BEFORE THE PUBLIC SERVICE COMMISSION

In re: Application for rate increase in Seminole County by Alafaya Utilities, Inc.	DOCKET NO. 020408-SU ORDER NO. PSC-04-0363-PAA-SU ISSUED: April 5, 2004

The following Commissioners participated in the disposition of this matter:

BRAULIO L. BAEZ, Chairman
J. TERRY DEASON
RUDOLPH "RUDY" BRADLEY
CHARLES M. DAVIDSON

NOTICE OF PROPOSED AGENCY ACTION ORDER APPROVING INCREASED WASTEWATER RATES AND CHARGES
AND
FINAL ORDER REDUCING RATES AT THE END OF THE FOUR-YEAR RATE CASE EXPENSE AMORTIZATION PERIOD, DECLINING TO INITIATE SHOW CAUSE, AND REQUIRING PROOF OF ADJUSTMENTS TO BOOKS

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service Commission that the action discussed herein, except for our decision reducing rates at the end of the four-year amortization period, declining to initiate a show cause proceeding, and requiring proof of adjustments to books, is preliminary in nature and will become final unless a person whose interests are substantially affected files a petition for a formal proceeding, pursuant to Rule 25-22.029, Florida Administrative Code.

CASE BACKGROUND

Alafaya Utilities, Inc. (Alafaya or utility), a subsidiary of Utilities, Inc., is a Class A wastewater utility located in Seminole County. Alafaya provides wastewater service to approximately 5,676 residential customers, 92 general service customers, and 55 residential reuse customers. Water service is provided in the area by the City of Oviedo. For the year ended December 31, 2002, the utility reported wastewater operating revenues of $1,912,970, and a net operating income of $308,915.

In 1986, Alafaya (formerly named Oviedo Utilities, Inc.) began serving customers. By Order No. 14841, issued September 3, 1985, in Docket No. 850209-SU, In Re: Application of Oviedo Utilities, Inc. for a certificate to provide sewer service in Seminole County, pursuant to the provision of Section 367.041, Florida Statutes, we granted the utility's original certificate and set its rates and charges. Since it was an original certificate case, rate base was calculated based upon projections and estimates of 80% of plant capacity. By Order No. PSC-95-0489-FOF-SU, issued April 18, 1995, in Docket No. 941106-SU, In Re: Application for transfer of majority organizational control of Certificate No. 379-S issued to ALAFAYA UTILITIES, INC., in Seminole County to UTILITIES, INC., we approved the transfer of majority organizational control from the utility's previous parent corporation to Utilities, Inc. The transfer involved the sale of stock, and thus did not alter the book value of the utility's assets. By Order No. PSC-98-0391-FOF-SU, issued March 16, 1998, in Docket No. 960288-SU, In Re: Application for approval of reuse project plan in Seminole County by Alafaya Utilities, Inc., we approved a reuse project plan and set reuse rates and charges. Rate base was not established in any of those dockets or in any subsequent rate proceeding.

On September 30, 2002, the utility filed an application for approval of permanent and interim rate increases. By letter dated October 24, 2002, Alafaya was informed of numerous minimum filing requirement (MFR) deficiencies. On January 10, 2003, Alafaya satisfied the MFRs, and this date was designated as the official filing date, pursuant to Section 367.083, Florida Statutes. The utility has requested that we process its case under the proposed agency action (PAA) procedures, pursuant to Section 367.081(8), Florida Statutes. Alafaya waived the 5-month statutory time frame until March 16, 2004.

The utility's requested test year for both interim and final purposes is based on the year ended December 31, 2001. Alafaya requested interim revenues of $1,988,523, which represents an increase of $177,045 or 9.77%. The requested final revenues are $2,125,634. This represents an increase of $314,156 or 17.34%. By Order No. PSC-03-0380-PCO-SU, issued March 19, 2003, we suspended the utility's proposed final rates and approved an interim revenue requirement of $1,857,865. This represented an interim revenue increase of $46,387, or 2.56%. This Order addresses the revenue requirement and rates that are approved on a prospective basis. We have jurisdiction pursuant to Sections 367.081 and 367.082, Florida Statutes.

I. QUALITY OF SERVICE

Pursuant to Rule 25-30.433(1), Florida Administrative Code, in every water and/or wastewater rate case, the Commission shall determine the overall quality of service provided by a utility by evaluating three separate components of water and/or wastewater operations. The components are: 1) the quality of the utility's product; 2) the operational conditions of the utility's plant and facilities; and, 3) the utility's attempt to address customer satisfaction. The rule further states that sanitary surveys, outstanding citations, violations, and consent orders on file with the Department of Environmental Protection (DEP) and the county health department over the preceding 3-year period shall be considered, along with input from the DEP and health department officials and consideration of customer comments and complaints.

Our analysis of the overall quality of service provided by the utility is derived from the quality of the utility's wastewater effluent, the operational condition of the utility's plant and facilities, and customer satisfaction. Comments and complaints received by the Commission from customers are reviewed. We have also considered the utility's current compliance with the Department of Environmental Protection.

Quality of the Product

In Seminole County, the wastewater operations and facilities are regulated by the DEP. According to the DEP, the utility is up-to-date with all chemical analyses and has met all chemical standards. Therefore, we find that the wastewater effluent quality is satisfactory.

Condition of Plant

On October 7, 2002, the DEP noticed the utility that it was out of compliance with its operating permit. This was a result of unauthorized overflow of effluent on July 15, 2002, from the Ekana Golf Course holding pond into the Econlockhatchee River via wetlands. A few other small deficiencies were also noted that the utility has corrected. The utility's DEP operating permit expired on January 15, 2003. According to the DEP, an operating permit will be issued shortly. However, effluent disposal continues to be a concern.

While Alafaya has 1.0 million gallons per day (mgd) of disposal capacity in its percolation\evaporation ponds, it will rely heavily on selling its treated effluent (reuse) for irrigation. The utility's reuse system is designed to ultimately dispose of 2.0 mgd when it is built out; however, there are several factors that affect Alafaya's ability to dispose of the reuse. Much of the utility's service area is in a low, wet area of Central Florida. Although the primary grass in Central Florida is St. Augustine, which needs frequent watering, irrigation is only needed in the spring and early fall. Homes in the service area are on relatively small lots and may not be able to absorb large quantities of reuse. In addition, although the Ekana Golf Course relies exclusively on reuse water to irrigate, it is only using .046 mgd (about 10%) of the .448 mgd that it was originally expected to use.

On October 17, 2002, the utility and the DEP met to discuss the effluent disposal issue. The utility proposed to add a wet weather discharge to the new permit to allow the reuse water to flow into the Econlockhatchee River. The DEP staff advised that the Econlockhatchee River is an outstanding water and that the utility would be required to upgrade to Advanced Wastewater Treatment standards to be able to discharge into the river. The DEP staff also indicated that it would be a difficult process to obtain a wet weather discharge permit.

A field investigation of the Alafaya system was conducted by our staff on February 19-21, 2003, and a second plant inspection was conducted on March 12, 2003. The wastewater treatment plants and the main percolation/evaporation ponds were in good working order. About 15 lift stations were checked and all were working satisfactorily. The wastewater system did not appear to have any deficiencies during the inspections.

On March 13, 2003, during a meeting with the DEP staff, the St. Johns River Water Management District (SJRWMD) staff, the utility, Commission staff, and the City of Oviedo (City), the City indicated that it has a need for reuse for 500 homes in the East Knightsbridge area. The utility is negotiating with the City to provide approximately .400 mgd of reuse on a temporary basis for approximately 1 ½ years. The utility hopes to provide reuse to the City in

June 2004. Temporary reuse service to the City for the homes in the East Knightsbridge area will provide time for the utility to establish its own residential reuse customer base.

An 18-inch reuse main went online on October 27, 2003, to provide reuse to the Sanctuary and Live Oak subdivisions in the utility's service area. There will be a total of about 2,000 residences in these areas when developed. There are 55 homes in the utility's service area currently taking reuse in Ekana Green (82 total homes), Waverly Woods (235 total homes), and Live Oak/Sanctuary (850 total homes). In addition, four homes are ready to be turned on for reuse service and 12 homes are being connected. Approximately 100 additional homes have requested reuse service.

It appears that the golf course could use additional reuse water. During our staff's inspection, the golf course green ways were green, but the rough areas were noticeably brown. On April 16, 2003, the golf course management was contacted to discuss reuse. It indicated that the area is wet and the cost of reuse ($.60/1,000 gallons) was high. If the rate went down, the golf course communicated that it probably would use additional reuse. We also asked if there were additional ponds that could be used to store the reuse water during the wet season. The golf course explained that there was no area onsite that could be used as a pond. However, it has a 2-acre site that is out of play that could be used as a spray field, and there is some grass that could be irrigated if the irrigation system is repiped. The golf course indicated that it would be willing to work with the utility and the Commission to dispose of additional reuse. The golf course stated initially that it would be willing to share in the capital cost to increase the amount of reuse. The utility and its consultant have met with the golf course and the utility is currently evaluating its options.

There have been several follow up conference calls with the utility to discuss potential solutions to the effluent disposal issue. The golf course could take additional reuse, but the reuse needs to be used both in dry and wet seasons. For the utility, the most critical time is during the wet season. The completion of the reuse main to serve additional customers in the utility's service area and a contract with the City to provide temporary reuse will also help to alleviate the utility's disposal issue. We believe the utility is making progress toward resolving the effluent disposal concerns and find that the quality of service for the plant is satisfactory.

<u>Customer Satisfaction</u>

The utility provided a copy of its customer complaints during the test year. Not all the customer concerns related to wastewater service complaints. The utility had a few electrical and mechanical problems at the lift stations. Most wastewater complaints were due to blocked sewer lines. If the blocked lines were determined to be the utility's responsibility, the utility either repaired or replaced the line. If the problem was determined to be the customer's responsibility, the utility advised the customer that he should contact a plumber.

We received four customer letters regarding the utility's service. As indicated below, our staff followed up on each letter and wrote a letter of response including information about the customer meeting.

One letter concerned odor, security at the plant site, capacity of the wastewater plant, ability to contact the utility by calling from the gate at Alafaya, and landscaping. Our staff responded to the customer by letter dated February 28, 2003. The utility uses Actamine, a deodorant that is misted into the air to control the odor. On February 20, 2003, and on March 12, 2003, our staff performed plant inspections and no offensive odor was noticed. We asked the utility to contact the customer about the odor concern. On March 25, 2003, the utility contacted the customer by letter indicating that it had tried to contact him on several occasions without success, and explained that he could contact the utility if he had further concerns. Also, the customer was provided with a DEP contact if he noticed the odor again.

With respect to security at the utility's plant site, there is a large dirt berm about 12 feet tall that surrounds the facility along with a 10-foot chain link fence with barb wire inside the berm. Our staff observed that the gate was locked on February 20, 2003, and utility personnel indicated that the gate is kept locked at all times. We contacted the DEP program manager for wastewater compliance and enforcement. He indicated that there is no special terrorism rule or requirement at this time for wastewater systems.

The customer was also concerned that the number of trucks seen removing waste from the site indicated that the plant was exceeding its capacity. According to the utility, the wastewater treatment plant has a capacity of 2.4 mgd although flows are limited to 1.535 mgd, the total capacity of the disposal system. Current flows average about .96 mgd. The trucks are used to remove the concentrated solids that are a normal byproduct of the treated wastewater. This is not a result of the plant being over capacity.

Another concern was the ability to contact the utility by calling from the gate at the plant site. We believe that it may be difficult for an operator to hear someone calling from the gate. The plant manager indicated that if a customer needed to contact the utility about the plant operations or to schedule a plant tour, the customer should call the customer service number. The customer was also concerned about the need for proper landscaping around the plant. During our staff's inspection, the utility indicated that it could add some additional landscaping.

Two customers complained in writing that the reuse availability charge is inappropriate. Our staff advised the customers by letter that the reuse charge was approved by Commission Order No. PSC-98-0391-FOF-SU, issued March 16, 1998, wherein the utility is authorized to charge $5.04 per month if a customer does not take reuse and $9.07 per month if a customer does take reuse. One of the customers was also concerned about the company profit of 17%. Both customers were advised to attend the customer meeting if they wanted to discuss their concerns further, but neither customer attended the customer meeting.

Another customer indicated that he had been promised reuse water over 7 years ago, and still has not received it. Our staff advised the customer by letter dated March 24, 2003, that his subdivision, Twin Rivers, was not included in the current reuse plan approved by the Commission because of the cost to retrofit existing subdivisions.

A customer meeting was held on March 12, 2003, at 6:00 p.m. at the Seminole County Services Building in Sanford, Florida. Only two customers attended the meeting. One customer spoke and explained that he was a first time homeowner and indicated that the 17% increase in rates was a little high, the interim rate was reasonable, and he thought the utility had made 16% in profit. Our staff explained that based on the utility's filing, Alafaya earned about a 5% return on its investment in 2001. The customers were also informed that the utility's stated reason for filing a rate increase is because the utility has invested about $4,000,000 since it purchased the system, an amount for which it was not earning a return. The customer was also concerned about reuse service being required. Our staff explained that DEP required the utility to make improvements to the wastewater system to provide reuse. The customer had concerns that the rate increase was due to a foreign company purchasing the utility. It was explained that ownership by a foreign company does not have any effect on the level of rates. The company has to demonstrate that its investment and expenses are prudent.

The Commission Complaint Tracking System (CATS) was also reviewed. There were a few billing complaints within the last two years that have been resolved. There was one inquiry, in March 2003, requesting when reuse service would be available. In its response, the utility indicated that reuse was available to the customer's home, and the customer has since submitted an application for reuse. Additionally, the utility was asked if there were any open complaints made directly to the utility. The response was that there were none. After reviewing the complaint files, it appears that the utility is providing prompt responses to customer concerns. We find that the quality of customer service is satisfactory.

Based on all of the above, we hereby find that Alafaya's overall quality of service is satisfactory.

II. RATE BASE

A. 2001 Test Year Plant in Service

At the time of Alafaya's transfer of majority organizational control, our practice was that if the transfer involved the sale of stock, it was not necessary to audit the books and records or establish rate base. This policy was based on the premise that a stock sale does not alter the utility's asset and liability accounts, nor should it change rate base. Currently, we perform an audit when a change in ownership occurs or is anticipated in the near future. This practice helps insure that a purchasing utility has obtained the prior owners' books and records and the continuing utility's investment in rate base is adequately supported.

