FLORIDA PUBLIC SERVICE COMMISSION
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MEMORANDUM

May 29, 1997

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYO)

FROM: DIVISION OF WATER & WASTEWATER (MERCHANT, FUCHS, GALLOWAY, VON FOSSEN, WEBB)
DIVISION OF LEGAL SERVICES (PARKER, VACCARO)

RE: DOCKET NOS. [illegible]-WS AND 960234-WS - GULF UTILITY COMPANY - APPLICATION FOR AN INCREASE IN WASTEWATER RATES AND CHARGES AND INVESTIGATION OF WATER RATES FOR POSSIBLE OVEREARNINGS
COUNTY: LEE

AGENDA: 6/10/97 - REGULAR AGENDA - POST HEARING DECISION - PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF

CRITICAL DATES: 8-MONTH EXPIRATION DATE: JUNE 10, 1997 (WAIVED)

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CASE BACKGROUND

Gulf Utility Company (Gulf or utility) is a Class A utility which serves approximately 7,040 water and 2,435 wastewater customers in Lee County, Florida. The utility is located in a water use caution area as designated by the South Florida Water Management District. Rate base was last established for Gulf's wastewater facilities by Order No. 20272, issued November 7, 1988, in Docket No. 880308-SU. Rate base for water facilities was last established by Order No. 24735, issued July 1, 1991, in Docket No. 900718-WU.

By Order No. PSC-96-0501-FOF-WS, issued April 11, 1996, in Docket No. 960234-WS, the Commission initiated an overearnings investigation and held $353,492 in annual water revenues subject to refund. As noted by that order, the overearnings investigation has been combined with this rate proceeding.

On June 27, 1996, Gulf filed an application for an increase in wastewater rates, approval of a decrease in water rates, and approval of service availability charges. The minimum filing requirements (MFRs) were satisfied on August 23, 1996, which was established as the official filing date pursuant to Section 367.083, Florida Statutes. The utility's requested test year for interim purposes is the historical year ended December 31, 1995. The requested test year for final rates is the projected year ending December 31, 1996.

By Order No. PSC-96-1310-FOF-WS, issued October 28, 1996, the Commission suspended Gulf's proposed rates, approved interim wastewater rates subject to refund, and granted the utility's request to reduce its water rates and held additional water revenues subject to refund. The Prehearing Conference was held on February 17, 1997. The technical and customer hearings were held on March 5 and 6, 1997 at the Elks Club of Bonita Springs in Bonita Springs, Florida. Two customer hearings were held during two different times which lasted a total of approximately 1 hour. Five golf course representatives testified opposing the establishment of a reuse rate and 6 customers testified opposing the quality of service or the rate increase in general.

Abbreviations and Technical Terms

The following is a list of acronyms and technical terms which have been used in the recommendation.

COMPANY AND PARTY NAMES

FPSC	Florida Public Service Commission
GULF	Gulf Utility Company
OPC	Office of Public Counsel

TECHNICAL TERMS:

AFUDC	Allowance for Funds Used During Construction
AWWA	American Water Works Association
BFC	Base Facility Charge
CIAC	Contributions in Aid of Construction
COC	Cost of Capital
DEP	Department of Environmental Protection
ERCs	Equivalent Residential Connections
FGCU	Florida Gulf Coast University
FAC	Florida Administrative Code
GPD	Gallons per Day
ISO	Insurance Services Organization
MFRs	Minimum Filing Requirements
MGD	Million Gallons per Day
NARUC	National Association of Regulatory Utility Commissioners
ROE	Return on Equity
ROR	Rate of Return
SFWMD	South Florida Water Management District
WRCA	Water Resource Caution Area
WTP	Water Treatment Plant
WWTP	Wastewater Treatment Plant

DISCUSSION OF ISSUES

ISSUE A: Should the proposed stipulations be approved?

RECOMMENDATION: Yes. (MERCHANT)

STAFF ANALYSIS: In Prehearing Order No. PSC-97-0208-PHO-WS, issued on February 24, 1997, all parties and staff agreed the following stipulations were reasonable. Further, the stipulated matters set forth below, should have no precedential value in any subsequent proceeding. Staff recommends that these be approved.

1. Wastewater plant in service should be reduced by $2,265 in order to correct the 13-month average balance of wastewater plant reported in the MFRs. (Audit Exception 4)

2. The water transmission and distribution system should be considered 100 percent used and useful because the water distribution lines are contributed.

3. The entire wastewater collection system should be considered 100 percent used and useful because the collection system is contributed.

4. Test year expenses should be reduced by $792, to remove lobbying-type expenses.

5. Test year expenses should be reduced by $235 to remove expenses related to rotary club dues.

6. Charitable contributions should not be included in operation and maintenance expenses. (Audit Exception 3)

7. An adjustment of $8,000 should be made to remove expenses for pond cleaning from the test year.

8. Consulting costs associated with the overearnings investigation case should be considered rate case expense and included in Gulf's documentation for requested rate case expense. Test year expenses should be reduced by $4,205 for water and $1,979 for wastewater. (Audit Disclosure No. 12)

9. Payroll taxes should be allocated based on the ratio of payroll costs between water and wastewater. The amounts are subject to the resolution of other issues. (Audit Disclosure 16)

10. Test year regulatory assessment fees should be computed to reflect 4.5 percent of adjusted test year revenues, resulting in adjustments of $(715) for water and $(1051) for wastewater. (Audit Disclosure 16)

11. Private fire protection rates should be calculated in accordance with Rule 25-30.465, Florida Administrative Code.

12. For both water and wastewater refund purposes, the final revenue requirements should be adjusted to remove any ratemaking components which were not in service or not incurred during the time interim rates were in effect. These adjusted revenue requirements should be compared to the adjusted test year revenues to determine whether any refund should be ordered. The water test year revenues should be annualized for the two time periods using the rates prior to the water interim rate reduction and the rates subsequent to the water interim rate reduction.

13. The appropriate AFUDC rate should be based on the rate of return found to be fair and reasonable by the Commission, and pursuant to Rule 25-30.116, Florida Administrative Code. The rate should be effective January 1, 1997.

14. The cost of common equity capital should be determined using the leverage formula in effect at the time of the Commission's decision in this case. OPC has no position as to the use of the leverage formula, but does not intend to pursue it as an issue.

15 If any plant costs related to funds received from the South Florida Water Management District's Alternate Water Supply Grants Program have been included in projected rate base, those costs should also be included in rate base as CIAC. Regardless of the ratemaking treatment followed in this rate case, the grant should be recorded as CIAC on the utility's books when received. In no event should the amount of CIAC exceed the amount of related plant in rate base resulting from this transaction.

QUALITY OF SERVICE

ISSUE 1: Is the quality of service provided by Gulf Utility Company satisfactory?

RECOMMENDATION: Yes, the quality of service provided by Gulf Utility Company to its customers is satisfactory. (FUCHS)

POSITION OF THE PARTIES

GULF: The quality of service provided by Gulf Utility Company is satisfactory.

OPC: The Citizens do not propose any penalties or reduction of Gulf's return on equity because of poor quality service.

STAFF ANALYSIS: Pursuant to Rule 25-30.433(1), Florida Administrative Code

> The Commission in every rate case shall make a determination of the quality of service provided by the utility. This shall be derived from an evaluation of three separate components of water and wastewater utility operations: quality of the utility's product (water and wastewater); operational conditions of utility's plant and facilities; and the utility's attempt to address customer satisfaction. Sanitary surveys, outstanding citations, violations and consent orders on file with the Department of Environmental Protection (DEP) and county health departments (HRS) or lack thereof over the preceding 3-year period shall also be considered. DEP and HRS officials' testimony concerning quality of service as well as testimony of utility's customers shall be considered.

Staff's recommendation on the overall quality of service provided by the Utility is derived from the evaluation of the above requirements.

In order to assess the overall quality of service provided by the Utility, the quality of the product (water and/or wastewater) must be evaluated. This evaluation consists of a review of the utility's current compliance with DEP and health department (water

and wastewater) standards as provided by DEP and/or HRS witness testimony. Mr. William D. Allen, P.E., Director of Environmental Engineering, HRS, Lee County Public Health Unit, and Mr. Andrew Barienbrock, Environmental Manager, Domestic Wastewater Compliance and Enforcement Section for the DEP, served as witnesses for Staff. Their testimony was stipulated into the record. (TR 367, 371)

Staff witness Allen testified that the facility is currently operating in compliance with all State and Federal maximum contaminant levels. Mr. Allen further testified that Gulf is also in compliance with other State requirements pertaining to power, wells, operators and chlorine levels. (TR 368-369)

Mr. Allen also testified that the Utility's water system has not been the subject of any enforcement action by the Lee County Health Department within the past two years. (TR 369) Staff witness Barienbrock testified that the wastewater plant and distribution system are in compliance with provisions of Ch. 62, FAC, and do not have any citations, violations or corrective orders in regard to the wastewater treatment plant and effluent disposal system. (TR 373)

The level of customer satisfaction which results from the utility's relations with its customers is also evaluated by a review of recent complaints and with direct customer testimony at a customer meeting or a service hearing held in the service area of the utility.

A service hearing was held in the Gulf Utility Company area at Estero, Florida, on March 5-6, 1997. Approximately 100 persons attended. Eleven customers testified. Six of the witnesses, Bill Butler, Paul Zile, Kevin Scott, Joe Heffernan, Bruce Lawson and Katherine Green testified in opposition to the Commission imposing a charge for reuse effluent. (TR 12-46 & 888) Two customers complained about the quality of the water provided by Gulf Utility. Mr. Dale Heusing complained about the level of corrosivity of the water and the need to install a water softener. (TR 47-48) Ms. Johanna Weeks complained that her water tastes bad and of the need to add a filter to her refrigerator to purify the ice cubes. (TR 68) The remainder were opposed to the rates or requesting information.

As supported by the record referenced above, Staff recommends the Commission find the quality of service provided to its customers by the Gulf Utility Company to be satisfactory.

ISSUE 2: Does the Utility provide adequate fire flow to its entire certificated area?

RECOMMENDATION: No. Areas exist in the service area which do not meet minimum flow standards required by the Lee County Development Code and the Insurance Service Organization (ISO). Staff recommends that Gulf Utility be ordered to coordinate with representatives from the fire districts in its service area to correct low flow problems where they exist and report to this Commission in 6 months and 12 months, after the issuance date of the final order, detailing the corrective measures taken and the progress of the corrective action. (FUCHS)

POSITION OF THE PARTIES

GULF: Gulf provides adequate fire flow to its certificated area.

OPC: Representatives from both fire control districts located in Gulf's service territory agree that the Utility fails to provide adequate fire flow to portions of its certificated area.

STAFF ANALYSIS: The issue is, does Gulf provide adequate fire flow to its **entire** certificated area. This issue was brought forth by the representatives of the local fire districts in the area served by Gulf Utility Company.

Staff witness Beard, employed by the San Carlos Fire and Rescue Service District as a fire inspector testified that **35** of **56** (62.5%) hydrants in commercial areas and **75** of **341** (22%) fire hydrants in residential areas do not meet fire flow needs for those areas. (TR 388-389) Staff witness Kleinschmidt, employed by the Estero Fire Control and Rescue Service District as its Deputy Chief, testified that fire districts are graded by the ISO, an agency that classifies and rates fire departments throughout the country. (TR 420) Mr. Kleinschmidt testified that the grading system is used by insurance companies to set insurance rates within the area covered by the respective departments. (TR 420) Both witnesses testified that lower fire flows result in added costs to construction of buildings by requiring sprinkler systems and additional fire walls to be installed. (TR 389 & 421)

Utility witness Elliott testified that staff witness Beard referenced Section 12 "Fire Safety Design Standards and

Requirements" which had been replaced by the current Lee County Development Code. (TR 709) The Lee County Development Code, referred to by Utility witness Elliott (EXH 36) in Section 10-385(b)(1) requires 750 gpm for one and two family developments when the distance between buildings is zero to 30 feet. Section (b)(2) requires fire flows to be in accordance with the formula shown in subsection (b)(3) of the same section. Subsection (b)(4) requires a minimum flow of 500 gpm with 20 pounds per square inch (psi)residual in all cases. (EXH 36) Mr. Elliott testified that the Utility was not required to meet fire flow standards as suggested by Mr. Beard because the Lee County Code makes no specific requirement of the Utility, since it refers to "new" construction. (TR 710) Mr. Elliott testified that the Utility was not required to "retrofit" the system under the new ordinance. (TR 713) When cross examined by Staff, Utility witness Elliott agreed that the old Section 12 (EXH 39) and the new Lee County Development Order pertaining to fire flow were substantially the same. (TR 749) Section 12 had been in effect since 1983, so any construction done after that time would effectively be the same as under the new requirement. Mr. Elliott testified that three fire flow tests were conducted by a state certified fire sprinkler contractor on January 14, 1997. Mr. Elliott stated that the tests were taken at the extremities of the Gulf Utility service area. Mr. Elliott further testified that the difference between the fire flow tests conducted January 14th, and those conducted by the San Carlos Fire Department, is that the duration of the test was a minimum of ten minutes, in contrast to the three to five minute test conducted by the Fire Department. (TR 14) Mr Elliot testified that the ten minute test permitted sufficient time that a pressure drop was experienced at one or more booster stations initiating the high service distribution pumps designed to provide fire flow to the system. (TR 14-15)

When asked by Staff if all fire hydrants met the utility requested 1,500 gpm, Utility witness Messner, who is Operations Manager for Gulf, answered, "No, not all fire hydrants." (TR 825)

OPC's position agrees with Staff. Throughout its post hearing briefs OPC makes liberal use of the testimony of Staff witnesses Beard and Kleinschmidt to support its agreement with Staff's position that the company does not provide adequate fire flow to its entire service area. (BR 2-5)

In his direct testimony and during cross examination by OPC, Staff witness Beard testified that there are some residential areas that do not produce 750 gpm. (TR 388 & 393) Upon cross examination by OPC, Mr. Beard stated that there are some commercial areas that the utility cannot produce 750 gpm. (TR 393) Mr. Beard testified that according to the development standards, if 750 gpm is not met, the development order will not be approved. (TR 393) OPC questioned Mr. Beard regarding the requirements of the university (Florida Gulf Coast University). Mr. Beard testified that according to calculations based on the Lee County Development Code, using the Hayes and Williams formula for fire flow, most of the university buildings do not come up to fire flow units. (TR 394) According to Mr. Beard the buildings require flows ranging from 755 gpm to 2,493 gpm. When asked how much flow is available to the university, Mr. Beard answered that several tests on the line performed in January, 1997, ranged from 1,064 gpm to 1,099 gpm. (TR 395-397) That is less than half the required flows required according to the calculations. OPC questioned Mr. Beard regarding the ten minute duration fire flow tests testified to by Utility witness Elliott at TR 711. Mr. Beard testified that ten minutes is too long for a fire to burn without putting the proper amount of water on it. (TR 400) Mr. Beard further testified that according to the American Water Works Association, (AWWA) Manual 17 and National Fire Protection Association (NFPA) 219, there is no requirement to leave a hydrant run 10 minutes until the pressure stabilizes. (TR 400) Mr. Beard stated that, it could cause property damage and waste water to the extent of 10,000 gallons for each flow test. (TR 401)

Based on the testimony in the record from expert witnesses Beard and Kleinschmidt, who are state certified, practicing fire officials, Staff recommends that Gulf Utility Company does not provide adequate fire flow protection in its **entire** certificated area service and should be ordered by the Commission to coordinate with representatives from the fire districts in its service area to correct low flow problems where they exist and report to this Commission in 6 months and 12 months, after the effective date of the final order, detailing the corrective measures taken and the progress of the corrective action.

ISSUE 3: Should the one million gallon reject holding tank for the Corkscrew Water Treatment Plant be included in rate base?

RECOMMENDATION: No. (FUCHS)

POSITION OF THE PARTIES

GULF: The reject holding tank should be included in rate base because, 1) it is required by Gulf's DEP permit, 2) the plant was constructed within 24 months from the historical test year. (Sec. 367.081(2), and (3) it is a prudent cost of providing service during the period when the rates will be effective (Sec.367.081(3).

OPC: No. Construction of the one million gallon holding tank has not even begun. If further delays occur, it could be 1998 before the facility is in service.

STAFF ANALYSIS: Gulf, in its MFRs, requested the inclusion of a one million gallon reject water holding tank. The tank, to be used for holding reject water from the Corkscrew water treatment plant, had not been constructed, nor were contracts let or construction even initiated during the utility requested test year ending December 31, 1996. (TR 128-129) In its position statement, the Utility cites Section 367.081(2), Florida Statutes, as authority for the Commission to include the cost of the reject water holding tank in rate base. This statute provides a utility with the opportunity to request the use of a projected test year of up to twenty-four months in a rate proceeding. Gulf opted to file its rate case using a 12 month projected test year ending December 31, 1996. Gulf was offered an opportunity to produce firm evidence of a commitment to construct the holding tank up to and including the hearing held on March 4&5, 1997, three months after the end of the test year chosen by the Utility. When questioned at the hearing, whether the tank had been constructed, Utility witness Moore answered, "No, it has not." (TR 128) When questioned further if contracts for the construction had been signed, Mr. Moore answered, "No. We are still awaiting the 90% plans which we can then take to bid." (TR 129)

Not only had the reject tank not been constructed by the end of the test year, 1996; the Utility did not have contracts for construction, nor did it have bids or a firm start/completion date in hand as late as the hearing on March 4&5, 1997. Mr. Moore stated the completion time was estimated by the engineer to be four

months. (TR 129) If the project were to be initiated in April, the estimated completion date would be August. Staff is very mindful of the cost for filing any rate proceeding. Had there been, at least a signed contract to construct the reject holding tank, Staff could have recommended its inclusion in some manner. However, there is no date certain in the record as to when this tank will be built. In its brief, Gulf also argues that case law requires the Commission to include the reject holding tank in rate base, because it is a known change that will occur within a reasonable time after the test year. Gulf cites the following cases in support of its arguments: Gulf Power v. Bevis, 289 So. 2d 401, 405 (Fla. 1974) relying on McCardle v. Indianapolis Water Co., 272 U.S. 400 (1926), and Floridians United v. Public Service Commission, 475 So. 2d 241 (Fla. 1985). (BR 5) Staff agrees with the holdings in these cases, but we believe that these cases do not apply in this instance because, as indicated earlier, the Utility failed to provide evidence of a date certain for construction of the tank. In a rate case, the burden of proof is on the utility seeking a rate change. See Florida Power Corp. v. Cresse, 413 So. 2d 1187 (Fla. 1982)

Therefore, the evidence does not support the inclusion of the one million gallon reject water holding tank in rate base. We believe the Utility could apply for a limited proceeding when it has firm figures and dates available if it can show financial need. Staff recommends the one million gallon reject holding tank for the Corkscrew Water Treatment Plant not be included in rate base.

ISSUE 4: Should any adjustments be made to the chlorine contact chambers at the new Three Oaks Wastewater Treatment Plant?

RECOMMENDATION: Yes. However, the chlorine contact chambers are included in Account 380.4 (Treatment and disposal equipment). All adjustments to Account 380.4 are addressed in Issue 15. (FUCHS)

POSITION OF THE PARTIES

GULF: No adjustments should be made to the chlorine contact chambers because these units are necessary in order to maintain the necessary assurance of compliance with Fla. Admin. Code R 62-610, that requires Class I reliability.

OPC: While the chlorine contact chamber at the new plant should be considered 64.63% used and useful, the chlorine contact chamber at the old plant (located at the same site) should be considered 48.48% used and useful, pursuant to Class I reliability requirements.

STAFF ANALYSIS: The chlorine contact chambers are the final stage of wastewater treatment before disposal. Chlorine contact chambers are necessarily a part of the treatment plant, recorded in Account No. 380.4. There is no separation of costs or funds. Therefore, adjustments made to Account No. 380.4, (Treatment and disposal equipment) will automatically apply to the contact chambers. In issue 7, Staff is recommending the Three Oaks Treatment plant be considered 87.15% used and useful.

Utility witness Elliott testified that the second chlorine contact chamber is a necessary element to provide the required redundancy to the online chamber as required by DEP Rule 62-610. (TR 704)

OPC questioned Utility witness Elliott about the DEP redundancy rule. Witness Elliott agreed that the rule relies on a reference to Federal Environmental Protection Agency (EPA) guidelines. (TR 731) Mr. Elliott also agreed that the EPA guidelines require a 75% backup for sedimentation basins and 50% design flow backup for disinfection of contact basins. (TR 732-733) Mr. Elliott also stated that those figures applied in an ideal world. (TR 734)

OPC witness Biddy testified that the cost of the chlorine contact chamber should be transferred to plant held for future use. (TR 248) In its post hearing brief, however, OPC's final position is to consider the original and new plant elements to have different used and useful percentages. (BR 7) There is no precedent for this type of consideration, nor is there any record support for different calculations for each required element. Additionally, since the cost for the chlorine contact chambers is not segregated from the total cost of the treatment facility, Staff believes it is not possible to determine an amount specifically dedicated to the chambers.

Based on the record, Staff recommends that chlorine contact chambers at the Three Oaks Wastewater Treatment Plant be considered to be in Account No. 380.4 which is recommended to be 87.15% used and useful as part of Issue 15.

ISSUE 5: Should any adjustments be made to the old Three Oaks Wastewater Treatment Plant?

RECOMMENDATION: No adjustments should be made. The facility is necessary to meet DEP Class I reliability requirements as stated in Rule 62-610, FAC, and should be considered 100% used and useful. (FUCHS)

POSITION OF THE PARTIES

GULF: No adjustments should be made to the old Three Oaks Wastewater Treatment Plant. This plant is required by DEP's Class I reliability rules requiring redundancy.

OPC: Yes, the old Three Oaks Wastewater Treatment Plant should be considered 60.59% used and useful.

STAFF ANALYSIS: The original Three Oaks WWTP is a 0.250 mgd circular steel aeration treatment plant. It has been replaced as the primary treatment plant by the new 0.750 mgd plant. Utility witness Elliott testified that the old tanks are a necessary element in the Three Oaks WWTP process to provide the required redundancy for online aeration and clarifier units according to DEP Rule 62-610, FAC, for Class I reliability. (TR 704) Mr. Elliott further testified that, upon the completion of Three Oaks Phase IV expansion, one of the old treatment tanks will be modified for use as a flow equalization basin and the second will be used for effluent storage. (TR 704)

OPC witness Biddy testified that the old Three Oaks WWTP is currently off line. (TR 248) OPC's position as stated in its post hearing brief is to consider the original and new plant elements to have different used and useful percentages. OPC recommends the old Three Oaks plants be considered 60.59% used and useful and the new plant to be 64.63% used and useful. (BR 8 & 25) There is no precedent for this type of consideration, nor did OPC provide any record support for using different percentages of used and useful for the old and new plants.

As previously stated in this analysis, OPC witness Biddy testified that the old WWTP is currently off line. (TR 248) If the plant were actually off line there would be no used and useful consideration. Utility witness Elliott testified that the additional plant is required to meet the Class I reliability rule.

(TR 704) It must be available for immediate use in an emergency situation. The old plant is an integral part of the system and necessary according to DEP rules requiring redundancy for Class I operation. According to Mr. Elliott, the plant was on line as recently as February 1997. (TR 730)

Staff recommends no adjustments should be made to the old Three Oaks WWTP. As reflected in the record, the facility is in service and necessary to meet DEP Class I reliability requirements as stated in DEP Rule 62-610, FAC, and should be considered 100% used and useful.

ISSUE 6: Should the costs associated with the Florida Gulf Coast University (FGCU) be included in this rate proceeding, and what, if any adjustments are necessary?

RECOMMENDATION: Costs associated with the Florida Gulf Coast University were incurred during the test year and should be included in rate base. No adjustments are necessary. (FUCHS)

POSITION OF THE PARTIES

GULF: The costs associated with FGCU should be included in this rate proceeding. The facilities were constructed and were providing service in 1996.

OPC: No. The costs, expenses and revenues related to Florida Gulf State University should be removed from the test year. In the alternative, if the water and wastewater lines are not removed from rate base, they should be considered no more than 24.96% and 23.15% used and useful respectively.

STAFF ANALYSIS: The Florida Gulf Coast University will not open its doors to students until the fall semester of 1997. However, the construction of the lines and other infrastructure for water and wastewater was undertaken and placed in service in the December 31, 1996 test year.

Utility witness Moore testified that the university is under construction, (TR 84) and actually began receiving service in December 1996. (TR 123) He further testified that the facilities to serve FGCU were designed by engineers contracted by the university and considered only their [FGCU] service requirements, (TR 565) and that the lines for the university were in place during the test year. (TR 123) Mr. Moore testified that the FGCU staff did not want other lines connected with the campus lines because of concern that such connections would negatively impact pressure and fire flow requirements of the university. (TR 565) Mr. Moore testified that FGCU will be the Utility's largest customer. (TR 87) Mr. Moore also testified that the university will be the largest single source of revenue in its first year of operation. (TR 89)

OPC witness Biddy expressed concern that the lines not be considered 100% used and useful because ultimately they will serve private developments off campus. (TR 249) OPC's final position

states the used and useful percentages should be no more than 24.96%, for water and 23.15% for wastewater. (BR 10)

Staff is not certain how OPC's percentages were derived since OPC provided no supporting testimony or documentation. In fact, OPC witness Biddy testified that without knowing the ultimate build out design, no reliable used and useful analysis can be performed for the water and wastewater lines. (TR 249)

Staff agrees with OPC that a reliable used and useful percentage on lines, based on actual demand, cannot be performed at this time. The university is in operation and receiving service from the Utility, even though there are no students present on campus. However, the record shows that the lines were constructed by the university according to its specifications and built with only its [FGCU] service requirements being considered. (TR 565) Because the record shows the lines were sized by university contracted engineers, for the university only, Staff recommends all costs relating to FGCU were prudently incurred in the test year and should be included in this rate proceeding with no adjustments.

ISSUE 7: Should a margin reserve be allowed for the water and wastewater systems, and if so, what amount?

RECOMMENDATION: Yes. Staff recommends that a margin reserve, using the linear regression method of forecasting future growth, should be included in the used and useful calculations. Margin reserve should be 18 months for water treatment plants (283,773 gpd) and 36 months for the Three Oaks wastewater treatment plant (225,623 gpd). No margin reserve is recommended for the San Carlos wastewater treatment plant, which is operating at capacity and recommended to be 100% used and useful in Issue 15. The water distribution and wastewater collection systems are contributed and therefore also considered to be 100% used and useful. **The recommendation for a 36-month Margin Reserve is a change from existing Commission policy.** (FUCHS)

POSITION OF THE PARTIES

GULF: The appropriate margin reserve periods are one and one half years in the water operations and three years in the wastewater operations.

OPC: No. Margin reserve is for the benefit of future customers and should not be borne by current customers. If the Commission grants a margin reserve, the reserve periods should not exceed those traditionally allowed by the Commission, 18 months for treatment plants and 12 months for collection and distribution lines.

STAFF ANALYSIS: The purpose for margin reserve is to allow a utility to expand prudently beyond current demands to enable it to meet reasonable projected short term growth. This practice allows the company to include a reasonable cost of expansion in its rate base without placing an unreasonable burden on current customers to pay for long term growth. It is Commission policy to grant a reasonable margin reserve if requested.

Utility witness Cardey testified that Section 367.111(1) Florida Statutes, provides that, "Each utility shall provide service to the area described in its certificate of authorization within a reasonable time." In order for a utility to meet its statutory responsibilities, it must have sufficient capacity and investment to meet the existing and changing demands of present and

potential customers. Therefore, the Commission has consistently recognized margin reserve as an element in used and useful calculations. (TR 642-643)

OPC witness Dismukes testified against granting a margin reserve because it represents capacity to serve future customers, not current customers. (TR 314) OPC witness Biddy agreed that a utility must be in a position to serve changing needs of its present customers. (TR 264) Mr. Biddy agreed that utilizing CIAC and AFPI funds is reserved until the new customers connect to the system. (TR 265)

It is Commission policy to grant a reasonable margin reserve to enable the utility to charge present customers for some of the additional capacity. For calculation of growth projections, Commission policy is to use linear regression analysis instead of the historical average method. (Order No. PSC-96-1320-FOF-WS, and Order No. PSC-97-0388-FOF-WS) Linear regression, because of the analysis of the two factors of growth and time, more reliably reflects positive or negative trends in growth than the simple historical averaging method of calculation. By tracking this relationship for several observations, a straight line can be established to reasonably predict growth by projecting out along the same path. Additional years can be added for further projections with reasonable confidence in the results.

Staff recommends a margin reserve of 18 months for water treatment plants, equal to 247,476 gpd, and 36 months for the Three Oaks wastewater treatment plant, equal to 173,206 gpd be authorized. **This recommendation is a change from existing Commission policy.** In past decisions, the Commission has granted margin reserve of 18 months when requested and appropriate. Testimony in this case has shown the 18 month cycle to be insufficient time for planning, permitting and construction for wastewater plants. Utility witness Elliott testified that the expansion process includes solicitation of engineering proposals, preliminary engineering and planning, site surveying, existing facilities evaluation, land acquisition and/or negotiation of reuse agreements, engineering design, zoning, final design, DEP/HRS permitting, local government permitting, bidding, financing, negotiating construction contract, construction and initial startup among others. (TR 702-703) Mr. Elliott further testified that DEP Rule 62-600.405, FAC, stipulates that if the capacity analysis report (CAR) indicates less than five years capacity remains in a

wastewater facility, that planning and preliminary design of the expansion must be initiated and documented in a signed and sealed statement provided by a professional engineer. Further, as the CAR time frame diminishes to four and three years, the requirements for further planning the expansion, such as design and planning, and cash outlay by the utility are increased. (TR 702) Mr. Elliot stated that without applying a margin reserve, the utility is forced into a continual design, permitting and construction sequence that would certainly increase costs to the utility and its customers. (TR 701) Mr. Elliott testified that a five year Margin Reserve is necessary to enable the Utility time to complete the expansion process. A 60-month margin reserve would give the Three Oaks WWTP a 100% used and useful rating. Based on the evidence presented, Staff believes that a three year margin reserve is a sufficient compromise. If the Commission decision is to grant an 18 month margin reserve for the Three Oaks WWTP, the used and useful percentage will be 72.11%.

Staff recommends margin reserve should be 18 months for water treatment plants (283,773 gpd) and 36 months for the Three Oaks wastewater treatment plant (225,623 gpd). Since the San Carlos WWTP is operating at or above capacity and the distribution and collection systems were contributed, they are considered to be 100% used and useful. Staff is recommending zero margin reserve for the San Carlos WWTP and the water distribution and wastewater collection systems. **The recommendation for a 36 month margin reserve for the wastewater plant is a change in Commission policy which has been 18 months.**

ISSUE 8: Should fire flow be included in the used and useful calculations for the water system, and if so, what is the appropriate allowance?

RECOMMENDATION: Yes. Fire flow should be included in the used and useful calculations. The appropriate amount for Gulf Utility Company is 750 gpm at 20 psi for four hours (180,000 gallons). (FUCHS)

POSITION OF THE PARTIES

GULF: Fire flow of 0.360 mgd should be included in the used and useful calculations for the water system

OPC: Fire flow should be included in the used and useful calculation of finished water storage but not for the supply wells, treatment plants or distribution mains. The fire flow allowance should be 750 gpm because that is the only documented fire flow filed in this proceeding.

STAFF ANALYSIS: In its position statement, Gulf states that the fire flow should be 360,000 gallons. This is calculated by using 1500 gpm at 20 psi for a four-hour duration as shown in the MFRs filed by the Utility. (EXH 8) Utility witness Elliott offered two fire flow tests as proof of the Utility's compliance with existing codes. (EXH 36) Staff examination of the tests reveals the highest flow was 1,213 gpm at 20 psi. Both tests fall short of the 1,500 gpm at 20 psi listed in the MFRs.

