**BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**

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| In Re: Application for increase in water rates in Franklin County by Water Management Services, Inc. | ) ) ) ) | Docket No: 110200-WU  Filed: December 17, 2012 |

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**PREHEARING STATEMENT OF THE OFFICE OF PUBLIC COUNSEL**

The Citizens of the State of Florida (“Citizens”), through the Office of Public Counsel (“OPC”), pursuant to the Order Establishing Procedure in this docket, Order No. PSC-12-0526-PCO-WU, issued October 3, 2012, and First Order Revising Order Establishing Procedure, Order No. PSC-12-0624-PCO-WU issued November 20, 2012, hereby submit this Prehearing Statement.

APPEARANCES:

Erik L. Sayler

Associate Public Counsel

Office of Public Counsel

c/o The Florida Legislature

111 West Madison Street, Room 812

Tallahassee, Florida 32399-1400

On behalf of the Citizens of the State of Florida

**1. WITNESSES:**

The Citizens intend to call the following witnesses, who will address the issues indicated:

NAME ISSUES

Helmuth Schultz III 1, 3, 4, 5, 9, 9(a), 10, 10(a)

Denise N. Vandiver 6, 7, 14

**2. EXHIBITS:**

Through Helmuth Schultz III, and Denise N. Vandiver, CPA, the Citizens intend to introduce the following exhibits, which can be identified on a composite basis for each witness:

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| **Witness** | **Exhibits** | **Title** |
| Helmuth Schultz III | HWS-1 | Qualifications of Helmuth W. Schultz, III |
| Helmuth Schultz III | HWS-2 | NARUC USOA for Class A Water Utilities |
| Helmuth Schultz III | HWS-3 | Response to Staff Audit Request No. 9 |
| Helmuth Schultz III | HWS-4 | Staff Reclassification Summarized |
| Helmuth Schultz III | HWS-5 | Deposition Transcript: Gene Brown |
| Helmuth Schultz III | HWS-6 | Staff Audit Workpapers – Account 123 |
| Helmuth Schultz III | HWS-7 | Response to Staff Audit Request No. 27 – BMG Financial Statements |
| Helmuth Schultz III | HWS-8 | CONFIDENTIAL – BMG Financials 2007-2011 – OPC POD 14 |
| Helmuth Schultz III | HWS -9 | August 1, 2012 Gene Brown Letter |
| Helmuth Schultz III | HWS-10 | Transcript of August 2, 2012 Agenda Conference, Excerpts |
| Helmuth Schultz III | HWS-11 | Commission Staff Audit Report Cash Flow Audit |
| Helmuth Schultz III | HWS-12 | Staff Audit Workpapers Response to OPC POD 5 |
| Helmuth Schultz III | HWS-13 | Audit Workpapers Identified for SMC Investment Properties |
| Helmuth Schultz III | HWS-14 | Deposition Transcript: Bob Mitchell |
| Helmuth Schultz III | HWS-15 | Amendment 6 to DEP Loan Agreement |
| Helmuth Schultz III | HWS-16 | Auditing Standards Section 341: Going Concerns |
| Helmuth Schultz III | HWS-17 | 2010 WMSI Annual Report |
| Helmuth Schultz III | HWS-18 | CONFIDENTIAL – WMSI Financial Statements-Response to OPC POD 4 |
| Helmuth Schultz III | HSW-19 | Commission Staff July 20, 2012 PAA recommendation: Issue 15 |
| Helmuth Schultz III | HSW-20 | BMG General Ledgers – Response to OPC POD 13 |
| Helmuth Schultz III | HSW-21 | CONFIDENTIAL - $40,000 Reclassification – WMSI General Ledger |
| Helmuth Schultz III | HSW-22 | Nature of WMSI Financial Sources and Uses Document |
| Helmuth Schultz III | HSW-23 | Staff Audit Report: Rate Case, dated March 12, 2012 |
| Helmuth Schultz III | HSW-24 | Requests for RAF Payment Plans |
| Helmuth Schultz III | HSW-25 | Objections to Appraisals of BMG & Compelled Response OPC POD 12 |
| Helmuth Schultz III | HSW-26 | DEP Loan & Amendments 1 through 6 |
| Helmuth Schultz III | HWS-27 | Cash Flow Analysis of Damage Settlement |
| Helmuth Schultz III | HWS-28 | DEP Inquiry and WMSI Response |
| Helmuth Schultz III | HSW-29 | Gulf State Bank Reserve – 2006 General Ledger |
| Helmuth Schultz III | HSW-30 | WMSI and DEP Correspondence |
| Helmuth Schultz III | HSW-31 | WMSI Audited Financial Statements |
| Helmuth Schultz III | HSW-32 | Accounts Payable Aging Report |
| Helmuth Schultz III | HSW-33 | DEP Loan Amortization Schedules |
| Helmuth Schultz III | HSW-34 | Secretary of State – BMG Name Changes 1994 to Present |
| Helmuth Schultz III | HSW-35 | Excerpt from Principles of Public Utility Rates |
| Helmuth Schultz III | HSW-36 | Remaining Gain on Sale Balance |
| Denise N. Vandiver, CPA | DNV-1 | Denise N. Vandiver Resume |
| Denise N. Vandiver, CPA | DNV-2 | Prior Rate Case Expense: Payments Made |
| Denise N. Vandiver, CPA | DNV-3 | Schedule of Bills and Payments: Radey Firm |
| Denise N. Vandiver, CPA | DNV-4 | History of Payments to Radey Firm |
| Denise N. Vandiver, CPA | DVN-5 | March 2012 Letters To and From Radey Firm |
| Denise N. Vandiver, CPA | DNV-6 | Representation Letter With Radey Firm |
| Denise N. Vandiver, CPA | DNV-7 | Questions On Any Bill Dispute |
| Denise N. Vandiver, CPA | DNV-8 | Agreement to Pay Radey Firm |
| Denise N. Vandiver, CPA | DNV-9 | Justification For Two Witnesses |

