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RECORDS AND REPORTING

STATE OF FLORIDA
OFFICE OF THE PUBLIC COUNSEL

c/o The Florida Legislature
111 West Madison St.
Room 812
Tallahassee, Florida 32399-1400
850-488-9330

JACK SHREVE
PUBLIC COUNSEL

January 25, 1999

Blanca S. Bayo, Director
Division of Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

Re: Case No. 960444-WU

Dear Ms. Bayo:

Enclosed for filing in the above-referenced docket are original and 15 copies of the Direct Testimony of Hugh Larkin, Jr. , witness for the Citizens of the State of Florida.

Please indicate the time and date of receipt on the enclosed duplicate of this letter and return it to our office.

Sincerely,

Harold McLean
Associate Public Counsel

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for rate increase and for increase in service availability charges in Lake County by Lake Utility Services, Inc.	Docket No. 960444-WU

DIRECT TESTIMONY OF
HUGH LARKIN, JR.
On Behalf of the Citizens of the State of Florida

Jack Shreve
Public Counsel
Office of Public Counsel
c/o the Florida Legislature
111 West Madison Street
Room 801
Tallahassee, FL 32399-1400
(850) 488-9330

DIRECT TESTIMONY OF HUGH LARKIN, JR.
ON BEHALF OF THE CITIZENS OF FLORIDA
BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION
DOCKET NO. 960444-WU

INTRODUCTION

Q. WHAT IS YOUR NAME, OCCUPATION AND BUSINESS ADDRESS?

A. My name is Hugh Larkin, Jr. I am a Certified Public Accountant licensed in the States of Michigan and Florida and the senior partner in the firm Larkin & Associates, Certified Public Accountants, with offices at 15728 Farmington Road, Livonia, Michigan 48154.

Q. HAVE YOU PREVIOUSLY FILED TESTIMONY IN THIS DOCKET?

A. Yes. I originally filed direct testimony in response to Lake Utility Services, Inc.'s ("LUSI") protest of the original Proposed Agency Action ("PAA"). The Proposed Agency Action was dated May 9, 1997. I subsequently filed rebuttal testimony to the Staff's testimony supporting the PAA issued May 18, 1998, which proposed a settlement between the Staff of the Florida Public Service Commission and Lake Utility Services, Inc.

Q. WHY DID YOU NOT SUPPORT THE SETTLEMENT REACHED BY THE STAFF OF THE FLORIDA PUBLIC SERVICE COMMISSION AND LAKE UTILITY SERVICES, INC., AS APPROVED BY THE COMMISSION IN THE PROPOSED AGENCY ACTION?

A. The settlement adopted in the Proposed Agency Action of May 18, 1998 results in a rate increase which was less than the Company's original request and more than the amount included in the Company's protest of the Proposed Agency Action dated May 9, 1997. Despite the fact that the rate increase is less than the amount originally requested, it still is not justified. The interim rates currently in effect have produced a return to the Company which is excessive. Thus, it is not appropriate for the Commission to approve the interim rates nor the revised proposed rates on a permanent basis. The approval of these excessive rates will result in Lake Utility Services, Inc. over-earning.

Q. WHY HAVE THE INTERIM RATES AND THE PROPOSED SETTLEMENT RATES RESULTED IN EXCESS EARNINGS TO LAKE UTILITY SERVICES, INC.?

A. It is clear that the test year used did not properly reflect the relationship between the investment of the Company and the revenues and expenses which would result from customer growth. The 1995 test year reflected the Company's investment in interconnecting the system which the Staff found to be 100% used and useful, and it also reflected the extension of the system to those areas south of the Clermont system that had become contaminated from citrus fumigant. However, the 1995 test year did not reflect the growth in customers which would be occasioned by this investment. Witness Wenz's testimony alludes to the growth which would be occasioned by the investment. On pages 4 and 5 of his direct testimony, he states:

> By interconnecting nearby systems, however, two or more wells can be combined to serve a greater number of customers in a reliable and efficient manner. This enables the utility not only to serve growth in existing areas in the most cost-effective manner possible, <u>but also provides a base to support</u>

extensions to serve nearby areas requiring service at a reasonable cost. This in turn has enabled developers to continue to develop new subdivisions in the desirable Clermont area. (Emphasis added)

As indicated in Mr. Wenz's testimony, the investment enabled the Utility to expand its service area and allowed developers to continue with new construction. However, the 1995 test year merely reflected the investment and allocated that investment to the average number of customers taking service during 1995.