OPC's position is that if a fire flow allowance is granted the flow should be 750 gpm because that is the only documented flow in this proceeding. OPC witness Biddy agreed that when there is a fire in this system, all of the wells, pumps and tanks are used to put out the fire. (TR 268)

Division 5, Fire Safety Section, of the Lee County Development Standards, admitted as Composite Exhibit 36, requires buildings spaced from zero to thirty feet to have 750 gpm available fire flow as does the code it replaced, Section 12, Fire Safety Standards Design Requirements. Mr. Elliott agreed the requirements were the same when questioned by Staff. (TR 748)

Staff witness Beard, Fire Inspector for the San Carlos Fire and Rescue Service, testified that 35 of 56 (62.5%) hydrants in

commercial areas and 75 of 341 (22%) in residential area do not meet fire flow needs. (TR 388-389) This means nearly 28% of the hydrants in the San Carlos Fire and Rescue District do not meet fire flow requirements. Mr. Beard testified that some residential area hydrants do not meet the minimum 750 gpm and further testified that there are some commercial areas that do not produce 750 gpm. (TR 388) Staff witness Kleinschmidt, Deputy Chief of the Estero Fire Control and Rescue Service, testified that single family homes are required to have a minimum fire flow of 750 gpm and fire flow in commercial areas is dictated by the type of buildings, size, spacing and use. (TR 420) Mr. Kleinschmidt testified that Gulf does not meet all these requirements in its service area. (TR 421)

Staff agrees with Fire Inspector Beard and Chief Kleinschmidt that if the company requests and is granted a fire flow of 1,500 gpm at 20 psi residual pressure, that amount should be available at every hydrant. Insurance companies rely on the flow in their rate making process. Home owners rely on the pressure and flows being available to protect their homes. Fire fighters rely on the pressure to ensure their safety when fighting a fire. Evidence in the record indicates that Gulf Utility either does not or cannot deliver the requested 1,500 gpm at 20 psi, at more than one fourth of their hydrants. Evidence also shows that Gulf can deliver 750 gpm at 20 psi residual pressure at most of its hydrants. If a customer has a residence or commercial building located in an area of low pressure, they are exposed to an unknown hazard that may cost them their lives or property. Fire flow is required by the Lee County Land Development Code. (EXH 36) The additional capacity required by the Code must be provided by the utility. As supported by the record, Gulf Utility does not provide the requested 1,500 gpm at 20 psi residual pressure. Therefore, Staff recommends fire flow should be included in the used and useful calculations. However, as discussed in Issue 2, the Utility does not or cannot provide the requested fire flow to its entire service area. This lack of adequate fire flow can result in increased insurance costs to customers. (TR 420) It also has contributed to added costs for construction due to the requirement for fire walls and sprinkler systems due to lack of adequate flows. (TR 411) As recommended in Issue 2, the Utility should be required to co-ordinate with representatives from the fire districts in its service area to correct the low flow problems where they exist.

Until the flow problems are corrected, Staff recommends the appropriate fire flow allowance for Gulf Utility Company should be

the amount customers actually can expect to have available if needed. Staff recommends fire flow be 750 gpm at 20 psi for 4 hours (180,000 gallons).

ISSUE 9: Should economies of scale be considered by the Commission in determining whether facilities are used and useful in the public interest?

RECOMMENDATION: Yes. Economies of scale should be considered on a case by case basis when supporting data is provided by the company. (FUCHS)

POSITION OF THE PARTIES

GULF: The Commission policy is to consider economies of scale in determining whether facilities are used and useful in the public service.

OPC: No, all existing and future customers should evenly share the facility costs.

STAFF ANALYSIS: This issue was proposed by the Utility. It is Commission policy to consider economies of scale, with regard to used and useful calculations, on a case by case basis when proper support is provided by the company. The only supporting documentation presented by Gulf Utility in this docket is that the Commission recognized the principle of economies of scale in a rate proceeding involving Gulf Utility Company in Order No. 24735, issued July 1, 1991, in Docket No. 900718-WU. (TR 141) Utility witness Cardey presented an economies of scale argument regarding Skid #3 in the Corkscrew WTP. He related economies of scale to the last increment of capacity, that being Skid #3 in the plant. (TR 138) Nothing in the record supports this method of calculating used and useful. The Gulf Utility Company WTP is considered a unit and all its parts are a whole. As recommended in Issue 4, regarding the WWTP chlorine contact chambers, the WTP plant is one entity. There is no account to provide for a separate Skid just as there is none for contact chambers.

Staff recommends continuing the policy of considering economies of scale in plant investment on a case by case basis with proper documentation from the company.

ISSUE 10: Should the Commission recognize economies of scale in determining used and useful for the Corkscrew well field, Corkscrew water treatment plant, Skid #3 and Corkscrew reject water facilities?

RECOMMENDATION: No. The Commission should consider economies of scale only when proper data is provided by the utility. (FUCHS)

POSITION OF THE PARTIES

GULF: The Commission should recognize the economies in determining used and useful for these facilities.

OPC: All facilities should be designed and constructed in the most cost effective sizes to take advantage of any economies of scale. However, the benefits of any economies of scale should be shared by all current and future customers.

STAFF ANALYSIS: The Utility proposed economies of scale consideration for several of its facilities, The Corkscrew well field, Corkscrew WTP Skid #3 and the Corkscrew reject water tank. Utility witness Cardey, in his testimony regarding the used and useful calculations for the water treatment plant, stated that this Commission, in Order No. 24735, recognized economies of scale in the construction of the Utility's water treatment facilities. Mr. Cardey theorized that excess capacity is related to the last increment of capacity which, in this case, is Skid #3. (TR 138) Under cross examination by OPC, Mr. Cardey agreed there is no express language to that effect in the order. (TR 181)

As recommended in Issue 9, and ordered in Docket No. 900718-WS, Order No. 24735, regarding the raw water line and the Corkscrew reuse line, economies of scale should be considered on a case by case basis when data is provided by the utility. In this docket, no data was presented or considered for the Corkscrew well field. In Issue 3, of this recommendation, Staff recommends against including the reject water holding tank in rate base due to it not being constructed during the Utility requested test year ending December 31, 1996. Staff did not consider economies of scale for Skid #3 in the Corkscrew WTP. When calculating used and useful percentages, we have never considered individual items such as skids as separate elements. They are considered a unit and treated as a single element. Staff agrees with Utility witness Cardey that this Commission did consider economies of scale in Order No. 24735,

however the Utility did not provide any testimony or documentation to support economies of scale in this case. In the rate case referenced by Mr. Cardey, Staff considered economies of scale for the Corkscrew WTP building.

Staff recommends there was no evidence presented by the Utility in this proceeding to warrant economies of scale consideration.

ISSUE 11: Should all facility lands be considered 100% used and useful, and if not, what is the appropriate used and useful percentages?

RECOMMENDATION: Yes. All facility lands should be considered 100% used and useful. (FUCHS)

POSITION OF THE PARTIES

GULF: All facility lands should be considered 100% used and useful.

OPC: No. Used and useful calculations should be performed to justify the 100% used and useful allocation for facility lands. The appropriate used and useful percentages for combined water treatment facility land are 67.16% and for combined wastewater facility land is 66.96%.

STAFF ANALYSIS: Facility lands were considered 100% used and useful by this Commission in Order No. 24735, for Docket No. 900718-WU.

Utility witness Cardey testified that the land at the Corkscrew water treatment plant was found to be 100% used and useful by the Commission. He further testified that nothing has changed since that case. (TR 658)

OPC witness Biddy offered no compelling testimony to the contrary. Mr. Biddy testified that the Utility can expand to the ultimate design capacities of 3.0 mgd for water and 5.0 mgd for wastewater. (TR 253) These capacities were evident in the prior case when the Commission granted 100% used and useful for the facility land per Order No. 24735.

Staff concludes, upon reviewing the record in this proceeding, that nothing has changed since the prior case regarding the amount of land or land use. Staff recommends all facility lands be considered to be 100% used and useful.

ISSUE 12: What are the appropriate method and resulting used and useful percentages for the water system components?

RECOMMENDATION: The appropriate method for calculating used and useful for the water system components is the sum of the average of five maximum days plus fire flow plus margin reserve minus excessive unaccounted for water divided by plant capacity. The resulting used and useful percentage for the water system components is 76.15%. (FUCHS)

POSITION OF THE PARTIES

GULF: The supply and treatment plant is 88.2% used and useful, and is based upon Gulf's obligation to provide service to existing and potential customers in its certificated area: the sum of the average of five consecutive days maximum flows, a margin reserve and fire service, divided by capacity. Storage and the distribution supplies is 100% used and useful.

OPC: For water treatment the average of 5 maximum daily flows of the maximum month divided by the total plant capacity results in a 68.43% used and useful percentage. The water lines are contributed and require no analysis.

STAFF ANALYSIS: Gulf Utility Company has two water treatment plants which are interconnected. Plant # 1 is the San Carlos lime softening plant with a capacity of 2.415 mgd. Plant #2 is the Corkscrew membrane softening plant with a capacity of 1.8 mgd. Total water plant treatment capacity is 4.215 mgd. (EXH 8)

Utility witness Cardey presented used and useful calculations in the MFRs (EXH 8) indicating the used and useful percent for the water treatment plant should be 88.2%. In his calculations to arrive at 88.2%, Mr. Cardey used 360,000 gallons for fire flow and margin reserve flows based on calculations which utilized artificially high ERC growth and flows per single family ERC. In Issue 8, based on evidence in the record, staff is recommending available fire flow to be 180,000 gallons. Cross examination of Mr. Cardey by OPC revealed that the single family ERC flows of 396 gallons per ERC for water and 250 gallons per ERC for wastewater, presented by the Utility in its MFRs are too high. Current flows for single family residences should actually be 206 gallons per ERC for water and 158 gallons per ERC for wastewater. (TR 176-177) Staff analysis reveals that, if the calculation is performed, using

flow figures and ERC numbers supplied by the company in its MFRs, Schedule F-9, (EXH 8) 206 gallons per single family ERC is the result, as indicated by OPC. Mr. Cardey presented as his argument, economies of scale, and extended the economies of scale to the last increment of capacity, Skid #3. Mr. Cardey also used a factor of 500 ERCs at 396 gallons per ERC from the Utility's tariff, as an indicator of expected flows from the university.

OPC witness Biddy, in his used and useful calculations does not include a margin reserve, testifying that OPC's policy is to not endorse a margin reserve. (TR 263) By not including margin reserve, a much lower used and useful percentage of 68.43% results.

The Commission's policy regarding the method of calculation of used and useful percentage, uses the sum of the average of five maximum days plus fire flow plus margin reserve minus excessive unaccounted for water divided by plant capacity. Attachment A shows the calculations. As indicated in Issue 7, the margin reserve includes an annual growth of 430 ERCs as calculated by the more reliable linear regression method. This differs from Mr. Cardey's number of 500 ERCs. Staff also recommends and used a lower fire flow figure of 180,000 gallons in lieu of the requested 360,000 gallons requested in the Company's MFRs, as reflected in Issue 2. Staff recommends the Commission consider the water treatment plants to be 76.15% used and useful.

DOCKETS NOS. 960329-WS & 960234-WS
DATE: MAY 29, 1997

ATTACHMENT A

UTILITY NAME: GULF UTILITY COMPANY
TEST YEAR: 12-31-96

WATER TREATMENT PLANT USED AND USEFUL CALCULATION
GULF UTILITY COMPANY

% USED AND USEFUL= $\frac{(3+4+5-6)}{1}$ 76.15%

(1)	Capacity of plant		4,215,000	GPD
(2)	Average Daily Flow		3,312,000	GPD
(3)	5 max day average flow		2,746,000	GPD
(4)	Fire flow capacity required		360,000	GPD
	Fire flow available		180,000	GPD
(5)	Margin Reserve (not to exceed 20% of present ERCs):			
	(a) Average number of unit connections	7,528		
	(b) Projected yearly customer growth in ERCs by regressive analysis of most recent 4 years	430		
	(c) Construction time for additional	18		

Margin Reserve= $5b \times \left(\frac{5c}{12mths}\right) \times \left(\frac{3}{5a}\right) =$ 283,773 GPD

(6)	Excessive Unaccounted for water		0	GPD
	(a) Total amount	38,615 GPD	5.81 % of Avg. Daily Flow	
	(b) Reasonable amount	66,484 GPD	10.00 % of Avg. Daily Flow	

ISSUE 13: What are the appropriate method and resulting used and useful percentages for water supply wells?

RECOMMENDATION: The appropriate method is to calculate capacity required versus capacity constructed as has been done historically by this Commission. The San Carlos well field should be 100% used and useful and the Corkscrew well field should be 62.5% used and useful. (FUCHS)

POSITION OF THE PARTIES

GULF: The water supply wells are 88% used and useful.

OPC: The appropriate method is "Average of 5 Maximum Daily Flows of the Maximum Month divided by Total Well Capacity." The resulting used and useful percentage is 46.82%.

STAFF ANALYSIS: Gulf Utility has two non-interconnected well fields. The San Carlos well field which serves the San Carlos WTP and the newer Corkscrew Swamp well field, which was developed in 1990, and serves the Corkscrew WTP. Eleven wells were drilled in the Corkscrew well field, of which five are equipped with pumps. The Utility claimed in Docket No. 900718-WU, that all 11 wells were drilled at one time at the request of the South Florida Water Management District, who wanted to protect the integrity of the Corkscrew Swamp. The company had only two of the 11 wells equipped with pumps in that Docket. Since then, 3 additional wells have been equipped with pumps.

Gulf Utility witness Cardey testified that the Commission found the San Carlos supply and treatment plant 100% used and useful in Order No. 24735. (TR 653) Mr. Cardey testified that the Commission included three of the Corkscrew wells in used and useful property in that same order. (TR 653) Review by Staff revealed that the Commission actually included 4 wells in calculating used and useful in that order. Mr. Cardey appears to request 100% used and useful for San Carlos independently then combines the two for an average percentage of 88%. (TR 657)

OPC witness Biddy testified that a water utility will customarily use a "firm reliable capacity" in calculating the used and useful percentages for water wells. The firm reliable capacity excludes the largest well capacity by assuming it to be out of service. (TR 251) Mr. Biddy further cited Section 3.2.1.1 (Source

Capacity) of the Recommended Standards for Water Works, (Ten States Standards) "The total developed groundwater source capacity shall equal or exceed the design maximum day demand and equal or exceed the design average day demand with the largest producing well out of service." (TR 251)

Staff utilized the method recognized by the Recommended Standards for Water Works (Ten States Standards) in our used and useful calculations for Gulf Utility's Corkscrew well field. That method uses a percentage of the capacity required versus capacity constructed as a criteria for used and useful calculations, observing economies of scale when appropriate. The San Carlos well field has a capacity of 2.808 mgd. The San Carlos water treatment plant has a capacity of 2.4 mgd (EXH 8). This Commission found all accounts associated with the San Carlos water treatment plant to be 100% used and useful in Order No. 24735. Utility witness Cardey testified that nothing has changed since that decision. (TR 653) Mr. Cardey testified that the five well pumps in the Corkscrew well field each has a capacity of 500 gpm. (TR 192) With the largest well out of service, the well field has a total capacity of 2.88 mgd. The Corkscrew water treatment plant has a current capacity of 1.8 mgd. Dividing the 1.8 mgd capacity of the WTP by the 2.88 mgd capacity of the well field equals 62.5% used and useful for the Corkscrew well field.

Based on the evidence in the record, Staff recommends the Commission find the San Carlos well field to be 100% used and useful and the Corkscrew well field to be 62.5% used and useful.

ISSUE 14: What is the appropriate method and resulting used and useful percentage for water storage?

RECOMMENDATION: The water storage capacity for Gulf Utility Company is less than a one day production of the treatment plants. The storage facility should be considered 100% used and useful. (FUCHS)

POSITION OF THE PARTIES

GULF: The company has 2.6 million gallons of ground storage, less than 18 hours of peak demand. The amount of adequate storage, including emergency storage is based upon an assessment of risk and degree of system reliability. The water storage facilities are 100% used and useful.

OPC: The appropriate method is "Half Average Daily Flow plus Fire Flow Storage, divided by the Total Storage Capacity." The resulting used and useful percentage is 63.15%, assuming 750 gpm fire flow is provided.

STAFF ANALYSIS: Gulf has 2.6 million gallons of storage, representing about 18 hours normal use. (TR 744) Average use for the system is 1.847 mgd, as indicated in the MFRs Schedule F-3. (EXH 8)

Utility witness Elliott testified that it is standard practice to provide emergency storage based on an assessment of risk and degree of system dependability. (TR 706) OPC witness Biddy raised the issue of dead storage. Dead storage is water in a storage tank which cannot be pumped out. Thus, is unavailable for consumption. Utility witness Elliott stated there is no dead storage to consider. (TR 746) Mr. Elliott testified that Lee County requires a 24-hour production for storage in smaller systems. (TR 743) Mr. Elliott also testified that Gulf only has an 18 hour storage capacity whereas other systems in the area, such as the City of Cape Coral and Sanibel have five to ten days storage. (TR 744) Mr. Biddy testified that the Commission granted 100% used and useful for storage in Order No. 24735, in Docket No. 900718-WU, by utilizing one day of peak demand plus fire protection. Mr. Biddy took exception to that allowance by testifying that he believed half of the average daily flow is adequate for equalization and emergency storage, but offered no supporting documentation for his

theory. (TR 252) Mr. Biddy also testified that no dead storage was used in his calculations.

The Commission found in Order No. 24735, issued in Docket No. 900718-WU, that normally a one day plant production is utilized for storage when available. The Commission granted 100% used and useful for storage in Docket No. 900718-WU, Order No. 24735. The system has grown since that time and no new storage has been added, therefore, based on the record, Staff recommends the storage should be considered 100% used and useful.

ISSUE 15: What is the appropriate method and resulting used and useful percentage for the wastewater treatment plants?

RECOMMENDATION: The appropriate method of calculation for the San Carlos WWTP is based on the annual average daily flow due to DEP permitting. The appropriate method of calculation for the Three Oaks WWTP is based on the average daily flow of the maximum month due to DEP permitting. The resulting used and useful percentages should be 100% for the San Carlos WWTP and 87.15% for the Three Oaks WWTP. (FUCHS)

POSITION OF THE PARTIES

GULF: The wastewater treatment plant is 100% used and useful, (average daily flow in max month divided by plant capacity).

OPC: The appropriate method is the "average daily flow of the maximum month or annual average daily flow divided by the total plant capacity," depending on the FDEP permits. San Carlos WWTP is 100% used and useful. Three Oaks WWTP is 64.63% used and useful.

STAFF ANALYSIS: Gulf has two wastewater treatment plants. The San Carlos WWTP has a capacity of 0.218 mgd, and is operating at or above its permitted capacity, as indicated in the MFRs Schedule F-4. (EXH 8) The Three Oaks WWTP is permitted by DEP at 0.750 mgd. The average daily flow from the maximum month during the test year was 0.428 mgd. The two plants are not currently interconnected. Therefore, they must be considered as separate facilities for used and useful calculation purposes.

Gulf witness Cardey testified that the plants should be 100%. (TR 142) For used and useful consideration, the Utility presented the two plants as one system in its MFRs, Schedule F-6. (EXH 8) During cross examination, Mr. Cardey, when asked if the San Carlos and Three Oaks treatment plants are interconnected, stated that they are not. (TR 189) Mr. Cardey requested 118.6% used and useful percentage for the two wastewater treatment plants together by calculating a growth factor of 507 ERCs at 250 gallons per single family ERC plus a growth factor for the university of 209 ERCs at 250 gallons per ERC, plus a margin reserve of 3 years times 400 ERCs times 250 gallons per ERC. OPC attempted to show Mr. Cardey that his calculations were erroneous at the hearing. OPC offered calculations showing the current wastewater gallons per single family ERC experienced by Gulf are 158. (TR 177) Mr. Cardey did not

agree with OPC. However, when Staff performed the calculations, using flow figures and total ERCs taken from the MFRs schedule F-10, are done, the result is 158 gallons per single family ERC. (EXH 8)

OPC witness Biddy offered exhibits regarding used and useful percentages at the hearing, but had no further testimony to support his position. (EXH 18) OPC agrees with Staff in its post hearing brief that the San Carlos WWTP should be 100% used and useful. (BR 25) OPC differs in the used and useful percentage of the Three Oaks WWTP. (BR 25) The difference is due to the exclusion of a margin reserve allowance.

OPC witness Dismukes testified against granting a margin reserve because it represents capacity to serve future customers not current customers. (TR 314) OPC witness Biddy agreed that a utility must be in a position to serve changing needs of its present customers. (TR 264)

It is Commission policy to grant a reasonable margin reserve to enable the utility to charge present customers for some of the additional capacity. The San Carlos plant is operating above capacity therefore should be considered to be 100% used and useful. (EXH 8) The Three Oaks WWTP should be considered to be 87.15% used and useful. Calculations are shown on Attachment B. As shown, in Issue 7, Staff recommends a margin reserve of 36 months equaling 225,623 gpd. **The recommendation for a 36 month Margin Reserve is a change in Commission policy**. If the Commission decides to grant an 18 month margin reserve for the Three Oaks WWTP, the used and useful percentage will be 72.11%.

Therefore, based on the record, Staff recommends the San Carlos WWTP be considered to be 100% used and useful and the Three Oaks WWTP be considered to be 87.15% used and useful including a 36-month margin reserve.

ATTACHMENT B

UTILITY NAME: GULF UTILITY COMPANY
TEST YEAR: 12-31-96

WASTEWATER TREATMENT PLANT USED AND USEFUL CALCULATION
GULF UTILITY COMPANY (THREE OAKS PLANT)

% USED AND USEFUL = $\frac{(2+3-4)}{1}$ — 87.15%

(1) Capacity of plant — 750,000 GPD

(2) Average Daily Flow — 428,000 GPD

(3) Margin Reserve (not to exceed 20% of present ERCs):

(a) Average number of customers in ERCs — 2,817

(b) Projected yearly customer growth in ERCs by regressive analysis of most recent 4 years — 495

(c) Construction time for additional capacity (mths) — 36

Margin Reserve = $3b \times \left(\frac{3c}{12mths}\right) \times \left(\frac{2}{3a}\right) =$ — 225,623 GPD

(4) Excessive Infiltration — 0 GPD

(a) Total amount — 0 GPD — 0% of Avg. Daily Flow

(b) Reasonable amount — 42,800 GPD — 10.00% of Avg. Daily Flow

ISSUE 16: What are the appropriate used and useful percentages for the water and wastewater facilities?

RECOMMENDATION: No decision on this issue is necessary because all used and useful percentages were discussed and covered in Issues 12 through 15. Staff recommendations can be found in each Issue. (FUCHS)

POSITION OF THE PARTIES

GULF: These are set forth in the MFRs and discussed in issues 12 through 15 above.

OPC: See Issues 12-15.

STAFF ANALYSIS: No decision on this issue is necessary because all used and useful percentages were discussed and covered in Issues 12 through 15. Staff recommendations can be found in each Issue.

ISSUE 17: Are adjustments necessary to increase CIAC and decrease equity for lines built for the Caloosa Group (Audit Disclosure 1)?

RECOMMENDATION: Yes. CIAC should be increased by $68,114 for water and $92,815 for wastewater. Equity should be decreased by $160,929. Accumulated Amortization of CIAC should be increased by $10,855 for water and $14,145 for wastewater. Test year amortization should be increased by $2,106 and $2,755 for water and wastewater, respectively. The utility should be required to adjust its books and records to correct the accounting treatment for this transaction. (MERCHANT)

POSITION OF THE PARTIES

GULF: Gulf's accounting for the Caloosa Trace transaction should be approved with no adjustments because it strengthens Gulf's equity base, reflects the continuing commitment of the stockholders to provide quality service on the area, and will benefit consumers over the long pull.

OPC: Yes, CIAC should be increased by $68,144 for the water operations and by $92,815 for the wastewater operations. Appropriate adjustments should likewise be made to accumulated amortization of CIAC and amortization expense. Equity should be decreased by $160,929.

STAFF ANALYSIS: Staff witness Welch testified about a property transaction that occurred between Gulf and an affiliate named the Caloosa Group. Caloosa Trace is a development owned by the Caloosa Group, which has the same owners as Gulf. Normally, Ms. Welch stated, when developers connect to the system, the lines and hydrants are contributed by the developers and recorded on the books of the utility as a debit to plant and a credit to CIAC. On February 20, 1990, Gulf recorded water and wastewater assets of $59,684 and $92,815, respectively, for Phase 1 and $8,430 in water assets for Unit 16, Phase 8, for the Caloosa Trace Development. Ms. Welch testified that instead of a credit entry to CIAC, the owners were given stock in the utility in exchange for the assets. Gulf had responded that the transaction had been reviewed by its auditors and was in compliance with all rules and regulations of the Commission and generally accepted accounting principles. Ms. Welch recommended that the transaction should have been recorded the same as those for non-affiliates transferring property to the utility. (TR 450; EXH 24, page 21)

OPC witness Dismukes also testified that Gulf and Caloosa had the same owners, and added that the ownership in Caloosa was in the same proportion as the ownership for Gulf. She stated that in response to OPC's Interrogatory 36, Gulf explained that the transaction was a routine business transaction was straightforward and violated no rule or law. Ms. Dismukes believed that Gulf had not provided a satisfactory reason why its developer-affiliate should be treated any differently than a non-affiliate developer. Accordingly, she recommended that CIAC be increased by $68,114 for the water operations and $92,815 for the wastewater operations. A corresponding adjustment should also be made to reduce equity by the same amount. (TR 291-292, 296)

Staff witness Rendell testified about the developer agreements between these two corporations on file with the Commission. He stated that those agreements covered the development of all phases of Unit 16. Mr. Rendell believed that any contributions made by developers, including an affiliate corporation, should be booked to CIAC. Exhibit 20 (WTR-1) reflects in Section 1(c) that any property received by the utility from the developer should be considered CIAC. Sections 1(j)&(k) indicate those water lines constructed by the developer should be considered on-site and off-site facilities, and Sections 3 and 4 of the agreement cover the installation of these facilities. Mr. Rendell testified that Gulf's tariff also required these facilities to be contributed. To do otherwise, in his opinion, would be discriminatory. He concluded that Rule 25-30.585, FAC, designates that, at a minimum, the cost of installing water transmission and distribution facilities and sewage collection facilities should be considered CIAC. (TR 379-383; EXH 20)

Utility witness Moore testified that the transaction between the companies was very open and straight forward, and the Commission should approve the way it was recorded for two reasons. First, he stated that there was a substantial difference in the conditions under which the stockholders obtained service in contrast to other developers in the area. Secondly, the Company's accounting of the transaction strengthened the company financially, benefitting the customer over the long pull. Instead of shifting the costs to other developers or customers, both have benefitted. (TR 538-539)

Mr. Moore included information regarding growth in customers and sales and the manner in which Gulf's operations have been

financed through the efforts of the shareholders and industrial development revenue bonds (IDRB) since the present owners acquired the company. He further stated that potential customers need the availability of service. In any real estate development, some group has to generate "up-front" money and construct facilities to have capacity available to serve that growth. Mr. Moore testified that it is Gulf's viewpoint that it, instead of the developer, must provide this money, and the stockholder has had to absorb the losses from this up-front investment. Further, he stated that the benefits of providing this investment in capacity go to the builders in the area and that equity dictates this situation be brought into balance. (TR 539-543)

In addition, Mr. Moore stated that from 1982-1988, the utility sustained losses from operations, but increased rates and charges in 1986, 1988 and 1991 brought the operations back into the black. However, earnings again suffered starting in 1991 when stockholder losses of over $1.5 million occurred from the differences in IDRB loans and temporary investments of these government securities funds. When Gulf stockholders absorb these losses, and the customers and developers benefit by having service available when needed, there is a substantial difference in the service provided to the stockholders in Gulf/Caloosa and the other developers in the area. For that reason, Mr. Moore contended that no discrimination occurred in the transaction. (TR 543-545)

Mr. Moore further stated that a higher equity base would benefit the customer very significantly. This would allow the utility better prospects of successfully negotiating the refinancing of the IDRBs with lower interest rates, plus freeing $1 million of reserve funds to invest in new facilities. Although the refinancing was suspended pending the Commission's investigation into overearnings, these actions could lower expenses by more than $300,000 annually. Since the cost of this equity transaction by Gulf/Caloosa only costs the customers an additional $14,800, the benefits of this refinancing pale in comparison to those a stronger balance sheet provide. If equity is further reduced from its already low level, Mr. Moore concluded that it would be even harder to sell bonds and attract new equity to finance construction if Gulf cannot demonstrate that it can sustain adequate earnings in the future. (TR 545-546)

On rebuttal, Mr. Moore admitted that the customers had no part in Gulf's decision to incur more debt than necessary at the time it

incurred $1.5 million in losses, and that the stockholders, not the customers, should bear those losses. He stated that if any unaffiliated developer sustained losses on obtaining more debt than was required that the developer would still have to contribute the lines. (TR 579-581)

Staff disagrees with Mr. Moore's assessment that no discrimination between developers occurred. His first point that there is a substantial difference between the stockholder and the other unaffiliated developers brings this to light. Staff believes that there should be no substantial differences in the way affiliate and non-affiliate developers are treated. Further, we disagree with Mr. Moore's statement that Gulf violated no rule or regulation of the Commission. Both Rule 25-30.565, FAC, and the utility's tariff state that off-site lines should, at a minimum, be contributed. Neither the rule or the tariff make any distinction between affiliate and non-affiliate developers.

Regarding Mr. Moore's second point, staff agrees that Gulf has a relatively low equity ratio and that this transaction as booked increased its equity. However, this transaction should not be the mechanism used to infuse equity into the company. As evidenced by Mr. Moore's testimony, since the current owners acquired the company, they have infused equity at various times when the stockholders deemed it necessary. Just as Mr. Moore states that the revenue impact of this equity transaction is minimal for the customers, staff questions whether a $160,000 equity adjustment would have such a material impact on Gulf's overall financial stability. It is logical that a greater equity infusion would be necessary to affect the long-term financial viability of a utility of this size.

Staff also disagrees with Mr. Moore in his belief that it is Gulf's responsibility to provide up-front money to affiliates or any other developers in the area. Staff believes that while a prudent utility should be concerned about growth potential in its territory, to extend its financial risks to the benefit of the builders in the area is inappropriate. This is clearly a developer's risk and should not be taken on by a regulated utility. This blurring of the lines between developer and utility has long been a concern of the Commission, to assure that the utility's customers pay for only those costs legitimately incurred to provide utility service. Further, we believe that Mr. Moore is placing too much emphasis on the financial responsibility of Gulf with respect

to this issue. Regardless of how these assets are recorded, Gulf still maintains the statutory responsibility of providing timely and quality service to its customers. Prudence also dictates utility service be provided in the least costly manner available.

Based on the above, staff believes that the transaction was discriminatory and was violating the utility's tariff and the Commission's rules and regulations. As a result CIAC should be increased by $68,144 for the water operations and by $92,815 for the wastewater operations. Adjustments should likewise be made to increase accumulated amortization of CIAC by $10,855 for water and $14,145 for wastewater. Test year amortization of CIAC should be increased by $2,106 and $2,755 for water and wastewater, respectively, and equity should be decreased by $160,929. The utility should be required to adjust its books and records to correct the accounting treatment for this transaction.

ISSUE 18: Are adjustments necessary to reflect prepaid CIAC as used and useful in rate base? (Audit Disclosure 8)

RECOMMENDATION: Yes, to the extent that prepaid CIAC relates to plant constructed and included as used and useful in the margin reserve. Since this is covered in Issue 19, no additional adjustment is necessary. (MERCHANT)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to reflect prepaid CIAC as used and useful in rate base because prepaid CIAC is related to future customers.

OPC: Yes, to the extent that the associated plant is included in rate base. In the absence of a showing by the utility that the plant related to prepaid CIAC is not included in rate base, CIAC should be increased by $379,319 for the water operations and by $207,304 for the wastewater operations.

