BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Emergency Petition by D.R. Horton Custom Homes, Inc. to eliminate authority of Southlake Utilities, Inc. to collect service availability charges and AFPI charges in Lake County	DOCKET NO. 981609-WS
In re: Complaint by D.R. Horton Custom Homes, Inc., against Southlake Utilities, Inc. In Lake County regarding collection of certain AFPI charges.	DOCKET NO. 980992-WS

REBUTTAL
TESTIMONY
OF
ROBERT L. CHAPMAN, III
ON BEHALF OF SOUTHLAKE UTILITIES, INC.

Q. Please state your name and address.

A. My name is Robert L. Chapman, III. My business address is 2525 Lanier Place, Durham, North Carolina 27705.

Q. Are you the same Robert L. Chapman, III who previously filed direct testimony in this proceeding?

A. Yes.

Q. Have you reviewed the prefiled direct testimony of James L. Boyd and Michael Burton filed on behalf of D. R. Horton Custom Homes ("D.R. Horton")?

A. Yes.

Q. Have you reviewed the prefiled direct testimony of William Troy Rendell filed on behalf of the Staff of the Florida Public Service Commission ("Commission") in this proceeding?

A. Yes.

Q. Would you please respond to Mr. Mr. Boyd's direct testimony starting on page 4, line 21, concerning the date on which the properties were first dedicated to public service.

A. In the ideal world, every project would have one plan and would proceed from that plan to construction. However, many projects involve weighing alternatives before a final decision is made. During 1990-1993 I was President of Southlake, Inc., doing business as Southlake Development Group, the developer of the 617 acre Southlake mixed-use development. Through my efforts Southlake, Inc., was designated as a Florida Quality Development, an elite form of Development of Regional Impact, and it received approvals for construction of 8,000 housing units and two town centers. Because the Southlake development would not happen without water and sewer service, we had

to figure out how to obtain it. We came up with three alternatives.

Our first alternative, Plan A, if you will, was to use Polk County which already had a sewer plant in operation less than one-half mile from the Southlake site. Plan B was to create and use our own utility company with its own franchise area. Plan C was to have our development included in the territory of Lake Groves which was being established to serve a new subdivision called Greater Groves about one mile north of our project. Both Greater Groves and Lake Groves Utilities were controlled by Greater Construction of Altamonte Springs, Florida. We met with Lake Groves management and they were quite willing to ask the Commission to include our project in their territory. However, when we saw their tariff, we concluded that we could save money if we pursued our own franchise.

To be safe, we pursued Plans A, B and C - going back and forth several times during the 1990-1993 period. Just as we were leaning toward the Southlake Utilities option, the Lake County Board of County Commissioners stipulated that if we obtained franchises from the Florida Public Service Commission and built plants, we would immediately

have to transfer the certificates and plants to Lake County. That was hardly desirable. This led us to shelve the Southlake Utilities, Inc. plan. We decided to use Polk County and instructed our attorneys to draft a contract. Then Polk County changed the proposed terms of their service by substantially raising prices. The increased prices were so extreme that they actually made our first project economically infeasible, at least from a Florida Housing credit-underwriting standpoint. So we were forced to dust off the idea of utilizing the Southlake Utilities alternative. By this time the one-year option to lease ten acres for the plants had long since expired.

Q. Please respond to Mr. Burton's discussion regarding increases in value because of later development of surrounding property.

A. Mr. Burton is incorrect in asserting that we are trying to have the Commission recognize an increase in value resulting from the later development of surrounding land. We believe it is correct to value the land as of the date when the property was first dedicated to public service. We have provided an MAI appraisal of the land as of August 17, 1993, and an MAI appraisal as of September 22, 1990.

Q. Please respond to Mr. Burton's comments that the assessed value should be used to value the land.

A. Mr. Burton errs when he suggests that Lake County assessed valuation is pertinent. Because the property was the beneficiary of an agricultural exemption in 1991, it was appraised by the Lake County Property Appraiser's office at its value for use in tree farming, not at the value it had because of its commercial zoning adjacent to a major four-lane highway less than five miles from the boundary of Walt Disney World.

Q. On page 2 of his testimony, Mr. Burton refers to the use of lease payments in the establishment of Southlake's initial rates. Please respond to his comments.

