

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Application for rate) DOCKET NO. 931052-SU
increase in Highlands County by) ORDER NO. PSC-94-1234-FOF-SU
HIGHLANDS UTILITIES CORPORATION.) ISSUED: October 11, 1994
_____)

The following Commissioners participated in the disposition of this matter:

J. TERRY DEASON, Chairman
SUSAN F. CLARK
JOE GARCIA
JULIA L. JOHNSON
DIANE K. KIESLING

NOTICE OF PROPOSED AGENCY ACTION

ORDER APPROVING INCREASED WASTEWATER RATES AND CHARGES

BY THE COMMISSION:

NOTICE IS HEREBY GIVEN by the Florida Public Service Commission that the action discussed herein 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.

BACKGROUND

Highlands Utilities Corporation (Highlands or utility) is a Class B utility providing wastewater services in Sebring and Lake Placid in Highlands County, Florida. Highlands has four wastewater treatment plants and service areas: Brunners, Clearview Terrace, Western Boulevard (all three in Sebring), and Pugh #1 (in Lake Placid). At December 31, 1993, the utility served approximately 1,290 customers. In 1993, the utility recorded operating revenues of \$344,018, while reporting a \$33,567 operating loss.

On May 2, 1994, the utility filed an application for approval of interim and permanent rate increases pursuant to Sections 367.081 and 367.082, Florida Statutes. The utility petitioned the Commission to process this application using the Proposed Agency Action (PAA) procedure outlined in Section 367.081(8), Florida Statutes. The utility's present rate structure was established by Order No. 18036, issued August 24, 1987.

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FPSC-RECORDS/REPORTING

The utility's application for increased rates is based on the twelve-month period ended December 31, 1993. The utility contended that its interim revenue requirement, determined in accordance with Section 367.082(5), Florida Statutes, was \$390,761. This amount exceeded annualized test year revenues by \$44,015 (12.69 percent). On July 11, 1994, we issued Order No. PSC-94-0840-FOF-SU approving an interim revenue requirement of \$380,860, for a \$12,742 (3.48 percent) increase. We approved that amount subject to refund. The utility contended that its permanent revenue requirement was \$533,025, a \$186,279 (53.72 percent) increase relative to test year revenues.

Our staff conducted a customer meeting on July 28, 1994 in Sebring, Florida, to allow customer comment with respect to the proposed increase and the quality of service.

QUALITY OF SERVICE

Our analysis of the overall quality of service provided by the utility is based upon quality of the utility's product, the operational conditions of the utility's plant and facilities, and the utility's attempt to address customer satisfaction. We have also considered customer comments, 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 three-year period.

Quality of the Product

In July, 1992, Highlands and DEP signed a consent order addressing the Western Boulevard plant's failure to meet treatment standards. It was agreed that the utility would evaluate the plant and determine the cause for not meeting standards and the modifications needed, apply to DEP for modification permits, and complete construction within 180 days. The utility was ordered to install a flow meter and implement a groundwater monitoring plan.

In March, 1993, the utility and DEP signed a consent order wherein the utility agreed to evaluate the Pugh #1 plant and determine what modifications were needed, make application to the DEP for modification permits, and complete construction within a specified time period. The utility also agreed to provide groundwater testing results for the Western Boulevard plant within thirty days.

In August, 1994, DEP and the utility signed another consent order which superseded the previous orders. The August, 1994 consent order reinforced the need for the upgrades referred to in

the two prior consent orders that had not been completed. The utility was also assessed civil penalties for violations of Section 403.161, Florida Statutes.

The Brunners and Clearview Terrace plants have achieved DEP treatment standards.

Operational Conditions

Our engineer conducted a field inspection of the four wastewater treatment plants and several lift stations on July 28, 1994. No unusual characteristics were observed and the plants appeared to be operating normally. No offensive odors were detected and visits to the plant by the operator were evident. However, as far as a plant's ability to meet treatment standards as dictated by DEP, physical observation is not sufficient; laboratory testing is required.

Customer Satisfaction

Four customers testified at the customer meeting held on July 28, 1994. One customer had several questions about what would happen to the rates if the utility was sold to the City of Sebring, and whether the utility earned revenues from the sale of its sludge. Two customers from the Brunners subdivision spoke about their flat rate of \$18.01 and testified that they preferred to be on a metered rate. Mr. Peter Ericson, the manager of Rosewood Care Center, explained that with the proposed increase his bill would increase from \$3,500 a year to \$5,000 per year. Due to internal leaks in the plumbing, he would rather have the Center's wastewater metered, rather than the water for wastewater billing. No customers commented about service inadequacies.

Upon consideration of the data in this case, we conclude that the quality of service provided by the utility is satisfactory, although compliance with the consent order issued by DEP must be achieved.

RATE BASE

Our calculation of the appropriate rate base for this proceeding is attached as Schedule No. 1-A. The adjustments to the rate base are attached as Schedule No. 1-B. Those adjustments which are self-explanatory or which are essentially mechanical are reflected on those schedules without further discussion in the body of this Order. The major adjustments are discussed below.

Used and Useful

Two service areas, Brunners and Clearview Terrace, are essentially built out. The other two service areas, Pugh #1 (Lake Placid) and Western Boulevard, are involved in consent orders with DEP and will be adding additional treatment plant to achieve better treatment standards. Both Pugh #1 and Western Boulevard are under moratorium by DEP and new connections are not permitted. The Pugh #1 plant is handling flows in excess of its capacity, while Western Boulevard is experiencing organic overloading, although only treating flows of 80 percent of its rated capacity. Neither of these plants has consistently met treatment standards.

Highlands intends to add additional treatment tanks to both the Pugh #1 and Western Boulevard plants. The most recent consent order requires the utility to complete construction of the Pugh #1 improvements by October 31, 1994, and the Western Boulevard improvements by December 31, 1994. Preliminary estimates for these improvements exceed \$200,000.

