
24 distribution lines running by those lots that were
25 still vacant were used and useful. There would not be

1 a question. There would not be a question as to
2 whether or not the lines, the telephone lines, that run
3 by those 160 lots, that only in the best of years have
4 about a 50 to 55 percent line fill, as to whether those
5 vacant lines were used and useful or the fact that it
6 passed over my lot there that nobody has built on is
7 used and useful. But in water and sewer, you count
8 used and useful based upon the number of vacant lots.

9 CHAIRMAN DEASON: The rule proposal right now is
10 100 percent used and useful on all the transmission
11 lines, isn't it, Mr. Cresse?

12 MR. CRESSE: I may be arguing in favor of that,
13 Mr. Chairman. And Mr. Shreve is going to be arguing
14 against it. And so maybe I'm ahead of my game. But
15 the point that I'm making is that if you start with the
16 principle, and this is the basic principle that I think
17 your rules have to be built around, that we want to
18 encourage long-term planning and long-term
19 implementation of what is least cost for your
20 ratepayers, we want to do that. And we think if you do
21 that, then you will be entitled to the opportunity to
22 earn a fair rate of return on that total investment,
23 one way or the other, whether it be in current rates or
24 we'll capitalize it. That is the principle that I am
25 asking you to think about and be sure these rules

1 permit that; in fact, require that.

2 CHAIRMAN DEASON: Okay.

3 COMMISSIONER CLARK: Mr. Chairman, I want to ask
4 you a question on the --

5 CHAIRMAN DEASON: Go right ahead.

6 COMMISSIONER CLARK: When you talk about the
7 electric, is it primarily the electricians where we have
8 taken it out and told them to market it?

9 CHAIRMAN DEASON: I think we have made decisions
10 that essentially reach that result.

11 COMMISSIONER CLARK: Well, here is my question.
12 It seems to me you -- they come in and they have to get
13 a certificate of need for a generating plant. And that
14 is our initial take that, yes, that is prudent. We
15 agree with your projections of growth and demand. And
16 what you have selected is appropriate to meet that
17 demand. We have not later gone back, after we have
18 made that decision of need and said, "We have changed
19 our mind." Haven't what we done -- what we have done
20 is say, "Demand didn't materialize; therefore, take
21 that extra power, market it somewhere, and we'll offset
22 it." So, they are in a sense, once that need is
23 determined, they are risk-free at this point.

24 CHAIRMAN DEASON: No, because we have imputed a
25 certain amount of revenue saying that it's reasonable

1 for you to market X percentage of the generation of
2 that plant. We impute those revenues and until the
3 next rate case, if they don't sell it, they are at risk
4 that they are not going to achieve their rate of
5 return. Likewise, if they sell a whole lot more, they
6 are going to do a lot better.

7 COMMISSIONER CLARK: But they are still --

8 CHAIRMAN DEASON: But they are partially at risk,
9 yes.

10 COMMISSIONER CLARK: But they are at the same risk
11 if -- with respect to if it were entirely in the retail
12 arena, because it may be what they projected in
13 consumption in the retail with that plant in it doesn't
14 materialized, and they won't earn their rate of return
15 because they won't get in retail rates what they were
16 anticipating.

17 CHAIRMAN DEASON: I assume that is possible. I
18 don't think there has been a case where we have said,
19 this -- you have got too much reserve capacity, so just
20 take this plant out of rate base. I don't think we
21 have ever done that, but we've imputed revenues.

22 MR. SEIDMAN: All of that applies to a generating
23 capacity. They are not at risk with regard to
24 distribution services. And I think that is the point
25 Mr. Cresse was making.

