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July 23, 1997

Division of Administrative Hearings
1230 Apalachee Parkway
Tallahassee, FL 32399-1550

HAND DELIVERY

**RE: Florida Waterworks Association v. Florida Public Service
Commission**

To whom it may concern:

Enclosed on behalf of the Florida Waterworks Association are an original and five copies of a Petition for Administrative Determination of Invalidity of Proposed Rule.

Please acknowledge receipt of the foregoing by stamping the enclosed extra copy of this letter and returning same to my attention. Thank you for your assistance.

Sincerely,

Wayne L. Schiefelbein
Wayne L. Schiefelbein

- ACK _____
- AFA _____
- APP _____
- CAF _____
- CMU _____
- CTR _____
- EAG _____
- LEG _____
- LIN _____
- OPC _____
- RCH _____
- SEC 1 _____
- WAS _____
- OTH _____

WLS/l dv
Enclosure
cc w/encl.:

Christiana T. Moore, Esq. (Hand Delivery)
Kenneth A. Hoffman, Esq. (Hand Delivery)
Blanca S. Bayo (Hand Delivery)

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FPSC-RECORDS/REPORTING

STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

FLORIDA WATERWORKS ASSOCIATION,

Petitioner,

v.

DOAH Case No. _____
Filed: July 23, 1997

FLORIDA PUBLIC SERVICE COMMISSION,

Respondent.

**PETITION FOR ADMINISTRATIVE DETERMINATION
OF INVALIDITY OF PROPOSED RULE**

The Petitioner, the Florida Waterworks Association (FWA), by and through its undersigned counsel, and pursuant to Section 120.56(2), Florida Statutes (1996), hereby seeks an administrative determination of the invalidity of proposed rule 25-30.431, Florida Administrative Code, as proposed by the Florida Public Service Commission (PSC). In support of this Petition, the FWA states:

1. For the purposes of this proceeding, the address and telephone number of the Petitioner, the FWA, should be considered that of its undersigned counsel.

2. The affected agency is the PSC at the address of 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850.

3. The FWA is comprised of investor-owned water and/or wastewater utility companies in the State of Florida, and is the Florida Chapter of the National Association of Water Companies, Inc. The FWA exists to assist its members with regulatory, technical and operational matters. A substantial number of the

members of the FWA are water and wastewater utilities regulated by the PSC, and are subject to its rules and regulations, including the Proposed Rule. As such, the FWA is substantially affected by the Proposed Rule.

Summary of Relief Requested

4. The FWA seeks a final order from the Administrative Law Judge that Proposed Rule 25-30.431, as modified, constitutes an invalid exercise of delegated legislative authority; violates the constitutional rights of affected utilities to due process, to just compensation for taking of property, to possess and protect property, and to equal protection of the law; and is, therefore, void. The FWA also seeks an award of reasonable costs and attorney's fees, pursuant to Section 120.595(2), Florida Statutes (1996).

Summary of Controversy

5. In virtually every water and wastewater rate case brought before it, the PSC addresses the issue of recognition of the appropriate "margin reserve," and the offsetting imputation of contributions-in-aid-of-construction (CIAC) against that margin reserve.

6. The term "margin reserve" is a ratesetting term of art which connotes an increment of capacity of water and wastewater facilities that is greater than the capacity needed to provide service to the historical demand of existing customers as of a

designated twelve-month period ("test year"¹), which increment is necessary for a utility to have on hand to meet increases in the demand of existing customers and to render service to new customers, for a designated period subsequent to the test year. Subject to the offsetting imputation of CIAC (discussed hereinbelow), investment in the capacity included in margin reserve is included in the net investment of a utility devoted to public service ("rate base"²) upon which the utility is entitled to earn a fair rate of return.³

7. Since it originally coined the term "margin reserve," the PSC has consistently adhered to the practice of allowing margin

¹A test year is an analytical devise used in ratemaking proceedings to compute levels of investment, expenses and income in order to determine the amount of revenue that will be required to assure the company a fair rate of return on its investment. Citizens of Florida v. Hawkins, 356 So.2d 254, 256 (Fla. 1978) The test year is chosen so that it will reflect typical conditions in the immediate future. United Telephone Company of Florida v. Mayo, 345 So.2d 648, 650 (Fla. 1977)

²Rate base is the total amount which a utility has invested in capital items to provide its service to the public. Citizens of Fla. v. Public Service Commission, 435 So.2d 784 (Fla. 1983); Citizens of Fla. v. Hawkins, 364 So.2d 723, 725 (Fla. 1978).

³The rate base upon which a utility is afforded an opportunity to earn a return is "not every dollar of investment made but only that investment in assets devoted to public service at the time rate base is quantified." Gulf Power Company v. Florida Public Service Commission, 453 So. 2d 799, 806 (Fla. 1984). A utility is "entitled to a just compensation, or a fair return on the value of its property used or useful in the public service." Keystone Water Company, Inc. v. Bevis, 278 So. 2d 606, 609 (Fla. 1973). The used and useful concept and its relationship to margin reserve is discussed in paragraphs 38 et seq. hereinbelow.

reserve periods of "18 months" for water supply and treatment plant and wastewater treatment and disposal plant,⁴ and "12 months" for water transmission and distribution and wastewater collection lines. These periods of time were derived from PSC Staff research in the early 1980s which found that for such facilities, these periods reflected the average time required for planning, design, bids, permitting, actual construction and clearance for service from the appropriate regulatory agency. A projection of expected growth in customer demand over the designated margin reserve period is made and converted into the increment of capacity needed to accommodate that increased demand.

8. For over a decade, the PSC has also consistently imputed CIAC⁵ as an offset to margin reserve.⁶ Although over the years a variety of rationales have been provided by the PSC for this practice, the underlying philosophy is that existing customers

⁴A singular exception is the three-year margin reserve period approved for a wastewater treatment plant expansion in Florida Cities Water Company, Golden Gate Division, 95 FPSC 6:141-142 (June 15, 1995).

⁵CIAC are customer contributions of cash paid or property conveyed by customers to a utility as they connect to a utility system to offset a portion of the cost of the facilities serving them. As a utility is not allowed to earn a return on plant funded by CIAC (Sec. 367.081(2)(a), Florida Statutes), CIAC is treated as an offset to the cost of plant in determining rate base.

⁶A singular exception is Poinciana Utilities Inc., 94 FPSC 9:354 (September 26, 1994), where the PSC, by a 2 to 1 decision, did not impute CIAC against margin reserve because of the absence of record support for the imputation.

should not "subsidize" the cost of extending service to future customers.⁷ The PSC projects the amount of CIAC it anticipates will be collected after the test year and over the margin reserve period, and subtracts this projected CIAC from the amount of existing utility investment in margin reserve capacity. The imputation can severely diminish or entirely offset ratemaking recognition of investment in margin reserve.

9. For at least the last six years, the FWA and its member utilities have sought reform of these policies. The essence of the FWA position has been and continues to be that the margin reserve periods recognized by the PSC are far too short to reflect the time needed under current environmental regulatory rules and requirements to bring capacity on line in an economical manner; that the offsetting imputation of CIAC results in an unfair denial of an opportunity to earn a fair rate of return on investment necessary for the utility to comply with its statutory obligations of service to existing and future customers; and that the inevitable effect of traditional margin reserve and imputation policies is to remove any incentive to construct plant capacity in prudent, economically sized increments, resulting in unnecessarily high water and wastewater rates for both existing and future

⁷This imputation policy was sustained by the First District Court of Appeal as being within the PSC's discretion. Rolling Oaks Utilities, Inc. v. Florida Public Service Commission, 533 So.2d 770, 773-775 (Fla. 1st DCA 1988). See paragraphs 50 et seq. hereinbelow.

customers.

Rulemaking Before the PSC

10. The FWA has sought meaningful reform of the PSC's margin reserve and imputation policies through rulemaking for six years. The PSC established a rulemaking docket in 1991 to consider an overhaul of its administrative rules governing water and wastewater utilities. Throughout a series of "staff workshops" held in 1992, the FWA attempted to facilitate rulemaking on the PSC's determinations of the amount of plant considered used and useful in providing service to the public, including margin reserve and imputation of CIAC. On March 24, 1993, the PSC issued a Notice of Rulemaking which contained a comprehensive rule proposal addressing used and useful, including proposals governing margin reserve for water source and treatment facilities, wastewater treatment and disposal facilities, water transmission and distribution lines and wastewater force and gravity mains, onsite collection lines, laterals and pumping stations, and calling for a prohibition of the imputation of CIAC against margin reserve. Order No. PSC-93-0455-NOR-WS, Proposed Rules 25-30.432, 25-30.433(5).