In its MFR filing, Alafaya submitted an original cost study to support its rate base components since inception through December 31, 1994. We analyzed the utility's original cost study and subsequent supplemental information submitted. As indicated below, we believe several adjustments are necessary to the utility's original cost study. Further, we have additional adjustments from 1995 to the 2001 test year.

Original Cost Study

We have recognized original cost studies when the books and records were not available. See Order No. PSC-01-1792-PAA-SU, issued September 5, 2001, in Docket No. 001820-SU, In Re: Application for transfer of wastewater utility facility in Lee County from Cross Creek of Fort Myers Community Association, Inc., a not-for-profit Florida corporation, to Utilities, Inc. of Eagle Ridge, holder of Certificate No. 369-S, and for amendment of Certificate No. 369-S to include additional territory; Order No. PSC-93-0430-FOF-WS, issued March 22, 1993, in Docket No. 920834-WS, In Re: Petition for limited proceeding to increase rates to recover cost of purchased assets disallowed in Docket No. 910020-WS by Utilities, Inc. of Florida; Order No. PSC-93-1816-FOF-WS, issued December 22, 1993, in Docket No. 930449-WU, In Re: Application for a staff-assisted rate case in Lake County by Glenn's Cove Central Water System; and Order No. 25139, issued September 30, 1991, in Docket No. 900966-WU, In Re: Application for a staff-assisted rate case in Sumter County for The Woods, a division of Homosassa Utilities, Inc.

The procedure for determining original costs without supporting documentation consists of identifying the existence of the assets, estimating the physical quantities, and estimating the cost of those assets at the time they were constructed or placed into service. Alafaya, in its analysis, was able to find some contracts, invoices, checks and sub-ledger summaries which were used to provide a basis to cost out the treatment and disposal system. The availability of this information meant that the original cost of a portion of the system assets could be identified from the records of paid invoices and a portion would be estimated through the original cost study.

In order to estimate the original cost for Alafaya, the utility used signed vendor payment requisitions for actual 1984 construction costs incurred by Utilities Inc. of Florida (UIF) in Pasco County. The utility then used an index to trend the UIF historical construction costs to the Alafaya facilities in-service date. The Means Historical Cost Index (HCI) was used, which is an index of the weighted average of material and labor costs of building construction projects published by R.S. Means Company, Inc. The utility also prepared a comparison of three indexes: the HCI index, the Engineering News Record (ENR), and the U.S. Environmental Protection Agency's (EPA) Construction Cost Index (CCI), the last of which is no longer maintained. A graphic comparison included in the utility's study showed that the HCI index trended favorably with both the ENR and the EPA's CCI indices. We have previously accepted the HCI methodology in Docket No. 001820-SU, by Order No. PSC-01-1792-PAA-SU (previously referenced). Based on our review, we believe that the HCI index appears to be a reasonable basis for trending wastewater construction cost for purposes of this study.

The utility's original cost study did not provide detail on the golf course irrigation system cost, and, as such, we requested additional information. On March 31, 2003, the utility provided a supplemental original cost study for the golf course irrigation system based on estimating the physical quantities and cost of the individual components. The supplemental original cost study used the Handy Whitman Index (HWI) and the ENR indices to trend the cost. The HWI is another index commonly used and accepted by the Commission to trend building construction costs.

The supplemental study included construction estimates for the Twin Rivers Golf Course effluent disposal facility (now the Ekana Golf Course). The total contract cost was $2,817,933 to the original developer that owned both Alafaya and the golf course. The utility assets recorded on the original developer's subsidiary ledger totaled $1,273,353, which was the amount allocated to the utility from the golf course construction. The supplemental original cost study calculated an original cost of $1,052,808, which is $220,545 less than the ledger amount. The utility believes that it should not be concluded that the ledger is incorrect because there are some supporting invoices. In addition, the utility stated the cost in the supplemental original cost study does not include the costs associated with an existing practice range pump station and related piping, and a river intake and its related wet well and pump station that are in existence, but not in use. The utility believes that the cost of these items may very well represent the difference in the cost recorded on the ledger and the costs determined in the supplemental original cost study.

We believe that since the practice range pump system is not in use it shall not be considered at this time as part of the treatment and disposal system. With respect to the river intake system, this does not appear to aid in the disposal of the utility's effluent; as a result, we find that it shall not be considered a part of the treatment and disposal system.

In Audit Disclosure No. 4, our staff auditors stated that the utility did not provide information to support rate base activity that occurred in 1994. Since the utility's original study includes activity from 1985 to the year ended December 31, 1993, the auditors stated that Alafaya's study should have included the rate base activity that occurred in 1994. As a result, the auditors pointed out that rate base was not audited for the 1994 calendar year. In response to the audit, Alafaya stated that the original cost study and the supplemental cost study included the plant additions reflected in the utility's 1994 annual report. Even though the study is as of December 31, 1993, Alafaya believes that the value of the assets through 1994 are already included in the cost study total as of December 31, 1993. The utility asserts that it is important to recognize that one cannot just compare the results of the study with the annual report balance for plant alone.

Further, by letter dated May 9, 2003, Mr. Frank Seidman (the utility's engineering consultant) stated that the study did not include a multiplier to the base original cost to account for engineering, administrative, and general overhead costs as is traditionally done in an original cost study. He explained that a multiplier for engineering costs was purposely excluded because source documents supporting actual engineering costs were found and actual original engineering costs were already included in the study. However, a multiplier for administrative and general (A&G) overheads in the amount of 10% should be have been included and should be considered as an adjustment to the study. Since A&G overheads are normal costs incurred as a part of the construction process and are typically included in original cost estimates, we agree that a multiplier for A&G overheads in the amount of 10% shall be applied to plant.

Based on our review, we find that the following original costs for the Alafaya's collection, system pumping, and treatment and disposal plant as of December 31, 1994, shall be accepted:

Account No. and Name	Original Cost Study	Allowance for A&G Overhead	Total Cost
354 Structures and Improvements	$ 528,619	$ 52,862	$ 581,481
355 Power Generation Equipment	5,147	515	5,662
360 Collection Sewers – Force	532,469	53,247	585,716
361 Collection Sewers – Gravity	2,763,827	276,383	3,040,210
363 Service to Customers	501,857	50,186	552,043
371 Pumping Equipment	845,448	84,545	929,993
380 Treatment & Disposal Equip	3,705,388	370,539	4,075,927
Total	$8,882,755	$888,276	$9,771,032

With regard to organization costs, Alafaya's general ledger reflects a balance of $2,484 for the year ended December 31, 1994. The utility's original cost study did not include any support documentation for organization costs. In a subsequent letter from the utility's engineering consultant, Alafaya stated that the prior owner's annual reports indicated that the $2,484 was originally booked for organization costs in 1985. According to the utility consultant's opinion, this amount is conservative, but an acceptable amount to be included as a part of the original cost. Other than the $2,484 balance reflected in the prior owner's annual reports, we note that no additional support or basis for the utility consultant's opinion was provided. We believe it is the utility's burden to justify its requested costs. Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982). Without further support illustrating why this amount is reasonable, we find that the $2,484 amount shall not be included in plant.

Regarding franchise costs, Alafaya's general ledger reflects a balance of $79,663 for the year ended December 31, 1994. In its study, the utility included $16,693 in Account No. 352 - Franchises. According to our review of the support documentation, costs totaling $16,289 were related to two certificate amendment cases the utility had in 1986. We find that those costs should have been treated as regulatory commission expense and amortized over five years consistent with the treatment of non-recurring expenses, pursuant to Rule 25-30.433(8), Florida Administrative Code. The remaining cost of $404 related to miscellaneous services provided to the utility by an engineering firm. We find that this cost should have been treated as an operation and maintenance (O&M) expense in 1989. Further, the utility has not provided any support documentation for the remaining $62,970 franchise amount. Therefore, we find that the $79,663 amount shall not be included in plant.

With regard to general plant, Alafaya's general ledger reflects a balance of $13,575 for the year ended December 31, 1994. The utility's original cost study did not include any support documentation for general plant. By letter dated May 9, 2003, the utility's engineering consultant asserted that general plant should not be included in the original cost estimate for Alafaya. Based on a review of the annual reports prior to the transfer and through the test year, Alafaya's consultant stated that it appears that the general plant assets did not carry over in the transfer and are properly excluded. Accordingly, we find that the $13,575 amount shall not be included in plant.

Based on the above, we find the appropriate balance of plant as of December 31, 1994, shall be $9,771,032. The MFRs reflected a 1994 year-end balance of $9,961,805. This represents a difference of $190,775. Therefore, we find that plant shall be reduced by $190,775.

Plant in Service from 1995 to 2001

Organization and Franchise Costs

In its MFRs, Alafaya reflected test year balances of $190,696 and $129,145 for organization costs and franchises, respectively. Our staff auditors recommended several adjustments to Organization and Franchises that had been booked after 1994. Based on our review, we believe several adjustments are necessary.

According to Audit Exception No. 1, the utility recorded $150,085 and $343 of organization cost additions in 1995 and 1997, respectively. With regard to the 1995 additions, our auditors recommended removing the entire amount for the following reasons. First, invoices totaling $288 for legal fees should have been charged to O&M expense in 1995. Second, invoices and capitalized executive time totaling $16,283 for legal fees and travel costs should have been recorded as utility acquisition costs and not recorded in plant. Third, invoice numbers and general ledger journal entries totaling $133,514 were not supported by any utility documentation. Regarding the 1997 addition, our auditors stated that an invoice totaling $343 was for legal fees related to Wedgefield Utilities, Inc. (Alafaya's sister company).

We have previously determined that the purchase cost of utility systems is to be charged as acquisition costs, not capitalized to plant as organization costs. See, Order No. PSC-98-0524-PAA-SU, issued April 16, 1998, in Docket No. 971065-SU, In Re: Application for rate increase in Pinellas County by Mid-County Services, Inc. In its response to the audit, Alafaya did not address the above adjustments. Based on the above, we find that organization costs shall be reduced by $150,428.

According to Audit Exception No. 1, the utility recorded $49,482 of franchise cost additions in 1998. These additions consisted of $34,686 for legal fees over a service territory dispute with the City of Oviedo and $14,796 for capitalized salaries. Our auditors stated that the litigation costs should have been recorded in Miscellaneous Deferred Debits pending our determination of the proper accounting treatment of these costs. Our auditors also stated that the capitalized salaries should have been recorded in Collection Sewers - Gravity. Alafaya did not respond to the auditor's recommended adjustments.

Based on the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts (USOA), we find that the $49,482 of additions are misclassified as franchises and shall be removed. The accounting treatment of the litigation costs is addressed later in this Order in the section regarding working capital. A corresponding adjustment shall also be made to increase Collection Sewers – Gravity by $14,796.

Unrecorded Retirements, Lack of Support, and Misclassifications

In Audit Exception No. 1, our staff auditors recommended several adjustments to plant. Our analysis of the auditors' recommended adjustments is shown below.

Account 354 - Structures and Improvements - The auditors recommended the following adjustments for the years 1995-2000:

Year	Auditors' Recommended Adjustments
1995	Failure to retire $3,282 of plant replaced by a rebuilt lift station pump and an unsupported general ledger plant journal adjustment of $4,796. Total plant reduction of $8,077.
1996	Unrecorded plant retirements related to a rebuilt effluent pump at the wastewater treatment plant and lift station rewiring of $3,410 and $7,895, respectively. Total plant reduction of $11,305.
1998	An unrecorded plant retirement related to rebuilding a lift station for a total plant reduction of $12,740.
1999	An unrecorded plant retirement related to a rebuilt pump and starter at Lift Station No. 16 for a total plant reduction of $8,452.
2000	A $1,605 addition for an alarm system at Lift Station No. 7 for Utilities, Inc. of Longwood (one of Alafaya's sister companies) that should be removed and reclassified to the proper utility system. Total plant reduction of $1,605.

In its response to the audit, the utility disagrees with two of the auditors' recommended adjustments. First, if the original cost of plant retired or the year that the retired plant was originally placed into service is not known, it is Alafaya's retirement policy to reduce plant by 75% of the replacement plant addition. However, if the year that the retired plant was placed into service is known, the utility uses the Handy Whitman Index (HWI) to determine the appropriate retirement percentage to apply to the cost of the replaced plant.

In 1998, with regard to the $12,740 retirement adjustment, the auditors retired 75% of the $16,987 replacement addition. Alafaya stated that this addition consisted of $11,369 for parts for a pump, and $5,618 related to labor. The utility states that the old pump was placed into service in 1988. Using the HWI, the utility states that the retirement percentage should be 55%, which should then be applied to the $11,369 amount for parts, resulting in a $6,253 reduction to plant. Based on our review, we find that the utility's proposed retirement percentage appears reasonable.

In 1999, with regard to the $8,452 retirement adjustment, the auditors retired 75% of the $11,269 replacement addition. Alafaya stated that this addition related to equipment placed into service in 1987. Using the HWI, the utility states that the retirement percentage should be 52%, which would result in a $5,860 reduction to plant. Based on our review, we find that the utility's proposed retirement percentage appears reasonable.

Based on the above, we find that Structures and Improvements shall be reduced by $33,100, to reflect retirements, to disallow unsupported costs, and to reclassify non-Alafaya costs.

Account 360 - Collection Sewers-Force – Our staff auditors recommended the following adjustments to this account:

Year	Auditors' Recommended Adjustments
1995	A $5,742 unsupported general ledger journal entry.
1997	An unrecorded plant retirement related to the relocation and replacement of 80 feet of force main for a total plant reduction of $1,762.
1999	A $1,329 unsupported addition and an addition of $910 related to another utility. Total plant reduction of $2,239.

Alafaya did not respond to the above recommended adjustments. Based on the above, we find that our staff auditors' recommended adjustments are appropriate in order to reflect retirements, to disallow unsupported costs, and to reclassify non-Alafaya costs. Therefore, we find that Collection Sewers - Force shall be reduced by $9,744.

Account 361 - Collection Sewers - Gravity - Our staff auditors recommended the following adjustments to this account:

Year	Auditors' Recommended Adjustments
1995	A $2,193 unsupported addition.
2001	A $17,133 addition to repair a force main break that should be recorded as an O&M expense and reduced plant.

We find that plant shall be reduced by $2,193 due to lack of support. With regard to the repair of a force main, we agree that the cost should be expensed. We further find that this cost is non-recurring, because a force main repair of this magnitude should not be an annually recurring event. Pursuant to Rule 25-30.433(8), Florida Administrative Code, non-recurring expenses shall be amortized over five years. The $17,133 amount includes $133 of allowance for funds used during construction (AFUDC). As a result of our reclassification, the $133 amount of AFUDC would not be amortized because expenses do not accrue AFUDC. As such, we find that the $17,000 cost shall be amortized over five years, in accordance with Rule 25-30.433(8), Florida Administrative Code.