1 MR. SHREVE: Mr. Chairman, may I make a couple of
2 brief comments?

3 CHAIRMAN DEASON: Yes.

4 MR. SHREVE: One, we are in favor of AFPI. We
5 think the company should be entitled to recover their
6 investment. However, where I disagree with Mr. Cresse
7 and Mr. Seidman is particularly along telephone and
8 electric. The telephone company and the electric
9 company weren't involved with Deltona or Palm Coast or
10 anybody when they came in and decided to put in 1,000
11 lots here and sell those lots. They had to put water
12 and sewer utility in there to serve those lots. They
13 made a business determination to serve those lots and
14 put in the facilities that they decided to serve. The
15 customers had absolutely nothing to say about that. If
16 those projections were wrong, and they are then not
17 going to be able to use the entire facility, for Mr.
18 Cresse to say that everything should then be borne by
19 the present ratepayer is totally in error. Are they
20 going to come back in and say, look, we didn't sell but
21 500 of these lots, and we put in roads and purchases.
22 And should all the present owners of the lots come in
23 and pick up their losses? Or does Deltona go ahead and
24 go bankrupt? When these utilities come in and purchase
25 from a developer-oriented utility that put the water

1 and sewer service in to serve themselves, they should
2 step into the shoes of that utility, and not be at some
3 point in a position to pass on the cost to the present
4 customers instead of the future customers they have
5 anticipated were coming on. The electric utilities and
6 telephone utilities were not in that same position of
7 being developer-oriented in the first place.

8 COMMISSIONER CLARK: Well, then is the real
9 solution to prohibit developers from being in the water
10 and wastewater business?

11 MR. SHREVE: Absolutely not.

12 COMMISSIONER CLARK: I mean, I'm not being
13 facetious.

14 MR. SHREVE: No, absolutely not. Let them make a
15 business decision, but they are responsible for it.
16 They don't want you managing their businesses. When
17 they come in and put a water and sewer division in, it
18 is incidental to the fact that they are going to sell
19 lots. And in most cases, if you go back and really
20 check it out, and we have had some testimony in this
21 area, most of the utilities have actually recovered
22 their expenses in the sell of the lots. No, let them
23 make their business decisions. If they were out in
24 competition, they would make them and they would live
25 by those decisions. When they sell the lots that

1 customer should be responsible for supporting that part
2 of the service that they have, not a future part of the
3 service that might not have come about because the
4 company made an error in their business decision, that
5 the customer had no part in.

6 MR. CRESSE: Commissioner, may I respond.

7 CHAIRMAN DEASON: Yes.

8 MR. CRESSE: He was very complimentary to me, and
9 I appreciate it.

10 MR. SHREVE: I object to him construing that as
11 being complimentary.

12 MR. CRESSE: The point I think Mr. Shreve is
13 making is that you may have a different kind of
14 incentive, motive and different goals, and so forth,
15 with developer-owned utilities. And I think the
16 Commission does have to guard against, a little extra
17 guarding against being exploited by developer-owned
18 utilities. I don't think there is any question about
19 that, and so forth. But I think you do that. And the
20 opportunity to do that is when a developer applies for
21 a certificate, and you make your thorough examination
22 then, and you set the standards, and so forth, that you
23 want the developer to use. How much of that particular
24 system is he going to pay for? Having developers pay
25 for extensions of lines, and so forth and so on, is a

1 part of your service acquisition or your service
2 availability policy, and so forth. And there is the
3 opportunity, right when they come in to get that pot
4 right, and so forth. And, obviously, I think you have
5 to -- you have to assure that there is not the double
6 recovery that Mr. Shreve is talking about, and so
7 forth. I don't argue with that point. It's maybe how.
8 In the effort to prevent developers from getting double
9 recovery, you shouldn't also prevent, really, utilities
10 from getting adequate recovery. And so sometimes you
11 just have to guard against that. And I think
12 Mr. Shreve would agree with that, that maybe you want
13 to treat developer and regular utilities somewhat
14 separately. As he has already said, he thinks
15 telephone companies and electric companies could be
16 treated separately.

17 MR. SHREVE: I agree with Mr. Cresse that the
18 utility should be in a position to recover their full
19 investment based on their business projections. And I
20 would assume that Mr. Cresse is also agreeing that the
21 present customers should not be paying for any part of
22 the service that he is not receiving and required to
23 support.

24 MR. CRESSE: We may have reached a general
25 philosophical agreement if we each understand what the

1 other one is saying.