Q. WHAT IMPACT WOULD THIS HAVE?

A. The effect of this would be to allocate all the fixed costs to the customers on-line in 1995 and none to those customers which subsequently were added to the system. Thus, since a major portion of the fixed costs would be recovered by allocation to customers receiving service during 1995, additional customer growth would add substantially to the profit of LUSI. The interconnection should never have been considered 100% used and useful.

Continuing on page 5 of his testimony, Mr. Wenz states:

> Second, DEP identified numerous residential well sites scattered throughout the area south of Clermont that had become contaminated from citrus fumigants.... By extending facilities to serve these residences, LUSI provided a safe, clean source of water and long-term solution to the contamination problem.

This investment was subsidized in part by the Department of Environmental

Protection, who provided funds to extend the utility system to those areas infected by citrus fumigants. This investment and the offsetting contributions in aid of construction provided by the Department of Environmental Protection was included in the 1995 rate base; however, the extent of customer growth did not occur in its entirety during that period of time. Customers were added subsequent to the extension of the Company's system to the contaminated area. Those customers provide additional revenues which serve to further the profitability of the Utility.

Q. DOES WITNESS WENZ ADDRESS CUSTOMER GROWTH FURTHER IN HIS TESTIMONY?

A. Yes. On page 5 of his direct testimony, Mr. Wenz confirms the growth resulting from the interconnection and the extension of the system as follows:

> Third, there was a need for a central water system to serve residences in areas around the subdivisions served by LUSI. Many of the residents are located along mains that LUSI had installed to serve new developments and residents with contaminated wells.

Clearly, the 1995 test year did not fully reflect the customer growth which was occasioned by the interconnection of the systems, the extension to adjacent areas and the extension of the system to those areas infected by citrus fumigants.

Q. WHY WAS A RATE CASE FILED USING THE 1995 TEST YEAR?

A. LUSI, in my opinion, realized that it was not appropriate to file for a rate increase. Rather, LUSI was requested to do so by the Staff. Mr. Wenz states in his testimony, at page 6, "Although LUSI wanted to postpone any rate proceeding until its interconnection project was complete, LUSI acquiesed to the Staff's request and filed an application for a limited proceeding to restructure rates on February 27, 1995 in order to make the monthly rates uniform for these systems."

The PAA Order in the limited proceeding to restructure rates was issued October 5, 1995. The Utility protested that Order and a settlement was reached with the Staff under which a rate case would be filed June 1, 1996. Mr. Wenz states in his testimony: "The Staff calculated uniform rates which would be implemented on the same date that interim rates became effective in the new rate case and would be used as the base from which to make interim rate calculations."

Q. ARE THE RESULTING INTERIM RATES APPROPRIATE?

A. No. It is those interim rates which are currently in effect and which result in over-earnings for Lake Utility Services, Inc. The test year, as I have previously stated, does not reflect customer growth which was occasioned by the interconnection and the extension of the systems, but it does reflect the investment. The test year utilized is, thus, inappropriate and not representative. That is, it does not reflect the purpose for which test years are adopted. A "test year" is the information base for constructing the "test period" which is intended to represent the period new rates will be in effect. In this instance, the adoption of a 1995 test year was inappropriate. It was not representative of the period new rates would be in effect. It was only representative of the investment that the utility would make. It did not adequately represent the level of customers that would utilize that investment. Thus, the test year is flawed.

The Company's protest and the settlement between the Company and the Staff of individual numbers related to rate base, depreciation, etc., cannot correct for the flaw in the test period adopted. Deciding what is the appropriate amount of rate base and the associated depreciation expense will not compensate for the deficiency in the test year; i.e., it does not reflect the appropriate level of customer growth. LUSI is willing to adopted those adjustments proposed by the Staff, because even under the Staff's lower rate base, the Company will still continue to over-earn.

Q. ARE YOU FAMILIAR WITH ANY LEGAL PRECEDENT IN THE STATE OF FLORIDA RELATED TO THE ADEQUACY OF A TEST YEAR?

A. Yes, I am. The Supreme Court of Florida Decision No. 43245, dated January 30, 1974, involving GULF POWER COMPANY, a corporation, petitioner, v. William H. BEVIS et.al., Respondents included the following quote from the Commission:

> In regulatory rate making, it is customary to select a test year or period for the purpose of testing the revenue requirements of the utility under consideration. The judicial decisions on the subject of the appropriate test year in a utility rate case uniformly adhere to the rule that the test period should be based on the utility's most recent actual experience With such adjustments as will make the test period reflect typical conditions in the immediate future. <u>The propriety or impropriety of a test year depends upon how well it accomplishes the objective of determining a fair rate of return in the future.</u> Thus, the realistic approach to this issue, since rates are fixed for the future and not for the past, is to use the most recently available data for a 12-months' period, Adjusted for known changes which will occur with in a reasonable time after the end of said period so as to fairly represent the future period for which the

rates are being fixed. (Emphasis added.)