Based on the above, we find that Collection Sewers-Gravity shall be reduced by $3,511 on a 13-month average basis and by $19,326 on a year-end basis. In addition, we find that Miscellaneous Deferred Debits shall be increased by $1,046 on a 13-month average basis and by $13,600 on a year-end basis. Lastly, we find that Contractual Services-Other shall be increased by $3,400.

Account 380 - Treatment & Disposal Equipment - Our staff auditors recommended the following adjustments to this account:

Year	Auditors' Recommended Adjustments
1995	Unsupported additions of $26,728. A $1,606 addition for generator repairs that should be recorded as an O&M expense. Unrecorded plant retirements of $74,033 for major repairs to plant. Total plant reduction of $102,367.
1996	Unrecorded retirement for rebuilt blower at the wastewater treatment plant. Reduce plant by $962.
1997	A $2,143 addition for annual maintenance of the emergency generator that should have been recorded as an O&M expense. Unrecorded retirements of $8,568 for major repairs or replacements to plant. Reduce plant by $10,711.
1998	Unsupported additions of $1,686.
1999	A $968 unsupported addition.
2000	A $4,967 unsupported addition. Unrecorded plant retirement of $55,013 related to major repairs to plant. Total plant reduction of $59,980.
2001	Additions of $66,706 for major maintenance work that is non-recurring and should be recorded as a miscellaneous deferred debit and amortized over five years.

In its response to the audit, the utility disagrees with one of the auditors' recommended adjustments. Regarding the $55,013 retirement in 2000, the auditors retired 75% of the plant addition. Alafaya stated that this addition related to a rehabilitation project of Lift Station No. 9. Specifically, the pumps from Lift Station No. 13 were rebuilt and put into service at Lift Station No. 9 in 1984. Using the Handy Whitman Index, the utility states that the retirement percentage should be 55%, which represents a retirement adjustment of $40,343. Based on our review, we find that the utility's proposed retirement percentage appears reasonable.

Regarding the major maintenance of $66,706 recorded in 2001, we note that this amount included $1,170 of AFUDC. As a result of the reclassification, the $1,170 amount of AFUDC shall not be expensed. As such, the $65,536 cost must be amortized over five years.

Further, according to the audit work papers, the utility had a $70,826 addition in 2001. This addition was a major rehabilitation project for three surge tanks that included removal and treatment of sand and sludge. This project included the installation of a new inlet box and bar screen for a surge tank which totaled $3,700; however, no retirement was made by Alafaya. Consistent with the utility's retirement policy, we find that plant and accumulated depreciation shall both be reduced by $2,775.

Based on the above, we find that Treatment & Disposal Equipment shall be reduced by $167,349 on a 13-month average basis, and by $231,485 on a year-end basis. In addition, we find that Miscellaneous Deferred Debits shall be increased by $4,033 on a 13-month average basis and by $52,429 on a year-end basis. Lastly, we find that Contractual Services-Other shall be increased by $13,107.

Account 393 - Tools, Shop and Garage Equipment and Account 394 - Laboratory Equipment - Our staff auditors recommended that Account 393 be reduced by $2,496 for unrecorded retirements and Account 394 be reduced by $396 for lack of support documentation. The utility did not respond to any of these adjustments. Based on the above, we find that Account 393 - Tools, Shop and Garage Equipment is reduced by $192 on a 13-month average basis and by $2,496 on a year-end basis. Further, we find that Account 394 - Laboratory Equipment is reduced by $396.

Plant Allocations from Affiliated Companies

Utilities, Inc. of Florida (UIF) is a sister company of Alafaya, both are subsidiaries of Utilities Inc. (UI). UIF allocates a portion of its common plant and accumulated depreciation to each Florida subsidiary. In addition, Water Services Corp (WSC), the service corporation for UI, allocates common costs, including billing costs to all of its subsidiary utilities, including Alafaya. UI allocates these common costs to its water and wastewater operations based on a calculated customer equivalent percentage that equates all UI customers in terms of single family residential units.

In Audit Exception No. 7 of the UIF audit in Docket No. 020071-WS, our staff auditors stated that in 2000, an addition of $29,880 was included in general plant for the purchase of a new Norstar voice mail system for the UIF office. The auditors stated that this new voice mail system replaced an existing system, but UIF did not record any retirement to plant or accumulated depreciation when the new system was installed. As such, the auditors recommended that plant and accumulated depreciation should be decreased both by $22,410 to reflect the retirement. In Audit Exception No. 2 in this docket, our staff auditors stated that Alafaya's portion of common UIF plant and accumulated depreciation was overstated by $1,717. In its response to the audit, Alafaya stated that it does not contest this audit exception. Therefore, we find that Alafaya's common plant allocation from UIF is decreased by $132 on a 13-month average basis and by $1,717 on a year-end basis.

Our staff also performed an undocketed affiliate transaction (AT) audit of UI and its subsidiary WSC for the 12-month period ended December 31, 2001. In Audit Exception No. 1 of the AT audit, our staff auditors recommended that WSC's office and communication equipment should be reduced by $4,608 and $4,210, respectively. The auditors stated that WSC's computer equipment should also be reduced by $56,774 for missing invoices and by $120,817 for transfers that were never recorded. The staff auditors did not recommend any adjustment be made for the following reasons. First, UI and WSC could not provide the support for the computers on its inventory list that would have enabled the auditors to determine the amount of accumulated depreciation related to its computer equipment. Second, an adjustment totaling $177,591, when applied to WSC's current balances for mainframe and minicomputers, would create a negative rate base balance since accumulated depreciation would exceed the balance in both accounts. Therefore, our staff auditors set the main frame and mini-computer accounts, and respective accumulated depreciation balances, to zero. Based on the above adjustments, the staff auditors recommended that Alafaya's 13-month average WSC's rate base allocation should be $73,519.

Upon further review, the utility did not record any amount for WSC common rate base in its MFRs. Therefore, we find that Alafaya's rate base shall be increased to reflect the appropriate allocation for WSC common rate base. In its response to the audit, Alafaya disagreed with our staff auditors' adjustment to decrease the minicomputers and the associated accumulated depreciation to zero. In Docket No. 020407-WS, the utility's sister company, Cypress Lakes, provided our staff with two invoices to support its computer inventory list. We have reviewed the invoices submitted and find that the utility's inventory list has been supported. We have calculated the 13-month average allocated minicomputers rate base allocation for Alafaya to be $1,383. After making this adjustment, we find that the appropriate 13-month average WSC rate base allocation is $74,902.

General Ledger Plant Additions and Retirements

In its MFRs, Alafaya reflected $4,407,930 in plant additions net of retirements from 1995 to 2001. According to the utility's general ledger, the net plant additions for the same period were $4,412,260, which represents a difference of $4,330. To reflect all of the general ledger net plant additions for this period, we find that plant per the MFRs shall be increased by $4,330.

Conclusion

Based on our original plant cost as of December 31, 1994, and the other specific adjustments outlined above, we find that plant in service shall be decreased by $511,081 on a 13-month average basis and by $594,921 on a year-end basis. In addition, we find that Miscellaneous Deferred Debits shall be increased by $5,079 on a 13-month average basis and by $66,029 on a year-end basis. Lastly, we find that Contractual Services-Other shall be increased by $16,507.

The following table summarizes the total 13-month average test year plant adjustment of $511,081:

Original Cost Adjustment		($190,775)
Audit Adjustments from 1995 to 2001		
Organization Costs	($150,428)	
Franchise Costs	(49,482)	
Structures & Improvements	(33,100)	
Collection Sewers – Force	(9,744)	
Collection Sewers – Gravity		

Reclassification from Franchise Costs	14,796	
Plant Reduction	(3,511)	
Treatment & Disposal Equipment	(167,349)	
Tools, Shop and Garage Equipment	(192)	
Laboratory Equipment	(396)	
UIF Common Plant Allocation	(132)	
Total Audit Adjustments from 1995 to 2001		(399,538)
WSC Rate Base Allocation		74,902
General Ledger Net Plant Addition Adjustment		4,330
Total 13-month Average Test Year Plant Adjustment		($511,081)

B. Valuation of Land

According to its MFRs, the utility reflected a balance of $26,255 for wastewater land as of December 31, 2001. In Audit Exception No. 4, our staff auditors pointed out that NARUC, Class A, Accounting Instruction 18A, requires that all amounts included in the amounts for utility plant acquired as an operating unit or system shall be stated at the cost incurred by the person who first devoted the property to utility service. The auditors stated that the utility's balance for wastewater land is understated by $34,588 ($60,843 - $26,255) as of December 31, 2001.

On May 16, 1984, Norman A. Rossman and William J. Goodman executed a special warranty deed that transferred 783 acres of undeveloped land to South Country Corp. (SCC), a California corporation, for $12,000,000, or $15,326 per acre. Included in this acreage was land used to construct a wastewater treatment plant to service the planned development. On September 17, 1992, SCC executed a warranty deed that transferred 3.97 acres to the utility, which was a related party of SCC. The legal description of the property transferred coincides with the Seminole County Property Appraiser's current legal description for the utility's wastewater treatment plant facility. Thus, the staff auditors recommended that the original cost of the land for the wastewater treatment plant site should be $60,843, based on the original cost of $15,326 per acre times 3.97 acres.

The utility did not respond to this adjustment. Based on the above, we find that the original cost of the land is $60,843, which represents an increase of $34,588.

C. Accumulated Depreciation

In Alafaya's original certificate case, we projected a composite depreciation rate of 3.3%. In Audit Exception No. 5, our staff auditors pointed out that the utility used account specific rates to depreciate its plant from 1985 through 1994. Upon reviewing Alafaya's annual reports filed with the Commission, the staff auditors indicated that the utility used a composite rate of 1.5 percent to depreciate its plant in 1995 and 1996. The auditors believe that the utility should have used the Commission approved rates.

In our analysis, we discovered that the utility also used depreciation rates other than those prescribed by Rule 25-30.140, Florida Administrative Code, for several plant accounts from 1997 to 2001. In order to establish the proper balance of accumulated depreciation, we started with our adjusted original cost study primary account classifications. In July 2003, we requested that the utility provide a detailed schedule to reconcile the plant additions from 1995 to 2001 to the original cost study primary plant account classifications. Upon receipt of this reconciliation in October 2003, we made corrections to several plant accounts to agree with the general additions and retirements.

Based on the plant adjustments approved earlier in this Order, the reconciled plant classifications, and the above adjustments, we recalculated accumulated depreciation in accordance with Rule 25-30.140, Florida Administrative Code. As a result, we find that accumulated depreciation shall be increased by $666,361 on a 13-month average basis and by $825,467 on a year-end basis. A corresponding adjustment shall also be made to increase test year depreciation expense by $143,861. We have reflected the approved 2001 year-end accumulated depreciation balance, by primary account, in Schedule No. 5, which is appended to this Order.

D. Contributions in Aid of Construction

In Alafaya's original certificate, we approved a plant capacity charge of $410 per ERC. See Order No. 14841, p. 4. Subsequently, in the utility's 1996 reuse proceeding, we increased Alafaya's plant capacity charge to $640 per ERC. See Order No. PSC-98-0391-FOF-SU, p. 19. According to its MFRs, the utility reflected 13-month average balances for CIAC and accumulated amortization of CIAC of $9,225,895 and $2,518,883, respectively.

Alafaya's original cost study included an analysis for both plant and CIAC. The utility initially calculated CIAC for plant capacity charges based on the number of meters in the annual reports. The utility later stated that the imputation of plant capacity charges should instead be based on the total number of customers that were actually served at the end of 2001 as detailed in MFR Schedule E-3 which is 5,693. We note that Alafaya's 2001 annual report listed a significantly greater number of meters than the customers reflected in its MFRs. Our staff auditors verified that the test year customers reflected in the MFRs were correct. Because the number of meters in the annual reports, from inception to the test year, was not audited, we agree with the utility that it is appropriate to utilize 5,693 as the total number of customers to impute plant capacity charges.

Consistent with our treatment of plant, we escalated the utility's CIAC for contributed plant by 10% to recognize administrative and general overheads. Based on the above, we calculated the original cost for the Alafaya's CIAC and accumulated amortization of CIAC to be $6,565,030 and $1,457,227, respectively. For the period 1995 to 2001, the utility provided a detailed schedule which reconciled the contributed plant additions from 1995 to 2001 to the original cost study primary plant account classifications. With this information, we were able to recalculate accumulated amortization of CIAC in accordance with Rule 25-30.140, Florida Administrative Code. Accordingly, we find that Alafaya's test year CIAC and accumulated amortization of CIAC is $9,566,581 and $3,450,340, respectively. As a result, we find that the 13-month average balance of CIAC and accumulated amortization of CIAC shall be increased by $340,686 and $931,457, respectively. We also find that a corresponding adjustment shall be made to increase the test year amortization expense by $154,964.

E. Pro Forma Plant Additions

According to its MFRs, Alafaya reflected pro forma plant additions of $2,847,259. All but $16,886 of this amount related to reuse plant additions to be completed in 2002. We have reviewed the support documentation and prudence for these pro forma plant amounts. Based on our review, we find that adjustments are necessary to Alafaya's requested pro forma plant additions.

In Audit Exception No. 3, our staff auditors stated that the utility provided construction project schedules and invoices totaling $2,529,378 to support the utility's pro forma plant additions included in its MFRs. The supported invoices represent $317,881 less than the amount originally requested by the utility in its MFRs, as follows:

Pro Forma Plant	Per MFRs	Per Audit	Audit Difference
On-site Reuse Plant Facilities	$1,170,924	$1,217,630	$46,706
Lift Station Submersible Pump	6,718	6,590	(128)
Two Blowers-WWTP Digester	10,168	10,503	335
Reuse Water Main	512,228	346,035	(166,193)
Reuse Distribution System	1,147,221	948,620	(198,601)
Total	$2,847,259	$2,529,378	($317,881)

In its response to the audit, Alafaya provided additional support documentation for $136,276 related to the reuse water main project, and $4,878 for the reuse distribution system.

We have reviewed these invoices and believe the additional amounts are supported. To properly reflect the total cost for each of the pro forma construction projects, we have recalculated AFUDC.