Based upon existing conditions and intended improvements, we find the used and useful percentages for all four utility plants to be 100 percent.

Margin Reserve

It has been the policy of this Commission to include a margin reserve in the used and useful calculation when a utility is experiencing growth and has unused capacity. As stated earlier, two of the utility's service areas, Brunners and Clearview Terrace, are essentially built out. During the test year Brunners added one customer and only one lot remains unconnected. In the last five years, Clearview has added only eight customers. The other two systems, Pugh #1 and Western Boulevard are under moratorium and cannot add new customers. Accordingly, we conclude that a margin reserve is not appropriate for this utility in this rate proceeding.

Adjustments Pursuant to Commission Order No. 18036

During the audit inspection, staff identified several adjustments that were required in a previous rate docket (Docket No. 861234-SU) that were not actually booked by the utility. These necessary corrections concern plant in service, accumulated depreciation, and contributions in aid of construction (CIAC). These adjustments are: a \$31,025 reduction to plant in service, a \$926 reduction to accumulated depreciation, and a \$11,933 increase

to CIAC. Accordingly, these adjustments have been included in the rate base calculation.

Retirement of Transportation Equipment

The utility retired two vehicles during the test year, but one vehicle was not retired correctly on the utility's books. To properly record this retirement, plant in service and accumulated depreciation shall be reduced by \$3,838 each, and depreciation expense shall be reduced by \$640.

Adjustment Related to Motor Home Expense

The utility's list of assets includes a \$4,000 motor home that is used for both personal and business purposes. However, according to utility personnel, this vehicle is used for business purposes only on an occasional basis. A travel log is not maintained and no allocations were attempted. Since the motor home is fully depreciated, its retirement does not affect the rate base determination. It does, however, reduce depreciation expense by \$268. Further, there were certain test year expenses that relate to ownership of this asset. These charges include \$674 for insurance and \$750 for equipment added to the motor home. We find it appropriate to remove these balances to eliminate expenditures that are non-utility in nature.

Working Capital

Pursuant to Rule 25-30.433(2), Florida Administrative Code, we have calculated working capital by using the formula approach, or the amount that equals one-eighth of operation and maintenance (O&M) expenses. The utility also used this approach but failed to consider the impact on expenses associated with pro forma expenses. Based upon our adjustments to O&M expenses, we find it appropriate to approve a \$49,546 provision for working capital.

DEP Compliance Expenses

At our September 20, 1994, Agenda Conference, the utility proposed to include certain post-test year expenditures to comply with a DEP consent order. As noted herein, DEP has required the utility to upgrade two of the wastewater treatment plants. The utility estimated that upgrading one plant will cost approximately \$51,696, and should be completed by October, 1994. The utility has expended approximately \$36,000 already. The second plant's improvements will cost approximately \$197,492. The utility stated

that including these improvements in rate base would not exceed its original revenue request.

After reviewing this request, we find it appropriate to deny the inclusion of these expenditures in this docket. This request was not included in the utility's original filing, and this information has not been analyzed. Instead, the utility may petition the Commission to address the costs of making the plant improvements by subsequently filing a request for a limited proceeding pursuant to Section 367.0822, Florida Statutes.

Test Year Rate Base

Based upon the approved test year and the adjustments made herein, we find that the appropriate rate base amount for Highlands is \$55,145.

COST OF CAPITAL

Our calculation of the appropriate cost of capital is depicted on Schedule No. 2-A, and our adjustments are contained on Schedule No. 2-B. Those adjustments which are self-explanatory or which are essentially mechanical in nature are reflected on those schedules without further discussion in the body of this Order. The major adjustments are discussed below.

The current capital structure consists of two categories: short-term debt payable to a related company, and a provision for customer deposits. Per the utility's application, a 6.99 percent interest cost is the weighted cost for intercompany loans and payables to owner interests. During the test year, the interest rate for customer deposits was 8 percent. For the purpose of establishing final rates, we have used the 6 percent interest rate that is currently prescribed for customer deposits according to Rule 25-30.311 (4)(a), Florida Administrative Code. When all of the debt components are reconciled to rate base in a pro rata fashion, which is the standard reconciliation treatment, the weighted cost of capital is 6.89 percent. Therefore, we find it appropriate to approve a 6.89 percent cost of capital provision.

In a letter dated August 12, 1994, the utility asked the Commission to consider a revised cost rate to replace the contractual 6 percent interest rate applied to certain intercompany loans. The utility reported that some monies are borrowed by the related company for subsequent use by the utility. Other intercompany loans were simply assigned a 6 percent interest rate since that rate was a conservative charge. We believe that it is not appropriate to approve a recalculation of these intercompany

loan rates. Because the rate base balance is relatively small, revising the cost of capital would cause a modest change in the revenue requirement. Furthermore, if one intercompany loan rate was revised, all intercompany or owner financed loans would need revision since the fairness of all loans would be at issue. We are reluctant to approve this recalculation since it might constitute a precedent for recalculation of all intercompany interest rates in each proceeding when intercompany debt is present. Therefore, the utility's request is denied.

Return on Equity

The utility did not request a return on equity investment since a deficit of \$425,998 presently exists in that account. Our approved rate of return of 6.89 percent likewise omits any current consideration of a return on equity investment. While this subject is not a controversial issue in this case, this Commission prefers to establish a base line return on equity investment for future rate setting purposes. Those prospective conditions include setting of interim rates in a subsequent rate case when equity investment may exist and for evaluation of possible overearnings under indexing and pass-through procedures.

We have calculated the allowed return on equity using the current leverage formula found in Order No. PSC-94-1051-FOF-WS, issued August 29, 1994. According to that Order, the appropriate return on equity is 11.34 percent.

NET OPERATING INCOME

Our calculation of net operating income is depicted on Schedule No. 3-A, and our adjustments are contained in Schedule No. 3-B. Those adjustments which are self-explanatory or which are essentially mechanical in nature are reflected on those schedules without further discussion in the body of this Order. The major adjustments are discussed below.

