State of Florida

Public Service Commission

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

DATE: OCTOBER 26, 2000

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

FROM: DIVISION OF ECONOMIC REGULATION (RENDELL, WILLIS, KYLE, MERCHANT, WETHERINGTON, CROUCH, LINGO, D. DRAPER)
DIVISION OF LEGAL SERVICES (FUDGE, GERVASI)

RE: DOCKET NO. 940109-WU - PETITION FOR INTERIM AND PERMANENT RATE INCREASE IN FRANKLIN COUNTY BY ST. GEORGE ISLAND UTILITY COMPANY, LTD. d/b/a WATER MANAGEMENT SERVICES, INC.

DOCKET NO. 000694-WU - PETITION BY WATER MANAGEMENT SERVICES, INC. FOR LIMITED PROCEEDING TO INCREASE WATER RATES IN FRANKLIN COUNTY.
COUNTY: FRANKLIN

AGENDA: 11/7/2000 - REGULAR AGENDA - PROPOSED AGENCY ACTION, EXCEPT FOR ISSUES 1, 2, 11, AND 12 - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\ECR\WP\000694.RCM

CASE BACKGROUND

Water Management Services, Inc. (WMSI or utility) is a Class B water utility providing service to approximately 1,461 water customers in Franklin County. For the year ended December 31, 1999, the utility reported in its annual report operating revenues of $711,252 and utility operating income of $43,543. Water rates were last established for this utility by Order No. PSC-94-1383-FOF-WU, issued November 14, 1994, in Docket No. 940109-WU.

On January 31, 1994, the utility filed an application for approval of interim and permanent rate increases pursuant to Sections 367.081 and 367.082, Florida Statutes. The application was assigned Docket No. 940109-WU. On November 14, 1994, Order No. PSC-94-1383-FOF-WU was issued in Docket No. 940109-WU, approving a rate increase and revising the service availability charges.

In addition, to provide assurance that funds would be available for capital improvements, the Order required that an escrow account be established for service availability charges. The docket has remained open for staff to monitor the utility's collections and additions to the escrow account along with the disbursements from the escrow account.

On June 6, 2000, WMSI filed an application, pursuant to Section 367.0822, Florida Statutes, for a limited proceeding to increase its water rates to cover the cost of building a new water transmission main to connect its wells on the mainland to its service territory on St. George Island, which was assigned Docket No. 000694-WU. In its petition, the utility states that it has been notified by the Florida Department of Transportation (DOT) that the existing bridge to St. George Island, to which WMSI's water main is attached, is to be demolished and replaced by a new bridge with an expected in-service date of March, 2003. Upon completion of the new bridge, WMSI will have to make alternative arrangements to provide service to its certified service area. The utility's petition sets forth its plan to construct a new main to be attached to the new bridge, along with ancillary modifications to its system, and requests a limited proceeding to increase its rates in order to provide funding for the proposed construction.

On July 28, 2000, staff sent a data request to the utility, requesting additional data and clarification of certain items in the petition. On August 11, 2000, WMSI responded and, along with providing the requested information, made various changes to the supporting schedules included in the original petition.

Staff held a customer meeting at the Franklin County Courthouse in Apalachicola on September 12, 2000, in order to allow the utility's customers the opportunity to comment on WMSI's petition. More than 100 customers attended, and 13 customers made statements. In general, the speakers believed that the projected cost of the project was excessive and that the utility should have planned for this contingency in such a way as to avoid such a large rate increase. There was also great concern over the utility's ability to provide fire protection.

The Commission has jurisdiction pursuant to Sections 367.011(2) and 367.0822, Florida Statutes.

This recommendation addresses staff's recommended disposition of the escrow account and whether the utility is in compliance with Order No. PSC-94-1383-FOF-WU. This recommendation also addresses the utility's request for a limited proceeding.

DISCUSSION OF ISSUES

ISSUE 1: Should the funds in the escrow account be released to the utility and the escrow account closed?

RECOMMENDATION: Yes, the funds in the escrow account should be released to the utility and the escrow account should be closed. (RENDELL)

STAFF ANALYSIS: As stated previously, pursuant to Order No. PSC-94-1383-FOF-WU, issued November 14, 1994, the utility was required to establish a commercial escrow account for service availability charges.

According to the Order, the contribution-in-aid-of-construction (CIAC) level for the utility, as of December 31, 1993, was seventy-six percent of net plant in service. However, the Commission acknowledged that there was significant potential for growth on St. George Island. In an effort to prevent the utility from becoming seriously over-contributed, rather than eliminate the service availability charges altogether, the Commission reduced the plant capacity charge. The Commission recognized that, while there was growth potential, the utility would need additional capacity to connect new customers.