In this opinion, the Supreme Court of Florida recognized that the purpose of a test year was to accomplish the objective of determining a fair rate of return in the future. Thus, if it is clear that the results of the test year do not meet the objective of setting rates that will result in a fair rate of return for the future, the test year is flawed.

The 1995 test year in the current case was a transitional year in which the Staff's audit of the Company's books and records discovered substantial overstatements of the plant accounts. Furthermore, the additional investment interconnecting the systems and an extension of the system to those area contaminated by citrus fumigants changed the dynamics of both the growth of the system and the operating expenses necessary to serve that growth. By adoption of a test year which did not clearly reflect these dynamic changes, the relationship between the investment, revenues, expenses and growth were not appropriately set for the determination of a fair rate of return in the future. The PAA issued May 18, 1998 supporting the Settlement reached by the Staff of the Florida Public Service Commission and Lake Utility Services, Inc. merely continues to tinker with a test year which has proven to be inappropriate. It does not address the basic problem of the inappropriate mismatch of investment, revenues and expenses.

Q. DID THE SUPREME COURT FURTHER ADDRESS THE ISSUE IN ITS DECISION?

A. Yes. In the same Supreme Court Opinion, which I have previously referenced, the Supreme Court took exception to the Florida Public Service Commission's blind adherence to test year rules when it was apparent that the rules would not result in the appropriate rate of return for future periods. The Court stated:

> The law is a tool of justice, not a goddess to be worshiped. When the Commission later took the position that test-period adjustments must recognize Only those changes which take place precisely within ninety days after the end of the test year, it lost sight of this basic objective of the "tool" it was using as a "test period" to arrive at a fair, "typical" result. For it is a correct Result which is the goal of the determination and not merely the Means or formula used in arriving at the answer. The blind application of such a time limitation is grossly arbitrary and completely ignores the purpose of the rule and the basic reason for test-year adjustments. These are used simply because it is unwieldy and cumbersome to try to apply a total and unending time.

We are faced in the instant case with the same situation. By reviewing subsequent periods, it is clear that the 1995 test year was not, and is not, the appropriate basis upon which to determine a fair rate of return in the future. It therefore should be abandoned.

Q. HAVE YOU PERFORMED AN ANALYSIS OF THE COMPANY'S GROWTH IN RECENT YEARS?

A. Yes, I have. Schedule 1, of Exhibit ____(HL-1) shows the increase in the Company's water system meter equivalents, by year, from 1994 through 1997. As shown on the Schedule, the growth rate by year has been in the 26% to 28% range. In other words, the number of equivalent meters has grown each year by over a quarter. This is phenomenal growth for any utility, and particularly for a small water company. Schedule 2 shows the Company's year-end rate base for the same years, 1994 through 1997, as taken from the Company's Annual Reports. The years following 1995 show minor growth in the rate base. There was a 3.8% growth rate in 1996 and a 6.2% growth rate in 1997. These rate base increases are minor when compared to the over 25% growth in meters which would fairly represent the growth in customers. I will note that I have also provided the rate base for 1994 in Schedule 2 but not have computed the percentage decrease in rate base between 1994 and 1995. This change (1994 vs. 1995 rate base) represents the decrease occasioned by the Staff audit which eliminated those items on the Company's books which could not be verified as investment. Clearly, when using a 1995 test year which reflected only the average number of customers for that period, but essentially reflected almost all of the investment of the utility, a mismatch was created. This mismatch will result in rates which will yield an excessive rate of return to the LUSI. It is, therefore, appropriate for the Commission to set aside the 1995 test year and proceed with a new test period which reflects the current status of customer growth and investment of the utility.

Q. IN YOUR REBUTTAL TESTIMONY TO THE STAFF'S TESTIMONY SUPPORTING THE PROPOSED AGENCY ACTION, DATED MAY 18, 1998, YOU ANALYZED THE RATES OF RETURN EARNED BY THE COMPANY UNDER VARIOUS SCENARIOS. IS THAT CORRECT?

A. Yes it is.

Q. WHAT DID YOUR ANALYSIS INDICATE?

A. My analysis indicated that the Company would over-earn based on the rates currently in effect and would also over-earn under the rates which were in effect prior to Docket No. 960444-WU.

