

St. George Island Utility Company, Ltd.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION
REGARDING THE APPLICATION FOR INCREASED RATES FOR
ST. GEORGE ISLAND UTILITY COMPANY, LTD.
IN FRANKLIN COUNTY
DOCKET NO.

TESTIMONY OF FRANK SEIDMAN

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5 IN FRANKLIN COUNTY
6 DOCKET NO. _____ -WU
7

8 Q. Please state your name, profession and address.

9 A. My name is Frank Seidman. I am President of
10 Management and Regulatory Consultants, Inc.,
11 consultants in the utility regulatory field. My
12 office is located at 11380 Prosperity Farms Road,
13 Suite 211, Palm Beach Gardens, Fl 33410.

14
15 Q. What is the nature of your engagement with the
16 Applicant, St. George Island Utility Company, Ltd
17 (SGI)?

18 A. I was engaged by SGI to complete an application for
19 an increase in water rates, to coordinate and
20 assist in all phases of the application procedure
21 and to give evidence in support of that application.

22
23 Q. State briefly your educational background and
24 experience.

25 A. I am a graduate of the University of Miami. I hold
26 the degree of Bachelor of Science in Electrical

1 Engineering. I have also completed several graduate
2 level courses in economics, including public utility
3 economics. I am a Professional Engineer, registered
4 to practice in the state of Florida. I have over
5 30 years experience in utility regulation,
6 management and consulting. This experience includes
7 nine years as a staff member of the Florida Public
8 Service Commission, two years as a planning engineer
9 for a Florida telephone company, four years as
10 Manager of Rates and Research for a water and sewer
11 holding company with operations in six states and
12 three years as Director as Technical Affairs for a
13 national association of industrial users of
14 electricity. I have either supervised or prepared
15 rate cases, prepared rates studies or testified as
16 an expert witness with regard to water and sewer
17 utilities in Florida, California, Michigan,
18 Missouri, Indiana and Ohio.

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1 Q. Are you familiar with the documents entitled Docket
2 No. _____-WU, Application of ST. George Island
3 Utility Company, Ltd for Increased Rates in Franklin
4 County, consisting of three volumes, Volumes I, II
5 and III (Exhibit _____) ?

6 A. Yes I am. I prepared or supervised the preparation
7 of these documents with the assistance of SGI's
8 staff, accountants and consulting engineers. Volume
9 I contains the financial, rate and engineering
10 minimum filing requirements (MFR's) required by
11 Commission Rule 25-30.437 F.A.C., including the
12 schedules supporting the request for interim rates.
13 Volume II contains the billing analysis schedules
14 of the MFR's. Volume III is a packet containing the
15 additional engineering information required by
16 Commission rules 25-30.440 F.A.C.

17

18 Q. Please summarize the major conclusions of this
19 filing.

20 A. SGI is seeking an increase in its water rates and
21 charges.

22

23 The request is based on the adjusted operating
24 information for the historical year ended December
25 31, 1992.

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As shown in Volume I of (Exhibit ____):

The average rate base for the adjusted test year ended December 31, 1992 is \$ 1,029,277 for the water system. (see Schedule A-1).

The adjusted operating income for the test year, without the requested increase, is a negative \$ 299,598. (see Schedule B-1).

A fair rate of return on Applicant's rate base is 8.07%. (see Schedule D-1). The Applicant's current equity in the system is negative. In accordance with PSC Rule 25-30.346(4)(f), SGI is requesting that the Commission set a return on equity at 9.07%, which is the maximum of the return of the current equity leverage formula approved in Order No. PSC-93-1107-FOF-WS, dated 7/29/93, pursuant to Section 367.081(4), F.S.

This application indicates that an increase in test year annual water revenues of \$ 428,201 is required to produce a fair rate of return. (see Schedule B-1).

1 THE TEST PERIOD

2 Q. I would now like you take us through the major
3 components of the rate case. First, what is the
4 test period for this rate application?

5 A. This application is based on the actual results of
6 operation for the twelve months ending December 31,
7 1992, with appropriate adjustments. This period
8 was chosen as incorporating the majority of the
9 major required plant additions, as the most recent
10 fiscal year for which complete information is
11 available, and, with appropriate proforma
12 adjustments, recognizes the operation and management
13 changes that are being undertaken by SGI to comply
14 with various state agency requirements to bring
15 service up to acceptable standards.

