

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Response to Commission) DOCKET NO. 961417-SU
order to show cause by Hudson) ORDER NO. PSC-97-0458-FOF-SU
Utilities, Inc. d/b/a Hudson Bay) ISSUED: April 22, 1997
Company in Pasco County)
_____)

The following Commissioners participated in the disposition of this matter:

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

NOTICE OF PROPOSED AGENCY ACTION
ORDER FINDING THAT HUDSON UTILITIES, INC. IS NOT REQUIRED
TO REDUCE ITS RATES OR REFUND REVENUES COLLECTED AS A RESULT OF A
DECREASE IN PURCHASED BULK WASTEWATER COSTS IN PASCO COUNTY

AND

ORDER RESOLVING SHOW CAUSE PROCEEDING

BY THE COMMISSION:

NOTICE IS HEREBY GIVEN by the Florida Public Service Commission that the action discussed herein, except our decision regarding the utility's request for a waiver and the resolution of the show cause proceeding, is preliminary in nature and will become final unless a person whose interests are substantially affected files a petition for a formal proceeding, pursuant to Rule 25-22.029, Florida Administrative Code.

BACKGROUND

Section 367.081(4)(b), Florida Statutes, provides that the approved rates of any utility which receives all or any portion of its utility service from a governmental authority or from a water or wastewater utility regulated by the Commission and which redistributes that service to its utility customers shall be automatically increased or decreased without hearing, upon verified notice to the Commission 45 days prior to its implementation of the increase or decrease that the rates charged by the governmental authority or other utility have changed.

DOCUMENT NUMBER-DATE

04055 APR 22 97

FPSC-RECORDS/REPORTING

On December 12, 1995, after a public hearing, the Pasco County Board of County Commissioners approved a rate change for all customers encompassing the period of January 1, 1996 through September 30, 1999. As a result of this rate change, the rates for all bulk water and/or wastewater customers were decreased effective January 1, 1996. On December 20, 1995, the Commission staff received from Pasco County copies of the notices it sent to utilities regulated by the Florida Public Service Commission (PSC), advising the utilities of the bulk water and/or wastewater rate change. There are nine PSC regulated utilities which purchase water and/or wastewater from Pasco County. According to the notice, Pasco County extended the January 1, 1996 effective date until April 1, 1996 in order to allow the utilities sufficient time to contact the Commission and/or incorporate the new charges into its rate structure.

The bulk water and/or wastewater rate change approved by Pasco County qualifies for a pass-through rate adjustment for PSC regulated utilities pursuant to Section 367.081(4)(b), Florida Statutes. Section 367.081(4)(e), Florida Statutes, provides that a utility may not adjust its rates under this subsection more than two times in any 12 month period. Therefore, on March 29, 1996, staff sent letters to the nine affected utilities regarding the Pasco County rate change advising them that because Pasco County approved two rate changes in 1996, the utilities had the option of using the pass-through statute to adjust their rates accordingly. Specifically, staff informed the utilities that one of the rate changes could be filed as a pass-through in conjunction with an index and the other pass-through adjustment could be filed separately to be effective October 1, 1996.

To date, only three of the nine (Utilities Inc. of Florida, Betmar Utilities, Inc. and Jasmine Lakes Utilities Corporation) have filed for a pass-through rate reduction. Another utility, Virginia City Utilities, Inc. (Virginia City) had a staff assisted rate case in Docket No. 960625-WU, through which the county's decreased rates were incorporated. The five utilities which have not filed a pass-through rate reduction are: Hudson Utilities, Inc., d/b/a Hudson Bay Company (Hudson or utility); Forest Hills Utilities, Inc. (Forest Hills); Mad Hatter Utility, Inc. (Mad Hatter or MHU); Aloha Utilities, Inc. (Aloha); and Southern States Utilities, Inc. (SSU). By Order No. PSC-96-1226-FOF-WS, issued September 27, 1996, in Docket No. 960878-WS, each of these five utilities was ordered to show cause in writing why their rates should not be adjusted, effective April 1, 1996, to reflect the reduction in purchased water and/or wastewater costs to bulk water and/or wastewater customers in Pasco County. On October 17, 1996, Hudson filed its response to the show cause order.

Hudson is a Class B wastewater utility providing service to the public in Pasco County. As of December 31, 1995, the utility served 1,172 wastewater customers. The utility had gross operating revenues of \$629,192 for the wastewater system and reported a net operating income of \$17,394 for the wastewater system.

REQUEST FOR WAIVER

In its written response to the show cause order, Hudson requests a waiver of that provision of Order No. PSC-96-1226-FOF-WS requiring the utility to file the information required by Rule 25-30.425(1)(a) through (f), Florida Administrative Code, along with a calculation of the rate reduction, for a period of twenty days after we vote on whether Hudson must reduce its rates, if such a rate reduction is ordered.

