

BEFORE THE PUBLIC SERVICE COMMISSION

In re: Application for increase in water and
wastewater rates in Highlands County by Lake
Placid Utilities, Inc.

DOCKET NO. 060260-WS
ORDER NO. PSC-06-0662-FOF-WS
ISSUED: August 7, 2006

The following Commissioners participated in the disposition of this matter:

LISA POLAK EDGAR, Chairman
J. TERRY DEASON
ISILIO ARRIAGA
MATTHEW M. CARTER II
KATRINA J. TEW

ORDER SUSPENDING PROPOSED FINAL RATES AND
DENYING INTERIM RATES

BY THE COMMISSION:

Lake Placid Utilities, Inc. (Lake Placid or utility) is a Class C utility providing water and wastewater service to approximately 125 water and 194 wastewater customers in Highlands County. Water and wastewater rates were last established for this utility in its 1995 rate proceeding in Order No. PSC-96-0910-FOF-WS, issued July 15, 1996, in Docket No. 951027-WS, In re: Application for rate increase in Highlands County by Utilities, Inc.

On May 11, 2006, the utility filed its application for approval of final and interim rate increases in this docket and requested that we process the case under the Proposed Agency Action (PAA) procedure. After review of the Minimum Filing Requirements (MFRs), we determined that the MFRs contained a number of deficiencies that will require revisions by the utility. These revisions will not be received until after the statutory 60-day limit to suspend the requested interim rate increase; therefore, the official filing date has not been established.

The test year for interim and final purposes is the historical test year ended December 31, 2005. Lake Placid has requested an annual interim revenue increase of \$49,376 or 70.12% for wastewater only. The utility has requested final revenue increases of \$30,017 (66.12%) for water and \$41,902 (102.12%) for wastewater.

The sixty-day statutory deadline for this Commission to suspend the utility's requested final rates was July 16, 2006. However, by letter dated June 5, 2006, the utility agreed to extend the statutory time frame by which this Commission is required to address Lake Placid's interim rate request. By letter dated May 24, 2006, the utility confirmed that it was not requesting interim water rates. This Order addresses the suspension of Lake Placid's final rates and the interim wastewater rate request. We have jurisdiction pursuant to Sections 367.081, and 367.082, Florida Statutes.

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SUSPENSION OF RATES

Section 367.081(6), Florida Statutes, provides that the rates proposed by the utility shall become effective within sixty days after filing unless we vote to withhold consent of implementation of the requested rates. Further, Section 367.081(8), Florida Statutes, permits the proposed rates to go into effect, secured and subject to refund, at the expiration of five months if we have not acted upon the requested rate increase or if PAA action is protested by a party other than the utility.

We have reviewed the filing and have considered the proposed rates, the revenues thereby generated, and the information filed in support of the rate application. We find that it is reasonable and necessary to require further amplification and explanation regarding this data, and to require production of additional and/or corroborative data. This further examination will include on-site investigations by our staff accountants and engineers. Based on the foregoing, we find that it is appropriate to suspend the utility's proposed rate increase.

INTERIM RATES

Lake Placid requested wastewater interim rates designed to generate annual revenues of \$119,788. This represents an increase of \$49,376 (70.12%). The utility has filed rate base, cost of capital, and operating statements to support its requested interim water and wastewater increase for the test year ended December 31, 2005.

Pursuant to Section 367.082(5)(b)1., Florida Statutes, the achieved rate of return for interim purposes shall be calculated by applying appropriate adjustments consistent with those made in the utility's most recent rate proceeding. We have reviewed the utility's interim request, as well as prior orders concerning the utility's rate base. The adjustments are discussed below. We have attached accounting schedules to illustrate the approved rate base, capital structure, and test year operating income amounts. The rate base schedule is labeled as Schedule No. 1, with adjustments shown on Schedule No. 1-A; the capital structure is shown on Schedule No. 2, and the operating income schedule is labeled as Schedule No. 3, with the adjustments shown on Schedule No. 3-A.

RATE BASE

In its application, Lake Placid used a simple average to calculate its requested rate base and cost of capital. Lake Placid is a Class C utility and filed its interim request consistent with the averaging requirement of Rule 25-30.433(4), Florida Administrative Code.

Used And Useful

In MFR Schedule F-4, the utility requested that the wastewater treatment plant be considered 86% used and useful. This determination is based on a four month seasonal flow average which occurred during the test year from January through April of 2005. The treatment plant is permitted by the Department of Environmental Protection (DEP) on an annual average

daily flow (AADF). Rule 25-30.432, Florida Administrative Code, indicates that used and useful percentages shall be based on the stated DEP permitted capacity. For comparison purposes, the utility provided used and useful analysis for both the AADF and seasonal flows. The AADF calculation showed a 43% used and useful determination.

