

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

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|--|----------------------|
| In re: Application of Florida Cities) | DOCKET NO. 890509-WU |
| Water Company, Golden Gate Division,) | ORDER NO. 23182 |
| for a rate increase in Collier) | ISSUED: 7-12-90 |
| County.) | |
| _____) | |

Pursuant to notice, a prehearing conference was held on Monday, July 9, 1990, before Commissioner Betty Easley, as Prehearing Officer, in Tallahassee, Florida.

APPEARANCES: KATHRYN COWDERY, Esquire, Gatlin, Woods, Carlson & Cowdery, 1709-D Mahan Drive, Tallahassee, Florida 32308
On behalf of Florida Cities Water Company

ROGER HOWE, Esquire, Office of Public Counsel, Room 801, 111 West Madison Street, Tallahassee, Florida 32399-1400
On behalf of the Citizens

MATTHEW FEIL, Esquire, Florida Public Service Commission, 101 East Gaines Street, Tallahassee, Florida 32399-0863
On behalf of Commission Staff

DAVID SMITH, Esquire, Florida Public Service Commission, 101 East Gaines Street, Tallahassee, Florida 32399-0863
Counsel to the Commission

PREHEARING ORDERI. Case Background

Florida Cities Water Company, Golden Gate Division, (Florida Cities or utility) provides water and wastewater service to an area of Naples, Florida. The utility was granted its certificates pursuant to Order No. 15608 in Docket No. 850278-WS, issued January 30, 1986. Service availability charges were grandfathered in that docket, along with rates and charges which were in existence when jurisdiction passed to the Florida Public Service Commission. As of December 31, 1989, the utility served approximately 2,000 residential water connections and 200 general service water connections, or a total of about 3,300 ERCs. The utility is a division of

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Florida Cities Water Company. The utility currently has water system capacity equal to 720,000 gallons per day (GPD). In order to meet demand associated with projected growth during the next several years, the utility initiated plans to increase the water system capacity by 500,000 GPD to a total capacity of 1,220,000 GPD.

On September 5, 1989, the utility filed an application pursuant to Sections 367.081(2), .081(3), and .082, Florida Statutes, to increase its water rates. The filing contained various deficiencies of which the utility was informed. An acceptable response from the utility was received on October 23, 1989, which became the official filing date for the application.

The utility contends that the rate increase is generally required because the adjusted test year indicates that its return on a rate base of \$4,075,207 will be 2.83 percent. The utility proposes to increase water revenues by \$560,047. This increase will result in a 11.19 percent return and amounts to an increase of approximately 76 percent. The Commission granted the utility's request to utilize a test year ending March 31, 1991, which is approximately one year after the plant expansion goes on line.

By Order No. 21902, issued September 18, 1989, the Prehearing Officer granted the utility's request to use the formula method, rather than the balance sheet method, to calculate working capital and to use a beginning and end of year balance, rather than a thirteen-month average, to calculate rate base.

By Order No. 22270, issued December 6, 1989, the Commission suspended the utility's requested rates. No interim rates were requested, and none were granted.

A customer meeting was held in the service area on January 11, 1990, at 7:00 pm. Approximately three hundred people attended, and forty-one testified.

On April 12, 1990, the Commission issued Order No. 22804 entitled "Notice of Proposed Agency Action Order Setting Final Rates and Charges," wherein Florida Cities was granted a general rate increase. However, several customers filed timely protests to this order; and on May 3, 1990, Public Counsel filed its timely protest to the order.

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On June 18, 1990, the utility filed a Notice of Placing Rates into Effect pursuant to Section 367.081(6), Florida Statutes. The rates listed on the Notice were to go into effect June 25, 1990, eight months from the official filing date established in this case.

This case is scheduled for an administrative hearing on July 18 through July 20, 1990, in Naples, Florida.

II. Prefiled Testimony and Exhibits

Testimony of all witnesses to be sponsored by Florida Cities, the Staff of this Commission (Staff), and the Office of Public Counsel (OPC) has been prefiled. All testimony which has been prefiled in this case will be inserted into the record as though read after the witness has taken the stand and affirmed the correctness of the testimony and associated exhibits. All testimony remains subject to appropriate objections. Each witness will have the opportunity to orally summarize his or her testimony at the time he or she takes the stand. Upon insertion of a witness' testimony, exhibits appended thereto may be marked for identification. After all parties and Staff have had the opportunity to object and cross-examine, the exhibit may be moved into the record. All other exhibits may be similarly identified and entered into the record at the appropriate time during the hearing.

Witnesses are reminded that, on cross-examination, responses to questions calling for a simple yes or no answer shall be so answered first, after which the witness may explain his or her answer.