The Commission recognized that St. George, on occasion, had difficulty obtaining capital funds from outside sources, and that some assurance was needed that funds would be available when future capital improvements were deemed necessary. Therefore, to ensure that monies would be available for additional capacity or capital improvements, pursuant to the above-referenced Order, the utility was required to establish a commercial escrow account for service availability charges. The utility was further ordered to file a monthly report with the Commission detailing the monthly collections, as well as the aggregate amount. The Order specified a procedure that the utility should follow before funds could be released.

According to the Order, "the escrow requirements shall remain in effect until the utility's next rate case or any modification in its service availability policies or charges." There have been no modifications to the service availability policies or charges. However, on June 6, 2000, the utility filed a petition for a limited proceeding to increase its water rates. This increase would allow the utility to recover the costs associated with building a new water transmission main to connect its wells on the mainland to its service territory on St. George Island. The

utility is proposing a rate increase related to estimated capital expenditures of approximately $6,000,000 to be implemented in three phases. This most recent filing was assigned Docket No. 000694-WU.

While the Commission had various concerns that were specifically addressed in the utility's previous rate proceeding, the requirement of an escrow account for service availability charges and our monitoring the escrow account is no longer necessary. The utility has been diligent in filing the monthly reports as required by Order No. PSC-94-1383-FOF-WU. The utility has also been diligent about following the procedures set forth in that Order for escrow funds to be released. Based on the utility responsibly carrying out the requirements related to the establishment of the escrow account and the process prescribed for disbursing funds from the escrow account and the recent filing for limited proceeding, staff believes that the funds in the escrow account should be released to the utility and the escrow account should be closed.

ISSUE 2: Is the utility in compliance with Order No. PSC-94-1383-FOF-WU, issued November 14, 1994 in Docket No. 940109-WU?

RECOMMENDATION: Yes. The utility is in compliance with Order No. PSC-94-1383-FOF-WU, issued November 14, 1994 in Docket No. 940109-WU. (CROUCH, WILLIS)

STAFF ANALYSIS: In addition to the service availability and escrow requirements mentioned in Issue 1, Order No. PSC-94-1381-FOF-WU required that this docket remain open until the utility submitted:

1) Pension plan documentation;
2) Insurance documentation;
3) the fire protection study;
4) proof of tank maintenance and pipe cleaning;
5) Revised consumptive use permit;
6) Capacity plan;
7) DEP permit application.

Staff has researched the official docket file maintained by the Commission and has received additional information and documentation from the utility and confirmed that all actions required by Order No. PSC-94-1383-FOF-WU, issued November 14, 1994 in Docket No. 940109-WU, have been complied with and are complete.

ISSUE 3: Is the new water transmission main connecting WMSI's wells on the mainland to its water treatment plant on St. George Island justified?

RECOMMENDATION: Yes, the new water transmission main is justified and the prudent costs to be incurred by WMSI in this project should be recovered through rates. (CROUCH)

STAFF ANALYSIS: WMSI's service territory and water treatment plant are located on St. George Island, in Franklin County. Its three water supply wells are located on the mainland. Raw water from the wells is currently transmitted to the island via an 8-inch ductile iron pipe (DIP) attached to and beneath the Bryant Patton bridge. This pipe was constructed in the mid-1970s. In mid-1998, WMSI was formally notified of DOT plans to replace and relocate the existing Patton bridge. Upon completion of the new bridge, DOT intends to abandon the existing Patton bridge and to demolish portions of the existing structure. This will require WMSI to abandon its existing water main and to construct a new main attached to the new bridge. WMSI fought this plan in the courts and lost. Consequently, the existing water main must be abandoned and a new main constructed. Staff, therefore, recommends that the new water transmission main is justified and that the prudent costs to be incurred by WMSI in this project should be recovered through rates.

ISSUE 4: Is the cost of installation of a 12-inch diameter pipeline across the causeway justified? If justified, what is the used and useful percentage?

