

## BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application of HYDRATECH	)	DOCKET NO. 880882-WU
UTILITIES, INC. for increase in	)	ORDER NO. 22226
water rates in Martin County.	)	ISSUED: 11-27-89
	)	

The following Commissioners participated in the disposition of this matter:

THOMAS M. BEARD  
GERALD L. GUNTER

APPEARANCES: F. MARSHALL DETERDING, Esquire, Rose, Sundstrom & Bentley, 2548 Blairstone Pines Drive, Tallahassee, Florida 32301  
On behalf of Hydratech Utilities, Inc.

ROBERT J. PIERSON, Esquire, Florida Public Service Commission, 101 East Gaines Street, Tallahassee, Florida 32399-0863  
On behalf of the Commission Staff

FINAL ORDER ESTABLISHING INCREASED  
RATES AND CHARGES FOR WATER SERVICE

BY THE COMMISSION:

CASE BACKGROUND

Hydratech Utilities, Inc. (Hydratech or utility) is a Class B utility providing service to approximately 3,500 water and 3,000 wastewater customers in Martin County. In its 1988 Annual Report, the utility reported operating revenues of \$367,147 and a net operating loss of \$15,169 for water. It also reported operating revenues of \$477,858 and a net income of \$20,772 for wastewater. Hydratech is an S corporation, owned one-third each by Harold L. Keathley, Terry M. Keathley and Gerald W. Bobo, all of whom are also land developers.

On March 8, 1989, the utility completed the minimum filing requirements (MFRs) for an increase in water rates and that date was established as the official date of filing. The test year for this docket is the twelve month period ended June 30, 1988, for the purpose of interim rates and the projected twelve month period ending December 31, 1989, for the purpose of establishing final rates. The utility has requested final

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rates designed to generate annual revenues of \$667,565 for water service. These revenues exceed the annualized test year revenues by \$310,806.

In its application, Hydratech also requested interim rates designed to generate water revenues of \$528,691. These revenues exceed annualized test year revenues by \$171,932. By Order No. 21168, issued May 5, 1989, the Commission suspended Hydratech's proposed rates and approved an interim rate increase, subject to refund, designed to allow Hydratech the opportunity to earn \$367,014 in annual water revenues. Hydratech was also ordered to file revised tariff sheets prior to implementing the interim rate increase. The utility chose not to file revised tariff sheets and the interim rates have not been implemented. It is our understanding that the utility did not believe that it would be cost effective to implement the interim increase because it was too small.

This case was originally scheduled for hearing on August 2 and 3, 1989. However, by letter dated April 7, 1989, Hydratech requested that the hearing be rescheduled because its manager and key witness would be out of the country on those dates. By Order No. 21219, issued on May 11, 1989, the Prehearing Officer, with the concurrence of the Chairman of this Commission, revised the hearing dates to August 16 and 17, 1989.

Approximately 135 customers attended the hearing and twenty-one customers offered testimony regarding quality of service. Their concerns are addressed under the discussion of quality of service.

#### STIPULATIONS

Prior to the hearing, Hydratech and the Staff of this Commission (Staff) reached a number of tentative stipulations. At the hearing, however, we directed Staff to more fully develop the issues addressed by tentative Stipulations Nos. 2 and 3. These issues are addressed under the discussion of rate base. Also at the hearing, we modified tentative Stipulation No. 6.

The following are the tentative stipulations between Staff and Hydratech:

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1. Utility plant-in-service should be decreased by \$2,534 in order to correct the methodology used to calculate the appropriate allowance for funds used during construction;
2. This issue, regarding the appropriate treatment for the costs of an abandoned well field, will be addressed under the discussion of rate base;
3. This issue, regarding the appropriate treatment for the construction costs of the replacement well, will be addressed under the discussion of rate base;
4. All plant is 100 percent used and useful without any margin reserve;
5. Accumulated amortization of CIAC and the associated amortization expense should be decreased by \$2,858 and \$5,937, respectively, in order to reflect the use of the correct composite rate and methodology;
6. The rate of return on equity to be used for interim rates, AFUDC and all other future proceedings should be established at 13.95 percent with a range of 12.95 percent to 14.95 percent;
7. Test year revenues and regulatory assessment fees should be increased by \$2,180 and \$50, respectively, to correct an error made in the projection of such revenues;
8. Projected hospital group insurance expense should be reduced by \$1,433 to reflect employee contributions;
9. Sales tax expense of \$5,091, applicable to contractual services, should be removed from test year operating and maintenance expenses;
10. The appropriate private fire protection charge should be based upon one-third of the Commission approved base facility charge; and

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11. The appropriate bills and gallons to be used to calculate final rates are 44,387 bills and 233,991,000 gallons.

Having heard no evidence to convince us otherwise, and finding them to be reasonable, we hereby approve the above stipulations.

#### QUALITY OF SERVICE

Gerald W. Bobo, General Manager and Secretary/Treasurer of Hydratech Utilities, testified that all state standards for water quality are being met. He also testified that, in its entire history, Hydratech has never been cited by the Department of Environmental Regulation (DER) for failure to meet water quality standards. Mr. Bobo testified regarding a number of awards that the utility has received, including a Safety Commendation received from the Florida Water and Pollution Control Operators Association in 1987. However, we note that these awards all apply to the wastewater system which is not a subject of this docket.

Witness Bobo stated in his rebuttal testimony that while DER's files might show that the utility's water exceeds the maximum contaminant levels (MCLs) for iron and odor, an error by the testing lab resulted in inaccurate data being supplied to DER. He further testified that the recheck results showed compliance with DER's standards. In addition, Mr. Bobo submitted a letter from the lab which explained that the original test results were in error and provided test results for the recheck samples.

Wesley Upham, Environmental Specialist in the Drinking Water Program for DER, testified concerning the utility's status with DER. While his prefiled testimony explained that the MCLs for iron were exceeded, Witness Upham stated at the hearing that the iron problem had been resolved. Witness Upham testified that, in general, the quality of Hydratech's water met DER's requirements, but that he still had some concerns, such as the locations from which samples were taken and some of the samples themselves.