Adjustment to Annualized Test Year Revenues

We find it appropriate to make several adjustments to test year revenues. In 1993, the utility recorded its revenues on a cash basis. An adjustment is necessary to reflect revenues on an accrual basis. An adjustment of \$9,445 is therefore appropriate. Furthermore, in order to reflect the rate index that occurred in October 1993, annualized revenues have been increased by \$11,607.

The utility billed several customers in the Brunners system on a flat basis in the test year. The utility has requested

conversion to a base facility and gallonage basis, and as discussed herein, we have approved that request. Therefore, an annualization adjustment is necessary to reflect this change. We find it appropriate to increase test year revenues by an additional \$2,086 to reflect this billing practice.

DEP Fines

During the test year the utility paid fines totalling \$3,207 to DEP for violations of pertinent rules. In accordance with the Uniform System of Accounts prescribed for this utility, all fines shall be charged to a below-the-line account. Therefore, a \$3,207 reduction to test year expenses is appropriate.

Undocumented Charges

Our audit included a review of operating expenses for assurance that accounts were properly classified and adequately documented. We noted that some of the booked expenses for local department store purchases included personal items and related party charges, but the full expense was charged to the utility. The auditor recommended removal of charges totalling \$7,267 for insufficiently documented payments. Upon receipt of the audit report, the utility reviewed each of the questioned invoices to allow proper assignment of charges. During that review, if an invoice was unavailable, the utility reclassified the entire payment to a non-utility business category. Other payments appear to represent additions to plant rather than utility operating expenses. After examination of the utility's proposed reallocation of charges, we hereby approve a reduction of test year expenses by \$4,827, which includes the full \$1,540 credit card payment and an additional \$3,287 for non-utility charges and items that should be capitalized.

Misclassified Plant Expenditures

The audit also reviewed test year expenses to determine whether amounts that were charged to expenses should properly be capitalized. Our auditor proposed reclassifying several charges (\$5,284 in total), and reviewed those items with the utility at the conclusion of the audit examination. The utility agreed that such reclassification would be correct with the exception of two items that were actually repairs and amounted to \$452. After considering the utility's explanation, we agree that the disputed \$452 amount should be expensed. The remaining \$4,832 charge shall be capitalized. Accordingly, we find that test year expenses shall be reduced by \$4,832 and that plant in service shall be increased by an equivalent sum.

Payroll Charges

The utility's application included proposed adjustments to increase wages for employees and management. The utility requested a 7.5 percent increase for field level employees and substantially increased payroll charges for officers. The utility proposed a \$27,500 increase (\$60,000 less \$32,500) for the president and a \$14,600 increase (\$25,000 less \$10,400) for the office manager/vice president.

We find it appropriate to approve a three percent pay increase for all utility employees. This rate is equivalent to the pay increase actually granted by the utility in 1994. The office manager's salary shall also be increased by three percent.

The president is also an officer and employee of Pugh Septic Tank, a related party, and his compensation from that business must be considered. After considering the utility's reasons for increasing the president's salary, we find it appropriate to approve a salary of \$50,000, or a \$17,500 increase. This takes into account salaries we have approved for presidents of comparable utilities, and recognizes the president's duties, qualifications, and other sources of income.

These actions reduce the requested payroll provision by \$26,453. Further, the reduction in salaries produces a \$2,077 reduction to payroll taxes.

Sludge Analysis and Laboratory Testing Costs

As a result of the recent consent order signed by the utility and the DEP, the utility is required to conduct additional laboratory testing. Additional testing of the effluent at Pugh #1 and Western Boulevard is needed to achieve treatment standards and to insure compliance. The application originally included a projected expense of \$1,391. The utility later reported that a \$1,125 expense is now projected. A corresponding \$266 reduction to the requested amount is therefore appropriate.

The utility also reported that laboratory testing expenses would also be increased. Originally, the utility reported that the annual expense would be about \$4,332, or a \$1,200 increase relative to the \$3,132 actual expense during the test year. Later, by letter dated August 12, 1994, the utility reported that further study indicated that the expense would be about \$14,026. Our review indicates that the projected charges appear reasonable and consistent with prescribed testing requirements. Therefore, we

approve of the projected \$14,026 cost, or a \$9,694 increase relative to the amount included in the initial filing.

Sludge Pumping Expenses

The utility's requested provision for sludge pumping expenses, 19,070, is based on projected expenses for 1995. The projected expense for that period exceeds the expected 1994 charges by 10 percent. However, the utility's rationale for that 10 percent increment is unclear. To the extent that the increment is associated with customer growth, such enlargement is inappropriate. We therefore approve a \$17,346 provision for sludge pumping expenses based upon the project expense for 1994. That amount exceeds the actual \$8,100 test year expense by \$9,245, but is \$1,724 less than that requested by the utility.

Upgrading of Lift Station Equipment

The utility asked the Commission to approve a pro forma expense of \$17,280 to maintain its 36 lift stations to meet minimum DEP requirements. The utility proposes to include installation of warning alarms and lights to indicate problems at the stations.

During the field inspection conducted our engineer, it was noted that some of the stations needed improvements to increase reliability. However, although some of the lift stations are older, others are fairly new and do not need immediate improvements. However, we agree that all lift stations should be maintained in proper and safe operating condition, which includes high level warning equipment.

We believe that a more reasonable annual amount for increased lift station maintenance is half the amount requested, or \$8,640. This will compensate for some of the new stations that are in good operating condition, and also allow the utility to phase in the improvements as time permits. It is unlikely that all of the proposed improvements can be accomplished in one year.

Postage Costs

Although the utility projected a 3 cent increase, or a \$450 increment, in postage rates, that increase has not yet occurred. Accordingly, we find it appropriate to remove the requested \$450 increase.