Q. WOULD YOU PLEASE DISCUSS THE CALCULATIONS WHICH YOU PREVIOUSLY SUBMITTED?

A. Yes I will. On Schedule 3, 4 and 5, attached, I have included the same calculations that I previously submitted. These are the same as the schedules I filed August 13, 1998, with the exception of a correction.

Q. WHAT IS THE CORRECTION?

A. In the original schedules, I inappropriately used a 5% state income tax rate rather than the actual state income tax rate of 5.5%. Other than that change, the calculations are the same.

Q. WOULD YOU PLEASE DISCUSS SCHEDULE 3 OF EXHIBIT__(HL-1)?

A. Schedule 3 of Exhibit__(HL-1) shows the earnings of the Company for the year ended December 31, 1997 based on the interim rates currently in effect. The income statement is shown on lines 1 through 8 and is the same as that shown in the Company's annual report, with the exception of the tax calculation. The Company's tax calculation erroneously used a 34% federal income tax rate instead of the stand alone federal income tax rate. It is the policy of the Florida Public Service Commission to use the stand alone tax rate when calculating taxes for a utility that is part of a larger holding company.

The net income of the Company, using the appropriate tax rate, should be $97,582, as shown on line 8 of Schedule 3. This results in an overall rate of return of 15.18%. I have calculated the achieved return on equity on lines 22 through 26 of Schedule 3. Deducting from the overall rate of return the weighted cost of debt leaves a weighted cost of equity of 10.01%. The equity component of the capital structure is 43.50%, which would result in an achieved return on equity of 23.01% (10.01% / 43.50%). This return on equity of 23.01% is significantly higher than the rate of return found appropriate in the 1998 PAA of 11.61% and significantly higher than the rate of return which would be appropriate under the current leverage graph of 8.57%.

Q. WHAT DOES SCHEDULE 4 SHOW?

A. Schedule 4 shows that using the average number of customers in 1997 to calculate the operating revenues and using the actual miscellaneous revenues which the Company received in 1997, the rate of return would be significantly higher than that calculated on Schedule 3.

Q. WHY IS IT APPROPRIATE TO ANNUALIZE REVENUES USING AVERAGE NUMBER OF CUSTOMERS FROM 1997 RATHER THAN USING THE COMPANY'S ACTUAL REPORTED REVENUES?

A. The average number of customers for 1997 will be available for generating revenues for the Company in all future years. It is appropriate to annualize revenues on that basis in order to project what the Company might receive in returns in future periods. The calculation does not include any growth in the number of customers for 1998 or any future period, nor does it include any increased investment or expenses. However, it is a good gauge of what will happen in future periods. The calculation indicates that the Company would achieve a 35.81% return on equity based on the average number of customers receiving service during 1997. This is an indication that the interim rates are generation revenues from in excess of what the utility needs to achieve a fair rate of return.

Q. DO YOU HAVE CONCERNS ABOUT THE REVENUES REPORTED IN THE COMPANY'S 1997 ANNUAL REPORT SUBMITTED TO THE PUBLIC SERVICE COMMISSION?

A. Yes. The Office of Public Counsel's staff and I were unable to calculate the revenue shown on the Company's annual report using the billing determinants provided by the Company. We have verbally requested an explanation, as has the Public Service Commission staff, but as yet have not received one.

Q. WHAT WOULD THE COMPANY HAVE RECEIVED AS A RATE OF RETURN HAD RATES NOT BEEN INCREASED IN DOCKET NO. 960444-WU?

A. That calculation is shown on Schedule 5. The Company would have received a return on equity of 15.41%. This is clearly higher than what was required by the leverage graph that was used in the PAA issued May 18, 1998 and higher than the leverage formula adopted in Docket No. 980006-WS issued July 6, 1998. The calculations on Schedule 5 are based on year end customers and the rates prior to Docket No. 960444-WU.

Q. HAVE YOU MADE AN ESTIMATE OF THE EARNED RATE OF RETURN BASED ON 1998?

A. Yes, I have. I have made two analyses for 1998, both of which show that the

Company will earn substantially over the leverage formula return on equity currently in effect and that which was in effect in 1995.

Q. WOULD YOU PLEASE EXPLAIN YOUR ANALYSIS OF 1998 AND THE RETURNS WHICH YOU HAVE CALCULATED?

A. The first analysis of 1998 is shown on Schedule 6 of Exhibit____(HL-1). The operating revenues shown on that Schedule have been calculated based on an estimate of bills provided by the Company and gallonage usage provided by the Company. The rate applied to the bills for the base facilities charge was $6.80 and a gallonage rate of $.84. This is the uniform rate approved prior to the interim rate currently in effect. To this calculation of metered revenue, I have added an estimate of miscellaneous revenue based on the actual received by the Company in 1997 of $10,275.