STAFF ANALYSIS: Staff witness Welch and OPC witness Dismukes both recommend that prepaid CIAC associated with plant that is in service be included as on offset to rate base. (TR 454-455, 309; EXH 24, page 31) Ms. Welch testified that since the utility only made a used and useful adjustment to the Corkscrew water plant, all the connections in prepaid CIAC appear to be related to plant already in service. Although the utility is not yet collecting revenue related to these contributions, it is earning a return on the assets to which the contributions relate since the assets were considered 100% used and useful. Ms. Welch stated that excluding the CIAC received from FGCU, Gulf has a balance of $550,999 for water and $207,304 for wastewater. This balance was based on the general ledger balance as of August 31, 1996, which was the most current actual data available during the audit. (EXH 24) According to Ms. Welch, the utility transferred $171,680 in water prepaid CIAC in the MFRs to used and useful CIAC, with none transferred for wastewater. She recommended that CIAC be increased by $379,319 for the water operations (net of the transfer) and by $207,304 for the wastewater operations. (TR 454-455)

On cross examination, Ms. Welch was asked if she matched up the prepaid CIAC with existing plant. She responded that she reviewed an exhibit Ms. Andrews provided that showed that the wastewater prepaid CIAC could be matched to individual plants that

are existing and in service. Ms. Welch also testified that when she asked if any additions were needed to the wastewater plant, the utility's answer was no. With respect to the water prepaid CIAC, Ms. Welch testified that Ms. Andrews told her that she could not identify the plants to which the water prepaid CIAC related. (TR 480-481)

Ms. Dismukes testified that she reviewed the staff audit workpapers and other information provided by the utility and the information was not clear to what the prepaid CIAC related. Further, Ms. Dismukes reviewed the exhibit provided to the auditors, and the utility's response which stated that the two water plants were interconnected and the prepaid CIAC could not be identified by specific plant. (TR 349-350) She also agreed that the 13-month average balance of prepaid CIAC projected by the utility in its MFRs could be derived by taking the total balance of CIAC, including prepaids, less the 13-month averages of the water and wastewater amounts provided. (TR 326-327) The utility's MFRs did not breakdown the 13-month balance of prepaid CIAC between water and wastewater. (EXH 8)

Utility witness Cardey testified that the proposals of staff and OPC are inconsistent with the legal framework of ratemaking, and the fundamentals in the MFRs. He defines a test year as the synchronization of four basic determinants in setting rates: (1) the revenues produced under the rate structure, (2) the expenses, including depreciation and taxes incurred to produce these revenues, (3) the property (rate base) that provides the service, and (4) return on said rate base. Gulf's investment in non-used and useful plant exceeds prepaid connection fees, including the $300,000 to be received in the future from the SFWMD by 21%. Mr. Cardey stated that the prepaid connection fees relate to future customers and Gulf's contractual obligation to meet their service requirement. Further, the treatment afforded in the MFRs is consistent with prior Commission rate orders for Gulf. (TR 641-642)

On cross examination, Mr. Cardey stated that the prepaid CIAC relates to central or treatment plants, as opposed to lines. He added that Gulf will have to build additional water and/or wastewater plant to be able to serve the future customers which have prepaid CIAC. However, he also stated that many prepaid connections will connect onto the system in the next year to three years, which is consistent with the utility's requested margin

reserve period. When asked if the utility keeps any documentation or worksheet to support that the prepaid connections are not associated with used and useful plant, Mr. Cardey responded with a general comment that it is just a matter of internal accounting procedures. (TR 675-678)

In its brief, OPC argued that it is the utility's burden to prove the issues identified in a rate proceeding. In the instant case, the utility has failed to meet its burden. Both Ms. Dismukes and Ms. Welch testified that they had requested information to determine if prepaid CIAC related to plant in service, and except for wastewater prepaid CIAC which is related to plant in service, the utility did not provide the data necessary to make such a determination. Accordingly, in the absence of proof to the contrary, OPC argued that the Commission should include as an offset to rate base prepaid CIAC related to both the utility's water and wastewater operations.

In its brief, the utility argued that the evidence showed that Gulf's internal accounting procedures "assure that prepaid balances for both water and wastewater are not associated with the used and useful plant already included in projected test year rate base." (BR 30) Staff disagrees with Gulf's interpretation that this assurance is provided in the record. The utility's witness states that Gulf keeps separate track of the payments of prepaid CIAC to match plant and CIAC. A reasonable interpretation of this evidence would lend one to believe that this is done for book purposes. There is no such reference in the record that such was done for the purposes of determining the prepaid CIAC associated with the projected test year rate base. If one had been done, it should have been provided in response to discovery requests made by the parties. The utility even admits in its brief that no such study exists supporting Ms. Welch's assumption that the prepaid CIAC appears to relate to plant already in service. (BR 30)

Staff agrees with OPC that it is the utility's burden to show that its balance of prepaid CIAC is not related to plant included in rate base. If the utility had provided sufficient evidence to show that these prepaid fees related to plant that is non-used and useful beyond the margin reserve period or related to plant not yet constructed, staff believes that the burden could have been met. Lacking any of this support, staff must analyze the dollar amount of plant removed from rate base as non-used and useful and compare this with the projected balance of prepaid CIAC. This analysis is

somewhat consistent with Mr. Cardey's comparison. His analysis was made on the utility's balance of non-used and useful water plant. However, as discussed in Issues 12-16, staff is recommending used and useful adjustments be made to both the water and wastewater treatment plants, including the well fields. As such, staff believes that the evidence supports making this comparison using staff's recommended amounts.

Staff generally agrees with Mr. Cardey's definition of a test year, but we believe that he is missing one component that should be included. Section 367.081 (2)(a), Florida Statutes, requires that the Commission set rates only on plant that has been found used and useful and that no return be allowed on contributed plant. If the Commission allows a utility to include a margin reserve in its used and useful calculation, this allows a utility to recover its investment required to be ready to serve future customers. A determination, however, should be made to ascertain that a utility that collects prepaid CIAC actually has invested in this plant. If the prepaid CIAC offsets the dollar amount of plant included in the margin reserve, and is not included as a reduction in rate base, then the Commission would be setting rates on contributed plant. As such, staff believes that it is necessary to compare these amounts in determining what amount of prepaid CIAC, if any, should be included in rate base.

In making this comparison, staff started with Ms. Welch's balance of prepaid CIAC, based on the actual balance as of August 31, 1996. We do note, however, that this balance would be inconsistent and does not match the projected rate base and assumptions as filed by the utility in its MFRs. While the record supports the projected 13-month average of total prepaid CIAC, it is silent as to the projected breakdown between water and wastewater. Given the large difference between Gulf's water and wastewater customers, (66% to 34%, respectively), it would be inaccurate to analyze this on a total company basis. (EXH 8) We believe that it would be a reasonable alternative to assume that the ratio of the actual balance between water and wastewater as of August, 1996, would apply to the projected balance. This estimate, however, does not take into account staff's recommendation to switch the service availability charges between water and wastewater from $800 to $550. Regardless, staff recommends that this is only reasonable alternative that the record provides to determine the split of prepaid CIAC. The projected 13-month balance in the MFRs of prepaid CIAC is as follows:

Total CIAC Per Balance Sheet	$22,274,234
Water U/U CIAC	(12,220,685)
Wastewater U/U CIAC	(9,060,383)
Total Prepaid CIAC Per MFRs	$ 993,166

Based on the actual balance of prepaid CIAC as of August, 1996, the ratio between water and wastewater is 64.66% for water and 35.34% for wastewater. By applying those percentages to the 13-month average balance in the MFRs, the allocated amounts should be $642,207 and $350,978 for water and wastewater, respectively.

In Issue 19, staff is recommending that the full amount of net water plant included in the margin reserve, $193,700, be recognized as used and useful CIAC. The remaining balance of water prepaid CIAC of $448,507 ($642,207-$193,700) should be matched with non-used and useful plant and should not reduce rate base. For comparison purposes, staff's recommended non-used and useful net plant balance (plant less accumulated depreciation) is $888,015 for water, which is greater than the amount of non-used and useful prepaid CIAC.

For the wastewater system, staff has recommended in Issue 19, that CIAC of $594,000 be imputed on the margin reserve. Accordingly, the estimated $350,978 in wastewater prepaid CIAC is less than the total amount CIAC imputed on the margin reserve. Therefore, no additional adjustment to reflect prepaid wastewater CIAC is appropriate. Staff's recommended net amount of wastewater non-used and useful plant is $527,581, and is not funded by any remaining prepaid CIAC.

In total, as discussed in Issue 19, staff is recommending that the CIAC associated with the margin reserve for both water and wastewater is $787,700. This is $205,483 less than the total company balance of projected CIAC of $993,183 for the 1996 test year. As a result, staff believes that the reflection of prepaid CIAC as used and useful CIAC in rate base is reasonable and should be approved, with no additional adjustments made other than those recommended with the margin reserve in Issue 19.

ISSUE 19: If a margin reserve is approved, should CIAC be imputed on margin reserve, and if so, what amount?

RECOMMENDATION: Yes. Since the utility has prepaid CIAC, those amounts should be first recognized as used and useful to be included in rate base associated with the margin reserve. It is appropriate to reclassify $193,700 of water prepaid CIAC to used and useful CIAC for the margin reserve. For the wastewater system, it is appropriate to reclassify prepaid CIAC of $350,978 and impute $243,022, for a total increase to CIAC of $594,000. This limits wastewater CIAC for the margin reserve to 50% as an averaging method to recognize that the imputed amount will be collected over the life of the margin reserve period, not all at the beginning. Adjustments should also be made to increase accumulated amortization of CIAC by $2,737 and $9,924 and test year amortization expense by $5,475 and $19,848 for water and wastewater, respectively. (MERCHANT)

POSITION OF THE PARTIES

GULF: If a margin reserve is approved, CIAC should not be imputed on margin reserve.

OPC: Yes.

STAFF ANALYSIS: Utility witness Cardey testified that he did not impute CIAC associated with the margin reserve. He stated that the margin reserve reflects the Company's obligation to serve existing and potential customers, and it invests in central plants to meet this service obligation. Gulf has included the investment in margin reserve in used and useful investment. If CIAC were imputed, the net effect would be to negate the Company's capital investment in plant and to have the stockholders absorb the cost of meeting the growth of the area. The 1996 test year matches gross revenues and the utility property that provides the service. If the Commission imputes CIAC from future customers, Mr. Cardey believed that the imputation would cause the test year to be out of synchronization. (TR 145)

OPC witness Dismukes testified that if margin reserve is included in the used and useful calculations, then, to achieve proper matching, an amount of CIAC equivalent to the number of equivalent residential connections (ERCs) represented by the margin reserve should be reflected in rate base. When determining the

amount of imputed CIAC, the Commission should use the proposed, interim, or final new capacity charges. The CIAC that will be collected from these future customers would serve to mitigate the impact on existing customers required to pay for plant to serve future customers. (TR 315-316)

Ms. Dismukes stated that imputation of CIAC on the margin reserve has been a longstanding policy of this Commission. She listed two orders where the Commission's practice of imputing CIAC on margin reserve is well documented: Order No. 20434, issued on December 8, 1988 in Docket No. 871134-WS; and Order No. PSC-93-0301-FOF-WS, issued on February 25, 1993 in Docket No. 911188-WS. If the Commission does not continue to impute CIAC associated with the margin reserve, Ms. Dismukes believed it would place the risk of customer connections on the backs of current ratepayers. The risk that future customers connect to the system, as projected by the utility in its margin reserve calculations, should be borne by stockholders, not customers. This is a risk that the utility is compensated for in its allowed return on equity. If the Commission were to change its policy, the utility would not only be provided with an opportunity to overearn, it would create a significant incentive for the utility to over project customer growth for margin reserve purposes. Imputation of CIAC on margin reserve gives the utility an incentive to properly project future connection and it matches plant in service with CIAC. In addition, if the Commission changes its policy it should likewise reduce the utility allowed return on equity to recognize that customers now bear this risk not the utility's stockholders. (TR 316-317)

Ms. Dismukes also agreed on cross examination that if prepaid CIAC has already been collected by the utility and a margin reserve is allowed in plant, that any adjustment to rate base would not be an imputation but rather a reclassification of prepaid to used and useful CIAC. Regardless of whether a company has prepaid CIAC or not, the imputation of CIAC on the margin reserve has merit. (TR 326-327) However, Ms. Dismukes testified that the Commission should not impute or reclassify prepaid CIAC more than the amount of plant in service. She also agreed that the imputation of CIAC on the margin reserve and any reclassification of prepaid CIAC to used and useful should not overlap. (TR 348-349)

On rebuttal, Mr. Cardey testified that imputing CIAC on the margin reserve deprives the utility of a return on and a return of investment in margin reserve. He stated that the Commission has

recognized the company's obligation to meet the service needs of existing customers and anticipate the service needs within the area it serves by allowing a margin reserve. The imputation causes a mismatch of economics with the stockholder by absorbing the cost of meeting this obligation imposed on the company. (TR 645)

Mr. Cardey computed what he believed to be the impact of imputing CIAC on the water operations. Based on the plant requested in the filing, his calculation reflected that the net plant in margin reserve in the water operations would be $397,330. If imputed, $412,500 in CIAC would be deducted from rate base, leaving a negative amount of $15,170. The loss of earning and loss of capital each year would be $55,893. (TR 645-646) Mr. Cardey stated that imputing CIAC as shown above ignores the company's obligation to serve the changing demands of present and potential customers. Further, Mr. Cardey testified that in proposed rule making Docket No. 960258-WS, two staff witnesses, Mr. Robert J. Crouch, P.E., and Mr. N. D. Walker, recommended a margin reserve with no imputed CIAC. Mr. Cardey's testimony is consistent with the two staff witnesses in the above docket that no imputation of CIAC be made. (TR 646-647)

In its brief, OPC argued that the company presented no new evidence that would require the Commission to change its policy of imputation of CIAC on margin reserve. Staff agrees with OPC that Gulf has not presented any new evidence which would require the Commission to change its policy in this docket.

In Gulf's last water rate case, (Docket No. 900718-WU, Order No. 24735, issued on July 1, 1991), the Commission imputed CIAC on the margin reserve. Specifically, the Commission found that:

> Commission policy is that only the utility's investment in the margin reserve should be recognized in rate base and the CIAC should not, however, reduce rate base further than if no margin reserve had been allowed. Without this adjustment, the utility would be allowed to earn a return on plant that would be contributed by future customer. As its policy, Gulf collects prepaid CIAC from developers in advance of when the future customers connect to the system. As such, this adjustment is not an imputation but a reclassification of prepaid to "used and useful" CIAC.

In Gulf's last wastewater rate case (Docket No. 880308-SU, Order No. 20272, issued on November 7, 1988), the Commission also imputed CIAC on the margin reserve allowed in plant. Staff does not believe that the circumstances since those last cases have dramatically changed. The issue of imputation of CIAC on the margin reserve for this utility is unique in that Gulf maintains a balance of prepaid CIAC on a recurring basis.

Further, the proposed rulemaking docket that Mr. Cardey referred to in his testimony has not been finalized or even considered by the Commission at Agenda as of the date this recommendation was filed. Regardless, the testimonies of those staff witnesses are not included in the record here and should not be considered as evidence in this docket. Staff also would point out that the Commission's policy, as addressed in the prior Gulf rate case dockets does not impute more CIAC than the amount of plant included in the margin reserve. Even if staff agreed with the plant investment included in Mr. Cardey's calculation of imputed CIAC, we would not agree that the full amount be imputed to reduce rate base further than the balance of plant included.

In conclusion, staff believes that the evidence in this case indicates that the Commission should continue to apply its current practice of imputing CIAC on the margin reserve. In the water facilities this equates to $354,750, based on the 645 ERCs included in the margin reserve (1½ years) times the $550 plant capacity charge recommended. Since net plant included in the margin reserve is only $193,700, the amount of CIAC recognized in rate base should be no greater. As discussed in Issue 18, the full amount of net water plant included in the margin reserve is funded by prepaid CIAC. Accordingly, no imputation is necessary, but instead it is appropriate to reclassify $193,700 of water prepaid CIAC to used and useful CIAC for the margin reserve.

For the wastewater facilities, the gross amount of CIAC collected would be $1,188,000. This is based on the 1,485 ERCs included in 3-year margin reserve times the recommended $800 plant capacity charge. Since the net plant included in the margin reserve of $1,234,992 is greater than the gross CIAC, no net-plant limit is necessary. However, as discussed in Issue 18, the amount of prepaid CIAC for the wastewater system is projected to be $350,978. Staff is recommending that this portion of the CIAC on the margin reserve be reclassified from prepaid CIAC to used and useful CIAC, making an imputation of this amount unnecessary.

However, the remaining balance to be imputed for wastewater needs to be addressed.

In the most recent rate proceedings of other water and wastewater utilities, the Commission has decided to impute only 50% of the CIAC estimated to be collected during the margin reserve period. This policy is based on the premise that all of the CIAC related to the margin reserve will not be collected on day-one of the period, but evenly over the three-year period. See Order No. PSC-97-0388-FOF-WS, issued on April 7, 1997; Order No. PSC-96-1320-FOF-WS, issued on October 30, 1996; and Order No. PSC-96-1338-FOF-WS, issued on November 7, 1996. Fifty percent of the gross CIAC for the wastewater system, stated above, is $594,000. Removing the balance of prepaid CIAC of $350,978, leaves an additional increase to impute CIAC of $243,022.

In conclusion, staff believes that to the extent that Gulf has prepaid CIAC, those amounts should be first recognized as used and useful to be included in rate base associated with the margin reserve. We believe that it is appropriate to reclassify $193,700 of water prepaid CIAC to used and useful CIAC for the margin reserve. For the wastewater system, staff recommends that it is appropriate to reclassify prepaid CIAC of $350,978 and impute an additional $243,022, for a total increase to wastewater CIAC of $594,000. Adjustments should also be made to increase accumulated amortization of CIAC by $2,737 and $9,924 and test year amortization expense by $5,475 and $19,848 for water and wastewater, respectively.

ISSUE 20: What is the dollar amount of plant costs included in rate base, and what dollar amounts should be included in rate base as CIAC, related to funds received from the South Florida Water Management District's (SFWMD) Alternate Water Supply Grants Program?

RECOMMENDATION: The dollar amount of plant costs that should be included in rate base is $66,667 and $133,333 for water and wastewater, respectively. CIAC related to this plant should be increased in the amount of $15,385 for water and $30,769 for wastewater, which reflects the 13-month average balance of plant included in rate base. Additionally, test year amortization and accumulated amortization of CIAC (AACIAC) should be increased by $142 and $236 for water and wastewater, respectively. Staff also recommends that, as the project is completed, CIAC up to the $300,000 received from the SFWMD should be included in rate base as an offset to plant investment. (WEBB)

POSITION OF THE PARTIES

GULF: The amount of the effluent reuse mixing system plant costs included in rate base should be $446,090, and the dollar amounts of CIAC (net) is $185,371.

OPC: The total plant costs associated with the reuse funding project included in rate base is $232,911. Since the Company will receive $300,000 in funding, $232,911 of the funds to be received from the water management district should be included as an offset to rate base, as CIAC.

STAFF ANALYSIS: According to the testimony of witness Andrews, Gulf requested funding under the SFWMD's Alternate Water Supply Grants Program. The request was for $375,000 and the grant will fund the cost of constructing and installing a portion of the control system and instrumentation for monitoring flow and quality parameters at the three effluent reuse disposal sites. Ms. Andrews stated that the grant was not included in the MFRs (as CIAC). (TR 850-851)

Utility witness Cardey stated that the grant has been approved in the amount of $300,000, but that no money has been received, yet. (TR 194) On cross examination, Mr. Cardey agreed to provide a late-filed exhibit which would detail the costs of the reuse project, where the costs are located in the MFRs and the account

numbers. (TR 197) Exhibit No. 11 details all of the projected costs associated with this reuse project. The project cost for the holding tank is $700,000, inclusive of transfer and pumping equipment and metering and controls. Additionally, there is a reuse line reflected at $200,000. This exhibit shows that the costs for the reuse line only were recorded in water account 339.3, at $66,667 and wastewater account 382.4, at $133,333. The exhibit states that these amounts were recorded in the respective plant accounts in the MFRs in December, 1996.

Upon staff's analysis of the plant accounts in the MFRs, on pages 16 and 22 for water and wastewater, respectively, we have found that the costs for the reuse line were included in the company's projections in October of 1996, not December. (EXH 8) To determine the 13-month average of CIAC to include in rate base as an offset to the plant costs, we multiplied the water and wastewater amounts for the reuse line by three and then divided by thirteen. Accordingly, the record supports that the appropriate amount of CIAC to be included in rate base, as it relates to the reuse line, is $15,385 for water and $30,769 for wastewater. Test year amortization and AACIAC is similarly computed, using the appropriate plant depreciation rates, and is $142 for water and $236 for wastewater for the test year. Staff believes that the record supports these adjustments, as Mr. Cardey has testified that the reuse line has been constructed and was in-service in the test year. (TR 199-200)

According to the utility's brief, the amount of the reuse project costs included in rate base should be $446,090 and the dollar amount of CIAC is $185,371. (BR 32) According to Exhibit No. 11 and to the utility's position in its brief, the utility's calculation considers the holding tank, pumps, and controls associated with the project. However, the utility did not consider the reuse line.

OPC's determination of total plant costs associated with the reuse project that are included in rate base is $232,911. Since OPC has determined this amount of plant to be included in rate base, its position is that the same amount should be included as CIAC as an offset to rate base. OPC's calculation includes a component related to the holding tank, pumps, and controls and a component related to the reuse line. OPC came to the same 13-month average as staff for the reuse line. (BR 30-31)

As outlined in Issue 3, the reject holding tank had not been constructed by the end of the test year, nor did the utility have contracts for construction, nor did the utility have bids or a firm start/completion date in hand as late as the hearing dates of March 4-5, 1997. (TR 129) Accordingly, staff has recommended, in Issue 3, that the holding tank be disallowed in rate base. To be consistent with staff's recommendation in Issue 3, we cannot consider the inclusion of the holding tank in this issue in terms of offsetting the related CIAC, as the evidence does not support that the holding tank should be included in rate base. Therefore, staff does not recommend an increase to CIAC for the costs related to the holding tank.

Thus, the year-end dollar amount of plant costs that should be included in rate base, related to the reuse line only, is $66,667 and $133,333 for water and wastewater, respectively. CIAC related to this plant should be increased in the amount of $15,385 for water and $30,769 for wastewater, which reflects the 13-month average balance of plant included in rate base. Additionally, test year amortization and accumulated amortization of CIAC should be increased by $142 and $236 for water and wastewater, respectively. Staff also recommends that, as the project is completed, CIAC up to the $300,000 received should be included in rate base as an offset to plant investment.

ISSUE 21: Are adjustments necessary to Accumulated Amortization of CIAC (AACIAC) to amortize cash contributions using yearly composite rates? (Audit Exception 2)

RECOMMENDATION: Yes, staff recommends that the Commission should reduce AACIAC for both the water and wastewater systems in the amount of $115,371 and $98,456, respectively. Additionally, we recommend that the Commission should increase test year amortization for water by $12,967 and decrease test year amortization for wastewater by $7,329. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary. Gulf amortizes CIAC using a composite amortization rate that is the same as the composite rate of utility plant, excluding common plant. This is one of the alternative methods permitted pursuant to rule 25-30.140, FAC, which Gulf has followed for a number of years.

OPC: Yes. Accumulated Amortization of CIAC in rate base should be decreased by $115,371 for the water operations and by $98,456 for the wastewater operations. Similarly, the CIAC amortization expenses should be increased by $12,967 for the water operations and decreased by $7,329 for the wastewater operations.

STAFF ANALYSIS: According to staff's Audit Exception No. 2, Gulf has been amortizing contributed property at the same rate as the related asset, but contributed cash is being amortized at a rate of 4.35% for water and 3.13% for wastewater. The utility does a true-up to come to the composite depreciation rates for total CIAC amortization. Staff witness Welch testified that the utility calculates 1) total depreciation for water divided by total plant for water and does the same for wastewater, and 2) total CIAC amortization divided by total CIAC for water and for wastewater. Next, the utility multiplies the difference in these two rates by the ending balance of CIAC and makes an adjustment to the reserve account for CIAC. (EXH 24, pg. 5, TR 445)

Ms. Welch stated that the audit staff performed a calculation to arrive at composite depreciation rates for 1996, using the plant at August, 1996. The composite rates exclude intangible and common plant and are 3.2% for water and 3.5% for wastewater. Further, Ms. Welch testified that the utility should be computing yearly composite rates only for the amortization of cash CIAC. Ms. Welch

testified that when the utility makes the adjustment as described above, the calculation is effectively changing total CIAC amortization to a composite rate and is eliminating the amortization of contributed plant at the same rate as the related asset. Further, Ms. Welch testified that the utility's true-up calculation should only apply to cash CIAC. (TR 445)

The staff auditors computed amortization expense for the projected test year by utilizing the August, 1996 balance of CIAC. The differences between staff's estimate of what amortization expense should be and the projected amount contained in the MFRs follow: (EXH 24, pg. 5)

	WATER	WASTEWATER
AUDIT STAFF'S CALC.	$351,176	$282,877
PER MFRs, SCH B-13	338,209	290,206
DIFFERENCE	12,967	(7,329)

Witness Welch testified that the staff auditors calculated the 13-month average of AACIAC by utilizing the utility's general ledger balance of AACIAC for the period ending September, 1996. The auditor's average, when compared to the average AACIAC contained in the MFRs, results in a reduction to water rate base of $115,371 and a reduction to wastewater rate base of $98,456. Audit staff's computation does not include forecasted CIAC not yet recorded on the company's books. The forecasted CIAC relates to the FGCU in the amount of $261,350 and to the force main on Corkscrew in the amount of $127,526. Ms. Welch concluded that, if the projected CIAC was amortized for the entire year, using a 13-month average, the increase would be $11,588 inclusive of water and wastewater. (TR 446)

The recommendation in the audit report indicates that the utility should recalculate amortization on cash using yearly composite rates and that the utility should not true-up contributed property to those rates. Thus, the report states that water expenses need to be increased by $12,967, and wastewater expenses need to be decreased by $7,329. The audit staff did not calculate the corrections to AACIAC that would occur as a result of the

utility's past (prior to the test year) true-up of contributed property at composite rates. As described above, audit staff only calculated an estimate of what AACIAC should be for the test period, based on the utility's general ledger balance. (EXH 24, pg. 6)

Utility witness Andrews stated that the utility amortizes CIAC using a composite rate and that Gulf has been doing this for a number of years. Further, she testified that this is one of the alternative methods permitted by Rule 25-30.140, Florida Administrative Code. Ms. Andrews testified that Ms. Welch's proposal to amortize CIAC by function is a change from the utility's current permitted practice. Ms. Andrews stated that she disagrees with the underlying procedures of implementing audit staff's recommendation. Ms. Andrews also stated, "we think a rate case is the wrong forum for settling these differences." (TR 847)

Ms. Andrews made the following comments regarding Audit Exception No. 2: (1) audit staff used a period different from the test year; (2) since audit staff tested the period September, 1995 through August, 1996, their assumptions are not consistent with a 13-month average required by the MFRs; and (3) the utility requested new service availability charges for both water and wastewater, so the balance in the MFRs is different from the general ledger. (TR 847-849)

On cross examination, witness Andrews was asked to read Rule 25-30.140, (8) (a), Florida Administrative Code, which, in part, states:

> The CIAC plant shall then be amortized either by account, function or bottom line depending on availability of supporting information. **The amortization rate shall be that of the appropriate account or function where supporting documentation is available to identify the account or function of the related CIAC plant.** Otherwise, the composite plant amortization rate shall be used. (emphasis added)

Ms. Andrews confirmed that the utility does maintain records of CIAC by function and that these records were available at the time Gulf filed this rate case. She testified that she came to work for

the utility in the 1980s and that the records were not as detailed at that time. Ms. Andrews testified that, since her employment, she has been able to update CIAC records by function. However, Gulf has continued to use a composite rate when amortizing CIAC. (TR 872-877)

After reading the rule on CIAC amortization, witness Andrews could not agree that, where supporting documentation is available by function, there is no option to use a composite amortization rate. She testified that Gulf has always used composite amortization rates, including the use of such rates in preparation of the MFRs. Ms. Andrews stated, again, that this rate proceeding is not the appropriate forum to determine whether the utility has used appropriate amortization rates. She testified that after this proceeding is over, that would be the appropriate time to discuss the correct method of amortizing CIAC. (TR 873-876)

Ms. Andrews was asked, at hearing, to provide a late-filed exhibit detailing the adjustments that would be necessary to AACIAC, assuming that the Commission disallowed Gulf's use of a composite amortization rate. In late-filed Exhibit No. 50, the utility did not provide an adjustment; instead, Gulf reiterated its position that it is an alternative under Rule 25-30.140, Florida Administrative Code, to use a composite amortization rate. (TR 876-877, EXH 50)

Staff agrees with Ms. Andrews that audit staff used the period from September, 1995 through August, 1996 in analyzing the balance of AACIAC. This fact is clearly stated in the audit report, along with the conclusion that audit staff did not calculate the corrections to AACIAC that would occur as a result of the utility's past (prior to the test year) true-up of contributed property at composite rates. Audit staff only calculated an **estimate** of what AACIAC should be for the test period, based on the utility's general ledger balance. For these reasons, the staff audit report contains a recommendation for the utility to correct the balance of AACIAC. Also, Late-Filed Exhibit No. 50 should have reflected the utility's corrected balance of AACIAC, assuming the Commission disallows the use of a composite amortization rate. As discussed above, the utility has not provided this information. In fact, witness Andrews continued to state that Rule 25-30.140, (8) (a), Florida Administrative Code, gives the utility an option to amortize CIAC using a composite rate even if the plant records are available by function. (TR 873-376)

Staff does not agree with Ms. Andrews' comments that this rate proceeding is not the appropriate forum to determine whether the utility is using incorrect amortization rates and that it is not the appropriate time to correct any errors. (TR 847, 875) It is staff's belief that it is well within the purview of this rate proceeding for the Commission to determine the appropriateness of Gulf's method of amortizing CIAC and to make any adjustments, as needed.

Accordingly, based on the evidence in the record, staff recommends that the Commission should make adjustments to correct test year amortization and AACIAC. We recommend an adjustment to AACIAC based on audit staff's calculations, which relied on the data made available to them by the utility. Staff points out that this is the best information with which to make an adjustment, as the utility did not make any attempt to enter proposed adjustments into the record. Therefore, we recommend that audit staff's adjustments be approved. Further, if the utility wants to have AACIAC corrected to a fully-supported balance, it is not precluded from coming before the Commission in its next filing to ask for such an adjustment. It is staff's opinion that we should not ignore this issue just because the utility has been using composite rates for a number of years and nothing has been done about it until this rate proceeding.

Therefore, staff recommends that the Commission should reduce AACIAC for both the water and wastewater systems in the amount of $115,371 and $98,456, respectively. Additionally, we recommend that the Commission should increase test year amortization for water by $12,967 and decrease test year amortization for wastewater by $7,329.

ISSUE 22: Is the utility's method of projecting its test year working capital accounts reasonable, and what, if any, adjustments are necessary?

RECOMMENDATION: Some components of the working capital projection were reasonable and some were not reasonable. Accordingly, staff recommends that an adjustment be made to reduce the company's working capital allowance by $106,758, to be prorated as a reduction to water of $64,178 and a reduction to wastewater of $42,580. (WEBB)

POSITION OF THE PARTIES

GULF: Gulf's method of projecting average (EXH 24, pg. 12) test year working capital accounts is reasonable, with adjustments as set forth in Gulf's positions on Issues 23 through 25.

OPC: No. Working capital should be adjusted as reflected on Ms. Dismukes schedule 17, Exhibit 19.

STAFF ANALYSIS: According to staff's audit report, Exhibit 24, Audit Exception No. 5, page 12, the MFRs did not provide the forecast methodology for working capital. Both Tallahassee and Miami staff requested the calculations supporting the utility's projections for working capital but Gulf could not provide that information. Therefore, the audit staff generated the most current 13-month average working capital for the period from August, 1995 through August, 1996. The audited amounts were then compared to the forecasted amounts in the MFRs and the utility was requested to provide reasons or support for amounts that would change from September through December, 1996. The utility was asked to provide this analysis in an attempt to bring any discrepancies closer to the forecast. One other error found during the audit of working capital was that Gulf's projection excluded/included certain accounts that should/should not have been included in the determination of working capital.

In its brief, Gulf argues that the staff audit contains a working capital computation based on an historic period rather than the approved projected test year ended 1996. Also, in its brief, Gulf contends that, other than requesting reasons for changes in working capital accounts for the period September, 1996 through December, 1996, no analysis was performed by staff as to the reasonableness of the working capital accounts. (BR 33)

Staff witness Welch testified that by auditing the period from August, 1995 through August, 1996 and then adjusting those numbers for known and measurable changes (requested from the utility) that the end result is still an audit of the projected test year ended December 31, 1996. (TR 482-483) It is staff's belief that the utility's comment that no analysis was performed by staff to determine the reasonableness of the working capital accounts is off-point. The very reason that the audit staff chose to audit the period from August, 1995 through August, 1996 was that the utility did not provide any forecast methodology, as required in the MFRs, for the working capital components. Further, as stated above, per Audit Exception No. 5, when asked, the utility could not and did not provide the support for the working capital projection. Therefore, audit staff had no choice but to utilize the most recent period at the time of the audit, which was August, 1995 through August, 1996. By the very nature of choosing this period, then requesting any changes from the utility for the period September, 1996 through December, 1996, and then comparing the results to the projected working capital accounts, staff auditors were testing the reasonableness of those projected working capital accounts.