Witness Upham also testified extensively about corrosivity of water, but could not actually state that Hydratech's water is corrosive. He noted that DER had recently received a

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complaint from a customer that the water is corroding his fixtures. Witness Upham stated that he intends to investigate the complaint and determine the cause.

Mr. Upham also testified that DER has received a complaint about the hardness of the water. We note, however, that hardness is an aesthetic consideration and not a health consideration. Witness Upham points out that the utility may resolve the problem through lime softening, reverse osmosis, or some other process, any of which would be costly.

Witness Upham also expressed concern that the utility is nearing the threshold which would cause it to be subject to trihalomethane (THM) monitoring. THM generation results from the use of free chlorine in the treatment process. In order to reduce THMs, the utility may need to further treat the water, possibly by ammoniation. Witness Upham's comments on treatment assume that THM testing will show that THM reduction will be required.

During the customer testimony portion of the hearing, twenty-one customers addressed several areas of concern. The specific problems identified related to the water's taste, odor, color and pressure, a recent water outage, the need for fixture replacement, the flushing of lines and the utility's responsiveness to customer inquiries.

Witness Upham addressed several of the customer concerns in his testimony. According to witness Upham, the water's odor is primarily a result of hydrogen sulfide. He also stated that the quality of service, from an operational standpoint, is about standard for utilities of a like size.

In its response to the customers' concerns, submitted after the hearing, Hydratech stated that there was no water outage as reported by the customers. Hydratech asserted that, on the date in question, an operations supervisor, who lives two blocks from the plant, noticed a drop in water pressure. He checked the plant, found some air-locking in pumps, and corrected the problem by bleeding air from these pumps. Although Hydratech's records may only indicate a reduction in pressure at the plant, these records would not show what happened out in the distribution system or in the customers' homes. Disregarding whether there was actually a water outage,

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we are encouraged to note that the utility responded quickly and corrected the problem.

From the utility's response, it appears that the pressure supplied by the company to witnesses Weise and Matson was adequate and within acceptable limits at the time of the pressure test. As for witness Matson's pressure problem, she may have a problem with the interior plumbing in her home since her pressure is always low. We note, in addition, that there was one customer who remarked that he had more pressure than he needed. To some degree, the amount of pressure required by a customer is a matter of preference. Customers become accustomed to a "normal" amount of water pressure. Considering that Hydratech's service area is long and narrow and that most of the plant and pumping equipment are located in the northern portion of the service area, periodic low pressure conditions in the southern part of the territory might occur.

Witness Hanson testified that she had lived at 7840 Shenandoah Drive for five years and had never seen the fire hydrant flushed. Witness Bobo said that the utility does not have a written policy for flushing, but its practice has been to flush hydrants at least yearly. Dead-end lines and small lines that do not have hydrants are flushed more often. He also stated that, if the company receives a complaint from a customer, it flushes the main immediately.

Hydratech provided its hydrant log book as a late filed exhibit. This exhibit indicates that the hydrant at 7851 Shenandoah Drive has been flushed five times since June, 1986. Entries for other hydrants in the area where Witness Hanson lives indicate similar flushing patterns. Accordingly, it appears that Hydratech has an adequate flushing program.

Several customers testified that Hydratech was not responsive to their inquiries. Although Hydratech did not address this complaint in its response, we note that a customer's perception of a utility's responsiveness to an inquiry or complaint can be very subjective. We hope that each customer will continue to attempt to resolve any problems at the utility level and that the utility will respond to those problems on a timely basis. However, if that fails, customers may contact the Division of Consumer Affairs of this Commission for assistance. A representative of that division attended the hearing and provided brochures to the customers explaining the policies and procedures that relate to customers.

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Upon consideration of the evidence in the record, we find that the quality of service provided by Hydratech is satisfactory.

#### RATE BASE

Our calculation of water rate base is attached as Schedule No. 1-A, with our adjustments to rate base reflected on Schedule No. 1-B. All adjustments which are self-explanatory or essentially mechanical in nature are shown on those schedules without further discussion in the body of this Order. All other adjustments are discussed below.

#### Capitalization of Taxes on Contributions- in-Aid-of-Construction (CIAC)

Prior to the Tax Reform Act of 1986 (TRA), C corporations were able to exclude CIAC from taxable income under Internal Revenue Code (IRC) Section 118(b). Hydratech, an S corporation, argued that this provision also applied to it and that it should, therefore, be allowed to capitalize, as intangible plant, the amount of tax that would be payable on CIAC. Hydratech sponsored the testimony of three witnesses on behalf of its position.

Utility witness Jackson testified that the purpose of Subchapter S is to allow an S corporation to perform in a manner similar to a partnership, yet retain the attributes of a corporation. He testified that, under IRC Section 1371, the rules, regulations and case history that have been established under Subchapter C are applicable to an S corporation. Witness Jackson also stated that, prior to 1987, S corporations were able to use IRC Section 118(b). In support of that contention, he testified that, although many transactions involved in determining the taxable income of an S corporation can be subject to the conduit principle of partnership taxation, he believes that the entity maintains its status as a legal and taxable corporation. He further stated that IRC sections specifically applicable to corporations will be applicable to S corporations unless there is a specific statutory exclusion. However, on cross examination, he admitted that an S corporation calculates income more like an individual than a corporation.

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Utility witness Nixon testified that the taxability of CIAC constitutes an equity cost for the shareholder. Mr. Nixon argued that suspended losses of an S corporation, which are similar to net operating losses (NOLs) in a C corporation, should be capitalized when they have been actually consumed to pay the tax on the CIAC. He contended that Hydratech should be allowed to capitalize these losses because they were funded by stockholders and not by customers or contributors of CIAC. He agreed, however, that this Commission does not allow C corporations to capitalize NOLs.

The essence of utility witness Leslie's testimony was that he, along with a number of other outside practitioners, agrees with Mr. Jackson's interpretation of the IRC.

