BEFORE THE PUBLIC SERVICE COMMISSION

In re: Petition by Water Management Services, Inc. for limited proceeding to increase water rates in Franklin County.	DOCKET NO. 000694-WU ORDER NO. PSC-05-1156-PAA-WU ISSUED: November 21, 2005

The following Commissioners participated in the disposition of this matter:

BRAULIO L. BAEZ, Chairman
J. TERRY DEASON
RUDOLPH "RUDY" BRADLEY
LISA POLAK EDGAR
ISILIO ARRIAGA

NOTICE OF PROPOSED AGENCY ACTION
ORDER APPROVING FINAL RATES, DECREASING FINAL RATES FOR THE FIRST TWELVE MONTHS TO RETURN OVERCOLLECTION
AND
FINAL ORDER REDUCING RATES AT THE END OF THE FOUR-YEAR RATE CASE EXPENSE AMORTIZATION PERIOD

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service Commission that the action discussed herein, except for our decision reducing rates at the end of the four-year amortization period, 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.

CASE BACKGROUND

Water Management Services, Inc. (WMSI or utility) is a Class A water utility providing service to approximately 1,776 water customers in Franklin County. For the year ended December 31, 2004, the utility reported in its annual report operating revenues of $1,419,587, and utility operating income of $269,290. The utility's water rates were last established in a rate case by Order No. PSC-94-1383-FOF-WU, issued November 14, 1994, in Docket No. 940109-WU, In re: Petition for interim and permanent rate increase in Franklin County by St. George Island Utility Company, Ltd.

On June 6, 2000, WMSI filed an application, pursuant to Section 367.0822, Florida Statutes, for a limited proceeding to increase its water rates to recover the cost of building a new water transmission main to connect its wells on the mainland to its service territory on St. George Island. In its petition, the utility stated that it was notified by the Florida Department of Transportation (DOT) that the existing bridge to St. George Island, to which WMSI's water main is attached, was to be demolished and replaced by a new bridge with an expected in-service date of March 2003. Upon completion of the new bridge, WMSI would have to make alternative arrangements to provide service to its certificated service area. The utility's petition set forth its plan to construct a new main to be attached to the new bridge, along with ancillary modifications to its system, and requested an increase in its rates to provide funding for the proposed construction.

A customer meeting was held at the Franklin County Courthouse in Apalachicola on September 12, 2000, in order to allow the utility's customers the opportunity to comment on WMSI's petition. More than 100 customers attended, and 13 customers made statements. In general, the speakers believed that the projected cost of the project was excessive and that the utility should have planned for this contingency in such a way as to avoid such a large rate increase. There was also great concern over the utility's ability to provide fire protection.

WMSI originally requested that we approve two tiers of temporary increases, to be approved concurrently, described as Phase 1 and Phase 2, in its initial consideration of this matter. Phase 1 would cover preliminary costs and Phase 2 would cover estimated total costs of the project. The utility then proposed a true-up, described as Phase 3, which would set final rates after the project was complete and all costs were verified.

By Order No. PSC-00-2227-PAA-WU, issued November 21, 2000 (consummated by Order No. PSC-00-2405-CO-WU, issued December 14, 2000), we found that construction of the new water transmission main was justified, and that the prudent costs to be incurred by WMSI for this project should be recovered through a three phase mechanism. Further, we found that replacement of the existing 8-inch main with a 12-inch water main was prudent, and that the used and useful percentage for the new main was 100 percent. We also approved the prudence of constructing a new line from Well No. 1 to Well No. 4 in connection with the replacement project. In addition, we approved a Phase 1 increase and deferred consideration of a temporary Phase 2 increase until the utility filed more complete and detailed cost information. The approved Phase 1 increase was 11.3 percent, or an annual revenue increase of $82,707.

On May 14, 2003, WMSI filed a Supplemental Petition for Limited Proceeding (supplemental petition) requesting revised rates for the Phase 2 rate increase. In its supplemental petition, the utility stated that numerous changes had occurred since the filing of the original petition. First, the projected bridge in-service date was changed from March 2003 to October 2003. Second, the estimated capital cost of the new transmission main and the other approved work on the mainland had decreased. Third, WMSI had obtained financial support from the State Revolving Fund (SRF) loan program administrated by the Department of Environmental Protection (DEP). Finally, an eminent domain case, which was filed by WMSI in an attempt to receive compensation from DOT for the old main, was unsuccessful.

Since the net effect of the above mentioned changes substantially reduced the total project cost, WMSI requested the inclusion of fire flow protection improvement measures in its supplemental petition for limited proceeding. The utility stated that fire flow protection is an issue of great importance to the utility's customers, as communicated at the customer meeting. The overall rate increase requested in the supplemental petition was designed to generate annual

Phase 2 revenues of $568,657 above the expected revenue from the previously approved Phase 1 rates, or an additional increase of 50.2 percent.

By Order No. PSC-03-1005-PAA-WU (Phase 2 PAA order), issued September 8, 2003, we approved a Phase 2 revenue requirement of $490,959, or an increase of 42.1 percent in base facility and gallonage charges. We also approved the utility's request to include the cost of improved fireflow protection in this proceeding, and established a depreciable life of 35 years for the portion of WMSI's transmission main attached to the new bridge.

The Office of Public Counsel (OPC) and the utility both filed Petitions on Proposed Agency Action. OPC objected to that portion of the utility's plan which called for removing the existing 150,000 gallon elevated water storage tank and replacing it with a new 200,000 gallon tank. WMSI stated that its petition was in response to its understanding that OPC was also filing a protest. WMSI's petition addressed the rate case expense that would be incurred as a result of a formal hearing. On May 28, 2004, WMSI and OPC filed a Joint Motion Requesting Commission Approval of Settlement Agreement to address both parties' protests. The substance of the settlement agreement was that, in lieu of replacing the storage tank, the utility would complete the looping of the water mains that serve the service territory from Bob Sikes Cut to the state park. By Order No. PSC-04-0791-AS-WU, issued August 12, 2004 (Settlement Agreement Order), we approved the settlement agreement.

On October 14, 2004, the utility filed its Petition for Approval of Phase 3 Final Rates (the final petition), which we address below. We have jurisdiction pursuant to Sections 367.081 and 367.121, Florida Statutes, to address this petition.

FINAL REVENUE REQUIREMENT

In its final petition, WMSI requested final water rates which, by its calculation, would generate annual revenues of $1,387,480. The utility's request for final rates was based upon a formula which included factors for the total expenditures for the supply main and fire flow improvements. These expenses included the interest rate applicable to construction financing, depreciation and property taxes on the new construction, rate case expense for the limited proceeding, increased property insurance costs, the expense of annual audits required by the lender, amortization of the residual value of the retired supply main, and regulatory assessment fees (RAF) associated with the increased revenue. The utility's calculation is summarized as follows:

Table 1 - WMSI Revenue Calculation

Total Cost of Project	$6,156,536
One-half Year Depreciation	-$96,116
Net Cost	$6,060,420
Average Depreciation on Total Cost at 3.13%	$192,233

Interest on Net Cost at 3.48%	$211,622
Personal Property Tax on Net Cost at 1.14%	$69,089
Rate Case Expense	$18,511
Increased Property Insurance Cost	$8,253
Cost of Annual Audit	$12,000
Amortization of Retired Property	$14,631
Subtotal	$526,339
Gross-up for RAF at 4.5%	$24,801
Total Additional Revenue	$551,140
Additional Revenue From Phase 2 Rates	$486,259
Excess of Additional Revenue Over Phase 2 Revenue	$64,881
Expected Total Revenue at Phase 2 Rates	$1,322,599
Required Final Revenue Requirement	$1,387,480

WMSI's calculation methodology is similar to the approach we approved in our Phase 2 PAA Order. We have reviewed the information submitted by the utility in support of its calculation and believe that the methodology is still reasonable, with adjustments as discussed below. The utility attached three schedules to the final petition providing details of its calculations. WMSI also responded to several formal and informal requests for additional data. As we ordered in the Phase 2 PAA Order, our staff conducted an audit of the expenditures claimed by the utility in the final petition. On May 4, 2005, OPC submitted a letter expressing seven specific concerns about the utility's filing. On May 9, 2005, WMSI submitted a letter responding to OPC's concerns. We will first address six of the specific areas of concern addressed in OPC's letter, then provide additional analysis and adjustments. The other area of concern included in OPC's letter will be addressed later in this Order in our analysis of the utility's proposal for a true-up.