2 CHAIRMAN DEASON: That's a big "if".

3 MR. SHREVE: And we will have an understanding as
4 long as I'm allowed to interpret what both of us said.

5 MS. MERCHANT: Commissioners, on section number
6 five of that rule it has been suggested that it be
7 reworded to take out some excess wording, and --

8 CHAIRMAN DEASON: I'm sorry, proposed to take out
9 what?

10 MS. MERCHANT: There are too many "unlesses." To
11 change the wording to say, "Unless there is competent
12 substantial evidence presented by the utility
13 demonstrating that a different period is appropriate,
14 it is prudent for a utility to have an investment in
15 future use plant for a period of no longer than five
16 years beyond the test year."

17 MS. MOORE: That is just taking out the first
18 "unless," and reversing the order of the next two
19 phrases.

20 CHAIRMAN DEASON: I understand. Any objection to
21 that?

22 MS. MOORE: Semantics.

23 CHAIRMAN DEASON: I don't think there is any
24 objection. That's fine.

25 I have one last question about the net plant

1 versus gross plant calculation. If the utility were
2 allowed to calculate that AFPI on gross plant, and say
3 they calculate that for three years, and then there is
4 a transaction where that AFPI charge is collected from
5 the customer, what does that then do to the accumulated
6 depreciation reserve?

7 MS. SWAIN: You have an accumulation of three
8 years, and that would reduce gross plant three years
9 worth of accumulation.

10 CHAIRMAN DEASON: And you would book that at the
11 time you collect the charge?

12 MS. SWAIN: That's correct.

13 CHAIRMAN DEASON: Staff, what's wrong with that?

14 MS. MERCHANT: Well, the part that was already
15 there disappeared. The part that was already
16 accumulated just disappeared.

17 MS. SWAIN: That's right. But it has not been
18 recovered. And my statement is we simply haven't had
19 an opportunity to recover it.

20 MS. MERCHANT: But my position on that is that in
21 Ms. Swain's example in the change in depreciation rates
22 that you're matching, you don't change the expense
23 until you receive the increased revenue associated with
24 the change in depreciation rates in that example. You
25 could make that same argument on income tax accounting

1 for nonused and useful plant at the point the utilities
2 should be depreciating all of their plant, whether it
3 is used and useful or nonused and useful, because it
4 physically is depreciating. And if you didn't
5 accumulate that depreciation in used and useful rates,
6 then you could have a point in time where customers are
7 paying a full rate of return on plant that's actually
8 been physically depreciated. So, I think really what
9 you have got to do is match the two different revenue
10 requirements, used and useful and nonused and useful.
11 And then taking it into the AFPI calculation, the
12 concept takes that net plant to begin with and each
13 year is netting it out. So, if you only start at
14 gross, you've just made that other portion disappear,
15 and it just doesn't ever show up.

16 CHAIRMAN DEASON: But the premise of AFPI is to
17 allow a return on all costs associated -- all the
18 carrying costs associated with carrying that plant
19 until the charge is collected and it becomes part of
20 plant in service.

21 MS. MERCHANT: From that point that you measure it
22 forward, because what happens to all the -- if they
23 never had an AFPI charge before that -- say they had
24 two rate cases before, and the prior rate case they
25 didn't have AFPI. What happened to all of that nonused

1 and useful return? They never earned a return on that
2 plant, so I guess they just gave it up. From that
3 point all of those customers have already connected and
4 they didn't pay an AFPI charge. So, then you're coming
5 up to the next group of customers and then you're
6 looking at the accumulated depreciation that's already
7 taking place on those, on that portion of the ERC.

8 MR. SEIDMAN: You're looking at AFPI as nonused
9 rate base instead of nonused plant.

10 MS. MERCHANT: That's correct. And if they --
11 what is not in the rule --

12 MR. SEIDMAN: That is what we disagree with.

13 MS. MERCHANT: What's not in the rule, because it
14 changes on so many different circumstances, would be
15 that if you had prepaid CIAC associated with that
16 plant, Staff's recommendation and the Commission policy
17 would be that you would also net that of any prepaid
18 CIAC associated, because the utility already has that
19 CIAC on their books.