Staff witness Brand's position was that IRC Section 118(b) did not apply to S corporations and that CIAC was, therefore, taxable income to them both before and after its amendment under the TRA. In support thereof, witness Brand testified that, under IRC section 1363(b), the taxable income of an S corporation is computed in the same manner as that of an individual, with four exceptions. The first exception is that items of income, loss, deduction, or credit, the separate treatment of which could affect the tax liability of any shareholder, must be stated separately. The second exception is that certain deductions listed in IRC Section 703(a)(2), such as personal exemptions and charitable contributions, may not be deducted. The third exception is that organizational expenses may be amortized over 60 months. The fourth exception is that the special rules in IRC Section 291, relating to corporate preference items, apply in certain circumstances.

In response to Mr. Jackson's testimony, Ms. Brand testified that IRC Section 1371(a)(1) only applies to Subchapter C. She further testified that IRC Section 1371(a)(1) does not make code sections of other subchapters, such as IRC Section 118(b), which is from Subchapter B, applicable to an S corporation.

In response to Mr. Nixon's testimony, Staff witness Brand testified that, since the shareholders of Hydratech did not actually pay income taxes, there really is no cost to capitalize. The shareholders did not pay taxes because all taxable income passed through to them was offset by net operating loss carry-forwards. Ms. Brand also testified that, since the shareholders of Hydratech have no equity in the



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corporation, they cannot have funded the utility's net operating losses. Although the shareholders have no equity, Ms. Brand agreed that they have a deficit in retained earnings. She testified that this deficit could be a result of accelerated depreciation, expenses being greater than revenues or any other variety of reasons. Due to the magnitude of the deficit, Ms. Brand agreed that it was caused by something more than accelerated depreciation. However, she contended that the funding for the losses could have come from additional debt or some other source not reflected on the books, and not necessarily from the shareholders.

Finally, witness Brand testified that C corporations are allowed to earn a return on income taxes actually paid on CIAC by including such amounts in rate base as prepaid (debit deferred) taxes. By definition, only those taxes actually paid qualify for this treatment. Since an S corporation pays no corporate level tax, there can be no prepaid tax on which to earn a return. In cases where taxes are paid on CIAC by the shareholders, the taxes paid will be recovered through the tax depreciation benefit of the contributed plant. This tax return depreciation will be passed through to the shareholders of an S corporation as a reduction in the taxable income to be included on the individual returns of the shareholders.

Since Hydratech's shareholders have no equity and have paid no taxes on CIAC, the utility has no investment in CIAC taxes on which to earn a return. We, therefore, find that the capitalization of Hydratech's tax liability as intangible plant is improper and should be removed. Accordingly, we have removed the average balance of \$240,113 in capitalized income taxes on CIAC from utility plant-in-service, with corresponding reductions of \$8,931 to the average balance of accumulated depreciation and \$9,132 to depreciation expense.

#### Abandoned Well

On May 16, 1988, a property adjacent to the proposed site for Well No. 10 was sold for use as an auto dealership. On June 13, 1988, the South Florida Water Management District issued a permit to allow Hydratech to drill the well. Hydratech completed its construction of the well on July 12, 1988. On September 30, 1988, DER issued a permit for the well, pump and raw water main.

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On October 25, 1988, Martin County adopted an ordinance, entitled the Wellfield Protection Ordinance, which limited certain uses of land within 500 feet of public water supply wells. The ordinance rendered the auto dealership property unusable.

The auto dealership asked the utility to remove the well in order to make its property usable, and informed Hydratech that it would pursue legal action if the well was not removed. The utility was advised by its attorneys that the cost of such litigation might be between \$50,000 and \$100,000. The utility was also advised that it was doubtful that it would be able to recover legal fees and costs from the auto dealership, even if the utility prevailed. In addition, it was unclear whether the Wellfield Protection Ordinance would provide a defense to the utility in such a suit.

Since litigation over the well could easily have been more costly than abandonment, the utility believes that it was prudent to abandon the well and amortize the costs over a five year period. Hydratech argues that its treatment of the abandonment is consistent with the NARUC System of Accounts and with general regulatory theory, unless it is found to be imprudent. We find no evidence to indicate that the utility acted in an imprudent manner.

This Commission's practice regarding abandonments has been to determine the amortization period by dividing the net loss by the sum of the annual depreciation expense and the return, in dollars, that would have been allowed. Broadview Utilities Corporation, Docket No. 810403-WS, Order 10984, issued July 12, 1982. Applying this methodology, it appears that the utility's request for a five-year amortization period is reasonable.

Based upon the discussion above, we find that the utility's abandonment of the well was a prudent management decision. Accordingly, we find that \$18,538, the cost of Hydratech's abandonment of the well, should be amortized over a five-year period, for an amortization expense of \$3,708, and a deferred debit of \$9,269 to be included in working capital.

#### Replacement Well

Hydratech originally requested an average balance of \$70,850 in utility plant-in-service for Well No. 10. As

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discussed above, the utility abandoned this newly constructed well in 1988. The cost to construct the replacement well is actually \$29,547 greater than the year-end cost of \$149,429 originally reported but, since construction was begun later than expected and due to the effects of averaging, the revised average balance should be \$68,837.

Notwithstanding the above, we note that the utility does not have a lease for the land where its replacement well is located. There is a proposed lease with Centel Cable Company; however, the utility was unable to provide information as to what the final terms of the lease would be.

Under Rule 25-30.035(3)(f), Florida Administrative Code, a utility is required to provide evidence that it owns the land where the utility treatment facilities are located or a copy of the agreement which provides for continuous use of the land. When questioned as to whether Hydratech would sign the proposed lease if the lease term was shorter than acceptable to the utility, witness Bobo stated that he did not know.

Since it is questionable, at best, whether an acceptable lease will be obtained or whether the utility will ever bring the replacement well on-line, it is difficult to find that the cost of the replacement well is a prudent investment. This is particularly true in light of the fact that this well is a replacement for one which was already abandoned.

Based upon the discussion above, we have removed \$70,850, the utility's reported average cost for the replacement well, from utility plant-in-service, with corresponding reductions of \$667 to accumulated depreciation and \$2,245 to depreciation expense.