Improvements to Office Building

OPC's first concern was that the final petition included costs associated with improvements to its office building on the island in the amount of $287,231. OPC believes that these costs are outside of the scope of the limited proceeding, that they have not been mentioned by the Commission in any previous orders in this docket, and that these costs have not been verified and reviewed for prudence in the audit conducted by the Commission.

WMSI responded that the improvements were included in the fire protection improvements approved by the Commission in the Phase 2 PAA Order. Although described as "island office improvements" in the final petition, the $287,231 represents an expenditure included in "other plant improvements" in the Supplemental Petition. WMSI stated that all of the high service pumps, the electrical equipment, and the generator are located in the office building structure. The utility explained that the building required substantial renovation in order to accommodate the operational requirements of the service improvements which are the subject of this proceeding, to improve safety and working conditions for WMSI employees, and to improve the appearance of the building.

The Commission audit report, issued March 16, 2005, did not contain any exceptions with respect to the expenditures which are the subject of this limited proceeding. On May 9, 2005, the Commission staff engineer made a physical inspection of the utility's water facilities. In his report dated May 16, 2005, the Commission staff engineer stated that he had reviewed the structural improvements to the utility's plant and the fire flow protection system. The improvements observed included a new electrical room, a new generator and generator room, a new chlorination room, a new spare parts room, and a new roof for the expanded building. The Commission staff engineer's report indicated that all of the improvements appear to be prudent and within the scope of this limited proceeding, with the possible exception of a second floor area created by the roof expansion. This area includes glass French doors, large windows, decking and vinyl siding. The utility stated that the area could be used for storage; however, the Commission staff engineer's observation was that it was not currently being used and construction had not been completed.

WMSI subsequently provided a detailed breakdown of the costs of the building improvements. The cost of the decking and other improvements which were questioned by the Commission staff engineer was $37,310. The utility reiterated its belief that all of the first floor improvements were integral to the implementation of the improvements which are the subject of this limited proceeding. We agree with this assessment, but believe that the second floor improvements go beyond what we approved in the Phase 2 PAA Order. Therefore, we find that $37,310 shall be removed from the total cost used in the utility's calculation.

We also find that the cost of the second floor shall be removed from the "net cost" component of the utility's calculation. We have calculated one-half year depreciation for the second floor to be $605 (this did not materially change the composite depreciation rate). Accordingly, our approved adjustment to the "net cost" is a reduction of $36,705.

<u>Depreciation Expense For Retired Supply Main</u>

In its May 4, 2005 letter, OPC observes that the utility does not appear to have made any adjustment to remove depreciation expense for the retired supply main in its calculations. In its response, the utility agrees with this assertion, and states that the depreciation expense included in the final petition includes only the expense related to the new construction.

We believe that the rationale of the utility's calculation of additional revenue required is, appropriately, the net increase in costs incurred for the replacement of the supply main and for the fire flow improvements. Therefore, we believe that it is appropriate to net the depreciation for assets which are being replaced and are no longer in service with the depreciation expense for the new construction.

We note that, in Schedule 2, page 2 of 3, of the final petition, WMSI assigned a 32 year life to the largest single component of the retired assets ($298,469 placed in service in 1985). Rule 25-30.140(2)(a), Florida Administrative Code, prescribes a 35 year life for supply mains recorded in NARUC Account 309 for Class A and B utilities. In response to a Commission staff request, the utility stated that WMSI was a Class C utility in 1985, and had used the prescribed 32 year life prescribed for Class C utilities. We believe that, because the utility is now subject to the Class A and B guidelines, it is more appropriate to use a 35 year life for purposes of this calculation, because the approved revenue adjustment will relate to future periods. The utility calculated the annual depreciation of the retired assets as $9,791, but did not include that amount as an offset to the depreciation expense for the new construction. Using a 35 year life for all of the retired assets, we calculate the annual depreciation as $8,992. We find that the utility's formula shall be adjusted to subtract that amount from the calculated depreciation on the new construction.

Depreciable Life for New Supply Main

In its final petition, the utility requests that the Commission approve a 30 year life for the portion of the new supply main which is attached to the bridge and exposed to air and salt spray. In the Phase 2 Supplemental Petition, the utility had described this main as a transmission main, for which the guideline depreciation rate would be 40 years. The utility requested a reduced depreciable life, and we approved a 5-year reduction from the guideline rate. In the final petition, the utility points out that the asset in question is actually a supply main, for which the guideline life is 35 years. WMSI states that the characterization of the main as a transmission main was a clerical error. The utility states that the same factors which were considered by the Commission in approving a 5-year reduction in the life of the exposed portion of the main are still relevant, and requests approval of a 30 year life for the exposed supply main and a 35 year life for the buried portion of the main.

In its May 4, 2005 letter, OPC states that "the utility changed the Commission approved depreciation rate for the water main now called a supply main from 35 to 30 years." OPC believes that this is an untimely motion for reconsideration of a final order, that the Commission fully considered the issue during the Phase 2 proceeding, and that a 35 year life is reasonable and should be used.

In its response to OPC's letter, WMSI states that it is only asking the Commission to recognize that there was an error in nomenclature, and to apply its previously approved adjustment for adverse environmental conditions to the correct category. The utility cites to Sunshine Utilities v. Public Service Commission, 577 So. 2d 663 (Fla. 1st DCA 1991), in which the Court upheld a Commission order that properly corrected a rate base computation in a prior Commission order issued five years earlier that required the utility to make refunds, holding that the Commission "has the authority to determine whether there are mistakes of this character in its prior orders and has a duty to correct such errors." Id. at 665.

After reviewing the above case and considering the parties' arguments, we find that the utility's request shall be approved. The final phase of this proceeding was always intended to consider all of the relevant facts in setting final rates. The main in question is clearly a supply main, properly assigned to NARUC Account 309, for which the guideline life is 35 years. We find that the rationale we employed in approving a 5-year reduction for the exposed portion of the main is still appropriate, and that we have the authority to approve this correction.

Amortization of Retired Supply Main

WMSI included in its final petition a provision for amortization of the undepreciated portion of the supply main which was replaced. The calculation of the requested amortization amount of $14,631 was provided in Schedule 2, page 2 of 3. In its May 4, 2005 letter, OPC notes that this factor was not included in the Phase 2 proceeding. OPC also expressed concern with the calculation of the amortization, the source of the figures used in Schedule 2, and the depreciation lives used.

In its response to OPC's letter, the utility correctly points out that the amortization could not have been included in the prior phases of this proceeding, because the date of the retirement would not have been known at that time. Further, WMSI states that the calculation was performed in accordance with Rule 25-30.443(9), Florida Administrative Code, and that the source of the figures was the company books, which were subject to audit by the Commission.

In response to questions about the calculation of the amortization amount, the utility stated that none of the retired property was contributed, and that the assets were not salvaged because the cost of preparing them for salvage would have exceeded the amount which might have been received. As noted in the previous discussion of depreciation expense for the retired main, the utility used a 32 year life for the portion of the retired assets placed in service in 1985. We believe that the appropriate life for purposes of this calculation is 35 years, because WMSI is now a Class A utility. We also questioned the discrepancy between the retirement date of December 31, 2003, used in WMSI's calculation, and the fact that the retirement was included in the utility's 2004 Annual Report. The utility responded that the actual date that the retirement was recorded in its books was February 27, 2004. WMSI provided an updated calculation of an amortization amount of $14,298, using a 35 year life for all of the assets and February 27, 2004, as the retirement date.

We have reviewed the supplemental data provided by WMSI, and believe that the revised calculation is in accordance with Rule 25-30.443(9), Florida Administrative Code. Accordingly, we find that the calculation of revenue requirement for final rates shall include amortization of undepreciated prudently retired plant in the amount of $14,298.

Incremental Property Insurance

In its May 4, 2005 letter, OPC questions whether the utility has provided support for the amount of the increase in property insurance cost. Further, OPC notes that the insured cost of the old main as stated on Schedule 2, page 3 of 3 ($113,000) differs from the total cost of the retired assets shown on Schedule 2, page 2 of 3 ($314,709).