OPC witness Dismukes recommended a negative working capital amount of $46,062. She arrived at this amount by starting with the working capital balance of $381,610 from staff's audit report. From this balance, she removed unamortized rate case expense, which she stated should be an incentive for the company to minimize rate case expense. Next, she removed unamortized debt discount and issuance expense because it is included in the company's cost of debt. She further decreased working capital for an additional amount of accrued interest related to the IDRBs. Finally, Ms. Dismukes increased working capital for accounts receivable and materials and supplies, in accordance with Gulf's response to staff's audit report. (TR 310-311)

Gulf contends that because OPC witness Dismukes used the working capital amount determined by staff in Audit Exception No. 5 as a basis for her analysis, that her working capital determination should also be rejected. (BR 33) In rebuttal, Gulf produced witness Nixon to address the issue of working capital. Primarily, Mr. Nixon's testimony responds to witness Dismukes' recommendation of a negative working capital allowance. Mr. Nixon testifies that Ms. Dismukes does not understand the concept of an allowance for working capital. He stated that an allowance is just that, "an allowance over and above the capital investment in plant

and other specifically measured rate base items". He stated that according to Ms. Dismukes' definition, current assets and current liabilities are a source of capital for rate base plant investment. Mr. Nixon stated that long-lived plant assets simply are not funded by working capital. Instead, he stated that working capital is a measurement of cash required to fund day-to-day operations. (TR 765)

Mr. Nixon first removed $43 which represents the 13-month average of interest earnings on the operating cash account. (TR 775) This adjustment corresponds to Issue 33, in which the utility and staff agree that interest income is appropriately matched with cash balances because both are removed from the rate making equations. Mr. Nixon removed $87,686 of plant construction payables from the utility's original balance in Trade Accounts Payable. (TR 775-776) Staff agrees with Mr. Nixon's explanation for this adjustment in which he stated that the plant assets related to the payables are included in rate base and earn a rate of return; therefore, such payables should be eliminated from working capital. Additionally, the source of payment for construction is long-term debt, which is accounted for in the capital structure, along with customer deposits. (TR 785-786) (EXH 40)

Mr. Nixon removed $114 of Accounts Receivable to a related party. Staff agrees with this adjustment because receivables with a related party are normally not included in working capital; regardless, the amount is very minimal. (TR 784, 786-787) Next, Mr. Nixon made an adjustment to increase materials and supplies by $13,150 for additional water chemicals needed to improve water quality. (TR 781) The balance of $78,031 in the account Miscellaneous Current and Accrued Assets was removed by Mr. Nixon because it represents interest receivable on the Industrial Development Revenue Bonds (IDRB) special deposits. This interest receivable correlates to Mr. Nixon's removal of $238,739 of Accrued Interest which represents interest payable on the IDRBs ($557 remains in the Accrued Interest account after this adjustment). Mr. Nixon contends that these adjustments to interest receivable and accrued interest follow the matching concept for accounting. (TR 776-777, 782, 786) (EXH 40)

Mr. Nixon removed the utility's original inclusion of $389,922 for Unamortized Debt Discount and Issuance Expense from the working capital calculation, as this account is being used in the capital

structure and cannot be included in both places. (TR 786) Also, this was stipulated to in Issue 23. Preliminary Survey and Investigation and Clearing Accounts in the amounts of $9,895 and $2,026, respectively, were removed, as these accounts do not relate to day-to-day operations. (TR 787) Finally, Mr. Nixon comments on the inclusion of Deferred Rate Case Expense in the working capital allowance. He states that the average amount of rate case expense ultimately approved should be substituted for the projected test year balance. The projected test year balance of Deferred Rate Case Expense is $57,561; therefore, Mr. Nixon included this amount is his calculation. (TR 783) (EXH 40)

Staff agrees with all of Mr. Nixon's adjustments and the conclusions drawn in his rebuttal testimony, with the exception of one statement. Mr. Nixon stated that the accuracy of the utility's original projections becomes irrelevant as an outcome of his analysis of the appropriate working capital allowance. (TR 780) Staff points out that the difference between the company's original $593,611 projection and Mr. Nixon's recommended $486,853 projection (which includes final deferred rate case expense) is considerable. It is staff's opinion that the difference of $106,758 is not irrelevant. We believe that this difference proves that some of the utility's working capital components included in the MFR projection were not appropriate. Therefore, we believe that some of the projections were reasonable and some were not reasonable.

Nonetheless, staff agrees with Mr. Nixon's recommendation on allowance for working capital and so we must disagree with witness Dismukes', as her analysis began with the staff audit balance of working capital. Additionally, we disagree with her removal of deferred rate case expense as an incentive for Gulf to keep rate case expense at a low level. This is an improper mechanism to lower rate case expense. Further, we believe it is consistent to match the unamortized expense with the allowed expense. Since the utility will not receive recovery of all rate case expense until the end of four years, disallowing the unamortized portion would deny recovery of the utility's investment.

Also, Ms. Dismukes does not remove accrued interest payable from her calculation, which automatically throws working capital into a negative position, even by matching such an adjustment with the removal of interest receivable. Another account which dramatically affects Ms. Dismukes' determination of working capital is Trade Accounts Payable. Again, she based her calculation on

staff's audit, which reflects a balance of $209,853 for this account. Witness Nixon testifies that this balance should be $83,203. This is a huge difference which speaks for itself in terms of the negative impact on Ms. Dismukes' working capital computation. The other accounts on which Ms. Dismukes differs in her analysis are relatively immaterial when compared to those larger differences just discussed above. As such, the differences do not warrant further discussion.

Attached to this issue is a schedule which reflects all of the components of working capital, the MFR projected balance, and witness Nixon's recommended adjustments and final working capital allowance. In accordance with the evidence in the record and with all of staff's analyses above, we recommend that an adjustment be made to reduce the company's working capital allowance by $106,758, to be prorated as a reduction to water of $64,178 and a reduction to wastewater of $42,580. Issues 23, 24, 25, and 33 relate to unamortized debt discount and issuance expense, accrued interest, interest receivable, and interest income, respectively. All of these issues tie into this issue and can be referenced for additional detail. Issue 26 is the appropriate allowance for working capital and is referenced to this issue, as well.

WORKING CAPITAL ANALYSIS - ISSUE 22

	MFR ACCOUNT BALANCES	[illegible]	STAFF'S ADJUSTED BALANCE
Cash	332,244	(43)	332,201
Accounts Rec. - Customer	305,246	0	305,246
Accounts Rec. - Other	114	(114)	0
Materials & Supplies	24,326	13,150	37,476
Unamortized Debt Dis. & Exp.	389,922	(389,922)	0
Unamortized Rate Case Expense	57,561	9,857	67,418
PS&I	(9,895)	9,895	0
Clearing Accounts	(2,026)	2,026	0
Other Deferred Debits	130,975	(1)	130,974
Prepayments	76,850	0	76,850
Miscellaneous Current Assets	78,031	(78,031)	0
Less:			
Accounts Payable - Trade	(170,889)	87,686	(83,203)
Taxes Other Than Income	(329,812)	0	(329,812)
Accrued Interest	(239,296)	238,739	(557)
Other Current Liabilities	(49,740)	0	(49,740)
Other Deferred Credits	0	0	0
TOTAL	593,611	(106,758)	486,853

Allocation of O&M Expenses Per Staff			Staff's WCA	Gulf's WCA	
Water	1,272,417 **	60.38%	293,966	358,144	(64,178)
Wastewater	834,905 **	39.62%	192,887	235,467	(42,580)
Total	2,107,322	100.00%	486,853	593,611	(106,758)

**Staff's recommended total for O&M expenses

ISSUE 23: Should unamortized debt discount and issuance expense be included in the working capital calculation? (Audit Exception 5)

RECOMMENDATION: No, this account has been included in determining the cost of debt in the cost of capital. (WEBB)

POSITION OF THE PARTIES

GULF: Unamortized debt discount and issuance expense should not be included in the working capital calculation because this amount is included elsewhere in the rate making process.

OPC: Stipulated.

STAFF ANALYSIS: In the MFRs, the utility included unamortized debt discount and issuance expense of $389,922 in the working capital calculation. (EXH 8, pg. 57) When audit staff performed their audit of the working capital forecast, they included $394,954 for this account in arriving at net working capital. Audit staff also reported that they were able to trace the accounts that comprise unamortized debt discount and issuance expense to the utility's cost of capital schedule, which means that these accounts were included in two places in the MFRs. (EXH 24, pg. 12) At the time of the Prehearing Order, all parties agreed that unamortized debt discount and expense could not be included in rate base and in cost of capital; therefore, it should be removed from working capital.

Utility witness Nixon provided extensive rebuttal testimony on the appropriate working capital allowance and his allowance does not include unamortized debt discount and expense. (EXH 40, RCN-1, pg. 1 of 3) Thus, the contention between the parties has become a question of the appropriate dollar amount that should be removed. Accordingly, because of the difference between the amount of unamortized debt discount and expense contained in the filing and the number arrived at by audit staff, this issue could not be fully stipulated at the time of the Prehearing Order.

Subsequent to the hearing, Gulf filed a letter on March 17, 1997, stipulating that this account was included in arriving at the cost of debt in the cost of capital. Therefore, Gulf argued that working capital should be reduced by $389,922, according to utility witness Nixon's working capital determination contained in Exhibit 40. (BR 35-36)

As stated above, all parties have agreed that unamortized debt discount and expense cannot be included in rate base and in cost of capital; therefore, the amount should be removed from the working capital calculation contained in the MFRs. Staff's analysis and recommendation with regard to overall working capital is covered in Issue 22. Accordingly, staff recommends that this account should not be included in working capital, and that no adjustment is necessary in this issue, as we have accounted for unamortized debt discount and expense in Issue 22.

ISSUE 24: Is an adjustment necessary to the projected balance of accrued interest for the Industrial Development Revenue Bonds (IDRBs) included in the working capital calculation? (Audit Exception 5)

RECOMMENDATION: Yes, the projected balance of accrued interest should be adjusted upward to $269,790; however, this adjusted balance should not be included in the determination of working capital. This recommendation correlates to staff's recommendation in Issue 25, which also excludes interest receivable from the working capital allowance. (WEBB)

POSITION OF THE PARTIES

GULF: The projected balance of accrued interest should be adjusted to $269,790, as set forth on page 15 of the Staff Audit Report. However, the adjusted accrued interest balance should not be included in the working capital computation.

OPC: Yes, working capital should be decreased by $30,494 to adjust the projected balance of accrued IDRB interest.

STAFF ANALYSIS: In the utility's filing, $239,296 was included as the balance in the accrued interest account. (EXH 8, pg. 57) According to page 15 of the Staff Audit Report, Exhibit 24, the utility adjusted this amount to $269,790 in response to staff's analysis of the working capital calculation. In the Prehearing Order, all parties agreed that the appropriate balance should be $269,790.

Witness Nixon testified that Gulf's interest payable is not funded by the operating cash account. Instead, cash is deposited into a special account from which the interest is paid. Mr. Nixon removed the balance of special deposits from his determination of working capital. Therefore, in keeping with the matching principle, Mr. Nixon also recommended removing the balance of accrued interest from the working capital calculation. Mr. Nixon testified that, conversely, if interest on the IDRBs was paid from the operating account then the balance of accrued interest should remain in the working capital computation. Since this is not the case with Gulf, his recommendation is that accrued interest should be removed in order to be properly matched with the elimination of the special deposits which fund the interest payments. (TR 776-777, 784, 786)

OPC witness Dismukes agreed with the utility as to the balance for accrued interest. (TR 311) However, staff notes that no analysis was made by witness Dismukes regarding the matching of the cash deposits (which fund the utility's interest payments) to the accrued interest account. OPC's brief only refers to its discussion in Issue 22, which outlines all of Ms. Dismukes' direct testimony on working capital. (BR 36-37)

Staff believes that the conclusions drawn by witness Nixon in his rebuttal testimony are valid and well supported. Our analysis and recommendation with regard to overall working capital is covered in Issue 22. Since we have recommended that interest receivable be removed from the working capital calculation (Issue 25), it follows that accrued interest should also be removed. Accordingly, staff agrees with witness Nixon that while an adjustment should be made to the balance of accrued interest, it should nonetheless be excluded from the working capital calculation in keeping with the matching principle.

ISSUE 25: Should interest receivable be included in the working capital calculation? (Audit Exception 5)

RECOMMENDATION: No, since staff's recommendation in Issue 24 eliminates accrued interest from the working capital allowance, interest receivable should not be included in order to achieve proper matching. (WEBB)

POSITION OF THE PARTIES

GULF: Interest receivable should only be included in the working capital calculation if accrued interest is included in the working capital computation.

OPC: No.

STAFF ANALYSIS: In the utility's filing, $78,031 was included as the balance of Miscellaneous Current Assets. This account represents interest receivable on special deposits related to the IDRBs.

In Issue 24, staff agrees with utility witness Nixon, and the evidence in the record supports, that accrued interest on the IDRBs should not be included in the working capital computation, so long as such an adjustment is offset with the exclusion of interest receivable. Staff agrees with witness Nixon in that such an offset achieves proper matching of assets with liabilities. Likewise, OPC agrees that interest receivable should not be included in the working capital calculation. Accordingly, staff recommends that interest receivable be excluded from the working capital allowance. Our analyses regarding total working capital components and the overall working capital allowance is covered in Issue 22.

ISSUE 26: What is the appropriate allowance for working capital?

RECOMMENDATION: Working capital in the amount of $486,853 should be approved, which was calculated using the balance sheet approach in accordance with Rule 25-30.433(2), Florida Administrative Code. The working capital allowance should be prorated $293,966 to water and $192,887 to wastewater. (WEBB)

POSITION OF THE PARTIES

GULF: The appropriate allowance for working capital is $476,195 plus the average rate case expense allowed.

OPC: Negative working capital of $315,852 should be included in rate base.

STAFF ANALYSIS: The components included in the determination of balance sheet working capital allowance have been discussed in Issues 22, 23, 24, 25, and 33. According to staff's recommendations in each of these issues, we have recommended a composite adjustment downward to the utility's projected balance of working capital in the MFRs. The utility projected $593,611 for a working capital allowance; however, based on our analyses in each of the issues mentioned above, and on the evidence in the record, we have recommended a decrease of $106,758 to the projected amount.

Therefore, staff recommends that working capital in the amount of $486,853 should be approved, which was calculated using the balance sheet approach in accordance with Rule 25-30.433(2), Florida Administrative Code. The working capital allowance should be prorated $293,966 to water and $192,887 to wastewater.

ISSUE 27: What are the appropriate rate base amounts?

RECOMMENDATION: Rate base should be established as $3,449,029 for water and $3,542,750 for wastewater. (MERCHANT)

POSITION OF THE PARTIES

GULF: The appropriate rate base amounts are $4,077,824 for water and $4,483,584 for wastewater.

OPC: The final amount of rate base is subject to the resolution of other issues.

STAFF ANALYSIS: Based on the staff's recommended adjustments and the use of a thirteen-month average, rate base is $3,449,029 for water and $3,542,750 for wastewater. The rate base schedules for water and wastewater are attached as Schedules Nos. 1-A and 1-B. The schedule of adjustments to rate base is attached as Schedule No. 1-C.

COST OF CAPITAL

ISSUE 28: What is the amount of credit accumulated deferred income taxes that should be included in the capital structure?

RECOMMENDATION: The appropriate amount is $1,517,923. (MERCHANT)

POSITION OF THE PARTIES

GULF: The accumulated deferred income taxes are $1,517,923 as shown on Schedule D-2, page 120 of the MFRs.

OPC: No position.

STAFF ANALYSIS: In its MFRs, the utility reported that credit accumulated deferred income taxes included in the capital structure were $1,517,923. This was reflected on Schedule D-2, page 120, of the MFRs. (EXH 8) This amount was prorated, along with the other sources of capital, to equal the utility's requested rate base. There was no testimony or cross examination on this issue. Staff has recommended adjustments to rate base as well as the dollar amount of equity included in the capital structure, as discussed in previous issues. Based on the above, staff recommends that no adjustments to credit accumulated deferred income taxes is necessary and the utility's projected balance should be approved.

ISSUE 29: What is the appropriate weighted average cost of capital including the proper components, amounts, and cost rates associated with the capital structure for the 1996 projected test year?

RECOMMENDATION: The appropriate overall cost of capital is 9.21%, with a range of 9.13% to 9.29%. Using the utility's adjusted equity ratio, the cost of equity should be 11.88%, with a range of 10.88% to 12.88%. (MERCHANT)

POSITION OF THE PARTIES

GULF: The appropriate overall cost of capital is 9.25%.

OPC: The appropriate overall cost of capital is 9.22%. The proper components, amounts, and cost rates associated with the capital structure can be found in Schedule 2 Exhibit 19.

STAFF ANALYSIS: The recommended overall cost of capital is based on the utility's projected 13-month average capital structure, as adjusted by staff's recommended adjustment to equity associated with lines contributed from the Caloosa Group (Issue 17). As outlined in Issue A, the parties have stipulated and staff agrees that the cost of common equity should be based on the leverage formula in effect at the time the commission make its decision in this case. Using the utility's adjusted equity ratio, the cost of equity should be 11.88%, with a range of 10.88% to 12.88%. The resulting overall cost of capital should be established as 9.21%. The range on the overall cost of capital should be established as 9.13% to 9.29%.

ISSUE 30: What are the appropriate water and wastewater gallonage projections for FGCU for the 1996 projected test year, and what adjustments, if any, are necessary to projected revenues?

RECOMMENDATION: The appropriate water and wastewater gallonage projections for FGCU for the 1996 projected test year are 15 million gallons and 10.6 million gallons, respectively. No adjustments to projected revenues are necessary. (GALLOWAY)

POSITION OF PARTIES

GULF: The MFRs already include all the necessary adjustments.

OPC: No Position.

STAFF ANALYSIS: Consistent with Staff's recommendation in Issue No. 6, Staff believes that costs, expenses and revenues associated with FGCU should be included in this rate proceeding. Therefore, the appropriate water and wastewater gallons for FGCU must be determined.

Consumption projections for the university were included in the utility's MFRs. (EXH 8) These projections are also contracted in the special service availability agreement which is discussed in Issue 63. The consumption projections were calculated based on number of students, faculty, and staff. Further, the calculations considered the university system scheduling. For example, during the spring and fall months, when enrollment is usually at a maximum, the actual consumption is projected to be more than the summer months when enrollment is not at a maximum. (EXH. 4)

On the other hand, according to staff's recommendations in Issues 12 and 15 , the adjusted gpd are calculated to be 206 gpd per ERC and 158 gpd per ERC for the water and wastewater system, respectively. (TR 176-177) Applying these amounts to the associated number of ERCs for the university results in lower projected gallons. Consequently, lowering the projected gallons would result in a higher gallonage charge. Further, resulting from the lower projected gallons is a lower revenue requirement which ultimately could put the utility in an overearnings posture.

Therefore, Staff believes that the appropriate water and wastewater gallonage projections for the 1996 projected test year are as follows:

	WATER	WASTEWATER
FGCU -	15 million gallons	10.6 million gallons

Further, Staff believes that until actual flows can be documented through meter readings, the above projections are acceptable. Staff is recommending no change to the projections made by the utility. Staff recommends that the projected water and wastewater gallons related to FGCU, found in the company's MFRs are appropriate. Therefore, no adjustment to projected revenues is necessary.

ISSUE 31: What adjustments, if any, are necessary to the 1996 projected test year revenues to reflect the appropriate miscellaneous service revenues?

RECOMMENDATION: No adjustments to the 1996 projected test year revenues are necessary to reflect the appropriate miscellaneous service revenues. (GALLOWAY)

POSITION OF PARTIES

GULF: No adjustments are necessary to the 1996 projected test year revenues regarding miscellaneous service revenues.

OPC: No Position.

STAFF ANALYSIS: A utility may record total miscellaneous revenues either as water miscellaneous revenues or as wastewater miscellaneous revenues. For this docket, miscellaneous revenues were included in total by the utility as water miscellaneous revenues. Commission practice has been to allow a utility to record miscellaneous revenues in this way when both water and wastewater miscellaneous charges exist. (EXH 8)

Staff agrees with the way that the miscellaneous revenues were recorded and agrees with the amount of miscellaneous revenues reported in the utility's MFRs. OPC does not take a position on this issue in their brief. The utility's position is stated above.

Staff is recommending no adjustment to the miscellaneous revenue account.

ISSUE 32: If a reuse rate is approved, and the rate is greater than $0, should test year revenue be adjusted?

RECOMMENDATION: No. Based upon Staff's recommendation in Issue No. 55 that a zero reuse rate be approved for all reuse customers, no adjustment is necessary to test year revenues. However, should the commission approve a rate greater than zero, it would be appropriate to adjust test year revenue by the level of revenue generated by that rate. (VON FOSSEN)

POSITION OF THE PARTIES

GULF: Reuse is part of the utility's effluent disposal and treatment process, and as such, golf courses are not customers, and no rate is appropriate.

OPC: Yes. The Commission should increase test year revenue by $87,668 to reflect the sale of reclaimed water at $.25 per 1000 gallons during the dry season and to reflect a credit of $.05 during the wet weather season.

STAFF ANALYSIS: This is a fall out issue dependent upon Commission action on Issue No. 55 which addresses whether a reuse rate should be approved and if so, the level of the rate. If the Commission approves staff's recommendation that a zero rate be approved for reuse, then no adjustment to test year revenue is necessary. However, should the commission approve a rate greater than zero, it would be appropriate to adjust test year revenue by the level of revenue generated by that rate in the test year.

ISSUE 33: Should any adjustments be made to include in test year income, interest income recorded below the line?

RECOMMENDATION: No, staff recommends that no adjustment should be made to move interest income above the line, since staff's recommendation in Issue 22 eliminates the associated cash balances from the working capital allowance. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments to test year income should be made to include interest income recorded below the line. The projected cash balance for the operating account (test year ended 12/31/96) included interest earnings of $559 ($43 on 13 mo. average basis). This amount was removed from the working capital computation.

OPC: Yes. Test year income should be increased by $4,000 to reflect interest income earned on cash included in the Company's working capital allowance.

STAFF ANALYSIS: This is an issue raised by OPC witness Dismukes whereby she contends that the utility has booked interest income below the line related to cash included in the working capital allowance. Ms. Dismukes arrived at this adjustment after reviewing the utility's response to an OPC interrogatory, which confirmed that the operating account included in the working capital calculation earns interest. (TR 305-306) Utility witness Nixon testifies that Gulf's operating account earns a modest amount of interest which he has removed in arriving at net working capital. In fact, Mr. Nixon's working capital calculation removes from cash all interest bearing money market accounts and the 13-month average of the interest earnings from the operating account. (TR 775, 784)

Mr. Nixon's testimony on working capital provides a revised number from that contained in the utility's filing. The filing had included the 13-month average of the interest earnings on the operating account. OPC contends that, in witness Andrews' rebuttal, the utility agreed with Ms. Dismukes' adjustment. (BR 39) Ms. Andrews does agree with OPC's adjustment. (TR 844) However, staff believes that this was just an error on the utility's part. After all, the utility did have Mr. Nixon provide rebuttal testimony on each component of the utility's requested working capital allowance. Based on this, staff supports the recommendation of witness Nixon to remove the interest from the

operating account in arriving at working capital (Issue 22), which negates the need for adjusting interest income above the line. Accordingly, staff recommends that no adjustment should be made to move interest income above the line, as this would result in improper matching.

ISSUE 34: Are any adjustments necessary to the projected test year salaries, benefits, and payroll taxes for employees that provide services to both Gulf and the Caloosa Group (Audit Disclosure 3)?

RECOMMENDATION: Yes, an adjustment is necessary to reduce Gulf's requested salaries expense by $5,905 for water and $3,042 for wastewater in order to properly allocate Caloosa-related payroll costs back to Caloosa. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to the projected test year salaries, benefits and payroll taxes for employees that prorate services to both Gulf and the Caloosa Group. Studies show that the amounts stated are reasonable.

OPC: Yes. Gulf's salaries should be reduced by $8,947 to reflect the higher salary paid to employees when they work for the utility instead of its affiliate Caloosa. Appropriate adjustments should likewise be made to employee benefits and payroll taxes.

STAFF ANALYSIS: Utility witness Cardey testified that the Caloosa Group is a land development company and an affiliate to the utility with the same owners as Gulf, and the same proportionate interests. Namely, 80% is owned by Russell B. Newton, Jr. and 20% is owned by James W. Moore. According to Mr. Cardey, some of Gulf's employees provide general supervision and accounting services to Caloosa. Those employees participate in selling lots and in the homeowners' association of Caloosa Trace, plus administration of the Caloosa-owned office building. (TR 146) The five employees which provide services to both Gulf and Caloosa are: the President (Mr. Moore), the Chief Financial Officer (Ms. Andrews), the Assistant to the CFO (Ms. Babcock), the Administrative Manager (Ms. Rivers), and the Administrative Assistant (Ms. Gravel). (TR 296) According to staff's audit report, each of these employees are paid directly from Caloosa for the services they provide. (EXH 24, pg. 23)

Mr. Cardey testified that in analyzing the payroll of Caloosa he first made a determination of the services Gulf provided to Caloosa, then reviewed the time required by each person who performed the service. He stated that two people maintain the books and perform record keeping at an estimated 9 hours per month. One person handles the selling of lots and does administrative work for the homeowners' association, at an estimated 16 hours per

month. Additionally, Mr. Moore and his secretary spend an estimated 5% of their time each on administrative duties related to Caloosa. Mr. Cardey stated that he used current payroll costs for each employee and added payroll taxes and health insurance cost to come up with an estimate of what Caloosa should have paid in salaries. His calculation is approximate to the $12,142 paid to Gulf's employees by Caloosa. Since the five employees are paid directly by Caloosa, Mr. Cardey determined that no salary expense allocation to Caloosa was needed, as his estimate is approximate to what was actually paid. (TR 147-148)

OPC witness Dismukes recommended an adjustment to the salaries of Gulf's employees that provide services to both the utility and to Caloosa. She demonstrated in her Exhibit 19, Schedule 6, that the hourly rate for those employees that perform services for Gulf is considerably higher than the hourly rate for services performed on behalf of Caloosa. Ms. Dismukes testified that the hourly rates charged should be the same for both Gulf and Caloosa. In order to achieve this, Ms. Dismukes reallocated the salaries charged to Caloosa based upon the combined hourly rate of Caloosa and Gulf. Ms. Dismukes utilized the information contained in Exhibit 32, which includes the Earnings and Deductions reports for Caloosa from September, 1995 to August, 1996. These reports detail the earnings for each of the five employees for the period, including a column for the hours worked during the period. (TR 299-300)

To ensure that both the utility and its affiliate Caloosa are paying the same amount per hour for the services of Gulf's employees, Ms. Dismukes reallocated total Gulf plus Caloosa salary for each of the employees based upon the total number of hours worked for each entity during a year. Ms. Dismukes' analysis assumed that Mr. Moore is the only one of the five employees who provides services to Caloosa above the standard 2,080 hours per year that he works for Gulf. Additionally, Ms. Dismukes' analysis assumed that the remaining of the shared employees work for Caloosa within the parameter of a 40-hour work week. By taking each employee and combining the salaries expense for Gulf and Caloosa and then dividing by the respective hours worked by each employee for both entities, Ms. Dismukes arrived at one combined hourly rate which she stated is appropriate to use in determining the salary for each entity. She used this new combined hourly rate and multiplied it by the number of hours taken for each employee from the Earnings and Deductions reports to determine the salary that should have been paid by Caloosa. Based on this difference, she

then reallocated some of Gulf's salaries expense to Caloosa. The result of this calculation for each of the five employees is an adjustment to reduce Gulf's requested salaries expense by $8,947. (TR 300, EXH 19)

Staff witness Welch testified that the percentage of Caloosa payroll to total Caloosa and Gulf payroll during the last audit was 12.67%, while the most recent payroll register reflected Caloosa payroll at 2.13% of total payroll. According to staff's audit report, Audit Disclosure No. 3, in analyzing the differences, the audit staff reviewed the Caloosa Earnings and Deductions reports and the pay shown to arrive at an hourly rate. The conclusion drawn in the audit report is that the hourly rates used for Caloosa and Gulf appear to be very different. (EXH 24, pg. 23, TR 451)

In rebuttal, utility witness Cardey states that he is the only witness who reviewed the services that Gulf's employees provide to Caloosa. The result of his direct analysis was that the present salaries paid to Gulf employees by Caloosa are reasonable. Mr. Cardey states that neither staff nor OPC made a study of the work performed or the time spent by the personnel involved. (TR 649-650) Gulf cites Sunshine Utilities v. Public Service Commission, 624 So. 2d 306, 312 (Fla. 1st DCA 1993), in which the Court found that in a rate case, "the best way to allocate employee expenses was actual time." Gulf alleges that witness Cardey allocated employees' time for both Gulf and Caloosa based on actual time expended in work for each entity. (BR 44)

Audit Disclosure 3, page 23, of the staff audit report reflects differences found in the hourly rates between Gulf and Caloosa employees. Staff's calculation for Caloosa's hourly rates was taken directly from Caloosa Earnings and Deductions reports provided to the auditors by the utility. Exhibit 32, the Earnings and Deductions reports, provides the basis for recommended adjustments in this Issue and in Issue 39. Referring again to witness Dismukes' Exhibit 19, Schedule 6, this represents her analysis of making an adjustment to allocate more salaries expense to Caloosa. Ms. Dismukes, like the audit staff, utilized the information contained in the Caloosa Earnings and Deductions reports to analyze the difference in pay rates between Gulf and Caloosa employees. Accordingly, this data is what Ms. Dismukes' recommended adjustment is based upon.

However, it is not clear what period Mr. Cardey used to analyze payroll costs or how he actually came up with percentages for time worked, other than subjectively arriving at a percentage just by talking to the employees. Witness Cardey's percentages found in Exhibit 8, KRC-3, range from 2% to 10%. The one person Mr. Cardey reflects as spending 10% of their time on Caloosa-related business is the administrative person that spends 16 hours per month, as mentioned above. This percentage does correlate to the calculated percentage from the Earnings and Deductions report for this same employee; however, Mr. Cardey's determination of 5% for Mr. Moore does not correlate. The report for Mr. Moore reflects that he spends approximately 12.5% of his time on Caloosa-related business. Similar analyses can be done for all of the related employees and percentage differences can be found, but Mr. Moore's is the greatest difference. It is staff's opinion that the percentages arrived at by witness Cardey are too subjective and should not be used as a benchmark for the appropriateness of salaries paid by Caloosa. Instead, it is staff's belief that the most reliable information on which to base analyses is the Caloosa Earnings and Deductions reports, which should be a reflection of actual time.

During cross examination, witness Cardey argued that the Earnings and Deductions reports do not represent the hours that employees work for Caloosa. He states that the salaries were set in 1988 and that hours are put into a computer program for payroll to come out to some number. Further, Mr. Cardey states that if we want to come up with 1996, we have to sit down with Mr. Moore and go over his functions related to Caloosa. He also states, "you've got to remember the calculation behind this is to fit the computer program more than anything else." (TR 679-681) In staff's opinion, Mr. Cardey's explanations and analysis regarding this issue are insufficient. We believe that it is irrelevant that the salaries were set in 1988; if logic dictates that salaries should be increased each year for Gulf, so should the salaries for Caloosa. Thus, it is staff's opinion that the utility has not satisfied its responsibility of burden of proof.

Staff believes that witness Cardey has not provided a solid basis on which the Commission can determine the reasonableness of the Caloosa salaries. He states that neither staff nor OPC did any analysis in arriving at their recommended adjustments. Contrary to his statement, both staff and OPC utilized documents provided by the utility as a basis for their respective analyses. Both staff

and OPC attempted to arrive at a fair hourly rate by utilizing the best information available, that being the Earnings and Deductions reports for the Caloosa Group for the most recent period of September, 1995 to August, 1996.

It is logical that in order to determine the appropriate percentage of time that each employee spends on Caloosa-related business, one would reference a record such as the Earnings and Deductions reports. By dividing the salary for the period by the total number of hours worked, this reflects an hourly rate. Taking the total number of hours worked and dividing them by 52 weeks in a year, this will reflect an approximate number of hours worked per week. Further, by dividing these hours per week by a 40-hour work week, this reflects the percentage of time worked, on average, for Caloosa. Accordingly, staff recommends that, based on the record and all above analyses, salaries expense should be reduced by $5,905 for water and $3,042 for wastewater in order to properly allocate Caloosa-related payroll back to Caloosa. The adjustment to benefits associated with Caloosa payroll is covered in Issue 39. Also, the payroll taxes are a fall-out to all recommended salary adjustments, and will be allocated in accordance with stipulation nine.