#### Working Capital

Hydratech used the balance sheet approach to calculate its working capital. The balance sheet approach generally defines working capital as current assets and deferred debits that are utility related and do not already earn a return, less current liabilities, deferred credits, and operating reserves that are utility related and upon which the company does not earn a return. Utility witness Nixon testified that this method is the one which has been preferred by the Commission.

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Commission practice is to include the average unamortized balance of deferred rate case expense in the working capital allowance calculated using the balance sheet approach. Deferred rate case expense represents an investment by the utility which will not be recovered for several years due to amortization. By including this deferred debit in the working capital allowance, the utility's average investment is reflected and included in rate base to earn a return. In its application, Hydratech estimated rate case expense based upon this case being processed as proposed agency action. Since this case was subsequently taken to hearing, Hydratech incurred additional expenses. Based upon our discussion of rate case expense further within this Order, we find that working capital should be increased by \$37,737 to reflect these additional expenses. This brings the average balance of deferred rate case expense to be included in working capital to \$72,768.

As discussed above, we also found that a deferred debit of \$9,269 should be included in working capital for the abandoned well.

Based upon Hydratech's application and the discussion above, we find that the appropriate working capital allowance is \$107,319.

#### Rate Base

Upon consideration of Hydratech's application and the adjustments discussed above, we find that the appropriate thirteen-month average rate base is \$892,501.

#### COST OF CAPITAL

Our calculation of the appropriate cost of capital is based upon the application of policy and is derived as shown on Schedule No. 2. Hydratech's net equity is negative. Accordingly, it is inappropriate to establish a return on equity for this proceeding. We note, however, that we have approved a rate of return on equity of 13.95 percent to be used for all future proceedings, including interim rates and AFUDC applications, as reflected by Stipulation No. 6.

Using the utility's adjusted capital structure with each item reconciled on a pro rata basis, we find that Hydratech's appropriate overall rate of return is 12.60 percent.

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#### NET OPERATING INCOME

Our calculation of the appropriate amount of test year net operating income (NOI) is attached as Schedule No. 3-A, with our adjustments shown on Schedule No. 3-B. All adjustments which are self-explanatory or essentially mechanical in nature are shown on those schedules without further discussion in the body of this Order. All other adjustments are discussed below.

#### Rate Case Expense

In its application, Hydratech estimated rate case expense to be \$66,330, based upon this case being processed as proposed agency action. Since the case was subsequently taken to hearing, the utility revised its estimate of total rate case expense to \$150,263. At the hearing, a number of questions were raised through cross examination, which we believe deserve some discussion.

One of our questions concerns whether there was any duplication of work done by the utility's original attorney and its current attorney. Under cross examination, witness Bobo testified that none of the work was duplicative. He also testified that a number of meetings were held regarding test year approval because Staff had recommended that the utility use a projected rather than an historic test year. According to Mr. Bobo, those meetings increased the expense involved in obtaining test year approval. Witness Bobo further testified that he examined the bills overall to see if they were reasonable, based upon the number of hours spent, and that he found them to be justified. We believe that the utility has met its burden to show that there has been no duplication of work. Accordingly, we have made no adjustment for charges by Hydratech's original attorney.

The next area of concern is for charges for the utility's review of Staff's recommendation on interim rates. Interim rates were based on an historic test year ended June 30, 1988. Hydratech requested a pro forma adjustment of \$1,467,477 for additions made in December, 1988. Since Staff's recommendation was to disallow this adjustment, the utility expended considerable time and effort to have the adjustment included in rate base for interim rate purposes.

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At the hearing, witness Nixon agreed that it is Commission policy to use only an historic average or end of period rate base for determining interim rates. However, Mr. Nixon argued that the Commission diverged from this policy in Docket No. 840033-WS, the application by Clay Utility Company for increased rates. In that case, DER had required the utility to add an advanced wastewater treatment plant. By Order No. 13294, issued May 17, 1984, this Commission allowed that plant to be included in construction work in progress for interim rate purposes. The basis for that exception was Section 367.081(2), Florida Statutes, which requires this Commission to consider the investment of the utility in property required by duly authorized governmental authorities.

Mr. Nixon argued that the Clay Utility Company exception should apply in this case because, by Order No. 18367, issued November 2, 1987, the Commission essentially ordered Hydratech to construct the pro forma plant in question. We note that Order No. 18367 grew out of an investigation into the level of Hydratech's earnings in which we found that, as of December 31, 1986, the utility was 124 percent contributed. Hydratech was allowed to retain its service availability charges, however, based upon certain proposed plant improvements which would reduce its percentage of contribution to an acceptable level. In other words, Hydratech made those improvements in order to keep its service availability charges, not because it was ordered to do so by this Commission. Accordingly, we do not believe that the Clay Utility Company exception applies to Hydratech.

Witness Bobo testified that Hydratech's attorney spent approximately fifteen hours on the recommendation for interim rates and approximately \$100 in out-of-pocket expenses. Witness Nixon testified that he spent approximately six hours on the recommendation for interim rates. The total cost for Hydratech's review of the recommendation on interim rates appears, therefore, to be \$2,485. Since the utility was aware of Commission policy regarding pro forma adjustments for interim rate purposes, we have removed this amount from rate case expense.

The next question concerns the prudence of certain charges for work done by witness Leslie, the utility's local accountant. Witness Leslie provided a breakdown of rate case expense for the preparation of various MFR schedules. Based

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upon our review of that information, we believe that this expense is reasonable for the amount of work involved. However, the expenditures for Mr. Leslie to provide testimony regarding the capitalization of taxes on CIAC appear to be unnecessary. Mr. Leslie stated that it was necessary for him to testify on that issue, in addition to the other two utility witnesses, because his experience in tax is somewhat different from that of the other witnesses. Upon review of Mr. Leslie's testimony, however, we find most of his arguments to be merely duplicative of those of the other witnesses. We have, therefore, removed the costs for his tax research, preparation of testimony and attendance at the hearing, estimated by Mr. Leslie to be \$1,380, from rate case expense.

