

State of Florida



Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: FEBRUARY 4, 1999

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYO)

FROM: DIVISION OF WATER AND WASTEWATER (JOHNSON, REDEMANN)
DIVISION OF LEGAL SERVICES (MCRAE)

RE: DOCKET NO. 981780-WS - APPLICATION FOR TRANSFER OF MAJORITY ORGANIZATIONAL CONTROL OF JASMINE LAKES UTILITIES CORPORATION, HOLDER OF CERTIFICATES NOS. 83-S AND 110-W IN PASCO COUNTY, FROM JAMES M. DREHER TO AQUASOURCE UTILITY, INC.

COUNTY: PASCO

AGENDA: FEBRUARY 16, 1999 - REGULAR AGENDA - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\WAW\WP\981780.RCM

Handwritten notes and signatures: "OK BSM", "JH", "RM", "AS", "BL". Vertical stamps: "RECORDS & REPORTING", "FEB 11 1999", "11:00 AM".

CASE BACKGROUND

Jasmine Lakes Utilities Corporation (JLUC or utility or Seller) is a Class B utility which provides water and wastewater services in Pasco County to 1,581 water and 1,569 wastewater customers. JLUC's service area is located in the Northern Tampa Bay Water-Use Caution Area as designated by the South Florida Water Management District. The annual report for 1997 shows that the operating revenue was \$448,471 and \$358,384 and the net operating income was \$37,849 and \$58,851, for the water and wastewater systems respectively. The utility's facilities consist of four systems: one water treatment plant, one water transmission and distribution system, one wastewater collection system and one wastewater treatment plant.

DOCUMENT NUMBER-DATE

01424 FEB-4 99

FPSC-RECORDS/REPORTING

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On December 1, 1998, AquaSource Utility, Inc. filed an application for approval of the transfer of majority organizational control (TMO) of Jasmine Lakes Utilities Corporation from James M. Dreher (Sellers) to AquaSource Utility, Inc. (Buyer). It is Commission practice not to establish rate base in TMO proceedings, and thus, rate base audits are not conducted in TMO cases. Rate base was established for this utility in Docket No. 920148-WS, Order No. PSC-93-1675-FOF-WS, issued November 18, 1993, as \$167,966 for water and \$438,860 for wastewater. According to the 1997 annual report, ratebase would be \$381,539 for water and \$583,527 for wastewater.

For informational purposes, the application contains a copy of the Stock Purchase Agreement which includes the purchase price, terms of payment, and a list of the assets purchased. According to the agreement, the purchase price is \$3,500,000, and it will be adjusted to reflect the value of Net Working Capital and other unknown assets or liabilities expenditures that may occur after the closing. The Buyer purchased the stock in a cash transaction.

JLUC closed on the transfer of majority organizational control of its facilities on January 4, 1999, prior to obtaining Commission approval. This will be discussed further in Issue 1. The following is staff's recommendation regarding the utility's request to transfer majority organizational control.

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DISCUSSION OF ISSUES

ISSUE 1: Should Jasmine Lakes Utilities Corporation be ordered to show cause, in writing within 21 days, why it should not be fined for its apparent violation of Section 367.071, Florida Statutes?

RECOMMENDATION: No. A show cause proceedings should not be initiated. (MCRAE)

STAFF ANALYSIS: As stated in the case background, JLUC closed on the transfer of majority organizational control of its facilities to AquaSource on January 4, 1999, prior to obtaining Commission approval. Section 367.071(1), Florida Statutes, states that:

No utility shall sell, assign, or transfer its certificate of authorization, facilities or any portion thereof..., without determination and approval of the commission that the proposed sale, assignment, or transfer is in the public interest...

Section 367.161(1), Florida Statutes, authorizes the Commission to assess a penalty of not more than \$5,000 for each offense, if a utility is found to have knowingly refused to comply with, or to have willfully violated any provision of Chapter 367, Florida Statutes. In closing on the transfer prior to Commission approval, the utility's act was "willful" in the sense intended by Section 367.161, Florida Statutes. In Order No. 24306, issued April 1, 1991, in Docket No. 890216-TL, titled In Re: Investigation Into The Proper Application of Rule 25-14.003, Florida Administrative Code, Relating To Tax Savings Refund For 1988 and 1989 For GTE Florida, Inc., the Commission having found that the company had not intended to violate the rule, nevertheless found it appropriate to order it to show cause why it should not be fined, stating that "[i]n our view, 'willful' implies an intent to do an act, and this is distinct from an intent to violate a statute or rule."