Permitting Charges

Highlands requested approval of a pro forma expense of \$4,180 to represent a normalized expense to obtain the required permits to operate its treatment plants. Our review of test year charges indicates that actual amounts paid to DEP and additional payments to consulting engineers for such permitting was \$7,100 more than the amount reported by the utility. Therefore, applying the principle suggested by the utility, but recognizing that an additional \$7,100 payment was actually incurred, the \$7,100 charge shall be removed from the test year to avoid double counting of the provision for on-going permit renewal charges.

Miscellaneous Expenses

Pursuant to Rule 25-30.433, Florida Administrative Code, charitable donations shall be charged below-the-line. Highlands incorrectly charged a \$100 charitable contribution above-the-line. Additionally, test year expenses included a \$455 payment for legal representation in this rate proceeding. This charge shall be included in the rate case expense category and amortized over four years. Accordingly, test year expenses shall be reduced by this \$455 charge.

Guideline Depreciation Rates

The utility did not employ guideline depreciation rates to calculate depreciation of plant assets nor the offsetting provision for amortization of CIAC. Instead, the utility's reported expense followed the accounting treatment used for income tax purposes. Pursuant to Rule 25-30.140(3), Florida Administrative Code, we find it appropriate to employ guideline depreciation rates. Application of guideline rates to existing balances, together with our adjustments to plant and CIAC, produces a \$14,217 net provision for depreciation expense, or a \$10,887 reduction to the utility's reported balance. Accordingly, depreciation expense shall be reduced by this \$10,887 difference.

Rate Case Expense

In its application, Highlands included a \$70,000 provision for rate case costs in its calculation of the revenue requirement. The utility proposed amortization of this charge over four years for a \$17,500 annual expense. On August 24, 1994, the utility produced additional detail regarding its latest estimate concerning that expenditure. That information indicated that the actual cost would be about \$67,416. This included \$5,000 for the filing fee and

other indirect costs, \$17,000 for legal services, \$20,416 for engineering services, and \$25,000 for accounting services.

Our review of supporting detail for the revised expense indicates that further adjustments are appropriate. First, the reported engineering cost includes \$10,500 for preparation of computerized service area maps, including \$8,000 which is still unspent. These charges are not directly related to this filing and their removal is appropriate. Next, the utility projected a \$6,836 completion cost for additional accounting work, but did not attach invoices to demonstrate what work was necessary to finalize accounting responsibilities. The utility also projected \$5,782 in completion costs to allow for 38 hours of additional legal work. Both the projected completion costs for legal and accounting work seem excessive. Therefore, we find it appropriate to reduce the projected expenses by one-third, or \$4,057. After making these adjustments, the allowance for total rate case charges is \$52,860. Amortization of that amount over four years is required by statute, resulting in a \$13,215 annual expense, or a \$4,285 reduction to the utility's initial estimate.

Miscellaneous Pro Forma Adjustments

The utility's requested revenue amount included a number of pro forma adjustments: 1) a \$250 increase in expenses to meet additional DEP monitoring requirements for wells that test for contaminants; 2) \$4,320 to lease additional computer and office equipment; 3) \$3,600 to lease a truck to provide transportation for a new field employee; 4) an additional \$13,897 to retain the services of a contract operator for daily plant inspections and to otherwise meet DEP minimum operator requirements; and 5) \$11,909 to maintain plant equipment in accordance with DEP requirements and enhanced plant repair practices.

We have reviewed each of the proposed adjustments and find them to be reasonable. The projections are reasonably accurate and represent costs which will be incurred on an on-going basis. Accordingly, we find it appropriate to approve the adjustments listed above.

REVENUE REQUIREMENT

Based upon our review of the utility's application and the adjustments discussed herein, we find that the appropriate annual revenue requirement is \$460,691 for the wastewater system. This revenue requirement represents an annual increase in revenues of \$93,535 or 25.48 percent. This revenue requirement will allow the

utility to recover its operating expenses and the opportunity to earn a 6.89 percent return on its investment.

RATES AND CHARGES

The final rates are designed to produce annual revenues of \$460,691. The utility's rates prior to the filing, the currently approved interim rates, the requested final rates and approved final rates are shown on Schedule No. 4-A.

Flat Rate Eliminated

Highlands has requested that its existing flat rate customers be converted to a base facility charge and gallonage basis. The utility's filing indicated that there were four flat rate customers; however the tariff shows only two, Brunners and Days Inn, have tariff approval. The other two flat rate customers listed by the utility, Rosewood Retirement and Placid Campground, do not have tariff approval.

Furthermore, even though the utility's filing indicates that there are four flat rate customers, in actuality these customers have already been switched to metered billing. Our staff requested that the utility explain where and when it obtained authority to charge flat rates to Rosewood Retirement and Placid Campground. The utility explained that Rosewood was hooked up in 1978 and was metered at one time but the meter was broken and not repaired or replaced by the Town of Lake Placid for quite sometime. As a result, the utility billed a flat rate based upon the DEP flow chart. When the utility discovered that the meter had been repaired the utility immediately switched the account back to measured billing based on water consumption. The switch over for Rosewood was on September 19, 1993. The Placid Campground was connected in 1977 and was switched to metered on February 18, 1994.

It has been Commission practice to use the base facility charge structure for setting rates because of the structure's ability to track costs. The base facility charge structure also gives the customers some control over their wastewater bills. Each customer pays the pro rata share of the related costs necessary to provide service through the base facility charge, and only the actual usage is paid for through the gallonage charge. Therefore, we find it appropriate to approve Highland's request to implement the base facility and gallonage charge rate structure.

Effective Date

The approved rates will be effective for meter readings on or after the stamped approval effective date of the tariff. The utility shall file and have approved revised tariff sheets and a proposed customer notice letter, pursuant to Rule 25-22.0406(9), Florida Administrative Code, prior to implementing the new rates.

