

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for increase
in wastewater rates in Seven
Springs System in Pasco County
by Aloha Utilities, Inc.

DOCKET NO. 991643-SU
FILED: SEPTEMBER 5, 2000

COMMISSION STAFF'S PREHEARING STATEMENT

Pursuant to Order No. PSC-00-0872-PCO-SU, issued May 3, 2000,
as revised by Order No. PSC-00-1370-PCO-SU, issued July 31, 2000,
the Commission Staff (Staff) files its prehearing statement as
follows:

A. All Known Witnesses

Staff intends to call the following witnesses:

David G. MacColeman of the Department of Environmental
Protection. He will testify to the proposed modification and
expansion of the Aloha wastewater treatment plant and the utility's
infiltration and inflow reduction program.

Paul Stallcup of the Florida Public Service Commission
Division of Economic Regulation. He will testify to the
appropriate method of projecting customers and consumption for the
projected test year.

James A. McPherson of the Florida Public Service Commission
Division of Regulatory Oversight. He will testify to the staff
audit report.

Thomas E. Stambaugh of the Florida Public Service Commission
Division of Regulatory Oversight. He will testify to the staff
audit report.

Patricia Merchant of the Florida Public Service Commission
Division of Economic Regulation. She will testify to the utility's
projection of customer deposits and the appropriate amount to
include in the capital structure. She will also testify to rate
case expense and the proper reuse rate and revenues to be included
in the revenue requirement.

APP _____
CAF _____
CMP _____
COM 3 _____
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FPSC-RECORDS/REPORTING

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Staff also intends to call Stephen G. Watford, President of Aloha Utilities, Inc. (Aloha or utility), as an adverse party witness. Staff will question him on the availability of reuse customers.

B. All Known Exhibits

Staff has identified and intends to sponsor the following exhibits:

- PWS-1: Forecast of equivalent residential connections
- PWS-2: Test of forecast methodologies
- JAM-1: Audit Report dated July 14, 2000
- JAM-2: Audit calculation of deferred taxes
- JAM-3: Comparison of accounting for CIAC
- TES-1: Audit Report dated May 19, 2000
- PWM-1: Schedule of customer deposit projections
- PWM-2: DEP's 1999 reuse inventory report - Appendix H
- PWM-3: Staff's deficiency letter dated March 2, 2000 mailed to the utility
- PWM-4: Utility's response letter to Staff's deficiency letter
- PWM-5: Pages from Florida Public Utilities Company's minimum filing requirements and Staff's deficiency letter dated July 29, 1999 to Florida Public Utilities Company

Staff reserves the right to identify additional exhibits at the Prehearing Conference and at hearing for purposes of cross-examination.

C. Staff's Statement of Basic Position

The information gathered through discovery and prefiled testimony indicates, at this point, that the utility is entitled to some level of increase. The specific level cannot be determined until the evidence presented at hearing is analyzed.

D. Issues & Staff's Respective Positions

The following are issues identified by Staff and its positions on these issues. Testifying Staffs' positions are set forth in their respective testimonies. Non-testifying Staff's positions are preliminary, are based upon materials filed by the utility or obtained through discovery and are intended to inform the parties of Staff's preliminary positions. Staff's final positions will be based upon an analysis of the evidence presented at the hearing.

QUALITY OF SERVICE

ISSUE 1: Is the quality of service satisfactory?

POSITION: For testifying Staff, the utility is the subject of an enforcement action and is required to comply with the provisions contained in the Amended and Restated Consent Final Judgement (ARCFJ). (MacColeman) For non-testifying Staff, the quality of service will depend on the results of customer testimony at the hearing.

RATE BASE

ISSUE 2: Are the proposed modifications and expansion of the Aloha wastewater treatment plant prudent and justified?