As stated previously, DEP has expressed concern over the utility's amount of effluent disposal capabilities, and that increased reuse should be utilized in order to alleviate this concern. Three of the projects discussed above are for facilities to increase reuse distribution. Section 367.0817, Florida Statutes, states: "[a]ll prudent costs of a reuse project shall be recovered in rates." The other pro forma projects included in the MFRs appear to improve the existing treatment and disposal facilities and do not increase the capacity of the system. As a result, we find that the appropriate pro forma plant for the five construction projects is $2,865,413. This represents $18,154 greater than the amount requested by the utility, which is further illustrated in the table below.

Pro Forma Plant	Per MFRs	Per Com'n	Difference
On-site Reuse Plant Facilities	$1,170,924	$1,239,396	$68,472
Reuse Submersible Pump	6,718	6,577	(141)
Two Blowers-WWTP Digester	10,168	10,501	333
Reuse Water Main	512,228	532,355	20,127
Reuse Distribution System	1,147,221	1,076,585	(70,636)
Total	$2,847,259	$2,865,414	$18,155

On September 26, 2003, the utility provided a schedule listing an additional $1.3 million of capital projects that are projected to be placed in service by September 2004. By letter dated October 8, 2003, Alafaya submitted approved internal company work orders for nine plant projects totaling $738,048. In addition, Alafaya listed fourteen other plant projects for which work orders had not been approved at the time, and the utility estimated the costs for those projects to be $3,010,500. On October 23, 2003, Alafaya provided several unexecuted contracts and cost proposals for the above projects which all except one dated back to early 2003. Alafaya stated that some projects have already been placed in service, and the utility requested ratemaking consideration in this docket for these additions.

Alafaya submitted documentation for numerous smaller projects totaling $112,590, such as a surge pump replacement/rehabilitation project, and filling and grading of low areas around the utility's percolation ponds. Of that amount, $74,090 was for plant improvements completed by 2003. Alafaya also provided an executed contract for engineering costs to analyze sludge handling for $38,500, which was anticipated to be completed in April 2004. The utility stated that these plant improvements were designed to modernize and repair several plant components.

On December 29, 2003, Alafaya provided another executed contract for a digester replacement project totaling $704,500, and an executed contract for a new project to rehabilitate its west plant for $189,724. The utility stated that the anticipated completion dates for the west plant and digester projects were April and August 2004, respectively.

Based on our review, the utility has supported an additional $74,090 in pro forma plant beyond that which was requested in the MFRs. As such, we find that the supported pro forma plant additions completed by the end of 2003 are reasonable and necessary either to serve the utility's existing wastewater customer base or to provide reuse to more customers.

The utility's supplemental request to include additional plant beyond 2003 shall not be allowed. Plant additions placed in service in 2004 exceed the 24-month post-test year timeframe, contemplated by Section 367.081(2)(a)2, Florida Statutes. This section states that:

> . . . . the commission shall consider utility property, including land acquired or facilities constructed <u>or to be constructed within a reasonable time in the future</u>, not to exceed 24 months after the end of the historic base year used to set final rates <u>unless a longer period is approved by the commission</u>, to be used and useful in the public service, if:
>
> a. <u>Such property is needed to serve current customers</u>; (Emphasis added.)

The utility has not presented a compelling argument as to why a period exceeding 24 months should be allowed. In addition, going outside the 24-month period could substantially affect the rate setting concept of a test year. To add material plant additions without considering the impact of CIAC, customer growth, or other changes to a test year can produce a revenue and rate mismatch. Accordingly, we find that no pro forma plant shall be considered for 2004, since that is two years beyond the end of the test year.

We requested that the utility document whether any of the 2002 and 2003 pro forma plant would be funded by CIAC. Based on our analysis, all of the invoices supporting the requested plant have been funded by the utility and not contributed by developers. The utility also provided detail regarding the CIAC added in 2002 and 2003, and the majority of those additions have come from contributed plant from developers, where neither the plant nor the CIAC have been included in this case.

Based on the above, the total amount of pro forma plant that shall be allowed in this rate case is $2,939,504, resulting in an increase of $92,245, which is the difference between the approved amount and the $2,847,259 amount included in the MFRs. Based on our approved pro forma plant, we calculated the associated pro forma accumulated depreciation and depreciation expense to be $80,976 for each. Accordingly, we find that accumulated depreciation and depreciation expense shall both be increased by $43,643 ($80,976 less $37,333 included in the MFRs).

F. Used and Useful Plant

Rule 25-30.432, Florida Administrative Code, provides the criteria to be used in calculating used and useful for a wastewater treatment plant, except in the case of reuse projects. The rule states:

> The flow data to be used in the numerator of the equation for calculating the used and useful percentage of a wastewater treatment plant shall be the same period or basis (such as annual average daily flow, three-month average daily flow, maximum month average daily flow) as the period or basis stated for the permitted capacity on the most recent operating permit issued by the Florida Department of Environmental Protection (DEP). The DEP permitted capacity shall be used in the denominator of the equation. In determining the used and useful amount the Commission will also consider other factors such as the allowance for growth pursuant to Section 367.081(2)(a)2., F.S., infiltration and inflow, the extent to which the area served by the plant is built out, whether the permitted capacity differs from the design capacity, and whether there are differences between the actual capacities of the individual components of the wastewater treatment plant and the permitted capacity of the plant, and whether flows have decreased due to conservation or a reduction in the number of customers. The rule does not apply to reuse projects pursuant to Section 367.0817(3), F.S. or investment for environmental compliance pursuant to Section 367.081(2)(a)2.c., F.S.

In addition, Section 367.0817 (3), Florida Statutes, provides that,

> All prudent costs of a reuse project shall be recovered in rates. The Legislature finds that 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.

Wastewater Treatment Plant and Reuse System

According to the utility's DEP permit, the Alafaya wastewater treatment plant consists of two 1.2 million gallons per day (mgd) Annual Average Daily Flow (AADF) extended aeration treatment plants (total design capacity 2.4 mgd) operating in parallel with three common influent surge tanks with manual screening and grit removal, aeration, secondary clarification, and chlorination with a splitter box side stream from each plant. The effluent either goes to the 1.0 mgd cloth filter and chlorination system for public reuse or the effluent is chlorinated and sent to the percolation/evaporation ponds. A .5 mgd sand filter system is used as a back-up system for the reuse system. Facilities also include turbidity/chlorine residual sensors and electronic diversion valves, chemical feed facilities, a 1.5 million gallon water storage tank with reclaimed high service pumping, pump back capability to the head of the plant for retreatment, and aerobic digestion of residuals. Flows at the wastewater treatment plant shall not exceed 1.535 mgd average annual daily flow (AADF), the total capacity of the disposal system (1.0 mgd percolation pond and .535 mgd public reuse/golf course). The utility is currently waiting for the renewal of its DEP operating permit, which expired on January 15, 2003.

Utility's Proposed Used and Useful

In its application, the utility asserted the wastewater treatment plant (accounts 371.3 Pumping Equipment, 354.4 Structures and Improvements, 380.4 Treatment and Disposal, and 382.4 Outfall Sewer Lines) is 77% used and useful. The utility based its used and useful determination on its DEP permitted capacity of 1.535 mgd. The utility asserted that the wastewater collection system in each development was constructed and contributed by the developers; therefore, a used and useful analysis is not necessary and the collection system should be considered 100% used and useful. The utility did not request 100% used and useful for its reuse facilities, pursuant to Section 367.0817(3), Florida Statutes, in its MFRs.

The utility provided additional information about the cost of the reuse system and incremental sizes and costs of various components of the wastewater treatment plant to help determine whether economies of scale or other analyses should be considered in evaluating used and useful. The utility indicated that all of its capacity is currently needed to fulfill DEP's redundancy requirement, pursuant to DEP Rule 62-610, Florida Administrative Code, and the Environmental Protection Agency (EPA) Reliability Class I requirements for a utility that disposes of its effluent through public access irrigation.

Approved Used and Useful

Rule 25-30.432, Florida Administrative Code, provides that the used and useful determination for a wastewater treatment plant should be based on, among other things, the DEP permitted capacity, the wastewater flows (using the same basis as the permitted capacity), an allowance for growth, infiltration and inflow, and whether the permitted capacity differs from the design capacity.

Permitted Capacity

The design capacity of the utility's wastewater treatment plant is 2.4 mgd AADF. However, the DEP permitted capacity is 1.535 mgd AADF because of the limitation of disposal capacity.

Since the utility disposes of its effluent through public access irrigation, it must meet EPA Reliability Class I redundancy requirements. Alafaya has two 1.2 mgd tanks. If one of the tanks is out of service, the remaining tank must be capable of handling the peak flow. In MFR Schedule F-6, the flows for the test year plus 5 years of growth, was about 1.18 MGD. On this basis, the second 1.2 MGD tank is necessary to provide the required redundancy. The utility looked at whether there was an economic benefit to adding a second 1.2 mgd tank rather than a .335 MGD tank, which is all that would have been required to treat the permitted treatment capacity of 1.535 mgd. The utility also looked at the potential benefits of adding three .750 mgd tanks or four .600 mgd tanks, instead of two 1.2 mgd tanks, since these are also standard sizes.

According to the utility, there were economic benefits to adding the larger 1.2 mgd plant instead of smaller incremental units. In addition, there is limited available space at the site and adding capacity in smaller steps would have required modifications of the existing system, such as modifying piping and relocating the surge tanks and digesters. Moreover, the second 1.2 mgd tank is currently needed to fulfill the EPA redundancy requirement. Therefore, we find that because this is a reuse system that must meet the EPA redundancy requirement and the system is growing, it was prudent to install the second 1.2 MGD tank and an economies of scale adjustment shall not be made.

There does not appear to be significant portions of the system that were oversized in anticipation of future growth. The utility plans to continue to modify the existing facilities (surge tanks and digester) to expand its capacity and keep up with growth. Therefore, we agree with the utility that, because of the DEP redundancy requirement and the limitation of disposal capacity, the permitted capacity of 1.535 mgd is the basis for determining the portion of the wastewater treatment plant that is used and useful.

Average Annual Daily Flow and Growth

We agree with the utility that the average annual daily flows for the test year were 964,197 gpd. Pursuant to Rule 25-30.431(2)(c), Florida Administrative Code, a growth allowance based on linear regression is included in the used and useful analysis; however, the utility made an error in its growth calculation. The utility proposed an annual growth allowance of 259 ERCs per year at 169 gpd per ERC, which would result in growth of 1,295 ERCs over a five year period (217,917 gpd). An annual growth factor 231.1 should have been used and multiplied by 5 years to obtain a five year growth allowance of 1,155.5 ERCs at 169 gpd per ERC (196,288 gpd) because the regression analysis r squared of .831 shows a good correlation with the data. The utility indicated it does not oppose our method of calculating the growth factor.

Infiltration/Inflow

Approximately 60% of the sold water is returned to the Alafaya wastewater system. This information is based on the billing analysis and assumes 80% of the water purchased (557,435,000 gallons) by the residential customers was returned as wastewater and 96% of the water purchased (22,429,000 gallons) by the commercial customers was returned as wastewater. The total water returned as wastewater was then compared to the treated wastewater (350,033,000 gallons). Infiltration/inflow does not appear to be a problem in the Alafaya wastewater collection system.

Used and Useful for Wastewater Treatment Plant

By adding the AADF of 964,197 gpd and a growth of 196,288 gpd, and dividing by the capacity of the system of 1,535,000 gpd, used and useful for the wastewater treatment plant is 75.60%. This calculation is shown in Table A below. The used and useful adjustment shall be made to Accounts 371.3 Pumping Equipment, 354.4 Structures and Improvements, 380.4 Treatment and Disposal Equipment, and 382.4 Outfall Sewer Lines.

Used and Useful for the Reuse System

The utility's original cost study included the golf course's disposal system and other components of the reuse system in account 380.4 Treatment and Disposal. At our request, the utility provided additional information regarding the cost of the reuse system. According to the utility, the wastewater plant account 380 included Phase I plant costs of $1,089,505, Phase II plant costs of $1,060,544, additional system related costs of $28,711, and $1,526,628 related to the reuse facilities. The portion of account 380 related to the reuse system shall be 100% used and useful.

Used and Useful for the Wastewater Collection System

Based on original certificate Order No. 14841, p. 3, dated September 3, 1985 in Docket No. 850209-SU, the original developer donated virtually all of the collection system. This policy of requiring the developer to donate the collection system is reflected in the utility's tariff. Therefore, a used and useful analysis is not necessary for the collection system. The wastewater collection system shall be considered 100% used and useful.

Conclusion

We have applied the above used and useful percentage to non-reuse plant with adjustments consistent with those previously approved in this Order. Corresponding adjustments have also been made to accumulated depreciation, depreciation expense, and property taxes. Accordingly, the non-used and useful plant, depreciation expense, and property taxes shall be $175,011, $28,444, and $653, respectively.

Table A

WASTEWATER TREATMENT PLANT - USED AND USEFUL DATA
Docket No. 020408-SU - Alafaya Utility, Inc.

1)	**Permitted Capacity of Plant** (Annual Average Daily Flow basis)	1,535,000	gallons per day
2)	Average Daily Flow in Maximum Month	1,012,355	gallons per day
3)	**Average Daily Flow** (12 month average - AADF)	964,197	gallons per day
4)	**Growth** (4b x 4c) x 3/4a	196,288	gallons per day

Table A

	a)	Test year Customers in ERCs:	Beginning		5,489
			Ending		5,862
			Average		5,676
	b)	Customer Growth in ERCs using Regression Analysis for most recent 5 years including Test Year		231.1	ERCs
	c)	Statutory Growth Period		5	Years
5)		Excessive Infiltration or Inflow (I&I)		0	gallons per day
		a)Total I&I:		0	gallons per day
		Percent of Average Daily Flow		0	
		b)Reasonable Amount (10% of average Daily Flow)		96,420	gallons per day
		c)Excessive Amount		0	gallons per day

USED AND USEFUL FORMULA

[(3)+(4)-(5)]/(1) = 75.60% Used and Useful

G. Working Capital

Rule 25-30.433(2), Florida Administrative Code, requires Class A utilities to use the balance sheet approach to calculate the working capital allowance. According to its filing, Alafaya utilized the balance sheet approach and calculated a working capital allowance of $112,900; however, as discussed below, several adjustments to the utility's working capital balance are necessary.