Q. HOW DID YOU DETERMINE THE OPERATING EXPENSES, DEPRECIATION AND TAXES OTHER THAN INCOME TAXES?

A. The Company has provided the Office of Public Counsel with the actual expenses through the six months ended June 30, 1998. I have doubled these expenses to annualize them for the entire year. I have excluded from that annualization the amortization of rate case expense. Rate case expense would not have been incurred had uniform rates approved in the settlement of Docket No. 950232-WU been placed into effect without the filing of Docket No. 960444-WU. I believe the Company should have known that those rates would have granted the utility more than a fair rate of return. Additionally, I have recalculated the income tax based on a stand alone basis and the tax that would be paid by LUSI under IRS Code Section 219.

Q. WHAT CAPITAL STRUCTURE IS THE EQUITY RATIO AND THE WEIGHTED COST OF DEBT BASED ON?

A. This information, again, was provided by the Company to the Office of Public Counsel and represents the capital structure at June 30, 1998. I have accepted that capital structure and the cost rate for long term debt for purposes of this calculation.

Q. WHAT CHANGES HAVE YOU MADE TO THE RATE BASE?

A. The Company, again, has provided the Office of Public Counsel with a schedule which shows the plant additions in 1998. I have accepted those additions and added them to the year-end rate base at December 31, 1997 to arrive at a rate base at year-end December 31, 1998. These plant additions are accepted without adjustment for used and useful or consideration of CIAC. All of the subsequent calculations are based on that rate base and the capital structure provided by the Company.

Q. WHAT RATE OF RETURN DO YOU ESTIMATE THAT THE COMPANY WOULD EARN ON ITS EQUITY FOR 1998?

A. I have estimated that the Company would earn a return on equity of 22.57%. Clearly, well in excess of what would be required by the current or former leverage formula.

Q. PLEASE DISCUSS THE SECOND ANALYSIS OF 1998 WHICH YOU PERFORMED.

A. The second analysis is shown on Schedule 7. This analysis is based on information provided by the Company in an unadjusted trial balance. The revenue shown on line 1 of $852,428 is taken from that trial balance. The operating expenses were calculated in the same manner as I have previously discussed for Schedule 6. That is, the balance at June 30, 1998 was doubled in order to arrive at the level of operating expenses for the year. Depreciation expenses were calculated in the same manner. Taxes, other than income taxes, have been adjusted to reflect the higher level of revenue shown on line 1.

Q. DID YOU CALCULATE THE RATE BASE FROM THE UNADJUSTED TRIAL BALANCE?

A. No, I did not. The unadjusted trial balance did not show an increase in the rate base and, therefore, to be conservative, I utilized the same rate base calculation utilized on Schedule 6, that is adding plant additions for 1998 to the year-end rate base for 1997. I recalculated the income taxes based on the capital structure provided by the Company at June 30, 1998 and have calculated the achieved rate of return based on the information provided. The rate of return on equity based on this estimate is 67.5%. As can be seen, this is far in excess of any leverage formula requirement.

Q. DO YOU THINK THIS ESTIMATE IS RELIABLE?

A. It seems that the Company's miscellaneous revenue as reported in the unadjusted trial balance is unusually high; it amounted to over $100,000. It would be unusual for a company to continuously have miscellaneous revenue of that amount. However, based on my estimate for 1998 using that level of revenue the Company would have a substantial return on equity. I would again reiterate that the Company would not be harmed if the Commission rolled back the rates to those prior to the interim rates which are currently in effect. The Commission could then adopt a new more representative test period on which to base future rates.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. As of this date, yes. However OPC is still awaiting certain material regarding an abandoned audit conducted by the staff. After OPC has the opportunity to examine these material, OPC may provide supplemental testimony limited to addressing that material.

CERTIFICATE OF SERVICE
DOCKET NO. 960444-WU

I HEREBY CERTIFY that a correct copy of the Rebuttal Testimony of Hugh Larkin, Jr. has been furnished by U.S. Mail or hand-delivery to the following party representatives on this 25th day of January, 1999.

Richard D. Melson
Hopping, Boyd, Green & Sams
123 South Calhoun Street
P.O. Box 6526
Tallahassee, FL 32314

Lake Utility Services, Inc.
200 Weathersfield Avenue
Altamonte Springs, FL 32714-4027

Tim Vaccaro
Division of Legal Services
Fla. Public Service Commission
2740 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

Harold McLean

Lake Utility Services, Inc.
Water System Meter Equivalents by Year
- 1994 through 1997

Docket No. 960444-WU
Exhibit__(HL-1)
Schedule 1
Witness Hugh Larkin, Jr.