**3. STATEMENT OF BASIC POSITION**

By Proposed Agency Action Order No. PSC-12-0435-PAA-WU, issued August 22, 2012 (PAA Order), the Commission approved an annual increase of $506,061. Most of the annual increase was due to the need for the Utility to replace a ground water storage tank and other pro forma plant capital expenditures. The increase along with revenues to repay the Department of Environmental Protection (DEP) were placed in an escrow account to ensure that those moneys were properly spent. Citizens chose not to protest these customer oriented protections, but instead protested other aspects of the PAA Order for the reasons set forth in its positions below and the testimony of its two expert witnesses.

First and foremost, the PAA Order failed to adequately address issues relating to the $1.2 million that the Utility advanced to the Utility owner and his associated companies. Specifically, the PAA Order failed to address the adverse impact of advancing this money and the management decisions which were and are the source of the Utility’s current financial distress. Additionally, the PAA Order failed to institute any protective measures designed to prevent further financial harm to the Utility or its customers, restore these advances for the Utility use (i.e. ensure that the Utility is repaid), or prevent future advances.

More than $1.2 million was removed from the Utility for non-utility purposes at a time when the Utility has debt which exceeds its rate base and has had difficulty paying its bills, so much so that the Utility eventually defaulted on its loan from the DEP. This default harmed the Utility. Managerial decisions regarding the loan harmed the customers by adding more than $1.1 million in interest to the DEP loan. Citizens believe that the advances made to associated companies were made for the benefit and convenience of WMSI’s president, in his personal capacity, and do not benefit the Utility or its customers. Moreover, it appears to Citizens that WMSI receives no interest for these so-called “investments” in the affiliated companies. The frequency and amount of advances raise the question whether this Utility is being prudently managed, and if not, should the Commission enter a finding of managerial imprudence. The owner has attempted to divert attention from this poor use or mismanagement of Utility funds by transferring his ownership of a holding company which was a net investor in the Utility to the Utility itself. This transfer of stock from one entity owned by the owner to another entity controlled by the owner does not erase the harmful effect of the advances. Additionally, the Utility has been unable to document that the Utility’s 100% ownership interest in Brown Management Group, Inc. can truly be valued at $1.2 million. The owner cannot demonstrate that this stock transfer fully repays what was advanced by the Utility to the owner and his associated companies. As demonstrated by the testimony of OPC witness Schultz, the adverse impact of these advances has demonstrably harmed both the Utility itself and its customers. Citizens are asking that the Commission take proactive measures to protect the Utility and its customers from continued managerial imprudence in order to ensure both the near term and long term viability of this water system.