Cash, Accounts Payable, and Miscellaneous Deferred Debits

In Audit Exception No. 7, our staff auditors stated that cash should be included under current assets. According to its MFRs, the utility did not include any cash in its working capital allowance. As such, the staff auditors included Alafaya's cash allocation of $10,046 from its parent company. The auditors also stated that accounts payable to associated companies of $293,768 should be excluded. Because the utility is utilizing its parent's capital structure to determine its cost of capital, we agree that the affiliated accounts payable balance is excluded from working capital. Additionally, the staff auditors stated that the utility's miscellaneous deferred debits should be decreased by $1,735, to reconcile the utility's MFR balance with its general ledger balance. The utility did not respond to these adjustments. Based on the above, we find that the working capital allowance shall be increased by $302,079.

Other Accounts Receivable

In Audit Exception No. 10, the staff auditors recommended reclassifying an $865 security deposit for electric service from Purchased Power to Other Accounts Receivable. In its response to the audit, Alafaya did not address this adjustment. To reclassify the security deposit, we find that working capital shall be increased and O&M expenses reduced by $865.

Miscellaneous Deferred Debits Associated with Alafaya's 1995 Certificate Amendment Case

In Audit Disclosure No. 1, our staff auditors stated that the utility's general ledger reflects a net unamortized balance of $196,949, which represents legal and engineering fees and employee time associated with the utility's 1995 certificate extension and 1996 reuse proceeding. The staff auditors also stated that the test year O&M expenses included amortization of $21,852 for these miscellaneous deferred debits. We have reviewed the invoices for the above miscellaneous deferred debits. We find that the costs associated with the reuse proceeding were properly recorded, but the costs associated with the certificate docket were not. Based on our analysis, the total net unamortized balance associated with the certificate case was $162,372, and the test year expenses included amortization of $20,917.

The costs associated with the certificate case were regulatory commission expenses and, as such, were non-recurring costs. Consistent with Rule 25-30.433(8), Florida Administrative Code, these costs should have been amortized over five years. The certificate case was closed on February 5, 1998. If the company had properly accounted for these amounts, the costs would have been completely amortized in 2002. Since the PAA rates in this docket go into effect in 2004, we find that it is inappropriate to include any of the cost associated with the certificate docket in working capital or test year expenses. Based on the above, we find that miscellaneous deferred debits are reduced by $162,372 and O&M expenses are reduced by $20,917.

DEP Operating Permit

On October 23, 2003, the utility provided an executed contract for engineering costs of $11,575 in expenses to renew its DEP operating permit. As stated previously, the utility's DEP operating permit expired on January 15, 2003, and, according to DEP, an operating permit will be issued shortly. Based on our review, the utility did not include any unamortized balance in working capital for the operating permit that expired in January 2003. Since this pro forma expense is known and measurable, we find that it would be appropriate to recognize the expense for ratemaking purposes in this docket. Since the DEP operating permits have to be renewed every five years, this pro forma expense shall be amortized over a five-year period. Based on the above, we find that working capital shall be increased by $712 on a 13-month average basis, and O&M expenses shall be increased by $2,315 ($11,575 divided by 5) to amortize the expenses to renew the utility's DEP operating permit.

Other Miscellaneous Deferred Debits

Earlier in this Order, we found that two projects, which the utility had capitalized to plant, were non-recurring expenses that should have been amortized over five years. Specifically, we found that miscellaneous deferred debits would be increased by $5,079 on a 13-month average basis.

Conclusion

Based on the above, we find that the appropriate working capital allowance is $259,263. As a result, working capital shall be increased by $146,363. Further, we find that O&M expenses shall be decreased by $19,467 (negative $865 less $20,917 plus $2,315).

H. Appropriate Rate Base

Consistent with the adjustments approved above, we find that the appropriate 13-month average rate base for the test year ending December 31, 2001, is $5,800,937. A summary of the approved rate base and adjustments is appended to this Order as Schedules 1-A and 1-B.

III. COST OF CAPITAL

In its MFRs, the utility used the debt and equity ratios of its parent, UI, to prorate Alafaya's share of the parent's capital. The utility reflected accumulated deferred income taxes that are specifically attributable to Alafaya, but reduced the total on a pro rata basis in its reconciliation of capital to rate base. The utility included the actual balance of customer deposits. Using the 2001 leverage formula, the utility reflected a cost of 11.05% for equity. Alafaya's requested overall cost of capital was 8.98%. As discussed below, we made several adjustments to the utility's capital structure.

Long and Short-term Debt

On MFR Schedule D-1, Alafaya stated that its parent's 13-month average long and short-term debt balances were $72,269,231 and $13,780,077, respectively, for the period ending December 31, 2001. In the affiliate transactions (AT) audit for the year ended December 31, 2001, our staff auditors stated that UI incorrectly calculated the balances for long and short-term debt. Based on the general ledger and the outstanding notes and bank statements, the staff auditors recommended that the 13-month average balances were $72,690,352 and $13,245,115 for long and short-term debt, respectively. This represents an increase of $421,121 for long-term debt and a decrease of $534,962 for short-term debt from the amounts reflected in the MFRs.

In its MFRs, Alafaya reflected cost rates of 8.82% and 0.03% for long and short-term debt, respectively. In the AT audit, the staff auditors also recommended that the 13-month average cost rates were 8.63% and 5.18% for long and short-term debt, respectively. According to its response to the AT audit, the utility agrees with our staff auditors' recommended 13-month average balances and cost rates for long and short-term debt.

We believe that pro forma capital structure adjustments are necessary to match the approved net pro forma plant of $2,895,861. It is reasonable to assume that the utility would fund plant in the same relative debt to equity ratio as the historical balances maintained by the parent. The historical 2001 test year long and short-term debt ratios were 45.80% for long-term debt and 8.35% for short-term debt. Using the historical 2001 test year long and short-term debt ratios, we find that long and short-term debt shall be increased by $1,326,467 and $241,699, respectively. The remaining amount shall be added to common equity as discussed below.

Based on the above, we find that the 13-month average balances of long-term debt shall increased by $1,747,588 and short-term debt shall be decreased by $293,262.

Common Equity

In its MFRs, Alafaya stated that its parent's 13-month average common equity balance was $73,349,305, for the period ending December 31, 2001. In the AT audit, our staff auditors recommended that the 13-month average common equity balance was $73,384,644, which represents an increase of $35,339 from the amount reflected in the MFRs. According to its response to the AT audit, the utility agrees with the staff auditors' recommended 13-month average balance. As such, the common equity shall be increased by $35,339.

Two more adjustments are appropriate to common equity. First, consistent with the historical test year rate base net reductions discussed earlier in this Order, we believe a corresponding reduction of $626,984 should be made to decrease retained earnings. Second, as discussed above, a pro forma adjustment to equity is necessary to correspond with our net pro forma plant. Thus, using the historical 2001 test year equity ratio of 45.85%, we also find that common equity shall be increased by $1,327,695.

Based on the above, we find that the common equity shall be increased by $736,050. We used the current leverage formula to calculate the ROE. See Order No. PSC-03-0707-PAA-WS, issued June 13, 2003, in Docket No. 030006-WS, In Re: Water and wastewater industry annual reestablishment of authorized range of return on common equity for water and wastewater utilities pursuant to Section 367.081(4)(f), F.S., which was consummated by Order No. PSC-03-0799-CO-WS, issued July 8, 2003. Using an equity ratio of 45.85%, the utility's return on equity shall be 11.47%, with a range of 10.47% to 12.47%.

Accumulated Deferred Income Taxes

In the MFRs, the 13-month average balance of accumulated deferred income taxes was specifically attributable to Alafaya, but the utility prorated that balance when reconciling its capital to rate base. Consistent with the required treatment of other UI Florida subsidiaries, only debt and equity balances are prorated in the reconciliation of the capital structure. Accordingly, we find that the entire amount of accumulated deferred income taxes shall be included in the calculation of the utility's overall cost of capital, instead of a prorated amount. In addition, consistent with plant adjustments approved earlier in this Order, we believe corresponding adjustments to accumulated deferred income taxes are necessary. First, using the historical 2001 test year ratio of accumulated deferred income taxes to net plant, we find that accumulated deferred income taxes shall be increased by $116,187. Second, consistent with our adjustment to correct accumulated depreciation for the utility's use of incorrect rates, a corresponding adjustment of $427,393 shall be made to decrease accumulated deferred income taxes.

Further, on March 9, 2002, the Job Creation and Work Assistance Act of 2002 was signed into law. As a result, a special tax depreciation allowance was created to allow the recovery of a portion of the cost of qualified property. The new law provided for an additional first-year depreciation deduction equal to 30% of the adjusted basis of qualified property placed into service between September 10, 2001, and September 11, 2004. In response to a data request, the utility indicated that it plans to claim this special depreciation allowance for its plant additions placed into service during this period. The result of claiming this allowance will be a greater difference between book and tax depreciation, which in turn will increase the credit balance of accumulated deferred income taxes in the utility's capital structure. This impact on accumulated deferred income taxes is a known and measurable change that must be recognized in this proceeding.

As discussed earlier, we have approved the inclusion of pro forma plant additions in the amount of $2,939,504. Based on our approved used and useful percentage, the total used and useful amount of pro forma plant is $2,926,232. As a corresponding adjustment, Alafaya's accumulated deferred income taxes shall be increased by $330,342, as illustrated in the following table:

Used and Useful Special Depreciation Qualified Plant Additions	$2,926,232
Multiply by 30% First Year Deduction	.30
U&U Special Depreciation Allowance	$877,870
Multiply by 37.63% Composite Income Tax Rate	.3763
U&U Accumulated Deferred Income Taxes Impact	$ 330,342

Based on the above, we find that the appropriate amount of accumulated deferred income taxes for Alafaya shall be $517,298, which represents an increase of $19,136.

Conclusion

Based on the above, we find that the 13-month average balances of long-term debt and common equity shall increased by $1,747,588 and $736,050, respectively. We find that short-term debt shall be decreased by $293,262 to reflect the appropriate 13-month average balance. We find that the appropriate cost rates for long and short-term debt are 8.63% and 5.18%, respectively. We find that Alafaya's total accumulated deferred income taxes shall be included in the calculation of the utility's overall cost of capital with no proration. Further, we find that the appropriate amount of accumulated deferred income taxes for Alafaya shall be $517,298, which represents an increase of $19,136. The return on equity shall be 11.47%, with a range of 10.47% to 12.47%. Based on the above, we find that the appropriate overall cost of capital is 8.72%, with a range of 8.31% to 9.13%. Schedule No. 2-A shows the components, amounts, and cost rates associated with the capital structure for the test year. Schedule 2-B reflects our approved adjustments. Both schedules are appended to this Order.

IV. NET OPERATING INCOME

A. Annualized Revenues

In Audit Exception No. 9, the staff auditors stated that the total gallons for the 3 inch and 4 inch meters recorded in MFR Schedule E-2 were understated, which in turn understated test year revenues by $4,212. In its response to the audit, Alafaya did not address this adjustment. Based on the above, we find that test year revenues shall be increased by $4,212.

B. Pro Forma Reuse Revenues

According to its filings, Alafaya reflected no residential reuse revenues during the 2001 test year. By letter dated March 19, 2003, the utility stated that it began providing residential reuse service to the Ekana Green and Waverlee Woods subdivisions in April 2002. The Ekana Green subdivision has 82 homes, and the Waverlee Woods subdivision has 235 homes. Currently, Alafaya is providing reuse service to 55 residences within these two subdivisions.

On October 27, 2003, the utility completed the reuse main extension which allowed The Sanctuary at River Oaks and Live Oak developments to receive reuse water. These developments have approximately 500 homes built currently. During a conference call on December 15, 2003, Alafaya stated that as of that date four homes are ready to be connected, 12 more are being connected, and 95 service applications have been received. To properly reflect current and projected reuse revenues, we have used these participation numbers to impute residential reuse revenues.

In this Order, we approve a $6.00 monthly flat rate for residential reuse and a $5.00 residential reuse availability charge. Based on these rates, we have calculated total projected residential reuse revenues to be $51,012. Thus, we find that a $51,012 pro forma residential reuse revenue adjustment shall be made.

On MFR Schedule E-2, the utility reflected $14,237 in general service reuse revenues. By letter dated March 19, 2003, Alafaya stated that the golf course normally utilizes approximately 100,000 gallons on an average daily basis. This equates to 36,000,000 gallons on a yearly basis. In this Order, we approve a reuse general service gallonage charge of $0.25 per 1,000 gallons, and we believe that general service reuse consumption will double by reducing the gallonage charge from $0.60 to $0.25. Using the typical annual gallons above, we have projected that general reuse revenues will increase to $18,250 ((36,000,000 gallons * 2) multiplied by $0.25 per 1,000 gallons). This represents an increase of $4,013 over test year reuse general service revenues for the golf course of $14,237.

Based on the above, we find that reuse revenues shall be increased by $55,025 to reflect current and projected reuse consumption.

C. Salaries and Payroll Taxes

In its filing, the utility decreased test year salaries by $32,641 in order to annualize salaries at 2002 pay rates. Alafaya also increased test year pension and benefits by $38,259 to annualize 2002 levels of pension and benefits expenses. The utility also made a corresponding adjustment to increase test year payroll taxes by $18,197 to reflect allocated payroll tax expenses for 2002.

In Audit Exception No. 10, the staff auditors stated that the utility incorrectly computed the annualized salary expense adjustment by failing to include $18,662 of historical WSC salary expenses in its calculations. In addition, Alafaya incorrectly computed the annualized pension and benefits expense adjustment by failing to include $70,531 and $12,799 of the historical operator and Florida office pension and benefits, respectively. The utility's pension and benefits expense adjustment was also incorrect because it overstated the historical WSC pension and benefits by $157. Further, in Audit Exception No. 13, the staff auditors stated the utility incorrectly computed the payroll tax expense adjustment by failing to include $27,773 for a historical operator, office, and WSC payroll taxes in its calculations. These errors caused Alafaya to overstate its payroll tax adjustment by $27,773.

In its response to the audit, Alafaya did not address these adjustments. As such, we find that these adjustments are appropriate. Thus, we find that salaries and pension and benefits shall be reduced by $18,662 and $83,173, respectively. In addition, we find that payroll taxes shall be reduced by $27,733.

D. Lack of Support for Expenses

In Audit Exception No. 10, our staff auditors recommended removing $4,699 in O&M expenses due to lack of support. Those expenses related to Sludge Removal, Materials and Supplies, Contractual Services – Legal, and Transportation. The utility provided invoices totaling $4,199 in its response to the above audit adjustment. Based on our review, we believe that the utility has supported these expenses. Thus, we find that only $500 for Materials and Supplies shall be disallowed as unsupported.