A. Mr. Burton implies that Southlake recovered lease payments through its rates commencing in 1990. This is inaccurate. Southlake provided the pro forma information required by the Commission in its application for its original certificate. Southlake did not provide any utility service to customers until 1994, and, therefore, Southlake did not charge for utility service until 1994. Accordingly, Southlake did not recover anything for lease payments through rates until 1994. Furthermore,

Southlake has operated at a loss for every year except for a few years in which AFPI revenues were sufficient to exceed the operating losses. Accordingly, Southlake has never fully recovered its operating expenses, including the expenses related to the lease when it was an operating lease. Of course, the lease is now a capital lease and Southlake is not recovering the lease payments as operating expenses. Since Southlake has been operating at a loss, Southlake has not earned a return on its ratebase, which includes the capitalized lease.

Q. In Mr. Burton's testimony, he also referred to a statement by you that development density issues were why the property was being leased rather than sold.

A. Southlake leased the property because, as a start-up, we did not have enough money to purchase it, just the same as why many companies rent equipment or office buildings. The land had been granted a density of 13 units gross, i.e., across the entire 617 acre parcel. As part of the negotiations it helped me persuade the owners to lease the land to Southlake to discuss the concept that if they leased it rather than sold it and it was not used for

multi-family purposes, they might be able to use some of the unused density elsewhere. That was strictly a hypothetical negotiating point because in reality the lease contained no provisions which would have prevented us from removing the plants and using all of the permitted density for the remainder of the 99-year lease period. When the lease was amended to include the bargain purchase option, the new landowners requested that we include a utility purposes only provision. We refused to agree to that because, if we outgrow the site or connect to other facilities, including the density in the residual value of the land was too valuable an asset to give away.

Q. On page 4 of Mr. Burton's testimony, he states "[w]e believe there is also an argument to be made that the recent capitalization of the land lease was done for no purpose other than to try and inflate the Service Availability charges." Please respond.

A. After several months of negotiating, Southlake obtained the bargain purchase option in June of 1998. Southlake had no plans at that time to revise its service availability charges. In fact, the reason why Southlake's service availability charges are before the Commission is because D. R. Horton

filed two matters with the Commission months after Southlake had obtained the bargain purchase option. The matter filed by D. R. Horton seeking to eliminate Southlake's service availability charges was not filed until on or about November 16, 1998, about 5 ½ months after the execution of the amendment providing the bargain purchase option. The other matter filed in August of 1998 was a complaint about Southlake's procedures in collecting AFPI charges and the Commission has already found in favor of Southlake on this issue. In short, Southlake had entered into the amendment for the bargain purchase option long before its service availability charges become the subject matter of Docket No. 981609-WS.

Q. Why did Southlake want a bargain purchase option in its lease?

A. First, Southlake wanted the security and flexibility of the constructive ownership of its plant sites. Southlake determined that it had a much better chance at getting from the owner a bargain purchase option to be exercised at a distant future time rather than an outright and immediate sale of the sites. Southlake also believed that the cost of the amendment of the lease would be much less expensive

than an outright purchase. Second, Southlake wanted to strengthen its balance sheet. Southlake's lease was an advantage to Southlake which did not show up as an asset on Southlake's balance sheet. By obtaining the bargain purchase option, Southlake was able to include the lease as an asset on its balance sheet and was also able to lower operating costs, which improved its profit and loss report. By improving Southlake's financial statements to clearly reflect the long-term lease as an asset, Southlake believes that it has improved its opportunities to obtain financing at lower costs. As discussed in my direct testimony, consistent with the advice of Southlake's accounting advisors and accounting instructions from NARUC, Southlake included the capitalized lease into its plant accounts in 1998, the year of the amendment for the bargain purchase option. Contrary to Mr. Burton's argument, Southlake was not seeking to act "for no purpose other than to try to inflate the Service Availability charges." Instead, Southlake had legitimate and prudent business reasons to obtain the bargain purchase option and to capitalize the lease in accordance with generally accepted accounting principles.

Q. In Mr. Rendell's testimony, he contends that the reassessment provision in Southlake's tariff does not apply to residential customers. Do you agree?

A. Yes. However, Southlake is not trying to charge individual residential customers for the reassessment charge. Southlake does believe that the provision allows for the reassessment regarding understatements of capacity needed made by developers of commercial property and developers of residential property. The tariff uses the term "all Contributors" and developers if the Commission had meant "all nonresidential developer Contributors", it should have not approved the tariff as it was written. However, if the Staff believes that the reassessment should be limited to commercial property, Southlake believes that the buildings which are used for short term rentals should be included as commercial property subject to such a reassessment.