16
17 This utility last filed for a rate case in Docket
18 No. 871177-WU. Order No. 21122 granted a rate
19 increase in April, 1989 based on a 1987 test year.
20 As this Commission is aware, Order No. 21122 granted
21 that increase with several conditions and identified
22 many areas which it required this utility to
23 improve. Those improvements required additional
24 plant, maintenance of plant, additional personnel,
25 changes in operation and improvements in accounting

1 procedures. After a long, arduous and often
2 frustrating process, the utility is now operating
3 in a satisfactory manner. On September 15, 1993,
4 Order No. PSC-93-1352-FOF-WU was issued, closing
5 Docket No. 871177-WU and acknowledging that the
6 requirements of all orders in that docket had been
7 met.

8

9 **RATE BASE**

10 **Q. How was rate base developed?**

11 A. The rate base consists of the beginning and ending
12 average balance for the period ending December 31,
13 1992 of the following components: plant in service,
14 less accumulated depreciation, less contributions
15 in aid of construction (CIAC) net of amortization,
16 less outstanding advances for construction plus an
17 allowance for working capital. Each of these
18 components is adjusted to reflect ratemaking
19 considerations such as out of period adjustments.
20 And, each of these components is adjusted, where
21 applicable, to reflect only the investment that is
22 used and useful in the public interest.

23

24

1 Q. Did you make any adjustments to the book balances
2 of these component accounts?

3 A. Yes. Several proforma adjustments was made to Plant
4 in Service, Accumulated Depreciation, Contributions
5 In Aid of Construction, and Amortization of CIAC
6 (see Schedules A-3 and A-3, Plant Detail).

7
8 An adjustment was made to include the cost of the
9 now completed and operating Well #3. The addition
10 of this well was mandated by the Department of
11 Environmental Protection (DEP) and this Commission.
12 Also included was an adjustment to reclassify land
13 obtained in 1990 for the third well site so that it
14 is reflected as Plant in Service.

15
16 An adjustment was made to include the net cost of
17 replacing the generator at the water plant, which
18 sustained non-repairable lightning damage.

19
20 An adjustment was made to Accumulated Depreciation
21 to reflect adjustments to the test year depreciation
22 expense and to retire the damaged generator.

23
24 An adjustment was made to Contributions in Aid of
25 Construction to reflect amounts collected in 1993

1 but netted against a note used to finance the
2 construction of Well #3 which is included as a
3 proforma adjustment. An adjustment was made to the
4 Amortization of CIAC balance. The utility has been
5 amortizing CIAC at a composite rate unrelated to the
6 life of the plant components with which they are
7 associated. I recalculated the amortization expense
8 for the test year at composite rates based on plant
9 components and adjusted the accumulated balance for
10 the difference in the test year expense. (see
11 Schedule B-13, page 4).

12

13 **Q. Have you included any deferred debits in rate base?**

14 **A.** No. In accordance with PSC Rule 25-30.433(3), no
15 deferred debits other than deferred taxes can be
16 considered in rate base for Class B utilities.
17 However, there are significant nonrecurring expenses
18 and expenses recurring less frequently than annually
19 that are being or will be incurred and which I would
20 classify as deferred debits. These expenditures are
21 primarily for studies and analyses that are required
22 to comply with DEP directives and/or related court
23 judgments or the directions of other regulatory
24 bodies. The annual expense associated with these
25 have been classified in this filing as Amortization

1 Expense and are addressed in Schedules B-3 and B-3,
2 Amort Detail. In accordance with PSC Rule 25-
3 30.433(8), they are amortized over a five year
4 period unless the experienced frequency of their
5 recurrence indicates otherwise.

6

7 **Q. How did you calculate the Working Capital component**
8 **of Rate Base?**

9 A. In accordance with PSC Rule 25-30.433(2), working
10 capital is calculated at 1/8 th of operating and
11 maintenance expense.

12

13 **Q. Were adjustments made to Plant in Service for used**
14 **and useful considerations?**

15 A. The components of the system were analyzed by
16 consulting engineer, Mr. Wayne Coloney, as to their
17 necessity and usefulness in providing service
18 during the test year. Mr. Coloney has submitted
19 testimony supporting his findings. Based on that
20 analysis, it was determined an adjustment for non-
21 used plant was not necessary.

22

23

1 Q. Mr. Seidman, you have prepared used and useful
2 analyses in several rate application before this
3 Commission, have you not?