ISSUE 35: Are any adjustments necessary to the vice president's salary and benefits (Audit Disclosure 13)?

RECOMMENDATION: Staff recommends that the Commission approve an adjustment to reduce Mr. Mann's salary to $25,400 per year, on a part-time basis. This adjustment results in a $22,954 reduction to test year expenses. Accordingly, staff recommends that the Commission reduce test year expenses by this amount and prorate the reduction $15,150 to water and $7,804 to wastewater. Additionally, on a going-forward basis, staff recommends that the utility be ordered to maintain records of Mr. Mann's daily, utility-related activities. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to the vice president's salary and benefits.

OPC: Yes. The vice president's salary should be reduced by $30,234. Appropriate adjustments should likewise be made to employee benefits and payroll taxes.

STAFF ANALYSIS: The utility projected $49,608 in salary expense for Mr. Randall Mann, the Vice-President of Gulf. (TR 117, 456) Mr. Mann does not physically work at the utility's location in Estero, Florida, instead he conducts his duties from Jacksonville, Florida, where he also works for another company and lives full-time. During cross examination, Mr. Moore stated that Mr. Mann has worked for Gulf for approximately 10 years. However, when asked if Mr. Mann worked full or part-time for this company in Jacksonville, Mr. Moore did not know, nor was Mr. Moore certain of Mr. Mann's position. (TR 114-116) Further, Mr. Moore testified that he does not know how Mr. Mann spends his days, but that Mr. Mann is available to the utility when he is needed. (TR 119)

Staff's Audit Disclosure No. 13 states that Mr. Mann was asked to provide a letter which would confirm how much time he spends on utility business. The staff auditors received a list of Mr. Mann's responsibilities with a statement from the utility which reads, "The amount of time spent per week on these various duties varies considerably depending on the needs of the company." (EXH 24, pgs. 36-39)

In its brief, the utility cites Metropolitan Dade Co. W&S Bd. v. Community U. Corp., 200 So. 2d 831, 832-833 (Fla. 3rd DCA 1967), whereby the Court held that a regulatory commission in ruling upon the reasonableness of an executive salary allowance must base its ruling on evidence establishing individual duties and activities and the complexity of those duties. In support of this argument, the utility also cited the following three cases: Southwestern Bell Telephone Co. v. Public Service Commission of Missouri, 262 U.S. 276 (1923); Sunshine Utilities of Central Florida, Inc. v. Florida Public Service Commission, 624 So. 2d 306 (Fla. 1st DCA 1993); and Florida Bridge Co. v. Bevis, 363 So. 2d 799 (Fla. 1978). (BR 46) Staff agrees with the evidentiary requirements set forth in the foregoing cases. However, we note that Gulf has the burden of establishing the individual duties, activities, and the complexity of Mr. Mann's duties. See Florida Power Corporation v. Cresse, 413 So. 2d 1187 (Fla. 1982). In the present case, staff believes that Gulf did not fully meet its burden of proof, as set forth below.

On cross examination, Mr. Moore was asked to read the utility's response to OPC's Interrogatory No. 41 (EXH 6), which, in part, was a request for Gulf to provide an estimate of the time Mr. Mann devotes to utility-related business. Mr. Moore read the response as follows: "Mr. Mann does not submit time records and is paid on a salary basis." (The remainder of the response was the same as that which was provided to staff's auditors, outlined above.) When asked why the utility was not able to obtain an hourly estimate, Mr. Moore responded that Mr. Mann was unavailable. OPC's contention, in its brief, is that if Mr. Mann is available to the utility when needed, as testified by Mr. Moore, then why could Gulf not obtain an estimate within the 30-day response period for discovery or at least by the time of hearing, which was apparently 117 days from the date the interrogatory was propounded. (TR 117-119, BR 42)

Utility witness Moore stated on cross examination that Mr. Mann is compensated based upon the value of his services. (TR 120) Mr. Mann holds a Master's Degree in Business Administration, is a Certified Public Accountant, and a Chartered Financial Analyst. (TR 563) According to the list of duties provided to both OPC and staff, Mr. Mann is responsible for various management-level accounting, financial, and tax matters. The list of duties is detailed and can be found in the Audit Report, Exhibit 24, pgs. 37-38. Gulf contends, in its brief, that Mr. Mann participates in all utility borrowings and related financing negotiations. Further,

that Mr. Mann testified in Docket No. 94-00418, Southwest Florida Capital Corporation vs. Gulf Utility, which involved issues related to CIAC. (TR 563-564, BR 45-46)

OPC witness Dismukes testified that she does not believe that Gulf has proven the reasonableness of the salary paid to Mr. Mann. Based upon her review of Mr. Mann's duties, she estimates that Mr. Mann should spend approximately 10 hours per week, or 520 hours per year on utility-related matters. Ms. Dismukes took the mid point between Mr. Moore's and Ms. Andrews' salary, which is roughly $35.00 per hour, and recommends that this be Mr. Mann's hourly rate. Thus, she recommends a salary of $18,200 per year, with a reduction to test year expenses of $30,234. (TR 302)

Although staff does not believe that the utility has fully met its burden of proof as to the reasonableness of Mr. Mann's salary, we recognize that Ms. Dismukes' recommendation is not entirely reasonable. To illustrate, one could consider Ms. Dismukes' estimate of 10 hours per week spent by Mr. Mann on utility business. However, instead of the hourly rate that she recommends, consider what it would cost to hire a certified professional who is paid by the hour to perform services similar to what Mr. Mann currently provides. Witness Nixon, for example, is a partner in his firm and commands a rate of $140 per hour. Considering the credentials of Mr. Mann, as outlined above, it would surprise staff if Mr. Mann did not command an hourly rate commensurate to that of witness Nixon's, assuming a similar contractual relationship. Based on this example, at 520 hours per year, Mr. Mann would realize $72,800 for his services, if he were a contractual employee. Using this figure as a benchmark, it becomes clear that on an annual basis Mr. Mann's compensation is reasonable.

Even though an estimate of hours has not been provided by the utility, logic dictates that whether Mr. Mann spends 8, 10, 12, or some other estimated number of hours per week on utility business, the time spent averages out over the year. Staff does believe, however, that some record/journal of utility-related activities should be maintained by Mr. Mann. Records of daily activities, not necessarily by hour, are common for vice presidents of the Class A utilities with which staff is familiar. Furthermore, it is logical that if a utility is requesting recovery of this magnitude of expense, it should certainly be able to provide all reasonable means of validating its position so as to avoid any questions of impropriety. It is staff's belief that Gulf has not provided all

reasonable means of validating its position. There was definitely enough time up through the conclusion of the hearings to provide an estimate for the parties to analyze; further, if the utility had done so, this matter may not have been disputed. Nonetheless, Gulf has not clarified whether Mr. Mann works 40 hours per week or less than 40 hours per week for the utility.

Therefore, staff believes that the record supports an adjustment to Mr. Mann's salary, based on the fact that the utility could not adequately support the requested amount and failed to fully respond to both staff's and OPC's requests for time estimates for Mr. Mann, as outlined above. Also, the evidence in the record suggests that Mr. Mann is not a full-time employee of Gulf, since he also works for a company in Jacksonville, where he lives. (TR 114-116) This is contrary to other Class A utilities with which staff is familiar, wherein vice presidents are full-time, even if they work at a parent company's headquarters in another state. As such, it is staff's opinion that Mr. Mann's responsibilities as vice president are more similar to the responsibilities of a contractual services person than to those of a regular employee. Staff does point out, however, that given the value of his services (which is based on his expertise and qualifications), we believe that Mr. Mann should undoubtedly be sufficiently compensated. The issue that staff is concerned with is how to measure Mr. Mann's time spent on utility-related business, as the utility has failed to provide this support.

Since the only support in the record on which to make an adjustment is the testimony of Ms. Dismukes, staff must rely on her analysis to the extent of her estimate of hours worked per week. We believe that Ms. Dismukes' estimate of 10 hours per week, or 520 hours per year, is fair based on the fact that Mr. Mann does have another job in Jacksonville. Staff does not agree with the hourly rate that Ms. Dismukes has used because we believe that a vice president with the responsibilities, expertise, and qualifications of Mr. Mann should be compensated at an hourly rate similar to the president of the utility. It is staff's opinion that there is not much of a difference between the level of responsibilities of the president and vice president of Gulf; although, it is certain that each one has their own responsibilities.

Thus, staff is recommending that in order to make an adjustment to Mr. Mann's salary, we should use an hourly rate of $49. This is approximately the hourly rate of Mr. Moore, after

staff's recommended salary adjustments in Issue 36. An estimated 520 hours per year at $49 per hour yields an annual salary of $25,480, on a part-time basis. Thus, staff recommends that the Commission approve an adjustment to reduce Mr. Mann's salary to $25,480, after considering staff's salary adjustments for pay increases in Issue 36. Staff's recommendation in Issue 36 is for a 5% increase for test year salaries, so this would have made Mr. Mann's test year salary $48,434. The difference between Mr. Mann's adjusted test year salary and staff's recommendation in this issue is a $22,954 reduction to test year expenses. Accordingly, staff recommends that the Commission reduce test year expenses by this amount and prorate the reduction $15,150 to water and $7,804 to wastewater. Additionally, on a going-forward basis, staff recommends that the utility be ordered to maintain records of Mr. Mann's daily, utility-related activities.

ISSUE 36: Should any adjustments be made to salary expense for excessive pay increases?

RECOMMENDATION: Yes, salaries expense should be reduced by $7,416, prorated $4,895 to water and $2,521 to wastewater. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments should be made to salary expense. Salary increases were reasonable.

OPC: Yes. Salaries should be reduced by $7,416 to remove excessive pay increases from the test year.

STAFF ANALYSIS: This is an issue brought forth by OPC witness Dismukes. Her recommended adjustment relates specifically to the 1996 pay increases for Gulf's management employees. According to Ms. Dismukes, the projected pay increases range from 6.5% to 9.6% for Gulf's officers and managers. Ms. Dismukes states that, according to the utility's response to OPC's Interrogatory No. 11, salary increases were 5% in 1992, 4% in 1993, 5% in 1994, and 4% in 1995. Witness Dismukes further states that the overall budgeted increase was 6.5%; however, the increases can vary by employee. Ms. Dismukes' Exhibit 19, Schedule 7 shows the percentage increases for the employees at issue. In this schedule, she shows that some individuals actually exceed the 6.5% overall increase. Based on the trend of salary increases in the past, Ms. Dismukes recommends reducing salaries expense for a 5% increase which results in a reduction to test year expenses of $7,416. (TR 301)

In rebuttal, utility witness Moore states that Gulf's salaries expense compares favorably to nine other utilities that operate in Lee County. He references an annual salary survey conducted by Pine Island Water Company, wherein he states that Gulf's 1995 wages were about 12% lower than the average for the other utilities. Mr. Moore further states that Gulf is attempting to narrow the gap between Gulf's salaries and those of the nine other utilities. Mr. Moore believes that the issue should be whether Gulf has excessive payroll costs and whether the utility is operating efficiently, not what salary levels are or what the increases might be. (TR 561-562)

During cross examination, Mr. Moore admits that his salary, the salary of Mr. Mann (Vice President), and the salary of Mr.

Messner (Operations Manager) were not included in the salary survey which he discusses in his rebuttal testimony. The apparent reason for not including the above salaries is that there were not comparable positions in the survey. (TR 603-604) Mr. Moore agrees that with two exceptions, Gulf's employees have fewer years of service than the average of the other companies. He also agrees that in many instances Gulf's employees have less than one-half the years of service of the other companies' average. Mr. Moore admits that one of Gulf's maintenance mechanics was categorized as a maintenance supervisor which, if categorized appropriately, would have shown that this person's salary was 42% higher than the average. (TR 608-609, EXH 33)

In its brief, the utility argues that the evidence in the record establishes the reasonableness of Gulf's salary increases and that no abuse of discretion in company management has been shown to exist. In support of this argument, the utility cited the following four cases: Metropolitan Dade Co. W&S Bd. v. Community U. Corp., 200 So. 2d 831, 832-833 (Fla. 3rd DCA 1967); Southwestern Bell Telephone Co. v. Public Service Commission of Missouri, 262 U.S. 276 (1923); Sunshine Utilities of Central Florida, Inc. v. Florida Public Service Commission, 624 So. 2d 306 (Fla. 1st DCA 1993); and Florida Bridge Co. v. Bevis, 363 So. 2d 799 (Fla. 1978). (BR 47)

Staff notes that, specifically, in the Sunshine and the Metropolitan Dade cases, the Court stated: "If any comparisons with the salaries paid by other utility companies are to be made, the comparisons must at least be based on showing of similar duties, activities, and responsibilities in the person receiving the other salary." (Sunshine, 624 So. 2d 306 at 311 and Metropolitan Dade, 200 So. 2d 831 at 833) Based on the record, staff does not believe that the salary survey supports the evidentiary requirements set forth in the foregoing cases.

Staff does not believe that the salary survey can be used as a valid comparison to Gulf's salaries based on the fact that Gulf's positions are not all comparable and that there was at least one position inappropriately categorized. Further, the years of service of Gulf's employees vary greatly from the average in the survey. We believe that, based on the record, the most appropriate gauge of reasonable and prudent salary increases is to look at past salary increases. Staff agrees with the analysis of OPC witness Dismukes and believes that it is appropriate to reduce salaries

expense for a 5% increase in the test year. Accordingly, we recommend that salaries expense be reduced by $7,416, prorated $4,895 to water and $2,521 to wastewater.

ISSUE 37: Is the annual lease amount charged to Gulf by Caloosa Group (Caloosa) reasonable and if not, what adjustments are necessary (Audit Disclosure 4)?

RECOMMENDATION: Yes, the lease is reasonable and staff recommends that no adjustment be made to the annual lease amount charged to Gulf by Caloosa. (WEBB)

POSITION OF THE PARTIES

GULF: The annual lease amount charged to Gulf by Caloosa Group is reasonable. This amount is justified based on an independent appraisal and the rental fee for the remainder of the space in the same building.

OPC: No. Test year expenses should be reduced by $26,182 for the lease of office space from Caloosa by Gulf.

STAFF ANALYSIS: Utility witness Moore testified that in approximately November, 1995, Gulf moved its administrative offices into a 3,931 square foot space within a new building owned by its affiliate, Caloosa. This space represents approximately one-third of the entire space in the building. The Lee Memorial Health System (the hospital), an independent third party, has a lease with Caloosa for the remainder of the office space. (TR 551, TR 596-597) Staff's Audit Disclosure No. 4 addresses Gulf's lease with Caloosa. Gulf's annual lease amount is $47,172, which is 3,931 square feet at $12 per square foot. Sales tax on the lease is $2,830 per year and common maintenance expenses are estimated at $9,828 per year. (EXH 24, pg. 25)

Staff's audit report states that if no proven outside market exists for affiliate rental property, a cost basis is used to determine the appropriate lease amount. To illustrate, the audit staff calculated what the lease amount would be at cost and compared that to the current amount. The calculation takes the building plus the land and multiplies this total by the allowed rate of return. Depreciation expense, assuming the standard 40-year life, is subtracted from the utility's return on investment in the building and land. This number is then multiplied by the percentage of space that the utility occupies in the new building, and this produces the rent using a cost basis. When compared to the current market value lease amount, the cost basis is approximately $20,762 lower. (EXH 24, pg. 25)

The audit report further states that Caloosa's lease with the hospital is a five year lease for 6,460 square feet at $12 per square foot. The lessee is also required to pay a proportionate share of operating expenses and is given a $15 per square foot improvement allowance. The utility provided the auditors with a report from a real estate broker which concludes that the appropriate market rental rate for smaller tenants would be $15 per square foot, inclusive of taxes and common maintenance expenses. The audit report states that Caloosa is currently charging $14.50; however, an analysis of other similar office space shows gross rent after adjustments ranging from $11.76 to $15.47 per square foot. (EXH 24, pg. 25-26)

In rebuttal, Mr. Moore testified that the utility opposes an adjustment to the lease amount. He testified that the utility moved its administrative operations because Gulf had outgrown the old space and because there was a need to provide a more easily accessible location for customers. Mr. Moore stated that Gulf was unable to finance a new office because of the utility's other capital demands related to plant expansion. He also stated that an independent appraiser substantiated the rental charge as being the market rate. Finally, he testified that there was no suitable office space available in the area to lease from a third party. (TR 547)

Mr. Moore testified that it was management's judgement that the new office space with the lease was the most economical method of serving Gulf's customers. He pointed out that most of the remaining two-thirds of the building was rented at a charge comparable to that being paid by Gulf, which justifies the reasonableness of the rental charge. He further pointed out that the report prepared by the real estate appraiser was done independently for the bank which ultimately financed the building. Mr. Moore quoted the conclusion of the report as follows: "After considering comparable rentals, it is our opinion the market rent for the subject property is between $10.00 and $12.00 per square foot on a triple net basis." (TR 546-551)

OPC witness Dismukes proposed an adjustment for the difference between the lease currently charged to Gulf and the present value of a levelized lease payment, based upon a 40-year life and a discount rate of 9.22%. Ms. Dismukes testified that the lease is not an arm's-length transaction. Therefore, she tested the reasonableness of this lease payment by comparing it to what the

lease payment would be over the life of the building using a cost of capital of 9.22%. (TR 298) The 9.22% is reasonably close to the utility's requested cost of capital of 9.25% contained on page 118 of the MFRs. (EXH 8)

Ms. Dismukes' Exhibit 19, Schedule 5, page 2 shows that the levelized lease payment over the life of the building would be $64,826 (this is based on the original cost of the building to Caloosa). As Gulf occupies 33.71% of the building, Ms. Dismukes multiplied the $64,826 times 33.71% to arrive at the lease payment that would apply to Gulf. The levelized lease payment would be $21,853, compared to the amount currently being charged of $47,152. Taking into consideration the allocation of rental expense back to Caloosa, Ms. Dismukes recommended that test year expenses be reduced by $26,182. (TR 298-299, EXH 19, pgs. 1-2)

It is the utility's position in its brief, pages 48-49, that to make an adjustment to the lease amount paid by Gulf would be contrary to the Supreme Court's decision in <u>GTE Florida Incorporated v. Deason</u>, 642 So. 2d 545 (Fla. 1994). In that ruling, the Court stated:

> We do find, however, that the PSC abused its discretion in its decision to reduce in whole or in part certain costs arising from transactions between GTE and its affiliates, GTE Data Services and GTE Supply. The evidence indicates that GTE's costs were no greater than they would have been had GTE purchased service and supplies elsewhere. The mere fact that a utility is doing business with an affiliate does not mean that unfair or excess profits are being generated, without more [citation omitted]. We believe the standard must be whether the transactions exceed the going market rate or are otherwise inherently unfair. If the answer is "no," then the PSC may not reject the utility's position. The PSC obviously applied a different standard, and we thus must reverse the PSC's determination of this question. (Id. at 547-548) [Citations omitted]

Staff points out that witness Welch did not render an opinion on Audit Disclosure No. 4. She only included information within that disclosure that would be helpful in analyzing the reasonableness of the lease paid by Gulf. During cross examination, she stated that there are different ways to look at

the reasonableness of the lease. She stated that when an affiliate transaction is involved, the policy has normally been to use the lower of cost or market. She further testified that if an outside market exists, the market value is allowed; however, that does not necessarily mean that management made a prudent decision in this case. Ms. Welch stated that the Commission should consider whether the utility could have found another building, or whether the utility could have built the building. (TR 463-467)

It is staff's belief that the report prepared by the independent appraiser, working for the lending bank, is a solid basis upon which to test the reasonableness of Gulf's lease with Caloosa. As stated above, both Gulf and the hospital pay $12 per square foot, not inclusive of taxes and common maintenance expenses. Staff believes it is reasonable that the hospital would also have sought the most reasonable cost per square foot when searching for space to lease. If the $12 per square foot was not the going market value, it is doubtful that a not-for-profit hospital (TR 551) would be paying such a charge. Mr. Moore has supported the utility's management decision to lease from Caloosa, as outlined above, and has made it clear that the utility simply does not have the credit to borrow what it would need to build its own structure. (TR 600-602)

Based on the independent appraiser's report, the $12 per square foot charge that Gulf is paying to Caloosa is at market value. Further, a third party is leasing the remainder of the office space for $12 per square foot. Staff believes that to make an adjustment to the lease would be inconsistent with the Court's decision in GTE v. Deason, as outlined above. Accordingly, we recommend that no adjustment be made to the annual lease amount charged to Gulf by Caloosa.

ISSUE 38: Are any adjustments necessary to the common maintenance expenses associated with the building lease (Audit Disclosure 4)?

RECOMMENDATION: Yes, staff recommends an adjustment to reduce test year expenses by $3,600, prorated $2,376 to water and $1,224 to wastewater. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to the common maintenance expenses because they are billed to Gulf at cost.

OPC: Yes. Common maintenance expenses should be adjusted to reflect the actual amount that will be paid during the test year. As of July 1996, the amounts in the test year were overstated by $3,600.

STAFF ANALYSIS: In staff's Audit Disclosure No. 4, it is noted that the maintenance costs that are paid with Gulf's lease are estimated and a portion may be refunded based on actual costs. The estimated common maintenance expenses that Gulf pays total $9,828 for the test year. Common maintenance expenses include insurance, property taxes, electric, lawn care, and garbage collection. The staff auditors tested the reasonableness of these estimated expenses by annualizing total maintenance costs for the seven months ended July 31, 1996. The first seven months of 1996 were used because this information was known and measurable at the time of the audit. To annualize, total costs were divided by seven and then multiplied by twelve. Real estate taxes and insurance were then added to this annualized number to produce total estimated expenses of $18,474 related to the building. As Gulf occupies 33.71% of the building, the utility's share of the estimated expenses is approximately $6,228. Comparing the auditors estimate of $6,228 to the projected amount of $9,828 indicates that the MFRs are overstated by approximately $3,600. The audit opinion is that expenses should be reduced by this amount and prorated $2,376 to water and $1,224 to wastewater. (EXH 24, pg. 26)

The utility does not rebut audit staff's adjustment to common maintenance expenses associated with the lease. However, Gulf's position in its brief is that audit staff's adjustment is not based on the projected test year because the expenses for the first seven months of 1996 were annualized. Further, the utility stated that

common maintenance expenses are billed to Gulf at cost and that no adjustment is necessary. (BR 49-50)

OPC witness Dismukes agreed with audit staff's adjustment to reduce expenses by $3,600 for the overstatement in the MFRs. Although she does not specifically discuss the adjustment, her agreement is reflected in EXH 19, Schedule 5, page 1 of 2, where she made an adjustment to decrease water by $2,376 and wastewater by $1,224. Also, in its brief, OPC supports the testimony of Ms. Welch, as outlined on transcript pages 452-453. The brief states that there is no reason to believe that the last four months of the test year will be any different than the first seven, so the Commission should reduce test year expenses by $3,600. (BR 48)

It is staff's belief that the record fully supports reducing the common maintenance expenses associated with the lease. The utility's position, in its brief, that the expenses are billed to Gulf at cost, is irrelevant. The fact is that the utility's projection of $9,828 is overstated in comparison to the $6,228 estimated by audit staff. It is logical that in order to test the reasonableness of a projection, audit staff would annualize known expenses and make a comparison to the projection. It is also logical that expenses of this nature would not change dramatically for the remaining five months of the year, which supports annualizing the seven months that are known and measurable.

Based on the record, we believe that audit staff's estimate of common maintenance expenses associated with the lease is the best reflection of what these expenses should have been for the projected test year. We do not believe that the utility has supported its higher projection of expenses. Even though a portion of the expenses may be refunded based on actual costs, it seems appropriate that the projection should be as close as possible to what actual costs have been year-to-date. Accordingly, we recommend that the Commission approve an adjustment to reduce test year expenses by $3,600. Such an adjustment represents the difference between audit staff's estimate and the projection contained in the MFRs. The adjustment should be prorated as a reduction of $2,376 to water and a reduction of $1,224 to wastewater.

ISSUE 39: Are adjustments necessary to allocate additional administrative and general expenses, including rent, office supplies, miscellaneous business and administrative expense, vehicle expense and computer depreciation to the Caloosa Group (Audit Disclosure 3)?

RECOMMENDATION: Yes, it is necessary to allocate employee benefits, rent, office supplies, miscellaneous business and administrative expenses, car expenses, and computer depreciation to Caloosa for shared services. Accordingly, staff recommends a composite adjustment to Gulf's requested expenses of $9,236, which represents a decrease to water of $6,096 and a decrease to wastewater of $3,140. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustment should be made to these expenses, except an additional $1,400 should be allocated to the Caloosa Group primarily because of higher rental charges. There is no administrative expense.

OPC: Yes. Test year expense should be reduced by $7,445 to reflect administrative and general expenses that have not been properly charged to Caloosa.

STAFF ANALYSIS: As explained in Issue 34, the Caloosa Group is an affiliate to Gulf. This issue addresses the allocation of expenses considered to be related to employees who provide services for both companies. Staff witness Welch testified that Caloosa is currently charged $50 per month for the use of Gulf's computer system to process payroll, the general ledger, and minimal accounts payable. Caloosa is also charged $50 per month for office rent and supplies. The $1,200 per year charge is credited by Gulf to materials and supplies, administrative and general, and miscellaneous expense accounts. (TR 451, EXH 24, pg. 23)

Utility witness Cardey allocated overhead costs to Caloosa based on the total square footage of offices and the customer accounting and collecting area. He took the square footage of the offices of the five employees who provide services to Caloosa and multiplied that number by the percentage of time each employee worked for Caloosa. Next, he took that square footage as a percentage of total office, customer accounting, and collecting square footage, which gave him an allocation factor of 2.8%. He

used the 2.8% to allocate rent, security, cleaning, power, office supplies, and pest control expenses. This calculation reflects approximately $2,000 compared to the $600 that Caloosa currently pays for these items. Mr. Cardey then analyzed Caloosa's reimbursement for monthly use of Gulf's computers and determined that the additional $600 per year charge for this was reasonable. (TR 148-149) His analysis regarding allocation of general office expenses to Caloosa can be found in Exhibit 8, KRC-3. In total, $2,600 per year is the amount which witness Cardey represents to be appropriate as reimbursement to Gulf from Caloosa for the costs listed above.

OPC witness Dismukes allocated shared expenses based on three different allocation factors. First, she allocated health insurance and IRA benefits for the five employees that work for both companies based upon their Caloosa salary relative to their total Caloosa plus Gulf salary. Next, she allocated rent, office supplies, computer depreciation, and other business and administrative expenses based upon total payroll for Caloosa relative to total payroll for Caloosa plus Gulf. Third, she allocated Mr. Moore's car expenses based upon his Caloosa salary relative to his total Caloosa plus Gulf salary. Next, she compared the total of her calculations to the $1,200 per year currently being reimbursed by Caloosa. (TR 297-298) Ms. Dismukes' analysis regarding the allocation of expenses to Caloosa can be found in her Exhibit 19, Schedule 4. As pointed out at the hearing (TR 325), Ms. Dismukes' schedule contained a footing error, which caused her adjustment to be inappropriately reflected. As adjusted, Ms. Dismukes' recommended total adjustment to test year expenses is $9,372, allocated $6,186 to water and $3,186 to wastewater.

Staff witness Welch testified that for the most recent pay period, the audit staff calculated the percentage of Caloosa payroll to total Caloosa plus Gulf payroll at 2.13%. Next, audit staff determined expense items related to employees who perform tasks for both companies for the year September, 1995 to August, 1996. Audit staff allocated these expenses at the 2.13% payroll ratio and compared the calculation to the $1,200 per year currently being reimbursed by Caloosa. Audit staff's calculations result in a recommended decrease to projected expenses of $6,276, prorated accordingly between water and wastewater. (TR 451, EXH 24, pgs. 23-24)

Staff witness Welch testified that by using the payroll ratio method, the resulting adjustment may be understated because the allocation basis used is total company payroll while many of the expenses relate to Mr. Moore, who should probably be allocated on an individually higher basis than on a total company basis. However, the audit used a payroll basis to allocate expenses because a more appropriate allocation method could not be determined. (TR 451-452)

In rebuttal, utility witness Cardey contends that by using total payroll of both Gulf and Caloosa to make allocations, this is in error because total Gulf payroll contains the salaries of a plant operator, meter readers, and others that have nothing to do with the Caloosa payroll issue. (TR 650)

During cross examination, utility witness Cardey agreed that allocating employee benefits based on direct payroll would be an appropriate method, versus allocating based on square footage. He would not agree that direct payroll for Mr. Moore would be an appropriate method of allocating Mr. Moore's car expenses. (TR 685-686) It is staff's interpretation that Mr. Cardey's argument is with only those allocation factors which contain Caloosa payroll over total Caloosa plus Gulf payroll. That would include Ms. Dismukes' allocation factors for rent, office supplies, business and administrative expenses, and computer depreciation. Mr. Cardey does not offer an alternative method of allocating these expenses, other than his method based on square footage. Since his allocation factor of 2.8%, discussed above, considers the percentage of time that the five employees spend on Caloosa-related business, and because staff believes that the evidence does not support his recommended percentages in Issue 34, we do not recommend using his factor as an alternative in this issue. Staff also points out that his allocation factor is higher than the allocation factor of 2.62% used by Ms. Dismukes and the factor of 2.13% used by the audit staff.

Staff believes that the allocation methodology used by Ms. Dismukes is appropriate. We believe that by taking Caloosa payroll over total payroll for Caloosa plus Gulf in allocating rent, office supplies, business and administrative expenses, and computer depreciation, it is appropriate because of the nature of these expenses. Further, if these expenses were allocated using the ratio of Caloosa payroll over payroll for only those employees of Caloosa plus Gulf, this would result in a higher allocation factor

of 8.85%, according to Ms. Dismukes' analysis. Thus, it is unclear to staff why the company has taken such issue with these allocation factors.

In conclusion, staff believes that the evidence supports Ms. Dismukes' expense allocations based upon three different allocation factors, as outlined in this issue. Attached to this issue is a schedule which reflects staff's recommended allocations to Caloosa. Accordingly, after consideration of staff's recommended adjustments to rent and business and administrative expenses covered in Issue 37 and Issue 48, respectively, staff recommends a reduction to Gulf's requested test year expenses (as individually discussed above) of $9,236. This adjustment is a decrease of $6,096 to water and $3,140 to wastewater, prorated according to a 66/34 ratio.

EXPENSE ALLOCATIONS TO CALOOSA – ISSUE 39

	Totals Before Adjustment	Totals After Staff Rec. Adjs.		Allocation Factor	Allocation to Caloosa
IRA	21,775	21,775		0.0885	1,927
RENT	59,830	56,230	(1)	0.0262	1,473
HEALTH INS	20,995	20,995		0.0885	1,858
OFFICE SUPPLIES	20,715	20,715		0.0262	543
BUS. EXP./ CONF./ADMIN.	56,709	55,084	(2)	0.0262	1,443
CAR EXP.	21,884	21,884		0.1111	2,431
COMPUTER DEPR.	29,027	29,027		0.0262	761
TOTAL	230,935	225,710			10,436

Recommended allocation to Caloosa	10,436
Amount currently charged by Gulf	1,200
Recommended adjustment to expenses	(9,236)
Allocation to Water @ 66%	(6,096)
Allocation to Wastewater @ 34%	(3,140)

(1) After staff's recommended adjustment in Issue 38
(2) After staff's recommended adjustment in Issue 48

ISSUE 40: Are any adjustments necessary to Gulf's requested level of directors fees (Audit Disclosure 2)?

RECOMMENDATION: No, staff believes that to have a Board of Directors for Gulf is prudent and that the fees are reasonable. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments to the directors fees are necessary. These fees are necessary and proper in the conduct of Gulf's business.

OPC: Yes. Test year expenses should be reduced by $9,000 for excessive fees paid to the board of directors.