POSITION: Yes. For non-testifying Staff, Staff's position is that the proposed modification and expansion are prudent. For testifying Staff, Staff's position is that the modifications and expansion of the Aloha wastewater treatment plant are required by the Florida Department of Environmental Protection in order to meet the Class I reliability standards necessary to provide properly treated effluent suitable for unrestricted access reuse

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and to meet additional capacity requirements.
(MacColeman)

ISSUE 3: Does Aloha have excessive infiltration and inflow (I&I)?

POSITION: For non-testifying Staff, Staff's position will depend upon further development of the record. For testifying Staff, Staff's position is that Aloha is experiencing I&I flows which, when added to seasonal peak flows, caused total flows to reach and sometimes exceed the capacity of the existing plant. Therefore, DEP ordered Aloha to take appropriate steps to further decrease its I&I flows.
(MacColeman)

ISSUE 4: Are the costs of the utility's infiltration and inflow reduction program prudent?

POSITION: For non-testifying Staff, yes. For testifying Staff, in an Amended and Restated Consent Final Judgement between DEP and Aloha, the utility is credited with additional flow by reducing inflow into the collection/transmission system or repairing sources of infiltration.
(MacColeman)

ISSUE 5: What are the appropriate adjustments for the accrual of allowance for funds used during construction for the wastewater treatment plant expansion from 1999 to 2000?

POSITION: Plant should be reduced by \$122,524 which reflects the appropriate Allowance for funds used during construction rate of 9.08%. Corresponding adjustments should also be made to reduce accumulated depreciation and depreciation expense. (Stambaugh)

ISSUE 6: Should the utility be allowed to capitalize invoices previously expensed?

POSITION: No. The capitalization of these previously expensed items would constitute double recovery and should be disallowed. Thus, the Seven Springs wastewater system's plant should be reduced by \$127,232 and accumulated

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depreciation should be reduced by \$76,548. Depreciation expense should also be reduced by \$6,675. (Stambaugh)

ISSUE 7: Is it appropriate to capitalize items expensed during the historical base year?

POSITION: Yes, the utility should capitalize the items that were erroneously expensed during the historical September 30, 1999 base year. Thus, the Seven Springs wastewater system's plant should be increased by \$11,616. Corresponding adjustments should also be made to increase accumulated depreciation and depreciation expense. (Stambaugh)

ISSUE 8: Should any adjustment be made to land?

POSITION: Yes. Seven Springs wastewater land should be reduced by \$12,120 and Aloha Gardens wastewater land should be increased by \$12,120. (Stambaugh)

ISSUE 9: What are the used and useful percentages of the wastewater treatment plant and the wastewater collection system?

POSITION: The wastewater treatment plant, collection lines and trunks, and associated maintenance costs should all be considered 100% used and useful.

ISSUE 10: Are any other adjustments necessary to test year accumulated depreciation and depreciation expense?

POSITION: Yes. For the base year ended September 30, 1999, the depreciation rate for computer equipment should be 16.67%. Adjustments should be made to correct the base, intermediate and projected test year accumulated depreciation and depreciation expense. (McPherson)

ISSUE 11: What is the appropriate test year CIAC and accumulated amortization of CIAC?

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POSITION: Adjustments may be necessary if the Commission changes the utility's projected customer growth rate or plant capacity charges.

ISSUE 12: What is the appropriate regulatory treatment of contributed taxes and accumulated deferred income taxes?

POSITION: Contributed taxes should be reflected as CIAC and included in rate base. The amortization of contributed taxes should be reflected as accumulated amortization of CIAC and also included in rate base. Used and useful debit deferred income taxes should be offset with used and useful credit deferred income taxes. Because the utility has a net debit balance, the net amount should be included as an addition to rate base. Credit deferred income taxes should be removed from the capital structure. (McPherson)

ISSUE 13: Should the cash operating account balance be removed from the working capital calculation?

POSITION: No. Either the interest bearing account should be excluded from the working capital calculation, or it should be included as long as the interest income from the account is included in above-the-line revenues.