The utility has indicated that Rule 25-30.432, Florida Administrative Code, permits this Commission to consider other factors. Lake Placid believes that circumstances in this case should allow for flows reflecting the seasonality of customer occupancy. The utility states that the use of AADF cannot properly reflect these flows in a used and useful determination. Rule 25-30.432, Florida Administrative Code, does allow for other flow considerations such as infiltration and inflow, permitted capacity differing from design capacity, plant component differences, and decreases due to conservation or a reduction in the number of customers. We believe that using seasonal flows, when the treatment plant is permitted for AADF, is inappropriate and not allowed according to the rule for used and useful considerations. Historically, when it comes to permitted capacity, this Commission has adhered to this rule. However, we will consider the utility's request during the analysis of the final used and useful determination.

For interim purposes, we believe that the AADF permitted capacity shall be used for consideration in the used and useful calculation for the wastewater treatment plant. Therefore, we find that the wastewater treatment plant shall be considered 43% used and useful.

We have recalculated the utility's used and useful amount based on the above. As such, the net used and useful plant shall be reduced by \$40,508. Corresponding adjustments shall be made to reduce depreciation expense by \$2,344, and property tax expense by \$293. We also believe that, in error, the utility reduced plant in service by \$17,900. As such, we have increased plant in service by this amount.

Based on the above adjustments, we find that Lake Placid's interim rate base shall be \$181,471.

COST OF CAPITAL

Rule 25-30.433(3), Florida Administrative Code, states:

Used and useful debit deferred taxes shall be offset against used and useful credit deferred taxes in capital structure. Any resulting net debit deferred taxes shall be included as a separate line item in the rate base calculation. Any resulting net credit deferred taxes shall be included in the capital structure calculation. No other deferred debits shall be considered in rate base when the formula method of working capital is used.

On MFR Schedule D-2, Lake Placid reflected a simple average balance of \$1,191 for accumulated deferred income taxes (ADITs). This amount was derived by a positive 2004 year-end balance of \$2,511 and a negative 2005 year-end balance of \$130. However, according to

MFR Schedule A-19, the utility reflected a simple average ADITs credit balance of \$24,582 and on schedule A-18 a year-end simple average ADITs debit balance of \$4,927. This results in a \$19,655 net credit balance of which \$15,884 is the used and useful portion. Thus, Lake Placid understated its ADITs in the capital structure because it did not offset the used and useful debit taxes against the used and useful credit deferred taxes in the capital structure. Therefore, we find that the utility's simple average ADITs balance shall be increased by \$14,693 (\$15,884 less 1,191).

The utility's capital structure is based on that of its parent company, Utilities, Inc., which includes long-term debt, short-term debt, and common equity. Deferred income taxes and customer deposits are specifically identified to Lake Placid. We have reviewed the utility's requested capital structure and find that the utility erred in using the leverage formula in calculating its cost rate for common equity. Section 367.082(5)(b)3., Florida Statutes, states that in calculating an interim increase, the minimum of the range of the last authorized ROE shall be used. In Lake Placid's last rate case, the midpoint of the authorized ROE was established as 11.56%, with a range of 10.56%-12.56%.¹ Accordingly, for interim purposes, a cost of equity of 10.56% is appropriate. Based on the above, we find that cost of capital for interim purposes shall be 7.20%. Schedule No. 2 details the approved capital structure.

The authorized range of reasonableness for the return on equity provides Lake Placid with an authorized overall rate of return from 7.37% to 8.10%. Upon review, we believe that the utility earned an overall rate of return in the interim test year of 8.37%, which is greater than the 8.10% maximum overall rate of return allowed by this Commission. Therefore, for interim purposes, the utility earned above the range of reasonableness established by this Commission.

NET OPERATING INCOME

Operating Revenues

Upon our review of the utility's operating revenues, we believe that one adjustment is appropriate. Section 367.082(5)(b)(1), Florida Statutes, states that revenues should be annualized to reflect any rate changes that occurred during the interim test year. We have annualized the utility's revenues from rates that became effective July 1, 2005, and find an increase of \$20,353 for wastewater.

Taxes other than Income

We have reviewed Lake Placid's operating income and believe that one adjustment is appropriate. The utility reflected test year regulatory assessment fees (RAFs) of \$1,715 for wastewater. Based on our review, that amount does not reflect 4.5% of test year revenues. To correct this, RAFs shall be increased by \$1,451 for wastewater.

¹ See Order No. PSC-96-0910-FOF-WS, issued July 15, 1996, in Docket No. 951027-WS, In re: Application for rate increase in Highlands County by Utilities, Inc.

