

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION
TALLAHASSEE, FLORIDA

IN RE: Annual reestablishment of authorized range of returns
on common equity for water and wastewater utilities,
pursuant to Section 367.081(4)(f), F.S.

DOCKET NO. 960006-WS

ORIGINAL

BEFORE: CHAIRMAN SUSAN F. CLARK
COMMISSIONER J. TERRY DEASON
COMMISSIONER JULIA L. JOHNSON
COMMISSIONER DIANE K. KIESLING
COMMISSIONER JOE GARCIA

PROCEEDING: AGENDA CONFERENCE

ITEM NUMBER: 36**PAA

DATE: May 21, 1996

PLACE: 4075 Esplanade Way, Room 148
Tallahassee, Florida

REPORTED BY: JANE FAUROT, RPR
Notary Public in and for the
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1 PARTICIPATING:

2 Kenneth Hoffman, Esquire, representing SSU and the
3 Florida Waterworks Association4 Marty Deterding, Esquire, representing Aloha
5 Utilities and Rainbow Springs

6 * * * * *

7 STAFF RECOMMENDATIONS8 Issue 1: Recommendation that, based on the current range of
9 returns on common equity authorized by the Commission for
10 other regulated utilities, the 10.18% to 11.88% range of
11 returns approved in Order No. PSC-95-0892-FOF-WS is still
12 reasonable for water and wastewater utilities for the period
13 until the leverage formula is readdressed.14 The authorized range of returns on common equity for
15 water and wastewater utilities should be based on the
16 following formula:17
$$\text{Return Common Equity} = 9.05\% + 1.131/\text{Equity Ratio where the}$$
18
$$\text{Equity Ratio} = \text{Common Equity}/(\text{Common Equity} + \text{Preferred}$$
19
$$\text{Equity} + \text{Long-term and Short-term Debt})$$
20 Further, the authorized return on equity should be
21 limited to a maximum of 11.88% for all equity ratios of less
22 than 40% in order to discourage imprudent financial risk.23 Issue 2: Recommendation that this docket remain open.
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P R O C E E D I N G S

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2 CHAIRMAN CLARK: Item 36. Questions,
3 Commissioners, on Item 36? Mr. Hoffman, are you here
4 to answer questions?

5 MR. HOFFMAN: Yes, ma'am. I'm here on behalf of
6 Southern States Utilities and the Florida Waterworks
7 Association to express our support for the
8 recommendation.

9 CHAIRMAN CLARK: Mr. Deterding.

10 MR. DETERDING: I'm here on behalf of Aloha
11 Utilities and Rainbow Springs, who both have pending
12 cases before the Commission, I assume to which this
13 would apply, also in support of the staff
14 recommendation.

15 CHAIRMAN CLARK: Isn't that usually the case
16 whatever the current index is? Is that what we do? Or
17 is there an issue in that case -- do we need to worry
18 about it? Has Mr. Deterding just raised an issue that
19 is not an issue?

20 MR. DETERDING: I didn't know I did, if I did.

21 COMMISSION STAFF: Commissioners, normally in our
22 cases if we don't reach a stipulation -- well, normally
23 we do reach a stipulation on return on equity. But
24 even if we don't, we normally use the leverage graph in
25 effect at the date of the agenda conference in our

1 cases.

2 CHAIRMAN CLARK: All right.

3 COMMISSIONER KIESLING: Move it.

4 COMMISSIONER DEASON: I have a question. When are
5 we going to readdress the appropriateness of the
6 leverage graph, or the mechanism by which we calculate?
7 Is that contemplated here or not?

8 COMMISSION STAFF: Soon, Commissioner. Maybe this
9 year.

10 COMMISSIONER DEASON: But in the meantime we are
11 going to not use the traditional means of the leverage
12 graph, is that correct?

13 COMMISSION STAFF: That was not my understanding.

14 COMMISSION STAFF: No, Commissioner, we would use
15 the leverage formula that is currently in place.

16 COMMISSIONER KIESLING: But we are not going to
17 update it.

18 COMMISSION STAFF: We're not going to update it at
19 this time, and -- well, you would be issuing an order
20 that the formula that was approved ... 95-0892 is still
21 appropriate, and an order to that effect --

22 COMMISSIONER DEASON: We're not going to update it
23 with current information.

24 COMMISSION STAFF: Well, depending on the outcome
25 of your vote.

1 COMMISSIONER DEASON: Well, my question is, if it
2 is staff's opinion that by using current information
3 you get an unrealistic result, that means there must be
4 something wrong with the formula.

5 COMMISSION STAFF: No, that is not the impression
6 that --

7 COMMISSIONER DEASON: Well, then why is that we
8 don't -- if the formula is fine, we put current
9 information in it, we turn the crank and the result is
10 the result. Where is the problem?