11. At a hearing in August, 1993, the PSC voted to delay further consideration of the used and useful, margin reserve, and imputation issues, indicating that it would revisit those issues after at least one additional meeting or workshop. Thus, the revised water and wastewater rules adopted by the PSC did not

address these issues. (Orders Nos. PSC-93-1663-FOF-WS and PSC-93-1704-FOF-WS, both issued in November 1993)

12. Despite repeated assurances by the PSC and its Staff that rulemaking on used and useful, margin reserve and imputation of CIAC would be pursued, the PSC did absolutely nothing for two years, despite pleas by the FWA and its member companies that the matter was "the key issue for the industry." In June, 1995, PSC Staff distributed a draft rule providing for a three-year margin reserve. Imputation of CIAC was not mentioned. At a Staff workshop held in July, 1995, the FWA and its member companies gave substantial testimony in support of five-year margin reserve periods and a cessation of the imputation practice. Representatives of the Florida Department of Environmental Protection (DEP) advocated longer margin reserve periods than that proposed by the industry. Another eight months passed with no action taken by the PSC.

13. On March 1, 1996, the FWA filed a Petition to Adopt Rules with the PSC, pursuant to Section 120.54(5), Florida Statutes (1995). The FWA thereby proposed that the PSC modify its nonrule policies to

- establish margin reserve periods of five years for water source and treatment and wastewater treatment and conventional effluent disposal facilities, and two years for onsite water distribution and collection lines and

laterals, unless otherwise justified;

- require PSC consideration of a nonexclusive list of factors which may justify a different margin reserve period;
- deem prudently constructed effluent reuse facilities, water transmission mains and off-site wastewater force and gravity mains and pumping stations as fully used and useful, with margin reserve not a factor; and
- prohibit the imputation of CIAC as an offset to margin reserve.

14. The PSC agreed to initiate rulemaking. 96 FPSC 5:48 (May 6, 1996) The PSC subsequently proposed a rule that would have codified the PSC's then-existing nonrule policy, of establishing margin reserve periods of 18 months for water source and treatment and wastewater treatment and disposal facilities, and 12 months for all water and wastewater lines, unless otherwise justified; and mandating the offsetting imputation of CIAC. Florida Administrative Weekly, Volume 22, No. 31, pp. 4385-4386 (August 2, 1996)

15. On August 14, 1996, the FWA filed a Petition for Administrative Determination of Invalidity of Proposed Rule with the Division of Administrative Hearings (DOAH). (Case No. 96-3809RP) Since the PSC was scheduled to conduct a hearing to consider the Proposed Rule on December 10, 1996, the FWA requested

that the DOAH proceeding be abated.

16. On August 23, 1996, Florida Water Services Corporation (FWSC), formerly known as Southern States Utilities, Inc., filed a Petition for Administrative Determination of Invalidity of Proposed Rule with DOAH. (Case No. 96-3949RP) FWSC is the largest investor-owned water and wastewater utility regulated by the PSC. FWSC also requested abatement of the DOAH proceeding, and consolidation with the FWA's proposed rule challenge proceedings. Abatement and consolidation of the two proceedings were granted.

17. The PSC issued an Order Establishing Procedures to be Followed at Rulemaking Hearing. Order No. PSC-96-1153-PCO-WS (September 16, 1996) The Order established a schedule and other procedural requirements for the submittal of initial and responsive prefiled comments, testimony and exhibits by interested persons. The FWA; FWSC; Utilities, Inc. of Florida; DEP; the St. Johns Water Management District; the South Florida Water Management District; the Southwest Florida Water Management District; the Office of the Public Counsel (OPC); and the Staff of the PSC all submitted comments, testimony and/or exhibits.

18. In October, 1996, in a rate case brought by Southern States Utilities, the PSC, while adhering to its standard margin reserve periods, declared that "(w)e recognize that CIAC will be collected evenly throughout the margin reserve period" and therefore found that it was appropriate to impute "half" of the

CIAC associated with the allowed margin reserve. Southern States Utilities, Inc. 96 FPSC 10:461-462 (October 30, 1996)⁸

19. The full five-member PSC convened a day-long hearing on December 10, 1996. The opportunity to present evidence and argument was extended to all interested persons. Six expert witnesses appeared on behalf of the industry. Representatives of DEP and three water management districts, and several members of PSC Staff, addressed the PSC. OPC provided no expert testimony or other documentation other than brief comments it had prefiled a few months previously. The opportunity to question each person appearing at the hearing was extended to all participating parties. The resulting record of the hearing consists of over 1100 pages of hearing transcript and exhibits.

20. The PSC informed interested persons of its intention to address adoption of the Proposed Rule at its April 14, 1997 agenda conference. Accordingly, the Administrative Law Judge continued abatement of the consolidated rule challenge proceedings, through May 30, 1997.

21. On April 2, 1997, the PSC Staff filed their recommendation for adoption of a rule establishing five-year margin reserve periods for water source and treatment and wastewater treatment and disposal facilities, unless otherwise justified, and

⁸See also Palm Coast Utility Corporation, 96 FPSC 11:41-42 (November 7, 1996); Gulf Utility Company,; Order No. 97-0847-FOF-WS (July 15, 1997), at pp. 30-34.

prohibiting the offsetting imputation of CIAC. The Staff recommendation and the notice of its consideration by the PSC at the April 14, 1997 agenda conference stated that discussion of the matter was restricted to the Commissioners and Staff, and that "adoption should not be deferred."

22. However, following a request by a state legislator, the PSC abruptly and indefinitely deferred any decision at its April 24, 1997 agenda conference.

23. On May 29, 1997, the FWA and FWSC filed a request for further abatement, after being advised by PSC Staff that it appeared the PSC would, pursuant to legislator request, likely reopen the record and conduct further hearings on the proposed rule. Pursuant to that request, the Administrative Law Judge granted continued abatement through November 30, 1997.

24. On June 10, 1997, after consideration of argument by among others, State Senator Cowin, OPC, the FWA and FWSC, the PSC voted to not reopen the record or to hold additional hearings. Instead, the PSC voted to change its proposed rule.

25. On June 24, 1997, the FWA and FWSC filed a joint motion seeking termination of the abeyance and leave to file amended petitions for administrative determination of rule invalidity addressing the proposed rule, as modified.

26. On June 27, 1997, the Administrative Law Judge ruled that:

Upon consideration, procedural safe guards afforded affected persons with regard to proposed rules would appear better served by Petitioners filing new, initial challenges to what will effectively be a new, and perhaps different, proposed rule than that which is presently at issue in this proceeding.

Accordingly, in order to permit Petitioners, and possibly others, full opportunity to file any future petitions challenging modification to the proposed rule, it is determined that further proceedings in this cause shall stand abated only until conclusion of a 20-day period following Respondent's publication of the notice of modification or proposed rule in the Florida Administrative Weekly, an event expected to occur on or about July 3, 1997. Following expiration of that period, the issue of whether the instant proceeding is mooted shall be considered.

27. The PSC published its Notice of Change of Proposed Rule in the Florida Administrative Weekly on July 3, 1997, at Volume 23, Number 27, pp. 3335-3336. A copy of the Notice and Proposed Rule 25-30.431, is appended hereto as Exhibit 1. The Proposed Rule, as modified, is hereinafter referred to as "the Proposed Rule."

The Proposed Rule, as Modified

28. The Proposed Rule

- a) provides a definition of the term "margin reserve" (Proposed Rule 25-30.431(1));
- b) provides a definition of the term "margin reserve period" (Proposed Rule 25-30.431(2));
- c) provides that margin reserve is an acknowledged component of the used and useful rate base determination (Proposed Rule 25-30.431(3));
- d) establishes an 18-month margin reserve period for water source and treatment facilities and wastewater treatment and effluent disposal; and identifies an exclusive list of three factors for the PSC to consider in determining whether another

margin reserve period is justified (Proposed Rule 25-30.431(4));

- e) provides a formula for determining margin reserve for water source and treatment facilities and wastewater treatment and disposal facilities (Proposed Rule 25-30.431(5)(a));
- f) deletes from the scope of the Proposed Rule water and wastewater lines;
- g) provides reference to a methodology for projecting customer growth (Proposed Rule 25-30.431(5)(b));
- h) requires a linear regression analysis of customer growth, and allows for the submittal of other information in that regard (Proposed Rule 25-30.431(5)(c));
- i) requires submittal of the most recent wastewater capacity analysis report filed with DEP (Proposed Rule 25-30.431(6)); and
- j) as an offset to margin reserve, mandates the imputation of "50 percent" of the projected CIAC that "will be collected" from the Equivalent Residential Connections (ERCs) included in the margin reserve, subject only to the limitation that the imputed CIAC "shall not exceed the rate base component associated with margin reserve." (Proposed Rule 25-30.431(7)).