ISSUE 14: Should income tax deposits be removed from the working capital calculation?

POSITION: Yes. Income tax deposits should be removed from the working capital calculation because the utility does not anticipate paying any income tax.

ISSUE 15: What is the appropriate working capital allowance?

POSITION: The appropriate amount is subject to the resolution of other issues.

ISSUE 16: What is the appropriate projected rate base?

POSITION: The appropriate amount is subject to the resolution of other issues.

COST OF CAPITAL

ISSUE 17: What is the appropriate return on equity?

POSITION: Based on the Commission approved equity ratio, the rate of return on equity should be calculated using the current leverage formula at the time of the Commission's vote on this matter. However, the appropriate equity ratio is subject to the resolution of other issues.

ISSUE 18: Should any adjustments be made to retained earnings and customer deposits to determine the overall cost of capital?

POSITION: Yes. Retained earnings should be reduced by \$172,806 because of an overstatement of the thirteen-month average balance by the utility. (McPherson) In addition, the final projected September 30, 2001 customer deposits balance should be \$438,412, resulting in a \$345,117 reduction in retained earnings. (Merchant)

ISSUE 19: What is the appropriate weighted average cost of capital for the projected test year ending September 30, 2001?

POSITION: The appropriate amount is subject to the resolution of other issues.

ISSUE 20: What is the appropriate prospective Allowance for funds Used During Construction rate for Aloha?

POSITION: The appropriate amount is subject to the resolution of other issues.

NET OPERATING INCOME

ISSUE 21: What is the appropriate method of projecting customers and consumption for the projected year ending September 30, 2001, and what changes, if any, are appropriate to the utility's projection factors?

POSITION: The appropriate method of projecting customers and consumption for the projected year ending September 30,

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2001 is an econometric model which incorporates changes in economic and/or demographic conditions to explain growth. The appropriate changes to be made to the utility's projection factors are that the utility's projection factor of 1.08535 should be changed to 1.07093, and the utility's projection factor of 1.04812 should be changed to 1.03486. (Stallcup)

ISSUE 22: What adjustments, if any, are necessary to the 2001 projected test year revenues and expenses to reflect the appropriate number of wastewater customers, bills, and consumption?

POSITION: Adjustments may be necessary if the Commission changes the utility's projected customer growth rate.

ISSUE 23: What is the appropriate amount of reuse revenue to include in the test year?

POSITION: The appropriate amount of test year reuse revenue is \$60,620. However, Staff's position may change pending further development of the record. (Merchant)

ISSUE 24: What is the appropriate salary for Aloha's vice-president?

POSITION: The vice-president's salary should be 20% of the president's salary. As a result, Salary & Wages - Officers, and Employee Benefits for the Seven Springs wastewater system should be reduced by \$15,507 and \$5,319, respectively. Payroll taxes should also be reduced by \$1,392. (Stambaugh)

ISSUE 25: Should the cost of the annual financial audit be allocated to all of the utility's systems?

POSITION: No position pending further development of the record.

ISSUE 26: Should any additional adjustments be made to Contractual Services - Accounting for non-recurring costs?

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POSITION: Accounting expenses for the Seven Springs wastewater system should be reduced by \$1,113 to remove non-recurring fees associated with the implementation of the new accounting software system. (McPherson)

ISSUE 27: Should any adjustments be made to transportation expenses?

POSITION: Yes. Non-utility charges recorded as transportation expenses should be disallowed. As such, transportation expenses should be reduced by \$280. The escalation for inflation that was applied to this account should also be removed. (McPherson)

ISSUE 28: Should expenses related to errors resulting from Aloha's computer system conversion be allocated to all of the utility's systems?

POSITION: Yes, material & supplies and chemical expenses for the Seven Springs wastewater system should both be reduced by \$1,087. The escalation factors for growth and inflation that were applied to these accounts should also be removed. (Stambaugh)

ISSUE 29: Should an adjustment be made to remove expenses associated with the settlement of the DEP enforcement action?

