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August 5, 2008

VIA HAND DELIVERY

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08 AUG -5 PM 2:49
COMMISSION
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Ann Cole, Director
Division of Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399

Re: Aloha Utilities, Inc.; Docket No. 060122-WU
Application for Limited Proceeding Increase in Water Rates in Pasco County
Our File No. 26038.49

Dear Ms. Cole:

Enclosed please find for filing the direct testimony of Stephen Watford, David Porter, PE, and Robert C. Nixon, CPA on behalf of Aloha Utilities, Inc.

Should you or any members of the Staff have any questions in this regard, please let me know.

Sincerely,

JOHN L. WHARTON
For the Firm

JLW/bsr

cc: Steve Reilly, Esquire
Jean Hartman, Esquire
Wayne Forehand

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION RECEIVED-FPSC
ALOHA UTILITIES, INC. 08 AUG -5 PM 2: 51
DOCKET NO. 060122-WU COMMISSION CLERK
APPLICATION FOR LIMITED PROCEEDING INCREASE
IN PASCO COUNTY, BY ALOHA UTILITIES, INC.
DIRECT TESTIMONY OF STEPHEN G. WATFORD

Q. Please state your name and employment address.

A. Stephen G. Watford, Aloha Utilities, Inc., 6915 Perrine Ranch Road, New Port Richey, Florida 34655.

Q. In what capacity are you employed by Aloha Utilities, Inc.

A. I am the Utility's President.

Q. What is the purpose of your direct testimony?

A. The purpose of my testimony is to provide some background, that I believe it is important for all concerned to be aware of, regarding Aloha's need to purchase bulk water from Pasco County. I know that over the last few years, several new Commissioners and Commission staff have either begun to work for the Commission or become involved in proceedings involving Aloha, and they may not be aware of some of this background.

Q. What is the relevant background as you have described it?

A. I think the best way for me to proceed is just to provide a narrative of events which explains the need for this rate increase and how we arrived where we are with regard to this case and Aloha's needs for the purchased water which is the subject of Aloha's application.

On April 27, 1999, the SWFWMD issued a WUP to Aloha for its wells with

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1 a total allowed annual average quantity of 2.04 mgd and a peak month
2 quantity of 2.47 mgd. The permit noted that "the quantities are unchanged
3 from the previously permitted quantities" and that "the permitted
4 withdrawals will serve a portion of the population of this service area, but
5 the quantities do not meet all of the present demand or the future demand
6 within the service area".

7 On February 5, 2001, Aloha filed a Limited Proceeding rate
8 increase request for its Seven Springs water system, and projected that it
9 would purchase 421,860,000 gallons annually from Pasco County, with a
10 pro forma adjustment of \$739,013. Aloha argued that the primary reason
11 for filing its rate case was because Aloha must obtain all the water above
12 its SWFWMD permit level from Pasco County. Aloha pointed out that
13 SWFWMD had also refused to allow an increase in the permit withdrawal
14 levels, leaving Aloha with no choice but to purchase additional water from
15 Pasco County. The Public Service Commission rejected this request and
16 instead ordered the utility to file a general rate increase request. On
17 August 10, 2001, Aloha complied and filed the general rate increase
18 request. Despite the fact that there were hundreds of thousands of dollars
19 spent litigating the case, there was never any issue as to whether Aloha
20 had any alternative for the purchase the bulk water from Pasco County to
21 meet its present and future needs. Staff never took the position that there
22 was any such alternative. Aloha maintained that there was no such
23 alternative. Neither OPC nor any representative of the customers ever
24 took the position that there was any such alternative. The Water

1 Management District witness testified that there was no other alternative.
2 Despite this, Order No. PSC-02-0593-FOF-WU disagreed and found that
3 "Aloha has not sustained its burden of proof" and that "no evidence was
4 presented to indicate whether or not the purchase of water from Pasco
5 County is a cost-effective alternative".
6 It is notable that, in an exhibit filed by SWFWMD's Water Use Regulation
7 Manager at that time, John Parker P.G., stated that
8 "any demand for water by Aloha's customers which cannot be met
9 within the terms of Aloha's WUP needs to be addressed by use of
10 an alternative source of water. The only alternative source of water
11 which is currently and immediately available to Aloha is the
12 purchase of water from Pasco County . . . For the reasons stated
13 herein, the District would not authorize any further delay in requiring
14 Aloha to begin purchasing water from Pasco County".
15 Several aspects of the Commission's decision in Order NO. PSC-02-0593-
16 OF-WU were surprising, not the least of which was the fact that the
17 testimony provide by all parties in the case, including the Staff, were
18 essentially in agreement that Aloha should be granted the necessary rates
19 to purchase the needed water from Pasco County. The issue of whether
20 the purchase of the water from Pasco County was the most "cost-effective
21 alternative" was never raised in the record itself and was only the subject
22 of evidence to the extent that the Water Management District filed the
23 above-referenced exhibit clearly indicating that there was no alternative
24 source of water. Even this evidence wasn't something that was

1 responsive to a clear issue (or even a matter which had peripherally arisen
2 while the case was being litigated).