Although JLUC's failure to obtain Commission approval prior to transferring majority organizational control of its facilities to AquaSource is an apparent violation of Section 367.071(1), Florida Statutes, there are circumstances which appear to mitigate the utility's apparent violation. According to a letter from the utility dated January 25, 1999, JLUC and AquaSource needed to close on the sale of the utility as close to January 1, 1999, as possible to facilitate the regulatory reporting requirements and to

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eliminate any requirement to file bifurcated reports with the various regulatory agencies. Furthermore, there is a provision in the contract between JLUC and AquaSource which states that the sale is subject to this Commission's jurisdiction and if the application is denied by the Commission, the parties will "unwind" the transaction.

Staff does not believe that the apparent violation of Section 367.071, Florida Statutes, rises in these circumstances to the level which warrants the initiation of a show cause proceeding. Therefore, staff recommends that the Commission not order JLUC to show cause for failing to obtain Commission approval prior to transferring majority organizational control of its facilities to AquaSource.

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ISSUE 2: Should the transfer of majority organizational control of Jasmine Lakes Utilities Corporation to AquaSource Utility, Inc. be approved?

RECOMMENDATION: Yes, the transfer of majority organizational control should be approved. (JOHNSON)

STAFF ANALYSIS: As discussed in the case background, on December 1, 1998, AquaSource Utility, Inc. filed an application for transfer of majority organizational control of the Jasmine Lakes Utilities Corporation from James M. Dreher to AquaSource Utility, Inc. The application is in compliance with the governing statute, Section 367.071, Florida Statutes, and other pertinent statutes and Administrative Code Rules concerning an application for transfer of majority organizational control. The application contains a check in the amount of \$3,000, which is the correct filing fee pursuant to Rule 25-30.020, Florida Administrative Code. The applicant has provided evidence that the utility owns the land upon which the utility's facilities are located as required by Rule 25-30.037(3)(I), Florida Administrative Code.

In addition, the application contains proof of compliance with the noticing provisions set forth in Rule 25-30.030, Florida Administrative Code, including notice to the customers of the system to be transferred. No objections to the notice of application have been received and the time for filing such has expired. A description of the territory served by the utility is appended to this memorandum as Attachment A.

The application states that the transfer is in the public interest because the Buyer's business is operating water and wastewater utilities. According to the application, AquaSource Utility, Inc. has an excellent reputation with the Texas regulatory agencies, which is where most of its systems are located. The Buyer has the financial resources to make the future improvements to the utility systems as deemed necessary. Additionally, the application contains a statement that the Buyer will fulfill the commitments, obligations and representations of the Sellers with regard to utility matters. In contrast the Seller is no longer interested in continuing to own and operate the utility systems.

Regarding the Buyer's financial ability, it has provided the company's consolidated financial statement, along with additional information regarding the sources of annual income. AquaSource Utility, Inc. is a wholly-owned subsidiary of DQE, Inc. DQE is listed on the New York Stock Exchange and has a market value in

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excess of \$2 billion. All acquisitions are funded through direct capital contributions from DQE. DQE, Inc., the funded parent of Duquesne Light Company, has assets of more than \$4.6 billion and annual revenues in excess of \$1.2 billion. According to the Buyer, DQE currently intends to continue to make substantial investments in AquaSource with a goal of providing the company with the financial stability required to maintain its utility systems in accordance with Florida Public Service standards.

Regarding the Buyer's technical ability, AquaSource Utility, Inc. is a subsidiary of DQE, Inc. which, as of December 1, 1998, owned and operated water and wastewater systems serving approximately 125,000 customers. Although AquaSource is a relatively new organization, it has experienced staff who have been providing operation, maintenance and management services for municipal and private water utilities for more than 25 years. AquaSource is expanding its technical capabilities and implementing improved quality control, maintenance management, training and safety programs. These improvements provide direct tangible benefits to utilities owned and operated by AquaSource and municipal utilities served by AquaSource. In addition to 25 years of experience in operating water and wastewater utilities, AquaSource has the financial resources to ensure consistent compliance with environmental regulations.

According to our records, the utility is current on its regulatory assessment fees and has filed an annual report for 1997 and all prior years. The 1998 annual report and the regulatory assessment fees will not be prorated and JLUC will be responsible for filing the utility's annual report and regulatory assessment fees for 1998. However, AquaSource Utility, Inc. will own JLUC and not Mr. James Dreher.

The application states that the Company's representative has performed a reasonable investigation of the Utility system. The plant facilities appear to be in satisfactory condition and in compliance with all applicable standards set by the Florida Department of Environmental Protection. Staff has contacted the DEP and learned that there are no outstanding notices of violation.