RECOMMENDATION: Yes. Staff recommends that cost of installation of a 12-inch line, approximately $4,517,535, is a prudent, cost effective investment which will provide additional fire flow, and meet expected growth, including the five year-growth (to 2008) required by statute. Further, staff recommends that the 12-inch line be considered 100% used and useful. (CROUCH)

STAFF ANALYSIS: Flow projections provided in the utility's filing indicate that flows in the year 2003, when the new bridge and pipeline are to be operational, will be approximately 1.141 million gallons per day (MGD). An 8-inch pipeline is only capable of .964 MGD. Consequently, an 8-inch pipeline would not be capable of meeting the demand the moment the new bridge and pipeline become operational. When a five-year growth period, authorized by Section 367.081(2)(a.)2.b., Florida Statutes, is added, the demand in the year 2008 is conservatively estimated to be 1.324 MGD. A 10-inch pipeline could be installed but the maximum capacity of a 10-inch pipe is only 1.5 MGD, slightly more than the expected demand in 2008.

During the customer meeting, numerous customers as well as the St. George Island Fire Chief voiced their concerns over the fact that the utility did not currently have sufficient water and pressure available to provide fire protection to the entire island. Everyone agreed that it would be prudent to increase the size of the causeway pipeline in order to provide better fire protection for the residents. Although not required by Franklin County ordinance, Water Management Services is striving to provide adequate fire flow to the residents of St. George Island. The demand of 120,000 gallons (1000 gallons per minute for 2 hours) is not being met with the existing 8-inch pipe and could not be met with a 10-inch pipe. Based upon best engineering judgement, fire flow requirements, and economy of scale considerations, as well as numerous customer requests, staff recommends that the installation of a 12-inch pipe is prudent and justified and should be considered 100% used and useful. Although the 12-inch pipe will greatly increase the volume and pressure of the water delivered to the island, the ability to provide adequate fire protection throughout the island is still limited by the size and layout of the distribution system.

ISSUE 5: Should the cost of the 10-inch line from Well #4 to Well #1 ($332,000); the new aerator ($4,500); and the new High Service Pump & Controls ($16,500) be included in this limited proceeding? If so, are they 100% used and useful?

RECOMMENDATION: Yes. While these projects and costs are not specifically related to the relocation of the causeway and the installation of a new pipeline, staff recommends that these costs are prudent and these installations could best be performed as part of the overall causeway relocation project. Staff recommends that they also be considered 100% used and useful. (CROUCH)

STAFF ANALYSIS: Staff is convinced that the installation of the pipeline from Well #1 to Well #4, the new aerator, and the new high service pump and controls can most economically be completed as part of the causeway pipeline relocation project. The new causeway pipeline must be installed and fully operational before the existing pipeline is disconnected. That means that the new pipeline must be connected to an aerator, flushed out, and bacteriological tests completed before it can become operational. The installation of a new, separate aerator, which can be tested without affecting the existing system, is prudent and should be approved.

While not directly related to the causeway relocation, the installation of the new pipeline from Well #4 to Well #1 is required and must be interconnected with the new causeway pipeline. This installation can be performed more economically if accomplished concurrently with the new causeway pipeline instead of trying to keep ditches open so that the Well #4 line can be interconnected at a later date. In addition, Well #4 is needed to meet current demand. Therefore, the pipeline connecting Well #4 to Well #1 is justified.

The installation of a new high service pump and controls is also prudent and can more economically be accomplished at the same time the other projects are being installed. This pump is required to maintain adequate pressure during peak demand periods and will also help WMSI meet the demand for increased pressure for fire protection.

Staff recommends that the three projects, while not specifically part of the causeway pipeline relocation, are prudent, and can more economically be completed at the same time as the relocation. Therefore, they should be approved as part of this limited proceeding. The Northwest Florida Water Management District has recognized that WMSI is exceeding the consumptive use

permitted drawdown for the existing three wells and has directed that the utility install Well #4 and associated controls in order to increase pumping capacity. Since all three projects are required to meet existing peak demand, staff further recommends that they be considered 100% used and useful.

ISSUE 6: Should the utility's requested three-phase rate increase be approved, to include the administrative approval by staff of rates for phases 2 and 3?