Citizens raised three other issues in its protest. Citizens’ testimony demonstrates the Commission’s apparent failure to carry forward the remaining amortization of a $242,040 gain on sale that was recognized and approved for amortization in the last rate case. Carrying this amortization forward would result in approximately a $51,000 rate decrease for customers. Citizens further believes it is against public policy to allow the continued recovery of the rate case expense included in rates for the prior rate case after the Utility has demonstrated its willingness to stop payment for legal fees, a substantial component of the past rate case expense, in order to attempt to negotiate a lower legal bill. Removing all or some of the prior rate case expense in rates would result in a meaningful rate decrease for customers. Citizens also contest aspects of the increase in service availability charges and the failure to require that those charges be trued-up and held in escrow. These charges should reflect what is actually placed in service and should be held in escrow to be available for future capital improvements.

Last, Citizens are very concerned that the Utility is unreasonably driving up the rate case expense by being unreasonably litigious and raising eight additional issues in its cross protest, most of which ask the Commission to revisit its proposed agency action decision. Citizens do not believe the Utility carried its burden of proof to secure an adjustment for any of its protested issues.

Citizens’ positions on all the issues are set forth in more specificity below and are subject to modification based upon the evidence adduced at the January 16-17, 2013 evidentiary hearing.

**4. ISSUES**

**Issue** : What is the appropriate working capital allowance?

OPC: Because the Utility is a Class A utility, the appropriate working capital allowance should remain what was approved and established by Proposed Agency Action Order No. PSC-12-0435-PAA-WU, issued August 22, 2012 (PAA Order). This issue was protested by the Utility and the Utility failed to carry its burden of proof to change what was approved by the PAA Order. Rate case expense for protesting and losing this issue is addressed under Issue 7. (Schultz)

**Issue** : What is the appropriate rate base for the test year ended December 31, 2010?

OPC: Fall-out from other issues.

**Cost of Capital:**

**Issue** : What is the appropriate weighted average cost of capital including the proper components, amounts, and cost rates associated with the capital structure for the test year ended December 31, 2010?

OPC: The appropriate weighted average cost of capital should remain what was approved and established by PAA Order No. PSC-12-0435-PAA-WU. This issue was protested by the Utility and the Utility failed to carry its burden of proof to change what was approved by the PAA Order. Rate case expense for protesting and losing this issue is addressed under Issue 7. (Schultz)

**Net Operating Income:**

**Issue** : Should any adjustments be made to contractual services – accounting expense?

OPC: Yes. Contractual Services – Accounting expense requested in the Utility’s Minimum Filing Requirements (MFRs) should be reduced to $3,667 as established by PAA Order No. PSC-12-0435-PAA-WU. This issue was protested by the Utility and the Utility failed to carry its burden of proof regarding any change to the expense approved by the PAA Order. Rate case expense for protesting and losing this issue is addressed under Issue 7. (Schultz)

**Issue** : Should any adjustments be made to transportation expense?

OPC: Yes. Transportation expense requested in the MFRs should be reduced to $31,721 as established by PAA Order No. PSC-12-0435-PAA-WU. This issue was protested by the Utility and the Utility failed to carry its burden of proof regarding any change to the transportation expense approved by the PAA Order. Rate case expense for protesting and losing this issue is addressed under Issue 7. (Schultz)

**Issue 6**: Should an adjustment be made to rate case expense previously authorized by Order No. PSC-11-0010-SC-WU, currently being amortized in customer rates, and if so, in what amount?