INVALID EXERCISE OF DELEGATED LEGISLATIVE AUTHORITY

29. As set forth hereinbelow, the FWA asserts that the Proposed Rule is an invalid exercise of delegated legislative authority, on the following grounds:

- a) the Proposed Rule is not supported by competent substantial evidence;
- b) the Proposed Rule contravenes the specific provisions of law implemented;

- c) the Proposed Rule is vague, fails to establish adequate standards for agency decisions, and vests unbridled discretion in the agency; and
- d) the Proposed Rule is arbitrary and capricious.

30. The FWA further asserts that the Proposed Rule is unfairly discriminatory and violates the right of affected utilities to equal protection of the law. In addition, the Proposed Rule violates the constitutional rights of affected water and wastewater utilities, to due process, to just compensation for taking of property, and to possess and protect property.

The Proposed Rule is not supported by
competent substantial evidence.

31. The PSC conducted a hearing on the instant rulemaking on December 10, 1996. The FWA and FWSC provided extensive expert testimony, studies and other documentation in support of five-year margin reserve periods for water source and treatment facilities and wastewater treatment and traditional effluent disposal facilities; two-year margin reserve periods for onsite water distribution and collection lines and laterals; special consideration for prudent effluent reuse facilities, water transmission mains and offsite wastewater source and gravity mains and pumping stations; and a prohibition of the practice of offsetting margin reserve by imputed CIAC. The DEP, and the three water management districts with the highest concentration of PSC-regulated water and wastewater utilities in the State of Florida,

appeared in support of the FWA's proposal of a five-year margin reserve period for source, treatment and conventional disposal facilities, and for special consideration of effluent reuse facilities. At hearing, PSC Staff itself advocated doubling the proposed margin reserve period for treatment facilities and abandoning the CIAC imputation policy. OPC opposed recognition of any margin reserve whatsoever, and, to the extent one is approved, its complete offset through imputation of CIAC. OPC prefiled brief comments, no expert testimony and no exhibits.

32. PSC Staff submitted a posthearing recommendation for adoption of five-year margin reserve periods for water source and treatment and wastewater treatment and disposal facilities, unless otherwise justified, and abandonment of the imputation policy. The PSC rejected this recommendation.

33. The PSC's decision to adopt the Proposed Rule utterly disregarded the record. There is no evidentiary support for 18-month margin reserve periods for water source and treatment and wastewater treatment and disposal facilities. There is no evidentiary support for imputation of "50%" of CIAC against margin reserve. There is no competent substantial evidence to support those central provisions of the Proposed Rule.

34. Under the 1996 revisions to the Administrative Procedures Act (APA), the definition of the term "invalid exercise of delegated legislative authority" was modified to include, inter,

alia, the following:

The rule is not supported by competent substantial evidence. Sec. 120.52(8)(f), Fla. Stat. (1996)

35. Further, the APA also provides the following regarding modification of proposed rules:

Any change, other than a technical change that does not affect the substance of the rule, must be supported by the record of public hearings held on the rule, must be in response to written material received on or before the date of the public hearing, or must be in response to a proposed objection by the [Administrative Procedures] committee. Sec. 120.54(3)(d), Fla. Stat. (1996)

36. The FWA anticipates that the PSC and possibly other intervenors will attempt to treat the instant proceeding as entirely a de novo proceeding, whereby evidence and argument will be offered in support of the Proposed Rule, which was not offered at the hearing before the PSC. The FWA respectfully submits that if this is permitted, Section 120.52(8)(f) would be rendered a nullity. If the PSC may disregard the record developed before it in its rulemaking proceedings with impunity, interested persons affected by its proposed rules would be better off to forego participation at rulemaking proceedings before the PSC until their conclusion, at which time they may initiate rule challenges at DOAH. This result would thwart the Legislature's intent to instill agency discipline in rulemaking proceedings.

37. Where as here an agency conducts a rulemaking proceeding which provides reasonable notice to interested persons, a reasonable opportunity to provide testimony, evidence and argument

on a proposed rule, and to question witnesses appearing before it, the agency should be bound to base its rule on competent substantial evidence in the record developed before it in that rulemaking proceeding. There is no competent substantial evidence supporting the provisions of the Proposed Rule establishing an 18-month margin reserve period offset by imputation of 50% of CIAC. As such, those provisions of the Proposed Rule are an invalid exercise of delegated legislative authority.

The Proposed Rule contravenes the specific provisions of law implemented.

38. The Proposed Rule cites Sec. 367.081, Florida Statutes, as the law implemented. Sec. 367.081(2)(a), Florida Statutes, provides in pertinent part:

The commission shall...fix rates which are just, reasonable, compensatory, and not unfairly discriminatory. In every such proceeding, the commission shall consider the value and quality of the service and the cost of providing the service, which shall include, but not be limited to...maintenance, depreciation, tax and operating expenses incurred in the operation of all property used and useful in the public service; and a fair return on the investment of the utility in property used and useful in the public service.

39. The term "used and useful" is undefined by statute or rule. However, a cogent explanation of the concept was given by

the PSC itself in a 1977 rate case order:⁹

The concept of "used and useful" in the public service," basically an engineering concept, is one of the most valuable tools in regulation and ratemaking. It is basically a measuring rod or test used to determine the portion or amount of the utility's assets which are to be included in its rate base and upon which the utility has an opportunity to earn a return.

Basically a two step determination, the first step is to establish the physical existence and costs of the assets which the utility alleges are in its operations....

Once the existence and cost of a utility's assets has been established, the second step in defining used and useful is to determine which identified assets are really used and useful in performing the utility's service obligation. The asset must be reasonably necessary to furnish adequate service to the utility's customers during the course of the prudent operation of the utility's business.

Generally, any asset which is required to perform a function which is a necessary step in furnishing service to the public is considered used and useful.

In addition, good engineering design will give a growing utility a sufficient capacity over and above actual demand to act as a cushion for maximum daily flow requirements and normal growth over a reasonable period of time. (emphasis added)

40. The Proposed Rule aptly defines the term margin reserve

as

the amount of plant capacity needed to preserve and protect the ability of utility facilities to serve existing and future customers in an economically feasible manner that will preclude a deterioration in quality of service and prevent adverse environmental and health

⁹In re: Petition of Deltona Utilities, a Division of the Deltona Corporation, to increase its water and sewer rates in Volusia County, Order No. 7684, Docket No. R-750626-WS, (March 14, 1977).

effects. Proposed Rule 25-30.431(1)

41. Investment in margin reserve is investment in plant used and useful in providing service. See for example Orange-Osceola Utilities, Inc., 88 FPSC 12:95 (December 8, 1988); Palm Coast Utility Corporation, 90 FPSC 4:361 (April 23, 1990); South Broward Utility, Inc., 90 FPSC 4:449 (April 23, 1990); Sailfish Point Utility Corporation, 91 FPSC 9:341 (September 23, 1991); Florida Cities Water Company, N. Ft. Myers Division, 92 FPSC 7:15 (July 1, 1992); Lehigh Utilities, Inc., 93 FPSC 2:783 (February 25, 1993); Southern States Utilities, Inc., 93 FPSC 3:522 (March 22, 1993); and Palm Coast Utility Corporation, 96 FPSC 11:39 (November 7, 1996). See also Proposed Rule 25-30.431(3), which provides that margin reserve "is an acknowledged component of the used and useful rate base determination...."

42. The used and useful character of margin reserve is predicated on the utility's statutory obligation of readiness to serve. Water and wastewater utilities subject to PSC jurisdiction are required by statute to provide safe, efficient and sufficient service, not less safe, less efficient, or less sufficient than is consistent with the approved engineering design of the system and the reasonable and proper operation of the utility in the public interest. Sec. 367.111(2), Fla. Stat. This obligation to serve applies to both existing and future customers located within the utility's certificated service area. Sec. 367.111(1), Fla. Stat.

43. To fulfill its statutory responsibility of "readiness to serve," a water and wastewater utility must have sufficient capacity to meet the existing and changing demands of existing customers and the demands of potential customers within a reasonable time and in an economic manner. The investment in that readiness to serve capacity is properly recognized in rate setting as a margin reserve.

44. The Proposed Rule would deprive affected utilities of an opportunity to earn a fair rate of return on this investment in margin reserve. First, the Proposed Rule provides for a 18-month margin reserve period which significantly understates a reasonable margin reserve for water source and treatment and wastewater treatment and disposal facilities. Second, the opportunity to demonstrate margin reserve periods longer than 18 months to the PSC's satisfaction is illusory. The PSC routinely disregards evidence, however substantial, supporting longer margin reserves, and adheres to 18-month margin reserve periods. Third, by its imputation or offset of CIAC that might be paid over the margin reserve period, the amount of investment in margin reserve on which a utility is allowed to earn a return is dramatically reduced far below that which is necessary to comply with the statutory obligation of readiness to serve, and can even be eliminated.