3 The denial of Aloha's requested rate increase placed Aloha in an
4 untenable position with the Water Management District, a position in which
5 it has remained to this day. Aloha, as a private entity, cannot simply
6 unilaterally raise its rates (as can any governmentally-owned utility), to
7 cover the cost of the needed bulk water to meet its present and future
8 customer demands. The District has continually indicated there is no
9 other source of water, and particularly no additional groundwater
10 available, for Aloha's needs. Hopefully, this rate increase will be approved
11 and Aloha will be able to move forward with the purchase of the bulk water
12 which it first requested in the prior rate case over seven years ago.

13 Aloha thereafter provided to the Commission and OPC a report detailing
14 its attempts to located alternative water sources in order to conform to the
15 maximum limits of its Water Use Permit while meeting the water supply
16 needs of its existing and future customers. Based upon that report and
17 upon the previous information provided to the Commission in Docket No.
18 020896-WS, the Commission found that Aloha has now complied with the
19 requirements of Order No. PSC-02-0593-FOF-WU with regard to the
20 further issues that needed to be analyzed and information that needed to
21 be produced by Aloha to demonstrate that the purchase of water from
22 Pasco County is the most cost effective alternative for obtaining additional
23 water resources as required by pages 52 and 53 of that 2002 Order.

24 Without going into all the details, suffice it to say that from 2002 until the

1 PSC's issuance of the Order Approving Settlement Agreement (Order No.
2 PSC-06-0270-AS-WU), Aloha operated under the cloud of the threat of
3 deletion of part of its service territory as a result of a proceeding initiated
4 by the Commission at the urging of several customers. During this time, it
5 was impossible for Aloha to finalize or even significantly move forward
6 with its arrangements for the purchase of bulk water from Pasco County
7 because of the potential for the loss of the very customers who needed
8 that bulk water. Aloha never anticipated that the deletion proceedings
9 would be successful, but fully understood that it would not be prudent to
10 invest in the purchase of water from Pasco County while the proceedings
11 were pending.

12 In late 2006, Aloha discovered that the County would begin collecting
13 substantially higher impact fees on December 20, 2006 to be charged for
14 plant capacity. Aloha knew that these new charges would apply to the
15 plant capacity that Aloha had already contracted to reserve by way of the
16 Bulk Water Agreement with Pasco County two years earlier. Aloha
17 initiated an effort to pay the County impact fees on December 19, 2006,
18 under the then current level of charges so as to avoid incurring and
19 therefore passing on the higher charges to customers. After confirming
20 with the County that the payment of the lower charges by December 19,
21 2006 would "lock in" the capacity needed for Aloha's customers in the
22 future, Aloha entered into a stipulation with the Office of Public Counsel.
23 The Stipulation and the Order approving it, specifically found that the
24 payment of the impact fees for the bulk water service was prudent, that no

1 used and useful adjustments should be made to those fees, and that
2 Aloha should be allowed to prudently accrue the carrying costs associated
3 with the payment of the impact fees until such time as the Commission
4 approved rate relief for Aloha, and that no *used and useful adjustments*
5 should be made on the amount of those prudently incurred carrying costs.
6 Aloha represented at the agenda conference that if the Commission
7 approved the settlement at its December 19, 2006 agenda conference
8 (which was so approved) that Aloha would pay the County impact fees
9 that same day. The Commission did approve the settlement and Aloha
10 did pay the impact fees to the County.

11 If this rate increase is denied, or if insufficient rates are granted for Aloha
12 to purchase the amount of bulk water it needs to meet its present and
13 *future demands*, Aloha will remain in the untenable position in which it has
14 found itself for so many years: unable to reduce pumpage from its
15 groundwater wells to fall within the allocations in its WUP, as demanded
16 by the District, because it cannot implement rates sufficient to allow the
17 *purchase of bulk water from the only available source, Pasco County,*
18 without the authorization of the Commission.

19 It is notable that, in face to face meetings with District personnel in 2008,
20 the District has reiterated its consistent position that the groundwater in
21 and around Aloha's *service area has been "fully allocated"*, reaffirming the
22 absolute need for the purchase of this bulk water from Pasco County.

23 Another important piece of this puzzle which the Commission should be
24 aware of is that in December, 2006, Aloha borrowed \$21.745 million, in

1 anticipation of facilities upgrades required by the Water Management
2 District and the PSC. These include the agreed upon construction of
3 anion exchange, and the payment of impact fees and infrastructure costs
4 related to purchase of bulk water from Pasco County. Aloha, to date, has
5 not recovered one penny of those monies. If Aloha had not undertaken
6 this loan, it would only be in a position to secure the funds needed to
7 effectuate this bulk water change for Pasco County after completion of this
8 rate case, which would cause the current situation to remain unresolved
9 for an even longer period and likely would have had a high issuance cost
10 and interest rate and therefore a greater rate impact on Aloha's
11 customers. Aloha cannot continue to carry this debt without immediate
12 rate relief. Just as OPC and certain customer groups opposed Aloha
13 earlier attempts to secure bulk water from Pasco County, OPC and certain
14 customer representatives have opposed this rate increase. This
15 opposition comes in the face of universal agreement that purchasing the
16 bulk water from Pasco County is the only alternative for Aloha and
17 something that should be accomplished as quickly as possible. Each time
18 OPC and the customers have opposed Aloha's attempt to secure needed
19 bulk water supplies, to meet present and future customer demands, this
20 opposition has resulted in not only delay, but increased costs which
21 ultimately will be passed on to the customers.

22 Q. Do you have anything else to add?

23 A. Not at this time.

24 aloha\49\direct testimony of watford.