Residential Gallonage Cap

The current Commission standard in setting residential wastewater rates is that only 80 percent of residential water usage is returned to the system as wastewater. The remaining 20 percent is attributed to outside uses such as lawn irrigation. Generally, this Commission sets monthly caps of 6,000 gallons, 8,000 gallons, or 10,000 gallons per month. When determining the appropriate cap, a comparison of the consolidated factors at the various levels is performed. Because 10,000 gallons is the highest cap we would consider setting in this case, the consolidated factor gallons at that level become the 100 percent marker.

The utility's billing analysis revealed that 96.7 percent of the utility's customers require treatment at the 8,000 gallons level and 93 percent of its customers require treatment at the 6,000 gallons level. Decreasing the gallonage cap has the effect of lowering the maximum bill and increasing the cost per 1,000 gallons. In consideration of our standard in setting residential wastewater rates to reflect that only 80 percent of residential water usage is returned to the system as wastewater, we find that a gallonage cap of 6,000 gallons is appropriate. Therefore, the gallonage cap shall be decreased from the current level of 10,000 gallons to 6,000 gallons.

There is no cap on usage for general service wastewater bills. The differential in the gallonage charge for residential and general service wastewater customers recognizes that a portion of a residential customer's water usage will not be returned to the wastewater system.

Refund of Interim Revenues

By Order No. PSC-94-0840-FOF-SU, issued on July 11, 1994, we suspended the utility's proposed rates and approved interim wastewater rates subject to refund, pursuant to Sections 367.082, Florida Statutes. The interim increase resulted in annual revenues of \$380,860 for wastewater, an increase of \$12,742 or 3.46 percent.

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.

In this proceeding, the test period for establishment of interim rates and final rates was the twelve months ended December 31, 1993. The approved interim rates did not include any provisions for pro forma consideration of increased operating expenses or increased plant. The interim increase was designed to allow recovery of actual interest costs, and the floor of the last authorized range of equity earnings. To establish the proper refund amount, we calculated a revised revenue requirement for the interim period using the same data used to establish final rates, but excluding the proforma provisions. These pro forma charges were excluded since they were not actual expenses during the interim collection period. We computed the comparable revenue requirement using the recommended cost of capital for final rate purposes, since this overall cost of capital includes the return on equity that, by statute, is the prescribed return to be used to test for excessive earnings during the interim collection period. Based on our calculations, we find that no interim refund is necessary.

Statutory Four-Year Rate Reduction

Section 367.0816, Florida Statutes, requires that rate case expense be apportioned for recovery over the period of four years. The statute further requires that the rates of the utility be reduced immediately by the amount of rate case expense previously included in the rates. This statute applies to all rate cases filed on or after October 1, 1989.

The wastewater rates shall be reduced by \$13,838 as shown on Schedule No. 5. The revenue reductions reflect the annual rate case amounts amortized (expensed) plus the gross-up for regulatory assessment fees. The utility shall file revised tariffs no later than one month to the actual date of the required rate reduction. The utility shall also file a proposed customer notice setting forth the lower rates and the reason for the 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 the reduction in the rates due to the amortized rate case expense.

Service Availability Charges

Rule 25-30.580 (1)(a), Florida Administrative Code, states that the maximum amount of CIAC, net of amortization, should not exceed 75 percent of the total original cost, net of accumulated depreciation, of the utility's facilities and plant when the facilities and plant are at their design capacity. The purpose of this percentage is to only allow 75 percent of the utility's facilities to be contributed. This ensures that the utility has at least 25 percent invested so that it will maintain an interest in the facilities.

In Order No. 18036, we approved an increase of the utility's plant capacity charges from \$700 to \$871 per ERC. The increase at that time was set so that the utility would be 60 percent contributed at design capacity. As of December 31, 1993 the utility's MFRs indicate that the utility is presently heavily over-contributed at 98.47 percent. Highlands did not request a change in its service availability charges in this proceeding.

As noted herein, the Brunners and Clearview Terrace plants are built out. The Pugh plant has reported very minimal growth over the past five years but is installing a series of surge tanks. These surge tanks will not add capacity but will improve wastewater treatment. The Western Boulevard plant has experienced the most growth in the past five years and there is considerable land in the service area for development. However, as stated earlier, the utility is under a DEP moratorium and cannot add new customers. A temporary operating permit was issued for the Western Boulevard WWTP on June 3, 1994, with an expiration or full compliance with Chapter 403, Florida Statutes, date of February 28, 1995. DEP stated that the permit was issued because the existing wastewater treatment plant facility does not consistently meet effluent standards and requires evaluation of the treatment plant to determine compliance with all applicable standards contained in Chapter 403, Florida Statutes, and Rule 17-600, Florida Administrative Code.

The utility has plans to add additional treatment facilities which will increase its capacity and will allow it to add more customers. This will also significantly increase its investment after the installation of these facilities. The DEP required improvements will cost the utility \$250,000. However, in order for the utility to reach at least a 75 percent level of contribution it would have to invest at least \$265,000. Therefore Highlands shall discontinue collection of CIAC.

Interest on Customer Deposits

Rule 25-30.311(4)(a), Florida Administrative Code, requires that the customer deposit interest shall be simple interest in all cases and settlement shall be made annually, either in cash or by credit on the current bill. Rule 25-30.311 (5), Florida Administrative Code, states that after a customer has established a satisfactory payment record and has had continuous service for a period of 23 months, the utility shall refund the residential customer's deposits, providing the customer has not, in the preceding 12 months, (a) made more than one late payment of a bill (after the expiration of 20 days from the date of mailing or delivery by the utility), (b) paid with a check refused by a bank, (c) been disconnected for nonpayment, or at any time, (d) tampered with the meter, or (e) used service in a fraudulent or unauthorized manner.