Because our staff has been able to obtain the necessary and pertinent information from other independent sources, a vote on the utility's request for a waiver is no longer required.

IMPLEMENTATION OF PASS-THROUGH DECREASES

The utility asserts in its response that it disagrees with the proposition that the Commission has the statutory authority to require a decrease in rates of a regulated utility to reflect a reduction in bulk purchased water and/or wastewater costs. The utility argues that such an interpretation of Section 367.081(4)(b), Florida Statutes, is inconsistent with the plain meaning and intent of the statute. The utility further asserts that it does not believe the Commission may implement pass-throughs in a Section 367.0822, Florida Statutes, limited proceeding. Moreover, the utility asserts that the legislature did not intend to mandate pass-through increases or decreases.

Section 367.081(4)(b), Florida Statutes, provides in part:

The approved rates of any utility which receives all or any portion of its utility service from a governmental authority or from a water or wastewater utility regulated by the Commission and which redistributes that service to its utility customers shall be automatically increased or decreased without hearing, upon verified notice to the Commission 45 days prior to its implementation of the increase or decrease that the rates charged by the governmental authority or other utility have changed. (emphasis added)

This statute establishes a procedure by which certain operating costs incurred by water and wastewater utilities are passed through to the utility's customers without further action by the Commission. The statute mandates that the utility's rates shall be automatically increased or decreased upon verified notice to the Commission.

The language in Section 367.081(4)(b), Florida Statutes, clearly and unambiguously addresses both decreases and increases. In prior decisions, we have found that rate reductions associated with decreases in the rates for purchased water and/or wastewater service are appropriate. In these cases, however, the utility initiated the proceeding. By Order No. 11026, issued July 26, 1982, in Docket No. 820264-W, we approved a reduction in the rates for Florida Water Service, Inc. to pass-through a decrease in the purchased water rate charged to Florida Water Service, Inc. by its supplier, Village of Palm Springs. In addition, by Order No. 20728, issued February 13, 1989, in Docket No. 890049-SU, we approved a rate reduction for Hudson Utilities, Inc. using the limited proceeding statute to pass-through a reduction in the cost of purchased wastewater treatment by Pasco County.

Noticeably absent from this statute is any language vesting this Commission with discretion in the implementation of pass-through increases or decreases. Specifically, the statute states that the utility's rates "shall be automatically increased or decreased without hearing. . . ." Section 367.081(4)(b), Florida Statutes. Therefore, we have no discretion to deny pass-through increases or decreases once notice is given to us. This interpretation is supported by the statute's legislative history which indicates that the legislature intended to allow utilities to pass increased costs on to consumers sooner than the law in effect at that time allowed. SB 297, 6th Leg., Spec. and 2nd Sess., 1980 Fla. Sess. Law Ch. 80-99 (enacted). Obviously, the goal was to keep the utility whole by providing a mechanism whereby the utility could recoup certain increased costs without resort to a rate case.

The statute further provides that the rates shall be automatically increased or decreased upon verified notice to the Commission 45 days prior to its implementation of the increase or decrease. The statute is unclear because it does not specify whether the utility's initiation of the pass-through process is mandatory or permissive.

Some of the affected utilities have argued that decreases should only be required in the event that the utility is overearning at the time the decrease occurs. While we agree that decreases should be implemented when a utility is overearning, as

stated earlier, we believe a more restrictive interpretation of the statute is required.

It is a basic tenet of statutory construction that statutes will not be interpreted so as to yield an absurd result. See Dorsey v. State, 402 So.2d 1178 (Fla. 1981). The practical application of our interpretation of the statute is to reduce the utility's rates to reflect the reduction in purchased water and/or wastewater costs so long as the utility is not underearning. We recognize that an interpretation which would require a utility that is underearning to reduce rates when certain decreases occur is not practical because such an action serves only to preserve an undesirable situation. Arguably, the customers of such a utility benefit by the utility retaining the revenue stream and in doing so mitigating its loss position. Not only does this reduce financial pressure on the utility, but it may also forestall future rate proceedings.

However, when the utility is within its authorized range of return, we believe that the utility should have no discretion in its initiation of decreases and any reduction should be passed through. If a utility is already earning within its authorized range, decreasing rates in accordance with the decrease in costs will leave the utility in the same earnings position and will benefit customers through a rate reduction. In fact, a reduction in costs without a corresponding reduction in revenues could conceivably result in creating an overearnings situation. In any event, if a utility within its authorized range does not decrease its rates commensurate with its decrease in costs, the utility clearly gains and the customers clearly lose. If the utility does implement a corresponding decrease in rates, the utility is no worse off from an earnings stand point and the customers receive the benefit of the reduction in purchased costs to which they are rightfully entitled. From a policy perspective, this is a preferred result because it is fair, just, and equitable.