III. Order of Witnesses

| <u>Witness</u> | <u>Appearing for</u> | <u>Issues</u> |
|-----------------------|----------------------|-------------------------|
| <u>Direct</u> | | |
| Antone A. Reeves, III | Florida Cities | 1 |
| Douglas T. Harrison | Florida Cities | 2-7, 9, 13-15, 17-19 |
| Hugh Larkin, Jr. | OPC | 4, 10-12, 14-16, 20, 21 |

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| <u>Witness</u> | <u>Appearing for</u> | <u>Issues</u> |
|---------------------|----------------------|------------------|
| <u>Direct</u> | | |
| Robert D. Glenn | Staff | 1 |
| <u>Rebuttal</u> | | |
| Douglas T. Harrison | Florida Cities | 8,10-12,16,20-22 |

The utility has represented that it will have Larry Griggs available to be a witness in the event that it is necessary to call him to answer any questions which cannot be answered by any of the utility's witnesses who have prefiled direct or rebuttal testimony.

IV. Basic Positions

Utility: The basic position of Florida Cities is that its application for an increase in water rates should be approved so it will have an opportunity to earn a fair and reasonable overall return on its rate base of 11.19 percent.

OPC: The Company's requested revenue increase is excessive, and CIAC and margin reserve have not properly been accounted for.

Staff: The information gathered through discovery and prefiled testimony indicates, at this point, that the utility is entitled to some level of increase. The final level cannot be determined until the evidence presented at hearing is analyzed.

V. Issues and Positions

Quality of Service

1. ISSUE: Is the utility's quality of service satisfactory?

POSITIONS

Florida Cities: Yes, the applicant's quality of water service is satisfactory. (Reeves)

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OPC: No position at this time pending customer testimony to be presented at the formal hearing.

STAFF: No position pending receipt of customer testimony.

Rate Base

2. ISSUE: What are the appropriate used and useful percentages for the water plant and distribution system?

POSITIONS

Florida Cities: The water plant and system are 100% used and useful. (Harrison)

OPC: Used and useful is excessive; however, no quantification can be provided at this time.

STAFF: The water plant and system are 100% used and useful, including a 5% margin reserve for the distribution system.

3. ISSUE: Should a margin reserve be included in the used and useful calculation? If so, what is the appropriate amount?

POSITIONS

Florida Cities: No, margin reserve should not be included in the used and useful calculations because water plant and system are 100% used and useful. (Harrison)

OPC: No, margin reserve should not be included in the used and useful calculation.

STAFF: Yes, margin reserve should be included in the used and useful calculations. There should be a 5% margin reserve for the water distribution system. There is no available capacity in the water treatment plant to be included as margin reserve.

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4. ISSUE: Should there be an imputation of CIAC to offset margin reserve? If so, what amount should be imputed?

POSITIONS

Florida Cities: There should be no imputation of CIAC since there is no margin reserve requested since the water plant and system are 100% used and useful. (Harrison)

OPC: If a margin reserve is allowed, there should be an imputation of CIAC in the amount of \$197,992. This amount is \$47,916 more than Staff's calculation, as adjustment is necessary to account for the \$363 differential between the approved main extension charge of \$1,500 and actual plant cost per lot of \$1,137. CIAC amortization should also be increased by \$1,125. (Larkin)

STAFF: Yes, CIAC of \$150,076 should be imputed for the customers included in the margin reserve with corresponding adjustments of \$3,524 to accumulated amortization of CIAC and \$3,524 to amortization expense.

5. ISSUE: Should utility plant-in-service be reduced to remove AFUDC which was accrued without a Commission-approved rate?

POSITIONS

Florida Cities: No. AFUDC is a legitimate and necessary cost of building utility plant to render water service. Removal of AFUDC would represent a confiscation of capital. (Harrison)

OPC: Agree with Staff's position.

STAFF: Yes, utility plant-in-service should be reduced by \$63,193, with a corresponding reduction of \$6,235 to accumulated depreciation and a reduction of \$2,117 to depreciation expense to reflect the removal of AFUDC which was accrued without a Commission-approved rate.

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6. ISSUE: What is the appropriate amount of working capital to include in rate base?

POSITIONS

Florida Cities: Agree with Staff's position. (Harrison)

OPC: Zero.

STAFF: Order No. 21902, issued September 18, 1989, granted the applicant's request to use the one-eighth of operations and maintenance method, rather than the balance sheet approach. The amount of working capital that should be included in rate base is one-eighth of the operating and maintenance expenses allowed in this case.