The utility's Tariff Original Sheet No. 14.0 states:

Company will pay interest on customer deposits at the rate of 8% per annum. The payment of interest will be made once each year as a credit on regular bills, and on final bills when service is discontinued. No customer depositor will receive interest on his deposit until at least six (6) months of continuous service, the interest will be paid from the date of the commencement of service. The company will pay or credit accrued interest to the customers account during the month of December each year."

We discovered during the billing compliance audit of the utility that it has not paid deposit interest in accordance with its Tariff Original Sheet No. 14.0 or Rule 25-30.311, Florida Administrative Code. The utility in the past has waited until the deposit is refunded to its customer and then the interest has been calculated from the initiation of service date and paid along with the return of the deposit. This is an improper handling of the interest on customer deposits. Additionally, the utility's tariff states that the interest rate is 8 percent on customer deposits but Rule 25-30.311(4)(a), Florida Administrative Code, states that the proper interest rate is 6 percent. We find it appropriate to require the utility to pay interest in accordance with Rule 25-30.311, Florida Administrative Code, and to correct wording in its tariff to bring it into compliance with Rule 25-30.311(4)(a), Florida Administrative Code.

BOOKS AND RECORDS

Rule 25-30.115, Florida Administrative Code, requires utilities to maintain their accounts and records in conformity with the NARUC Uniform System of Accounts (USOA). Highland's books and records have not been maintained in full compliance with the USOA for Class B Wastewater Utilities. Specifically, some account numbers (particularly balance sheet accounts) do not match the prescribed account numbers, some utility charges are billed to a related party (which causes auditing difficulties), some intercompany billings are not adequately documented, and revenues are recorded on a cash basis rather than the prescribed accrual treatment.

In responding to these concerns, the utility's outside accountant agreed that certain improvements are needed. He reported that the utility will immediately begin to more adequately disclose the nature of all work performed by related parties and will at least annually convert its records to the accrual accounting system. The utility will also work to achieve better compliance with the prescribed accounting system.

Based upon these representations regarding acknowledged accounting problems and planned improvements, we shall not impose any penalties for noncompliance. However, because we find that substantial record keeping improvements are warranted, the utility shall correct material deficiencies within twelve months. The utility may obtain assistance from the Commission staff for clarification regarding these compliance concerns.

If a protest is not received within 21 days of issuance of this PAA rder, this Order will become final, and the docket may be closed upon the utility's filing of and staff's approval of revised tariff sheets. Further, in the event that no protest is filed, the escrow agreement may be released.

Based on the foregoing, it is, therefore,

ORDERED by the Florida Public Service Commission that Highlands Utilities Corporation's application for increased wastewater rates is 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 all matters contained in the schedules attached hereto are by reference incorporated herein. It is further

ORDERED that Highlands Utilities Corporation is authorized to charge the new rates and charges as set forth in the body of this Order. It is further

ORDERED that prior to its implementation of the rates and charges approved herein, Highlands Utilities Corporation shall submit and have approved a proposed customer notice to its customers of the increased rates and charges and reasons therefor. The notice will be approved upon our staff's verification that it is consistent with our decision herein. It is further

ORDERED that prior to its implementation of the rates and charges approved herein, Highlands Utilities Corporation shall submit and have approved revised tariff pages. The revised tariff pages will be approved upon staff's verification that the pages are consistent with our decision herein, that the protest period has expired, and that the customer notice is adequate. It is further

ORDERED that the rates shall be reduced at the end of the four-year rate case expense amortization period, consistent with our decision herein. The utility shall file revised tariff sheets no later than one month prior to the actual date of the reduction and shall file a customer notice. It is further

ORDERED that all provisions of this Order are issued as proposed agency action and shall become final, unless an appropriate petition in the form provided by Rule 25-22.029, Florida Administrative Code, is received by the Director of the Division of Records and Reporting at her office at 101 East Gaines Street, Tallahassee, Florida, 32399-0870, by the date set forth in the Notice of Further Proceedings below. It is further

ORDERED that Highlands Utilities Corporation shall submit a statement of the actual rate case expense incurred as set forth within the body of this Order. It is further

ORDERED that Highlands Utilities Corporation shall implement guideline depreciation rates in accordance with Rule 25-30.140, Florida Administrative Code. It is further

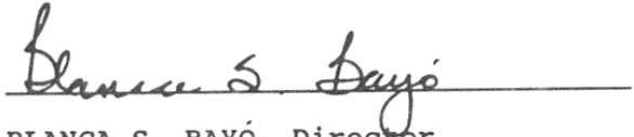
ORDERED that Highlands Utilities Corporation shall correct material deficiencies in its books and records within twelve months, and shall further maintain the books and records in conformity with the NARUC Uniform System of Accounts and Rule 25-30.155, Florida Administrative Code. It is further

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DOCKET NO. 931052-SU
PAGE 20

ORDERED that if no timely protest is received from a substantially affected person, the escrow agreement may be released. It is further

ORDERED that this docket shall be closed if no timely protest is received from a substantially affected person, and upon the utility's filing and staff's approval of revised tariff sheets and the customer notice.

By ORDER of the Florida Public Service Commission, this 11th day of October, 1994.

A handwritten signature in cursive script, reading "Blanca S. Bayó", is written over a horizontal line.

BLANCA S. BAYÓ, Director
Division of Records and Reporting

(S E A L)

MEO

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.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 101 East Gaines Street, Tallahassee, Florida 32399-0870, by the close of business on November 1, 1994.

In the absence of such a petition, this order shall become effective on the day subsequent to the above date as provided by Rule 25-22.029(6), Florida Administrative Code.

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.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by 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 Records and Reporting 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 of the effective date 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.