POSITION: Yes. Testifying Staff's position is that legal expenses associated with a DEP enforcement action are non-recurring and should be amortized over five years. As such, legal fees should be reduced by \$17,525. (Stambaugh) Non-testifying Staff's position is that miscellaneous expenses should be reduced by \$18,400 for the DEP settlement fee, which should be disallowed as a payment of a non-utility penalty. The escalation factors for growth or inflation that were applied to the settlement fee should also be removed.

ISSUE 30: Is an adjustment necessary to chemicals and purchased power expenses as a result of the utility's infiltration and inflow reduction program?

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POSITION: No position pending further development of the record.

ISSUE 31: What is the appropriate amount of current rate case expense?

POSITION: Rate case expense of \$31,739 associated with the utility's emergency variance petition and its MFRs deficiencies should be disallowed. The final amount is subject to further development of the record. However, only prudently incurred rate case expense should be allowed and amortized over four years. (Merchant)

ISSUE 32: Should the utility be allowed to recover excess rate case expense not approved by the Commission in Order No. PSC-97-0280-FOF-WS?

POSITION: No. In 1999, the utility expensed \$31,401 of rate case expense over and above what the Commission allowed in Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, in Dockets Nos. 970536-WS and 980245-WS. This amount should be expensed below-the-line. (Stambaugh)

ISSUE 33: What is the appropriate amortization period of contributed taxes associated with the Seven Springs wastewater system?

POSITION: Contributed taxes should be amortized over 26.9 years which results in annual amortization of \$57,430. This is a reduction to expenses of \$18,808.

ISSUE 34: What is the appropriate millage rate to project tangible personal property taxes?

POSITION: The effective millage rate of 1.93677 is appropriate to project tangible personal property taxes. As a result, the utility's intermediate and final test year balances should be reduced by \$22,564 and \$23,819, respectively. (Stambaugh)

ISSUE 35: What is the test year operating income before any revenue increase?

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POSITION: The appropriate amount is subject to the resolution of other issues.

REVENUE REQUIREMENT

ISSUE 36: What is the appropriate revenue requirement?

POSITION: The appropriate amount is subject to the resolution of other issues.

ISSUE 37: Should any of the revenue requirement approved in this docket be allocated to the utility's water customers?

POSITION: No. Consistent with Order No. PSC-97-0280-FOF-WS, it is not appropriate to raise water rates by shifting a portion of reuse costs to the water customers until the utility adequately addresses the water quality concerns. (Merchant)

RATES

ISSUE 38: What are the appropriate final wastewater rates?

POSITION: The final wastewater rates are subject to the resolution of other issues.

ISSUE 39: Should the Commission determine a reuse rate in this proceeding, and if so, what is the appropriate rate?

POSITION: Yes, the utility's current reuse rate of \$0.25 per thousand gallons should be increased to \$0.32 per thousand gallons. (Merchant)

ISSUE 40: Who should bear the risk that the company will not find buyers for its reclaimed water?

POSITION: The utility should bear the risk that it will not find buyers for its reclaimed water. (Merchant)

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ISSUE 41: Should the three-step rate reduction required by Order No. PSC-97-0280-FOF-WS be implemented, modified, or canceled?

POSITION: The three-step rate reduction should not be implemented. The Commission should monitor Aloha's reuse revenue and customers by requiring the utility to submit additional information in its annual report. This information should include the name of each non-residential reuse customer, number of gallons of reuse sold and the revenue collected for the year. For residential reuse service, Aloha should provide the number of residential customers by development, the numbers of gallons sold (if metered) and the revenue collected for the year. (Merchant)

ISSUE 42: Should Aloha's Seven Springs wastewater plant capacity charge be revised?