The fourth area of concern is the estimated expense for a motion for reconsideration. According to Hydratech, the estimated cost of such a motion is \$4,625. Since this expense has not been incurred, we have removed \$4,625 from rate case expense. If a motion for reconsideration is filed, a determination should be made at that time as to the reasonableness of the amounts requested and whether inclusion of those amounts are appropriate.

Witness Bobo testified that rate case expense, both actual and estimated, should be added to \$3,762, the amount of unamortized rate case expense from the utility's last rate investigation as of the date of the Commission's final order, and that the sum of these two figures should be amortized over a four-year period. This is in line with Commission policy on the amortization of rate case expense.

Based upon the discussion above, we find that the appropriate amount of current and prior rate case expense is \$145,535. We further find that the appropriate annual amortization amount to include in operating and maintenance (O & M) expense is \$36,384, which reflects an increase of \$18,868 to O & M expenses.

#### Pro Forma Rent Expense

In its application, Hydratech requested approval for a pro forma expense to lease a site for Well No. 10. Hydratech originally estimated that the monthly expense would be \$550. At the hearing witness Bobo referred to a proposed lease between Hydratech and Centel Cable Company for \$500 per month.

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However, he also testified that the lease had not yet been finalized. He further testified that the proposed term of the lease was fifty years, but that Centel Cable Company was not comfortable with the proposed term and wanted something shorter. Mr. Bobo was unable to say how long the lease term would be.

As addressed in our discussion of the appropriate rate base treatment for the well, a utility must either own or have a long-term lease for the land upon which its treatment facilities are located. The utility has made no such showing. It does not have a current lease and cannot describe what the terms of such a lease might be. Since it is so speculative, we cannot determine whether this lease will be a prudent expenditure. We have, therefore, removed the entire estimated pro forma rent expense of \$6,600 from O & M expenses.

#### Employee Compensation Plan

Hydratech proposed an annual expense of \$10,485 for an employee compensation plan. Witness Bobo testified that the utility believes that the plan is necessary in order for it to retain good, qualified employees. To demonstrate that this plan is intended solely for the purpose of retaining such qualified employees and not as a benefit to the owners of the utility, Hydratech has excluded all owner-employees from participation in this plan. Mr. Bobo testified that Hydratech found it necessary to use a compensation plan rather than a qualified pension plan because, under IRC Section 414(b), it was unable to adopt a new plan for utility employees without extending it to the employees of a related company.

Under its plan, Hydratech proposes to accrue an amount equal to fifteen percent of each non-owner employee's annual base salary, excluding overtime, for each year. The utility will pay this amount on or before December 31 of each year to each employee who has been employed by the utility in a non-temporary position and who has averaged 35 or more hours of work per week for at least three consecutive months. The utility has committed itself to this program under a corporate undertaking.

Upon consideration of the above, we find that the employee compensation plan is a prudent expense. We have, therefore, allowed the entire amount in O & M expenses.



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NOI

Based upon the utility's application and the adjustments discussed above, we find that the appropriate amount of test year NOI is \$112,455.

REVENUE REQUIREMENT

Upon consideration of Hydratech's application and the calculations and adjustments discussed above, we find that the appropriate water revenue requirement, which will give the utility the opportunity to earn a 12.60 percent return on its investment, is \$641,535. This amount represents an increase of \$252,878 (65.06 percent) in annual water revenues.

RATES AND CHARGES

Miscellaneous Service Charges

Hydratech's current miscellaneous service charges were approved by this Commission by Order No. 20457, issued December 15, 1988. In its application, the utility proposed several increases to its approved miscellaneous service charges.

Hydratech's first request is for charges of \$15 for locking and \$15 for unlocking a meter. In witness Bobo's testimony, he stated that the proposed meter locking/unlocking charges are for initial connections and normal and violation reconnections. Since two trips are required, witness Bobo argues that the charge should be \$15 per trip for a total of \$30 for each such connection.

During cross examination, Witness Bobo agreed that the existing charge anticipates two trips for each initial connection and each normal and violation reconnection. Upon further questioning regarding the cost justification for the proposed charges, he responded that, "we are not really going to argue this too much."

We do not find sufficient justification in the record to support a doubling of the charges for initial connections and normal and violation reconnections. Accordingly, we hereby reject Hydratech's proposed charges for initial connections and normal and violation reconnections.

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Hydratech also requested an after-hours reconnection charge of \$33.50. In his testimony, witness Bobo stated that the utility's regular business hours are 9:00 a.m. to 5:00 p.m., Monday through Friday. He further stated that the utility pays its field men a minimum of one hour of overtime pay if they are called out for any after-hours work. These calls occur often, especially during the winter season when most of the part time residents return to their homes. He stated that, if such a charge is not approved, the utility's only alternative will be to discontinue providing after-hours reconnections and provide that service only during normal business hours.

We are persuaded by the utility's argument. If a customer requests a reconnection after hours, that customer, not the general body of ratepayers, should bear the cost. Accordingly, we hereby approve the proposed \$33.50 after-hours reconnection fee.

Based upon the discussion above, we hereby approve the following miscellaneous service charges:

<u>Miscellaneous Service</u>	<u>Current Charge</u>	<u>Proposed Charge</u>	<u>Approved Charge</u>
Initial Connection	\$15.00	\$30.00	\$15.00
Normal Reconnection	15.00	30.00	15.00
Violation Reconnection	15.00	30.00	15.00
After-Hours Reconnection	N/A	33.50	33.50
Premises Visit	10.00	10.00	10.00

#### Reinspection Charge

The utility proposes to charge \$13.50 for a reinspection of a customer installation after the first free inspection. The utility inspects the manner in which the customer's service line has been connected to the water meter and whether the meter has been tampered with or damaged by the customer's plumber during installation. It also determines whether the plumber has connected the proper unit to the meter. In his testimony, witness Bobo stated that, without the charge, the cost of reinspections will be borne by the general body of ratepayers.

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The utility's proposed charge for reinspection of customer installations is consistent with inspection fees normally approved for other utilities. We agree that, if more than one inspection is required, the customer should be responsible for paying the utility's cost for the additional inspections. Accordingly, we hereby approve the proposed \$13.50 reinspection charge.