Line No.	Description	Dec. 31, 1997	Dec. 31, 1996	Dec. 31, 1995	Dec. 31, 1994
1	Amber Hill	47.5	44.5	40.0	34.0
2	Clermont I	134.5	130.5	121.5	116.5
3	Clermont II	43.0	43.0	41.0	41.0
4	Crescent Bay, et.al.	990.5	696.5	487.5	351.5
5	Four Lakes	57.0	55.0	52.0	48.0
6	Lake Ridge Club	89.0	82.0	72.0	48.0
7	Lake Saunders	40.0	38.0	37.0	35.0
8	The Oranges	93.0	88.0	78.0	74.0
9	The Vistas	94.5	66.5	41.5	22.5
10	Total Meter Equivalents	1,589.0	1,244.0	970.5	770.5
11	Percentage Increase	27.7%	28.2%	26.0%	

Source: Annual Report

Lake Utility Services, Inc.
Year End Rate Base
- 1994 through 1997

Docket No. 960444-WU
Exhibit__(HL-1)
Schedule 2
Witness Hugh Larkin, Jr.

Line No.	Description	Dec. 31, 1997	Dec. 31, 1996	Dec. 31, 1995	Dec. 31, 1994
1	Utility Plant in Service	$2,756,793	$2,195,669	$1,809,483	$1,902,290
2	Accumulated Depreciation	(274,883)	(217,460)	(154,993)	(109,024)
3	Accumulated Amortization of Plant	(12,946)	(10,541)	(8,136)	0
4	CIAC	(2,022,629)	(1,555,180)	(1,155,178)	(829,859)
5	Accumulated Amortization of CIAC	202,376	158,702	126,729	92,130
6	Advances for Construction	(38,400)	0	0	0
7	Net Acquisition Adjustments (A)	0	0	(61,987)	(64,162)
8	Working Capital Allowance	32,559	34,224	27,371	21,623
9	Total Rate Base	$642,870	$605,414	$583,289	$1,012,998
10	Percentage Increase	6.2%	3.8%		

(A) Only includes the Acquisition Adjustments approved by the Commission.

Source: Annual Report

Lake Utility Services, Inc.
Earned Rate of Return Rates per Annual Report Form PSC 5
Year End Rate Base
December 31, 1997

Docket No. 960444-WU
Exhibit ___ (HL-1)
Schedule 3
Witness Hugh Larkin Jr.

Line No.	Description	Amount
	Income Statement	
1	Operating Revenues	$474,822
2	Operating Expenses	260,474
3	Depreciation Expense	35,497
4	Taxes Other Than Income	61,577
5	Operating Expenses Before Income Tax	$357,548
6	Operating Income Before Income Tax	117,274
7	Income Tax (Line 38)	19,692
8	Net Income	$97,582
	Year End Rate Base	
9	Utility Plant in Service	$2,756,793
10	Accumulated Depreciation	(274,883)
11	Accumulated Amortization of Plant	(12,946)
12	C.I.A.C.	(2,022,629)
13	Accumulated Amortization of C.I.A.C.	202,376
14	Advances for Construction	(38,400)
15	Working Capital Allowance	32,559
16	Total Rate Base	$642,870
	Earned Rate of Return	
17	Net Income Before Income Tax	$117,274
18	Income Tax	19,692
19	Net Income (Line 8)	$97,582
20	Rate Base (Line 16)	642,870
21	Overall Rate of Return	15.18%
22	Overall Rate of Return	15.18%
23	Less Weighted Cost of Debt	5.17%
24	Weighted Cost of Equity	10.01%
25	Equity Ratio	43.50%
26	Achieved Return on Equity	23.01%
	Tax Calculation	
27	Rate Base	$642,870
28	Weighted Cost of Debt	5.17%
29	Interest Expense	$33,236
30	Operating Income Before Income Tax	$117,274
31	Less Interest Expense	(33,236)
32	Taxable Income	$84,038
33	State Income Tax (5.5% of amount over $5,000)	4,347
34	Federal Taxable Income	$79,691
35	Effective Federal Income Tax Rate (Line 36 / Line 34)	19.26%
36	Federal Income Tax	$15,345 (1)
37	State Income Tax	4,347
38	Total Income Tax	$19,692

Note: (1) Federal Income Tax calculated using the Graduated Tax Rates for Corporations. IRS Code Section 219.
Calculation: $13,750 + (Line 34 - 75,000) * 34.00%

Lake Utility Services, Inc.
Earned Rate of Return Interim Rates
Year End Rate Base
December 31, 1997

Docket No. 960444-WU
Exhibit ___ (HL-1)
Schedule 4
Witness Hugh Larkin Jr.