4 A. That is correct.
5

6 Q. Do you agree with Mr. Coloney's conclusions?

7 A. Yes I do. With regard to the supply treatment and
8 storage plant, there is no doubt in my mind that
9 those facilities are necessary and are 100% used and
10 useful. I have reviewed the Commission's Order No.
11 21122 from the last case. In that case, the supply
12 treatment and storage facilities were all found to
13 be 100% used and useful, but "insufficient to serve
14 existing customers." In that order, the Commission
15 included 19 compliance requirements, six of which
16 required additions or improvements to the system.
17 Those completed improvements, necessary to provide
18 adequate, sufficient and reliable service to the
19 customers on St. George Island, are what are
20 reflected in the test year adjusted plant in service
21 balances. Although, as Mr. Coloney points out,
22 those improvements are capable of serving limited
23 growth, they are, of themselves, necessary to meet
24 the mandates of the Department of Environmental
25 Protection and of this Commission.

1 Q. Mr. Coloney has also found that the transmission and
2 distribution system is also 100% used and useful.
3 Do you agree with that finding?
4 A. Yes I do.
5
6 Q. Are you aware that the Commission, in the last case,
7 found the transmission and distribution system to
8 be only 18% used and useful?
9 A. Yes I am. That finding was based on a strict ratio
10 of connected lots to available lots without
11 consideration for any other factors.
12
13 Q. And is it your contention that the current ratio of
14 connected lots to available lots now equals 100%?
15 A. Not at all. It is my contention that the situation
16 at St. George Island is unique and that a strict
17 ratio calculation severely understates the used and
18 usefulness of the transmission and distribution
19 plant. That was true for the last case as well as
20 now.
21
22 Q. In what ways is service at St. George Island unique?
23 A. St George Island is a resort island that is
24 approximately 18 miles long and approximately one
25 half mile wide wherever development is feasible. The

1 service area is the whole island. Its main
2 attraction is its beach front, so development is
3 most naturally dispersed along nearly the island's
4 whole length as people tend to favor beach front
5 access rather than the interior. Even so, the
6 interior is only about three blocks in either
7 direction from the main east-west road. In order to
8 reach development as it occurs along the "length"
9 of the island, but toward the beaches, the utility
10 has no choice but to have a core transmission line
11 that runs the length of the island and distribution
12 lines toward the beach fronts. Those transmission
13 and distribution lines must be considered 100% used
14 and useful, regardless of the fill of lots.

15
16 Another unique feature of this service area is that,
17 unlike most certificated service areas, it is not
18 protected from competition. So even though the
19 utility must be ready to serve and must bring water
20 from the mainland in order for it to meet acceptable
21 quality standards, nearly any one can elect to drill
22 a shallow well on their own lot to obtain water
23 service, regardless of the water quality. It is
24 interesting, that in this time of general concern
25 for the environment and control of water resources,

1 that St. George Island has no restrictions on the
2 drilling of shallow wells, when a central water
3 system is available. As a result, there is a
4 proliferation of shallow wells on the island. As of
5 August, 1993, 128 buildings get there potable water
6 from shallow wells. That represents over 10 percent
7 of the buildings on the island with water service.
8 Another 231 buildings have both wells and utility
9 service. So nearly 30% of the buildings on the
10 island have access to private wells as either a
11 primary or secondary source of potable water. If
12 used and useful is determined on strict ratio basis,
13 is will be impossible for the utility to recover the
14 cost of the system dedicated to public service.

15
16 In this unique environment, where the service area
17 is very long but only a few blocks wide, where
18 development tends to take place along the length of
19 the service area and away from the main line toward
20 the beachfront, and where the option for private
21 wells is not controlled, the transmission and
22 distribution system, as installed, should be
23 considered totally used and useful.

24
25

1 Q. What is the net result of the adjustments to Rate
2 Base?

3 A. After all adjustments, the rate base for the test
4 year ended December 31, 1992 is \$ 1,029,277.

5

6 OPERATING REVENUE

7 Q. What is included in operating revenue?

8 A. Operating revenue includes revenue received from the
9 sale of utility services and from miscellaneous
10 charges to the customer such as connection or
11 reconnection charges.