STAFF ANALYSIS: Directors fees are the subject of staff's Audit Disclosure No. 2, and were included in the audit report for informational purposes. For the test year, directors fees total $18,000. Staff witness Welch made no opinion in her testimony regarding directors fees. (TR 450, EXH 24, pg. 22)

OPC witness Dismukes recommended an adjustment to directors fees based on her review of the Board of Directors Meeting Minutes, which indicate that not all of the directors attend the meetings. She states that in 1996, only Russell Newton, Jr. attended all three meetings. William Newton attended only one, and Russell Newton, III attended two of the three meetings. In 1995, Russell Newton, Jr. again attended all three meetings. William Newton and Russell Newton, III attended only one of the three meetings. (TR 306)

The directors fees included in the test year include $4,500 to be paid to Russell Newton, Jr., $4,500 to be paid to William Newton, and $9,000 to be paid to Russell Newton, III. (EXH 24, pg. 22) Ms. Dismukes recommended reducing two-thirds of the fees for William Newton, since he attended only one meeting in both of the years analyzed. Further, she recommended reducing the fees paid to Russell Newton, III, first by one-half because she does not believe that he should be paid twice as much as the other directors. Next, she further reduced the fees for Russell Newton, III by one-third, based on his attendance at two of the three meetings in 1996. Witness Dismukes' recommended adjustments to directors fees reduces test year expenses by $9,000. She stated that further adjustments

could certainly be made at the discretion of the Commission, as not much is discussed at the meetings. (TR 306-307)

Utility witness Moore stated that directors have potential liabilities in exercising their responsibilities and that it is common practice to pay non-employee directors a fee for their services. He stated that, while the directors may not attend every meeting, they are very active in meetings amongst themselves and management. Mr. Moore testified that the fees are reasonable given the size of the company, the needs of the company, and the directors' responsibilities. (TR 564)

Staff believes that it is appropriate for a Class A utility to have a Board of Directors, unless the evidence demonstrates that to have one is not prudent. We believe that the record supports that the Board of Directors for Gulf is acting in a prudent manner and that the fees are reasonable. Staff does not believe that the record supports Ms. Dismukes' suggested adjustments because she has looked only to the minutes of the meetings to make her recommendation. Ms. Dismukes did not consider the work that the directors might perform outside of the business conducted at directors' meetings. Staff believes that it is logical for directors to conduct their responsibilities in a variety of ways. Therefore, staff agrees with Mr. Moore that the directors fees are reasonable given the size of the company and the directors' responsibilities. Accordingly, we recommend that no adjustment be made to directors fees.

ISSUE 41: Should any adjustments be made to remove expenses for lift station coating from the test year?

RECOMMENDATION: No. The expenses incurred are ongoing expenses and no adjustments should be made. (FUCHS)

POSITION OF THE PARTIES

GULF: No adjustments should be made for lift station maintenance.

OPC: Yes. Test year expenses should be reduced by $10,500 to remove nonrecurring expenses.

STAFF ANALYSIS: Gulf Utility has numerous manholes and lift stations in its wastewater collection system. The Utility has a preventive maintenance program to assure proper operation of the system. OPC disagrees with a portion of the expenses claimed by Gulf claiming that it is a non-recurring expense.

Gulf witness Messner testified that Gulf has 42 lift stations and more than 600 manholes. The maintenance of these facilities is included in the requested $21,000. (TR 798) Mr. Messner testified that to relate the allowance proposed by OPC witness Dismukes would allow just $250 per lift station per year. Mr. Messner testified that it is not possible to maintain adequate and safe service to Gulf's customers without adequate maintenance expenditures. (TR 798) Mr. Messner offered a cost breakdown of liftstation repairs that averages $1,500 to $2,000 per station per year. This cost does not include coating costs of $8,000 each for the three planned per year to be coated. (TR 799) Mr. Messner testified that there must be routine annual preventive maintenance to prevent damage to the liftstations. (TR 799)

OPC witness Dismukes testified that Gulf indicated it did not incur any cost to coat liftstations in 1993, 1994, or 1995, but that it did incur liftstation repair costs of $11,919 in 1994 and $6,980 in 1995. It did not, however, incur these costs in 1993. (TR 304) Ms. Dismukes testified that the liftstation expense should be reduced by $10,500, due to this expense being non-recurring. (TR 304)

According to the record, Gulf has $18,000 to $24,000 per year scheduled in coating costs, not including the regularly scheduled maintenance of the liftstations and manholes. (TR 799) Based on

evidence in the record, Staff believes the expenses and repair schedule outlined by Gulf to be reasonable. Staff recommends the liftstation expenses presented by Gulf Utility Company are reasonable and no adjustments be made.

ISSUE 42: Are adjustments necessary to remove charitable contributions from operations and maintenance expenses? (Audit Exception 3)

RECOMMENDATION: No, charitable contributions are not included in test year expenses; therefore, no adjustment is necessary. However, staff does recommend that the utility be required to reclassify charitable contributions to a below-the-line account in accordance with Rule 25-30.115(1), Florida Administrative Code. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to remove charitable contributions from operations and maintenance expenses because these are not included in Gulf's test year.

OPC: Yes. $3,200 of charitable contributions included in the Company's budget should be removed from test year expenses.

STAFF ANALYSIS: Audit Exception No. 3 states that charitable contributions totaling $1,910 ($1,270 for water and $640 for wastewater) were included by the utility in accounts 675.8 and 775.8, miscellaneous expenses, for the audited period of September, 1995 to August, 1996. The miscellaneous expense accounts are above-the-line accounts, which means that these accounts would be included in the utility's test year projections. Staff witness Welch testified that Commission Rule 25-30.115(1), Florida Administrative Code, requires that water and wastewater utilities shall maintain accounts and records in conformity with the 1984 NARUC Uniform System of Accounts (USOA) adopted by the National Association of Regulatory Utility Commissioners. The USOA prescribes that "donations for charitable, social, or community welfare purposes" should be charged to Account 426, Miscellaneous Nonutility Expense, a below-the-line account. Accordingly, Ms. Welch recommended that these expenses be reclassified to the below-the-line expense account. (EXH 24, pg. 10, TR 446)

On cross examination of utility witness Andrews, OPC pointed out a correlation between the company's 1996 budgeted expenses and the miscellaneous expense projections contained in the MFRs. Ms. Andrews was referred to page 76 of the MFRs, which is a schedule of adjustments to operating income. Ms. Andrews agreed that miscellaneous expenses listed on this page total $71,289. Next,

Ms. Andrews was referred to a breakdown of these miscellaneous expenses that was provided by the utility in response to a MFR deficiency letter. She agreed that the $71,289 miscellaneous expense projections include $3,200 for a customer survey. Next, OPC referred Ms. Andrews to the utility's response to OPC's Document Request No. 32, which is a copy of Gulf's 1996 budget. Here, OPC pointed out that the utility's 1996 budget for miscellaneous expenses totals $71,289 and contains $3,200 for charitable and political contributions. OPC matched every other item in the utility's budget to the MFRs, except charitable and political contributions. OPC suggested that the charitable and political contributions are being covered up in the MFRs as expenses related to a customer survey. (TR 860-866, EXH 47, 48)

Utility witness Andrews testified that charitable contributions were not included in test year expenses. She stated that the survey was estimated at approximately $3,200, that it was performed in the latter part of 1996, and that the results were provided to OPC. It is Ms. Andrews' position that no adjustment is necessary to remove charitable contributions from test year expenses. (TR 845, 863-865)

Although the utility has included charitable contributions in above-the-line accounts, staff does not believe that the dollar amount for such contributions has been included in test year expenses. The customer survey to which Ms. Andrews referred was conducted by the utility and the results were provided to staff. Additionally, there were costs associated with conducting the survey, which is the subject of Issue 46 and Audit Disclosure No. 10. Based on this, staff does not agree with OPC that the $3,200 expense projection for the customer survey is a disguise for charitable contributions. Staff recommends that no adjustment should be made to remove charitable contributions from test year expenses, as none are listed in the MFRs under miscellaneous expenses. However, staff does recommend that the utility be required to reclassify charitable contributions to a below-the-line account in accordance with Rule 25-30.115(1), Florida Administrative Code.

ISSUE 43: Should any adjustments be made to remove from test year expenses golf outings and gift basket expenses?

RECOMMENDATION: Yes, however, no adjustment is necessary in this issue, as staff has considered the expenses for golf outings and gift baskets as part of our analysis in Issue 48. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments to test year expenses for "golf outings and gift basket expenses" should be made because these expenses are not included in Gulf's test year.

OPC: Yes. Test year expenses should be reduced by $185.

STAFF ANALYSIS: This is an issue brought forth by OPC witness Dismukes, wherein she made an adjustment to remove from test year expenses $780 related to golf outings and gift baskets. Ms. Dismukes revised her testimony at the hearings to a reduction of only $185. (TR 305, 288)

The utility's position, in its brief, is that these sort of expenses are not included in the test year projections and, therefore, no adjustment is necessary. (BR 54)

Staff is uncertain what Ms. Dismukes' suggested adjustment is based upon; although, it appears that it may be based on the data obtained from Mr. Moore's travel and entertainment expense reports. These expense reports are identified as Exhibit No. 5 and the contents are the subject of Issue 48. Items such as golf outings and gift baskets are contained in the expense reports. While staff agrees with Ms. Dismukes that it is not appropriate to include expenses for golf outings and gift baskets in test year projections, we will address the removal of such costs in Issue 48. Staff notes that the utility did not rebut this issue or Issue 48, so there is nothing in the record to prove that the expenses are not included in test year projections. Accordingly, we recommend that the Commission make no adjustment in this issue.

ISSUE 44: Should the Commission include budgeted "unanticipated" expenses in the test year?

RECOMMENDATION: No, staff recommends that the Commission disallow total unanticipated expenses of $5,000, which should be prorated as a reduction to water and wastewater of $3,300 and $1,700, respectively. (WEBB)

POSITION OF THE PARTIES

GULF: These miscellaneous expenses should be allowed in the test year.

OPC: No. These expenses, in the amount of $4,895, should be removed from test year expenses.

STAFF ANALYSIS: On page 75 of the MFRs, EXH 8, the utility has included $1,000 in unanticipated expenses for contractual services for treatment-operations, prorated $660 to water and $340 to wastewater. On page 76 of the MFRs, the utility has included $4,000 of unanticipated expenses in the miscellaneous expense account, prorated $2,640 to water and $1,360 to wastewater.

In OPC witness Dismukes' testimony, she has recommended the removal of expenses which the utility has characterized as "unanticipated". In her opinion, it would not be good Commission policy to allow such nondescript expenses in the projected test year. Ms. Dismukes further stated that it is the utility's burden to prove the reasonableness of its projected expenses, including all expenses that it anticipates. Therefore, she recommended that the Commission disallow all unanticipated expenses. Ms. Dismukes' adjustment is contained in her Exhibit 19, Schedule 10. Her adjustment related to the miscellaneous expense account is net of an allocation to Caloosa of 2.62%. Her allocation factor is taken from her recommended adjustments in Issue 39. In total, Ms. Dismukes recommended that expenses be reduced by $4,895, which represents a $3,231 reduction to water and a $1,664 reduction to wastewater. (TR 304)

Utility witness Andrews' opinion is that the company must allow for unanticipated expenses that occur annually in the normal course of business and which are not specifically itemized in the company's budget. Ms. Andrews explained that the utility had to hire a safety consultant to manage the company's safety program,

which is necessary in order to meet OSHA standards. During cross examination, Ms. Andrews was asked how the Commission could be assured that the category of unanticipated expenses does not include nonutility related expenses. Her response was, "Well, I don't know that you would know that." (TR 868-870, BR 54)

It is staff's belief that the utility has not met its burden of proof that the category of unanticipated expenses relates to valid, utility-related business expenses. It is staff's opinion that the utility's inclusion of $5,000 in unanticipated expenses is nothing more than a padding of the total requested expenses. The purpose of the projected test year is for the utility to include its best estimates of costs that will be prudently incurred. Staff does not believe that it is acceptable to include in projections a category of expenses which are not identified, but are included as a safety net for costs which may or may not occur in the future.

Staff agrees with witness Dismukes' recommended adjustment, with the exception of the small amount that she allocates to Caloosa. We believe that she should not have made an adjustment to allocate anything to Caloosa. Further, we believe that she probably confused this issue as being related to Issue 39, but the two issues are not related. By applying her allocation factor in this adjustment, she allows a small amount of unanticipated expenses to remain in the test year and we do not believe that this is appropriate.

Accordingly, staff recommends that all unanticipated expenses should be removed from the projected test year expenses. The total unanticipated expenses are $5,000 and should be prorated as a reduction to water and wastewater in the amount of $3,300 and $1,700, respectively.

ISSUE 45: Are adjustments necessary to remove amortization of the San Carlos water line project (Audit Disclosure 5)?

RECOMMENDATION: No, the utility has abandoned this project, so test year amortization is appropriate. However, according to the numbers in Audit Disclosure 5, the annual amortization should be $5,920 instead of $8,184. Therefore, staff recommends an adjustment to reduce test year amortization for the water system by $2,264. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to remove amortization of the water line project.

OPC: Yes. These costs have not been demonstrated to be prudent. Test year amortization should be reduced by $8,184.

STAFF ANALYSIS: According to staff's Audit Disclosure No. 5, as of December, 1993, the utility had recorded $11,827 of engineering costs for the San Carlos waterline project in a deferred account. The utility recently added $17,773 to this account for additional costs. The account was projected to be amortized over 5 years at an annual expense of $8,184. Originally, the utility described this project as construction work in progress. During the last audit, when asked why the costs had not been charged to construction work in progress as part of the water line costs, the utility responded that it had not yet received approval from the county for the installation of the line, nor was the county going to require mandatory hook-ups. The auditors in this case again asked the question and the utility responded that the project was being abandoned because the county would not require mandatory hook-ups. (TR 453, EXH 24, pg. 27)

OPC's position, in its brief, is that these costs have not been demonstrated to be prudent. Further, the brief questions why the charges were incurred in the first place if the utility had to wait on the county to require mandatory hook-ups. The brief states that this determination should have been made by Gulf prior to expending funds on the project. Therefore, OPC recommends that test year expenses be reduced for the amortization of project costs. (BR 55)

Staff does not agree with OPC because we believe that the record supports the utility's uncertainty regarding the county's requirement for mandatory hook-ups. We believe that the utility acted with prudence in planning and expending funds for this project. The utility is required by Section 367.111(1), Florida Statutes, to provide service within a reasonable time frame from the time that a customer requests service. Therefore, we believe that Gulf was anticipating the future needs of the utility.

Utility witness Moore confirmed that this project has been abandoned. (TR 619) According to Rule 25-30.433 (8), Florida Administrative Code, nonrecurring expenses shall be amortized over five years, unless a shorter or longer period can be justified. Staff believes that a five-year amortization period is appropriate, as it relates to this project. However, according to the numbers in Audit Disclosure 5, the annual amortization should be $5,920 instead of $8,184. Therefore, staff recommends an adjustment to reduce test year amortization for the water system by $2,264.

ISSUE 46: Is an annual customer satisfaction survey necessary, and what, if any, adjustments are appropriate to test year expenses (Audit Disclosure 10)?

RECOMMENDATION: No, staff recommends that an annual survey is not necessary, but the evidence supports conducting one on a less frequent basis, because Gulf does not have quality of service problems. Therefore, we recommend that the Commission allow the costs associated with the survey, but that the costs should be amortized over five years. Thus, staff recommends that test year expenses be reduced by $5,145 for water and $2,650 for wastewater. (WEBB)

POSITION OF THE PARTIES

GULF: The cost of an annual customer survey should be included in test year expenses.

OPC: Customer survey expenses appear to be a disguise for charitable contributions and should therefore be removed from test year expenses.

STAFF ANALYSIS: Staff witness Welch testified to the customer survey costs addressed in Audit Disclosure No. 10. She stated that the costs associated with the survey were included in the company's test year projections and that this is the first time the utility has conducted such a survey. The costs total $9,744 and are allocated $6,431 to water and $3,313 to wastewater. Ms. Welch does not give an opinion as to whether the survey costs should or should not be included in test year expenses, she only testified to the projections contained in the MFRs. (TR 455, EXH.24, pg. 33)

OPC's position, in its brief, is that the customer survey expenses appear to be a disguise for charitable contributions discussed in Issue 42. Accordingly, OPC recommended that the customer survey expenses be removed from test year expenses. (BR 56)

Ms. Andrews testified that the survey was conducted in the late summer of 1996. She stated that the utility conducted the survey to find out what the customers think of the quality of service, and to obtain the customers' input on improvements. The utility's position, in its brief, is that the survey should be done at least annually as an ongoing effort to assure a satisfactory

level of service to its customers. Further, the utility states that there is no connection between the $3,200 cost of the survey and charitable contributions. (TR 864-865, BR 55)

Staff believes that it is important for a utility to be aware of its customers' opinions regarding the services provided by the utility. We also believe that a survey is a legitimate method for Gulf to determine how it rates with its customers. Staff does note that there are no quality of service concerns associated with this proceeding, nor have there been any such concerns in the past that have come to the attention of staff. We believe that Gulf should be commended for the level of service that it is able to provide to its customers.

Since there are no quality of service concerns in this proceeding and there are no other concerns with which staff is aware, we do not believe that the survey is necessary on an annual basis. Considering Gulf's record of good customer service, it seems that a survey could be conducted every five years and still be effective and informative. It is staff's opinion that if the utility wishes to receive feedback from its customers on a more frequent basis, it could achieve the same results by including a note or questionnaire in the monthly bill. For these reasons, staff believes that a customer satisfaction survey is not necessary on an annual basis. Accordingly, we recommend that the Commission allow the costs associated with the survey, but that the costs should be amortized over five years, in accordance with Rule 25-30.433, (8), Florida Administrative Code. Thus, staff recommends that test year expenses be reduced by $5,145 for water and $2,650 for wastewater to reflect that the $9,744 in projected expenses should be amortized over a five-year period.

ISSUE 47: Are adjustments necessary to remove expensed costs related to preliminary survey charges for FGCU (Audit Disclosure 11)?

RECOMMENDATION: No, staff witness Welch agrees with the utility that audit staff made an error; therefore, no adjustments are necessary. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to remove expensed costs. These costs are for engineering service required under the bond indenture, engineering service on franchise mapping, etc. and only $32 relate to FGCU.

OPC: Yes, it appears that Contractual Services-Engineering should be reduced by $1,029 for water and $310 for wastewater and recorded in construction work in progress.

STAFF ANALYSIS: According to Audit Disclosure No. 11, there were two invoices for engineering costs related to FGCU that were charged to the contractual services expense account instead of being capitalized as part of the university. The costs were related to the preliminary survey for the university. (EXH 24, pg. 34)

Utility witness Andrews testified that the charges on the invoices that audit staff reviewed needed to be broken out in order to determine that only a small portion related to the university. Since the utility did not break out the charges for audit staff, Ms. Andrews believed that audit staff made an innocent error. She states that there was one charge for $100 that was expensed which related to the university. (TR 217)

Staff witness Welch agreed with Ms. Andrews that the audit staff made an error. Thus, Ms. Welch deleted page 34 of the audit report which is Audit Disclosure No. 11. (TR 441)

Since Ms. Welch deleted Audit Disclosure No. 11, this has become a non-issue. Also, OPC deferred analysis of this issue to staff. (BR 56) Staff believes that OPC's position, as stated above, is erroneous in that OPC did not follow up and correct its position after the testimony provided at hearing. We believe that OPC's intention is for its position to be in accordance with

staff's position. Accordingly, staff recommends that no adjustment be made to expensed costs related to preliminary survey charges for the FGCU.

ISSUE 48: Are adjustments necessary to remove local business and entertainment expenses for Gulf's president (Audit Disclosure 15)?

RECOMMENDATION: Yes, staff recommends that the Commission should reduce test year expenses by $1,625, prorated $1,072 to water and $553 to wastewater. (WEBB)

POSITION OF THE PARTIES

GULF: No adjustments are necessary to remove "local business and entertainment expenses." All expenses are utility business expenses and are explained. There are no entertainment expenses.

OPC: Yes. Excessive and unreasonable business meals and entertainment expenses should be removed from test year expenses.

STAFF ANALYSIS: Audit Disclosure No. 15 states that test year expenses include $1,868 for business meals and $120 for entertainment related to Mr. Moore. The descriptions on business meals include: discussing health insurance plans, trusts and investments, engineering services, and waterline projects, among other things. The entertainment expense was for drinks while discussing the San Carlos waterline project and a golf outing to discuss the cost of insurance. (EXH 24, pg. 47) Staff witness Welch did not render an opinion or recommendation on these expenses, she only testified to what the disclosure is reporting. (TR 457)

Mr. Moore did not rebut the information contained in staff's Audit Disclosure No. 15, nor did witness Andrews or witness Cardey. On cross examination, Mr. Moore was asked to explain various expenses of his related to business meals and entertainment. Exhibit No. 5, the source of questioning, includes travel, meal, and entertainment expense reports for Mr. Moore from October, 1994 through mid-October, 1996. Mr. Moore was asked to explain why customers should pay for meal expenses for business associates and their spouses in order to discuss business; for rounds of golf and lunches to discuss insurance and capital projects; for drinks for board members prior to a board meeting; for meals to discuss security for the Caloosa-owned office building; for meals to discuss the purchase of vehicles from Ford sales representatives; for gift baskets for vendors; and for meals to discuss the development of property that would be in the utility's service

area. The meal expense items discussed with Mr. Moore ranged from $6 per person up to $50 per person. (TR 91-114)

In quite a few instances, Mr. Moore agreed that the business he discussed with his associates could have been conducted at his office or at the offices of his associates. However, Mr. Moore stated that his expenses are legitimate business expenses. He also stated that it is cost efficient to have meals with people where business can be discussed and the utility is not being billed an hourly rate for services. Further, Mr. Moore testified that, in bringing people together over a meal, the objective of cooperation among the parties is accomplished. The utility's position, in its brief, is that no adjustment is necessary to remove any of Mr. Moore's business expenses. (TR 92-114, BR 55) There was no redirect by Gulf's attorneys related to this topic. (TR 130)

In its brief, OPC contends that Mr. Moore spends considerable resources and money on entertaining his associates and vendors. OPC points out that while Mr. Moore may believe it is customary to entertain spouses of business associates, OPC believes it is inappropriate and that the expenses should not be borne by ratepayers. OPC contends that, in many instances, the per person cost of a meal is extravagant and not a legitimate business expense. As such, OPC recommends that the Commission disallow 50% of all of Mr. Moore's projected test year entertainment expenses. OPC suggests that 50% should be disallowed, as this is the policy followed by the IRS for deductible items for tax purposes. OPC believes that such an adjustment would be an incentive for the utility to hold down its meal and entertainment expenses. Accordingly, the Citizens recommend a $3,250 reduction to test year expenses. (BR 56-57)

Staff reviewed the travel, meal, and entertainment expense reports contained in Exhibit No. 5 and we believe that, in many instances, the business could have been discussed at the utility or at the offices of Mr. Moore's associates. Likewise, Mr. Moore agreed to this, as outlined above. Staff does not believe that it is appropriate to entertain spouses of business associates, even though this may be customary in a private company. The distinction, here, is that the expenses are definitely nonutility related and should not be borne by ratepayers. Additionally, we believe that Mr. Moore's meal and entertainment expenses are sometimes excessive, on a per person cost basis.

Staff agrees with OPC's position regarding Mr. Moore's meal and entertainment expenses, to the extent that his expenses are considerably high and that some are not legitimate. However, we do not agree with OPC's 50% adjustment based on the IRS's rules for deductible expenses. We do not believe that the issue is whether or not an expense is deductible; rather, the issue is whether the expenses are legitimate, utility-related expenditures. Therefore, staff has come to a different determination of making an expense adjustment. From Exhibit No. 5, staff determined Mr. Moore's total reimbursable expenses for the most recent 12-month period of October, 1995 through mid-October, 1996 to be $12,104. For the same period, we calculated only those expenses related to meals and entertainment, which were $2,670. Next, we took total expenses related to meals and entertainment divided by total reimbursable expenses, which indicates that 22% of his expenses are related to meals and entertainment. We performed the same calculation for the period of January through December, 1995 expenses, and found that 33% of Mr. Moore's total business expenses related to meals and entertainment.

Staff realizes that some allowance should be approved for meals and entertainment which would occur in the normal course of utility business. Staff points out, however, that the record is not clear as to what a legitimate amount would be for meals related to travel. Additionally, staff believes that the record does not support the utility's position that no adjustment needs to be made. To reiterate, the utility did not provide rebuttal on this issue nor did Gulf's attorney provide redirect examination after OPC's extensive cross examination of the topic. Thus, staff believes that, while some allowance should be made for legitimate meals related to travel, some adjustment should be made to Mr. Moore's expenses that are either nonutility or extravagant in nature.

Staff does not believe that the record is clear as to the contents included in the utility's $6,500 projection for Mr. Moore's travel and other business expenses. (EXH 47, pg. 76 of MFRs) In other words, it is not certain what percentage of this projection is related to meals. Therefore, it is difficult to make a correlation between the projection in the MFRs and the total dollar amount of expenses for the 1995 and 1996 periods, described above. Lacking a more precise alternative, staff recommends an adjustment to reduce Mr. Moore's projected travel and other business expenses by 25%. We arrived at this percentage by considering our calculations above, which demonstrate that 22% and

33% of total business expenses related to meals and entertainment for 1995 and 1996, respectively. (We do want to note that we also annualized the data for 1996, which yielded a percentage of 23%. This is not materially different from the 22% we arrived at by utilizing the most recent 12 months of data.) The 25% recommended adjustment allows for an 8% (33% minus 25%) allowance for meals included in our calculation which would relate to legitimate travel, as travel expenses are not at issue. Staff believes that, based on the evidence in the record, this is the most appropriate way to make an adjustment for those expenses of Mr. Moore's that we believe to be extravagant or nonutility related.

Applying the 25% reduction to the $6,500 projection in the MFRs yields a decrease of $1,625 to test year expenses. Accordingly, staff recommends that the Commission reduce test year expenses by this amount, prorated $1,072 to water and $553 to wastewater.

ISSUE 49: What is the appropriate provision for rate case expense?

RECOMMENDATION: The appropriate provision for rate case expense is $220,000, resulting in an increase of $97,521 over the amount requested in the MFRs. The four-year amortization results in additional test year rate case expense of $24,380, prorated $16,091 and $8,289 to water and wastewater, respectively. (WEBB)

POSITION OF THE PARTIES

GULF: The amount of rate case expense is $251,890.65.

OPC: The Citizens believe that the Commission should hold the utility to its initial estimate of rate case expense of $122,479.

STAFF ANALYSIS: The projected provision for rate case expense contained in the MFRs totals $122,479, representing an allocation of $80,836 to water and $41,643 to wastewater. (EXH 8, pg. 86) Utility witness Moore provided an updated rate case expense estimate in his rebuttal testimony. The estimate shows that, in accordance with Stipulation No. 8, total rate case expense also includes costs associated with the overearnings investigation. The utility's final request for rate case expense, including estimates to complete and costs associated with the overearnings investigation, totals $220,000. This amount results in annual amortization expense of $36,300 and $18,700 for water and wastewater, respectively. (EXH 30, JWM-7) The components of the original and final requests are as follows:

	MFRs	EXH 30
Cronin, Jackson, Nixon & Wilson	$19,500	$38,153
Keith R. Cardey, Consultant	40,000	55,246
Gatlin, Schiefelbein & Cowdery	47,500	90,508
Source, Inc.	0	6,292
Gulf Utility Company	15,479	29,801
Total	$122,479	$220,000

On cross examination, utility witness Moore was asked to correct the utility's Exhibit No. 30, the final request for rate case expense. According to the summary page of Exhibit 30, JWM-7, the fees and additional costs for Mr. Nixon's estimate to complete were not consistent with the backup data. Mr. Moore agreed that the utility made an error and that the total costs related to Mr. Nixon should be $38,153. Considering this adjustment, the utility's request for recovery of rate case expense totals $220,000. Mr. Moore argued that the increase in rate case expense over the original estimate in the MFRs was due to OPC's intervention. Further, Mr. Moore explained that due to the extensive lines of questioning by OPC and the nature of the testimony required, it was necessary for the utility to bring in expert witnesses. Also, Mr. Moore stated that Gulf chose not to file a Proposed Agency Action (PAA) case because they were advised not to, as the case would probably end up at hearing, anyway. (TR 581-591)

In its brief, OPC argued that the utility's requested increase in rate case expense, about 80% over the original estimate, is unsupported. Additionally, in response to witness Moore's explanation on cross examination (TR 587-588) that the increase was a result of the intervention of the Office of Public Counsel, OPC argued that intervention is routine in dockets that are initially set for hearing. Thus, OPC contends that Mr. Moore's explanation is inadequate and not compelling. OPC also argued that the utility did not act prudently in that Gulf estimated rate case expense without anticipating the intervention of Public Counsel. Therefore, OPC recommends that the Commission should only allow rate case expense in the amount that was originally requested, $122,479. (BR 57-58)

It is staff's belief that the utility's request for rate case expense is fully supported by Exhibit 30. Based on our review of the supporting documentation, we believe that the costs incurred were reasonable and prudent. Further, considering the fact that this case began as an overearnings investigation, and the costs associated with the investigation are added to rate case expense, it seems reasonable that costs are somewhat higher.

We agree with OPC that the utility and its consultants could have projected for OPC's intervention. However, we do not believe

that it would be appropriate to deny recovery of additional rate case expense over that which was requested in the MFRs. Staff believes that projections for rate case expense are somewhat different from other expense projections in that it is difficult to determine the extent to which consultants will be needed to defend the utility's positions. It is staff's opinion that rate case expense can sometimes vary dramatically from the projection in the MFRs, but this does not mean that the utility acted imprudently. The prudence of the overall rate case expense should be evaluated on a case-by-case basis. In this case, we believe that Gulf acted prudently in defending its positions related to this proceeding.

Based on the record, we do not recommend any adjustments to the utility's requested rate case expense. Accordingly, staff recommends that the Commission approve a provision of $220,000 for rate case expense, resulting in an increase of $97,521 over the amount requested in the MFRs. The four-year amortization results in additional test year rate case expense of $24,380, prorated $16,091 and $8,289 to water and wastewater, respectively.

ISSUE 50: What adjustments are appropriate to test year depreciation expense? (Audit Exception 6)

RECOMMENDATION: Staff recommends that the Commission should approve an increase to depreciation expense for water and wastewater in the amount of $78,338 and $42,770, respectively. Also, staff recommends that a matching adjustment be made to increase the 13-month average accumulated depreciation on water and wastewater plant in the amount of $44,416 and $21,385, respectively. (WEBB)

POSITION OF THE PARTIES

GULF: Test year depreciation expense, should be increased by $78,338 for water and should be increased by $42,770 for wastewater.

OPC: Adjustments appear necessary to remove retirement adjustments incorrectly made and to remove depreciation expense on any additional non-used and useful plant adjustments.

STAFF ANALYSIS: According to staff's Audit Exception No. 6, the utility's projection for depreciation expense is understated due to the fact that retirements were booked against this account. When an asset is retired, it should only be adjusted against the accumulated depreciation account. The utility had also used an incorrect rate in their calculation of depreciation for the proforma for the Corkscrew addition. Staff witness Welch testified that in order to correct the depreciation expense projection, the audit staff utilized Gulf's depreciation rates and plant as of August, 1996. Depreciation on fully depreciated plant was removed and the net was then compared to the company's forecast. The audit includes the detailed calculation, which results in audit staff's adjustment to increase depreciation expense for water by $102,236 and wastewater by $46,689. (TR 448-449, EXH 24, pg. 16)

Utility witness Andrews stated that all parties are using the same depreciation rates, but not the same investment in assets being depreciated. She explained that in December, 1995, Gulf put into service the Three Oaks WWTP and that the projections include 12 months of depreciation. Ms. Andrews testified that, based on audit staff's analysis of the period September, 1995 through August, 1996, audit staff erroneously left out the 2 months of October and November, 1995, for the depreciation on Three Oaks

WWTP. Therefore, Ms. Andrews has calculated an adjustment to depreciation expense that she believes is appropriate. Her adjustment also included corrections for retirements inappropriately booked by the utility, which is in agreement with staff's audit. Ms. Andrews recommended an adjustment to increase depreciation expense for water by $78,338 and to increase wastewater by $42,770. Her testimony also suggested an adjustment to accumulated depreciation for water and wastewater in the amount of $87,458 and $42,770, respectively. (TR 845-846)

OPC witness Dismukes agreed with audit staff's recommended adjustments in Audit Exception No. 6. However, she later had her testimony stricken because she believed that, with the exception of how the retirements are treated, this is a fall-out issue. She stated that all parties have agreed on the treatment for retirements. (TR 288, 309-310, 346-347)

Staff agrees with the rebuttal testimony of Ms. Andrews that the audit staff's adjustment related to the Three Oaks WWTP is incorrect due to the fact that a full twelve months of depreciation was not included in the calculation. It has been stated above that all parties agree on the adjustment to correct for retirements inappropriately booked against the depreciation expense account. Accordingly, the record shows that the only adjustments necessary are to correct for the retirements and the Three Oaks WWTP, as outlined above. Therefore, staff recommends that the Commission approve an adjustment to increase depreciation expense for water and wastewater in the amount of $78,338 and $42,770, respectively. Also, staff recommends that a matching adjustment be made to increase the 13-month average accumulated depreciation on water and wastewater plant in the amount of $44,416 and $21,385, respectively. Although Ms. Andrews' adjustment was on a year-end basis, staff believes that a 13-month average is appropriate to be consistent with the averaging methodology required in the MFRs.

