

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into potential)	DOCKET NO. 881554-WS
overearnings of REGENCY UTILITIES,)	ORDER NO. 20794
INC. in Duval County.)	ISSUED: 2-22-89

The following Commissioners participated in the disposition of this matter:

MICHAEL MCK. WILSON, Chairman
 THOMAS M. BEARD
 GERALD L. GUNTER
 JOHN T. HERNDON

ORDER ESTABLISHING A REDUCTION IN
RATE BASE, RETURN ON EQUITY
AND MONTHLY RATES

BY THE COMMISSION:

BACKGROUND

Regency Utilities, Inc. (Regency or utility) provides water and sewer service to customers in Duval County. Its last rate case, Docket No. 820314-WS, culminated in the issuance of Order No. 12008 on June 6, 1983. Regency also received a price index increase in Docket No. 850015-WS through Order No. 14070, issued on February 11, 1985.

Section 367.082, Florida Statutes, authorizes this Commission to initiate an investigation of a utility's earnings and to require a refund where the rate of return realized by the utility exceeds the range of the last authorized rate of return determined by the Commission to be fair and reasonable on a prospective basis for such utility.

A desk audit by staff of Regency's 1987 Annual Report by the Commission disclosed that while it appeared that the utility's earnings were within its authorized rate of return, Regency had a negative water rate base, and an unusually high level of funds in its Contributions-in-Aid-of-Construction (CIAC) account. Consequently, staff conducted a comprehensive investigation of Regency's financial records to determine the utility's actual earnings on its investment. Such investigation was conducted from May 7, 1988 through July 21, 1988, with 1987 being utilized as the test year for rate-making purposes.

Subsequent to our staff's informal investigation, the utility agreed with staff's conclusions in the audit report, except in the area of taxes. After further investigation, staff concurred with the utility that taxes should be removed in this instance since the utility is an "S" Corporation. At the January 3, 1989 agenda conference in which we initially considered this matter, counsel for the utility agreed to the resulting prospective reduction in rates and the new reduced return on equity. However, subsequent to the agenda conference, but prior to the issuance of our Order, it was

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discovered that an error in calculating the new sewer rates had occurred, so we reconsidered this matter at the February 7, 1989 agenda conference .

Our review of the information and our conclusions set forth therefrom, are set forth below.

RATE BASE

The audit of Regency's water and sewer rate base indicated several deficiencies in the utility's accounting methods. Prior to the audit, Regency advised that it had an average water rate base of (\$89,091) and an average sewer rate base of \$537,387. The audit report disclosed that Regency had incorrectly expensed meter purchases during the test year on which the base rates were determined. These purchases have now been removed from expenses and correctly included in plant-in-service. Further, in the utility's prior rate case, we directed that meter purchases were to be capitalized rather than expensed. Regency never made a correcting entry to its books. Therefore, the utility's rate base must be increased to incorporate this prior rate case adjustment in Regency's present rate base. The audit also determined that an old sewage treatment plant that had been reverted back to the utility was included in the utility's rate base. Since the old plant is no longer "used and useful", staff removed it from the utility's rate base. Working capital was also reduced to remove investments which earned a return from the calculation. In conclusion, utilizing a thirteen-month average and the adjustments referred to above, Regency's correct average rate base is (\$151,682) for water, and \$454,979 for sewer.

OPERATING INCOME

The audit report indicated the utility had annual operating revenues of \$231,053 for water and \$539,519 for sewer. Several adjustments were made to Regency's Net Operating Income Statement to more accurately reflect the true financial condition of the utility. First, salary and contracted services costs which were incurred outside the test year period were removed from Regency's income statement as test year expenses. Second, meter purchases which were expensed rather than capitalized were also removed from test year expenses. Third, test year expenses were reduced to remove unsupported consulting fees charged to the utility by each of its directors. Fourth, and finally, depreciation expense was adjusted to reflect the effect of the other above adjustments.

CAPITAL STRUCTURE

Regency's last authorized rate of return on equity was established at 16.35% in Docket No. 820314-WS, with a range of reasonableness of 15.35% to 17.35%. Our staff's calculations, which were agreed to by Regency, indicate that its rate of return on equity should be 12.73%, with a range of reasonableness of 11.73% to 13.73%.

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Regency's long-term debt was adjusted to reflect the utility's decision to reclassify a dividend payment to its two stockholders.

As of January 1, 1987, Regency became an "S" Corporation for federal income tax purposes. We concur with the utility that no consideration of federal income taxes, expenses, deferred income taxes, or investment tax credits is appropriate in setting Regency's prospective rates.

APPARENT OVERTURNINGS

The examination of the financial records of Regency indicates that it earned a true rate of return during the 1987 test year of 34.9% in water, and 27.73% in sewer. The utility reported gross operating revenues of \$231,053 for water, and \$539,519 for sewer. We find Regency's appropriate annual revenue requirements to be \$177,537 and \$482,753 for its water and sewer operations, respectively. Further, we find that its annual prospective revenues should be adjusted as follows:

	<u>TOTAL</u>	<u>(\$)</u> DECREASE	<u>(%)</u> DECREASE
WATER	\$177,537	\$53,563	23.18%
SEWER	\$482,753	\$56,813	10.53%

NEW RATES

The new rates to reflect the reduced revenue requirements are set forth below. The old and new rates are shown for comparison.

MONTHLY WATER RATES

Monthly Charges	<u>Present Rates</u>	<u>New Rates</u>
<u>Residential and General Services</u>		<u>Base Facility Charge</u>
Meter Size		
5/8" X 3/4"	\$ 1.22	\$.94
1"	3.05	2.34
1-1/2"	6.09	4.68
2"	9.75	7.49
3"	19.50	14.98
4"	30.46	23.40
6"	60.92	46.81
Gallage Charge per 1,000 gallons	\$.73	\$.56

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<u>Fire Hydrants</u>		<u>Monthly Charge</u>
Line Size		
2"	\$ 3.25	\$ 2.50
4"	10.15	7.80
6"	20.31	15.61
8"	32.49	24.96

MONTHLY SEWER RATES

<u>Monthly Charges</u>	<u>Present Rates</u>	<u>New Rates</u>
<u>Residential</u>		<u>Base Facility Charge</u>
All Meter Sizes	\$ 7.10	\$ 6.35
Gallage Charge per 1,000 gallons	\$ 3.02	\$ 2.70
Maximum charge at 10,000 gallons		
<u>General Service</u>		
Meter Size		
5/8 x 3/4"	\$ 7.10	\$ 6.35
1"	17.76	15.89
1-1/2"	35.51	31.77
2"	56.81	50.83
3"	113.62	101.66
4"	177.54	158.85
6"	355.07	317.68
8"	568.12	508.30
Gallage Charge per 1,000 gallons	\$ 3.02	\$ 2.70

We find that the revised tariff sheets filed by the utility accurately reflect the above reduced rates and are approved. The new rates will be effective for all meter readings on or after February 5, 1989.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the investigation into the apparent overearnings of Regency Utilities, Inc. is disposed of as set forth in the body of this order. It is further

ORDERED that Regency Utilities, Inc.'s rate base is as indicated in the body of this Order. It is further

ORDERED that the authorized return on equity is established as 12.73%. It is further

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ORDERED that the adjusted water and sewer rates contained in the body of this Order are hereby approved, and shall be effective for all meter readings on or after February 5, 1989. It is further

ORDERED that this Docket is hereby closed.

By Order of the Florida Public Service Commission
this 22nd day of FEBRUARY, 19 89.



STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

JRF