In its response to OPC's letter, WMSI states that the information provided in the final petition was taken from a summary of present and subsequent premiums provided by the utility's insurance agent, and that the information was available to the Commission staff auditor, who made no comment in the audit report. In response to a request for additional information, the utility provided copies of the actual Common Policy Declarations and Notices of Acceptance detailing the property covered and the applicable premiums, as well as documentation of payment of the premiums. The utility also provided a copy of the original memorandum which was the basis for the amount of increased insurance cost included in the final petition. WMSI stated that it is not known why the insured value of the old main was less than the cost reflected on the books; however, the utility noted (and the documents provided supported) that the amount of the premium on the old assets was $147, as reflected on Schedule 2, page 3 of 3.

We have reviewed the information provided and the utility's explanation, and we find that WMSI's requested amount, $8,253, shall be included as incremental insurance cost in the calculation of the revenue requirement for final rates.

Used and Useful Analysis of Transmission and Distribution Mains

In its May 4, 2005 letter, OPC asks whether we have considered the "used and usefulness of additional island water distribution mains added to WMSI's system, since the Commission's last order in this limited proceeding." In a follow-up memorandum, OPC stated its belief that "a used and useful analysis should be performed on all water distribution pipes installed on the island since the 'first' Commission Order was issued in this Limited Proceeding, not the 'last' Commission Order issued in this proceeding. This analysis should be performed on all of the additions to the WMSI's island transmission and distribution mains since the inception of this limited proceeding."

WMSI's response stated that, in the Phase 2 PAA Order, the Commission found the utility's proposal for fire flow improvements including 17,700 feet of 6 inch and 8 inch mains, a new 200,000 gallon elevated storage tank, high speed service pumping, an emergency generator and other plant improvements to be prudent. Further, the utility noted that the settlement agreement resolving the protests of the Phase 2 PAA Order called for using the money originally approved for the new storage tank to be spent instead to complete the looping of the water mains. In the final petition, WMSI stated that a total of approximately 35,000 feet of 6 inch and 8 inch distribution lines were installed pursuant to the Phase 2 PAA Order and the settlement agreement. The utility's response to OPC's letter and memorandum noted that the Commission accepted the settlement agreement, and by inference, approved the prudence of all of the new mains. WMSI explained that the lines were not installed for the sole purpose of providing potable water to individual lots, because this was already being done by existing lines. The utility reiterated its belief that the new lines, "roughly half of which have been designed and installed at the request and agreement of OPC, are used and useful in the provision of the enhanced fire protection service and capacity."

We agree with the utility's assertion that the prudence of the installation of the transmission and distribution lines included in the final petition was established by the Phase 2 PAA Order and the subsequent settlement agreement. Pursuant to their review of the utility's expenditures related to this limited proceeding, the Commission staff auditors did not state any exceptions to WMSI's final listing and categorization of plant additions as stated in Schedule 2, page 1 of 3. Accordingly, we find that no used and useful adjustment shall be made with respect to the transmission and distribution mains included in the final petition.

Rate Case Expense

In its final petition, WMSI included a request for recovery of the cost of pursuing this limited proceeding. In Schedule 2, page 3 of 3, the utility provided details of actual and projected expenses totaling $74,043, of which the utility is including 25 percent ($18,511) in its calculation of additional revenue requirement. In response to a request, WMSI provided copies of invoices in support of the amounts claimed. We have reviewed the data submitted and believe that the utility's request is reasonable, with one exception. The utility included $2,100 in legal fees from Nicholas Yonclas, P.A. for "legal representation regarding water tower." Our review of the invoices provided by the utility indicates that this representation relates to the protests of the Phase 2 PAA Order and the resulting negotiated settlement agreement. In the Settlement Agreement Order, we ruled that "both Petitions shall be deemed to be resolved, with both parties bearing their own expenses associated with this proceeding (OPC on behalf of the customers and the shareholders of the company on behalf of WMSI)." As a result of this agreement, we find that the legal fees for the representation by Nicholas Yonclas, P.A. shall not be included in the cost of pursuing this limited proceeding. Accordingly, we hereby approve a reduction in the amount of $525 (25 percent of $2,100) to the utility's calculated expense of pursuing this proceeding.

Summary of Revenue Requirement Calculation

In Schedule 1, page 2 of 3, of the final petition, WMSI provided details of billing units and consumption for the year ended June 30, 2004, along with a calculation of the revenue expected to be generated by those billing determinants at the rates approved in Phase 2 of this proceeding. The expected total revenue calculated by the utility was $1,322,599, which included $486,259 of revenue resulting from the excess of the approved Phase 2 rates over the rates in effect prior to the filing of this limited proceeding. As noted above, the utility calculated a final additional revenue requirement of $551,140, or an increase of $64,881 over the additional revenue provided by the Phase 2 rates. WMSI's total final revenue requirement request was $1,387,480, an increase of 4.9 percent over the total Phase 2 revenue estimate of $1,322,599.

The billing determinants provided in Schedule 1, page 2 of 3, reflected total consumption of 175,747,000 gallons; however, in its response to a data request, the utility provided a revised total of 178,638,000 gallons along with some changes in billing categories. Using the utility's revised figure, we recalculated the excess of revenue from Phase 2 rates over pre-filing rates as $489,584. As shown in Table 2, our approved adjustments to WMSI's calculation of total final additional revenue requirement reduced that amount from $551,140 to $537,163. The excess of this amount over our recalculated additional revenue provided from Phase 2 rates is $47,579. Adding this amount to the utility's estimated total Phase 2 revenue ($1,322,599) results in a tentative final revenue requirement of $1,370,178.

As will be discussed later in this Order, we find that a repression adjustment is appropriate. This results in an adjustment of $1,371. To calculate the impact of this adjustment on the revenue requirement in rate cases, we would normally make an adjustment to reduce purchased power and chemicals included in the Operation and Maintenance (O & M) expenses that are part of a utility's filing. In this proceeding, the utility has not filed a detailed description of its O & M expenses; however, the Commission staff audit included an examination of WMSI's O & M expenses for the year ended June 30, 2004. The total amount of purchased power and chemicals, per the audit report, was $59,867. Accordingly, our approved final revenue requirement for this proceeding is $1,368,807. Our approved adjustments are summarized in Table 2 below.

Table 2 – Revenue Calculation

	Per Utility	Commission Approved Adjustments	Commission Adjusted
Total Depreciable Cost of Project	$6,136,385	-$37,310	$6,099,075
Land	$20,151	$0	$20,151
One-half Year Depreciation	-$96,116	$605	-$95,511
Net Cost	$6,060,420	-$36,705	$6,023,715
Average Depreciation on Total Cost at 3.13%	$192,233	-$1,210	$191,023
Interest on Net Cost at 3.48%	$211,622	-$1,929	$209,693
Personal Property Tax on Net Cost at 1.14%	$69,089	-$359	$68,730
Rate case Expense	$18,511	-$525	$17,986
Increased Property Insurance Cost	$8,253	$0	$8,253
Cost of Annual Audit	$12,000	$0	$12,000
Amortization of Retired Property	$14,631	-$333	$14,298
Depreciation on Retired Property	$0	-$8,992	-$8,992
Subtotal	$526,339	-$13,348	$512,991
Gross-up for RAF at 4.5%	$24,801	-$629	$24,172
Total Additional Revenue	$551,140	-$13,977	$537,163
Additional Revenue From Phase 2 Rates	$486,259	$3,325	$489,584
Excess of Additional Revenue Over Phase 2 Revenue	$64,881	-$17,302	$47,579
Expected Total Revenue at Phase 2 Rates	$1,322,599	$0	$1,322,599
Tentative Required Final Revenue Requirement	$1,387,480	-$17,302	$1,370,178

Repression Adjustment	$0	-$1,371	-$1,371
Required Final Revenue Requirement	$1,387,480	-$18,673	$1,368,807

REDUCTION IN RATES FOR FIRST YEAR TO RETURN OVER-COLLECTION

In its final petition, WMSI requested that it be allowed to collect a surcharge of $72,957 from ratepayers during the first twelve months that final rates are in effect. The utility stated that the Phase 2 rate increase went into effect in September 2003, on the assumption that all of the constructed plant would go into service in the first half of 2004. The utility stated that, in fact, some of the new construction was placed in service as early as January 2001, and that the calculation of depreciation accrual should begin at the actual in-service date. The utility also noted that it was required to fund a one-time reserve payment of $209,785 in 2003 in conjunction with the construction loan from DEP.