Line No.	Description	Amount
	Income Statement	
1	Operating Revenues	$538,004
2	Operating Expenses	260,474
3	Depreciation Expense	35,497
4	Taxes Other Than Income	64,420
5	Operating Expenses Before Income Tax	$360,391
6	Operating Income Before Income Tax	177,613
7	Income Tax (Line 39)	44,233
8	Net Income	$133,380
	Year End Rate Base	
9	Utility Plant in Service	$2,756,793
10	Accumulated Depreciation	(274,883)
11	Accumulated Amortization of Plant	(12,946)
12	C.I.A.C.	(2,022,629)
13	Accumulated Amortization of C.I.A.C.	202,376
14	Advances for Construction	(38,400)
15	Working Capital Allowance	32,559
16	Total Rate Base	$642,870
	Earned Rate of Return	
17	Net Income Before Income Tax	$177,613
18	Income Tax	44,233
19	Net Income (Line 9)	$133,380
20	Rate Base (Line 17)	642,870
21	*Overall Rate of Return*	20.75%
22	Overall Rate of Return	20.75%
23	Less Weighted Cost of Debt	5.17%
24	Weighted Cost of Equity	15.58%
25	Equity Ratio	43.50%
26	Achieved Return on Equity	35.81%
	Tax Calculation	
27	Rate Base	$642,870
28	Weighted Cost of Debt	5.17%
29	Interest Expense	$33,236
30	Operating Income Before Income Tax	$177,613
31	Less Interest Expense	(33,236)
32	Taxable Income	$144,377
33	State Income Tax (5.5% of amount over $5,000)	7,666
34	Federal Taxable Income	$136,711
35	Effective Federal Income Tax Rate (Line 36 / Line 34)	26.75%
36	Federal Income Tax	$36,567 (1)
37	State Income Tax	7,666
38	Total Income Tax	$44,233

Note: (1) Federal Income Tax calculated using the Graduated Tax Rates for Corporations. IRS Code Section 219.
Calculation: $22,250 + (Line 34 - 100,000) * 39.00%

Lake Utility Services, Inc.
Earned Rate of Return Rates Prior to Docket 960444-WU
Year End Rate Base
December 31, 1997

Docket No. 960444-WU
Exhibit ___ (HL-1)
Schedule 5
Witness Hugh Larkin Jr.

Line No.	Description	Amount
	Income Statement	
1	Operating Revenues	$442,685
2	Operating Expenses	260,474
3	Depreciation Expense	35,497
4	Taxes Other Than Income	60,131
5	Operating Expenses Before Income Tax	$356,102
6	Operating Income Before Income Tax	86,583
7	Income Tax (Line 38)	10,262
8	Net Income	$76,321
	Year End Rate Base	
9	Utility Plant in Service	$2,756,793
10	Accumulated Depreciation	(274,883)
11	Accumulated Amortization of Plant	(12,946)
12	C.I.A.C.	(2,022,629)
13	Accumulated Amortization of C.I.A.C.	202,376
14	Advances for Construction	(38,400)
15	Working Capital Allowance	32,559
16	Total Rate Base	$642,870
	Earned Rate of Return	
17	Net Income Before Income Tax	$86,583
18	Income Tax	10,262
19	Net Income (Line 8)	$76,321
20	Rate Base (Line 16)	642,870
21	Overall Rate of Return	11.87%
22	Overall Rate of Return	11.87%
23	Less Weighted Cost of Debt	5.17%
24	Weighted Cost of Equity	6.70%
25	Equity Ratio	43.50%
26	Achieved Return on Equity	15.41%
	Tax Calculation	
27	Rate Base	$642,870
28	Weighted Cost of Debt	5.17%
29	Interest Expense	$33,236
30	Operating Income Before Income Tax	$86,583
31	Less Interest Expense	(33,236)
32	Taxable Income	$53,347
33	State Income Tax (5.5% amount over $5,000)	2,659
34	Federal Taxable Income	$50,688
35	Federal Income Tax Rate	15.00%
36	Federal Income Tax	$7,603
37	State Income Tax	2,659
38	Total Income Tax	$10,262

Lake Utility Services, Inc.
Earned Rate of Return based on estimated 1998
Year End Rate Base
December 31, 1998

Docket No. 960444-WU
Exhibit ___ (HL-1)
Schedule 6
Witness Hugh Larkin Jr.