OPC: Yes. This issue presents a case of first impression. To OPC’s knowledge, no other regulated utility has done what this Utility has done regarding previously approved rate case expense. This Utility previously stopped payment to its prior law firm for legal services incurred in the last rate case. This Utility indicated in writing to the law firm that it disputed its final bill contrary to statements which the Utility made to the Commission that it did not dispute the amount owed. There is no written agreement or guarantee in writing (subsequent to the original representation agreement) that the Utility will continue making payments to its prior law firm in the amount approved by Order No. PSC-11-0010-SC-WU after this contested proceeding concludes. The stopping of payment and attempts to negotiate and lower its legal bill all constitute a change in circumstances that calls on the Commission to revisit the amount of rate case expense it previously approved. Further, as demonstrated by evidence presented for Issue 10, the Utility has a history of advancing utility money that should be used for utility purposes (such as paying rate case expense) for non-utility purposes. For these reasons, the Commission should remove from rates all or a substantial portion of the legal fees previously approved by the Commission which to date remain unpaid. Further the Commission should consider removing other previously approved rate case expense for other consultants which at the time of the contested hearing still remains outstanding. (Vandiver)

**Issue 7**: What is the appropriate amount of additional rate case expense associated with the protest of Order No. PSC-12-0435-PAA-WU?

OPC: The Commission should review and remove the unreasonable rate case expense incurred for the Utility’s motion to dismiss, the unreasonable rate case expense incurred for objections to OPC’s lawful discovery requests, the unreasonable rate case expense incurred for responses opposing OPC’s motions to compel lawful discovery responses, and remove rate case expense for other unsupported and/or otherwise unreasonable rate case expense. After the unreasonable or unsupported rate case expense, the Commission should allow only 1/12 of the remaining rate case expense for each of the issues OPC protested and for each of the successfully protested Utility issues. If the Utility fails to gain an adjustment for any of its protested issues or otherwise disturb the amount approved by PAA Order No. PSC-12-0435-PAA-WU, the Commission should disallow rate case expense for each of those losing issues consistent with the Commission precedent established by Order No. PSC-94-0738-FOF-WU, issued June 15, 1994, in Docket No. 900386-WU, In re: Application for a rate increase in Marion County by Sunshine Utilities of Central Florida, Inc. As a matter of good regulatory policy, the Commission should not encourage a utility to protest a PAA order or cross protest, to up-the-ante with increased rate case expense, simply because another party protested the PAA. The Commission has discretion to determine whether it was reasonable for the Utility to cross protest the issues it protested and lost. Further, for any additional rate case expense approved, the Commission has the discretion to require quarterly reports from the Utility which show payment is being made during the four-year amortization period. (Vandiver)

**Issue 8**: Should any adjustments be made to miscellaneous expense?

OPC: Yes. Miscellaneous expense requested in the MFRs should be reduced to $72,698 as established by PAA Order No. PSC-12-0435-PAA-WU. This issue was protested by the Utility. The Utility failed to carry its burden of proof regarding any change to the miscellaneous expense approved by the PAA Order. Rate case expense for protesting and losing this issue is addressed under Issue 7.

**Issue 9**: How should the net gain on sale of land and other assets be treated?

OPC: OPC has specifically raised the issue of net gain on sale of land and other assets as framed by Issue 9(a). If Issue 9 is different and distinct from Issue 9(a), OPC supports any additional adjustments to net gain on sale of land and other assets which the Commission staff recommends so long as it benefits the customers by reducing customer rates.

**Issue 9(a)**: How should the $242,000 net gain on sale of land and other assets as determined by Order No. PSC-11-0010-SC-WU be treated in Docket No. 110200-WU? *(Added by OPC to specifically address a discrete issue protested by OPC)*

OPC: The Commission should reinstate and continue the amortization of the $242,000 net gain on sale land and other assets as determined by Order No. PSC-11-0010-SC-WU to be amortized to the benefit of the ratepayers. The PAA Order apparently omitted carrying this previously determined gain on sale forward. Since the amortization of the gain on sale approved in the last rate case did not start amortizing until after January 3, 2011 when that order was issued, there remains a little more than three years of amortization on that $242,000 gain of sale to be amortized to the benefit of the ratepayers. As shown in HWS-36, OPC calculates the remaining amount of this gain on sale to be amortized to be $153,292. If amortized over a three-year period, it would result in approximately a $51,000 per year reduction in customer rates. (Schultz)

**Issue 10**: Have the Utility’s cash advances to WMSI’s President and associated companies in the amount of $1.2 million, represented by Account 123, affected the Utility’s ability to meet its financial and operating responsibilities? If so, what was the effect, and what action, if any, should the Commission take?