12

13 Q. Were there any adjustments to the 1990 per book
14 operating revenues?

15 A. Yes. I removed \$4,000 that was improperly booked to
16 Other Revenue. Under a PSC approved agreement with
17 the St. George Island Volunteer Fire Department, SGI
18 received \$4,000 as an installation and maintenance
19 fee for two hydrants. The fee, collected in 1992,
20 was for hydrants that are not being installed and
21 are not in use until 1993. In addition, the part of
22 the fee related to installation of the hydrants
23 should be booked as CIAC. Since the fee includes
24 perpetual maintenance, the portion not booked to
25 CIAC should be booked as deferred revenue and

1 amortized over the life of the hydrants. I also
2 included a small adjustment to reconcile sales
3 revenues to the billing analysis calculation.
4 Adjusted test year water revenue at existing rates
5 is \$ 314,517.

6

7 **OPERATING REVENUE DEDUCTIONS**

8 **Q. What is included in operating revenue deductions?**

9 A. Operating revenue deductions include operation and
10 maintenance expenses, depreciation and amortization
11 expenses and all tax expenses.

12

13 **Q. Did you make any adjustments to test year operating
14 and maintenance expenses?**

15 A. Yes. I made several adjustments to test year
16 operating and maintenance expenses. The changes
17 are summarized on page 2 Schedule 5 and page 1 of
18 Schedule B-3 O&M Detail. These changes were
19 necessary to normalize existing expenses, to reflect
20 personnel additions not made until 1993 that are
21 necessary to provide adequate service to existing
22 customers, to reflect the cost of employee benefits
23 and insurance and to reflect new and necessary
24 maintenance programs.

25

1 Q. Briefly describe these adjustments.

2 A. I adjusted Account 601, Salaries & Wages to reflect
3 the current employees at their current wage rate and
4 to add the annualized salaries of and additional
5 office worker and a second field worker, neither of
6 which were employed during the test year, but are
7 now employed and will be during the period when
8 these proposed rates would be in effect.

9

10 Q. Why are these new employees necessary?

11 A. The field worker is needed to keep service on the
12 island from deteriorating. There are only two
13 personnel presently on the island, one of which is
14 the certified plant operator and operations manager.
15 The on-site personnel do all plant operation,
16 maintenance, test sampling, meter and service
17 installation, meter reading, pump monitoring, cross
18 connection control monitoring, chlorine tank
19 operations and readings, flushing and prepare all
20 reports. The geography of the island is such that
21 these personnel must cover a service area twenty
22 miles long on a daily basis, and, in addition,
23 inspect and maintain the wells and pumping
24 facilities located on the mainland. The compliance
25 monitoring required by DEP is extensive and in

1 excess of that required for other utilities. Also,
2 because of the proliferation of private wells,
3 utility personnel are required to continuously
4 monitor and inspect for cross connection potential,
5 keep records of customers with wells, notify them
6 of the need to install cross connection control
7 devices, notify them of when annual inspections are
8 due, police these customers and keep records of the
9 state of their compliance. As recently as May, 1993,
10 DEP noted during one of its inspections that
11 management did not have the capability to complete
12 the required initial inspections and keep up with
13 all requirements of previously installed cross
14 control devices.

15
16 The office worker is needed to assist in maintaining
17 the books and records of the company in sufficient
18 detail to meet the requirement of the Commission.
19 The Commission staff has made it clear that more
20 detailed records are necessary.

21

22 **Q. What is the net adjustment to Account 601?**

23 **A. The net adjustment is an increase of \$60,241 for the**
24 **test year.**

1 Q. What other adjustments were made to Operations &
2 Maintenance expenses?
3 A. Account 604, Employee Pension and Benefits was
4 adjusted to annualize the and reflect the health and
5 pension benefits now being made available to all
6 employees. The adjustment also reflects the expense
7 associated with education benefits necessary to
8 train employees for operator certification, customer
9 billing and ledger programs and to keep up with
10 plant safety and operational requirements. The total
11 adjustment to Account 604 is \$29,997.
12
13 A \$404 adjustment was made to Account 615, Purchased
14 Power, to normalize electric expense to reflect the
15 actual 12 months of the test year and to recognize
16 the additional expense for operating Well #3.
17
18 Account 631, Contractual Services, Engineering was
19 adjusted by \$1,849 to remove all non-recurring
20 expenses and to recognize the retainer agreement
21 with Coloney Engineering. Through this agreement,
22 for \$500 per month, SGI has the availability of
23 engineering advice on ongoing operations and
24 compliance.
25

1 An adjustment was made to Account 632, Contractual
2 Services, Accounting in the amount of \$(8,796). This
3 removes all expenses except those for J. Drawdy and
4 B. Withers. Ms. Drawdy oversees the upkeep of the
5 general ledgers and assures compliance with the
6 Uniform System of Accounts. Ms. Withers provides
7 expertise regarding tax accounting and accounting
8 related to limited partnerships.