Based on the above, staff believes the transfer of majority organizational control of JLUC to AquaSource Utility, Inc. is in the public interest and therefore, it should be approved.

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Attachment A

Jasmine Lakes Utilities Corporation
Water and Wastewater Service Area
Pasco County

In Township 25 South, Range 16 East, Pasco County, Florida.

That portion of Sections 14, 15 and 16 being more particularly described as follows:

Commence at the Northwest corner of said Section 15; thence run South 0°14'40" West, a distance of 1680.03 feet; thence South 89°48'12" East, a distance of 24.08 feet for a Point of Beginning; thence continue South 89°48'12" East, a distance of 1284.63 feet; thence North 0°14'40" East, a distance of 334.62 feet; thence South 89°44'34" East, a distance of 1308.74 feet; thence South 89°54'36" East, a distance of 2623.16 feet; thence South 0°21'11" West, a distance of 1328.55 feet; thence South 89°43'05" East, a distance of 643.97 feet; thence South 03°16'30" West, a distance of 2641.28 feet; thence North 89°41'55" West, a distance of 475.00 feet; thence North 89°54'36" West, a distance of 2650.37 feet; thence North 0°15'00" East, a distance of 1645.51 feet; thence North 89°53'51" West, a distance of 2617.11 feet; thence North 89°45'23" West, a distance of 609.96 feet to the Easterly right-of-way line of U.S. #19 (SR #55); thence 2101.65 feet along said right-of-way line and along an arc of a curve to the left, said curve having a radius of 5803.87 feet and a chord of 2090.19 feet which bears North 17°54'00" East, to the Point of Beginning.

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ISSUE 3: Should rate base be established?

RECOMMENDATION: No, different ownership of stock does not affect the rate base balance. (JOHNSON)

STAFF ANALYSIS: It is Commission practice that rate base is not established in TMOG proceedings. The reason behind this approach is the philosophy that stock is publicly traded and has no regulatory relationship to rate base. Thus, different ownership of stock does not affect a utility's rate base balance. Consequently, stock purchase price and rate base are not considered in making a public interest determination of a TMOG. This same approach is followed even if the stock is privately held rather than publicly traded. The sale of the stock of JLUC from James Dreher to AquaSource Utility, Inc. will not alter the utility's asset and liability accounts. Accordingly, the transfer of stock ownership will not change the rate base balance. In consideration of the above, staff recommends that rate base not be established in this docket.

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ISSUE 4: Should an acquisition adjustment be approved?

RECOMMENDATION: No, an acquisition adjustment should not be included in the calculation of rate base for transfer purposes. (JOHNSON)

STAFF ANALYSIS: An acquisition adjustment results when the purchase price differs from the original cost calculation. The Commission routinely makes determinations regarding acquisition adjustments in cases involving the transfer of certificates, assets, or facilities because the purchase price is considered when determining whether the transfer is in the public interest. Conversely, it is Commission practice that acquisition adjustments are generally not considered in stock transfers because the price of stock has no regulatory relationship to a utility's established rate base.

Because the assets are not actually being sold and the value will remain the same after the transfer, staff believes that an acquisition adjustment does not result from this transfer. Therefore, staff recommends that an acquisition adjustment should not be included in the calculation of rate base.

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ISSUE 5: Should the rates and charges approved for this utility be continued?

RECOMMENDATION: Yes, the rates and charges approved for JLUC should be continued. Staff will approve the tariff filing reflecting the transfer of majority organizational control effective for services rendered or connections made on or after the stamped approval date. (JOHNSON)

STAFF ANALYSIS: The utility's approved water and wastewater rates were effective July 11, 1998, in a administrative price index proceeding.

Rule 25-9.044(1), Florida Administrative Code, provides that:

In case of change of ownership or control of a utility which places the operation under a different or new utility...the company which will thereafter operate the utility business must adopt and use the rates, classification and regulations of the former operating company (unless authorized to change by the Commission)...

The Buyer has not requested a change in the rates and charges of the utility and staff sees no reason to change them at this time. Accordingly, staff recommends that the utility continue operations under the existing tariff and apply the approved rates and charges. The utility has filed a revised tariff reflecting the change in issuing officer due to the transfer of majority organizational control. Staff will approve the tariff filing effective for services rendered or connections made on or after the stamped approval date.

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ISSUE 6: Should this docket be closed?

RECOMMENDATION: Yes, this docket should be closed. (MCRAE)

STAFF ANALYSIS: No further action is required in this docket. Therefore, staff recommends that this docket be closed.