RECOMMENDATION: No. Staff recommends that a rate increase for Phase 1 is appropriate at this time as addressed later in this recommendation. All three phases should be subject to express Commission approval on a Proposed Agency Action (PAA) basis. Staff's recommended time frame for implementation is July 1, 2002 for Phase 2, and six months after completion of the main replacement project for Phase 3. (KYLE)

STAFF ANALYSIS: In its original petition, WMSI requested an increase in rates which would be phased in so as to enable the utility to service new long-term debt incurred to finance the required construction. The utility proposed a Phase 1 increase of 61.2% in its water rates, to be effective November 1, 2000, and to be applied across the board to the base facility and gallonage charges for all classes of service. The utility further proposed a Phase 2 increase of an additional 51.17% of Phase 1 rates (143.7% of existing rates), to be effective January 1, 2002. Finally, WMSI proposed establishing Phase 3 rates, which would be effective six months after the actual in-service date of the project in 2003 and would be designed to recover the actual capital costs incurred, net of any recovery from DOT with respect to the taking of the existing water main. Under the utility's proposal, the Phase 3 rates would reflect the actual cost of debt on a going-forward basis, and the first twelve months of the Phase 3 rates would be adjusted to true-up for over-or under-collection of rates during Phases 1 and 2. The utility also proposed that the Commission approve the methodology and effective dates described above and grant Staff the authority to approve tariff sheets for Phases 2 and 3 that contain rates calculated in accordance with the approved methodology.

The utility proposes that the Phase 1 rates be effective from November 1, 2000 through December 31, 2001. Staff's analysis of WMSI's amended Exhibit G suggests that it would be more logical to extend Phase 1 through June 30, 2002. Exhibit G projects a substantial amount of construction activity from November, 2000 through April, 2001, then only minor monthly engineering costs until major construction resumes in July, 2002. For example, the utility estimates total costs through December, 2001 of $880,803, but total costs through June, 2002 of only $897,518. Staff does not believe that it is appropriate to increase rates to Phase 2 levels until the commencement of the major construction and associated financing draws projected for the last six months of the project.

Further, while the costs and timing associated with Phase 1 are reasonably estimable at this time, there is considerably more uncertainty regarding the Phase 2 time-frame. WMSI is expected to obtain bids for the major construction. When this process is completed, it will be possible to estimate the actual cost with a higher degree of precision than that of an engineering estimate performed two years in advance. Additionally, the utility has applied for a loan from the Florida Department of Environmental Protection's revolving trust fund. If approved, funds from this loan would be available in approximately July, 2002, and would allow funding of the major construction at a substantially lower interest rate than conventional construction financing. Staff believes that it would be prudent for the Commission to consider the appropriate level of additional revenue required for Phase 2, if any, at a later date, when the relevant data is more precisely known or estimable. Staff also believes that the Commission should expressly act upon any increase in rates associated with Phases 2 and 3 and not provide staff the administrative authority to approve those phases.

ISSUE 7: Are any adjustments necessary to the factors used in the utility's calculation of its Phase 1 revenue requirement increase?

RECOMMENDATION: Yes. The utility's calculation should be adjusted to exclude property taxes, depreciation, and the expense of pursuing this limited proceeding. Further, the calculation should be based on average projected expenditures, the interest rate factor should be 10.5%, and the utility's projection of revenue at current rates during the Phase 1 period should be increased to $731,971. (KYLE)

STAFF ANALYSIS: The utility calculated the proposed rate increases for Phase 1 by estimating the additional revenue requirement needed during each phase to service the debt required to finance the construction. The additional revenue for each phase was then compared to the revenue expected to be collected from existing customers at existing rates in order to determine the percentage increases required. The utility's estimate of additional revenue requirement was accomplished by using a formula which included factors for the total projected expenditures for each phase (net of any recovery from DOT), the interest rate applicable to construction financing, depreciation and property taxes on the new construction, expense of pursuing the limited proceeding, and regulatory assessment fees associated with the increased revenue.

Property Taxes

Staff does not believe that property taxes on the new construction should be part of the calculation. In its response to staff's initial data request, the utility states, and staff agrees, that the first payment of additional property tax on the new property would not be due before November, 2004. Accordingly, staff does not believe that any rate increase associated with increased property taxes should be included in Phase 1 of this limited proceeding.

Cost of Construction

In its proposed formula, the utility states that the component for cost of construction should be the total costs incurred through the end of each phase. In staff's initial data request, the utility was asked to explain why the calculation should not be based on the average construction draws outstanding during each phase. WMSI's response was:

> There is no reason that the revenue requirement for each phase cannot be based on average rather than total

> expenditures during any period, as long as, through the phasing and true-up process, the proceeds are sufficient to have covered the costs incurred in financing WMSI's investment in the new main and associated appurtenances and sufficient to generate cash flow to support repayment of the debt from the date of the first draw.

Staff believes that using the average draws outstanding will generate sufficient cash flow, and that basing the calculation on total draws would result in rates which are higher than required during Phases 1 and 2.