7. ISSUE: What is the appropriate level of test year rate base?

POSITIONS

Florida Cities: The appropriate level of test year rate base should be \$4,075,207. (Harrison)

OPC: This is a fall-out number.

STAFF: This is a fall-out number.

Cost of Capital

8. ISSUE: Should common equity be reduced to reflect the payment of dividends?

POSITIONS

Florida Cities: No. (Harrison)

OPC: Agree with Staff's position.

STAFF: Yes. Common equity should be reduced by \$2,357,299.

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9. ISSUE: What is the appropriate rate of return on equity?

POSITIONS

Florida Cities: The rate of return on equity should be 13.64%. (Harrison)

OPC: Agree with Staff's position.

STAFF: The rate of return on equity should be 13.35%, with a range of 12.35% to 14.35%.

10. ISSUE: Were the Series G first mortgage bonds held by the utility's parent, Consolidated Water Company, issued at "arm's length"?

POSITIONS

Florida Cities: Consolidated Water Company issued bonds to outside investors at the terms indicated for the Series G bonds shown in the MFR's. Consolidated Water Company in turn loaned a portion of the Series G money to Florida Cities at these same terms. (Harrison)

OPC: No. (Larkin)

STAFF: No position at this time.

11. ISSUE: What cost rate should be used for the Series G first mortgage bonds?

POSITIONS

Florida Cities: The cost rate reflected in the MFR's. (Harrison)

OPC: 12% is used until it can be determined whether the bonds were issued at "arm's length." (Larkin)

STAFF: No position at this time.

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12. ISSUE: What cost rate should be used for short-term debt.

POSITIONS

Florida Cities: The cost rate reflected in the MFR's.
(Harrison)

OPC: The short-term debt cost should be zero since it is
guaranteed by the parent. (Larkin)

STAFF: No position at this time.

13. ISSUE: What is the appropriate overall rate of return?

POSITIONS

Florida Cities: The appropriate overall rate of return
should be 11.19%. (Harrison)

OPC: This is a fall-out position.

STAFF: The appropriate overall rate of return should be
11.01%, with a range of 10.59% to 11.43%.

Net Operating Income

14. ISSUE: Are the utility's projections of expenses
reasonable?

POSITIONS

Florida Cities: Yes. (Harrison)

OPC: No. (Larkin)

STAFF: Yes, except as stated in Staff's position in Issue
15.

15. ISSUE: Should salaries and pension and benefit expenses be
adjusted?

POSITIONS

Florida Cities: No. The utility's projection methodology
adequately reflects anticipated salaries and pension and
benefit expenses. (Harrison)

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OPC: A dollar amount of adjustment has not been determined. However, per the 1988 audit report of Ernst & Whinney, pension costs are prepaid. If no contributions are required in the test year, then no deduction should be allowed. Pension expense should be accounted for on a pay-as-you-go basis. (Larkin)

STAFF: Yes, salaries should be reduced by \$13,883, with a corresponding reduction to payroll taxes of \$910, and pension and benefit expense should be reduced by \$2,858 to correct the utility's projection methodology.

16. ISSUE: Should miscellaneous expenses be adjusted for temporary help?

POSITIONS

Florida Cities: No. (Harrison)

OPC: Yes, miscellaneous expenses should be adjusted. The amount of the adjustment cannot be quantified at this time. (Larkin)

STAFF: No position at this time.

17. ISSUE: What is the appropriate amount of rate case expense and amortization period to be allowed?

POSITIONS

Florida Cities: The amount of rate case expense that should be allowed is estimated to be \$63,219.61, which is to be amortized over a period of four years. (Harrison)

OPC: Agree with Staff's position.

STAFF: An amount yet to be determined which should be amortized over a period of four years.

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18. ISSUE: Should taxes other than income be reduced to reflect a lower amount of property tax paid by the utility?

POSITIONS

Florida Cities: No. (Harrison)

OPC: Agree with Staff's position.

STAFF: Yes, taxes other than income should be reduced by \$3,398 to reflect a lower amount of tax paid by the utility than that included in the test year.

19. ISSUE: What is the appropriate amount of income tax expense?

POSITIONS

Florida Cities: The amount listed in the MFR's. (Harrison)

OPC: The amount listed in the MFR's is excessive. An adjustment cannot be quantified at this time.

STAFF: No position at this time.

20. ISSUE: Should revenue associated with the margin reserve be recognized?

POSITIONS

Florida Cities: No. (Harrison)

OPC: Yes. Staff has determined that the treatment plant is 100% used and useful and the distribution plant is 95% used and useful. Further, Staff partially imputed CIAC for the additional 5% as margin reserve. However, the additional customers and revenue in the margin reserve were not properly accounted for. Therefore, 132 additional customers and \$25,091 of associated revenue should be included based on the average bill as calculated in the MFR's. (Larkin)

STAFF: No.