45. Under the Proposed Rule, utilities will be deprived of an opportunity to a return on prudent investment in margin reserve.

Included in the record of the PSC hearing is a financial model developed by the FWA to measure the impact of various margin reserve periods and CIAC imputation scenarios. This model assumes that the regulatory situation is an ideal one, where there is full recovery of operation and maintenance expenses, predictable customer growth and plant utilization, and no regulatory lag. This enabled the FWA to isolate the impact of only those components being measured. Even under the model's "best case" scenario, the model predicts that if a utility is allowed an eighteen month margin reserve and if CIAC is imputed it will not be able to recover its authorized rate of return in the 30 year forecast period.¹⁰

46. The PSC has previously attempted to justify its imputation policy on the grounds of "fairness," that, without imputation, future customers may be subsidized by current customers. This purported justification rests on the assumption that the amount of capacity represented by the margin reserve exists solely to serve future customers, and that those customers, with absolute certainty, will appear in the time frame of the margin reserve period. This oversimplified connection between margin reserve and future customers ignores the legitimate purposes

¹⁰Under its financial model, the FWA has determined that even if only 50% of CIAC were imputed, the return only improved by .1% on rate base over the 30 years -- maintaining the utility in a situation of consistently underearning.

of a margin reserve, which is purportedly recognized by the Proposed Rule's definition of margin reserve. Margin reserve provides a cushion such that a utility can be prepared to meet the anticipated peak load conditions of its existing customers, with a reasonable degree of reliability, even when unanticipated outages occur. Margin reserve provides a cushion such that a utility can be prepared to meet changing load conditions of its existing customers, over and above the peak loads historically experienced, with a reasonable degree of reliability. Margin reserve includes capacity over and above that required for existing loads that may exist merely because economic sizing and timing of plant expansions dictate that result. As a fallout, margin reserve provides capacity adequate to meet ongoing projected growth.

47. The PSC has attempted to justify its limited recognition of margin reserve on the grounds that its existing used and useful nonrule policies already provide adequate recognition of changing load conditions of existing customers. This is ludicrous, particularly in light of a series of PSC decisions beginning in September, 1996, in which the PSC allowed as used and useful the ratio of annual average daily flows for wastewater treatment for permitted capacity, disregarding substantial seasonal flow variations experienced by such plants. See, for example, Florida Cities Water Company, N. Ft. Myers Division, 96 FPSC 9:146-148 (September 10, 1996); Palm Coast Utility Corporation, 96 FPSC 11:55

(November 7, 1996); Southern States Utilities, Inc., 96 FPSC 10:438 (October 30, 1996); but see Florida Cities Water Company, Barefoot Bay Division, 97 FPSC 2:568 (February 25, 1997).

48. Even if the PSC properly recognized sufficient capacity to meet peak demand, a margin reserve remains necessary. To fulfill its statutory mandate of readiness to serve, in a manner that is consistent with the reasonable operation of the utility in the public interest, utilities must be able to react to changes in the historical peak demands of their existing customers. For example, for most water plants, the variability of the maximum day demand from existing customers can easily be 10% from year to year. It would be shortsighted and irresponsible not to have capacity in reserve on hand to meet changing peak demand. Utilities cannot wait for expressed customer demand before they commit funds to provide service. Utilities are obligated by law to be ready to serve, and in return, the law gives them the opportunity to earn on the investment necessary to meet their obligations. The appropriate vehicle to facilitate compliance with such statutory requirements is recognition of adequate margin reserve in rate base.

49. Margin reserve periods of 18 months are far too short to allow a utility to plan, construct and permit capacity additions in an economical manner or, in some cases, to operate in compliance with DEP regulations. The Proposed Rule will perpetuate

disincentive for complying with DEP and water management district regulatory requirements regarding public health and water quality protection. See for example Rule 62-600.405, Florida Administrative Code, which sets a five-year time period for the planning, design and construction of needed expansion of wastewater facilities.

50. Nine years ago, in Rolling Oaks Utilities, Inc. v. Florida Public Service Commission, the First District Court of Appeal sustained the PSC's imputation of CIAC against an allowed margin reserve. 533 So 2d 770 (1st DCA 1988) at 773-775. The Court found that margin reserve "in a sense rewards the utility for its investment in plant capacity which the utility has readily available, but not currently in use." (emphasis added) According to the Court, the PSC thereby "permits the utility to charge its existing customers a portion of the cost necessary to have service available for future customers." (at 773) According to the Court, through imputation of CIAC to the margin reserve, the PSC requires "the utility and future users of the utility's services to bear a part of the cost of making future services readily available. Absent this policy, existing customers would bear all of the cost of making services available to future customers." (at 774) The Court noted with apparent approval that the CIAC imputation was limited so as not to exceed a rate base reduction "further than if no margin reserve had been allowed." (at 774) The Court ultimately

upheld the PSC's "incipient policies" on margin reserve and imputation of CIAC as within the PSC's discretion.

51. We do not have the evidence of record in the Rolling Oaks case at hand. However, in the rulemaking proceedings before the PSC, there is overwhelming record support for recognition that margin reserve should be considered "currently in use," and which therefore should be given full weight in rate-making, without imputation of CIAC. The Proposed Rule purports to recognize that margin reserve is currently in use, by its definition of margin reserve as capacity "needed to preserve and protect the ability of utility facilities to serve existing and future customers in an economically feasible manner that will provide a deterioration in quality of service and prevent adverse environmental and health effects." Proposed Rule 25-30.431(1) Further, the Proposed Rule deems margin reserve "an acknowledged component of the used and useful rate base determination...." Proposed Rule 25-30.431(3)

52. The FWA believes that the Rolling Oaks case was incorrectly decided by the court. In any event, circumstances have substantially changed over the decade following the PSC's decision in that rate case. The premise for the Court's decision was that margin reserve was "not currently in use." This premise is not valid and, therefore, the Court's conclusion is no longer valid. Florida has adopted a new state water policy and a far more complicated environmental permitting process, which have had a

tremendous impact on the economics of water and wastewater utility decision-making for reserve capacity.

53. The FWA submits that the statutory requirement that the PSC set rates which are just and reasonable requires meaningful consideration of economic feasibility. As it has long been for PSC rate-setting for electric utilities, the guiding principle should be "what alternative results in the lowest long run cost?"

54. The Proposed Rule includes in its definition of margin reserve the amount of plant capacity needed to protect the ability of utility facilities to serve existing and future customers in an economically feasible manner. Further, margin reserve period is defined as the time period needed to plan, design and install the next economically feasible increment of plant capacity. The FWA believes that an evaluation of economic feasibility must properly involve considerations of economies of scale. The 18-month margin reserve period proposed by the rule utterly disregards obvious documented economies of scale associated with larger size increments of plant capacity. In practice, the PSC disregards economies of scale in adhering to 18-month margin reserve periods.

55. It is better for both the utility investor and the utility customers to incorporate the economy of scaling a plant by constructing a larger size plant and providing for some reasonable amount of extra capacity. Economically sized construction results in lower rates and service availability charges than do smaller

sized plants, in the short term and over the long term. In addition, the net present value of revenue requirements is lower when economically sizing plant.

56. As a result of the PSC's blind adherence to 18-month margin reserve periods, offset by imputed CIAC, utilities have chosen to expand in smaller increments in order to achieve a higher level of cost recovery, rather than in longer increments which would provide economies of scale but on which cost recovery is unlikely. Additional costs which are incurred and passed along to customers as a result of these decisions include higher construction costs associated with smaller incremental expansions, duplicative engineering, permitting, and contractor mobilization costs; and higher rate case expense from more frequent rate hearings. The result is higher customer rates, in both the short and long term.

57. The PSC has previously rationalized its margin reserve and imputation policies on the basis of the assertion that the availability of an Allowance for Funds Prudently Invested (AFPI) is a valid surrogate for margin reserve.

58. PSC policy and rules provide for recovery of an Allowance for Funds Prudently Invested (AFPI). The AFPI charge purports to be a "mechanism which allows a utility to earn a fair rate of return on prudently constructed plant held for future use from the future customers to be served by that plant in the form of a charge

paid by those customers." Rule 25-30.434(1), Fla. Admin. Code. The intent of the allowance is to enable utilities to recover carrying costs and expenses associated with prudent non-used and useful plant, to be paid by future customers as they connect to the system, along with service availability charges. Generally, AFPI accumulates certain fixed costs associated with non-used and useful plant and compounds for five years. By approving the charge, the PSC has acknowledged that investment in non-used and useful plant is prudent and the utility should receive a return on that prudent investment.