As to our authority to require regulated utilities to decrease their rates, contrary to the utility's assertions, we believe that this Commission is vested with the authority to order a reduction in rates when the utility fails to initiate a decrease pursuant to Section 367.081(4)(b), Florida Statutes. Section 367.011(2), Florida Statutes, vests this Commission with the exclusive jurisdiction over each utility with respect to its authority, service, and rates. Section 367.121, Florida Statutes, provides that this Commission shall have the power to prescribe fair and reasonable rates and to do all things necessary or convenient to the full and complete exercise of its jurisdiction and the enforcement of its orders and requirements.

We also believe that we may address such decreases in a limited proceeding pursuant to Section 367.0822(1), Florida Statutes. Section 367.0822(1), Florida Statutes, specifically allows the Commission on its own motion to require a rate adjustment if a matter is within its jurisdiction. Clearly, we have exclusive jurisdiction over each regulated utility with respect to rates. See Section 367.011(2), Florida Statutes. Furthermore, Section 367.0822, Florida Statutes, provides that if the issue of rate of return is not specifically addressed in the limited proceeding, we may adjust rates so long as the adjustment does not effect a change in the utility's last authorized rate of return. Pass-through increases and decreases have no effect on a utility's earnings because the change in revenue equals the change in expense. In other words, pass-through increases and decreases are earnings neutral, and the utility's rate of return is not affected by a pass-through adjustment. Therefore, we may properly order such pass-through adjustments pursuant to Section 367.0822, Florida Statutes. Furthermore, we note that we have previously ordered a pass-through rate reduction in a limited proceeding. See Order No. 20728.

Based on the foregoing, we find it appropriate to require pass-through decreases in the event that the utility meets or exceeds the minimum of its authorized range of return on equity to reflect the reduction in purchased water and/or wastewater costs to bulk water and/or wastewater customers in Pasco County.

APPLICATION OF PASS-THROUGH STATUTE TO HUDSON

On April 1, 1996, Pasco County reduced its bulk wastewater rate from \$3.11 to \$2.20. On October 1, 1996, the rate was increased from \$2.20 to \$2.23. As a result, the net decrease in Pasco County's rate was \$.88, on a prospective basis, as of October 1, 1996. However, Hudson elected not to reduce its wastewater rates to reflect the reduced cost of purchased wastewater.

The utility's position is that in the case of an underearning utility, such as itself, the Legislature intended to allow the utility to forego a pass-through decrease if the impact of foregoing the pass-through decrease leaves the underearning utility in an improved financial situation yet below the bottom of the range of its last authorized rate of return on equity. The utility states that in 1995, Hudson had an achieved rate of return of less than 1 percent. Further, the utility contends that by not passing through Pasco County's reduction in purchased wastewater treatment costs, Hudson's 1995 earnings climb to a meager 2.74%, well below its authorized 12.73% rate of return.

Hudson's last authorized rate of return on equity was established as 13.51%, with a range of 12.51% - 14.51%, by Order No. 23810, issued November 27, 1990, in Docket No. 900293-SU. The utility provided Exhibit A in its response to the show cause order. Exhibit A reflects an achieved rate of return for the utility of .90% for 1995. Based on this achieved rate of return, the utility's achieved rate of return of equity is calculated to be a negative (297%). Further, in Exhibit A, the utility calculated a reduction in purchased wastewater costs of \$56,393. This reduction was calculated by multiplying the gallons of wastewater treated by Pasco County in 1995 (61,970,000), by the reduction in purchased wastewater cost per thousand gallons on April 1, 1996 (\$3.11 - \$2.20 = \$.91). Exhibit A also reflects the impact on earnings of a reduction in purchased wastewater expense of \$56,393, without a corresponding reduction in revenues. As a result of this adjustment, the utility calculated an achieved rate of return of 2.74%. Based on this rate of return, the utility's achieved rate of return on equity is calculated to be a negative (240.62%).

We used the information contained in the utility's 1995 annual report to calculate a reduction for purchased wastewater costs of \$57,104, resulting in a decrease of \$.92 per thousand gallons of wastewater treated. The reduction was calculated by computing the difference in purchased wastewater costs at the old rate (\$3.11) and the new rate (\$2.23) and then dividing by the gallons of wastewater treatment sold for the most recent twelve month period. According to the utility's 1995 annual report, 61,970,000 gallons of wastewater treatment was purchased and sold. Using the old Pasco County bulk wastewater rate of \$3.11 per thousand gallons of wastewater treated, the total purchased wastewater cost is calculated to be \$192,727 (61,970 x 3.11). The new reduced bulk rate of \$2.23 results in a total cost of \$138,193 (61,970 x \$2.23). The difference between the cost at the old rate and the new rate results in an annual decrease of \$57,104 (($\$192,727 - \$138,193$) / (.955)). The decrease of \$57,104 divided by the total gallons of wastewater treatment sold of 61,970 results in a \$.92 change to the gallonage charge. Our calculations of the decrease are shown on Schedule No. 1.