ISSUE 51: What is the appropriate provision for income tax expense, before any rate increase for water and wastewater, respectively?

RECOMMENDATION: The appropriate income tax expense is $107,436 for water and $(49,542) for wastewater. (MERCHANT)

POSITION OF THE PARTIES

GULF: Income tax expense should be $19,663 for wastewater and $19,770 for water.

OPC: No position in brief.

STAFF ANALYSIS: Utility witness Nixon prepared the Income Tax Section in the MFRs based on the 1995 historic test year and the projected test year ended December 31, 1996. (TR 229-321) In the MFRs, the utility requested income tax expenses of $85,449 and $0 for water and wastewater, respectively. Staff is unsure as to how the utility's amounts in its briefs were determined, as they are not in the MFRs or other evidence in the record. There was no evidence in the record that supports a specific adjustment to income tax expense and any adjustments would be a fall-out of any changes made to rate base, capital structure or operating income before taxes.

As a result of staff's recommendations in previous issues, the appropriate income tax expense should be $107,436 for water and $(49,542) for wastewater, before any revenue increase.

ISSUE 52: What is the test year operating income before any revenue increase?

RECOMMENDATION: The appropriate amount of operating income before any revenue increase is $462,950 for water and $210,507 for wastewater. (MERCHANT)

POSITION OF THE PARTIES

GULF: Test year operating income is $384,977 for water and $97,152 for wastewater.

OPC: The test year operating income amounts are subject to the resolution of other issues.

STAFF ANALYSIS: Based on the adjustments discussed in previous issues, staff recommends that the test year operating income before any provision for increased (or decreased) revenues should be $462,950 for water and $210,507 for wastewater. This represents an achieved rate of return of 13.42% and 5.49% for water and wastewater, respectively. The schedules of operating income are attached as Schedules No. 3-A for water and 3-B for wastewater. The schedule of adjustments to operating income is attached as Schedule No. 3-C.

REVENUE REQUIREMENT

ISSUE 53: What is the appropriate revenue requirement?

RECOMMENDATION: The appropriate revenue requirements are as follows: (MERCHANT)

	Revenue Requirement	$ Increase/ Decrease	% Increase/ Decrease
Water	$ 2,051,191	$ (244,191)	-10.64%
Wastewater	$ 1,498,871	$ 194,141	14.88%

POSITION OF THE PARTIES

GULF: The appropriate revenue requirement is $2,282,299 for water and $1,705,800 for wastewater.

OPC: The revenue requirements are subject to the resolution of other issues.

STAFF ANALYSIS: The revenues required as a result of staff's analysis are $2,051,191 for water and $1,498,871 for wastewater. This will allow the utility the opportunity to recover its allowed level of expenses and to earn a 9.21% rate of return on its investment in rate base.

RATES AND CHARGES

ISSUE 54: Should the public fire protection charge be continued, and if so, what is the appropriate charge?

RECOMMENDATION: The public fire protection charge should be continued with no change to the current charge. (GALLOWAY)

POSITION OF THE PARTIES

GULF: The public fire protection charges should be continued, and should be set forth in Appendix B, page 4, note 7, attached hereto.

OPC: No Position.

STAFF ANALYSIS: The utility's tariff provides for a public fire protection charge of $55.00 per year per hydrant payable on a quarterly basis. An additional clause in the utility's tariff provides that:

> The Company will maintain the fire hydrant and will use diligence to see that pressure is maintained at each hydrant; however, the Company will not be responsible for any damage or liability caused by or attributed to low pressure in the lines or at the hydrant. This charge shall not apply where there is a maintenance contract satisfactory to the Company making the fire district responsible for the maintenance of fire hydrants. (EXH 20)

The public fire protection charge is in place to provide customers with the option of maintaining the fire hydrants through the utility or through another source. Mr. Bernard Kleinschmidt, witness for Staff, who is Deputy Chief for the Estero Fire Control and Rescue Service District testified that an agreement exists between Gulf and the fire district which places the responsibility of maintaining fire hydrants in the Estero fire district on the Estero fire district. (TR 420)

Mr. Kleinschmidt further testified that in order to maintain an ISO rating, which is a grading system used by insurance companies which rates fire departments throughout the U.S., the fire department must provide a maintenance program or contract an

outside agency. "In the past, maintenance programs have been cost prohibitive. It is because of this that most fire districts have chosen to provide the service in-house." (TR 420)

Mr. Thomas Beard, witness for staff, who is the fire inspector for the San Carlos Park Fire and Rescue Service District, provided similar testimony. Mr. Beard testifies that as the local fire official, he is responsible for testing the fire hydrants. When asked about whose responsibility it is to maintain the hydrants, Mr. Beard refers to the maintenance agreement between the utility company and the department indicating this responsibility is assumed by the department. (TR 387-388)

As indicated by Mr. Kleinschmidt's and Mr. Beard's testimony, most fire departments choose to provide their own "in-house" maintenance program for the fire hydrant's. Nevertheless, Section 367.081(2)(a) provides that the Commission shall set rates which are just, reasonable, compensatory and not unfairly discriminatory. Therefore, in setting the current charge, the Commission was required to consider the foregoing statutory criteria. Staff believes that the record supports that the current charge is just, reasonable, compensatory and not unfairly discriminatory. As such, staff believes that the current charge should remain in the utility's tariff. Further, staff believes that, should the situation ever arise where a fire department or another customer must depend on the utility for maintaining the fire hydrants in their district, a charge should be in place in the utility's tariff.

Staff is recommending that the public fire protection charge remain in the utility's tariff and remain unchanged.

ISSUE 55: Should the Commission determine a reuse rate in this proceeding, and if so, what is the appropriate rate?

RECOMMENDATION: Yes, the Commission should approve a reuse rate of zero for all existing reuse customers. Gulf should file a reuse tariff sheet listing reuse customers and reflecting the approved rate. Since this recommendation is based upon a combination of existing factors which are subject to change, Gulf should be placed on notice that this issue will be revisited in its next wastewater rate case. Also, any future reuse agreements should be filed with the Commission for approval of the rate contained therein along with justification for the proposed rate. (VON FOSSEN)

POSITION OF THE PARTIES

GULF: No reuse rate is appropriate because discharge by spray irrigation is part of Gulf's effluent disposal system, Gulf has no reasonable alternatives, and the golf courses receiving the effluent will not accept the effluent if a charge is imposed.

OPC: Yes. The reuse rate should be set at $.25 per 1,000 gallons during the dry months and a credit of $.05 per 1000 gallons should be given to the golf courses during the wet weather months.

STAFF ANALYSIS: Gulf presently provides reclaimed water to four golf courses/developments. Reuse is provided at no charge and the utility has no tariff provisions regarding reuse. Within its initial filing, Gulf did not specifically address any issues related to reuse other than to note that it was its sole source of effluent disposal. None of Gulf's witnesses addressed reuse in their direct testimony.

Staff offered the testimony of Edith Xanders of the PSC and Scott Burns, Director of Water Use with the SFWMD. While not recommending a specific charge, Staff Witness Xanders provided a range of factors to be considered in determining whether reuse rates should be approved, and if so, at what level. These factors include the utility's alternatives for effluent disposal, the customers' alternative water sources and the cost of these alternatives, the contents of the reuse agreements, reuse rates within the area and the utility's ability to secure additional customers. (TR 490) Witness Burns provided an overview of the district's rules and efforts to promote reuse. The District's water use permit rules require an applicant for a new permit, permit

renewal or permit modification to show that the applicant makes use of a reclaimed water source unless it demonstrates that its use is either not economically, environmentally or technically feasible. (TR 522,523) However, according to Witness Burns, the applicant's determination of feasibility is considered final, and the conclusions are not independently reviewed by District staff. (TR 524) In fact, the District does not have any standards to determine the economic feasibility of requiring golf courses to take reuse. (TR 532)

OPC provided the testimony of Ms. Kim Dismukes. She agreed that golf course irrigation is beneficial to Gulf and its customers but noted that it is also beneficial to the golf courses. She testified that since Gulf operates in a Water Resource Caution Area, the SFWMD closely monitors the need for water use permits and associated withdrawals. She notes that the District's water use permit rules require an applicant for a new permit, permit renewal or permit modification to show that the applicant makes use of a reclaimed water source unless the applicant, demonstrates that its use is either not economically, environmentally or technically feasible. (TR 294) She stated that since reuse is presently being provided to three golf courses and has a contract for the fourth, it is unlikely they could prove that the provision of reclaimed water is not technically or environmentally feasible. Further, she stated that the SFWMD should find that a reasonable rate for reclaimed water is economically feasible. (TR 295) Accordingly, she initially recommended a rate of $.25 per thousand gallons for reuse. (TR 295)

In rebuttal, Utility Witness Jim Moore, provided the utility's position on setting a rate for reuse. Gulf disposes 100% of its effluent through golf course irrigation. (TR 553) Presently Gulf has contractual agreements with four golf courses which allow it to dispose of effluent at no charge on those properties.(EX 31) With the exception of the 1996 River Ridge agreement, which will be separately discussed, all other agreements have been in place since the 1980's. According to Mr. Moore, the utility's position is that no charge is appropriate since the golf courses are not customers but, instead, an integral part of the wastewater treatment process. Through contracts with these properties, Gulf believes it has in place the lowest cost alternative to dispose of its effluent. These agreements provide that Gulf can dispose of all its effluent, even during the rainy season, with the golf courses being responsible for constructing both off-site and on-site lines and

providing effluent storage meeting DEP standards. Mr. Moore asserts that through this relationship with the golf courses, Gulf and its wastewater customers have avoided the cost of the portion of the reuse system paid for by the golf courses. Mr. Moore stated that Gulf believes that the cost of the reuse system should be considered solely as effluent disposal costs and included in the wastewater rates as would the effluent disposal costs of any other utility. (TR 553-555)

Mr. Moore stated that Gulf's main concern is the impact implementing a positive reuse charge would have on its present operations. Since existing reuse agreements provide for no charge for reuse, Gulf believes there is the possibility that it may be sued or that the golf courses may declare their reuse contracts void. (TR 559) According to Witness Moore, to avoid the expense, the existing reuse users would decrease their usage. Additionally, he testified that prospective customers would attempt to avoid accepting reuse or would limit contractually the amount they would accept. This would place Gulf in the position, on a daily basis, of being unable to dispose of its effluent in the quantities it has historically delivered to its present sites. This could lead to a temporary moratorium on new wastewater service and a need for Gulf to develop alternate methods of disposal.(TR 557, 559)

While the golf courses did not intervene in this docket, all four golf courses provided testimony during the customer service hearing. All of the golf courses presently taking reclaimed water from Gulf have no-charge contracts. (EX 31) They testified that they would modify the amount of water taken if a reuse charge were implemented. Specifically, two golf courses indicated that they would not take effluent in the wet season, when irrigation is not needed, if a charge were implemented.(TR 7,26,28,31,37,44) Additionally, the golf courses stated that consideration should be given for both the on-site and off-site investment they have made in order to accept reuse. For example in 1994, the San Carlos Golf Club (San Carlos)invested $140,000 to upgrade its effluent holding ponds in order to be able to accept reuse.(TR 16,17) The Vines Country Club (Vines) spent at least $100,000 to construct the effluent line from the utility to its holding ponds. (TR 26) The Country Creek Golf and Country Club (Country Creek) paid for the line from the utility to its holding pond and incurred significant expense in lining its holding ponds.(TR 34,35) They suggest that decisions to accept reuse and pay for the off-site lines and on-

site improvements were based upon reuse being provided at no charge.(TR 17,26,27,36)

In its brief, OPC responded to the testimony of the utility and golf courses. In response to the argument that reuse customers would cease or lessen their usage, OPC states that using fresh water, instead of reuse, would appear to cause two of the golf courses to exceed their present permitted withdrawals. (BR 61) Additionally, OPC argues that Gulf was unable to explain why other utilities in the area were able to charge for reuse and that reuse at $.25 per 1,000 gallons is reasonable compared to the $2.01 charge for potable water. (BR 63,61) This is the basis for OPC recommending a charge for reuse. However, in consideration of the utility's concern over wet weather storage and to offer an incentive for golf courses to take effluent during wet weather, OPC modified its original rate proposal to include a $.05 credit to the golf courses during the wet weather months of June through September. (BR 63,64)

Gulf is totally dependent upon the golf courses as its sole means of effluent disposal.(TR 553) The three golf courses presently receiving reuse all have active Water Use Permits allowing them to provide all or a portion of their irrigation needs through wells or surface withdrawals.(TR 555) Presently, with the addition of the River Ridge Property in late 1996, Gulf is able to utilize its plants at full capacity and dispose of all of its effluent.(TR 129,130) Therefore, the record indicates that Gulf has in place an effective means of effluent disposal. At issue is weighing the impact a charge for reuse would have on effluent disposal versus the benefit to the wastewater customers of the revenue derived from a positive reuse rate. The reuse customers have indicated that if a charge were imposed, they would cut back on their usage. While the reuse customers have alleged they would take reduced flows, a key point is whether through existing reuse contracts and the policy of the SFWMD, customers would be able to reduce flows.

Presently, Gulf has no-charge reuse agreements with the San Carlos, Country Creek and the Vines. All three agreements contain provisions relating to minimum and maximum amounts Gulf can dispose of on the respective properties. To receive reuse, all three properties have incurred expense in paying for off-site lines and designing effluent storage facilities meeting DEP standards. (TR

17,22,26,34,35, EX 2) Based upon this investment, staff believes it is unlikely that any of the golf courses would cease using reuse.

However, the possibility does exist that flows would be reduced. Since the above contracts have no contingency regarding a future charge, the golf courses could declare the existing agreements void and renegotiate minimum and maximum flows to limit their irrigation expense. However, to meet their irrigation needs, the golf courses may need to increase their fresh water withdrawals which would involve the SFWMD. Witness Dismukes stated that if SFWMD uses an objective measure of economic feasibility it should find that a reasonable reuse rate is economically feasible.(TR 295) However determination of economic feasibility is left to the applicant, not the District. According to Witness Burns of SFWMD, the applicant's determination of feasibility is considered final, and the conclusions are not independently reviewed by District staff. (TR 524) In fact, as mentioned, the District does not have any standards to determine the economic feasibility of requiring golf courses to take reuse.(TR 532) Therefore, staff is concerned that the golf courses have the ability to decrease their use of reclaimed water.

We believe we must recognize that golf courses are businesses and a charge for reuse creates an economic incentive to take less effluent. Based upon total irrigation needs and the limitation of present water use permits, it is not clear to what extent reuse consumption could be immediately decreased. However, Mr. Burns testified that the three existing permits are all up for renewal in December of 1997.(TR 526) At that time, it would appear the golf courses could make their own determination that reuse was not economically feasible for all or a portion of their present usage and be able to increase their fresh water withdrawals. Such a decision could have a serious impact on Gulf's ability to dispose of its effluent.

Gulf's fourth and most recent reuse agreement is with the River Ridge development. This agreement was executed in 1996 and provides that the utility may ultimately dispose of up to 1.5 million gallons per day of effluent.(EX 31) River Ridge has applied for a water use permit which is presently under review by The SFWMD. (TR 526) As with the other agreements reuse is to be provided at no charge. However, this agreement differs from the other reuse agreements in that it specifies there may be a future charge for reuse and the utility, not the customer, paid for the

line to bring effluent to the development.(EX 31) Gulf has stated that it was "up against the wall" for immediate additional disposal capacity and constructed the line to achieve that goal. (TR 632) Since the River Ridge property will not be developed for at least a year, it did not need effluent for irrigation. (TR 623) Pursuant to the agreement, Gulf constructed the effluent line and River Ridge constructed holding ponds, prior to development, to accept the effluent. This is a temporary holding area until the development is complete and lines are constructed to irrigate the golf course. (TR 622,623,632) Therefore, River Ridge is presently receiving and storing effluent, but not using it for irrigation. (TR 622,890) Since the benefit of reuse to the property is irrigation, River Ridge is in effect a disposal site at this time. As with pricing effluent in wet weather when it is not needed by the golf courses, staff believes a positive charge at this time would create a disincentive to accept reuse.

First and foremost, Gulf is a water and wastewater utility. Therefore, staff believes it is important to note that care must be taken that a recommendation to establish a reuse rate does not negatively effect the primary operation of the utility. In determining whether a reuse rate should be implemented in this docket, staff believes a primary factor to consider is the impact a rate would have on the ability of the utility to dispose of its present and future effluent. Since Gulf has no alternative means of effluent disposal, it is dependent upon a cooperative relationship with neighboring golf courses. As noted by the utility, prior to the River Ridge agreement, it was unable to operate its Three Oak plant at full capacity due to limited disposal capacity. (TR 622) The River Ridge agreement was needed to dispose of incremental flows which could not be taken at the other sites. Therefore, staff infers that existing sites are at their permitted capacity. Due to anticipated customer growth, Gulf continues to look for additional sites.(TR 622-623) As previously discussed, based upon present SFWMD rules as well as the testimony of Witness Burns, both existing and future reuse sites may unilaterally determine if reuse is economically feasible. If a positive rate is approved in this docket, any existing reuse customer could budget the amount they would pay and limit their usage because of that economic constraint or choose not to take reuse. Due to the dependency of the utility on reuse and the ability of reuse users to limit their usage, staff believes the potential negative impact of a reuse rate on Gulf's ability to dispose of its effluent outweighs the benefit to the

wastewater customers of shifting some of the reuse costs to the end users.

While the reuse revenue would lessen wastewater rates, we believe that wastewater customers will and have been the beneficiary of decreased wastewater disposal costs. Through its relationship with the golf courses, Gulf has not incurred the cost of land or construction of its own storage facilities and has been able to utilize transmission mains, storage facilities and irrigation systems paid for by the golf courses. Through its existing agreements, Gulf has been able to dispose of all of its effluent even during the wet season. Due to problems disposing of its effluent in wet weather, Lee County, as a safety valve, has an agreement where it will pay a neighboring utility to take its effluent.(EX 27) Witness Burns, Director of Water Use with SFWMD has stated that it has been his experience, across his district, that golf courses will utilize their wells if the cost of effluent exceeds the cost of using their wells. (TR 534,535) Absent tighter SFWMD guidelines which would require reuse be used and strictly limit fresh water irrigation, staff recommends a zero rate be approved.

Gulf should file a reuse tariff sheet listing customers served and indicating the zero rate. As stated by Witness Xanders, a zero rate in the tariff will show that the Commission has considered this issue and approved a zero rate.(TR 502) Since this recommendation is based upon a combination of existing factors which are subject to change, Gulf should be placed on notice that this issue will be revisited in its next wastewater rate case. Also, any future reuse agreements should be filed with the Commission for approval of the rate contained therein along with justification for the proposed rate.

ISSUE 56: In light of Section 367.0817, Florida Statutes, should any of the revenue requirement associated with reuse be allocated to water customers and recovered through water rates?

RECOMMENDATION: No. No portion of the reuse revenue requirement should be allocated to water customers and recovered through water rates at this time. (VON FOSSEN)

POSITION OF THE PARTIES

GULF: Gulf does not believe that a reuse rate should be set, but if one is established, it should be allocated to the water customers pursuant to 367.0817.

OPC: No position.

STAFF ANALYSIS: Section 367.0817(3), Florida Statutes, states in part:

> All prudent costs of a reuse project shall be recovered in rates. The Legislature finds that reuse benefits water, wastewater, and reuse customers. The Commission shall allow a utility to recover the costs of a reuse project from the utility's water, wastewater, or reuse customers or any combination thereof as deemed appropriate by the Commission. (TR 493)

This legislation acknowledges that water customers benefit from the water resource protection afforded by reuse and gives the Commission latitude to consider whether a portion of the cost of reuse should be borne by water customers. On rebuttal, Gulf Witness James Moore agreed that every water user which uses the aquifer benefits by reuse. (TR 628)

Staff Witness Xanders provided the only testimony directly related to this issue. She notes that quantifying the benefits to water customers is a judgement call. (TR 498) However, in attempting to quantify reuse benefits, the Commission can consider the additional cost to implement reuse over alternative methods of disposal. Since the lower cost alternative could provide adequate effluent disposal, the additional cost of reuse could be identified as costs incurred for conservation and protection of the water supply and recovered, in part, through water rates. (TR 496) Also, the Commission can consider cost avoidance by water customers due

to reuse. For example, if using reuse should reduce the demand for potable water, water facilities may not need to be expanded and this cost could be avoided. (TR 496) Specific to Gulf, its Corkscrew Water Treatment Plant is a low pressure membrane treatment facility which must dispose of concentrate created in the treatment process. Presently, the concentrate is blended with effluent from Gulf's Three Oaks Wastewater plant and sprayed on the golf courses. By being able to dispose of this reject water, Gulf has been able to avoid the cost of a $2.5 million deep well.(TR 497) Obviously this is to the economic benefit of the water customers.

These are generic methods which may be used to quantify the benefits of reuse to water customers, however, none appear to be applicable to Gulf. Gulf has disposed of all its effluent through reuse since 1982. It is its only method of effluent disposal.(TR 489,554) The record supports that reuse is the lowest cost disposal alternative. (TR 553) Therefore, there is no additional cost which could be considered solely for resource protection. Regarding cost avoidance, since none of the golf courses use potable water from Gulf which would be replaced by reuse, reuse would not decrease demand to Gulf's water system. Also, it appears that the cost of the deep well is being delayed as opposed to being avoided. Mr. Moore testified that there is little doubt that the deep well will be required, probably at the time the plant is next expanded, which could be as early as 1997. (TR 85,143) Also, it is not clear at this time if the deep well would be used only for reject water or if it could be dual permitted to also accept effluent. (Tr 629,630) Staff believes that it would not be appropriate to increase water rates based upon this avoided cost when water customers may be solely responsible for the cost of the deep well in the near future.

However, the fact remains when reuse is used to fill the irrigation needs of golf courses, water customers benefit because the use of reclaimed water helps to preserve ground water supplies for potable water needs. (TR 493) Witness Xanders testified that if reuse is the only disposal alternative or the Commission is unable to precisely quantify benefits, these factors should not be an obstacle to allocating some reuse cost to water customers. Absent specific quantification, this allocation becomes a judgement call. (TR 498) This judgement can be guided by additional criteria which include the average usage of water customers, the level of water rates, the magnitude of the water and wastewater increases, and the

need to send a stronger price signal to achieve water conservation. (TR 497,498) Through this criteria, the latitude to allocate reuse costs to water customers provides the Commission additional regulatory tools.

Allocation to water customers can help promote reuse. For example, if the result of implementing a reuse system were to result in extremely high wastewater rates, the Commission now has the latitude to mitigate this increase through a cost allocation to water customers. On the other hand, if a utility providing reuse were to have low water rates and corresponding high usage, the Commission can allocate a portion of the reuse costs to water, increasing the water rate as an additional conservation measure. Addressing other goals lessens the need for precise quantification of benefits.

Since the magnitude of the wastewater increase is moderate and water rates are decreasing slightly, we don't believe there is a need for a stronger conservation signal. Average monthly residential usage is approximately 7,000 gallons and even with the decrease the water gallonage charge is still approximately $2.00. (EX 8) While, undeniably there exist benefits to the water customers, we recognize that clear standards have not been established to recognize these benefits. Therefore, conclusions reached on similar criteria may differ as experience is gained through different cases. In this docket, staff does not believe that the evidence supports a compelling reason to merit a "pure judgement" allocation to water customers. Therefore, we recommend that no portion of the reuse revenue requirement be allocated to water customers and recovered through water rates at this time.

ISSUE 57: What is the appropriate master meter influent service rate?

RECOMMENDATION: The appropriate master meter influent service rate is the base facility charge associated with the related meter size along with a gallonage charge of $4.39/1,000 gallons. (GALLOWAY)

POSITION OF THE PARTIES

GULF: The appropriate master meter influent service rate is a gallonage charge of 5.29/mgd plus a base facility charge based on the size of the meter.

OPC: No Position.

STAFF ANALYSIS: Consistent with Commission Order No. 21450, issued on June 26, 1989 in Cocket No. 890110-SU, staff believes that an excess influent consumption charge is appropriate for those master metered wastewater customers whose wastewater flows exceed the customer's water flows. According to this Order and testimony provided by Mr. Moore, two customers in the utility's service area are affected by the master meter influent service rate. These customers are Coach Light Manor and Mariner's Cove, both mobile home parks. (T. 121-122)

Mr. Moore testified that the excessive infiltration situation described in PSC Order No. 21450 will exist as long as no further repairs to the system are made. Mr. Moore testified that, to his knowledge, no repairs have been made to either mobile home park since the issuance of Order No. 21450. (T. 121) Based on testimony provided, Staff believes that an infiltration problem still exists for these two master-metered wastewater customers, resulting in the need for continuing the master meter influent service rate.

Pursuant to Order No. 21450, the gallonage charge was calculated for the master metered wastewater customers at 4% above the gallonage charge for general service customers. Further, pursuant to this Order, the total charge for these customers consisted of a gallonage charge (as stated above) per 1,000 gallons of influent for all wastewater flows, in addition to the existing base facility charge. This methodology and these charges are described on page 3 of PSC Order No. 21450.

Further, Staff believes that the appropriate base facility charge related to the customer's meter size along with a gallonage charge rate four percent above the general service wastewater gallonage rate will insure equitable treatment of all wastewater customers in the system. No testimony was presented to the contrary. In consideration of the foregoing, staff recommends that the gallonage charge should be $4.39 per 1,000 gallons as found on Schedule No. 4B, for the master meter influent customers.

ISSUE 58: What are the appropriate water and wastewater rates?

RECOMMENDATION: Consistent with staff's recommendations in Issues 53, 55, and staff's recommendation in Issue 57, the recommended rates should be designed to allow the utility the opportunity to generate annual operating water revenues in the amount of $2,016,390 and annual operating wastewater revenues in the amount of $1,498,871, both of which exclude miscellaneous revenues. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Section 25-30.475(1), Florida Administrative Code, provided the customers have received notice. The rates should not be implemented until proper notice has been received by the customers. The utility should provide proof to staff of the date notice was given within 10 days after the date of notice. (GALLOWAY)

POSITION OF THE PARTIES

GULF: The appropriate water and wastewater rates are those as set forth in the MFRs.

OPC: The final rates are dependent upon the resolution of other issues.

STAFF ANALYSIS: The company requested permanent rates designed to produce water revenues of $2,139,422 and wastewater revenues of $1,671,070. According to the utility's MFRs, the requested revenues represent a decrease in water revenues of $155,935 or 6.79% and an increase in wastewater revenues of $366,340 or 28.07%. However, in accordance with Issues 53, 55, and 57, staff is recommending that the rates be designed to recover annual operating water revenues of $2,016,390 and annual operating wastewater revenues of $1,498,871.

While the allocation of revenue requirement was not at issue in this case, Ms. Andrews, a utility witness, states that an allocation was assigned based on number of customers served. (TR 212) Staff believes that a more accurate method of allocation should be used when designing rates. Therefore, the recommended rates were allocated consistent with Commission practice based on a fixed cost vs. variable cost basis.

When calculating the base facility and gallonage charges, Staff must consider the portion of the revenue requirement which is

to be recovered through service rates. Miscellaneous revenues along with guaranteed revenues and reuse revenues are generated through sources other than the service rates. Therefore, when calculating base facility and gallonage charges, miscellaneous revenues along with guaranteed revenues and reuse revenues are excluded from the revenue requirement so that the utility is not collecting these revenues twice. For this utility, only miscellaneous revenues are excluded from the revenue requirement since no guaranteed revenues or reuse revenues apply.

Further, for this utility, the miscellaneous revenues, in their entirety are excluded from the water revenues only rather than from both water and wastewater revenues. (EXH. 8) Therefore, while the water revenue requirement is $2,051,191, the rates are designed to allow the utility the opportunity to recover $2,016,390, which is a reduction to the revenue requirement of $34,800, the amount of miscellaneous revenues.

As stated in Issue 31, the utility's tariff provides that whenever both water and sewer service are provided, only a single charge is appropriate unless circumstances beyond the control of the Company require multiple actions. (EXH. 20) The miscellaneous revenues were included in total by the utility as water miscellaneous revenues. It has been Commission practice to allow a utility to record miscellaneous revenues in this way when water and wastewater miscellaneous charges exist.

Consistent with the utility's request, Staff recommends a 20% differential between the residential and general service wastewater gallonage charges. (EXH. 8) The purpose of the 20% differential in the wastewater gallonage charge between residential and general service customers recognizes that approximately 20% of the water used by residential customers is used for purposes such as irrigation and is not collected by the wastewater systems.

The utility should be required to file revised tariff sheets and a proposed customer notice to reflect the appropriate rates pursuant to Rule 25-22.0407(10), Florida Administrative Code. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code, provided the customers have received notice. The rates should not be implemented until proper notice has been received by the customers. The utility should

provide proof of the date notice was given within 10 days after the date of the notice.

A comparison of the utility's water and wastewater rates prior to filing, Commission approved interim rates, Gulf's requested final rates, and Staff's recommended final rates are shown on Schedule No. 4-A and 4B.

ISSUE 59: What is the appropriate amount by which rates should be reduced four years after the established effective date to reflect the removal of the amortized rate case expense as required by Section 367.0816, Florida Statutes?

RECOMMENDATION: The water and wastewater rates should be reduced as shown on Schedule No. 5-A and 5-B, to remove rate case expense in the amount of $145,200 and $71,548, respectively, grossed-up for regulatory assessment fees and amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the four-year recovery period, pursuant to Section 367.0816, Florida Statutes. The utility should be required to file revised tariff sheets and a proposed customer notice setting forth the lower rates and the reason for the reduction not later than one month prior to the actual date of the required rate reduction. (GALLOWAY)

POSITION OF PARTIES

GULF: The appropriate amount by which rates should be reduced four years after the established effective date to reflect the removal of the amortized rate case expense is one quarter of the approved rate case expense.

OPC: No position.

STAFF ANALYSIS: Section 367.0816, Florida Statutes, requires that the rates be reduced immediately following the expiration of the four-year period by the amount of rate case expense previously authorized in the rates. The reduction will reflect the removal of water and wastewater revenues associated with the amortization of rate case expense and the gross-up for regulatory assessment fees which is $145,200 and $71,548. The removal of rate case expense will reduce rates as recommended by staff on Schedule No. 5-A and 5-B.

The utility should be required to file revised tariffs no later than one month prior to the actual date of the required rate reduction. The utility also should be required to file a proposed customer notice setting forth the lower rates and reason for the reduction.

If the utility files this reduction in conjunction with a price index or pass-through rate adjustment, separate data shall be

filed for the price index and/or pass-through increase or decrease, and for the reduction in the rates due to the removal of the amortized rate case expense.

ISSUE 60: What are the appropriate amounts of refunds, if any, for water revenues held subject to refund and the interim wastewater increase?

RECOMMENDATION: The utility should be required to refund 12.30% of the water revenues held subject to refund from April 11, 1996, to November 1, 1996, the date of the interim rate reduction. From November 1, 1996, to the effective date of the final rate, Gulf should refund 4.70% of the water revenues held subject to refund for the period subsequent to the interim rate reduction. No refund is necessary for wastewater. The refund should be made with interest in accordance with Rule 25-30.360(4), FAC. The utility should be required to submit the proper refund reports pursuant to Rule 25-30.360(7), FAC. The utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), FAC. (MERCHANT)

POSITION OF PARTIES:

GULF: No refunds are necessary.

OPC: Based upon Gulf's revenue requirement (Issue 53) and water and wastewater rates and charges approved on this case (Issue 54-58), no refunds are necessary.

STAFF ANALYSIS: As addressed in Issue A, Stipulation 12, all parties and staff agreed that for both water and wastewater refund purposes, the final revenue requirements should be adjusted to remove any ratemaking components which were not in service or not incurred during the time interim rates were in effect. These adjusted revenue requirements should be compared to the adjusted test year revenues to determine whether any refund should be ordered. The water test year revenues should be annualized for the two time periods using the rates prior to the water interim rate reduction and the rates subsequent to the water interim rate reduction.