#### Meter Installation Charges

Hydratech does not have currently approved meter installation charges. The cost of the meter is included in its plant capacity charge. In its application, Hydratech requested a meter installation charge of \$100 for a 5/8 inch by 3/4 inch meter and actual cost for larger meter sizes.

In his testimony, witness Bobo stated that because of the small number of larger meter sizes installed in the past, the utility has not calculated its costs for installing those meters. He stated that, unless we approve the utility's proposal to charge actual costs for installing meters of 1 inch and larger, all customers will subsidize, to some extent, any additional customers added to the system.

Witness Bobo testified that a 1 inch meter costs \$87, a 1-1/2 inch meter costs \$153 and a 2 inch meter costs \$339. He testified that the labor cost to install a meter increases with size, because of the time involved, but not proportionately. He did not offer testimony as to what the labor cost should be.

The proposed meter installation charge of \$100 for the 5/8 inch by 3/4 inch meter includes \$64 for materials and \$36 for labor. We believe that these costs are reasonable. However, we are not persuaded that the costs for installing the larger meters varies sufficiently to preclude setting a charge for the 1, 1-1/2 and 2 inch meters. Upon consideration of witness Bobo's testimony that labor costs increase non-proportionately with meter size, and the above information on 5/8 inch by 3/4 inch meters, we believe that the labor costs should be no more than \$40 for a 1 inch meter, no more than \$44 for a 1-1/2 meter and no more than \$48 for a 2 inch meter.

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Based upon the discussion above, we find that the following meter installation charges are appropriate.

<u>Meter Size</u>	<u>Installation Charge</u>
5/8 inch x 3/4 inch	\$100.00
1 inch	127.00
1-1/2 inch	197.00
2 inch	387.00
over 2 inches	Actual Cost

Temporary Hydrant Meter Charge

Hydratech does not currently have a charge for temporary hydrant meters. This type of meter is installed on the outlet of a fire hydrant and is often used during construction to obtain water from an existing hydrant while developers' mains are under construction. Hydratech's proposed charge for such a meter is \$95.

In his testimony, witness Bobo stated that some of the materials used in such an installation can be reused anywhere from one to ten times. He also testified that this was taken into account in the calculation of the proposed charge. Mr. Bobo believes that the full cost of a temporary hydrant meter, including the parts that can be reused, would be over \$400.

Upon consideration, we are persuaded that the utility's proposed charge is appropriate. Accordingly, we hereby approve the proposed \$95 temporary hydrant meter charge.

Service Line Installation Charges

Hydratech also requested approval of separate service line installation charges for those installations which require road crossings (\$448) and those which do not (\$218).

Witness Bobo testified that these charges will only apply where service lines do not exist. For example, in some portions of the utility's service area a main may be installed through an existing development to serve an adjacent developer's new project. If a resident in the existing area

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desired service from Hydratech in lieu of his private well, service lines would have to be installed from the main to provide water to the resident. In some cases, the main will be on the same side of the road as the resident's home requesting service. In other cases, the main is on the opposite side of the road. Martin County requires the road crossings to be installed with a casing pipe that is jacked and bored under the roadway. After the casing is installed, the service line is inserted through the casing.

Upon consideration, we believe that the utility's proposed service installation charges, for those areas where service lines do not already exist, appear reasonable. Accordingly, we hereby approve the proposed service installation charges of \$218 without a road crossing and \$448 with a road crossing.

#### Rates For Water Service

Based upon all of the previous discussions, we find that the final approved rates for this utility should be designed to produce annual revenues of \$641,535 for water service, using the base facility charge rate structure. It is our policy to use the base facility charge structure for setting rates because of its ability to track costs and to give the customers some control over their water bills. Each customer pays his pro rata share of the fixed costs necessary to provide service through the base facility charge and only his actual usage through the gallonage charge. These final approved water rates are uniform for residential and general service customers.

We note that Hydratech never filed revised tariff sheets to implement the interim rates authorized by Order No. 21168. We also note that, as addressed under our discussion regarding the stipulations, the final rates include rates for private fire protection, which the utility did not previously have.

On the following pages are comparisons of the utility's existing rates, its proposed rates and those approved by this Commission.

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MONTHLY RATES - WATER

Residential Service

	<u>Current</u>	<u>Utility Requested</u>	<u>Commission Approved</u>
<u>Base Facility Charge</u>			
<u>Meter Size</u>			
5/8 inch x 3/4 inch	\$ 2.61	\$ 4.84	\$ 6.89
1 inch	6.53	12.10	17.22
1-1/2 inch	13.04	24.20	34.44
2 inch	20.87	38.72	55.10
<u>Gallonage Charge, per 1,000 gallons</u>	\$ 1.03	\$ 1.78	\$ 1.14

General Service

	<u>Current</u>	<u>Utility Requested</u>	<u>Commission Approved</u>
<u>Base Facility Charge</u>			
<u>Meter Size</u>			
5/8 inch x 3/4 inch	\$ 2.61	\$ 4.84	\$ 6.89
1 inch	6.53	12.10	17.22
1-1/2 inch	13.04	24.20	34.44
2 inch	20.87	38.72	55.10
3 inch	41.74	77.44	110.20
4 inch	65.21	121.00	172.19
6 inch	130.43	242.00	344.37
<u>Gallonage Charge, per 1,000 gallons</u>	\$ 1.03	\$ 1.78	\$ 1.14

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Private Fire Protection Service

	<u>Utility Requested</u>	<u>Commission Approved</u>
<u>Base Facility Charge</u>		
<u>Meter Size</u>		
2 inch	\$ 12.91	\$ 18.37
3 inch	25.81	36.73
4 inch	40.33	57.40
6 inch	80.67	114.79

Effective Date

The rates approved herein shall be effective for meter readings on or after thirty days from the stamped approval date on the revised tariff sheets. The miscellaneous service, reinspection, meter installation, temporary hydrant meter and service line installation charges approved herein shall be effective for services rendered on or after the stamped approval date on the revised tariff sheets. Prior to its implementation of the approved rates and charges, the utility shall have filed and received approval of revised tariff sheets and a proposed customer notice. Pursuant to Rule 25-22.0406(9), Florida Administrative Code, Hydratech shall provide a copy of this notice to its customers with the first regular billing under the rates approved by this Order.