As discussed above, the utility's achieved rate of return for 1995 was .90% prior to any adjustment for the purchased wastewater cost reduction. This results in an achieved return on equity of negative (297%). When the utility's revenues and expenses are reduced by our calculated reduction of \$57,104, the utility's achieved rate of return is calculated to be .91%, with a return on equity of negative (297%). However, if the utility's expenses are adjusted without a corresponding reduction in revenues, the rate of

return is calculated to be 2.68%, with a achieved return on equity of a negative (243%).

We have determined that a utility's rates will be reduced to reflect a reduction in purchased water and/or wastewater costs only in the event that the utility meets or exceeds the minimum of its authorized range of return on equity. The utility is earning well below its minimum 12.51% authorized rate of return on equity. Therefore, we find that no reduction in rates is appropriate at this time.

REFUND

As discussed previously, because the utility's achieved rate of return on equity is well below the minimum of its authorized range of return, no reduction is required. Further, we find that no refund is appropriate.

CLOSING OF DOCKET

Upon expiration of the protest period, if a timely protest is not received from a substantially affected person, this docket shall be closed.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that Hudson Utilities, Inc. shall not be required to reduce its rates to reflect the April 1, 1996 reduction in purchased wastewater costs to bulk wastewater customers in Pasco County. It is further

ORDERED that Hudson Utilities, Inc. shall not be required to refund or make any other adjustment as a result of the April 1, 1996 decrease in purchased wastewater costs to bulk wastewater customers in Pasco County. It is further

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

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

ORDERED that the provisions of this Order, except our decision regarding the utility's request for a waiver and the resolution of the show cause proceeding, are issued as proposed agency action and shall become final unless an appropriate petition in the form provided by Rule 25-22.029, Florida Administrative Code, is received by the Director, Division of Records and Reporting, 2540

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Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings or Judicial Review" 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 13th day of April, 1997.

BLANCA S. BAYÓ, Director
Division of Records and Reporting

by: Kay Flynn
Chief, Bureau of Records

(S E A L)

BLR

DISSENT

Commissioner Diane K. Kiesling dissents with opinion:

I respectfully dissent on the issue of measuring a utility's earnings against the range of its authorized rate of return to determine whether a pass-through decrease should be implemented. A dollar for dollar reduction in a known expense, as described in Section 367.081(4)(b), Florida Statutes, should produce a dollar for dollar reduction in rates. A pass-through expense is not a variable expense within the control of the utility. The statute recognizes this and provides the utility the flexibility in its rates to pass on expenses such as the cost of utility service from a governmental entity. Therefore, I believe that a reduction in this expense should be followed with a concomitant reduction in rates. In reaching this conclusion, I have not overlooked Section 367.081(4)(c), Florida Statutes, which precludes a utility from benefiting from a pass-through expense where it is already overearning. The statutory scheme of rate making is designed to give a utility an opportunity to earn a fair rate of return on its equity, not to guarantee such a return. Therefore, I believe that we are not obligated to insure that a utility will not be underearning in determining that a pass-through decrease is to be implemented. The decrease is required.

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.

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.

The action proposed herein, except our decision regarding the utility's request for a waiver and the resolution of the show cause proceeding, is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a)

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and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on May 13, 1997.

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

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days of the effective date of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

| HUDSON UTILITIES INC. -PASCO DOCKET NO. 961417-SU | SCHEDULE 1 |
|--|---------------------------|
| PURCHASED SEWAGE TREATMENT CALCULATION | WASTEWATER |
| PURCHASE SEWAGE TREATMENT ANNUALIZED AT OLD RATE | (192,727) |
| PURCHASE SEWAGE TREATMENT ANNUALIZED AT NEW RATE | - 138,193 |
| LESS ACTUAL PURCHASED SEWAGE TREATMENT COSTS | \$ (54,534) |
| DIVIDED BY EXPANSION FACTOR FOR RAFS | <u>0.955</u> |
| DECREASE IN PURCHASED SEWAGE TREATMENT COSTS | \$ (57,104) |
| DIVIDE BY GALLONS SEWAGE TREATED | - <u>61,970</u> |
| DOLLAR CHANGE TO GALLONAGE CHARGE ONLY | \$ <u>(0.92)</u> ===== |

**** (OLD RATE = \$3.11, NEW RATE \$2.23, GAL. TRT. 61,970,000)**