The utility's original petition proposed that "to the extent that the additional revenues produced by the Phase I and Phase II rates either over- or under-recover the actual additional revenue requirement associated with the project during those time periods, the Phase III rates would be subject, for the first twelve months they are in effect, to a credit or surcharge in the amount necessary to effect a true-up." In the Phase 2 PAA Order, we held that the approved Phase 2 rates were "held subject to over-collection with interest pending the final decision in this docket."

Schedule 4 of the utility's final petition provides detail of interest, depreciation and rate case expense incurred from the inception of this limited proceeding through June 30, 2004, including the timing of the expenses. These amounts, along with the reserve payment, are compared with a calculation of the cumulative total revenue collected as a result of the Phase 1 and Phase 2 rate increases. WMSI concludes that the revenue required to fund the expenses is greater than the revenue collected by $72,957.

In its May 4, 2005 letter, OPC notes that the cost of funding the DEP loan reserve was not included in the Phase 1 or Phase 2 revenue requirements, and states that it does not believe that this cost should be included in determining whether a refund or surcharge is appropriate. In its response to OPC's letter, WMSI states that the reserve payment was addressed in the Supplemental Petition, and that it is an appropriate consideration for true-up because it was a cash expense incurred during the period in question. Further, the utility argues that "if the projected interest to be earned on the required cash reserve over twenty years is being included as part of WMSI's operating revenue, then it is only fair and appropriate to include the interest cost to WMSI for the cash required to fund this reserve for the twenty year period."

We considered the issue of the loan reserve payment in Phase 2 of this proceeding. In the Phase 2 PAA Order, we stated that:

> We also computed the annual revenue increase projected at the approved Phase 2 rates, less property taxes, as $415,977 ($490,959 - $74,982). We compared this amount with the total of the utility's first two payments on the SRF loan ($419,608, per Exhibit A of the supplemental petition). We believe that the

additional revenue to be received from Phase 2 rates is sufficient to meet the utility's needs, in view of the fact that the accrued property taxes will not be payable until November 2004.

We note that, in the final petition, WMSI's calculation of additional Phase 2 revenues collected was $486,259. As discussed previously in this Order, we recalculated this amount as $489,584, based on revised billing determinants. A comparison of this amount with the approved Phase 2 revenue requirement of $490,959 would indicate that the utility did not experience an unexpected shortfall of revenue from Phase 2 rates.

In Schedule 3, page 2 of 2, of the final petition, the utility calculates the effective interest rate of the DEP loan as 3.32 percent. In Schedule 3, page 1 of 2, this amount is then used in a calculation of an overall weighted interest rate of 3.48 percent for financing the construction which is the subject of this limited proceeding. We note that the calculation on Schedule 3, page 2 of 2, includes a factor for amortization of the loan reserve. This is consistent with the effective interest rate calculation we approved in the Phase 2 PAA Order. In a letter dated July 8, 2005, WMSI proposes to omit the reserve payment from the interest rate calculation, but to include it in the true-up. The utility states that this would result in a weighted interest rate of 3.37 percent, and an under-collection of $62,471. The utility further states that omitting the loan reserve payment from the true-up calculation would result in a severe cash flow shortfall for WMSI during the true-up period. In a letter dated July 29, 2005, OPC expressed its opposition to the utility's new proposal. In addition, OPC noted that the reserve payment would eventually be returned to WMSI at the end of the loan period. After considering the parties' arguments, and the data provided, we do not believe that it is appropriate to include the reserve as a separate cost for purposes of calculating a true-up, while at the same time including the amortization of the reserve in the calculation of the effective interest rate used in calculating the final revenue requirement. Accordingly, we find that the reserve payment of $209,785 shall not be included in the true-up calculation.

The utility's true-up calculation in Schedule 4 reflected a "total revenue requirement through 6/30/04" of $727,091, including the loan reserve payment. WMSI calculated a "cumulative total collected at phased rates" of $654,134. We have reviewed the utility's calculations and believe that they are reasonable, with the exception of the loan reserve payment. Subtracting the loan reserve payment from the utility's total revenue requirement reduces that amount to $517,306, which would result in an over-collection of $136,828. As a test of reasonableness, we reviewed the earnings and cost of capital reported in the utility's annual reports for the years 2000 through 2003. WMSI has no positive equity; therefore, the cost of capital consists of debt and customer deposits. After adjusting the cost rate on customer deposits to the Commission standard 6 percent for each year, we compared the utility's reported rate of return with its reported cost of capital for each year, and noted that, for all of the years except 2001, the utility was earning slightly more than 1 percent below its cost of capital. We calculated the additional revenue (grossed up for RAF) which would have been required to bring the utility's earnings within one percent of its reported cost of capital for each year. Our analysis is summarized in Table 3.

Table 3

Year	Adjusted Cost of Capital	One Percent Below Cost of Capital	Rate of Return	Required Revenue Increase (Decrease)
2000	10.23%	9.23%	8.02%	$8,331
2001	8.86%	7.86%	7.92%	($459)
2002	5.07%	4.07%	3.40%	$4,179
2003	3.94%	2.94%	2.59%	$20,813
		Total		$32,864

We considered offsetting the total net under earnings reflected in the utility's annual reports against our previously calculated over-collection of $136,828, resulting in a net over-collection of $103,964. However, as noted by OPC in its letter dated July 29, 2005, the annual reports have not been audited. Further, the utility's annual report for 2004 reflected a small over-earning posture. We believe that there is not sufficient support in the annual reports to offset apparent net under-earnings against the calculated over-collection. We believe that it is reasonable to return the over-collection to current customers by means of a credit over the first twelve months during which the final rates are in effect. The over-collection represents 10.0 percent of our approved final revenue requirement of $1,368,807. Accordingly, we find that the final rates approved in this proceeding shall be reduced by 10.0 percent for the first twelve months that the rates are in effect. These reduced rates are shown in Schedule No. 1 attached to this Order.

TEST YEAR BILLING DETERMINANTS

According to the utility's final petition, the utility reported test year billing determinants of 23,367 ERCs and 175,747 kgals. The utility's requested ERCs was based on its statement that effective November 2004, metering at the State Park would change, eliminating numerous smaller meters and replacing them with a 6" turbine meter; however, as of June 2005, one year after the end of the test period, this change has not yet occurred.

We believe it is inappropriate to set rates on the ERCs contained in the utility's filing. Our calculated test period ERCs are based on a compilation of the utility's monthly reports which have been filed in compliance with a prior Commission Order. (See Order No. PSC-00-2227-PAA-WU, issued November 21, 2000 in Docket No. 000694-WU, In re: Petition by Water Management Services, Inc. for limited proceeding to increase water rates in Franklin County, p. 14.) In addition, we used residential billing analysis data, including the reclassification of 180 bills from the residential to the nonresidential class, which was provided by the utility in response to a data request. We found apparent consumption discrepancies between the utility's filing, billing analysis data, and the consumption that results from a compilation of the above-referenced monthly reports. The initial resulting billing determinants were 24,465 ERCs and 178,637 kgals.

We received a letter from the utility dated July 8, 2005, in which the utility addressed specific areas of disagreement with our initial analysis of its petition. One area of disagreement was that, according to the utility, we erred in using raw, unadjusted kgals for rate setting which did not include any adjustments to account for leaks or meter reading errors. When this was discussed with the utility, the utility realized that it had not filed revised monthly consumption reports to reflect the corrected consumption information. On August 3, 2005, the utility provided an itemization of its monthly test year consumption adjustments totaling 2,620 kgals. Based on this information, we revised our number of kgals for rate setting purposes to 176,017 kgals. In addition, we recalculated ERCs, and find that the appropriate figure is 24,441 ERCs.

Based on the foregoing, we find that the appropriate test year billing determinants before repression are 24,441 equivalent residential connections (ERCs) and 176,017 kgals. Our analysis of the appropriate test year billing determinants is contained in Attachment A to this Order.

RATE STRUCTURE

The utility's current rate structure is the traditional base facility charge (BFC) / uniform gallonage charge rate structure. Under this usage-sensitive rate structure, customers are charged a monthly BFC of $33.06, plus $3.13 for each 1,000 gallons (kgal) used during the month. The utility's current rates were approved as a result of its Phase 2 filing in this case.