Refund Requirement

Since Hydratech never placed its approved interim rates into effect, no refund is appropriate for this proceeding.

CONCLUSIONS OF LAW

1. This Commission has jurisdiction to establish Hydratech's rates and charges pursuant to Chapter 367, Florida Statutes.

2. As the applicant in this case, Hydratech has the burden to prove that its proposed rates and charges are justified.

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3. The rates and charges approved herein are just, reasonable, compensatory, not unfairly discriminatory and are in accordance with the requirements of Section 367.081, Florida Statutes and other governing law.

Upon consideration of the foregoing, it is

ORDERED by the Florida Public Service Commission that the application by Hydratech Utilities, Inc. for increased rates and charges for water service is hereby approved to the extent set forth in the body of this Order. It is further

ORDERED that each of the stipulations contained in the body of this Order is hereby approved in every respect. It is further

ORDERED that each finding contained in the body of this Order is hereby approved in every respect. It is further

ORDERED that all matters contained herein, whether in the form of discourse or schedules attached to this Order are, by reference, expressly incorporated herein. It is further

ORDERED that the increased rates for water service approved herein shall be effective for meter readings taken on or after thirty (30) days from the stamped approval date on the revised tariff sheets. It is further

ORDERED that the miscellaneous service, reinspection, meter installation, temporary hydrant meter and service line installation charges approved herein shall be effective for services rendered on or after the stamped approval date on the revised tariff sheets. It is further

ORDERED that, prior to its implementation of the rates and charges approved herein, Hydratech Utilities, Inc. shall submit a proposed customer notice explaining the increased rates and charges and the reasons therefor. It is further

ORDERED that, prior to its implementation of the rates and charges approved herein, Hydratech Utilities, Inc. shall submit revised tariff sheets. These tariff sheets will be approved upon Staff's verification that they accurately reflect this Commission's decision and upon Staff's approval of the proposed customer notice. It is further



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ORDERED that Docket No. 880882-WU be and is hereby closed.

By ORDER of the Florida Public Service Commission,  
this 27th day of NOVEMBER, 1989.

  
\_\_\_\_\_  
STEVE TRIBBLE, Director  
Division of Records and Reporting

( S E A L )

RJP

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

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HYDRATECH UTILITIES, INC.  
SCHEDULE OF WATER RATE BASE  
PROJECTED TEST YEAR ENDED DECEMBER 31, 1989

SCHEDULE NO. 1-A  
DOCKET NO. 880882-WU

COMPONENT	TEST YEAR PER UTILITY	UTILITY ADJUSTMENTS	ADJUSTED TEST YEAR PER UTILITY	COMMISSION ADJUSTMENTS	COMMISSION ADJUSTED TEST YEAR
1 UTILITY PLANT IN SERVICE	\$ 3,139,090	\$ 0	\$ 3,139,090	\$(313,497)	\$ 2,825,593
2					
3 LAND	25,852	0	25,852	0	25,852
4					
5 NON-USED & USEFUL COMPONENTS	0	0	0	0	0
6					
7 C.W.I.P.	0	0	0	0	0
8					
9 C.I.A.C.	(1,938,850)	0	(1,938,850)	0	(1,938,850)
10					
11 ACCUMULATED DEPRECIATION	(352,760)	0	(352,760)	9,598	(343,162)
12					
13 AMORTIZATION OF C.I.A.C.	218,607	0	218,607	(2,858)	215,749
14					
15 ADVANCES FOR CONSTRUCTION	0	0	0	0	0
16					
17 WORKING CAPITAL ALLOWANCE	0	60,313	60,313	47,000	107,319
18					
19 RATE BASE	\$ 1,091,939	\$ 60,313	\$ 1,152,252	\$(259,751)	\$ 892,501
20					

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HYDRATECH UTILITIES, INC.  
 ADJUSTMENTS TO RATE BASE  
 PROJECTED TEST YEAR ENDED DECEMBER 31, 1989

SCHEDULE NO. 1-B  
 PAGE 1 OF 1  
 DOCKET NO. 880882-WU

EXPLANATION	WATER ADJUSTMENTS
-----	
1 UTILITY PLANT IN SERVICE	
2	
3 A. To reflect correct methodology in	
4 computing AFUDC. Audit Exception 3.	\$ (2,534)
5	
6 B. To remove capitalized income tax on CIAC.	
7 Audit Disclosure 2.	(240,113)
8	
9 C. To reflect disallowance of well no. 10 costs.	(70,850)
10	
11 NET ADJUSTMENT	\$ (313,497)
12	=====
13	
14 ACCUMULATED DEPRECIATION	
15	
16 A. To reflect disallowance of depreciation on	
17 well no. 10.	\$ 667
18	
19 B. To remove depreciation on capitalized income	
20 tax on CIAC. Audit Disclosure 2.	8,931
21	-----
22 NET ADJUSTMENT	\$ 9,598
23	=====
24	
25 AMORTIZATION OF C.I.A.C.	
26	
27 A. To reflect the use of the correct composite	
28 rate and methodology to calculate amortization of	
29 C.I.A.C. Audit Exception 1.	\$ (2,858)
30	=====
31	
32 WORKING CAPITAL ALLOWANCE	
33	
34 A. To include the average balance of the	
35 abandoned well field in working capital.	
36 capital.	9,269
37	
38 B. To include the average balance of	
39 deferred rate case expense in working capital.	37,737
40	-----
41 NET ADJUSTMENT	\$ 47,006
	=====