11 COMMISSION STAFF: Staff is still comfortable with
12 the models, and we are still comfortable with the
13 methodology we use. We have looked at Commission
14 decisions rendered since the leverage formula was last
15 put in place. The Commission can exercise its judgment
16 on return on equity in these other industries, and we
17 have looked at the level of returns for the other
18 industries, we have looked at the level of returns that
19 fall out from the current leverage formula, and we
20 believe they are in sync. And we would recommend that
21 the formula remain in place. We have not lost
22 confidence in the formula.

23 COMMISSIONER DEASON: But you feel a better result
24 using the old information as opposed to the new
25 information?

1 COMMISSION STAFF: At this time, yes. And there
2 has been a change, as the capital markets have moved
3 over time, we have -- I mean, certain returns, the
4 level of returns, 10.18 to 11.88 that are currently
5 authorized under the formula, we think are reasonable
6 at this point in time given the allowed returns in the
7 other utility industries.

8 COMMISSION STAFF: And, Commissioner Deason,
9 that's where we, in the division of water and sewer,
10 support the recommendation, is that we believe that the
11 current -- even the old or current, whichever one is in
12 effect right now, are still too low, because all of the
13 returns are less than the electric and telephone
14 industries.

15 COMMISSIONER DEASON: And I don't necessarily
16 disagree with you. The problem I'm having is that it
17 runs afoul of the concept of having a leverage graph
18 formula. That you take the judgment out. You take the
19 data, you put it in the formula, and you get a result.
20 And nobody is supposed to argue with it, because the
21 model is supposed to work.

22 And what I'm hearing is that it's not working.
23 Nobody is comfortable with the results, so we are
24 comfortable with what it generated last year, so let's
25 just stick with it, and we may look at it again. And

1 what we are trying to do is get away from the judgment
2 side by having the formula and we are getting ourselves
3 right back into it, and saying, well, judgment-wise, we
4 want to live with what we had before and let's don't
5 update it and we may look at the formula again and we
6 may not. That's what I'm uncomfortable with.

7 COMMISSION STAFF: And I guess my only response to
8 that is we are uncomfortable with lowering the leverage
9 graph when we feel that it is already too low.

10 COMMISSIONER DEASON: This is another one of these
11 philosophical problems I have. I mean, the whole
12 reason we have is it to get it out of the judgment side
13 of things. If not, every time we had a rate case we
14 would just say, staff, what do you think is a good rate
15 of return? And, say, oh, well, we think what we did
16 last week is fine. Okay, let's plug it in. But we
17 have got a formula that we update with current
18 information, and supposedly it takes all of that
19 judgment out of it, and it is objective, and we live
20 with the results, and that's the problem that I'm
21 having.

22 CHAIRMAN CLARK: I guess -- what are you concerned
23 about the judgment, the judgment that is being
24 exercised? What the formula has produced this time is
25 lower than what is currently --

1 COMMISSION STAFF: That's correct.

2 CHAIRMAN CLARK: And yet staff feels that it is
3 too low already and it shouldn't be lowered, so you're
4 exercising judgment, one. I agree with that. But it
5 will be applied throughout the year and it avoids the
6 necessity of doing it in each rate case. But I would
7 agree with Commissioner Deason, to the extent if we
8 don't think the formula is producing what it ought to
9 produce, we need a new formula.

10 COMMISSION STAFF: Again, Commissioners, staff
11 does not believe the formula no longer works. We are
12 looking at the issue of parity within the industries,
13 and we are looking at how ROE changed in the other
14 industries since this decision was rendered. And those
15 allowed ROEs are not coming down. We are still
16 confident in the methodology we are employing in the
17 water and wastewater industry, we just believe that for
18 parity, for fairness that the level of returns
19 indicated by the current formula should remain in
20 place.

21 CHAIRMAN CLARK: Any other questions,
22 Commissioners? Was there a motion?

23 COMMISSIONER KIESLING: I moved it.

24 COMMISSIONER JOHNSON: Second.

25 CHAIRMAN CLARK: All those in favor say aye.

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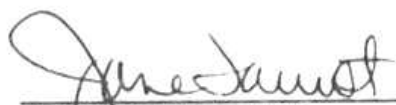
COMMISSIONER JOHNSON: Aye.
COMMISSIONER GARCIA: Aye.
COMMISSIONER KIESLING: Aye.
CHAIRMAN CLARK: Aye. Opposed, nay.
COMMISSIONER DEASON: Nay.

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3 CERTIFICATE OF REPORTER

4 STATE OF FLORIDA)

5 COUNTY OF LEON)

6 I, JANE FAUROT, Court Reporter, do hereby certify
7 that the foregoing proceedings was transcribed from cassette
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11 employee, attorney or counsel of any of the parties, nor
12 relative or employee of such attorney or counsel, or
13 financially interested in the foregoing action.14 DATED THIS 19th day of May, 1997.15
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