59. The investment in margin reserve is used and useful plant, and the portion offset by imputed CIAC that is not earned on in rate base is not recoverable through the AFPI charge. See Rule 25-30.434(3)(f), Fla. Admin. Code. Since there is by definition no opportunity to earn on investment in margin reserve against which CIAC has been imputed, from either current or future customers, the utility is never made whole. Those earnings on prudent investment are lost forever.

60. AFPI does not adequately compensate utilities for a full margin reserve. AFPI has resulted in an unfair shifting of costs from current customers to future customers. When cost recovery is shifted from the current revenue requirement to AFPI, future customers end up paying for all "non-used and useful" plant through higher AFPI charges while current customers receive the benefits of

any economies of scale associated with that plant.

61. AFPI is speculative, that is to say, collection of AFPI revenue is entirely dependent upon growth. Even though the PSC recognizes the investment is prudent, the utility bears the entire risk of growth occurring as projected.

62. Utilities are not made whole by AFPI, even when growth occurs as projected. The revenue from rates plus AFPI falls far short of providing the authorized rate of return.

63. The effect of computation problems related to imputation of CIAC also needs to be considered. There being no adjustment to increase the number of future customers subject to AFPI when CIAC is imputed, substantial earnings on prudent investment are forfeited by the utility.

64. The inherently speculative nature of AFPI has a real world impact on utility financing. AFPI does not generate cash flow, it generates "paper earnings" which may or may not materialize. Accordingly, lenders will not loan money to utilities on the basis of AFPI. Utility auditors do not allow a utility to record revenues related to AFPI on an accrual basis. It's only recorded when the cash is actually in hand.

65. AFPI also poses a dilemma for utilities: they must choose between the excessively complex administration associated with a myriad of qualifying assets, or having to start the carrying cost accruals and calculation of the charge all over again. Each

calculation of AFPI is (typically) for a five-year period, associated with a specific qualifying asset, where the costs are accumulated, therefore increasing during that period. If during those five years other qualifying assets are added, then a new total of all qualifying assets is calculated and used as the basis for the new fee. However, the fee begins accumulating from zero once again. The only way to prevent this is to calculate a separate fee for each new qualifying asset, every time one is added. This would be nearly impossible to administer since utilities are in a continuous state of extending lines, expanding treatment plant, and adding wells. Furthermore, there is no rational mechanism to apply the correct fee to each individual customer.

66. In a best case scenario, receipt of AFPI charges is speculative, that is to say, collection of AFPI revenue is entirely dependent upon growth. If customer growth does not materialize, for whatever reason, no recovery of the carrying costs is achieved. FWSC's recent rate case represents the worst case scenario regarding recovery of AFPI.¹¹ The PSC, sua sponte, eliminated previously approved AFPI charges associated with some of FWSC's systems before all ERCs projected in the AFPI calculation were connected, and "zeroed out" previously approved AFPI charges for

¹¹Southern States Utilities, Inc., Order No. PSC-96-1320-FOF-WS (October 30, 1996) at 256-257; Florida Water Services Corporation, Order No. 97-0374-FOF-WS (April 7, 1997), Sch. 10-B

other FWSC systems, whereby the accumulated accrual of carrying costs were disallowed and the accrual process began anew, starting over from a zero cost base. These decisions permanently foreclosed FWSC's recovery of substantial prudent plant-related costs.

The Proposed Rule is vague, fails to establish adequate standards for agency decision, and vests unbridled discretion in the agency.

67. The Proposed Rule declares that unless otherwise justified, a margin reserve period of 18 months for water source and treatment facilities and wastewater treatment and effluent disposal facilities. The Proposed Rule identifies the following factors that the PSC shall "consider" in determining whether another margin reserve period is justified:

the rate of growth in the number of equivalent residential connections (ERCs); the time needed to meet the guidelines of the Department of Environmental Protection (DEP) for planning, designing and construction of plant expansion; and the technical and economic options available for sizing increments of plant expansion. Proposed Rule 25-30.431(3)

68. How a utility may show that consideration of these factors warrant margin reserve periods longer than 18 months, and how these factors will be considered or evaluated by the PSC, is not addressed by the Proposed Rule. Because of the vagueness of the rule and the inadequacy of the standards for PSC decisions, the Proposed Rule would inevitably result in a continuation of the PSC's longstanding exercise of unbridled discretion on the issue,

wherein no matter what evidence is provided, the result is the same: 18-month margin reserve periods.

69. The so-called "DEP guidelines" referenced by the Proposed Rule are codified at Rule 62-600.405, Florida Administrative Code. Utility compliance with these requirements is mandatory. The DEP rule sets a five-year time period for planning, design and construction of wastewater treatment, reuse and disposal facilities.¹² The purpose of the DEP rule is to ensure the continuous availability of adequate wastewater treatment and disposal capacity, and to thereby avoid capacity crisis which endanger the environment and the public health. The requirements of the rule have been in effect since early 1991. During that period, the PSC has nonetheless consistently set margin reserve periods for wastewater treatment, reuse and disposal facilities at eighteen months, rejecting utility reliance on the rule as justification for longer margin reserve periods for such facilities.¹³

¹²The DEP intends to implement a comparable rule regulating community public water systems in order to ensure the timely planning, design and construction of water facilities necessary to provide proper supply and treatment of drinking water. In any event, the DEP and the water management districts in fact often seek assurance of reserve capacity for water facilities, sufficient to accommodate growth over a period of five or more years.

¹³The PSC penalizes utilities for failing to comply with DEP requirements. See, for example, Indian Springs Utilities, Inc., 93 FPSC 12:420-421, (December 23, 1993).

70. The PSC has also consistently adhered to 18-month margin reserve periods for water source and treatment and wastewater treatment and disposal facilities, rejecting utility requests for longer margin reserve periods based on documentation of the benefits of economies of scale and threshold facility sizing.

71. In the absence of adequate standards, the opportunity to justify a margin reserve period other than 18 months to the PSC's satisfaction is illusory, under prior longstanding PSC nonrule policy, and under the Proposed Rule.

The Proposed Rule is arbitrary and capricious.

72. An arbitrary decision is "one not supported by facts or logic" while a capricious action is "one which is taken without thought or reason." Agrico Chemical Co. v. State, Dept. of Envir. Reg., 365 So. 2d 759 (Fla. 1st DCA 1979) at 763.

73. The PSC's designation of 18-month margin reserve periods is arbitrary and capricious. As previously discussed, this designation has no record support from the PSC proceeding. Further, there is no rational basis for the PSC to consider an 18-month margin reserve period as an appropriate standard for source, treatment and disposal facilities. There is no rational basis for the proposition that 18 months is "the time period needed to install the next feasible increment of plant capacity" (i.e., the PSC's proposed definition of margin reserve period) for such facilities.

74. In the early 1980s, the PSC Staff conducted research and found that the average planning, permitting and construction time for water source and treatment and wastewater treatment and disposal facilities was 18 months. These time frames allowed for design, bids, actual construction and clearance for service from the appropriate regulatory agency.

75. In recent years, environmental regulation and policy has substantially extended the time it takes for water and wastewater utilities to obtain permits, increasing the associated costs. Under generic circumstances, it typically requires three and a half to five years to plan, design, permit, construct, test and certify water and wastewater facility expansions, without any regards to economies of scale or "threshold sizing" constraints for various plant components. Further, meeting environmental and conservation concerns in a manner acceptable to permitting agencies often leads to several alternatives being designed and considered before being accepted a process that can entail many additional months or even years.¹⁴ During the period from conception to completion, capacity must be available to provide service. And as this time increases, the capacity reserve requirement also increases. These factors are not given their due weight, under existing PSC policy, as embodied in the Proposed Rule. In practice, after "consideration" of such

¹⁴See, for example, Florida Cities Water Company, Barefoot Bay Division, 96 FPSC 9:238-242 (September 12, 1996).

factors, the PSC disregards them and establishes margin reserve at the 18-month level set forth in the Proposed Rule. As a result, the amount of plant in which a utility should economically invest to serve the public is either not being built or, when it is built, its cost is not being allowed to be recovered through rates.

76. The PSC's proclamation that "50 percent" of the projected CIAC that "will" be collected from the ERCs included in the margin reserve shall offset margin reserve is arbitrary and capricious. By this imputation or offset of half of the CIAC that in actuality might be paid over the margin reserve period, the amount of investment in margin reserve on which a utility is allowed to earn a return is dramatically reduced and can even be eliminated. In actuality, a "50%" imputation results in minimal recognition of investment in margin reserve, far below that which is necessary to comply with the utility's statutory obligations to provide service.¹⁵ Even under a "best case" scenario (no regulatory lag, full recovery of operation and maintenance expenses, and predictable plant customer growth and plant utilization) where an 18-month margin reserve is allowed and 50% of CIAC is imputed, a utility will be denied an opportunity to earn its authorized rate

¹⁵See for example Palm Coast Utility Corporation, 96 FPSC 11:42 (November 7, 1996). The net result of the PSC's "50%" imputation of CIAC was the recognition of capacity and investment necessary to serve customers all of 3.75 weeks beyond the midpoint of the test year for water source and treatment plant, and 13.50 weeks beyond the midpoint of the test year for wastewater treatment and disposal plant.

of return.