At the customer meeting held on September 12, 2000, during Phase One of this proceeding, several customers mentioned their preference for a rate structure with a greater emphasis placed on usage in order to reflect the different consumption habits of permanent residents versus renters. However, because the utility's Phase One increase in the instant docket was treated as an emergency, and because we did not have sufficient customer usage data at that time, we approved a continuation of the utility's BFC / uniform gallonage charge rate structure, but ordered that the utility's current rate structure be examined in Phase Three of this case. (See Order No. PSC-00-2227-PAA-WU at pp. 13-14.)

Based on the discussion contained in Attachments B and C to this Order, we find that the appropriate rate structure for this utility is a three-tier inclining-block rate structure. The appropriate usage blocks shall be set for monthly usage of: 1) 0 – 8 kgals; 2) 8.001 – 15 kgals; and 3) for usage in excess of 15 kgals. The appropriate rate factors are 1.0, 1.25 and 1.5, respectively, while the appropriate base facility charge cost recovery percentage shall be set at 50%. Our approved rate structure was designed in part to comply with the multi-tier inclining block rate structure conditions of the utility's Consumptive Use Permit issued by the Northwest Florida Water Management District. This also is discussed further in Attachment B to this Order.

REPRESSION ADJUSTMENT

Absent direct, comparable data from our database of utilities receiving price increases and decreases, we utilized the proportional equation approach to calculate the recommended repression adjustment, which is consistent with prior Commission orders. (See Order No. PSC-01-2385-PAA-WU, issued December 10, 2001, in Docket No. 010403-WU, In re: Application for staff-assisted rate case in Highlands County by Holmes Utilities, Inc., p. 22; Order No. PSC-02-1168-PAA-WS, issued August 26, 2002, in Docket No. 010869-WS, In re: Application for staff-assisted rate case in Marion County by East Marion Sanitary Systems, Inc., p. 40.) Our approved rate structure results in pre-repression price decreases below 12 kgal and nominal price increases from 12 kgal to 15 kgal; therefore, no repression adjustment is warranted for consumption less than 15 kgal.

The average, pre-repression monthly consumption for those customers using greater than 15 kgal is approximately 32.6 kgal. This level of consumption corresponds to a pre-repression price increase of approximately 25.5%. We found that, for utilities receiving a water system only increase, a price increase of 33.33% leads to a 6.98% reduction in consumption. These relationships may be used to solve for the anticipated consumption reduction as follows:

$$\frac{33.33\%\ \text{water-only increase}}{-6.98\%\ \text{consumption reduction}} = \frac{25.50\%\ \text{pre-repression price increase}}{\mathbf{X\%}\ \text{anticipated consumption reduction}}$$

X% = Repression = -5.34%

Residential kgals > 15 kgal	43,761.000
x Repression percent	-5.34%
= Residential kgals repressed	**-2,337.210**
Residential kgals repressed	-2,337.210
/ Total overall kgals	176,016.7
= Overall repression	**-1.3%**
Residential kgals after repr	148,180.790 kgals
+ General Service kgals	25,498.700 kgals
= Total kgals for rate setting	**173,679.490 kgals**

Based on the foregoing, we find that a repression adjustment is appropriate. Residential consumption shall be reduced by 1.6%, resulting in a consumption reduction of approximately 2,337.2 kgals. The resulting total water consumption for rate setting shall be 173,679.5 kgals, which represents a 1.3% reduction in overall consumption. In order to monitor the effects of both the changes in revenue and rate structure, the utility shall continue filing the monthly reports that were required by Order No. PSC-00-2227-PAA-WS. These reports shall be continued for a period of two additional years, beginning the first billing period after the approved rates go into effect. To the extent the utility makes adjustments to consumption in any month during the reporting period, the utility shall be ordered to file a revised monthly report for that month within 30 days after all adjustments to that month have been closed.

FINAL RATES

As discussed earlier in this Order, we found that the water revenues to be recovered through the rates approved by us herein are $1,368,807. We determined that the appropriate billing determinants before repression are 24,441 ERCs and 176,017 kgals. We also determined that the appropriate rate structure is a three-tier inclining block rate structure, with usage blocks of: 1) 0 – 8 kgals; 2) 8.001 – 15 kgals; and 3) usage in excess of 15 kgals, with a BFC cost recovery percentage of 50%. The appropriate usage block rate factors are 1.0, 1.25 and 1.5, respectively. The appropriate repression adjustment is 2,337.2 kgals. Therefore, the resulting approved monthly rates are shown in Schedule No. 1 to this Order.

Our approved increase in revenue requirement is $46,208 (approximately 3.5% over Phase 2 rates, and approximately 64.7% over pre-filing rates). Approximately 50% (or $684,403) of the revenue requirement is recovered through ERCs, while approximately 50% (or $684,404) represents revenue recovery through the consumption charges.

As discussed in Attachment B to this Order, the utility has a seasonal customer base, and, in the utility's 1994 rate case, we approved a rate design more heavily weighted to the BFC to increase cash flow during the utility's off-season. However, our approved BFC in the instant case represents an approximate 15% reduction from the current BFC. We prepared a cost recovery analysis in order to determine whether the fixed revenue stream generated from our final approved rates would cover the utility's requested 58% cost recovery from monthly base facility charges. This analysis, contained in page 1 of Attachment C, demonstrates that, based on our approved final rates, the utility's fixed revenue stream each month generates approximately $26,200 (or 40%) in excess of the requested fixed recovery amount. As discussed earlier in this Order, we approved a credit of 10.0 percent to be reflected as reduced rates for a period of one year. A similar analysis, contained in page 2 of Attachment C, demonstrates that, with the reduced rates for one year, the utility continues to recover in excess of its requested fixed recovery by approximately 26%.

In the utility's July 8, 2005 letter, the utility stated that our fixed cost recovery /fixed revenue stream analysis was flawed. The utility stated that "Under the current rate structure, the BFC accounts for 58% of revenues and staff has apparently assumed that the BFC includes all fixed costs. It does not and never has. Fixed monthly costs are those recurring costs that the utility faces each month, regardless of output; i.e., even if only the minimum quantity of water is produced."

In ratemaking, the terms "revenue requirements" and "cost of service" are synonymous. If the utility has requested that 58% of the revenue requirement be generated from fixed charges, then it may also be said that the utility has requested that 58% of the costs be covered by fixed charges (i.e., through a fixed revenue stream). The purpose of fixed charges is to generate a fixed, stable revenue stream to cover fixed charges, and certainly the BFC represents an important component in any utility's fixed revenue stream. However, the minimum quantity of gallons sold each month represents the other component of any utility's fixed revenue stream. The purpose of Attachment C is to demonstrate that, based on the utility's request that 58% of the revenue requirement be recovered from fixed charges (a fixed revenue stream), our final rate structure and rates would more than meet the utility's 58% request.

Based on the foregoing, the appropriate water monthly rates are shown on Schedule No. 1 to this Order. Excluding miscellaneous service revenues, the approved water rates are designed to produce revenues of $1,368,807. The utility shall file revised tariff sheets and a proposed customer notice to reflect our approved rates. The approved rates shall be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code. In addition, the rates shall not be implemented until Commission staff has approved the proposed customer notice. The utility shall provide proof of the date the notice was given no less than 10 days after the date of the notice.

FOUR-YEAR RATE CASE EXPENSE REDUCTION

Section 367.0816, Florida Statutes, requires that the rates be reduced immediately following the expiration of the four-year period by the amount of the rate case expense previously included in the rates. The reduction will reflect the removal of revenues associated with the amortization of rate case expense in the amount of $17,986, grossed-up for regulatory assessment fees to $18,834. The decreased revenues will result in the rate reduction shown on Schedule No. 1 to this Order. The water rates shall be reduced as shown on Schedule No. 1 to remove $17,986 in rate case expense amortization, grossed-up for regulatory assessment fees.

The utility shall be required to file revised tariff sheets and a proposed customer notice to reflect the approved rates. The approved rates shall be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), Florida Administrative Code. The rates shall not be implemented until Commission staff has approved the proposed customer notice and the notice has been received by the customers. The utility shall provide proof of the date notice was given no less than 10 days after the date of the notice.