HYDRATECH UTILITIES, INC.  
 CAPITAL STRUCTURE  
 PROJECTED TEST YEAR ENDED DECEMBER 31, 1989

SCHEDULE NO. 2  
 DOCKET NO. 880882-WJ

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DESCRIPTION	ADJUSTED TEST YEAR PER UTILITY	WEIGHT	COST	WEIGHTED COST	COMMISSION		WEIGHT	COST	WEIGHTED COST
					PRO RATA RECONCIL.	BALANCE PER COMMISSION			
LONG TERM DEBT	\$ 3,824,829	99.04%	12.64%	12.52%	\$ (2,940,927)	\$ 883,902	99.04%	12.64%	12.52%
SHORT TERM DEBT	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%
CUSTOMER DEPOSITS	37,210	0.96%	8.00%	0.08%	(28,611)	8,599	0.96%	8.00%	0.08%
PREFERRED STOCK	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%
COMMON EQUITY	0	0.00%	0.00%	0.00%	0	0	0.00%	13.95%	0.00%
INVESTMENT TAX CREDITS	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%
DEFERRED INCOME TAXES	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%
OTHER CAPITAL	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%
TOTAL CAPITAL	\$ 3,862,039	100.00%		12.60%	\$ (2,969,538)	\$ 892,501	100.00%		12.60%

RANGE OF REASONABLENESS

LOW HIGH

EQUITY

-1.00% 1.00%

OVERALL RATE OF RETURN

12.60% 12.60%

HYDRATECH UTILITIES, INC.  
 STATEMENT OF WATER OPERATIONS  
 PROJECTED TEST YEAR ENDED DECEMBER 31, 1989

SCHEDULE NO. 3-A  
 DOCKET NO. 880882-WU

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 DOCKET NO. 880882-WU  
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DESCRIPTION	TEST YEAR PER UTILITY	UTILITY ADJUSTMENTS	UTILITY ADJUSTED TEST YEAR	COMMISSION ADJUSTMENTS	COMMISSION ADJUSTED TEST YEAR	REVENUE INCREASE OR (DECREASE)	REVENUE REQUIREMENT
1 OPERATING REVENUES	\$ 386,477	\$ 281,088	\$ 667,565	\$ (278,908)	\$ 388,657	\$ 252,878	\$ 641,535
2							
3 OPERATING EXPENSES						65.06%	
4							
5 OPERATION AND MAINTENANCE	\$ 396,665	\$ 29,321	\$ 425,986	\$ 5,744	\$ 431,730		\$ 431,730
6							
7 DEPRECIATION	40,776	0	40,776	(5,440)	35,336		35,336
8							
9 AMORTIZATION	0	0	0	3,708	3,708		3,708
10							
11 TAXES OTHER THAN INCOME	51,934	7,027	58,961	(6,977)	51,984	6,322	58,306
12							
13 INCOME TAXES	0	0	0	0	0	0	0
14							
15							
16 TOTAL OPERATING EXPENSES	\$ 489,375	\$ 36,348	\$ 525,723	\$ (2,965)	\$ 522,758	\$ 6,322	\$ 529,080
17							
18							
19 OPERATING INCOME	\$ (102,898)	\$ 244,740	\$ 141,842	\$ (275,943)	\$ (134,101)	\$ 246,556	\$ 112,455
20							
21							
22 RATE BASE	\$ 1,091,939		\$ 1,152,252		\$ 892,501		\$ 892,501
23							
24							
25 RATE OF RETURN	-9.42%		12.31%				12.60%
26							

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HYDRATECH UTILITIES, INC.  
ADJUSTMENTS TO OPERATING STATEMENT  
PROJECTED TEST YEAR ENDED DECEMBER 31, 1989

SCHEDULE NO. 3-B  
PAGE 1 OF 2  
DOCKET NO. 880882-WU

EXPLANATION	WATER ADJUSTMENTS
-----	-----
1 OPERATING REVENUES	
2	
3 A. To remove utility's requested increase.	\$ (281,088)
4	
5 B. To correct test year revenues.	2,180
6	-----
7 NET ADJUSTMENT	(278,908)
8	=====
9	
10 OPERATION AND MAINTENANCE EXPENSES	
11	
12 A. To adjust hospital group insurance to reflect	
13 employee contributions. Audit Disclosure 6.	(1,433)
14	
15 B. To remove sales tax expense applicable to	
16 contractual services.	(5,091)
17	
18 C. To adjust rate case expense to staff calculation.	18,868
19	
20 D. To remove pro forma rent expense.	
21 Audit Disclosure 3.	
22	(6,600)
23	-----
24 NET ADJUSTMENT	\$ 5,744
25	=====
26	
27 DEPRECIATION EXPENSE	
28	
29 A. To reflect use of the correct composite rate	
30 and methodology to calculate amortization	
31 of CIAC. Audit Exception 5.	\$ 5,937
32	
33 B. To remove depreciation expense for	
34 well no. 10.	(2,245)
35	
36 C. To remove depreciation expense associated with	
37 capitalized CIAC tax. Audit Disclosure 2.	(9,132)
38	-----
39 NET ADJUSTMENT	\$ (5,440)
40	=====
41	
42	
43 AMORTIZATION	
44	
45 A. To amortize the cost of an abandoned well over	
46 five years.	\$ 3,708
47	=====

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HYDRATECH UTILITIES, INC.  
 ADJUSTMENTS TO OPERATING STATEMENT  
 PROJECTED TEST YEAR ENDED DECEMBER 31, 1989

SCHEDULE NO. 3-B  
 PAGE 2 of 2  
 DOCKET NO. 880882-WU

EXPLANATION -----	WATER ADJUSTMENTS -----
1 TAXES OTHER THAN INCOME	
2	
3 A. To remove regulatory assessment fees	
4 related to requested revenues.	\$ (7,027)
5	
6 B. To reflect RAfs on test year revenue adjustment.	50
7	-----
8 NET ADJUSTMENT	\$ (6,977)
9	-----
10	
11 OPERATING REVENUES	
12	
13 A. To adjust revenues to allow a fair	
14 rate of return.	\$ 252,878
15	-----
16	
17 TAXES OTHER THAN INCOME	
18	
19 A. To reflect regulatory assessment fees	
20 related to staff adjustment to revenues.	\$ 6,322
21	-----
22	
23	
24	