*(Based upon evidence contained in the testimony and exhibits of OPC witness Schultz and Staff witness Dobiac, OPC suggests revising Issue 10. This is necessary because the adverse impact of advancing utility money for non-utility purposes occurred before, during, and after the test year and continued after the Utility ceased using Account 123 for recording these advances. Below is revised language previously agreed to by Staff and OPC for this issue.)*

**Issue 10:** Have the Utility’s advances to WMSI’s President and associated companies had any adverse impact on the Utility or its ratepayers, and if so, what action, if any, should the Commission take?

OPC: Yes. The Utility’s advances to the WMSI President and his associated companies have adversely impacted the Utility and its ratepayers as demonstrated by the testimony and exhibits of OPC witness Schultz. The advancing of utility money for those non-utility purposes has caused harm to the Utility, in that the Utility was compelled to renegotiate its Department of Environmental Protection (DEP) loan several times to miss required payments. Because of the advances to the President and his associated companies, the Utility ultimately defaulted on its DEP loan because it lacked the money to make its May 2012 loan payment. The advancing of utility money has caused the Utility to be more than 90 days past due on a number of accounts payable, including but not limited to, fees owed to its prior law firm. This failure to pay its bills could harm its credit and/or its ability to secure the services of these or other vendors in the future. The advancing of utility money has caused harm to the customers, in that the renegotiation and subsequent amendments to the DEP loan added more than $1.1 million in interest to the DEP loan, which the customers will ultimately have to pay. If the advancing of utility money for non-utility purposes is not halted, it could harm the day-to-day operation of this utility and ultimately the customers if the Utility through management decisions is unable to provide water service to the island. Based on the evidence that will be presented at hearing, the Commission should enter a finding that the actions of the Utility and its President have harmed not only the Utility’s ability to meet its financial and operating responsibilities, but also the customers as well. The Commission should also enter a finding of managerial imprudence or managerial negligence. It should institute a policy of required escrow accounts and strict oversight of the management of this utility in order to provide assurances to current and future creditors that they will be repaid. To prevent further harm, the Commission should order the Utility to stop advancing any additional money to the WMSI President and associated companies. The Commission should also establish a method for the WMSI President and associated companies to repay the money previously advanced to them. In addition, the Commission should order that the assets of Brown Management Group be retitled in the name of WMSI and remain retitled in the name of WMSI unless the Utility receives permission from the Commission to sell those assets. In addition, the Commission should order that Brown Management Group assets that do not relate to utility operations, and do not otherwise provide regular income to WMSI, to be liquidated (but only if a reasonable price can be obtained in this current economy) and the proceeds from those sales used to repay the advances first to WMSI’s President and, if any remains, to associated companies. (Schultz)

**Issue 10(a)**: Should any adjustment be made to the WMSI President’s salary?

OPC: Because of the $1.2 million of Utility money advanced to the WMSI President and associated companies, WMSI had to renegotiate its DEP loan several times even though the Commission had approved rates sufficient to allow the Utility to repay the DEP loan. These imprudent renegotiations of the DEP loan directly added more than $1.1 million in additional interest which the customers will eventually have to pay. Because the advancing of utility money for non-utility purposes was imprudent, and because adding the additional interest was not a prudent business decision, the Commission should further reduce the President’s salary in order to prevent the customers from having to pay for any of the imprudently added interest. If necessary, the Commission could look to reducing other O&M areas to help offset the imprudently added interest. (Schultz)

**REVENUE REQUIREMENT:**

**Issue 11**: What is the appropriate revenue requirement?

OPC: Fall-out from other issues.