9
10 Account 633, Contractual Services, Legal was
11 adjusted by \$2,182. The adjustment removes all one
12 time expenditures and reflects the revised agreement
13 for minimum retainer for legal services with Gene
14 D. Brown, P.A. The retainer revision reflects the
15 time being spent on legal matters as documented by
16 recent time records.

17
18 A major adjustment was made to Account 635,
19 Contractual Services, Other, in the amount of
20 \$85,091. As Mr. Brown will explain, SGI is being
21 required to arrange for ongoing storage tank
22 maintenance and protection programs that are quite
23 costly. In addition, water testing requirements
24 have been imposed that are increased in frequency
25 and complexity. Also, SGI is undertaking an ongoing

1 distribution line cleaning program that will improve
2 system pressure, reduce turbidity and minimize
3 leaks. The annual cost for all of these programs is
4 reflected in the adjustment.

5

6 An adjustment of \$1,076 was made to Account 642,
7 Rents - Buildings/Property to reflect the ongoing
8 rental expense for the Tallahassee office and for
9 storage space.

10

11 An adjustment of \$2,633 was made to Account 642,
12 Rental Equipment. This account had included the cost
13 of renting a backhoe on a periodic basis. The
14 utility has arranged for the lease/purchase of a
15 backhoe so that it can have full time access at very
16 little difference from the cost of periodic rentals.
17 Because of St. George Island's remote location, full
18 time access to a backhoe on the island substantially
19 improves the response time for maintenance of, and
20 additions to, the lines.

21

22 An adjustment of \$(2,422) was made to Account 650,
23 Transportation Expense. SGI does not own any of its
24 own vehicles. In lieu of utility ownership of
25 vehicles and the related fixed and operating costs,

1 SGI provides a transportation allowance to each
2 employee, based on their duties and estimated
3 mileage requirements. The amount of each allowance
4 is detailed at page 6 of Schedule B-3 O&M Detail.

5
6 Proforma adjustments were made to Accounts, 657, 658
7 and 659 which are general liability, workman's
8 compensation and property insurance expenses,
9 respectively. The total adjustment for the three
10 accounts is \$36,502 which represents the total
11 quoted premium for these insurance requirements and
12 the specific premium required to insure the
13 replacement generator at the water plant. SGI has
14 been operating without insurance because of its cash
15 flow situation. This makes the utility and its
16 customers quite vulnerable to economic and property
17 losses. The quoted premium is utility specific and
18 in line with that for similar coverage for other
19 utilities. It should be recognized as a reasonable
20 and necessary expense for this utility to provide
21 adequate and safe service.

22
23 An adjustment of \$6,276 was made to Account 670,
24 Bad Debt Expense. This adjustment reflects the

1 allowance necessary to provide for losses from
2 uncollectible utility revenues.

3

4 Finally, an adjustment of \$2,773 was made to Account
5 675, Misc. Expense. This adjustment reflects
6 reclassification of some test year expenses to other
7 expense accounts and an increase in several
8 administrative expenses.

9

10 The total of all adjustments to test year Operating
11 & Maintenance expenses is \$217,806. Although these
12 are major adjustments, they reflect what SGI
13 management feels are necessary to provide safe,
14 adequate and sufficient service to its customers and
15 to comply with the mandates of DEP, this Commission
16 and other regulatory agencies.

17

18 **Q. Did you compare the adjusted operating expenses with**
19 **those allowed in the last rate case?**

20 **A. Yes. That comparison is set out in required MFR**
21 **Schedule B-7. In that schedule, the adjusted test**
22 **year expenses are compared to the expenses allowed**
23 **in the last rate case after allowing for changes in**
24 **customer growth and the consumer price index.**