Line No.	Description	Amount
	Income Statement	
1	Operating Revenues	$577,172
2	Operating Expenses	312,406
3	Depreciation Expense	29,736
4	Taxes Other Than Income	51,341
5	Operating Expenses Before Income Tax	$393,483
6	Operating Income Before Income Tax	183,689
7	Income Tax (Line 40)	44,945
8	Net Income	$138,744
	Year End Rate Base	
9	Utility Plant in Service	$2,756,793
10	Accumulated Depreciation	(274,883)
11	Accumulated Amortization of Plant	(12,946)
12	C.I.A.C.	(2,022,629)
13	Accumulated Amortization of C.I.A.C.	202,376
14	Advances for Construction	(38,400)
15	Working Capital Allowance	32,559
16	Total Rate Base - 12/31/97	642,870
17	1998 Plant Additions	234,289
18	Total Rate Base - 12/31/98	$877,159
	Earned Rate of Return	
19	Net Income Before Income Tax	$183,689
20	Income Tax	44,945
21	Net Income (Line 8)	$138,744
22	Rate Base (Line 18)	877,159
23	Overall Rate of Return	15.70%
24	Overall Rate of Return	15.70%
25	Less Weighted Cost of Debt	4.29%
26	Weighted Cost of Equity	11.41%
27	Equity Ratio	50.55%
28	Achieved Return on Equity	22.57%
	Tax Calculation	
29	Rate Base	$877,159
30	Weighted Cost of Debt	4.29%
31	Interest Expense	$37,630
32	Operating Income Before Income Tax	$183,689
33	Less Interest Expense	(37,630)
34	Taxable Income	$146,059
35	State Income Tax (5.5% amount over $5,000)	7,758
36	Federal Taxable Income	$138,301
37	Effective Federal Income Tax Rate (Line 38 / Line 36)	26.89%
38	Federal Income Tax	$37,187 (1)
39	State Income Tax	7,758
40	Total Income Tax	$44,945

Note: (1) Federal Income Tax calculated using the Graduated Tax Rates for Corporations. IRS Code Section 219.
Calculation: $22,250 + (Line 36 - 100,000) * 39.00%

Lake Utility Services, Inc.
Earned Rate of Return based on estimated 1998
Year End Rate Base
December 31, 1998

Docket No. 960444-WU
Exhibit ___ (HL-1)
Schedule 7
Witness Hugh Larkin Jr.

Line No.	Description	Amount
	Income Statement	
1	Operating Revenues (1)	$852,428
2	Operating Expenses	312,406
3	Depreciation Expense	29,736
4	Taxes Other Than Income	63,728
5	Operating Expenses Before Income Tax	$405,870
6	Operating Income Before Income Tax	446,558
7	Income Tax (Line 40)	150,793
8	Net Income	$295,765
	Year End Rate Base	
9	Utility Plant in Service	$2,756,793
10	Accumulated Depreciation	(274,883)
11	Accumulated Amortization of Plant	(12,946)
12	C.I.A.C.	(2,022,629)
13	Accumulated Amortization of C.I.A.C.	202,376
14	Advances for Construction	(38,400)
15	Working Capital Allowance	32,559
16	Total Rate Base - 12/31/97	642,870
17	1998 Plant Additions	234,289
18	Total Rate Base - 12/31/98	$877,159
	Earned Rate of Return	
19	Net Income Before Income Tax	$446,558
20	Income Tax	150,793
21	Net Income (Line 8)	$295,765
22	Rate Base (Line 18)	877,159
23	Overall Rate of Return	33.72%
24	Overall Rate of Return	33.72%
25	Less Weighted Cost of Debt	4.29%
26	Weighted Cost of Equity	29.43%
27	Equity Ratio	43.50%
28	Achieved Return on Equity	67.65%
	Tax Calculation	
29	Rate Base	$877,159
30	Weighted Cost of Debt	5.17%
31	Interest Expense	$45,349
32	Operating Income Before Income Tax	$446,558
33	Less Interest Expense	(45,349)
34	Taxable Income	$401,209
35	State Income Tax (5.5% amount over $5,000)	21,791
36	Federal Taxable Income	$379,417
37	Effective Federal Income Tax Rate (Line 38 / Line 36)	34.00%
38	Federal Income Tax	$129,002 (2)
39	State Income Tax	21,791
40	Total Income Tax	$150,793

Note: (1) 1998 Unadjusted trial balance

(2) Federal Income Tax calculated using the Graduated Tax Rates for Corporations. IRS Code Section 219.
Calculation: $113,900 + (Line 36 - 335,000) * 34.00%