77. The PSC has attempted to justify its imputation of CIAC against the margin reserve as necessary "to achieve proper matching of the CIAC collections made from those customers which will connect during the margin reserve period." Palm Coast Utility Corporation, 96 FPSC 11:42 (November 7, 1996). This reasoning is specious. The PSC ignores the fact that margin reserve is an increment of investment already made in the current period to serve existing and future customers, while imputed CIAC is CIAC which may be contributed by future customers (if customer growth materializes as projected) beyond the test year. Moreover, as new customers are added, there is then a need for yet additional margin reserve. Investment in margin reserve is necessary to serve existing and new customers, whether or not growth expectations are realized. The imputation of CIAC against margin reserve is an illogical mismatching of actual period investment with speculative future contributions that denies a utility the ability to earn on its investment in margin reserve. Such imputation is not matching, it is the antithesis of matching, which violates the concept of the test year. It is a mismatch which the PSC does not even consider for any other revenue or cost category. For example, the PSC does not impute into the test year the revenues or expenses not yet incurred but associated with future customers beyond the test year.

78. The Proposed Rule's failure to distinguish between

conventional effluent disposal facilities and reuse facilities¹⁶ is arbitrary and capricious. This failure cannot be reconciled with the statutory mandate of Florida's Air and Water Pollution Control Act, which is administered by DEP. Section 403.064(10), Florida Statute provides that

Pursuant to Chapter 367, the Florida Public Service Commission shall allow entities under its jurisdiction which conduct studies or implement reuse projects... to recover the full, prudently incurred cost of such studies and facilities through their rate structure.

Further, Chapter 367 itself has been amended to provide that "(a)ll prudent costs of a reuse project shall be recovered in rates." Sec. 367.0817(3), Fla. Stat. The PSC has nonetheless declined to make any special provision for reuse facilities to facilitate full cost recovery. Under nonrule policy, and in the Proposed Rule, the PSC refuses to distinguish between conventional disposal facilities and reuse facilities. See, for example, Southern States Utilities, Inc., 96 FPSC 10:441-444 (October 30, 1996).

79. The encouragement and promotion of water conservation and reuse of reclaimed water, as defined by DEP, have been declared to be state objectives and are considered to be in the public interest. Sec. 373.250(1), Fla. Stat. The PSC's refusal to allow

¹⁶Reuse is defined by DEP as the deliberate application of reclaimed water, in compliance with DEP and water management district rules, for a beneficial purpose. Rule 62-610.200(49), Fla. Admin. Code. DEP has also codified its criteria in great detail for classifying projects or portions of projects as "reuse" versus the more traditional methods of "effluent disposal." Rule 62-610.810(2) and (3), Fla. Admin. Code.

recovery of the full prudently incurred costs of reuse facilities through rates is in clear derogation of State water policy and the aforementioned statutes. This refusal has a far-reaching chilling effect, discouraging investor-owned utilities contemplating implementation of a reuse strategy to make investments in such technology. Simply put, absent assurance of cost recovery for prudent reuse facilities, such projects will be deemed not economically feasible by investor-owned utilities.¹⁷

80. The Proposed Rule's enumeration of the factors that the PSC "shall consider" are limited to the rate of customer growth; the time needed to meet the "guidelines" of the DEP for planning, designing and construction of plant expansion; and the technical and economic options available for sizing increments of plant expansion. There are additional factors which the PSC should be required to meaningfully consider, including the regulatory requirements of water management districts, and the effect of regulatory lag. These additional factors have a substantial impact on the ability of a utility to earn a fair rate of return on investment in margin reserve. The PSC's failure to include such

¹⁷A utility applying for a permit to construct or operate a wastewater treatment facility located within, serving a population located within, or discharging within a water resource caution area is required to prepare a reuse feasibility study. Such study must include a cost/benefit analysis, including an evaluation of rates and fees necessary to implement reuse and other economic constraints. So long as the study evaluates the requisite criteria, the permit applicant's determination of feasibility is final. Sec. 403.064(2) and (3), Fla. Stat.

factors in the Proposed Rule is arbitrary and capricious.

The Proposed Rule is unfairly discriminatory and violates the right of affected utilities to equal protection of the law.

81. The concept of used and useful is not unique to water and wastewater utilities. Chapter 366 of the Florida Statutes, which regulates electric and gas utilities, requires the PSC "to investigate and determine the actual legitimate costs of the property of each utility company, actually used and useful in the public service...." For ratemaking purpose the net investment in such property is "the money honestly and prudently invested by the public utility company in such property used and useful in serving the public...." Sec. 366.06(1), Fla. Stat. This is substantially the same statutory grant of ratemaking authority to the PSC for water and wastewater utilities. Sec. 367.081(2)(a), Fla. Stat.

82. Reserve capacity is a necessity for water and wastewater utilities and electric utilities, to assure their ability to provide adequate and reliable service to existing customers, whose level of demand on such capacity may increase, and to future customers. Therefore, investment in prudent reserve capacity is properly considered used and useful in providing service to the public.

83. Although capacity reserves are recognized as necessary to protect and provide service to the customers of water and wastewater and electric utilities, the PSC nonetheless describes and measures reserve capacity differently for water and wastewater

utilities than for electric utilities, as illustrated below:

RESERVE CAPACITY

Water and Wastewater

Referred to as MARGIN RESERVE.

"Needed" to preserve and protect the ability of utility facilities to serve existing and future customers, but must be requested. (Proposed Rule 25-30.431(1), (3))

Expressed in terms of annual growth.

Must be requested by the utility, but then is restricted to a maximum of 18 months, unless "otherwise justified." (Proposed Rule 25-30.431 (3) & (4))

Electric

Referred to as MARGIN RESERVE.

"Required" in order to meet all reasonable demands for service. (Rule 25-6.035(1), Fla. Admin. Code)

Expressed in terms of a percentage of annual peak demand.

Minimum reserve (15% of peak demand) required by PSC (Rule 25-6.035, Fla. Admin. Code)

84. The PSC's disparate treatment of capacity reserves for water and wastewater utilities and electric utilities is evident in its rate orders. A typical rate order for a water and wastewater utility contains substantial discussion of why margin reserves should be limited to the maximum of 18 months even though greater reserves may be economically justified and will increase the ability to render service.¹⁸ A typical rate order for an electric utility is devoid of any discussion of reserve margins unless there is some event that might reduce reserves below the minimum during

¹⁸See, for example, Southern States Utilities, 96 FPSC 10:426-428 (October 30, 1996).

the test year or for future years.¹⁹ But one has to go beyond the rate orders, and into the docket records themselves to realize that the investment allowed in rate base for electric utilities includes capacity reserves sufficient to meet the long term demands of customers while the investment allowed in rate base for water and wastewater utilities barely provides for capacity reserves sufficient to make it through the test year.

85. The planned reserves for the three privately-owned electric generating utilities serving peninsular Florida for the next ten years provide capacity that ranges from the equivalent of 6.5 years to 24.3 years of anticipated growth in peak load demand. Using only the minimum level required by the PSC to be maintained by electric generating utilities, the reserves provide capacity that range from the equivalent of 4 years to 17 years anticipated of growth in peak load demand. The electric utilities include reserves in excess of the minimum required generally because the combination of capacity additions that result in the higher level of reserves represent the best economic choice of alternatives for serving the growing demand over the long run. The regulatory treatment accorded reserve capacity for water and wastewater utilities should parallel that for electric utilities.

86. PSC-regulated electric and gas utilities and water and wastewater utilities are similarly situated as to the type of

¹⁹See, for example, Tampa Electric Company, 93 FPSC 2:63-64 (February 2, 1993).

facilities required to provide utility service. In order to provide service to the public, these utilities must construct, purchase or pay for, maintain, service and upgrade various types of fixed assets, including production, transmission, distribution, storage and processing facilities and capacity. These facilities require reserve capacity to ensure adequate and reliable service to existing and future customers.

87. Under the equal protection guarantee of the United States Constitution, PSC-regulated water and wastewater utilities are entitled to regulatory treatment for prudent investment in utility plant similar to that employed by the PSC to determine used and useful investment for electric facilities, including the recognition of prudent reserve capacity.

The Proposed Rule violates the constitutional rights of affected water and wastewater utilities, to due process, to just compensation for taking of property, and to possess and protect property.