25

1 Q. How do adjusted test year expenses compare?

2 A. Some expenses have increased dramatically, but one
3 must consider that the base year expenses were
4 severely understated. As this Commission is aware,
5 the quantity and quality of personnel was sorely
6 lacking at the time of the last rate case and for
7 a period after it. In Order No. 21122 and again in
8 Order No. 23038, the Commission cited the utility
9 for failure to maintain proper accounting records,
10 failure to keep proper plant records and failure to
11 keep proper billing records. In addition, service
12 quality was suffering because of inadequate plant
13 maintenance and a leak detection program. Further,
14 a cross connection control program was mandated and
15 the costs of administering that program were not
16 included in the base year. The adjusted test year
17 expenses reflect the salaries and benefits for a
18 complement of personnel, in both numbers and
19 competence, necessary to provide sufficient and
20 adequate service. The increase in expenses reflects
21 the cost of maintenance and testing programs
22 instituted in response to DEP mandates. And the
23 increase in expenses also reflects a level of
24 material and supplies necessary for adequate and
25 timely repairs. In the base year, the utility was

1 cited for nineteen instances of inadequate service.
2 Service has improved substantially since that
3 time. Changes in excess of the bench mark are, for
4 the most part, to include expenses that were not
5 being incurred during the base year but should have
6 been. The largest single account change is for
7 Materials & Supplies. This only indicates that the
8 utility is now purchasing supplies to maintain and
9 operate the system. During the base year,
10 maintenance was non-existent.

11

12 **Q. Did you adjust operating expenses for the test year**
13 **to recover the cost of this rate case application?**

14 **A. Yes. I have estimated the cost of this application**
15 **to be \$ 105,039 to complete it through the hearing**
16 **and post hearing process. Schedule B-10 details the**
17 **rate case expense components. By statute, rate case**
18 **expense is to be amortized over four years, which**
19 **amounts to an annual rate of \$ 26,260.**

20

21

22

23

24

1 Q. You previously indicated that SGI would be incurring
2 significant nonrecurring expenses and expenses
3 recurring less frequently than annually. How are
4 these expenses reflected in this application?
5 A. These are expenses that I would classify as deferred
6 debits. The annual write off of these expenses are
7 included in Schedule B-1 as Amortization Expense and
8 are discussed in detail in Schedules B-3 and B-3
9 Amort Detail. As previously indicated, these
10 expenditures are primarily for studies and analyses
11 that are required to comply with DEP directives
12 and/or related court judgments or the directions
13 of other regulatory bodies. They include the
14 expense for preparing and updating system maps,
15 performing detailed analyses of the distribution and
16 treatment systems, preparing hydrological studies
17 to support amendments to the consumptive use permit
18 and a study of the capability and feasibility of the
19 utility to provide complete fire protection. In
20 accordance with PSC Rule 25-30.433(8), they are
21 amortized over a five year period unless the
22 experienced frequency of their recurrence indicates
23 otherwise. The total adjustment to Amortization
24 Expense is \$41,452.
25

1 **Q. What adjustments were made to depreciation expenses?**
2 A. I verified the test year per books depreciation
3 expense by calculating the depreciation expense for
4 the average plant primary account balances using the
5 utility's stated depreciation rates and found the
6 per book expense was understated. I therefore
7 adjusted the test year expense to reflect the proper
8 amount. In addition, the depreciation expense
9 associated with the new Well #3 and adjustments for
10 the replaced generator were included.
11
12 **Q. Did you adjust the CIAC amortization expense also?**
13 A. Yes. As I previously pointed out, the test year per
14 book amortization expense was based on a composite
15 rate that did not relate to the lives of the
16 associated plant. I recalculated the amortization
17 expense and adjusted the per book amount.
18
19 **Q. What adjustments were made to payroll taxes?**
20 A. I adjusted payroll taxes to reflect the tax
21 associated with proforma changes in salaries.
22
23
24

1 Q. What adjustments were made to the regulatory
2 assessment fee (RAF)?

3 A. The RAF was adjusted to reflect the rate of 4.5% of
4 the adjusted revenue before the requested increase
5 and including the proposed increase in operating
6 revenue.

7

8 Q. Have you included an allowance for income taxes?

9 A. No. As will be discussed later, the present
10 capitalization is 100% debt. Therefore there is,
11 currently, no taxable income. In addition, SGI is
12 a limited partnership and PSC Rule 25-30.433(7)
13 prohibits the recovery of income tax expense for
14 partnerships.

15

16 **CAPITAL STRUCTURE**

17 Q. What is the capital structure of the utility?

18 A. The capital structure includes a substantial amount
19 of negative equity offset by long and short term
20 notes from both related and unrelated entities.
21 Essentially, the non-contributed investment in this
22 utility is currently being financed by debt, the
23 majority of which was provided by Leisure
24 Properties, a general partner of the utility.