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 pass-through increase or decrease, and for the reduction in the rates due to the amortized rate case expense.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that final water rates for Water Management Services, Inc. are hereby approved as set forth in the body of this Order. It is further

ORDERED that the utility's final rates shall be decreased by 10.0% during the first twelve months that final rates approved in this proceeding are in effect in order to return to ratepayers revenues collected during Phase 1 and Phase 2 of this proceeding in excess of the actual incremental costs incurred by the utility. It is further

ORDERED that each of the findings made in the body of this Order are hereby approved in every respect. It is further

ORDERED that Schedule No. 1 and Attachments A, B, and C to this Order are incorporated herein by reference. It is further

ORDERED that the utility shall continue filing the monthly reports that were required by Order No. PSC-00-2227-PAA-WS. These reports shall be continued for a period of two years, beginning the first billing period after the approved rates go into effect. To the extent the utility makes adjustments to consumption in any month during the reporting period, the utility shall be ordered to file a revised monthly report for that month within 30 days after all adjustments to that month have been closed. It is further

ORDERED that the utility shall file revised tariff sheets and a proposed customer notice reflecting the approved rates. The approved rates shall be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code. It is further

ORDERED that the rates shall not be implemented until after the Commission staff has approved the proposed customer notice. The utility must provide proof of the date notice was given no less than 10 days after the date of the notice. It is further

ORDERED that rates shall be reduced at the end of the four-year rate case expense amortization period as set forth in the body of this Order. The utility shall file revised tariff sheets and a proposed customer notice setting forth the lower rates and the reason for the reductions no later than one month prior to the actual date of the required rate 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 for the reduction in rates due to the amortized rate case expense. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, except for our decision reducing rates at the end of the four-year rate case expense amortization period, shall become final and effective upon the issuance of a Consummating Order unless an appropriate petition, in the form provided by Rule 28-106.201, Florida Administrative Code, is received by the Director, Division of the Commission Clerk and Administrative Services, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings" attached hereto. It is further

ORDERED that in the event this Order becomes final, this docket shall be closed.

By ORDER of the Florida Public Service Commission this 21st day of November, 2005.

BLANCA S. BAYÓ, Director
Division of the Commission Clerk
and Administrative Services

(S E A L)

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), 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.

As identified in the body of this order, our action, except for our decision reducing rates at the end of the four-year rate case expense amortization period, is preliminary in nature. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, in the form provided by Rule 28-106.201, Florida Administrative Code. This petition must be received by the Director, Division of the Commission Clerk and Administrative Services, at 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on December 12, 2005. If such a petition is filed, mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing. In the absence of such a petition, this order shall become effective and final upon the issuance of a Consummating Order.

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.

Any party adversely affected by the Commission's final action, reducing rates at the end of the four-year rate case expense amortization period, in this matter may request: (1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of the Commission Clerk and Administrative Services within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or (2) 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 wastewater utility by filing a notice of appeal with the Director, Division of the Commission Clerk and Administrative Services 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 after the issuance 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.

WATER MANAGEMENT SERVICES, INC.
HISTORICAL TEST YEAR ENDED 6/30/04

ATTACHMENT A
PAGE 1 OF 1

COMPARISON OF COMMISSION v. UTILITY-FILED BILLING DETERMINANTS FOR RATESETTING

ERCs

Customers	ERCs Before Reclassification	Adjustments / Reclassification	Rate setting ERCs After Reclassification	ERCs Per Utility Filing	Com'n ERCs Greater Than Utility's Filing
Residential 5/8"	19,800		19,800	19,578	222
Residential 1"	970	(180)	790	958	(168)
Total Residential	**20,770**	**(180)**	**20,590**	**20,536**	**55**
All Other ERCs	**3,695**	**180**	**3,851**	**2,831**	**1,020**
TOTALS			**24,441**	**23,367**	**1,074**

CONSUMPTION (000)

Customers	Consump Before Reclassification	Adjustments / Reclassification	Rate setting Consump After Reclassification	Per Utility Filing	Com'n Consump Greater Than Utility's Filing
Residential 5/8"	149,076		149,076	146,198	
Residential 1"	5,767	(1,705)	4,062	5,755	
Total Residential	154,843	(1,705)	**153,138**	**151,953**	**1,185**
All Other Custs	23,794	1,705	**25,499**	**23,794**	**1,705**
Subtotals			**178,637**	**175,747**	**2,890**
Leaks / Bills Adjust		(2,620)			**(2,620)**
TOTAL			**176,017**	**175,747**	**270**

Sources: Water Management Services, Inc. (Utility), monthly reports filed in compliance with Order No. PSC-00-2227-PAA-WU; Utility Filing, Schedule 1; response to staff's first data request, item no. 1; response to staff's fourth data request, item no. 3; workpaper obtained from the utility during staff's site visit on July 28, 2005.

WATER MANAGEMENT SERVICES, INC.
HISTORICAL TEST YEAR ENDED 6/30/04

DETERMINATION OF APPROPRIATE RATE STRUCTURE

CURRENT RATES AND HISTORY OF CURRENT RATE STRUCTURE:

(1) The utility's current rate structure is the traditional base facility charge (BFC) / uniform gallonage charge rate structure. Under this usage-sensitive rate structure, customers are charged a monthly BFC of $33.06, plus $3.13 for each 1,000 gallons (kgal) used during the month. The utility's current rates were approved as a result of its Phase 2 filing in this case.

(2) The most recent time the utility's rates were adjusted as a result of a rate case was in Docket No. 940109-WU. In that case, the utility proposed a rate design more heavily weighted towards the BFC in order to increase cash flow to cover fixed expenses during the off-season. We approved the utility's request. (See Order No. PSC-94-1383-FOF-WU, issued November 14, 1994, in Docket No. 940109-WU, In re: Petition for interim and permanent rate increase in Franklin County by St. George Island Utility Company, Ltd., p. 64.)

(3) At the customer meetings held on September 12, 2000 during Phase One of this proceeding, several customers mentioned their preference for a rate structure with a greater emphasis placed on usage in order to reflect the different consumption habits of permanent residents versus renters. However, because the utility's Phase One increase in the instant docket was treated as an emergency, and because we did not have sufficient customer usage data at that time, we approved a continuation of the utility's BFC / uniform gallonage charge rate structure, but ordered that the utility's current rate structure be examined in Phase Three of this case. (See Order No. PSC-00-2227-PAA-WU, issued November 21, 2000, in Docket No. 000694-WU, In re: Petition by Water Management Services, Inc. for limited proceeding to increase water rates in Franklin County, pp. 13-14.)

PRIOR ORDERS AND PRACTICES WITH THE WATER MANAGEMENT DISTRICTS:

(4) The Commission has a Memorandum of Understanding (MOU) with the five Water Management Districts (WMDs or Districts). A guideline of the five Districts is to set the base facility charges such that they recover no more than 40% of the revenues to be generated from monthly service. (See Order No. PSC-02-0593-FOF-WS, issued April 30, 2002, in Docket No. 010503-WU, In re: Application for increase in water rates for Seven Springs system in Pasco County by Aloha Utilities, Inc., p. 81; Order No. PSC-03-1440-FOF-WS, issued December 22, 2003, in Docket No. 020071-WS, In re: Application for rate increase in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida, p. 144.) Based on our MOU with the Districts, we follow that guideline whenever possible. (See Order No. PSC-94-1452-FOF-WU, issued November 28, 1994, in Docket No. 940475-WU, In re: Application for rate increase in Martin County by Hobe Sound Water Company, p. 12; Order No. PSC-01-0327-PAA-WU, issued January 6, 2001, in Docket No. 000295-WU, In re: Application for increase in water rates in Highlands County by Placid Lakes Utilities, Inc., pp. 23, 28; Order No. PSC-00-2500-PAA-WS, issued December 26, 2000, in Docket No. 000327-WS, In re: Application for staff-assisted rate case in Putnam County by Buffalo Bluff Utilities, Inc., p. 27; Order No. PSC-02-0593-FOF-WS, issued April 30, 2002, in Docket No. 010503-WU, In re: Application for increase in water rates for Seven Springs system in Pasco County by Aloha Utilities, Inc., pp. 81-82.)

DETERMINATION OF APPROPRIATE RATE STRUCTURE (cont.)