HIGHLAND UTILITIES CORPORATION SCHEDULE OF WASTEWATER RATE BASE TEST YEAR ENDED 12/31/93			SCHEDULE NO. 1-A DOCKET NO. 931052-SU		
COMPONENT	TEST YEAR PER UTILITY	UTILITY ADJUSTMENTS	ADJUSTED TEST YEAR PER UTILITY	COMMISSION ADJUSTMENTS	COMMISSION ADJUSTED TEST YEAR
1 UTILITY PLANT IN SERVICE	\$ 1,174,370	\$ 0	\$ 1,174,370	(\$ 34,031)	1,140,339
2 LAND	30,499	0	30,499	0	30,499
3 NON-USED & USEFUL COMPONENTS	0	0	0	0	0
4 ACCUMULATED DEPRECIATION	(359,930)	0	(359,930)	8,628	(351,302)
5 CIAC	(968,259)	0	(968,259)	(11,933)	(980,192)
6 AMORTIZATION OF CIAC	166,255	0	166,255	0	166,255
7 ACQUISITION ADJUSTMENTS - NET	0	0	0	0	0
8 ADVANCES FOR CONSTRUCTION	0	0	0	0	0
9 DEFERRED TAXES	0	0	0	0	0
10 WORKING CAPITAL ALLOWANCE	0	40,522	40,522	9,024	49,546
RATE BASE	\$ 42,935	\$ 40,522	\$ 83,457	(\$ 28,312)	55,145

HIGHLAND UTILITIES CORPORATION
 ADJUSTMENTS TO RATE BASE
 TEST YEAR ENDED 12/31/93

SCHEDULE NO. 1-B
 DOCKET NO. 931052-SU
 PAGE 1 OF 1

EXPLANATION	WATER	WASTEWATER
(A) UTILITY PLANT IN SERVICE		
1) Adjustment to agree with previously established balance		\$ (31,025)
2) Remove account balance for mobile home		(4,000)
3) Adjustment to reclassify plant expenditures		4,832
4) Adjustment to correct retirement of vehicles		(3,838)
		\$ <u>(34,031)</u>
(B) ACCUMULATED DEPRECIATION		
1) Adjustment to agree with previously established balance		\$ 926
2) Remove account balance for mobile home		4,000
3) Adjustment to reclassify plant expenditures		(136)
4) Adjustment to correct retirement of vehicles		3,838
		\$ <u>8,628</u>
(C) CIAC		
Adjustment to agree with previously established balance		\$ <u>(11,933)</u>
(D) WORKING CAPITAL ALLOWANCE		
Adjustment to reflect adjustment to test year expenses		\$ <u>9,024</u>

HIGHLAND UTILITIES CORPORATION CAPITAL STRUCTURE TEST YEAR ENDED 12/31/93					SCHEDULE NO. 2-A DOCKET NO. 931052-SU					
DESCRIPTION	ADJUSTED TEST YEAR PER UTILITY	WEIGHT	COST	UTILITY WEIGHTED COST	COMMISSION RECONC. ADJ. TO UTILITY EXHIBIT	BALANCE PER COMMISSION	WEIGHT	COST	WEIGHTED COST PER COMMISSION	
1 LONG TERM DEBT	\$ 0	0.00%	0.00%	0.00%	\$ 0	0	0.00%	0.00%	0.00%	
2 SHORT-TERM DEBT	76,621	91.81%	6.90%	6.33%	(22,287)	54,334	98.53%	6.90%	6.80%	
3 PREFERRED STOCK	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%	
4 COMMON EQUITY	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%	
5 CUSTOMER DEPOSITS	6,836	8.19%	8.00%	0.66%	(6,025)	811	1.47%	6.00%	0.09%	
7 DEFERRED ITC'S	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%	
8 DEFERRED TAX CREDITS	0	0.00%	0.00%	0.00%	0	0	0.00%	0.00%	0.00%	
9 TOTAL CAPITAL	\$ 83,457	100.00%		6.99%	\$ (28,312)	\$ 55,145	100.00%		6.89%	
RANGE OF REASONABLENESS							LOW	HIGH		
							-----	-----		
RETURN ON EQUITY							0.00%	0.00%		
							=====	=====		
OVERALL RATE OF RETURN							6.89%	6.89%		
							=====	=====		

HIGHLAND UTILITIES CORPORATION ADJUSTMENTS TO CAPITAL STRUCTURE TEST YEAR ENDED 12/31/93			SCHEDULE NO. 2-B DOCKET NO. 931052-SU		
DESCRIPTION	SPECIFIC ADJUSTMENT (1)	SPECIFIC ADJUSTMENT (2)	PRO RATA RECONCILE	NET ADJUSTMENT	
1 LONG TERM DEBT	\$ 0	\$ 0	0 \$	0	
2 SHORT-TERM DEBT	381,320	0	(403,607)	(22,287)	
3 PREFERRED STOCK	0	0	0	0	
4 COMMON EQUITY	0	0	0	0	
5 CUSTOMER DEPOSITS	0	0	(6,025)	(6,025)	
6 ACCUM. DEFERRED INCOME TAX	0	0	0	0	
7 OTHER (Explain)	0	0	0	0	
8 TOTAL CAPITAL	\$ 381,320	\$ 0	(409,632) \$	(28,312)	
	=====	=====	=====	=====	

HIGHLAND UTILITIES CORPORATION
STATEMENT OF WASTEWATER OPERATIONS
TEST YEAR ENDED 12/31/93

SCHEDULE NO. 3-A
DOCKET NO. 931052-SU

DESCRIPTION	TEST YEAR PER UTILITY	UTILITY ADJUSTMENTS	UTILITY ADJUSTED TEST YEAR	COMMISSION ADJUSTMENTS	COMMISSION ADJUSTED TEST YEAR	REVENUE INCREASE	REVENUE REQUIREMENT
1 OPERATING REVENUES	\$ 344,018	\$ 189,007	\$ 533,025	\$ (165,869)	\$ 367,156	\$ 93,535	460,691
OPERATING EXPENSES		54.94%				25.48%	
2 OPERATION AND MAINTENANCE	\$ 324,178	\$ 121,983	\$ 446,161	\$ (49,794)	\$ 396,367	\$	396,367
3 DEPRECIATION	25,104	0	25,104	(10,887)	14,217		14,217
4 AMORTIZATION	1,710	17,500	19,210	(4,285)	14,925		14,925
5 TAXES OTHER THAN INCOME	26,593	10,123	36,716	(9,541)	27,175	4,209	31,384
6 INCOME TAXES	0	0	0	0	0	0	0
7 TOTAL OPERATING EXPENSES	\$ 377,585	\$ 149,606	\$ 527,191	\$ (74,507)	\$ 452,684	\$ 4,209	456,893
8 OPERATING INCOME	\$ (33,567)	\$ 39,401	\$ 5,834	\$ (91,362)	\$ (85,528)	\$ 89,326	3,798
9 RATE BASE	\$ 42,935		\$ 83,457		\$ 55,145		\$ 55,145
RATE OF RETURN	-78.18%		6.99%		-155.10%		6.89%