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OTHER

21. ISSUE: Should the utility be required to file its rate case on a "stand alone" basis? (This is a mixed question of law and policy.)

POSITIONS

Florida Cities: No. (Harrison)

OPC: Yes. (Larkin)

STAFF: No position at this time.

22. ISSUE: Rule 25-30.347, Florida Administrative Code, which was in effect when the utility filed its case, required rate base computations on a 13-month average basis. Should the utility be permitted to use a simple average for its rate base in this case?

POSITIONS

Florida Cities: Yes. (Harrison)

OPC: No.

STAFF: Yes, Order No. 21902, issued September 18, 1989, granted the applicant's request to use a beginning-and-end-of-year balance rather than a thirteen-month average. Thus, the issue is already resolved.

VI. Proposed Stipulations

1. A composite adjustment should be made to increase operation and maintenance expense by \$4,481 to reflect corrections as determined by staff.
2. A reduction in the amount of \$4,571 should be made to the pro forma chemical expense.
3. The company should change to guideline depreciation rates per Rule 25-30.140, Florida Administrative Code. No further adjustments are necessary as a result of this change.

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4. Regulatory assessment fees should be increased to reflect the change from 2.5% to 4.5%, which became effective July 1, 1990.
5. The appropriate level of test year operating income is a fall-out number.
6. The total revenue requirement is a fall-out number.
7. The water rates for the utility are fall-out numbers.

VII. Exhibits

| <u>Witnesses</u> | <u>Proffered By</u> | <u>I.D. No.</u> | <u>Description</u> |
|-----------------------|---------------------|----------------------|--|
| Antone A. Reeves, III | Staff | AAR-1 | Responses to Staff's First Set of Interrog. 1-12 |
| Hugh Larkin, Jr. | OPC | HL-1 (Composite) | Recommended revenue requirement; recommended rate base; and summary of capital structure accompanying prefiled testimony |
| Douglas T. Harrison | Florida Cities | DTH-1 (Composite) | MFR's, all schedules. |
| Douglas T. Harrison | Staff | DTH-2 (Composite) | Additional accounting information transmitted by letter dated February 9, 1990. (The parties and |

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| <u>Witnesses</u> | <u>Proffered By</u> | <u>I.D. No.</u> | <u>Description</u> |
|---------------------|---------------------|----------------------|---|
| | | | Staff have stipulated as to the admission of this item.) |
| Douglas T. Harrison | Staff | DTH-3 (Composite) | Staff audit report and audit work-papers. (The parties and Staff have stipulated as to the admission of this item.) |
| Douglas T. Harrison | Florida Cities | DTH-4 | Summary and schedule of rate case expense. |

In addition to the above, Staff requests that administrative notice be taken of the following orders and rules:

| | | |
|---|---|---|
| Imputation of CIAC on Margin Reserve | - | Order No. 20434 Docket No. 871134-WS |
| Margin Reserve | - | Order No. 22843 Docket No. 890277-WS |

Rule 25-30.116, Florida Administrative Code - AFUDC

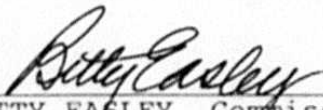
Staff reserves the right to identify exhibits for the purpose of cross-examination.

Based upon the foregoing, it is

ORDERED by Commissioner Betty Easley, as Prehearing Officer, that this Prehearing Order shall govern the conduct of these proceedings unless modified by the Commission.

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By ORDER of Commissioner Betty Easley, as Prehearing Officer, this 12th day of July, 1990.



BETTY EASLEY, Commissioner
and Prehearing Officer

(S E A L)

MF

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), 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.

Any party adversely affected by this order, which is preliminary, procedural or intermediate in nature, may request: 1) reconsideration within 10 days pursuant to Rule 25-22.038(2), Florida Administrative Code, if issued by a Prehearing Officer; 2) reconsideration within 15 days pursuant to Rule 25-22.060, Florida Administrative Code, if issued by the Commission; or 3) 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 sewer utility. A motion for reconsideration shall be filed with the Director, Division of Records and Reporting, in the form prescribed by Rule 25-22.060, Florida Administrative Code. Judicial review of a preliminary, procedural or intermediate ruling or order is available if review of the final action will not provide an adequate remedy. Such review may be requested from the appropriate court, as described above, pursuant to Rule 9.100, Florida Rules of Appellate Procedure.