By Order No. PSC-96-0501-FOF-WS, issued April 11, 1996, the Commission initiated an overearnings investigation and held $353,492 or 16.92 percent in annual water revenues subject to refund. Pending the resolution of the investigation, Gulf Utility was ordered to undertake a surety bond, letter of credit or escrow agreement in the amount of $179,203, which represents a six-month

time frame, plus interest. Also, by that order, the overearnings investigation was combined with this current rate proceeding.

In this application, Gulf requested interim and final revenue decreases of $141,709 (6.67%) and $155,935 (6.79%), respectively, for the water system. For wastewater, Gulf requested interim and final wastewater increases of $256,885 (22.98%) and $366,340 (28.08%), respectively. (EXH 8) Staff witness Rendell testified that the utility did not request interim water rates, but instead requested that its proposed final rates be effective simultaneously with its proposed interim wastewater rates. (TR 377)

By Order No. PSC-96-1310-FOF-WS, issued on October 28, 1996, the Commission approved an interim wastewater rate increase and water rate reduction, with additional water revenues held subject to refund. For wastewater, the Commission approved a revenue requirement of $1,288,391 for interim purposes. This resulted in an annual increase of $170,821 or 15.29%. For the water system, the Commission calculated an interim revenue requirement of $1,796,651, which resulted in decreased revenues of $329,920 or a negative 15.51%. The Commission determined that it could not make a final determination regarding the potential overearnings of the water system at the time of interim. Therefore, the Commission approved the company's proposed final rates, which generated annual revenues of $1,982,871 on an interim basis, pending the determination of the appropriate final water rates in this case. The difference between the annual revenue reduction implemented by the utility ($1,982,871) and the interim revenue requirement determined by the Commission ($1,796,651) is $186,220, and this was the amount held subject to refund. This equated to 9.39% of the revenues collected during the interim period to be held subject to refund. Mr. Rendell testified that the tariff sheets containing the interim water and wastewater rates were approved on November 1, 1996. (TR 377-378)

Mr. Rendell testified that water revenues should be annualized for both periods reflecting the different rates that were in effect. For the first period, April 11, 1996 through November 1, 1996, the revenue should be calculated based upon the appropriate billing determinants for the projected 1996 test year at the rates in effect as of October 31, 1996. For the second period, November 1, 1996, through the effective date of the final rates, the revenue should be calculated based upon the appropriate billing determinants for the 1996 projected test year at the lower water

rates as of November 1, 1996. (TR 378) Since no parties have disputed this methodology, staff has accordingly calculated $2,221,539 in annualized water revenues for the first period. For the second period, staff has calculated $2,071,243 in annualized revenues. To be consistent, staff has also recalculated the wastewater interim revenues using the projected test year billing determinants. This results in annualized revenues for wastewater of $1,442,084.

Additionally, Mr. Rendell testified that adjustments made in the rate case test period that do not relate to the period that interim rates were in effect should be removed. Mr. Rendell testified that examples of such adjustments would be plant in service which was not in service during the interim collection period but will be in service after the final rates go into effect and expenses which will be recovered only after final rates are established, such as rate case expense, should also be removed. Mr. Rendell further testified that after these items are removed, staff should then calculate a revised revenue requirement for the interim period using the same data used to establish final rates. (TR 379) Since this was also stipulated by the parties, staff agrees that this methodology should also be applied.

To establish the proper refund amount, staff has calculated a revised interim revenue requirement utilizing the same data used to establish final rates. Rate case expense was excluded, because it was not an actual expense during the interim collection period. Based on the record, staff believes that there are no other items that should be removed to determine the revised revenue requirement for refund purposes. Accordingly, staff has calculated the revised revenue requirement for the interim collection period to be $2,013,093 for water and $1,480,228 for wastewater.

As shown below, the annualized water revenue requirements for both the first and second interim periods exceed the adjusted final revenue requirement for water. In order to determine the appropriate refund percent, miscellaneous revenues have been excluded. Therefore, staff recommends refund percentages for water of 12.30% for the period prior to the interim decrease and 4.70% for the period subsequent to the interim decrease. Compared to the restated interim revenue requirement, the revised revenue requirement for wastewater exceeds interim revenues and no wastewater refund is necessary.

		Water		Wastewater
		Pre-interim	Interim	Interim
1	Adj. Final Rev. Req.	$2,013,093	$ 2,013,093	$1,480,228
2	Less: Misc. Revenues	$ 0	$ -34,800	$ 0
3	Revenues- Serv. Rates	$ 1,978,293	$ 1,978,293	$1,480,228
4	Restated Annualized Interim Revenues	$ 2,221,539	$ 2,071,243	$1,442,084
5	Refund Amt. (ln 3-4)	**$ 243,246**	**$ 95,950**	**$ -38,144**
6	Refund Percentage	**12.30%**	**4.70%**	**0.00%**

Section 367.082(4), Florida Statutes, states that refunds shall not be in excess of the amounts held subject to refund. The refund amounts above are less than the amounts held subject to refund; therefore, no limitation is necessary and the full percentages should be made. As shown in the above schedule, for the period April 11, 1996, to October 31, 1996, the utility should be required to refund 12.30% of the water revenues collected during this time frame. From November 1, 1996, the utility should be required to refund 4.70% of the water revenues collected during this time frame until the effective date of the final water rates. The refunds should be made with interest as required Section 25-30.360(4), FAC. Further, staff is recommending that the utility be required to submit the proper refund reports pursuant to Rule 25-30.360(7), FAC. Also, the utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), FAC.

ISSUE 61: Should the utility's tariff filing to modify its service availability charges be approved as filed?

RECOMMENDATION: Yes. The utility should be allowed to implement plant capacity charges of $550.00 per ERC for the water system and $800.00 per ERC for the wastewater system, for connections made after the stamped approval date of the tariff sheets pursuant to Rule 25-30.475(2), Florida Administrative Code. (GALLOWAY)

POSITION OF THE PARTIES

GULF: Gulf's request to modify its service availability charges should be approved as filed.

OPC: No position.

STAFF ANALYSIS: Pursuant to Section 367.101, Florida Statutes, the Commission shall set just and reasonable charges and conditions for service availability. The utility requested that the plant capacity charges for the water system be reduced from $800.00 to $550.00 per ERC and that the plant capacity charges for the wastewater system be increased from $550.00 to $800.00 per ERC. By Order No. PSC-96-1310-FOF-WS, issued October 28, 1996, the Commission suspended the utility's proposed service availability charges.

Staff's analysis of the utility's contribution level reveals that the utility is currently within the minimum and maximum level as required by Rule 25-30.580 (1)(a) & (b), Florida Administrative Code and this rule states:

> (a) The maximum amount of contributions-in-aid-of-construction, net of amortization, should not exceed 75% of the total original cost, net of accumulated depreciation, of the utility's's facilities and plant when the facilities and plant are at their designed capacity; and (b) the minimum amount of contributions-in-aid-of-construction should not be less than the percentage of such facilities and plant that is represented by the water transmission and distribution and sewage collection systems.

Based on historical data provided in the utility's application, Staff calculated the water system's average growth to

be 430 connections per year and the wastewater system's average growth to be 495 connections per year. Consistent with Issue No. 6, Staff considered FGCU as part of the utility's growth. If this growth continues, the water plant will reach full capacity in approximately 11 years while the wastewater plant will reach full capacity in approximately 4 years.

From the information provided in this application, Staff agrees with the utility's calculations regarding the plant capacity charges. Staff recommends decreasing the plant capacity charge for the water system from $800 per ERC to $550 per ERC. Staff also recommends increasing the plant capacity charge for the wastewater system from $550 per ERC to $800 per ERC.

Schedules 6-A and 6-B have been prepared and are attached illustrating the basis for Staff's recommendation that a plant capacity charge for the water and wastewater system in the amount of $550 and $800, respectively, is appropriate. Based on the foregoing, Staff recommends that the plant capacity charge for the water system be decreased to $550 and the plant capacity charge for the wastewater system be increased to $800.

ISSUE 62: What is the appropriate Allowance for Funds Used During Construction (AFUDC) rate?

RECOMMENDATION: The appropriate AFUDC rate should be 9.21%, or 0.766839% on a monthly discounted basis. The charge should be effective for plant construction recorded on or after January 1, 1997.

POSITION OF THE PARTIES

GULF: The appropriate AFUDC rate is 9.25%.

OPC: (OPC did not provide a position on this issue.)

STAFF ANALYSIS: As previously addressed in Issue A, in Stipulation 13, the parties and staff have all agreed that the appropriate AFUDC rate should be based on the rate of return found to be fair and reasonable by the Commission, and pursuant to Rule 25-30.116, FAC. Further, the rate should be effective January 1, 1997. In Issue 29, staff recommended that the overall cost of capital should be 9.21%. Applying the above mentioned rule, the monthly discounted rate should be 0.766839%.

ISSUE 63: Should the special service availability agreement dated December 12, 1996 between Gulf and the Board of Trustees of the Internal Improvement Trust Fund of the State of Florida (FGCU) be approved as filed?

RECOMMENDATION: Yes, the special service availability agreement dated December 12, 1996 between Gulf and the Board of Trustees of the Internal Improvement Trust Fund of the State of Florida (FGCU) should be approved as filed. (GALLOWAY)

POSITION OF THE PARTIES

GULF: The special service availability agreement dated December 12, 1996 between Gulf and the Board of Trustees of the Internal Improvement Trust Funds of the State of Florida (FGCU) should be approved as filed.

OPC: No Position.

STAFF ANALYSIS: When the utility filed their application for this proceeding and a docket was opened, included in the filing were costs, expenses and revenues related to FGCU. However, no signed agreement existed between the utility and the university. Staff believed that, at a minimum, to give FGCU consideration in this docket, the special service availability agreement should be signed and filed with the Commission. Therefore, Staff included this issue.

Mr. Moore's supplemental direct testimony included the special service availability agreement. This exhibit was entered into the record as Exhibit 4. Also, in response to Staff's POD request, the utility filed with the Commission a signed copy of the aforementioned special service availability agreement.

Upon review of the special service availability agreement, Staff finds that the document is in compliance with the utility's tariff and with Commission rules. Staff is recommending that the agreement be approved as filed.

ISSUE 64: Should the docket be closed?

RECOMMENDATION: Yes. This docket should be closed after the time for filing an appeal has run, upon staff's verification that the utility has completed the required refunds with interest and the proper revised tariff sheets and customer notice have been filed by the utility and approved by staff. Further, the utility's escrow account can be closed upon staff's verification that the refund has been completed. (GALLOWAY, PARKER)

STAFF ANALYSIS: Yes, the docket should be closed 32 days after issuance of the order, to allow time for filing an appeal to run, upon staff's verification that the utility has completed the required refunds with interest and the proper revised tariff sheets and customer notice have been filed by the utility and approved by staff. Further, the utility's escrow account can be closed upon staff's verification that the refund has been completed.

GULF UTILITY COMPANY
SCHEDULE OF WATER RATE BASE
TEST YEAR ENDED 12/31/96

SCHEDULE NO. 1-A
DOCKET 960329-WS

1	UTILITY PLANT IN SERVICE	$16,700,337	$1,794,445	$18,494,782	($700,000)	$17,794,782
2	LAND & LAND RIGHTS	$200,372	$0	$200,372	$0	$200,372
3	NON-USED & USEFUL COMPONENT	($193,954)	($881,535)	($1,075,489)	$187,475	($888,014)
4	ACCUMULATED DEPRECIATION	($4,173,672)	($93,220)	($4,266,892)	($23,103)	($4,289,995)
5	CIAC	($12,220,685)	$0	($12,220,685)	($277,199)	($12,497,884)
6	AMORTIZATION OF CIAC	$2,942,325	$0	$2,942,325	($101,637)	$2,840,688
7	ADVANCES FOR CONSTRUCTION	($4,885)	$0	($4,885)	$0	($4,885)
8	WORKING CAPITAL ALLOWANCE	$358,144	$0	$358,144	($64,179)	$293,965
9	RATE BASE	$3,607,982	$819,690	$4,427,672	($978,643)	$3,449,029

GULF UTILITY COMPANY
SCHEDULE OF WASTEWATER RATE BASE
TEST YEAR ENDED 12/31/96

SCHEDULE NO. 1-B
DOCKET 960329-WS

1 UTILITY PLANT IN SERVICE	$14,282,349	$0	$14,282,349	($2,265)	$14,280,084
2 LAND	$473,626	$0	$473,626	$0	$473,626
3 NON-USED & USEFUL COMPONENT	$0	$0	$0	($527,582)	($527,582)
4 ACCUMULATED DEPRECIATION	($2,978,837)	$0	($2,978,837)	($21,385)	($3,000,222)
5 CIAC	($9,060,383)	$0	($9,060,383)	($717,584)	($9,777,967)
6 AMORTIZATION OF CIAC	$1,976,074	$0	$1,976,074	($74,151)	$1,901,923
8 ADVANCES FOR CONSTRUCTION	$0	$0	$0	$0	$0
11 WORKING CAPITAL ALLOWANCE	$235,467	$0	$235,467	($42,579)	$192,888
RATE BASE	$4,928,298	$0	$4,928,298	($1,385,546)	$3,542,750

GULF UTILITY COMPANY
ADJUSTMENTS TO RATE BASE
TEST YEAR ENDED 12/31/96

SCHED. NO. 1-C
DOCKET 960329-WS

PLANT IN SERVICE		
1 To remove the projected cost of the reject holding tank	($700,000)	$0
2 To correct transposition error to wastewater plant in rate base (Stip #1)	0	(2,265)
Total	($700,000)	($2,265)
NON-USED AND USEFUL		
To reflect net non-used and useful adjustment	$187,475	($527,582)
ACCUMULATED DEPRECIATION		
1 To remove the projected cost of the reject holding tank	$21,313	$0
2 Correct error to test year depreciation rate used	(44,416)	(21,385)
Total	($23,103)	($21,385)
CIAC		
1 CIAC for lines which should have been contributed by Caloosa Group	($68,114)	($92,815)
2 Reflect prepaid and/or impute CIAC on the margin reserve	(193,700)	(594,000)
3 Impute CIAC for grant from SFWMD (Stip #15)	(15,385)	(30,769)
Total	($277,199)	($717,584)
ACCUM. AMORT. OF CIAC		
1 CIAC for lines which should have been contributed by Caloosa Group	$10,855	$14,145
2 Reflect prepaid CIAC on the margin reserve	2,737	9,924
3 Impute CIAC for grant from SFWMD (Stip #15)	142	236
4 To decrease for utility's use of a composite rate on total CIAC amort.	(115,371)	(98,456)
Total	($101,637)	($74,151)
WORKING CAPITAL		
To reflect 13-month average adjusted working capital using the balance sheet approach.	($84,179)	($42,579)

GULF UTILITY COMPANY
CAPITAL STRUCTURE
TEST YEAR ENDED 12/31/96

SCHEDULE NO. 2
DOCKET 960329-WS

PER UTILITY 1996 - YEAR-END								
1	LONG TERM DEBT	$8,668,424	$0	($1,673,070)	$8,995,354	74.77%	10.63%	7.95%
2	SHORT-TERM DEBT	$75,360	$0	($14,969)	$60,391	0.65%	11.01%	0.07%
3	PREFERRED STOCK	$0	$0	$0	$0	0.00%	0.00%	0.00%
4	COMMON EQUITY	$1,077,293	$0	($208,021)	$869,272	9.29%	11.88%	1.10%
5	CUSTOMER DEPOSITS	$205,735	$0	$0	$205,735	2.20%	6.00%	0.13%
6	DEFERRED INCOME TAXES	$1,517,923	$0	($292,707)	$1,225,216	13.10%	0.00%	0.00%
7	DEFERRED ITC'S-ZERO COST	$0	$0	$0	$0	0.00%	0.00%	0.00%
8	DEFERRED ITC'S-WTD. COST	$0	$0	$0	$0	0.00%	0.00%	0.00%
9	OTHER	$0	$0	$0	$0	0.00%	0.00%	0.00%
10	TOTAL CAPITAL	$11,544,735	$0	($2,188,767)	$9,355,968	100.00%		9.25%
PER COMMISSION 1996 - 13-MONTH AVERAGE								
11	LONG TERM DEBT	$8,668,424	$0	($3,405,950)	$5,262,474	75.36%	10.63%	6.01%
12	SHORT-TERM DEBT	$75,360	$0	($29,610)	$45,750	0.66%	11.01%	0.07%
13	PREFERRED STOCK	$0	$0	$0	$0	0.00%	0.00%	0.00%
14	COMMON EQUITY	$1,077,293	($160,929)	($360,053)	$556,311	7.97%	11.88%	0.95%
15	CUSTOMER DEPOSITS	$205,735	$0	$0	$205,735	2.95%	6.00%	0.18%
16	DEFERRED INCOME TAXES	$1,517,923	$0	($605,126)	$912,797	13.07%	0.00%	0.00%
17	DEFERRED ITC'S-ZERO COST	$0	$0	$0	$0	0.00%	0.00%	0.00%
18	DEFERRED ITC'S-WTD. COST	$0	$0	$0	$0	0.00%	0.00%	0.00%
19	OTHER	$0	$0	$0	$0	0.00%	0.00%	0.00%
17	TOTAL CAPITAL	$11,544,735	($160,929)	($4,392,026)	$6,983,068	100.00%		9.21%

Staff Specific Adjustments

A) Reduce equity for lines which should have been contributed by Caloosa.

	LOW	HIGH
RETURN ON EQUITY	10.88%	12.88%
OVERALL RATE OF RETURN	9.13%	9.29%

GULF UTILITY COMPANY
STATEMENT OF WATER OPERATIONS
TEST YEAR ENDED 12/31/96

SCHEDULE NO. 3-A
DOCKET 960329-WS

1	OPERATING REVENUES	2,295,357	(155,935)	$2,139,422	$155,935	$2,295,357	($244,166) -10.64%	$2,051,191
	OPERATING EXPENSES:							
2	OPERATION AND MAINTENANCE	1,307,395	0	1,307,395	(34,995)	1,272,400		1,272,400
3	DEPRECIATION	165,417	0	165,417	59,268	224,685		224,685
4	AMORTIZATION	6,977	0	6,977	0	6,977		6,977
5	TAXES OTHER THAN INCOME	227,672	(7,017)	220,655	255	220,910	(10,987)	209,922
6	INCOME TAXES	0	29,383	$29,383	$78,053	$107,436	($87,745)	$19,690
7	TOTAL OPERATING EXPENSES	1,707,461	22,366	$1,729,827	$102,580	$1,832,407	($98,733)	$1,733,674
8	OPERATING INCOME	$587,896	($178,301)	$409,595	$53,355	$462,950	($145,434)	$317,516
9	RATE BASE	$3,607,982		$4,427,672		$3,449,029		$3,449,029
10	RATE OF RETURN	16.29%		9.25%		13.42%		9.21%

GULF UTILITY COMPANY
STATEMENT OF WASTEWATER OPERATIONS
TEST YEAR ENDED 12/31/96

SCHEDULE NO. 3-B
DOCKET 960329-WS

1	OPERATING REVENUES	1,304,730	366,340	$1,671,070	($366,340)	$1,304,730	$194,141 14.88%	$1,498,871
	OPERATING EXPENSES							
2	OPERATION AND MAINTENANCE	859,570	0	$859,570	($24,673)	$834,897		$834,897
3	DEPRECIATION	170,257	0	$170,257	$718	$170,975		$170,975
4	AMORTIZATION	3,594	0	$3,594	$0	$3,594		$3,594
5	TAXES OTHER THAN INCOME	132,610	16,485	$149,095	($14,795)	$134,300	$8,736	$143,036
6	INCOME TAXES	0	32,706	$32,706	($82,248)	($49,542)	$69,768	$20,225
7	TOTAL OPERATING EXPENSES	1,166,031	49,191	$1,215,222	($120,999)	$1,094,223	$78,504	$1,172,727
8	OPERATING INCOME	$138,699	$317,149	$455,848	($245,341)	$210,507	$115,637	$326,144
9	RATE BASE	$4,928,296		$4,928,296		$3,542,750		$3,542,750
10	RATE OF RETURN	2.81%		9.25%		5.94%		9.21%

GULF UTILITY COMPANY
ADJUSTMENTS TO OPERATING INCOME
TEST YEAR ENDED 12/31/96

SCHED. NO. 3-C
DOCKET 960329-WS
PAGE 1 OF 1

	OPERATING REVENUES		
	Remove requested final revenue increase/(decrease)	$155,935	($366,340)
	OPERATION & MAINTENANCE EXPENSE		
1	Reallocate salaries to Caloosa Group	($5,905)	($3,042)
2	To reduce salary increase to 5%.	(4,895)	(2,521)
3	To reallocate common maint. expenses for lease to Caloosa Group	(2,376)	(1,224)
4	Reallocate additional A&G, vehicle, computer, etc. to Caloosa Group	(6,098)	(3,140)
5	To remove projection for unanticipated expenses	(3,300)	(1,700)
6	Correct 5-year amortization of San Carlos water line project	(2,264)	0
7	To amortize costs associated with customer survey	(5,145)	(2,650)
8	To reduce president's meals and entertainment costs	(1,072)	(553)
9	To reflect adjusted rate case expense amortization	16,091	8,289
10	To remove lobbying expenses (Stip #4)	(523)	(269)
11	To remove Rotary dues (Stip #5)	(155)	(80)
12	To remove pond cleaning expenses (Stip #7)	0	(8,000)
13	Add consulting expenses to rate case expense (Stip #8)	(4,205)	(1,979)
14	To reduce vice president's salary	(15,150)	(7,804)
	Total	($34,995)	($24,673)
	DEPRECIATION EXPENSE-NET		
1	To correct test year depreciation expense	$78,338	$42,770
2	To adjust for non-used and useful depreciation expense	1,620	(26,542)
3	CIAC for lines which should have been contributed by Caloosa Group	(2,108)	(2,755)
4	Reflect prepaid CIAC on the margin reserve	(5,475)	(19,848)
5	Impute CIAC for grant from SFWMD (Stip #15)	(142)	(236)
6	To adjust ty amort. exp. for use of composite rates for CIAC amort	(12,967)	7,329
	Total	$59,266	$718
	TAXES OTHER THAN INCOME		
1	RAFs on revenue adjustments above	$7,017	($16,485)
2	Reallocate payroll taxes	(6,047)	2,741
3	Correct test year regulatory assessment fees	(715)	(1,051)
	Total	$255	($14,795)
	INCOME TAXES		
	To adjust to test year income tax expense	$78,053	($82,248)

UTILITY: GULF UTILITY COMPANY
COUNTY: LEE COUNTY DIVISION
DOCKET NO. 960329-WS

Schedule 4A

WATER RATE SCHEDULE

Monthly Rates

Base Facility Charge					
5/8"x3/4"		$8.45	$7.88	$7.88	$7.77
3/4"		$12.68	$11.82	$11.82	$11.66
1"		$21.13	$19.70	$19.70	$19.43
1-1/2"		$42.25	$39.38	$39.38	$38.85
2"		$67.61	$63.02	$63.02	$62.16
3"		$135.21	$126.03	$126.03	$124.32
4"		$211.27	$196.92	$196.92	$194.25
6"		$422.54	$393.85	$393.85	$388.50
Gallonage Charge, per 1,000 gallons		$2.16	$2.01	$2.01	$1.93
Base Facility Charge:					
5/8"x3/4"		$8.45	$7.88	$7.88	$7.77
1"		$21.13	$19.70	$19.70	$19.43
1-1/2"		$42.25	$39.38	$39.38	$38.85
2"		$67.61	$63.02	$63.02	$62.16
3"		$135.21	$126.03	$126.03	$124.32
4"		$211.27	$196.92	$196.92	$194.25
Gallonage Charge, per 1,000 gallons		$2.16	$2.01	$2.01	$1.93
Base Facility Charge:					
1"		$7.04	$6.56	$6.56	$1.62
1-1/2"		$14.08	$13.12	$13.12	$3.24
2"		$22.54	$21.01	$21.01	$5.18
3"		$45.07	$42.01	$42.01	$10.36
4"		$70.42	$69.37	$69.37	$16.19
6"		$140.85	$131.29	$131.29	$32.38
8"		$225.35	$210.05	$210.05	$51.80
12"		$605.64	$564.52	$564.52	$139.21
- Residential Usage (gallons) -					
	3,000	$14.93	$13.91	$13.91	$13.56
	5,000	$19.25	$17.93	$17.93	$17.42
	10,000	$30.05	$27.98	$27.98	$27.07

UTILITY: GULF UTILITY COMPANY
COUNTY: LEE COUNTY DIVISION
DOCKET NO. 960329-WS

Schedule 4B

WASTEWATER RATE SCHEDULE

Monthly Rates

[illegible]				
Base Facility Charge				
All Meter Sizes	$14.48	$16.73	$16.48	$16.70
Residential Gallonage Charge, per 1,000 gallo	$3.07	$3.55	$4.23	$3.52
Wastewater Gallonage Cap - 10,000 gallons				
[illegible]				
Base Facility Charge:				
5/8"x3/4"	$14.48	$16.73	$16.48	$16.70
1"	$36.20	$41.82	$41.19	$41.74
1-1/2"	$72.39	$83.62	$82.37	$83.48
2"	$115.85	$133.83	$131.81	$133.57
3"	$231.68	$267.64	$263.61	$267.15
4"	$362.01	$418.19	$411.89	$417.41
6"	$724.01	$836.39	$823.76	$834.38
Gallonage Charge, per 1,000 gallons (No Maximum)	$3.68	$4.25	$5.08	$4.22
[illegible]				
Base Facility Charge:				
5/8"x3/4"	$14.48	$16.73	$16.48	$16.70
1"	$36.20	$41.82	$41.19	$41.74
1-1/2"	$72.39	$83.62	$82.37	$83.48
2"	$115.85	$133.83	$131.81	$133.57
3"	$231.68	$267.64	$263.61	$267.15
4"	$362.01	$418.19	$411.89	$417.41
6"	$724.01	$836.39	$823.76	$834.38
Gallonage Charge, per 1,000 gallons (No Maximum)	$3.84	$4.25	$5.29	$4.39
[illegible]				
- Residential Usage (gallons) -				
3,000	$23.69	$27.38	$29.17	$66.06
5,000	$29.83	$34.48	$37.63	$104.92
10,000	$45.18	$52.23	$58.78	$202.07

UTILITY: GULF UTILITY COMPANY
COUNTY: LEE COUNTY DIVISION
DOCKET NO. 960329-WS

Schedule 5A
Water

Schedule of Rate Decrease After Expiration of Amortization Period for Rate Case Expense

[illegible]	[illegible]	[illegible]
Base Facility Charge		
5/8"x3/4"	$7.77	$0.19
3/4"	$11.66	$0.30
1"	$19.43	$0.49
1-1/2"	$38.85	$0.97
2"	$62.16	$1.55
3"	$124.32	$3.09
4"	$194.25	$4.83
6"	$388.50	$9.67
Gallonage Charge, per 1,000 gallons	$1.93	$0.03

[illegible]	[illegible]	[illegible]
Base Facility Charge:		
5/8"x3/4"	$7.77	$0.19
1"	$19.43	$0.49
1-1/2"	$38.85	$0.97
2"	$62.16	$1.55
3"	$124.32	$3.09
4"	$194.25	$4.83
Gallonage Charge, per 1,000 gallons	$1.93	$0.03

[illegible]	[illegible]	[illegible]
Base Facility Charge:		
1"	$1.62	$0.04
1-1/2"	$3.24	$0.08
2"	$5.18	$0.13
3"	$10.36	$0.26
4"	$16.19	$0.40
6"	$32.38	$0.81
8"	$51.80	$1.29
12"	$139.21	$3.40

UTILITY: GULF UTILITY COMPANY
COUNTY: LEE COUNTY DIVISION
DOCKET NO. 960329-WS

Schedule 5B
Wastewater

Schedule of Rate Decrease After Expiration of Amortization Period for Rate Case Expense

[illegible]	[illegible]	[illegible]
Base Facility Charge		
All Meter Sizes	$16.70	$0.25
Residential Gallonage Charge, per 1,000 gallo	$3.52	$0.04
Wastewater Gallonage Cap - 10,000 gallons		

[illegible]	[illegible]	[illegible]
Base Facility Charge:		
5/8"x3/4"	$16.70	$0.25
1"	$41.74	$0.61
1-1/2"	$83.48	$1.22
2"	$133.57	$1.95
3"	$267.15	$3.90
4"	$417.41	$6.09
6"	$834.38	$11.73
Gallonage Charge, per 1,000 gallons (No Maximum)	$4.22	$0.04

[illegible]	[illegible]	[illegible]
Base Facility Charge:		
5/8"x3/4"	$16.70	$0.25
1"	$41.74	$0.61
1-1/2"	$83.48	$1.22
2"	$133.57	$1.95
3"	$267.15	$3.90
4"	$417.41	$6.09
6"	$834.38	$11.73
Gallonage Charge, per 1,000 gallons (No Maximum)	$4.39	$0.04

GROSS BOOK VALUE	$17,794,782
LAND	200,372
DEPRECIABLE ASSETS	17,594,410
ACCUMULATED DEPRECIATION TO DATE	4,289,995
ACCUMULATED DEPRECIATION AT DESIGN CAPACITY	10,270,335
NET PLANT AT DESIGN CAPACITY	$7,524,447
TRANSMISSION & DISTRIBUTION/COLLECTION LINES	$10,408,139
MINIMUM LEVEL OF C.I.A.C.	58.49%
C.I.A.C. TO DATE	$12,497,884
ACCUMULATED AMORTIZATION OF C.I.A.C. TO DATE	2,840,688
NET C.I.A.C. TO DATE	9,657,196
LEVEL OF C.I.A.C. TO DATE	71.51%
ACCUMULATED AMORTIZATION OF C.I.A.C. AT DESIGN CAPACITY	$7,432,411
FUTURE CUSTOMERS (ERC) TO BE CONNECTED	430
COMPOSITE DEPRECIATION RATE	3.09%
COMPOSITE C.I.A.C. AMORTIZATION RATE	3.34%
NUMBER OF YEARS TO DESIGN CAPACITY	11.00
EXISTING SERVICE AVAILABILITY CHARGE PER ERC	$800.00
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	71.05%
NET C.I.A.C. AT DESIGN CAPACITY	$5,345,802
REQUESTED SERVICE AVAILABILITY CHARGE PER ERC	$550.00
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	69.88%
NET C.I.A.C. AT DESIGN CAPACITY	$5,258,199
MINIMUM SERVICE AVAILABILITY CHARGE PER ERC	$0.00
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	58.49%
NET C.I.A.C. AT DESIGN CAPACITY	$5,065,473
MAXIMUM SERVICE AVAILABILITY CHARGE PER ERC	$1,649 10
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	75.00%
NET C.I.A.C. AT DESIGN CAPACITY	$5,643,335

GROSS BOOK VALUE	$14,280,084
LAND	473,626
DEPRECIABLE ASSETS	13,806,458
ACCUMULATED DEPRECIATION TO DATE	3,000,222
ACCUMULATED DEPRECIATION AT DESIGN CAPACITY	4,605,637
NET PLANT AT DESIGN CAPACITY	$9,674,447
TRANSMISSION & DISTRIBUTION/COLLECTION LINES	$8,871,486
MINIMUM LEVEL OF C.I.A.C.	62.12%
C.I.A.C. TO DATE	$9,777,967
ACCUMULATED AMORTIZATION OF C.I.A.C. TO DATE	1,901,923
NET C.I.A.C. TO DATE	7,876,044
LEVEL OF C.I.A.C. TO DATE	69.82%
ACCUMULATED AMORTIZATION OF C.I.A.C. AT DESIGN CAPACITY	$3,142,943
FUTURE CUSTOMERS (ERC) TO BE CONNECTED	495
COMPOSITE DEPRECIATION RATE	3.06%
COMPOSITE C.I.A.C. AMORTIZATION RATE	3.34%
NUMBER OF YEARS TO DESIGN CAPACITY	3.80
EXISTING SERVICE AVAILABILITY CHARGE PER ERC	$550.00
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	71.21%
NET C.I.A.C. AT DESIGN CAPACITY	$6,889,619
REQUESTED SERVICE AVAILABILITY CHARGE PER ERC	$800.00
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	72.41%
NET C.I.A.C. AT DESIGN CAPACITY	$7,005,343
MINIMUM SERVICE AVAILABILITY CHARGE PER ERC	$0.00
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	62.12%
NET C.I.A.C. AT DESIGN CAPACITY	$6,635,024
MAXIMUM SERVICE AVAILABILITY CHARGE PER ERC	$1,341.14
LEVEL OF C.I.A.C. AT DESIGN CAPACITY	75.00%
NET C.I.A.C. AT DESIGN CAPACITY	$7,255,835