20 CHAIRMAN DEASON: But they've actually collected
21 the dollars.

22 MS. MERCHANT: That's correct. So, they shouldn't
23 earn a return on the future plant, nonused and useful
24 plant.

25 CHAIRMAN DEASON: But in regards to depreciation,

1 they have not collected those dollars until they
2 collect the AFPI charge. And in normal ratemaking,
3 depreciation expense is an expense upon which current
4 rates are based. And so when the utility charges those
5 rates, they are recovering those depreciation dollars
6 currently. So, it's only proper then to calculate
7 revenue requirements on net investment. I'm not
8 following that in regard to AFPI. It seems like the
9 company is not getting the full carrying costs on that
10 until they actually collect the dollars through the
11 depreciation. And once they collect the dollars, well,
12 then the full amount of depreciation should be
13 recognized. And that is what they said they would do.

14 MS. MERCHANT: I guess the same argument could be
15 made that a utility, for some reason, is earning less
16 than a fair rate of return. Why are they earning less
17 than a fair rate of return? That is their choice. And
18 you are not going to ever be able to go back and
19 collect that, or, you know, that would be retroactive
20 ratemaking.

21 CHAIRMAN DEASON: Let me say this. I think that
22 when the AFPI charge starts it should be based upon the
23 net investment at that time. But then on a
24 going-forward basis the mechanics should be that the
25 AFPI is always calculated on that same base until the

1 depreciation that's part of the AFPI is actually
2 received in dollars in the form of a payment. And I
3 think that's what they are saying. I thought -- at
4 first I thought they were saying that it should be
5 retroactive, that it should be based upon the net
6 plant, even though that plant was built 30 years ago
7 and has already been mostly depreciated. If that is
8 what they are saying, I disagree with that. But the
9 actual mechanics of AFPI, I agree, should be based upon
10 the amount of investment at the time the AFPI charge
11 originates and should not be reduced for depreciation
12 until the AFPI charge is collected. I think that is
13 only fair, because that gives them 100 percent carrying
14 costs on the AFPI investment when the AFPI charge
15 begins.

16 MS. MERCHANT: So, does that mean that the
17 accumulated depreciation in the calculation, it does
18 not accumulate in the calculation? That would be --
19 because you haven't collected those charges, either.

20 CHAIRMAN DEASON: Well --

21 MS. MERCHANT: I mean --

22 MR. TODD: Wait a minute. The accumulated
23 depreciation you charge is what -- that's the actual
24 current period expense that you're accumulating, but
25 you're not calculating the carrying costs on those

1 accumulated charges as they go through time. So, when
2 you calculate AFPI in five years based on future net
3 plant balance, you have not taken the average cost of
4 carrying that money over that time.

5 MS. SWAIN: Commissioner, if I filed for an AFPI
6 charge on the inception of new plant, I would do a
7 calculation based on gross plant. And I would begin
8 collecting from every single customer that connects to
9 that newly installed plant. If for some reason I wait
10 three years and do that calculation, I want to do a
11 calculation based on gross plant, but I've already
12 foregone recovering from three years of connected
13 customers. The charge will be the same. That actually
14 -- it's the same charge, the same schedule of fees, but
15 it's pushed three years in the future. It starts back
16 at the first month of accumulation, and I only recover
17 depreciation from that point forward. I don't want to
18 accumulate what I've already given up. I don't want to
19 have that as a reduction.

20 CHAIRMAN DEASON: The three years of depreciation
21 is gone. Is that correct, on a going-forward basis?

22 MS. SWAIN: Right. Because I can't go back -- the
23 way that it's done right now, by using net plant, that
24 three years of depreciation would have been used to
25 reduce what I can earn on, what my carrying cost is

1 now. I have been able to recover that. But from this
2 point forward, I want to be able to recover from all of
3 my future customers, but I've only got three more years
4 that I can recover from them. If it's -- or three
5 years that I have already given up, now I can add on.
6 And I haven't recovered from anybody yet. I want to
7 start out with gross plant as if it were a newly
8 installed plant.