E. Allocated Expenses

UI, the parent, through its subsidiary WSC, allocates common costs, including billing costs to all of its subsidiary utilities. Alafaya's allocated share of common O&M expenses was $88,746. In Audit Exception No. 11, the staff auditors believe that the Alafaya allocated WSC O&M expenses are overstated by $10,859, based on its customer ratio allocation. In addition, the staff auditors recommended that several expense items should be removed because the utility did not provide support or incorrectly charged expenses to Alafaya. These recommended audit adjustments are based on the Affiliate Transaction (AT) audit of WSC.

In its response to the audit, the utility disputed only one of the adjustments recommended by the staff auditors, which was the removal of finder's fees. According to Audit Exception No. 5 in the AT audit, the company provided finder's fees for informing the company about systems that could be purchased. The staff auditors believed that these costs should have been charged to the acquisition costs of the system being purchased and should be removed from expenses.

In its response to the audit, Alafaya stated that the auditors were mistaken that this account related to system acquisition costs; instead, these costs related to key-employee finder's fees. The utility provided documentation to support the employee finder's fees account. The utility states that the $21,615 recorded as an expense in 2001 is comprised of amortized amounts from 1999, 2000, and 2001 additions. Also, the utility notes that all expenses are related to WSC employees and should be allocated to UI subsidiaries.

We have reviewed the utility's response and find that the employee finder's fees are reasonable and should be included. Alafaya's allocated share of these costs is $670. Thus, we find that O&M expense shall be reduced by $10,189 ($10,859 less $670). This decision is consistent with a similar adjustment we recently approved for Alafaya's sister company in Order No. PSC-03-0647-PAA-WS, issued May 28, 2003, Docket No. 020407-WS, <u>In Re: Application for rate increase in Polk County by Cypress Lakes Utilities, Inc</u>.

F. Rate Case Expense

The utility included a $110,500 estimate in the MFRs for current rate case expense. We requested an update of the actual rate case expense incurred, with supporting documentation, as well as the estimated amount to complete the case. On April 28, 2003, the utility submitted a revised estimated rate case expense through completion of the PAA process of $134,097. The components of the estimated rate case expense are as follows:

	MFR Estimated	Actual	Additional Estimated	Total
Filing Fee	$4,500	$4,500	$0	$4,500
Legal Fees	50,000	10,933	4,050	14,983
Consultant Fees	45,000	83,082	4,080	87,162
WSC In-house Fees	11,000	7,991	5,190	13,181
Miscellaneous Expense	0	9,475	4,908	14,383
Total Rate Case Expense	$110,500	$115,869	$18,228	$134,097

Pursuant to Section 367.081(7), Florida Statutes, we must determine the reasonableness of rate case expenses and shall disallow all rate case expenses determined to be unreasonable. We have examined the requested actual expenses, supporting documentation, and estimated expenses listed above for the current rate case. Based on our review, we believe several adjustments are necessary to the revised rate case expense estimate.

The first adjustment relates to costs incurred to correct deficiencies in the MFR filing. Based on our review of invoices, the utility's consultant and attorney billed a combined amount of $10,159 for correcting the MFR deficiencies. We have previously disallowed rate case expense associated with correcting MFR deficiencies because of duplicate filing costs. See Order No. PSC-01-0326-FOF-SU, issued February 6, 2001, in Docket No. 991643-SU, In Re: Application for increase in wastewater rates in Seven Springs System in Pasco County by Aloha Utilities, Inc. Accordingly, we find that $10,159 shall be removed as duplicative and unreasonable rate case expense.

The second adjustment relates to WSC miscellaneous rate case expenses. First, the utility's actual and estimated expenses for postage, paper, and envelopes associated with customer mailings were based on 6,415 customers; but, according to the utility's response to a data request, Alafaya only had 6,151 customers as of April 2003. Using the customer count of 6,151, we believe that the utility overstated these expenses by $1,139. Second, the utility estimated that copying costs for the final customer notice would be $1,871. Alafaya estimated this amount by assuming the notice would be three pages and mailed to 6,415 customers at a per page cost of $0.0972. According to the invoices provided, the actual per page cost for the interim notice was $0.0903. We also note that the interim notice was only two pages. We believe the utility has failed to support the $760 difference between the actual copying cost of the interim notice and its estimated cost of the final notice. Therefore, we find that $1,899 shall be removed as unsupported and unreasonable rate case expense.

The final adjustment relates to the costs associated with the utility's original cost study. As discussed earlier, Alafaya provided an original cost study to establish the original cost of plant assets from inception through December 31, 1994. In its study, Alafaya stated that it does not have the prior owner's accounting entries in order to support rate base indicated in the annual reports prior to the transfer. Based on our review of invoices provided, the utility's cost to complete this study was $28,791.

In a data request, we asked the utility what steps it took to obtain the prior owner's general ledgers/journals and other accounting support prior to the transfer of the utility to UI. In its response, Alafaya stated that, when UI acquires a system, its personnel always ask for the former owner's financial information during the transfer application process. Alafaya also stated that the individuals who had personal knowledge of the acquisition and who processed the transfer application are no longer employed by UI, but the utility stated that UI has no reason to believe that this practice was not followed in the acquisition of Alafaya. Further, the utility stated that the Commission has previously allowed recovery of the cost to perform an original cost study as rate case expense.

It is the utility's burden to justify its requested costs, with no exceptions made for rate case expense. Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982). Further, the Commission has broad discretion with respect to allowance of rate case expense. Florida Crown Util. Servs., Inc. v. Utility Regulatory Bd. of Jacksonville, 274 So. 2d 597, 598 (Fla. 1st DCA 1973). It would constitute an abuse of discretion to automatically award rate case expense without reference to the prudence of the costs incurred in the rate case proceedings. Meadowbrook Util. Sys., Inc. v. FPSC, 518 So. 2d 326 (Fla. 1988).

We agree that we have previously allowed the recovery of costs associated with an original cost study as rate case expense. In fact, we addressed the allowance of such costs in the 1992 limited proceeding of the utility's sister company, UIF. That proceeding established the rate base of UIF's Paradise Pointe West (PPW) water and wastewater systems. By Order No. PSC-93-0430-FOF-WS, issued March 22, 1993, in Docket No. 920834-WS, In Re: Petition for limited proceeding to increase rates to recover cost of purchased assets disallowed in Docket No. 910020-WS by Utilities, Inc. of Florida, we found the following:

> In its last rate case, the utility used an audit and an original cost study prepared by the Commission to establish rate base at the date of transfer. At the hearing, it was determined that there was no supporting or corroborative evidence to support the audit and the cost study. For that reason, the audit and cost study were ruled inadmissible, and rate base for the transferred assets was established as zero at the date of transfer. In this proceeding, the utility has developed its own original cost study to establish rate base. We believe that it is appropriate to allow the cost of preparing the original cost study in rate case expense for this proceeding. However, for ratemaking purposes, we believe that rate case expense should include only those costs that could not have been avoided had the utility presented supporting or corroborative evidence in the prior rate case.

We note that there is a key difference between the PPW and Alafaya cases. At the time of each respective transfer, PPW was a Class C utility, while Alafaya is a Class A utility. A Class A utility's books and records should be much more sophisticated than those of a Class C utility, which is also the reason it is rare for original cost studies to be required for Class A utilities and much more common for small Class C utilities. Most larger-sized utilities are financially capable of obtaining qualified accounting and bookkeeping services, even those utilities that are associated with developers. According to Alafaya's annual reports from 1987 to 1993, the prior owner retained one CPA firm to prepare its annual reports during this period. From 1987 to 1993, the utility's annual reports reflected that additional CPA firms were retained to either audit or review the records and operations of Alafaya.

Based on the above, we believe that it is likely that the previous owner had sufficient accounting records, specifically since CPA firms were retained to prepare the annual reports and to audit or review the records prior to the transfer to UI. Since no one at UI today is able to provide the original accounting records, we have to assume the documents were never obtained or were lost in the intervening years. Either way, the ratepayers should not have to bear the substantial cost incurred to support assets that easily could have been supported by advance planning. As such, we believe that the utility's cost associated with the original cost study should be treated as an acquisition cost, which is a below-the-line expense. Accordingly, we find that $28,791 of costs associated with the original cost study shall be disallowed.

Since April 2003, both our staff and the utility have spent a tremendous amount of time analyzing plant, accumulated depreciation, CIAC, and accumulated amortization of CIAC. Our staff had to reconcile the numerous differences between the primary plant account classifications in the original cost study and the utility's general ledger, annual reports, and MFRs. We have not included any additional rate case expense after the update received in April 2003. Due to the inordinate amount of time it took for both our staff and the utility to reconcile the utility's books with its MFRs, we find that no additional rate case expense is appropriate in this instance.

Therefore, we find that the appropriate total rate case expense shall be $93,360. A breakdown of the approved rate case expense is as follows:

	MFR Estimated	Utility Revised Actual &Estimated	Commission Adjustments	Total
Filing Fee	$4,500	$4,500	$0	$4,500
Legal Fees	50,000	14,983	(659)	14,324
Consultant Fees	45,000	87,162	(38,291)	48,871
WSC In-house Fees	11,000	13,181	0	13,181
Miscellaneous Expense	0	14,383	(1,899)	12,484
Total Rate Case Expense	$110,500	$134,208	($40,848)	$93,360
Annual Amortization	$27,625		($4,285)	$23,340

The approved rate case expense shall be amortized over four years, pursuant to Section 367.0816, Florida Statutes, at $23,340 per year. Based on the data provided by the utility and the adjustments approved above, we find that the rate case expense shall be reduced by $4,285. This represents the difference between the $23,340 allowed rate case expense and the $27,625 included as expenses on MFR Schedule B-10.

G. Taxes Other Than Income

After further investigation and consulting the audit report, we believe that adjustments are necessary to taxes other than income.

Regulatory Assessment Fees

In Audit Exception No. 13, the staff auditors stated that the utility recorded RAFs of $81,743 in 2001, which reflected the payment for 2000 revenues. The auditors stated that the appropriate balance of RAFs for the 2001 test year was $81,411. This represents a difference of $332. In its response to the audit, Alafaya did not address this adjustment. Thus, we find that RAFs shall be decreased by $332.

Property Tax Discounts

According to MFR Schedule B-15, the utility reflected a total test year book balance of $20,927 for real estate and tangible personal property taxes. In a data request, the staff auditors requested support documentation for this amount. In its response, the utility provided two real estate tax bills and one tax bill for tangible personal property taxes. According to these tax bills, the amount due by November 30, 2001, contained a discount. The total amount due in November for the three tax bills provided was $18,910. We believe that it is the utility's responsibility to take advantage of available discounts, and, as such, it is unfair for ratepayers to bear any additional expenses if the utility neglects to do so. See Order No. PSC-99-1917-PAA-WS, issued September 28, 1999, in Docket No. 980245-WS, In Re: Application for limited proceeding increase in water and wastewater rates in Pasco County by Aloha Utilities, Inc. Accordingly, we find that only the November due amounts shall be allowed for rate setting purposes. As such, we find that real estate and tangible personal property taxes collectively shall be decreased by $2,017.

Pro Forma Property Taxes

According to MFR Schedule B-3, the utility made an adjustment to increase property taxes by $19,840 associated with the utility's pro forma plant additions. Alafaya calculated the tax increase as follows:

Pro forma Plant Additions	$2,847,259
Less: Construction Work in Progress	(1,777,306)
Net Increase in Plant for Property Tax	$1,069,953
Millage Rate	18.5427
Utility's Pro forma Property Tax Increase	$19,840

In Audit Disclosure No. 2, our staff auditors stated that the utility's actual tangible property tax bill for 2001 was $6,974, and was calculated on an assessed value of $360,000. The staff auditors noted that the utility's net year-end plant balance as of December 31, 2001, was $10,196,672 (plant of $14,396,565 less accumulated depreciation of $4,199,983). The staff auditors stated that they were unable to determine the validity of the utility's requested tangible personal property tax adjustment, based on the information provided in its filing; however, the staff auditors did state that the utility's proposed increase to tangible personal property taxes appears to be inordinately high because it represents a 284% increase above the 2001 property taxes.

In its response to the audit, the utility stated that the millage rate was increasing to 21.4827, which represents an increase of 2.94, but Alafaya failed to explain the resulting material difference in its calculation. We agree with our staff auditors that the utility's pro forma property tax adjustment appears excessive. As a result, we find that the appropriate pro forma property taxes shall be based on the ratio of the net pro forma plant to the historical 2001 net plant. In addition, Seminole County's new millage rate of 21.4827 shall be utilized. Using this methodology, we calculated pro forma tangible personal property taxes of \$2,250. Based on the above, we find that tangible personal property taxes shall be decreased by \$17,588.

H. Test Year Operating Income

As shown on Schedule 3-A, which is appended to this Order, after applying our approved adjustments, net operating income for the test year is \$385,995. Our adjustments to operating income are listed on Schedule 3-B, which is also appended to this Order.

V. REVENUE REQUIREMENT

Alafaya requested final rates designed to generate annual revenues of \$2,125,634. These revenues exceed test year revenues by \$314,156 (or 17.34%). Based upon our findings concerning the underlying rate base, cost of capital, and operating income, we hereby approve rates designed to generate a revenue requirement of \$2,071,594. This represents a revenue increase of \$200,879, or 10.74%, over the approved test year revenues of \$1,870,715, as shown on Schedule 3-A. This increase will allow the utility the opportunity to recover its expenses and earn an 8.72% return on its investment in rate base.

VI. RATES AND RATE STRUCTURE

A. Monthly Service Rates

As discussed above, the appropriate revenue requirement is \$2,071,594. After excluding miscellaneous service and reuse revenues of \$87,470, the revenue to be recovered through rates is \$1,984,124. Alafaya's current rate structure is the base facility charge and gallonage charge with a 10,000 gallon cap for residential customers. The utility's current rate structure does not contain a differential in the gallonage charge between residential and general service. The differential is designed to recognize that approximately 80% of the residential customer's water usage will not return to the wastewater system. For multi-family and general service customers, approximately 96% of water usage is returned. This wastewater gallonage rate differential is employed by us in wastewater rate settings and is widely recognized as an industry standard. Based on the above, we find that the gallonage rate differential shall be used in this case.

The utility shall file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates shall be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), Florida Administrative Code. The rates shall not be implemented until our staff has approved the proposed customer notice, and the notice has been received by the customers. The utility shall provide proof of the date notice was given no less than 10 days after the date of the notice.

A comparison of the utility's original rates, requested rates, and approved rates is shown on Schedule 4, which is appended to this Order.