PRIOR ORDERS AND PRACTICES WITH THE WATER MANAGEMENT DISTRICTS (cont):

(5) The BFC / uniform gallonage charge rate structure had been our rate structure of choice because it is designed to provide for the equitable sharing by the rate payers of both the fixed and variable costs of providing service. (See Order No. PSC-00-2227-PAA-WU, issued November 21, 2000, in Docket No. 000694-WU, In re: Petition by Water Management Services, Inc. for limited proceeding to increase water rates in Franklin County, p. 13.) However, over the past several years, based in large part on requests made by the WMDs, we have been implementing the inclining-block rate structure as our rate structure of choice. (See. Order No. PSC-03-0647-PAA-WS, issued May 28, 2003, in Docket No. 020407-WS, In re: Application for rate increase in Polk County by Cypress Lakes Utilities, Inc., p. 31; Order No. PSC-00-0248-PAA-WU, issued February 7, 2000, in Docket No. 990535-WU, In re: Request for approval of increase in water rates in Nassau County by Florida Public Utilities Company (Fernandina Beach System), p. 37; Order No. PSC-01-0327-PAA-WU, issued February 6, 2001, in Docket No. 000295-WU, In re: Application for increase in water rates in Highlands County by Placid Lakes Utilities, Inc., p. 25; Order No. PSC-02-0593-FOF-WS, issued April 30, 2002, in Docket No. 010503-WU, In re: Application for increase in water rates for Seven Springs system in Pasco County by Aloha Utilities, Inc., pp. 80-81; Order No. PSC-03-1440-FOF-WS, issued December 22, 2003, in Docket No. 020071-WS, In re: Application for rate increase in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida, pp. 184, 208.)

(6) Although the utility's current rate structure is considered usage sensitive because customers are charged for all water used, the WMDs do not consider this rate structure to be a conservation-oriented rate structure. (South Florida Water Management District, Section 2.6.1, District's Basis for Review; Northwest Florida Water Management District, Permit No. 20040013, p. 5.)

SPECIFIC CONCERNS OF THE NORTHWEST FLORIDA WATER MANAGEMENT DISTRICT:

(7) The utility is located in the Northwest Florida Water Management District (NWFWMD) in an area of special concern. The utility's current Consumptive Use Permit (CUP) was issued on March 25, 2004. Its previous CUP had expired due to the utility's failure to timely submit a request for renewal of water use. Additionally, WMSI failed to comply with its pumping limits and a number of the specific conditions of the expired permit. (Northwest Florida Water Management District, Staff Report to Governing Board (District Staff Report), February 13, 2004, p. 1.)

(8) According to the above-referenced District Staff Report issued to the Governing Board before the current CUP was renewed, one of the permit conditions that WMSI failed to comply with was consistently reporting its progress in implementing water conservation and efficiency measures. (Ibid.)

DETERMINATION OF APPROPRIATE RATE STRUCTURE (cont.)

SPECIFIC CONCERNS OF THE NORTHWEST FLORIDA WATER MANAGEMENT DISTRICT (cont.):

(9) WMSI's cumulative drawdown, coupled with water quality data that may indicate an increasing trend in chloride concentrations, indicate a future potential for adverse impacts from WMSI's withdrawals. (Ibid., p. 2.) The current permit expires on April 1, 2006. The current permit duration is two years rather than five years so that the District may closely monitor WMSI's compliance with its permit. (Ibid.)

(10) A specific permit condition of the utility's current CUP is that WMSI, by July 31, 2005, implement "action towards the adoption of a rate structure that promotes water efficiency and conservation (e.g., a multi-step inverted block rate structure)." (Northwest Florida Water Management District Individual Water Use Permit No. 20040013, issued to Water Management Services, Inc. on March 25, 2004, p. 5.)

UTILITY'S REQUESTED PHASE THREE RATES AND RATE STRUCTURE:

(11) The utility requested a continuation of its BFC / uniform gallonage charge. The requested BFC was increased from \$33.06 to \$34.68, representing an increase of 4.9%. The gallonage charge was increased from \$3.13 to \$3.28, or 4.8%. Application of the utility's requested BFC and gallonage charges result in 58% of the requested revenue requirement being recovered through the BFC and the remaining 42% through the gallonage charges. (Water Management Services, Inc., Phase Three Petition, Schedule 1, p. 2)

THEORY BEHIND INCLINING BLOCK RATE STRUCTURES:

(12) The goal of the inclining block rate structure is to reduce average demand. Under this rate structure, it is anticipated that demand in the higher usage blocks will be more elastic (responsive to price) than demand in the first usage block.

(13) There are several factors to consider when designing inclining block rates, including, but not limited to, selection of the appropriate: a) BFC cost recovery percentage and the required conservation adjustment; b) usage blocks; and c) usage block rate factors.

BFC COST RECOVERY, USAGE BLOCKS AND RATE FACTORS:

(14) Approximately 64% of the utility's bills and 41% of the corresponding kgals are captured at 5 kgal or less. The majority of consumption at or below 5 kgal is considered highly nondiscretionary, essential consumption. Therefore, an important rate design goal is to minimize, to the extent possible, the price increases at 5 kgal or less. (See Order No. PSC-94-1452-FOF-WU, issued November 28, 1994, in Docket No. 940475-WU, In re: Application for rate increase in Martin County by Hobe Sound Water Company, p. 12; Order No. PSC-02-0593-FOF-WS, issued April 30, 2002, in Docket No. 010503-WU, In re: Application for increase in water rates for Seven Springs system in Pasco County by Aloha Utilities, Inc., p. 83; Order No. PSC-03-1440-FOF-WS, issued December 22, 2003, in Docket No. 020071-WS, In re: Application for rate increase in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida, pp. 143-144.)

WATER MANAGEMENT SERVICES, INC.
HISTORICAL TEST YEAR ENDED 6/30/04

DETERMINATION OF APPROPRIATE RATE STRUCTURE (cont.)

BFC COST RECOVERY, USAGE BLOCKS AND RATE FACTORS (cont.):

(15) Based upon our site evaluation of the utility's service area, there is a great size disparity among residential customers' homes. There is a greater percentage of nondiscretionary consumption in smaller homes than in the much larger homes.

(16) It is important to quantify the consumption disparity in order to appropriately target high-end users while rewarding those customers who usage is mainly nondiscretionary. Therefore, a consumption analysis, detailing relationships between the percentage of bills and the related percentage of kgals captured at given consumption levels, is detailed in Table 4 below.

TABLE 4

	IF THE FOLLOWING PERCENTAGE OF BILLS AND KGALS ARE CAPTURED AT THESE LEVELS:		THEN THE REMAINING PERCENTAGE OF BILLS ACCOUNT FOR THE REMAINING PERCENTAGE OF KGALS USED:	
(a)	(b)	(c)	(d) = 100% - (b)	(e) = 100% - (c)
Consump:	% Bills	% Kgals	% Bills	% Kgals
8 kgals	75%	53%	25%	47%
10 kgals	80%	59%	20%	41%
15 kgals	88%	70%	12%	30%
20 kgals	92%	77%	8%	23%

(17) As shown in columns (b) and (c) of Table 4, approximately 80% of the utility's bills and 59% of the corresponding kgals are captured at consumption of 10 kgal or less, 88% of the bills and 70% of the kgals are captured at consumption of 15 kgal or less, and 92% of the bills and 77% of the kgals are captured at consumption of 20 kgal or less.

(18) As shown in columns (e) and (d) on Table 4, 41% of the water is used by only 20% of the bills at usage levels of 10 kgal or greater. Similarly, 30% of the water is used by only 12% of the bills at usage levels of 15 kgal or greater, and 23% of the water is used by only 8% of the bills at usage of 20 kgal or greater. These figures represent consumption disparities at usage levels greater than 8 kgal.

(19) Based on a detailed analysis of the utility's billing data, plus the information contained in Table 4 above, we find that a three-tiered inclining block rate structure is appropriate. The usage blocks are for monthly usage of: a) 0 – 8 kgal; b) 8.001 – 15 kgal; and c) in excess of 15 kgal.

WATER MANAGEMENT SERVICES, INC.
HISTORICAL TEST YEAR ENDED 6/30/04

DETERMINATION OF APPROPRIATE RATE STRUCTURE (cont.)

BFC COST RECOVERY, USAGE BLOCKS AND RATE FACTORS (cont.):

(20) Setting the BFC to 40% would reduce the current BFC by approximately 32%. This represents a significant reduction in the current BFC. We believe setting the BFC to 50%, representing a 15% reduction, is more appropriate. In instances in which the recommended BFC represents a significant reduction from the current BFC, it is appropriate to evaluate the utility's fixed vs. variable cost recovery (fixed vs. variable revenue streams). This analysis is included in Attachment C to this Order addressing the appropriate rates for WMSI. Based upon the results of the analysis in Attachment C, we find that reducing the BFC to 50% does not harm the utility.