88. The Proposed Rule's failure to provide adequate standards (discussed in paragraphs 67-71 hereinabove) violates constitutional due process rights of affected utilities to adequate and full notice of what it must do to justify a margin reserve period other than eighteen months.

89. Under the Proposed Rule's provisions setting 18-month margin reserve periods offset by imputed CIAC, utilities will never have the opportunity to earn their authorized rate of return on its investment in margin reserve. Such utilities will be denied an

opportunity to earn on the investment necessary to fulfill its statutory obligations to provide safe, efficient and sufficient service, not less safe, less efficient, or less sufficient than is consistent with the approved engineering design of the system and the reasonable and proper operation of the utility in the public interest. Sec. 367.111(2), Fla. Stat. Further, such utilities will be denied an opportunity to earn on the investment necessary to fulfill its statutory obligation of "readiness to serve" existing and future customers within their certificated service areas. Sec. 367.111(1), Fla. Stat. In addition, such utilities will be denied an opportunity to earn on the investment necessary to comply with environmental agency regulatory requirements governing availability of capacity.

90. Utilities are entitled to "a fair return upon the value of that which it employs for the public convenience." Smyth v. Ames, 169 U.S. 466, 547; 42 L. Ed. 819, 849, 18 S. Ct. 418 (1898) Rates which are not sufficient to yield a fair return on the value of is property used and useful in the public service are unjust, unreasonable, and confiscatory, and their enforcement deprives the utility of its property, in violation of the Fifth and Fourteenth Amendments to the Federal Constitution. Bluefield Water Works and Improvement Company v. Public Service Commission, 262 U.S. 679, 690; 43 S. Ct. 675, 67 L.Ed. 1176 (1923); Keystone Water Company, Inc. v. Bevis, 278 So. 2d 606, 609 (Fla. 1973).

Costs and Attorney's Fees

91. As it does in individual rate cases, the PSC has ignored all evidence in support of rational margin reserve policies. The PSC has chosen to disregard the unrefuted financial models, economies of scale studies, and analyses of the impact of environmental regulation on margin reserve submitted in the PSC rulemaking proceedings, which were developed by the industry at great expense. After six years of delay, the PSC has instead proposed a rule which appears to have been a foreordained result, regardless of the evidence. There is in fact an utter absence of record support for the provisions of the Proposed Rule setting an 18-month margin reserve period for water source and treatment and wastewater treatment and disposal facilities, and mandating the offsetting imputation of CIAC. Further, those provisions lack a rational basis. Accordingly, the Proposed Rule is not substantially justified. There are no special circumstances which would make an award of costs and attorney's fees unjust. The FWA therefore requests recovery of its reasonable costs and attorney's fees, pursuant to Section 120.595(2), Florida Statutes (1996).

Material Facts in Dispute

92. The following material facts are in dispute in this proceeding:

- a) What, if anything, from the record of the PSC rulemaking proceedings supports an 18-month margin

reserve period for water source and treatment and wastewater treatment and disposal facilities?

The FWA alleges that there is no competent substantial evidence to support 18-month margin reserve periods for such facilities.

- b) What, if anything, from the record of the PSC rulemaking proceedings supports the 50% imputation of CIAC as an offset to margin reserve?

The FWA alleges that there is no competent substantial evidence to support the 50% imputation of CIAC as an offset to margin reserve.

- c) Must PSC-regulated water and wastewater utilities have sufficient capacity available to meet the existing and changing demands of existing customers, and the demands of potential customers, within a reasonable time and in an economic manner?

The FWA alleges that such capacity is an operational necessity, and that the investment in that capacity is properly recognized in ratesetting as a margin reserve.

- d) Is margin reserve capacity "currently in use?"

The FWA alleges that margin reserve capacity is "currently in use."

- e) Does an 18-month margin reserve period provide an

opportunity to earn a reasonable rate of return on investment in margin reserve?

The FWA alleges that an 18-month margin reserve period does not provide an opportunity to earn a reasonable rate of return on investment in plant capacity needed to preserve and protect the ability of utility facilities to serve existing and future customers in an economically feasible manner.

- f) Has the PSC routinely disregarded evidence supporting margin reserve periods larger than 18 months?

The FWA alleges that the PSC routinely disregards such evidence.

- g) What effect does the imputation of 50% of the CIAC that might be paid over the margin reserve period have on margin reserve?

The FWA alleges that the imputation reduces recognition of margin reserve, far below that which is necessary to comply with the statutory obligation of readiness to serve, and can effectively eliminate any recognition of margin reserve.

- h) Do existing PSC used and useful nonrule policies provide adequate recognition of changing load

conditions of existing customers?

The FWA alleges that these nonrule policies do not adequately recognize changing load conditions of existing customers.

- i) How have PSC policies on margin reserve and imputation affected utility decision making for reserve capacity?

The FWA alleges that utilities have chosen to expand in smaller increments in order to achieve a higher level of cost recovery, rather than in longer increments which would provide economies of scale but on which cost recovery is unlikely.

- j) How have the PSC policies on margin reserve and imputation affected customer rates?

The FWA alleges that higher construction costs; duplicative engineering, permitting and contractor mobilization costs; and higher rate case expense have resulted in higher customer rates.

- k) Does AFPI compensate utilities for margin reserve?

The FWA alleges that AFPI does not compensate utilities for investment in margin reserve.

- l) What is the time required to plan, design, permit, construct, test and certify water and wastewater facility expansions?

The FWA alleges that under generic circumstances, it requires 3½ to 5 years to plan, design, permit, construct, test and certify such expansions, without any regard to associated economies of scale or threshold sizing constraints. Further, meeting environmental and conservation concerns in a manner acceptable to permitting agencies often leads to several alternatives being designed and considered before their acceptance, a process that can add many additional months or years to the process.

- m) During the period from conception to completion, must capacity be available to provide service?

The FWA alleges that during said period, adequate capacity to meet the existing and changing demands of current customers and the demands of new customers is an operational necessity.

- n) What additional factors, other than those enumerated in the Proposed Rule, may justify margin reserve periods greater than 18 months?

The FWA alleges that, among other factors, permitting and other regulatory requirements of the water management districts, and the effect of regulatory lag, may justify greater margin reserve periods.

- o) What net margin reserve would likely be recognized after 50% imputation of CIAC?

The FWA alleges that typically, where an average test year is used, the net margin reserve recognized will be no more than 3 months capacity beyond that allowed in the test year, and in fact may not extend beyond the test year.

- p) Is imputation necessary to achieve "proper matching" of CIAC and margin reserve?

The FWA alleges that imputation is an illogical mismatch of actual investment and speculative collections of CIAC.

- q) Does the Proposed Rule provide reasonable assurance of cost recovery for prudent reuse facilities?

The FWA alleges that it does not.

- r) Are PSC-regulated water and wastewater utilities and PSC-regulated electric utilities similarly situated as to the type of facilities required to provide service?

The FWA alleges that these utilities are in fact similarly situated.

- s) Is the PSC's ratemaking authority for water and wastewater utilities and electric utilities substantially similar?

The FWA alleges that PSC ratemaking authority for these utilities is substantially similar.

- t) How are electric utilities' investment in reserve capacity treated by the PSC?

The FWA alleges that the PSC encourages and in fact requires electric utility investment in capacity required to meet anticipated growth in peak load demand over periods far in excess of the margin reserve periods it allows for water and wastewater utilities.

- u) Is the Proposed Rule substantially justified, and, if not, what special circumstances, if any, would make an award to FWA of its reasonable costs and attorney's fees unjust?

The FWA alleges that the Proposed Rule is not substantially justified and no such special circumstances exist.

WHEREFORE, the Petitioner, the Florida Waterworks Association, requests that:

(a) the Division of Administrative Hearings accept this Petition and assign an Administrative Law Judge to conduct a formal hearing in accordance with Section 120.56(1) and (2), Florida Statutes;

(b) the Administrative Law Judge enter a Final Order

determining that Proposed Rule 25-30.431 constitutes an invalid exercise of delegated legislative authority and is therefore void;

(c) the Administrative Law Judge enter a Final Order finding that Proposed Rule 25-30.431 violates the constitutional rights of affected utilities to due process, to just compensation for taking of property, to possess and protect property, and to equal protection of the law;

(d) the Administrative Law Judge award reasonable costs and attorney's fees to the FWA, pursuant to Sec. 120.595(2), Florida Statutes (1996); and

(e) such other relief as may be deemed just and proper.

Respectfully submitted this 23^d day of July, 1997.



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Association

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by hand delivery to Christiana T. Moore, Esquire and David L. Smith, Esquire, Division of Appeals, Florida Public Service Commission, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850 on this 23^d day of July, 1997.