B. Appropriate Reuse Rate

Reuse rates for this utility were originally approved by Order No. PSC-98-0391-FOF-SU, issued March 16, 1998, in Docket No. 960288-SU. In that docket, we approved a rate of $0.60 per thousand gallons for the golf course, a $5.00 monthly reuse availability fee for residential customers for which reuse was available, and a $9.00 monthly flat rate for residential customers who connected to the reuse system. These rates have been increased nominally by index adjustments and the interim increase approved in this docket.

As previously discussed, the utility has had difficulty in disposing of its treated effluent. One of the options available to the utility is to increase its disposal through increased reuse consumption. This method of disposal is encouraged by both the Water Management District and the DEP. Currently, only 23% of customers who have reuse available to their home have elected to connect to the reuse system.

We believe the major barrier in customers electing reuse is the cost of connection. Although the reuse lines are in place and irrigation systems are installed, there is a cost associated with disconnecting the irrigation system from the potable line and connecting the reuse line. Previously, the utility indicated this cost could range between $500 and $600 per connection depending on the location of the irrigation system relative to the reuse line. Now, the utility has identified a contractor who will do the retrofit for between $150 and $200 per connection. Unfortunately, these connections occur on the customer's side of the meter. Pursuant to Rule 25-30.231, Florida Administrative Code, the utility is only responsible for the lines up to and including the point of delivery (in the case of water this is usually the meter).

Another barrier we believe is inhibiting more customers connecting to the reuse system is a backflow preventor maintenance charge by the City of Oviedo. The city collects a monthly charge of $5.00 for residents who have potable irrigation systems and $8.00 per month for those residents who have irrigation systems other than potable. This is an inhibiting factor over which we do not have jurisdiction.

The initial reuse rates we approved resulted in a difference of $4.00 ($9.00 - $5.00) per month between those who accepted reuse and those who did not. When the backflow preventor charge is added to the equation the "real" cost to customers for using reuse is $7.00 per month ($8.00 - $5.00 + $4.00). Since the potable water rate is $1.00 per thousand gallons ($1.50 per thousand above 10,000 gallons), customers would have to use between 4,667 gallons and 7,000 gallons of potable water for irrigation on average per month before there is a rate incentive to connecting to the reuse system. Although we do not have jurisdiction over the City's charges, we can change the utility's reuse rate to encourage consumption.

Generally, reuse rates cannot be determined in the same fashion as other water and wastewater rates. Reuse rates based on rate base and revenue requirement would typically be so high that it would be impractical to use reuse at all based on the revenue needed to supply the service. When we analyze reuse rates, we must consider the type of customer being served, and balance the disposal needs of the utility with the consumption needs of the customer.

In cases where a utility has excess reuse capacity, rates typically should be set lower to encourage customers to use reuse at a level sufficient to meet the utility's disposal needs. In cases where a utility's reuse capacity is unable to meet demand, rates should be set higher or the rate structure should be changed in order to promote conservation. In this case, the utility is unable to meet its disposal needs.

We believe that shrinking the gap between those who connect to reuse and those that do not connect to the reuse system would encourage more reuse customers. By approving a $5.00 monthly availability fee and a $6.00 flat rate for reuse, we are encouraging more customers to connect to the reuse system. Using the same analysis discussed above, the "real" monthly cost of connecting to the reuse system would be $4.00 ($1.00 difference in approved rate + $3.00 difference in the backflow preventor charge). Therefore, customers would have to use between 2,667 gallons and 4,000 gallons of potable water for irrigation on average per month before there is a rate incentive to connecting to the reuse system. We believe this rate will increase the incentive level for connection by including a broader range of users.

In Order No. PSC-98-0391-FOF-SU, issued March 16, 1998, in Docket No. 960288-SU, we contemplated eventually moving Alafaya's reuse rate to a consumption-based rate for residential service. It was anticipated that this would be the next step in a maturing reuse system to curb excessive use. At this time, excessive use is not a problem; in fact, the opposite is true. We believe that continuing a flat rate is appropriate in this case to encourage consumption.

Order No. PSC-98-0391-FOF-SU also required that the utility specify in its customer application for reuse that if, in the future, service is provided under a metered rate structure, the customer will be responsible for the cost of the meter. We believe that adding a potential meter installation fee to the cost barriers already existing may discourage future connections. As such, we find that this language shall no longer be required on the application for reuse. Currently, the rationale for implementing a consumption-based rate is to encourage conservation. We believe that at the time a consumption-based rate is implemented, the concern will have shifted from barriers to entry to conserving a resource. At that time, we can take up the issue of a meter installation charge for future customers. The cost of meters for existing customers can be considered as a utility investment and recovered through reuse and wastewater rates pursuant to Section 367.0817(3), Florida Statutes.

The utility also has a potential major user of reuse, the golf course. However, since the $0.60 per thousand gallon rate has been charged to the golf course, consumption at the golf course has dropped to half of its prior use. The golf course indicated that the $0.60 rate and the weather are restricting factors on the amount of reuse the golf course consumes. The golf course is willing to work with the utility to help dispose of the utility's reuse. The golf course has an unused two-acre site that the utility could use as a sprayfield. As a long-range project, the existing reuse irrigation system of the golf course could be modified so that it could be used in other places on the golf course where reuse currently is not being used. We believe that it is appropriate to encourage both the golf course and utility to continue negotiating these items in order to help the utility meet its disposal needs. However, even if these items are agreed to by the golf course and the utility, the $0.60 rate is still a restricting factor. Accordingly, we hereby approve a $0.25 per thousand gallon rate for the golf course. This rate is slightly less than half the existing reuse rate. This rate will allow the utility to double its consumption (back to its pre-$0.60 consumption levels) and allow for additional consumption associated with the modified reuse irrigation system. This rate shall not apply to the two-acre site that is being considered as an additional sprayfield. There shall be no charge to the golf course for this site since it will only benefit the utility.

Although there are several non-jurisdictional factors restricting reuse in this case, we believe that we can still encourage reuse through the establishment of rates. The rates approved above will counter some of the existing barriers. We also believe that these rates will encourage reuse consistent with our responsibilities pursuant to our Memorandum of Understanding with the DEP and Water Management Districts.

For the foregoing reasons, we find that the appropriate reuse rate for this utility is a $6.00 monthly flat rate for residential use and a $0.25 per thousand gallon rate for the general service golf course. The appropriate residential reuse availability charge is $5.00. The utility shall file revised tariff sheets which are consistent with our decision within one month of our final vote in this matter. The revised tariff sheets shall be approved upon our staff's verification that the tariffs are consistent with our decision. The approved rates shall 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.

C. Interim Refund

By Order No. PSC-03-0380-PCO-SU, issued on March 19, 2003, we authorized the collection of interim wastewater rates, subject to refund. Rates were increased by 2.59%, pursuant to Section 367.082, Florida Statutes. The approved interim revenue from these rates is shown below:

	Test Year Revenues	$ Increase	Revenue Requirement	% Increase
Wastewater	$1,811,478	$46,387	$1,857,865	2.56%

According to Section 367.082, Florida Statutes, any refund should be calculated to reduce the rate of return of the utility during the pendency of the proceeding to the same level within the range of the newly authorized rate of return. Adjustments made in the rate case test period that do not relate to the period interim rates are in effect should be removed. An attrition allowance and rate case expense are examples of adjustments which are recovered only after final rates are established.

In this proceeding, the test period for establishment of interim and final rates is the twelve-month period ended December 31, 2001. Alafaya's approved interim rates did not include any provisions for pro forma or projected operating expenses or plant. The interim increase was designed to allow recovery of actual interest costs, and the floor of the last authorized range for equity earnings.

To establish the proper refund amount, we calculated a revised interim revenue requirement utilizing the same data used to establish final rates. Rate case expense was excluded because this expense is prospective in nature and did not occur during the interim collection period.

Using the principles discussed above, we have calculated the revenue requirement for the interim collection period to be $2,047,154. Since the $1,857,865 revenue requirement for the interim test year is less than the revenue requirement for the interim collection period, we find that no refund is required.

D. Four-Year Rate Reduction

Section 367.0816, Florida Statues, 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 revenues associated with the amortization of rate case expense and the gross-up for regulatory assessment fees, which is $24,440. The decreased revenues will result in the rate reductions shown on Schedule No. 4, which is appended to this Order.

The utility shall file revised tariff sheets and a proposed customer notice to reflect the lower rates we approved and the reason for the reductions no later than one month prior to the actual date of the required rate reduction. The approved rates shall be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), Florida Administrative Code. The rates shall not be implemented until our staff has approved the proposed customer notice, and the notice has been received by the customers. The utility shall provide proof of the date notice was given no less than 10 days after the date of the notice.

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 amortized rate case expense.

VII. SHOW CAUSE

Rule 25-30.115, Florida Administrative Code, requires all water and wastewater utilities to maintain their accounts and records in conformance with the 1996 NARUC USOA.

Rule 25-30.450, Florida Administrative Code, states:

> In each instance, the utility must be able to support any schedule submitted, as well as any adjustments or allocations relied on by the utility. The work sheets, etc., supporting the schedules and data submitted must be organized in a systematic and rational manner so as to enable Commission personnel to verify the schedules in an expedient manner and minimum amount of time. The supporting work sheets, etc., shall list all reference sources necessary to enable

> Commission personnel to track to original source of entry into the financial and accounting system and, in addition, verify amounts to the appropriate schedules. (emphasis added)

Utilities, Inc. and its Florida subsidiaries have been cited in prior Commission Orders for failure to comply with one or both of the above-mentioned rules. See Order Nos. PSC-95-0574-FOF-WS, issued May 9, 1995, in Docket No. 940917-WS, In Re: Application for rate increase in Seminole, Orange, and Pasco Counties by Utilities, Inc. of Florida; PSC-97-0531-FOF-WU (LUSI Order), issued May 9, 1997, in Docket No. 960444-WU, In Re: Application for Rate Increase and for Increase in Service Availability Charges in Lake County by Lake Utility Services, Inc.; PSC-96-0910-FOF-WS, issued July 15, 1996, in Docket No. 951027-WS, In Re: Application for rate increase in Highlands County by Lake Placid Utilities, Inc.; PSC-98-0524-FOF-SU, issued April 16, 1998, in Docket No. 971065-SU, In Re: Application for rate increase in Pinellas County by Mid-County Services, Inc.; and PSC-00-1528-PAA-WU (Wedgefield Order) issued August 23, 2000, in Docket No. 991437-WS, In Re: Application for Increase in Water Rates in Orange County by Wedgefield Utilities Inc.

According to Audit Exception No. 14, the utility's books and records continue to not be in substantial compliance with the NARUC USOA, and the utility has not complied with Orders Nos. PSC-00-1528-PAA-WU and PSC-00-2388-AS-WU. The staff auditors stated that their discussion of the books and records could be found in Exception No. 26 of the audit for Docket No. 020071-WS.

Based on the above, it appears that Alafaya is in apparent violation of Rule 25-30.115, Florida Administrative Code, and Orders Nos. PSC-00-1528-PAA-WU and PSC-00-2388-AS-WU. At this time, we find that it is not appropriate to require that Alafaya show cause as to why it should not be fined for its apparent noncompliance because the utility's future compliance and actions has been addressed in Docket No. 020407-WS. In Docket No. 020407-WS, we approved the opening of a separate docket to address the compliance of all of UI's Florida subsidiaries with Rule 25-30.115, Florida Administrative Code. In this docket we also adjusted rate case expense to remove excessive costs incurred for poor record keeping.

VIII. PROOF OF ADJUSTMENTS REQUIREMENT

To ensure that the utility adjusts its books in accordance with our decision, Alafaya shall provide proof, within 90 days of an effective order finalizing this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made. To assist the utility, we have reflected our approved 2001 year-end plant and accumulated depreciation balance, by primary account, in Schedule No. 5, which is appended to this Order. This schedule excludes pro forma plant adjustments and the utility's WSC rate base allocation.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that Alafaya Utilities, Inc.'s application for increased wastewater rates is hereby approved as set forth in the body of this Order. It is further

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

ORDERED that Schedules 1-A, 1-B, 2-A, 2-B, 3-A, 3-B, 4, and 5 are incorporated herein by reference. It is further

ORDERED that the utility shall file revised tariff sheets and a proposed customer notice reflecting the approved rates. The approved rates shall be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code. It is further

ORDERED that the rates shall not be implemented until after the Commission staff has approved the proposed customer notice, and after the notice has been received by the customers. The utility must provide proof of the date the notice was given no less than 10 days after the date of the notice. It is further

ORDERED that the appropriate reuse rate for this utility is a $6.00 monthly flat rate for residential use and a $0.25 per thousand gallon rate for the general service golf course. The appropriate residential reuse availability charge is $5.00. The utility shall file revised reuse tariff sheets which are consistent with our decision within one month of our final vote in this matter. The revised tariff sheets shall be approved upon Commission staff's verification that the tariffs are consistent with our decision. The approved sheets shall 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. It is further

ORDERED that no refund of the interim rate increase is required. It is further

ORDERED that rates shall be reduced at the end of the four-year rate case expense amortization period as set forth in the body of this Order. The utility shall file revised tariffs and a proposed customer notice setting forth the lower rates and the reason for the reductions no later than one month prior to the actual date of the required rate 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 rates due to the amortized rate case expense. It is further

ORDERED that it is not appropriate to require the utility to show cause as to why it should not be fined for its apparent noncompliance with Rule 25-30.115, Florida Administrative

Code, because the utility's future compliance will be addressed in a separate docket opened to address the compliance of all Utilities, Inc.'s Florida subsidiaries. It is further

ORDERED that the utility shall provide proof, within 90 days of an effective order finalizing this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made in accordance with the provisions of this Order. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, except for our decision reducing rates at the end of the four-year rate case expense amortization period, declining to initiate a show cause proceeding, and requiring proof of adjustments to books, shall become final and effective upon the issuance of a Consummating Order unless an appropriate petition, in the form provided by Rule 28-106.201, Florida Administrative Code, is received by the Director, Division of the Commission Clerk and Administrative Services, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings" attached hereto. It is further

ORDERED that this docket shall remain open for Commission staff's verification that the revised tariff sheets and customer notice have been filed by the utility and approved by Commission staff. Once these actions are complete, this docket may be closed administratively, and the corporate undertaking shall be released.

By ORDER of the Florida Public Service Commission this 5th day of April, 2004.