POSITION: Yes. According to the historical September 30, 1999 balances, the Seven Springs wastewater system has a 61.82% CIAC ratio. Based on the utility's MFRs, the CIAC ratio is 46.31% for the projected intermediate test year and 44.42% for the projected final test year. Since this construction phase will increase the capacity of the plant to accommodate future growth, the current plant capacity charges should be increased. The appropriate amount of new plant capacity charges is subject to further development of the record.

ISSUE 43: Should the extension of the Mitchell agreement dated March 19, 1999 be approved?

POSITION: Yes, it is appropriate to approve this contract, although the utility failed to timely seek the approval pursuant to Order No. PSC-97-0280-FOF-WS. However, any further extension of the contract after this current term expires should be approved by the Commission before such an extension is executed. (Merchant)

LEGAL ISSUES

ISSUE 44: Should Aloha be ordered to show cause for its apparent violation of Order No. PSC-97-0280-FOF-WS by its failure

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to timely file the extension of the Mitchell agreement with the Commission for approval?

POSITION: Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, required any extension of the Mitchell contract to be filed with the Commission for approval. Although an extension agreement was entered into on March 19, 1999, the utility only submitted the agreement upon request of Staff on March 10, 2000. Therefore, in accordance with Section 367.161, Florida Statutes, the utility should be made to show cause in writing within 21 days why it should not be fined \$250 for its failure to timely submit the Mitchell contract for approval as required by the Order. (Factual basis - Merchant)

ISSUE 45: Should Aloha be ordered to show cause for its apparent violation of Order No. PSC-97-0280-FOF-WS by its failure to file sufficient information to enable the Commission to address reuse rates for all reuse customers and whether and how much of the reuse revenue requirement should be allocated to its water customers?

POSITION: Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, directed that the next rate case filing of the utility contain information sufficient to enable the Commission to address reuse rates for all reuse customers, and further ordered that the utility explore how much of the reuse revenue requirement should be allocated to its water customers. Moreover, the Commission found that "until the utility adequately addresses . . . water quality concerns, we do not believe it is appropriate to raise water rates by shifting a portion of reuse water costs to the water customers." Because the utility is still addressing the water quality concerns, Staff believes that it is still too early to address allocating any portion of the reuse revenue requirement to the water customers. In addition, by its filing, the utility apparently thought the zero rate for the Mitchell property and the reuse rate of \$.25 for all other customers was still appropriate. Therefore, Staff does not believe that the utility should be made to show cause for its apparent failure to file the directed information in violation of the Order. (Factual basis - Merchant)

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ISSUE 46: Should this docket be closed?

POSITION: If the Commission's final order is not appealed, this docket should be closed upon the expiration of the time for filing an appeal.

E. Stipulated Issues

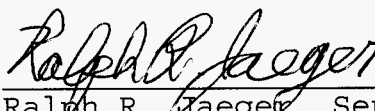
There are no issues that have been stipulated at this time.

F. Pending Matters

There are no matters pending at this time.

G. Requirements That Cannot Be Complied With

There are no requirements of Orders Nos. PSC-00-0872-PCO-SU and PSC-00-1370-PCO-SU that cannot be complied with at this time.



Ralph R. Jaeger, Senior Attorney
FLORIDA PUBLIC SERVICE COMMISSION
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850
(850) 413-6199


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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the **COMMISSION STAFF'S PREHEARING STATEMENT** has been furnished to Steve Burgess, Esquire, Office of Public Counsel, c/o The Florida Legislature, 111 West Madison Street, Suite 812, Tallahassee, Florida 32399-1400 and to F. Marshall Deterding, Esquire, Rose, Sundstrom & Bentley, LLP, 2548 Blairstone Pines Drive, Tallahassee, Florida 32301 by regular U.S. Mail, this 5th day of September, 2000.



Ralph R. Jaeger, Senior Attorney

FLORIDA PUBLIC SERVICE COMMISSION
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850
(850) 413-6199