WAYNE L. SCHIEFELBEIN

Exhibit 1

Proposed Rule 25-30.431

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available, and partially obliterated signs which do not identify a particular product, service, or facility shall be considered void of advertising matter.

37. 14-10.007(2) is amended to read:

(2) The Department may authorize the reconstruction of a nonconforming sign in instances where Occupational Safety and Health Act (OSHA) or other safety related requirements necessitate removal and recreation, provided that reconstruction shall not be authorized for modifications which are primarily for the purpose of replacement of deteriorated materials. Documentation of these requirements must be submitted to the Department for approval prior to making any sign modifications. If approval for reconstruction is granted by the Department, the location, structural configuration, number of faces, size of the sign faces, sign structure height, and the materials used in the sign structure and sign faces must be the same type as those used in the sign prior to the removal and reconstruction. During the period of temporary removal for those approved modifications, the permittee must permanently display the permit tag at the site.

38. 14-10.049(1)(b)2.c., last sentence is amended to read:

The Department at its option will, when required by FHWA, may prepare and implement a screening plan for a junkyard upon approval by FHWA and the junkyard owner.

DEPARTMENT OF TRANSPORTATION

RULE CHAPTER NO.: 14-51
RULE CHAPTER TITLE: Signing for Supplemental Guide Signs and Motorist Services on Limited and Non-Limited Access Highways

RULE NO.: 14-51.004
RULE TITLE: Signing for Supplemental Guide Signs and Motorist Services on Limited and Non-Limited Access Highways

NOTICE OF CHANGE

SUMMARY OF CHANGE: On Page II-68 of Section II.19, *Traffic Engineering Manual*, Signing for Off-Site Rental Car Return Facilities, which is being incorporated by reference, there are listed criteria required for the off-site rental car return facility to meet. In the fifth bullet listing of the criteria, the word "ramp" is being changed to "interchange exit" based upon written comments received from affected parties within the 21 days of publication of the notice of rulemaking. Specifically, the changed language is as follows:

"• Be located within 5 km of the primary interchange that services the airport and not be directly accessed from the interchange exit ramp serving the airport."

There are no changes to the text of the proposed rule itself. Notice was published in Florida Administrative Weekly, Volume 23, Number 24, June 13, 1997, Page 2928.

PUBLIC SERVICE COMMISSION

DOCKET NO. 960258-WS

RULE NO.: 25-30.431
RULE TITLE: Margin Reserve

NOTICE OF CHANGE

Notice is hereby given that the following changes have been made to the proposed rule in accordance with subparagraph 120.54(3)(d)1., F.S., published in Vol. 22, No. 31, August 2, 1996, issue of the Florida Administrative Weekly:

25-30.431 Margin Reserve.

(1) "Margin reserve" is defined as the amount of plant capacity needed to preserve and protect the ability of utility facilities to serve existing and future customers in an economically feasible manner that will preclude a deterioration in quality of service and prevent adverse environmental and health effects meet the expected demand due to customer growth.

(2) "Margin reserve period" is defined as the time period needed to install the next economically feasible increment of plant capacity ~~that will preclude a deterioration in the quality of service.~~

(3) Margin reserve is an acknowledged component of the used and useful rate base determination that when requested and justified shall be included in rate cases filed pursuant to section 367.081, Florida Statutes.

(4) Unless otherwise justified, the margin reserve period for water source and treatment facilities and wastewater treatment and effluent disposal facilities will be 18 months. ~~Unless otherwise justified, the margin reserve period for water transmission and distribution lines and the wastewater collection system will be 12 months.~~ In determining whether another margin reserve period is justified, the Commission shall consider the rate of growth in the number of equivalent residential connections (ERCs); the time needed to meet the guidelines of the Department of Environmental Protection (DEP) for planning, designing, and ~~construction~~ constructing of plant expansion; and the technical and economic options available for sizing increments of plant expansion.

(5)(a) Margin reserve for water source and treatment facilities and wastewater treatment and effluent disposal facilities shall be calculated as follows:

$$EG \times MP \times D = MR$$

where:

EG = Equivalent Annual Growth in ERCs determined pursuant to (b)(6) or (c)(d) below

MP = Margin Reserve Period determined pursuant to subsection (4)

D = Demand per ERC (customer demand applied in the used and useful calculations for water and wastewater facilities)

MR = Margin reserve expressed in gallons per day (GPD)

(b) ~~Margin reserve for water transmission and distribution lines and the wastewater collection system shall be calculated as follows:~~

$$EG = MP - MR$$

where:

~~EG = Equivalent Annual Growth in ERCs determined pursuant to (c) or (d) below~~

~~MP = Margin Reserve Period determined pursuant to subsection (4)~~

~~MR = Margin reserve expressed in ERCs~~

(b)(c) The equivalent annual growth in ERCs (EG) is measured in terms of the projected annual growth and shall be calculated in Schedules F-9 and F-10 of Form PSC/WAW 19 for Class A utilities and Form PSC/WAW 20 for Class B utilities, incorporated by reference in Rule 25-30.437.

(c)(d) The utility shall also submit a linear regression analysis using average ERCs for the last 5 years. The utility may submit other information that will affect growth in ERCs.

(6) As part of its application filed pursuant to Rule 25-30.437, the utility shall submit its most recent wastewater capacity analysis report, if any, filed with DEP.

(7) Contributions-in-aid-of-construction (CIAC) shall be imputed when a margin reserve is authorized. The amount of imputed CIAC shall be determined based on 50 percent of the number of ERCs included in the margin reserve period and the projected CIAC that will be collected from those ERCs. However, the imputed CIAC shall not exceed the rate base component associated with margin reserve.

Specific Authority 367.121 FS. Law Implemented 367.081 FS. History-New _____

REGIONAL PLANNING COUNCILS

Withlacoochee Regional Planning Council

RULE CHAPTER NO.: 29E-14
 RULE CHAPTER TITLE: Strategic Regional Policy Plan

RULE NO.: 29E-14.001
 RULE TITLE: Adoption

NOTICE OF CHANGE

Notice is hereby given that the following changes have been made to the proposed rule in accordance with subparagraph 120.54(3)(d)1., F.S., published in Vol. 23, No. 18, (May 2, 1997), issue of the Florida Administrative Weekly:

TEXT OF PROPOSED RULE CHANGES:

The Strategic Regional Policy Plan that is adopted and incorporated by reference, as previously noticed, has been changed by the addition of an Appendix H. That appendix contains the State Report of Findings and Recommendations dated September 5, 1995 and its Addendum dated April 8, 1997 as issued by the Executive Office of the Governor.

AGENCY FOR HEALTH CARE ADMINISTRATION

Board of Dentistry

RULE NO.: 59Q-2.014

RULE TITLE:
 Licensure Requirements for Applicants from Accredited Schools or Colleges

NOTICE OF CHANGE

The Board of Dentistry hereby gives notice of a change being made to the above-referenced rule in response to written comments received from the Joint Administrative Procedures Committee. The rule was originally published in Vol. 23, No. 20, of the May 16, 1997, issue of the Florida Administrative Weekly. The change is as follows:

The last sentence in subsection (2)(b) of the rule shall be deleted.

The person to be contacted regarding this rule is William Buckhalt, Executive Director, Board of Dentistry, 1940 North Monroe Street, Tallahassee, Florida 32399-0750.

AGENCY FOR HEALTH CARE ADMINISTRATION

Board of Dentistry

RULE NOS.: 59Q-2.0144
 59Q-2.0146

RULE TITLES:
 Licensure Requirements for Dental Hygiene Applicants from Unaccredited Dental Schools or Colleges
 Licensure Requirements for Applicants from Non-Accredited Schools or Colleges

NOTICE OF CHANGE

The Board of Dentistry hereby gives notice of changes being made to the above-referenced rules in response to written comments received from the Joint Administrative Procedures Committee. The rules were originally published in Vol. 23, No. 15, of the April 11, 1997, issue of the Florida Administrative Weekly. The changes are as follows:

1. In Rule 59Q-2.0144(5), the last sentence shall read, "Proof of the 5 years of required education shall include a report from an American Association of Dental Schools (AADS) approved evaluating service which evaluation includes a year by year evaluation of the applicant's credentials."

2. In Rule 59Q-2.0146(2), the first sentence shall read, "Prior to issuance of a license, the applicant shall submit proof of having successfully completed a Board-approved course on human immuno-deficiency virus and acquired immune deficiency syndrome, as set forth in Rule 59Q-12.019, F.A.C."

3. In subsection (2) of 59Q-2.0146, the word "may" shall be changed to "shall."

The person to be contacted regarding these rules is William Buckhalt, Executive Director, Board of Dentistry, 1940 North Monroe Street, Tallahassee, Florida 32399-0750.