Kay Flynn
BLANCA S. BAYÓ, Director
Division of the Commission Clerk
and Administrative Services

(S E A L)

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

As identified in the body of this order, our action, except for our decision reducing rates at the end of the four-year rate case expense amortization period, declining to initiate a show cause proceeding, and requiring proof of adjustments to books, is preliminary in nature. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, in the form provided by Rule 28-106.201, Florida Administrative Code. This petition must be received by the Director, Division of the Commission Clerk and Administrative Services, at 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on April 26, 2004. If such a petition is filed, mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing. In the absence of such a petition, this order shall become effective and final upon the issuance of a Consummating Order.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

Any party adversely affected by the Commission's final action in this matter, reducing rates at the end of the four-year rate case expense amortization period, declining to initiate a show cause proceeding, and requiring proof of adjustments to books, may request: (1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of the Commission Clerk and Administrative Services within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or (2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of the Commission Clerk and Administrative Services and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

ALAFAYA UTILITIES, INC. **SCHEDULE NO. 1-A**

SCHEDULE OF WASTEWATER RATE BASE

TEST YEAR ENDED 12/31/01

	DESCRIPTION	TEST YEAR PER UTILITY	UTILITY ADJUST-MENTS	ADJUSTED TEST YEAR PER UTILITY	COM'N ADJUST-MENTS	COM'N ADJUSTED TEST YEAR
1	UTILITY PLANT IN SERVICE	$14,109,471	$2,847,259	$16,956,730	($418,835)	$16,537,895
2	LAND	26,255	0	26,255	34,588	60,843
3	NON-USED & USEFUL COMPONENTS	0	(1,009,020)	(1,009,020)	834,009	(175,011)
4	ACCUMULATED DEPRECIATION	(4,018,476)	(37,333)	(4,055,809)	(710,003)	(4,765,812)
5	CIAC	(9,225,895)	0	(9,225,895)	(340,686)	(9,566,581)
6	AMORTIZATION OF CIAC	2,518,883	0	2,518,883	931,457	3,450,340
7	CWIP	1,777,306	(1,777,306)	0	0	0
8	WORKING CAPITAL ALLOWANCE	0	112,900	112,900	146,363	259,263
	RATE BASE	$5,187,544	$136,500	$5,324,044	$476,893	$5,800,937

	ALAFAYA UTILITIES, INC. **ADJUSTMENTS TO RATE BASE** **TEST YEAR ENDED 12/31/01**	**SCHED. NO. 1-B**
	EXPLANATION	**WASTEWATER**
	PLANT IN SERVICE	
1	To reflect the appropriate original cost of plant at 12/31/94.	($190,775)
2	To reflect the audit adjustments for 1995 to 2001. (Test year is 13-month avg.)	(399,538)
3	To reflect rate base allocation from WSC.	74,902
4	To reflect the appropriate general ledger net plant additions from 1995 to 2000.	4,330
5	To reflect the appropriate pro forma plant additions.	92,245
	Total	($418,835)
	LAND	
	To reflect the appropriate original cost of land.	$34,588
	NON-USED AND USEFUL	
	To reflect net non-used and useful adjustment.	$834,009
	ACCUMULATED DEPRECIATION	
1	To reflect the recalculation of test year accumulated depreciation from inception to 2001.	($666,361)
2	To reflect the appropriate pro forma plant additions.	(43,643)
	Total	($710,003)
	CIAC	
	To reflect the appropriate test year CIAC.	($340,686)
	ACCUM. AMORT. OF CIAC	
	To reflect the recalculation of test year accumulated amortization from inception to 2001.	$931,457
	WORKING CAPITAL	
	To reflect the appropriate working capital allowance.	$146,363

ALAFAYA UTILITIES, INC. **SCHEDULE NO. 2-A**
CAPITAL STRUCTURE
TEST YEAR ENDED 12/31/01

	DESCRIPTION	TOTAL CAPITAL	SPECIFIC ADJUST-MENTS (EXPLAIN)	PRO RATA ADJUST-MENTS	CAPITAL RECONCILED TO RATE BASE	RATIO	COST RATE	WEIGHTED COST
PER UTILITY 2001 -13-MONTH AVERAGE								
1	LONG TERM DEBT	$72,269,231	$0	($69,912,573)	$2,356,658	44.26%	8.82%	3.90%
2	SHORT-TERM DEBT	13,780,077	0	(13,330,644)	449,433	8.44%	0.03%	0.00%
3	PREFERRED STOCK	0	0	0	0	0.00%	0.00%	0.00%
4	COMMON EQUITY	73,349,305	0	(70,957,714)	2,391,591	44.92%	11.05%	4.96%
5	CUSTOMER DEPOSITS	110,199	0	0	110,199	2.07%	6.00%	0.12%
6	DEFERRED INCOME TAXES	498,163	0	(482,000)	16,163	0.30%	0.00%	0.00%
7	DEFERRED ITC'S	0	0	0	0	0.00%	0.00%	0.00%
8	**TOTAL CAPITAL**	$160,006,975	$0	($154,682,931)	$5,324,044	100.00%		8.98%
PER COMMISSION 2001 - 13-MONTH AVERAGE								
9	LONG TERM DEBT	$72,269,231	$1,747,588	($71,647,093)	$2,369,726	40.85%	8.63%	3.53%
10	SHORT-TERM DEBT	13,780,077	(293,262)	(13,055,020)	431,794	7.44%	5.18%	0.39%
11	PREFERRED STOCK	0	0	0	0	0.00%	0.00%	0.00%
12	COMMON EQUITY	73,349,305	736,050	(71,713,436)	2,371,920	40.89%	11.47%	4.69%
13	CUSTOMER DEPOSITS	110,199	0	0	110,199	1.90%	6.00%	0.11%
14	DEFERRED INCOME TAXES	498,163	19,136	0	517,298	8.92%	0.00%	0.00%
15	DEFERRED ITC'S	0	0	0	0	0.00%	0.00%	0.00%
16	**TOTAL CAPITAL**	$160,006,975	$2,209,512	($156,415,550)	$5,800,938	100.00%		8.72%

	LOW	HIGH
RETURN ON EQUITY	10.47%	12.47%
OVERALL RATE OF RETURN	8.31%	9.13%

ALAFAYA UTILITIES, INC. **SCHED. NO. 2-B**
ADJUSTMENTS TO CAPITAL STRUCTURE
TEST YEAR ENDED 12/31/01

	EXPLANATION	WASTEWATER
	LONG TERM DEBT	
1	To reflect appropriate 13-month average balance.	$421,121
2	To reflect the corresponding impact of net pro forma plant additions.	1,326,467
	Total	$1,747,588
	SHORT-TERM DEBT	
1	To reflect appropriate 13-month average balance.	($534,962)
2	To reflect the corresponding impact of net pro forma plant additions.	241,699
	Total	($293,262)
	COMMON EQUITY	
1	To reflect appropriate 13-month average balance.	$35,339
2	To adjust retained earnings for historical rate base adjustments.	(626,984)
3	To reflect the corresponding impact of net pro forma plant additions.	1,327,695
	Total	$736,050
	ACCUMULATED DEFERRED INCOME TAXES	
1	To reflect the corresponding impact from plant adjustments, including pro forma additions.	$116,187
2	To reflect the corresponding impact associated with the correction of depreciation rates.	(427,393)
3	Reflect impact of special depreciation allowance on U&U pro forma plant additions.	330,342
	Total	$19,136

ALAFAYA UTILITIES, INC. **SCHEDULE NO. 3-A**
STATEMENT OF WASTEWATER OPERATIONS
TEST YEAR ENDED 12/31/01

	DESCRIPTION	TEST YEAR PER UTILITY	UTILITY ADJUST-MENTS	ADJUSTED TEST YEAR PER UTILITY	COM'N ADJUST-MENTS	COM'N ADJUSTED TEST YEAR	REVENUE INCREASE	REVENUE REQUIREMENT
1	OPERATING REVENUES	$1,809,140	$316,494	$2,125,634	($254,919)	$1,870,715	$200,879	$2,071,594
							10.74%	
	OPERATING EXPENSES							
2	OPERATION & MAINTENANCE	$1,162,351	$33,243	$1,195,594	($119,769)	$1,075,825		$1,075,825
3	DEPRECIATION	150,171	(5,450)	144,721	46,880	191,601		191,601
4	AMORTIZATION	0	0	0	0	0		0
5	TAXES OTHER THAN INCOME	133,212	51,948	185,160	(59,834)	125,326	9,040	134,366
6	INCOME TAXES	60,160	61,900	122,060	(30,093)	91,967	72,189	164,156
7	TOTAL OPERATING EXPENSES	$1,505,894	$141,641	$1,647,535	($162,815)	$1,484,720	$81,229	$1,565,948
8	OPERATING INCOME	$303,246	$174,853	$478,099	($92,104)	$385,995	$119,650	$505,646
9	RATE BASE	$5,187,544		$5,324,044		$5,800,937		$5,800,937
10	RATE OF RETURN	5.85%		8.98%		6.65%		8.72%

	ALAFAYA UTILITIES, INC. ADJUSTMENTS TO OPERATING INCOME TEST YEAR ENDED 12/31/01	SCHED. NO. 3-B
	EXPLANATION	**WASTEWATER**
	OPERATING REVENUES	
1	To remove requested final revenue increase.	($314,156)
2	To reflect the appropriate amount of annualized revenues.	4,212
3	To reflect pro forma reuse revenues.	55,025
	Total	($254,919)
	OPERATION & MAINTENANCE EXPENSE	
1	To adjust for misclassified O&M expenses.	$16,507
2	To reclassify a security deposit for electric service as an accounts receivable.	(865)
3	To reflect appropriate amortization of miscellaneous deferred debits.	(20,917)
4	To amortize the expenses to renew its DEP operating permit.	2,315
5	To correct error in utility's salary adjustment.	(18,662)
6	To correct errors in the utility's pension and benefits adjustment.	(83,173)
7	To remove unsupported O&M expenses.	(500)
8	Reflect the appropriate WSC O&M allocations.	(10,189)
9	To reflect the appropriate amortization of rate case expense.	(4,285)
	Total	($119,769)
	DEPRECIATION EXPENSE-NET	
1	To reflect the recalculation of test year depreciation from inception to 2001.	$143,861
2	To reflect the recalculation of test year amort. of CIAC from inception to 2001.	(154,964)
3	To reflect the appropriate pro forma plant additions.	43,643
4	To remove the net depreciation on non-U&U plant.	14,339
	Total	$46,880
	TAXES OTHER THAN INCOME	
1	RAFs on revenue adjustments above.	($11,471)
2	To remove the property taxes on non-U&U plant.	(653)
3	To correct errors in the utility's payroll adjustment.	(27,773)
4	To reflect the appropriate historical RAFs.	(332)
5	To reflect the appropriate historical real estate and tangible personal property taxes.	(2,017)
6	To reflect the appropriate pro forma tangible personal property taxes.	(17,588)
	Total	($59,834)
	INCOME TAXES	
	To adjust to test year income tax expense	($30,093)

ALAFAYA UTILITIES, INC. **SCHEDULE NO. 4**
WASTEWATER MONTHLY SERVICE RATES
TEST YEAR ENDED 12/31/01

	Rates Prior to Filing	Commission Approved Interim	Utility Requested Final	Commission Approved Final	Four-Year Rate Reduction
Residential Service					
Base Facility Charge:					
All meter sizes	$12.85	$13.18	$15.08	$14.45	$0.17
Gallonage Charge - Per 1,000 gallons (10,000 gallon cap)	$1.76	$1.81	$2.07	$1.92	$0.02
General Service					
Base Facility Charge:					
Meter Size:					
5/8" x ¾"	$12.85	$13.18	$15.08	$14.45	$0.17
1"	$32.15	$32.98	$37.70	$36.12	$0.43
1-1/2"	$64.29	$65.95	$75.40	$72.25	$0.85
2"	$102.86	$105.52	$120.64	$115.59	$1.36
3"	$205.72	$211.04	$226.20	$231.19	$2.73
4"	$321.45	$329.77	$377.00	$361.23	$4.26
Gallonage Charge, per 1,000 Gallons	$1.76	$1.81	$2.07	$2.30	$0.03
Reuse Service					
Monthly Residential Availability Charge	$5.04	$5.17	$5.91	$5.00	N/A
Monthly Residential Flat Rate	$9.07	$9.30	$10.64	$6.00	N/A
General Service Gallonage Charge	$0.60	$0.62	$0.70	$0.25	N/A
		Typical Residential Bills			
5/8" x ¾" meter					
3,000 Gallons	$18.13	$18.61	$21.29	$20.21	N/A
5,000 Gallons	$21.65	$22.23	$25.43	$24.05	N/A
10,000 Gallons	$30.45	$31.28	$35.78	$33.65	N/A
(Wastewater Gallonage Cap - 10,000 Gallons)					

ALAFAYA UTILITIES, INC.			SCHEDULE NO. 5
STAFF RECOMMENDED 2001 YEAR-END PLANT BALANCE			
ACCT NO.	ACCOUNT NAME	PLANT BALANCE	ACCUMULATED DEPRECIATION BALANCE
351	Organization	$37,784	$5,195
352	Franchises	0	0
353	Land and Land Rights	60,843	0
354	Structures and Improvements	1,436,537	248,939
355	Power Generation Equipment	49,113	9,025
360	Collection Sewers – Force	929,797	148,982
361	Collection Sewers – Gravity	4,462,978	953,373
362	Special Collecting Structures	0	0
363	Services to Customers	552,044	186,338
364	Flow Measuring Devices	0	0
365	Flow Measuring Installations	0	0
366	Reuse Services	3,047	(1,349)
367	Reuse Meters and Meter Installations	8,543	1,068
370	Receiving Wells	0	0
371	Pumping Equipment	929,993	722,727
374	Reuse Distribution Reservoirs	127	(1,259)
375	Reuse Transmission and Distribution System	193,380	6,783
380	Treatment and Disposal Equipment	4,899,161	3,003,515
381	Plant Sewers	0	0
382	Outfall Sewer Lines	0	0
389	Other Plant Miscellaneous Equipment	0	0
390	Office Furniture and Equipment	14,840	(22,820)
391	Transportation Equipment	49,356	(94,965)
392	Stores Equipment	0	0
393	Tools, Shop and Garage Equipment	54,396	(18,148)
394	Laboratory Equipment	4,669	(7,384)
395	Power Operated Equipment	0	0
396	Communication Equipment	2,930	1,849
397	Miscellaneous Equipment	0	0
398	Other Tangible Plant	71,216	(297,926)
	Total Wastewater Plant (1)	$13,760,755	$4,843,943

Notes: (1) Excludes Pro forma Plant Adjustments and WSC rate base allocation.