9 CHAIRMAN DEASON: Okay. That is where I disagree
10 with you, then, so we're -- but what I am saying is, as
11 an example, you have got \$100-investment, \$100-plant.
12 If you carry it, and say it's \$10 a year depreciation.
13 You carry it for three years before you have an AFPI,
14 well, when that AFPI is first calculated, you're saying
15 calculate it on 100. I'm saying calculate it on 70,
16 but each year. The next year the AFPI would still be
17 calculated on 70, not on 60. And then the next year it
18 will still be calculated on 70, until it's actually
19 collected. What you're saying is even though the three
20 years have passed, AFPI should be calculated on the
21 full 100, even though you waited three years to start
22 the charge.

23 MS. SWAIN: That's right. But the reason is that
24 I have not been able to recover that depreciation
25 expense from anybody, not from current customers, not

1 from those customers that connected over three years,
2 those three years.

3 CHAIRMAN DEASON: Okay. I understand.

4 MS. MERCHANT: In her scenario the first year it
5 would be on 100 percent, the second year it would be on
6 90 percent and the third year it would be on 80
7 percent. Even though it was three years -- even though
8 it was three years out, in your scenario it would be
9 70, 60, 50. That is the way the rule -- that is the
10 way the Commission practice has been.

11 CHAIRMAN DEASON: I think it's -- maybe I am a
12 hybrid. I think it should be 70 --

13 MS. MERCHANT: All the way out?

14 CHAIRMAN DEASON: -- 70 and 70 and 70 until the
15 charge is calculated.

16 MS. MERCHANT: Okay.

17 COMMISSIONER CLARK: Mr. Chairman, it seems like
18 this is something that, for me, it would be helpful if
19 the two examples were given. You know, this is what we
20 are proposing. This is what the industry is proposing.
21 And then, you know, in a footnote you say why yours is
22 correct, and they can say why theirs is correct.

23 MS. MERCHANT: We can certainly do that.

24 CHAIRMAN DEASON: Patricia, just so I understand
25 what you're saying is that it should be, in that very

1 simple example, which we just described, that the first
2 year's charge would be based on 70 and the second year
3 charge would be based on 60.

4 MR. MERCHANT: That's correct. Each year -- in
5 each year the 100 percent of the nonused and useful
6 depreciation expense is also charged, in addition to
7 the return on the decreasing rate base components.

8 CHAIRMAN DEASON: And I guess I'm kind of
9 somewhere in the middle here. Okay. Maybe you could
10 put all three examples together.

11 MS. MERCHANT: That was my next thought. I'll do
12 all three examples.

13 CHAIRMAN DEASON: Okay.

14 MS. SWAIN: And we'll get together with Staff so
15 that we can make sure that we are all starting with the
16 same hypothetical.

17 CHAIRMAN DEASON: Okay. Very good.

18 COMMISSIONER CLARK: On the same sheet of paper.
19 I mean, as far as I'm concerned, you get together and
20 you put yours there, Trish, you put yours there, and
21 you interpret Commissioner Deason's, and it's all on
22 one sheet.

23 (Simultaneous conversation.)

24 COMMISSIONER CLARK: Well, I hope you use like
25 100.

1 MS. MERCHANT: I will make it as simple as -- as
2 simple, you know, round numbers as I can.

3 CHAIRMAN DEASON: And you can do a Cresse spread
4 sheet if you like, it just may be that long
5 (indicating).

6 MS. MERCHANT: I'll make it very simple
7 depreciation lives.

8 CHAIRMAN DEASON: Okay. I think that that
9 concludes the discussion of .434.

10 Commissioners, do you desire to give any further
11 direction to Staff at this time?

12 COMMISSIONER CLARK: No.

13 CHAIRMAN DEASON: Okay. Very well. Before we
14 conclude today --

15 COMMISSIONER CLARK: Partly because I think we
16 extended the opportunity to Mr. Cresse, and anyone
17 else, to rewrite that rule so that it incorporates the
18 concept that he thinks is appropriate with respect
19 to --

20 CHAIRMAN DEASON: Yes, he said he may have some --

21 MR. CRESSE: I promise to give you some in
22 writing. I certainly hope my lawyer fulfills that
23 promise.

24 CHAIRMAN DEASON: Have the parties had an
25 opportunity to look at the so-called noncontroversial

1 rules to see if we can go ahead and move any of those?
2 It would be nice to do that before we leave today.