Q. Mr. Rendell states that the reassessment of service availability charges would cause confusion on the part of residential customers. Please respond.

A. Apparently, Mr. Rendell thinks that Southlake intended to seek the increased charges from the individual residential customers. To the contrary,

Southlake intended to seek the additional charge from the developer, the contributor who underrepresented the capacity needed for its development and thereby understated the associated service availability charges. Southlake had not sought to recover the additional charge from residential customers. As noted in its December 17, 1999, letter:

> It appears that D. R. Horton Custom Homes, Inc. [the developer] has not paid for its pro rata share of the cost of the Utility's water and wastewater treatment facilities. Accordingly, it may be necessary for Southlake Utilities, Inc. to collect additional contributions in aid of construction from D. R. Horton Custom Homes, Inc.'s [the developer] existing construction and its future construction.

Because it is the developer who underrepresented the capacity needed, it is appropriate to reassess residential developments on a whole subdivision basis rather than on an individual home basis. Furthermore, the reassessment for the contributor

would be for its development, not just one homeowner's house. The necessity for a reassessment become evident as a result of a water audit as ordered by the water management district that showed the overusage by certain subdivisions.

Q. Mr. Rendell indicated that Southlake's actions appeared to be discriminatory, especially since Southlake had not offered any refunds. Please respond.

A. First, Southlake has not reassessed anyone in a discriminatory manner. Southlake has not reassessed D. R. Horton for the additional plant capacity charges. Southlake in two letters to the Staff has demonstrated that the tariff allows for reassessment and that such reassessment is needed based upon the results of its water audit. As shown by the audit results, D. R. Horton has been the developer who was biggest offender in understating capacity usage and it seemed appropriate to start with D.R. Horton, but Southlake had not intended to limit the reassessment to only D. R. Horton. Southlake intended to obtain direction from the Staff on how to conduct the reassessment and use that information to reassess all developers who substantially understated their capacity usage pursuant to the tariff. With respect

to not offering refunds, Southlake is following its tariff. Southlake's tariff provides for the recovery of additional charges related to the reassessment - it does not provide for refunds. Southlake does not seek to act outside of its tariff. Furthermore, it would not be prudent for a utility company which has traditionally lost money to give money away in the form of refunds when the refunds were not required by the tariff. Obviously, Southlake has not acted in a discriminating manner.

Q. Mr. Rendell indicated that Southlake had the remedy of going to the Commission with a petition to revise its service availability charges if residential customers were not paying their pro rata share of facilities. Please respond.

A. Southlake did not need to go to the Commission for a remedy because the Commission had already given Southlake a remedy. The Commission had approved tariff provisions which allowed Southlake to reassess and recover the additional charges. Southlake did not need another remedy to recover the additional charges.

Q. Do you agree with Mr. Rendell's suggestion that Southlake give refunds for underusage?

A. No. As discussed in Mr. Guastella's rebuttal testimony, there should be no refunds. Southlake needs to have its plant built to provide for expected usages by developments and collect the charges for such expected usage. If someone is requiring substantially more service than they contracted for, they are using more plant capacity than they paid for, and they should contribute more accordingly. If someone is underusing service, Southlake must still be prepared to provide the level of service that would be expected from that type of development. Furthermore, underusage could have many causes which should make refunds inappropriate. For example, if the developer of a new office building was only able to rent the building for only three of the first twelve months and had standard usage those three months, the developer would probably be entitled a refund under Mr. Rendell's approach - even if the developer rented the office building for the next twelve months and it had normal usage. Or the developer could have planned to use the office building for itself and grow its staff over time. Again the usage in the first twelve months might result in a refund under Mr. Rendell's approach, even if the

building will start having normal usage in another year or two. A utility might not be able to determine how or why underusage occurs, but it can see if overusage is occurring and seek the appropriate additional charge. One action the Commission might consider is to establish a commercial classification for service availability charges for single family residence buildings being used as short term rentals. Southlake's experience would indicate that such units could constitute 2.5 ERCs.

Q. Does this conclude your rebuttal testimony?

A. Yes. However, I will be glad to answer any questions that anyone would like to ask.