25

1 Q. What has contributed to the growing negative equity.

2 A. It appears that two things have contributed to this
3 condition. First, rates are and have been
4 inadequate, as the necessity of this filing makes
5 clear. Second, the interest associated with the debt
6 has been steadily accruing until it is now nearly
7 as much as the debt itself.

8

9 Q. How has the negative equity balance been treated in
10 this application?

11 A. The negative equity balance in this application has
12 been treated consistent with the Commission's
13 treatment in Order No. 21122, that is, it has been
14 added back such that the capital structure is
15 considered to be 100% debt.

16

17 Q. Is SGI requesting that the Commission set a return
18 on equity in this proceeding, for future use?

19 A. Yes. PSC Rule 25-30.346(4)(f) states that if the
20 capital structure contains zero or negative equity,
21 a return shall be requested, which shall be the
22 maximum of the return of the current equity leverage
23 formula established by order of this Commission
24 pursuant to Section 367.081(4), F.S. On that basis,
25 SGI is requesting that the return on equity be set

1 at 10.97% as approved in Order No. PSC-93-1107-FOF-
2 WS, dated 7/29/93.

3

4 **Q. Is it necessary to make any adjustments to the debt**
5 **portion of the capital structure?**

6 A. Yes. Additional debt was incurred in 1993 to
7 finance, in part, the construction of Well #3 which
8 has been included as a pro forma adjustment to Rate
9 Base. That debt should be rolled in with the
10 embedded debt to determine the amount and embedded
11 cost of debt that is relevant for the adjusted test
12 year. A portion of that new debt has already been
13 repaid from CIAC collected in 1993. For purposes of
14 this application, that CIAC has been included as an
15 offset to Plant in Service and as an offset to the
16 debt.

17

18 **Q. What is the rate of return which the utility should**
19 **be allowed to earn on its rate base?**

20 A. The rate of return which the utility should be
21 allowed to earn for the test year is 8.07%, which
22 is the adjusted imbedded cost of debt.

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1 REVENUE REQUIREMENT

2 Q. What is the revenue requirement necessary to recover
3 the utility's cost of service, including a 8.07%
4 return on rate base?

5 A. The revenue requirement is \$ 742,718 for the water
6 system as shown on Schedule B-1. The additional
7 revenue required is \$428,201.

8

9 RATES AND RATE STRUCTURE

10 Q. What rates are proposed to produce the revenues
11 required?

12 A. The rates proposed are summarized on Schedule E-1.

13

14 Q Have you proposed any change in rate structure?

15 A. No. The present rate structure includes a base
16 facilities charge and a gallonage charge as required
17 by the Commission. The requested rates maintain
18 that same rate structure. However, because of the
19 seasonality of service at St. George Island, the
20 relative portions of costs to be recovered through
21 the base facility charge and the gallonage charge
22 has been changed. The rate structure is now more
23 heavily weighted toward the base facility charge.

24

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1 Q. Why did you weight the rate more heavily toward the
2 base facility charge?

3 A. Since St. George Island is a resort community, its
4 consumption pattern and therefore its cash flow is
5 very seasonal. Revenues are highest between May and
6 September because the peak holiday use occurs on
7 Memorial Day, Fourth of July and Labor Day weekends.
8 During the other months, revenues are very low and
9 not even sufficient to cover payroll. I therefore
10 increased the base facility charge in an attempt to
11 stabilize cash flow.

12

13 **SERVICE AVAILABILITY CHARGES**

14 Q. Are you proposing any changes to the service
15 availability charges?

16 A. No changes to the service availability charges are
17 being requested at this time. The current charges
18 should keep the amount of CIAC collected within
19 Commission guidelines.

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1 AFPI CHARGES

2 Q. Have you requested an adjustment to the Allowance
3 for Funds Prudently Invested (AFPI) charge in this
4 filing?

5 A. We have proposed that the plant in service be
6 considered 100% used and useful. Consistent with
7 that, the AFPI charge would no longer be required.
8 If the Commission accepts our used and useful
9 determination, we propose that the AFPI charge be
10 withdrawn. However, should the Commission determine
11 that a portion of plant is not used and useful, then
12 the AFPI charge should be restated to recover the
13 carrying costs of that portion of plant designated
14 as non-used and useful.

15

16 Q. Does that conclude your prefiled direct testimony?

17 A. Yes it does.

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