HIGHLAND UTILITIES CORPORATION ADJUSTMENTS TO OPERATING STATEMENTS TEST YEAR ENDED 12/31/93		SCHEDULE NO. 3-B DOCKET NO. 931052-SU PAGE 1 OF 1	
EXPLANATION	WATER	WASTEWATER	
(A) OPERATING REVENUES			
1) Remove requested rate increase		\$	(189,007)
2) Adjustment to annualize revenues			9,445
3) Adjustment to show accrual accounting practice			11,607
4) Adjustment to show collection of base facility charges in Brunner system			2,086
		\$	<u>(165,869)</u>
(B) OPERATING EXPENSES			
1) Adjustment to remove fines paid to DEP			(3,207)
2) Adjustment to remove expenses related to Mobile Home			(1,424)
3) Adjustment to remove charitable contributions			(100)
4) Adjustment to remove inadequately documented cash payments			(3,287)
5) Adjustment to remove inadequately documented credit card purchases			(1,540)
6) Adjustment to capitalize plant expenditures			(4,832)
7) Adjustment to remove misclassified provision for rate case expense			(455)
8) Adjustment to reduce provision for salaries to 3% increase			(16,453)
9) Adjustment to show \$50,000 salary for president			(10,000)
10) Adjustment to reflect estimate of normalized sludge analysis costs			(266)
11) Adjustment to show 1994 rather than 1995 sludge removal costs			(1,734)
12) Adjustment to show reduced estimate of annual lift station improvements			(8,640)
13) Adjustment to show estimated increase for lab testing charges			9,694
14) Adjustment to remove provision for increased postage			(450)
15) Adjustment to show normalized permitting charges			(7,100)
			<u>(49,794)</u>
(C) DEPRECIATION EXPENSE			
Adjustment to reflect application of guideline depreciation rates			<u>(10,887)</u>
(D) AMORTIZATION EXPENSE			
Adjustment to reflect revised provision for rate case expense			<u>(4,285)</u>
(E) TAXES OTHER THAN INCOME TAXES			
1) Adjust provision for regulatory assessment fees			(7,464)
2) Adjustment to payroll taxes related to reduction to payroll expense			(2,077)
			<u>(9,541)</u>
(F) OPERATING REVENUES			
Adjustment to reflect recommended revenue requirement			<u>93,535</u>
(G) TAXES OTHER THAN INCOME TAXES			
Regulatory assessment taxes on additional revenues			<u>4,209</u>

**RATE SCHEDULE
WASTEWATER**

UTILITY: Highlands Utility Corporation
 COUNTY: Highlands
 TEST YEAR ENDED: December 31, 1993

Monthly Rates

	<u>Current Rates</u>	<u>Commission Approved Interim Rates</u>	<u>Utility Requested Final Rates</u>	<u>Commission Approved Final Rates</u>
<u>Residential</u>				
Base Facility Charge: All Meter Sizes	\$8.70	\$9.00	\$12.70	\$11.59
Gallonage Charge per 1,000 G.	\$2.49	\$2.58	\$3.64	\$2.95
Wastewater Cap	10M	10M	10M	6M
<u>General Service and Multi-Family</u>				
Base Facility Charge: Meter Size:				
5/8"x3/4"	\$8.70	\$9.00	\$12.70	\$11.59
1"	\$21.73	\$22.50	\$31.74	\$28.98
1-1/2"	\$43.44	\$44.96	\$63.44	\$57.95
2"	\$69.52	\$71.95	\$101.51	\$92.72
3"	\$139.03	\$143.88	\$203.00	\$185.44
4"	\$226.32	\$234.21	\$634.34	\$289.75
6"	\$434.47	\$449.60	\$778.00	\$579.50
Gallonage Charge per 1,000 G. (No Maximum)	\$2.49	\$2.58	\$3.64	\$3.54

Typical Residential Bills

<u>5/8" x 3/4" meter</u>				
3 M	\$16.17	\$16.74	\$23.62	\$20.44
5 M	\$21.15	\$21.90	\$30.90	\$26.34
8 M	\$28.62	\$29.64	\$41.82	\$29.29
10 M	\$33.50	\$34.80	\$49.10	\$29.29

Highlands Utilities Corporation
 COUNTY: Highlands
 TEST YEAR ENDED: December 31, 1993

SCHEDULE OF STAFF RECOMMENDED RATES
 AND RATE DECREASE IN FOUR YEARS

WASTEWATER

Monthly Rates

	Staff Recommended Final Rates	Rate Decrease
<u>Residential</u>		
Base Facility Charge: All Meter Sizes	\$11.59	\$0.36
Gallonage Charge per 1,000 G.	\$2.95	\$0.09
<u>General Service and Multi-Family</u>		
Base Facility Charge: Meter Size:		
5/8"x3/4"	\$11.59	\$0.36
1"	28.98	0.91
1-1/2"	57.95	1.81
2"	92.72	2.90
3"	185.44	5.81
4"	289.75	9.07
6"	579.50	18.15
Gallonage Charge per 1,000 G.	\$3.54	\$0.11