Based on these adjustments, we find that the appropriate test year operating income is \$15,182 for wastewater. Schedule 3 details the approved net operating income, with adjustments reflected on Schedule No. 3-A.

REVENUE REQUIREMENT

The revenue requirement derived from using the minimum of the range of the authorized return on equity is \$87,722, which is less than the utility's test year revenues of \$90,765. The utility's authorized range for overall rate of return is from 7.37% to 8.10%. The utility earned an overall rate of return in the interim test year of 8.37%, which is greater than the 8.10% maximum overall rate of return allowed by this Commission. Based on the utility's operating expenses and the appropriate cost of capital on an average rate base, we find that an interim revenue increase is not appropriate.

Pursuant to Section 367.082(2)(b) & (5)(b), Florida Statutes, where there is an interim decrease in rates, the maximum of the range of the last authorized rate of return on equity shall be placed subject to refund.

As the utility appears to be overearning, when using the maximum of the range of the authorized return on equity of 12.56%, the revenue requirement is \$89,954 resulting in a potential overearnings of approximately \$811, which is less than 1% of operating revenues. We believe this amount is immaterial. Therefore, this amount shall not be held subject to refund. Accordingly, we find that Lake Placid's rates remain unchanged for interim purposes and that an interim rate increase is denied.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the water and wastewater rates proposed by Lake Placid Utilities, Inc.'s are hereby suspended. It is further

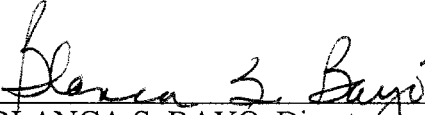
ORDERED that the request for an interim wastewater rate increase is hereby denied. It is further

ORDERED that Lake Placid Utilities, Inc.'s rates shall remain unchanged for interim purposes. It is further

ORDERED that all matters contained in the schedules attached hereto are incorporated herein by reference. It is further

ORDERED that this docket shall remain open pending the Commission's final action on the utility's requested rate increase.

By ORDER of the Florida Public Service Commission this 7th day of August, 2006.



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

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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.

Any party adversely affected by this order, which is non-final in nature, may request (1) reconsideration within 15 days pursuant to 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. A motion for reconsideration shall be filed with the Director, Division of the Commission Clerk and Administrative Services, in the form prescribed by Rule 25-22.060, Florida Administrative Code. Citizens of the State of Florida v. Mayo, 316 So.2d 262 (Fla. 1975), states that an order on interim rates is not final or reviewable until a final order is issued. Such review may be requested from the appropriate court, as described above, pursuant to Rule 9.100, Florida Rules of Appellate Procedure.

Lake Placid Utilities, Inc. Schedule of Wastewater Rate Base Test Year Ended 12/31/05			Schedule No. 1 Docket No. 060260-WS		
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Commission Adjust- ments	Commission Adjusted Test Year
1 Plant in Service	\$560,019	(\$16,835)	\$543,184	\$17,900	\$561,084
2 Land and Land Rights	\$21,665	\$0	21,665	0	21,665
3 Non-used and Useful Components	0	(13,188)	(\$13,188)	(40,508)	(53,696)
4 CWIP	0	0	0	0	0
5 Accumulated Depreciation	(302,910)	0	(302,910)	0	(302,910)
6 CIAC	(154,466)	0	(154,466)	0	(154,466)
7 Amortization of CIAC	\$103,172	\$0	103,172	0	103,172
8 Working Capital Allowance	<u>\$0</u>	<u>\$6,622</u>	<u>6,622</u>	<u>0</u>	<u>6,622</u>
9 Total Rate base	<u>\$227,480</u>	<u>(\$23,401)</u>	<u>\$204,079</u>	<u>(\$22,608)</u>	<u>\$181,471</u>

Lake Placid Utilities, Inc.
Adjustments to Rate Base
Test Year Ended 12/31/05

Schedule No. 1-A
Docket No. 060260-WS

Explanation	Wastewater
<u>Plant In Service</u>	
To reflect the appropriate amount of historical plant	\$17,900
Total	<u>\$17,900</u>
<u>Non-used and Useful</u>	
To reflect net non-used and useful adjustment	<u>(\$40,508)</u>

Lake Placid Utilities, Inc.
Capital Structure-Simple Average
Test Year Ended 12/31/05