3 Mr. Hoffman?

4 MR. HOFFMAN: Yes, we can stick to what I
5 originally stated to you, Mr. Chairman.

6 CHAIRMAN DEASON: Very well.

7 Commissioners, I believe Public Counsel has
8 already indicated a number of rules which they do not
9 have any problems with. And I would be inclined -- I
10 can identify those, and I would be inclined to go ahead
11 and direct Staff to incorporate those rules, which
12 would be their final version, which would incorporate
13 any minor modification that's included in Staff's
14 testimony, and have that incorporated into the final
15 version which we see in September. And according to my
16 notes, that would be Rule .090, .111, .135, .320, .335
17 and .460.

18 MR. SHREVE: Right.

19 COMMISSIONER CLARK: I move that they be left as
20 is with Staff changes and be presented in that format
21 for adoption in September.

22 CHAIRMAN DEASON: Okay. Without objection.

23 Now, I realize -- I think there were some that
24 Mr. Schiefelbein indicated that he felt may fall into
25 the category, but Public Counsel was still reviewing.

1 My question is, have you had a chance to look at those,
2 or are you going to need further time to look at those?

3 MR. SHREVE: I think we can get together on them.
4 There may be some others that will fall in the
5 category. We have some others we can agree on; they
6 may not. And they have some that I think we need to
7 look at and see. I think that we all agree that
8 Mr. Cresse can't rewrite any of them.

9 CHAIRMAN DEASON: Right.

10 MR. SCHIEFELBEIN: Absolutely.

11 MR. CRESSE: That is unanimous.

12 CHAIRMAN DEASON: Well, at least we have
13 identified six, which I think is a step forward.

14 MS. MOORE: I think here is also .060 on
15 exemptions. I don't think there were any comments on
16 that at all.

17 CHAIRMAN DEASON: Is there any problem, Public
18 Counsel, with .060?

19 Staff indicates that there were no comments filed
20 on .060.

21 MR. MANN: No, sir, there were not.

22 COMMISSIONER CLARK: I move .060 be treated the
23 same way.

24 CHAIRMAN DEASON: Without objection? You can
25 include .060 in that list as well.

1 All right. Ms. Moore, where do we stand at this
2 point? We are just going to continue where we left off
3 here today when the hearings resume in July?

4 MS. MOORE: That's correct.

5 CHAIRMAN DEASON: And you will issue all of the
6 proper notices and make sure everything is appropriate?

7 MS. MOORE: That's correct. Will there be more
8 documents being filed as part of the hearing?

9 MR. SCHIEFELBEIN: I suspect that there may well
10 be. I know we have been, as we all have been, deluged
11 with quite a bit of new information, particularly the
12 runs on used and useful. There is an awful lot to
13 digest that has gone on over the last couple and half
14 days.

15 CHAIRMAN DEASON: I think that is appropriate. I
16 just don't want to relitigate or rediscuss ground that
17 has already been covered, those rules that we have
18 already given instructions to Staff on.

19 MR. SCHIEFELBEIN: Sure. One thing that jumps to
20 mind, one of the few things that I specifically
21 remember, is the Fire Sprinkler Association's filing
22 that we were not aware of until the blue books were
23 produced here today. For all I know, we may not want
24 to respond to that. I don't know, but it was an awful
25 lot to digest in just a few minutes. So, that might be

1 something that we may want to follow up on.

2 And on that note, I would respectfully ask that if
3 we can't have a petition for intervention that would be
4 granted here, we would ask for some direction from the
5 Commission that, if possible, that when folks file
6 additional filings and comments and post-hearing
7 suggestions, or whatever you all want to call them, if
8 they would have the courtesy to provide the other -- if
9 they would be directed to have the courtesy to provide
10 copies to all the other participants. I think that
11 would be worthwhile. I realize that Ms. Moore has said
12 that is not required, but it would be required if you
13 directed them to. And it's not been a tremendous
14 problem in this case, because everyone at this table
15 and Staff has been very courteous to each other on
16 that. But there have been exceptions, and I think it
17 ought to be a requirement that that be done.