**Issue 12**: Is a repression adjustment appropriate in this case, and, if so, what is the appropriate adjustment to make for this Utility?

OPC: Fall-out from other issues.

**Issue 13**: What are the appropriate water rates for the Utility?

OPC: Fall-out from other issues.

**Issue 14**: Should the Utility be authorized to revise certain service availability charges, and, if so, what are the appropriate charges?

OPC: The increased service availability charges requested by the MFRs should not be approved, and any rate case expense associated with the Utility’s protest of this issue should be disallowed as discussed in Issue 7. The increased charges established by the PAA Order are based on future pro forma plant yet to be trued-up and adhere to the Commission’s methodology for calculating these charges. If the Commission maintains the PAA Order approved service availability charges, the Commission should order that the service availability charges be subject to a true-up after the pro forma plant is completed. In addition, the service availability charge should be escrowed along with the pro forma increase in rates in order to assure that service availability charges will be available for future capital improvements. (Vandiver)

**Other:**

**Issue 15**: In determining whether any portion of the interim increase granted should be refunded, how should the refund be calculated, and what is the amount of the refund, if any?

OPC: If OPC succeeds on all the issues it protested, a refund of the interim increase might be required. If required, the amount should be calculated according to standard Commission practice for calculating refunds.

**Issue 16**: In determining whether any portion of the implemented PAA rates should be refunded, how should the refund be calculated, and what is the amount of the refund, if any?

OPC: If OPC succeeds on all the issues it protested, a refund of a portion the implemented PAA rates might be required. If required, the amount should be calculated according to standard Commission practice for calculating refunds.

**Issue 17**: What is the appropriate amount by which rates should be reduced four years after the established effective date to reflect the removal of the amortized rate case expense as required by Section 367.0816, F.S.?

OPC: Fall-out of rates approved by the Commission in Issue 7.

**Issue 18**: Should this docket be closed?

OPC: No. It should be held open.

**5. STIPULATED ISSUES:**

None at this time.

**6. PENDING MOTIONS:**

WMSI’s Motion for temporary protective order with regard to documents submitted in connection with OPC's First Request for Production of Documents dated October 25, 2012 is pending. In OPC’s Response to WMSI's motion for temporary protective order dated November 1, 2012, OPC expressed its position that WMSI had not justified treating the documents that are the subject of this motion as confidential. OPC notes that the testimony and exhibits of OPC witness Schultz has referenced the content of the following discovery responses which are currently subject to the Utility’s October 25, 2012, motion for temporary protective order:

Utility’s response to OPC’s First Request for Production of Documents No. 2

Utility’s response to OPC’s First Request for Production of Documents No. 4

Utility’s response to OPC’s First Request for Production of Documents No. 14

At the time this prehearing statement was filed, it is unknown whether the Utility would request confidential treatment for these responses. If the Commission has not ruled on whether the Utility’s responses to OPC’s First Request for Production of Documents Nos. 2, 4, and 14 are confidential, OPC will make the appropriate motion at the appropriate time.

No other pending motions at this time.

**7. STATEMENT OF PARTY’S PENDING REQUESTS OR CLAIMS FOR**

**CONFIDENTIALITY:**

None.

**8. OBJECTIONS TO QUALIFICATION OF WITNESSES AS AN EXPERT:**

None at this time.

**9. STATEMENT OF COMPLIANCE WITH ORDER ESTABLISHING PROCEDURE:**

There are no requirements of Order No. PSC-12-0526-PCO-WU with which the Office of Public Counsel cannot comply.

Dated this 17th day of December, 2012

J.R. Kelly

Public Counsel

s/ Erik L. Sayler

Erik L. Sayler

Associate Public Counsel

Office of Public Counsel

c/o The Florida Legislature

111 West Madison Street, Room 812

Tallahassee, FL 32399-1400

(850) 488-9330CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of the foregoing  **PREHEARING STATEMENT OF THE OFFICE OF PUBLIC COUNSEL** has been furnished by electronic mail and/or U.S. Mail to the following parties on this 17th day of December, 2012, to the following:

Martha Barrera Mr. Gene D. Brown

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