In its amended Exhibit K, Schedule 1, the utility uses $880,803 as the amount of construction costs to be used in calculating the Phase 1 additional revenue requirement. This is the estimate of the total costs to be incurred through December 31, 2001. As discussed in Issue 6, staff believes that the appropriate time frame for Phase 1 rates is from the effective date stated in this recommendation through June 30, 2002. Further, as discussed in the preceding paragraph, staff believes that it is appropriate to use an average of the construction draws outstanding during the period, rather than the total for the period. The utility's amended Exhibit G projects total expenditures prior to November 1, 2000 as $169,500 and total expenditures through June 30, 2002 as $897,518, and projects expenditures and cumulative balances for each intermediate month. Staff believes that it is appropriate to use the average of these monthly amounts, $752,241, as the average amount of utility plant constructed for Phase 1.

Interest Rate

WMSI uses 11.5% as its assumed interest rate. In its original filing the utility based its assumption on the expectation that construction financing would be at the same rate as its existing mortgage with Transamerica SBC (i.e. prime + 2%, per Schedule F-17 of the utility's 1999 Annual Report). In Exhibit K, Schedule 4 of its original filing, the utility included a handwritten note from its internal accountant to the effect that the rate on this loan would increase to 11.5% on July 1, 2000. In its response to staff's initial data request, WMSI stated that it had secured a commitment from The Citizens Bank of Perry and the State Office in Gainesville of the USDA Rural Business Services group to refinance the existing mortgage and provide funding for "soft costs" associated with the required construction. The utility included a copy of the commitment letter for this loan, which stated that the interest rate would be prime + 1%. Accordingly, staff believes

that the appropriate interest rate to be used for calculating the Phase 1 additional revenue requirement is 10.5%.

Depreciation

Staff also has concerns about including in the formula depreciation on property which has not yet been placed into service. In its response to staff's initial data request, the utility stated that, because final construction financing has not been formalized, it is uncertain whether repayment terms will require payments of interest only, or a combination of interest and principal, during the construction period. WMSI's rationale for including depreciation is that it would provide additional cash flow in the event that principal repayments are required during construction. In essence, the utility is requesting that depreciation be considered a surrogate for principal payments which may or may not be incurred. It is staff's understanding that payments for construction financing are customarily interest-only until the project is complete and the construction loan is converted to permanent financing. It has not been the practice of the Commission to allow recovery of depreciation before property is placed into service. Accordingly, staff does not believe that depreciation should be used in calculating Phase 1 or Phase 2 rates in this proceeding.

Cost of Pursuing Limited Proceeding

WMSI's request for Phase 1 and Phase 2 rate increases is analogous to a request for interim rates in a file-and-suspend rate case. In such cases, rate case expense is not included in the calculation of allowable interim rates. Staff therefore recommends that the utility's estimated costs of pursuing this limited proceeding should not be used in calculating the revenue requirements for Phases 1 and 2. Staff believes that the actual costs should be included in Phase 3.

Projection of Revenue at Current Rates

In its original and amended Exhibit K, Schedule 1, the utility calculated a percentage increase in rates by adding the additional revenue requirement to what it refers to as the "Present Metered Revenues," then dividing the total by the "Present Metered Revenues." The "Present Metered Revenues" is the amount estimated to be collected from existing customers using existing rates. The utility used $703,091 in its calculation, an amount which closely approximates the total operating revenue reported on its 1999 Annual Report. In staff's initial data request, the utility was

asked to project its customer growth for a ten-year period. The utility responded with a chart showing 1,461 customers in 2000 and a growth rate of 60 customers per year thereafter, with the exception of 2003, in which a growth of 223 customers was projected. The utility stated that its projected growth rate was "conservative," based on an average growth rate of 70 customers per year from 1990 through 2000.

Staff believes that it is more appropriate to estimate the "Present Metered Revenues" for Phase 1 using the number of customers expected to be connected during the period the Phase 1 rates are in effect. The utility projected 1,461 customers in 2000 and 1,581 in 2002. The average of these amounts is 1,521 and staff believes that this is a reasonable estimate of the average number of customers expected to be served during Phase 1. This is an increase of approximately 4.1% over the number of customers used by the utility in its calculation of the "Present Metered Revenues." Accordingly, staff has recalculated the "Present Metered Revenue" as $731,971.

Summary

In summary, staff believes that the utility's proposed formula for calculating additional revenue requirement for Phase 1 should be adjusted to exclude property taxes, depreciation, and the expense of pursuing this limited proceeding. Further, the calculation should be based on average projected expenditures, the interest rate factor should be 10.5%, and the utility's projection of revenue at current rates during the Phase 1 period should be increased to $731,971.