18 CHAIRMAN DEASON: Is the exception the Fire
19 Sprinkler Association, is that what you're --

20 MR. SCHIEFELBEIN: Yes. And who knows who else
21 will join us between now and --

22 CHAIRMAN DEASON: I think that Staff can just, to
23 the extent the Fire Sprinkler Association has any
24 further comments to file, I think Staff can just in a
25 very friendly manner request that they provide that to

1 everyone. They indicated that if they had known they
2 should have done that, they probably would have anyway.
3 I don't think there has been any problems with the
4 participants that are here today in attendance, and I'm
5 sure they will continue to do that. I'm just not
6 comfortable making any directive here at the Commission
7 until there is a large specific problem. And I don't
8 think we have that. We have had one isolated problem,
9 and I think that was more of a misunderstanding than it
10 was overt attempt to --

11 MR. SCHIEFELBEIN: I don't suggest that it was an
12 overt anything, but it certainly was disruptive.

13 CHAIRMAN DEASON: But I would just reiterate to
14 continue the spirit in which we are operating here and
15 be cooperative and provide information on a timely
16 basis to all participants.

17 MS. MOORE: I'm concerned that there could be a
18 participant in July who hasn't participated here, and
19 we can't require that they serve --

20 CHAIRMAN DEASON: But, Staff can communicate to
21 new participants how we generally expect persons to
22 participate in this process, and I'm sure they probably
23 would abide by those directions.

24 Is there anything further to come before the
25 Commission today?

1 MR. HOFFMAN: Mr. Chairman, would there be some
2 type of order outlining when post-hearing comments will
3 be filed following the July hearing?

4 MS. MOORE: Is it necessary to do it now? I think
5 that -- could that be taken care of in July?

6 MR. HOFFMAN: That's fine with us, just as long as
7 -- we want to make sure that we do have that
8 opportunity.

9 CHAIRMAN DEASON: We will take care of that then.
10 Thank you all.

11 MR. SCHIEFELBEIN: One other question. I'm sorry.
12 We are talking about an agenda, then, sometime in
13 September, presumably?

14 CHAIRMAN DEASON: It looks like there's -- we are
15 having some difficulty, but right now we are trying to
16 shoot for an agenda in mid-September.

17 MR. SCHIEFELBEIN: The reason I asked is we -- I
18 would assume that Staff will agree and the Commission
19 will agree to keep our various matters pending at DOAH
20 in abatement, not even waste any of our resources on
21 that matter. And the Hearing Officer over there, I
22 would think as a condition of doing that, would like to
23 know from us or whomever when we would know whether we
24 need to continue the abatement or litigate. So, I
25 guess we'll ask for something into the fall anyway and

1 see what happens.

2 CHAIRMAN DEASON: That's fine. I feel comfortable
3 we can do it in September. Right now we are shooting
4 for mid-September. It may end up being late September.
5 It just depends on how we can juggle some things on the
6 calendar.

7 MR. SCHIEFELBEIN: Thank you.

8 CHAIRMAN DEASON: Anything further? Thank you
9 all.

10 (The hearing was adjourned at 1:20 p.m.)

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CERTIFICATE OF REPORTER


STATE OF FLORIDA)

COUNTY OF LEON)

I, JANE FAUROT, Court Reporter, do hereby certify that the foregoing proceedings was taken before me at the time and place therein designated; that my shorthand notes were thereafter translated under my supervision; and the foregoing pages are a true and correct record of the proceedings.

I FURTHER CERTIFY that I am not a relative, employee, attorney or counsel of any of the parties, nor relative or employee of such attorney or counsel, or financially interested in the foregoing action.

DATED THIS 10th day of June, 1993.


JANE FAUROT
100 Salem Court
Tallahassee, Florida 32301
(904) 878-2221

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4 SWORN TO AND SUBSCRIBED TO before me, this 10th
5 day of June, 1993, in the CITY OF TALLAHASSEE, COUNTY
6 OF LEON, STATE OF FLORIDA, by the above person who is
7 personally known by me.



Melanie Y. Bradford
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