APPROVED RATE STRUCTURE

Based on the foregoing, we find that the appropriate rate structure is the three-tiered inclining block rate structure with usage blocks for monthly consumption at: 1) 0-8 kgal; 2) 8.001-15 kgal; and 3) for usage in excess of 15 kgal. A BFC cost recovery percentage of 50%, coupled with rate factors of 1.0, 1.25 and 1.5 best captures the balance between revenue stability and conservation pricing. Furthermore, it addresses the customers' preference for a rate structure with a greater emphasis placed on usage, and satisfies the rate structure requirement that the NWFWMD has placed on the utility.

WATER MANAGEMENT SERVICES, INC.
HISTORICAL TEST YEAR ENDED 6/30/04

COST RECOVERY ANALYSIS: FIXED

(A) Assumptions:

1. The utility's revenue requirement is $1,368,807.

2. Approximately 58% of the utility's revenues represent fixed recovery of the utility's costs. This is consistent with the fixed vs. variable cost recovery that is represented in WMSI's Phase Three filing on Schedule 1, p. 2.

3. The utility's fixed monthly revenue stream should be used to cover its fixed cost recovery.

4. The revenues generated from the minimum number of gallons sold each month represent part of the utility's monthly fixed revenue stream. The month in which the fewest gallons are sold by WMSI occurs in February of each year. Therefore, the number of February gallons sold represents the minimum gallons the utility can expect to sell each month, and should be included as part of the cost recovery analysis from fixed revenue streams.

(B) Analysis:

	Annual Revenue Requirement	**($1,368,807)**	
x	Requested Percentage of Fixed Recovery	58%	
=	Annual Fixed Recovery	($793,908)	
/	Months in a Year	12	
=	**Monthly Fixed Recovery**		**($66,159)**
	<u>**Recovery from Approved BFC Revenues:**</u>		
	Annual Residential BFC Revenues	$576,727	
less	Divided by 12 Months = Monthly RS BFC Revs		**$48,061**
	Annual Nonresidential BFC Revenues	$107,867	
less	Divided by 12 Months = Monthly NonRS Revs		**$8,989**
=	**Remaining Monthly Fixed Recovery from Sales of Kgals**		**($9,109)**
	<u>**Recovery From Minimum Monthly Kgals Sold Each Month:**</u>		
	Minimum Monthly Kgals Sold (occurs in Feb)	9,429.158	
	X 65% Min Kgals Sold @ Block 1 Rate	$20,409	
	X 20% Min Kgals Sold @ Block 2 Rate	$7,850	
	X 15% Min Kgals Sold @ Block 3 Rate	$7,065	
less	**Minimum Monthly Kgal Revenues**		**$35,324**
=	**Surplus (Remaining) Monthly Fixed Recovery**	**Amount**	**$26,215**
		Percent	**40%**

WATER MANAGEMENT SERVICES, INC. **ATTACHMENT C**
HISTORICAL TEST YEAR ENDED 6/30/04 **PAGE 2 OF 2**

COST RECOVERY ANALYSIS: FIXED

(A) Assumptions:

1. The utility's revenue requirement is $1,368,807 **(excludes credit).**
2. Approximately 58% of the utility's revenues represent fixed recovery of the utility's costs. This is consistent with the fixed vs. variable cost recovery that is represented in WMSI's Phase Three filing on Schedule 1, p. 2.
3. The utility's fixed monthly revenue stream should be used to cover its fixed cost recovery.
4. The revenues generated from the minimum number of gallons sold each month represent part of the utility's monthly fixed revenue stream. The month in which the fewest gallons are sold by WMSI occurs in February of each year. Therefore, the number of February gallons sold represents the minimum gallons the utility can expect to sell each month, and should be included as part of the cost recovery analysis from fixed revenue streams. **This analysis reflects rates including 10% credit.**

(B) Analysis:

	Annual Revenue Requirement (excludes credit)	**($1,368,807)**	
x	Requested Percentage of Fixed Recovery	58%	
=	Annual Fixed Recovery	($793,908)	
/	Months in a Year	12	
=	**Monthly Fixed Recovery**		**($66,159)**
	<u>Recovery from Approved BFC Revs (incl credit):</u>		
	Annual Residential BFC Revenues	$519,055	
less	Divided by 12 Months = Monthly RS BFC Revs		**$43,255**
	Annual Nonresidential BFC Revenues	$97,081	
less	Divided by 12 Months = Monthly NonRS Revs		**$8,090**
=	**Remaining Monthly Fixed Recovery from Sales of Kgals**		**($14,814)**
	<u>Recovery From Minimum Monthly Kgals Sold Each Month (incl credit):</u>		
	Minimum Monthly Kgals Sold (occurs in Feb)	9,429.158	
	X 65% Min Kgals Sold @ Block 1 Rate	$18,368	
	X 20% Min Kgals Sold @ Block 2 Rate	$7,065	
	X 15% Min Kgals Sold @ Block 3 Rate	$6,358	
less	**Minimum Monthly Kgal Revenues**		**$31,792**
=	**Surplus (Remaining) Monthly Fixed Recovery**	**Amount**	**$16,977**
		Percent	**26%**

Sources: Water Management Services, Inc. (Utility), monthly reports filed in compliance with Order No. PSC-00-2227-PAA-WU; Utility's Filing, Schedule 1; Utility's response to staff's fourth data request, item 3; Table 2; Schedule 1.

Schedule No. 1

Water Management Services, Inc.
Water Monthly Service Rates

	Rates Prior to Filing	Commission Approved Phase 2	Utility Requested Final	Commission Approved Final	12-month True-Up Rates	4-year Rate Reduction
Residential and General Service						
Base Facility Charge by Meter Size:						
5/8" x 3/4"	$20.90	$33.06	$34.68	$28.01	$25.21	$0.39
3/4"	N/A	N/A	N/A	$42.02	$37.81	$0.58
1"	$52.25	$82.66	$86.71	$70.03	$63.02	$0.96
1 1/2"	$104.51	$165.34	$173.45	$140.05	$126.05	$1.93
2"	$167.20	$264.52	$277.50	$224.08	$201.67	$3.08
3" Compound	$334.40	$529.03	$554.98	$420.15	$378.14	$5.78
3" Turbine	$365.77	$578.67	$607.06	$490.18	$441.16	$6.74
4" Compound	$522.52	$826.50	$867.04	$700.25	$630.23	$9.63
4" Turbine	$627.02	$991.98	$1,040.64	$840.30	$756.27	$11.56
6" Compound	$1,045.03	$1,653.00	$1,734.09	$1,400.50	$1,260.45	$19.27
6" Turbine	$1,306.30	$2,066.64	$2,168.02	$1,750.63	$1,575.56	$24.09
8" Compound	$1,672.05	$2,644.80	$2,774.40	$2,240.80	$2,016.72	$30.83
8" Turbine	$1,881.06	$2,975.40	$3,121.20	$2,520.90	$2,268.81	$34.69
10" Compound	$2,403.58	$3,801.90	$3,988.20	$3,221.15	$2,899.04	$44.32
10" Turbine	$3,030.59	$4,793.70	$5,028.60	$4,061.45	$3,655.31	$55.88
12" Compound	$4,493.65	$6,281.40	$7,456.20	$6,022.15	$5,419.94	$82.86
Gallonage Charge, per 1,000 gallons						
Current and Requested, Residential	$1.98	$3.13	$3.28	N/A	N/A	N/A
Residential						
0 - 8 kgal	N/A	N/A	N/A	$3.33	$3.00	$0.05
8 - 15 kgal	N/A	N/A	N/A	$4.16	$3.74	$0.06
Over 15 kgal	N/A	N/A	N/A	$5.00	$4.50	$0.07
General Service	$1.98	$3.13	$3.28	$4.74	$4.27	$0.07
	Typical Residential Bills 5/8" x 3/4" Meter					
3,000 Gallons	$26.84	$42.45	$44.52	$38.00	$34.21	
8,000 Gallons	$36.74	$58.10	$60.92	$54.65	$49.21	
10,000 Gallons	$40.70	$64.36	$67.48	$62.97	$56.69	
17,000 Gallons	$54.56	$86.27	$90.44	$93.77	$84.39	