Schedule No. 2
Docket No. 060260-WS

Description	Total Capital	Specific Adjustments	Subtotal Adjusted Capital	Prorata Adjustments	Capital Reconciled to Rate Base	Ratio	Cost Rate	Weighted Cost		
Per Utility										
1 Long-term Debt	\$124,044,203	\$0	\$124,044,203	\$0	\$124,044,203	54.84%	6.81%	3.73%		
2 Short-term Debt	11,347,000	0	\$11,347,000	0	\$11,347,000	5.02%	2.00%	0.10%		
3 Preferred Stock	0	0	\$0	0	\$0	0.00%	0.00%	0.00%		
4 Common Equity	90,787,422	0	\$90,787,422	0	\$90,787,422	40.14%	11.77%	4.72%		
5 Customer Deposits	0	0	\$0	0	\$0	0.00%	6.00%	0.00%		
6 Deferred Income Taxes	<u>1,191</u>	<u>0</u>	<u>\$1,191</u>	<u>0</u>	<u>\$1,191</u>	<u>0.00%</u>	<u>0.00%</u>	<u>0.00%</u>		
7 Total Capital	<u>\$226,179,816</u>	<u>\$0</u>	<u>\$226,179,816</u>	<u>\$0</u>	<u>\$226,179,816</u>	<u>100.00%</u>		<u>8.56%</u>		
Per Commission										
8 Long-term Debt	\$124,044,203	\$0	\$124,044,203	(\$123,953,388)	\$90,815	50.04%	6.81%	3.41%		
9 Short-term Debt	11,347,000	0	\$11,347,000	(\$11,338,693)	8,307	4.58%	2.00%	0.09%		
10 Preferred Stock	0	0	\$0	\$0	0	0.00%	0.00%	0.00%		
11 Common Equity	90,787,422	0	\$90,787,422	(\$90,720,955)	66,467	36.63%	10.56%	3.87%		
12 Customer Deposits	0	0	\$0	\$0	0	0.00%	6.00%	0.00%		
13 Deferred Income Taxes	<u>1,191</u>	<u>14,693</u>	<u>\$15,884</u>	<u>\$0</u>	<u>15,884</u>	<u>8.75%</u>	<u>0.00%</u>	<u>0.00%</u>		
14 Total Capital	<u>\$226,179,816</u>	<u>\$14,693</u>	<u>\$226,194,509</u>	<u>(\$226,013,036)</u>	<u>\$181,472</u>	<u>100.00%</u>		<u>7.37%</u>		
						LOW	HIGH			
						RETURN ON EQUITY	<u>10.56%</u>	<u>12.56%</u>		
						OVERALL RATE OF RETURN	<u>7.37%</u>	<u>8.10%</u>		

Lake Placid Utilities, Inc.
 Statement of Wastewater Operations
 Test Year Ended 12/31/05

Schedule No. 3
 Docket No. 060260-WS

Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Commission Adjust- ments	Commission Adjusted Test Year	Revenue Increase	Revenue Requirement
1 Operating Revenues:	<u>70,362</u>	<u>49,426</u>	<u>119,788</u>	<u>(29,023)</u>	<u>90,765</u>	<u>(\$3,042)</u> -3.35%	<u>87,722</u>
Operating Expenses							
2 Operation & Maintenance	52,976	0	52,976	0	52,976	0	52,976
3 Depreciation	13,194	0	13,194	(2,344)	10,850	0	10,850
4 Amortization	529	(529)	0	0	0	0	0
5 Taxes Other Than Income	5,271	3,348	8,619	(2,190)	6,429	(137)	6,292
6 Income Taxes	<u>13,559</u>	<u>13,971</u>	<u>27,530</u>	<u>(22,202)</u>	<u>5,328</u>	<u>(1,093)</u>	<u>4,235</u>
7 Total Operating Expense	<u>85,529</u>	<u>16,790</u>	<u>102,319</u>	<u>(26,736)</u>	<u>75,583</u>	<u>(1,230)</u>	<u>74,353</u>
8 Operating Income	<u>(15,167)</u>	<u>32,636</u>	<u>17,469</u>	<u>(2,287)</u>	<u>15,182</u>	<u>(1,812)</u>	<u>13,369</u>
9 Rate Base	<u>227,480</u>		<u>204,079</u>		<u>181,471</u>		<u>181,471</u>
10 Rate of Return	<u>-6.67%</u>		<u>8.56%</u>		<u>8.37%</u>		<u>7.37%</u>

Lake Placid Utilities, Inc.
 Adjustment to Operating Income
 Test Year Ended 12/31/05

Schedule 3-A
 Docket No. 060260-WS

Explanation	Wastewater
<u>Operating Revenues</u>	
1 Remove requested final revenue increase.	(49,376)
2 To reflect the appropriate amount of TY Revenues	20,353
Total	<u>(29,023)</u>
<u>Depreciation Expense – Net</u>	
To remove net depreciation of non-U&U plant.	(\$2,344)
<u>Taxes Other Than Income</u>	
1 RAFs on revenue adjustments above	(3,348)
2 To reflect the appropriate historical TY RAFs	1,451
3 To reflect reduced property taxes on NU & U Property.	(293)
4 Total	<u>(2,190)</u>