ISSUE 8: What is the revenue requirement increase, if any, for Phase 1?

RECOMMENDATION: The appropriate revenue requirement increase for Phase 1 is $82,707 (11.3%). (KYLE)

STAFF ANALYSIS: In Exhibit K, Schedule 3 of the filing, the utility calculated the metered service revenue to be collected from existing customers at existing rates as $703,091, consisting of total operating revenue of $708,796, less miscellaneous revenues of $5,705. The total operating revenue amount is the same amount as that reported on WMSI's Annual Report for 1999. Using its requested revenue increase of $430,416, the utility proposed an increase in rates of 61.2% for Phase 1.

In its response, dated August 11, 2000, to staff's initial data request, the utility provided updated information and amplified its justification of some of the theories supporting its methodology in calculating the proposed rate increases. The utility also included amendments of Exhibits G, J and K. The amended exhibits reflect a revised Phase 1 revenue increase of $146,547, and a corresponding increase in rates of 20.8%. The methodology used by WMSI in its revised calculation was the same as described above, except that the estimate of expenditures to be incurred through 12/31/01 was decreased to $880,803 from the original projection of $2,636,196.

Using the utility's proposed formula, but incorporating the adjustments recommended in Issue 7, staff has calculated the additional revenue requirement for Phase 1 as $82,707 (11.3%).

ISSUE 9: What is the appropriate rate structure for this utility?

RECOMMENDATION: The appropriate rate structure for the Phase 1 increase is the continuation of the current base facility charge (BFC)/gallonage charge rate structure. In order to properly evaluate whether a change in rate structure for the Phase 2 increase is appropriate, staff recommends that the utility be ordered to prepare monthly reports detailing the number of bills rendered, the consumption billed and the revenue billed. These reports should be prepared, by customer class and meter size, for the period beginning January 1999 and until such time as a recommendation for Phase 2 rates is filed. The reports for the period January 1999 through September 2000 should be provided to staff within 30 days of the date of the Commission's vote on Phase 1 rates. The reports for the periods after September 2000 should be provided on a monthly basis within 30 days of the end of the preceding month. (LINGO)

STAFF ANALYSIS: The utility's current rate structure is the traditional BFC/gallonage charge rate structure. This is the Commission's preferred rate structure, because it is designed to provide for the equitable sharing by the rate payers of both the fixed and variable costs of providing service.

Although the current rate structure is considered usage sensitive because customers are charged for all water consumed, in its last rate case, St. George proposed a rate design more heavily weighted towards the base facility charge in order to increase cash flow to cover fixed expenses during the off-season. The Commission agreed with the utility's proposed rate structure; however, the resulting rate structure decreases the gallonage charge, thereby decreasing the usage sensitivity of the rate structure.

The utility has requested that the Phase 1 increase be treated as an emergency rate increase, in order to secure financing of the new pipeline. Because this initial increase is being treated as an emergency increase, and because staff does not have sufficient customer usage data at this time, we recommend that the appropriate rate structure for the Phase 1 increase is the continuation of the utility's current rate structure.

However, at the customer meetings held on September 12, 2000, several customers mentioned their preference for a rate structure with a greater emphasis placed on usage in order to reflect the different consumption habits of permanent residents versus renters. Staff agrees that it is appropriate to examine the feasibility of a more usage-sensitive rate structure that sends stronger pricing

signals to customers with respect to conservation, while also considering the cash flow requirements of the utility. Therefore, staff recommends that the utility be ordered to prepare monthly reports detailing the number of bills rendered, the consumption billed and the revenue billed. These reports should be prepared, by customer class and meter size, for the period beginning January 1999 and until such time as a recommendation for Phase 2 rates is filed. The reports for the period January 1999 through September 2000 should be provided to staff within 30 days of the date of the Commission's vote on Phase 1 rates. The reports for the periods after September 2000 should be provided on a monthly basis within 30 days of the end of the preceding month.

ISSUE 10: What is the appropriate rate increase, if any, for Phase 1?

RECOMMENDATION: The appropriate rate increase for Phase 1 is an 11.3% increase in both base facility and gallonage charges, resulting in the rates depicted in Attachment A to this recommendation. The approved Phase 1 rates should be effective for service rendered on or after the stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), Florida Administrative Code, and should be held subject to refund with interest pending the final decision in this docket. The Phase 1 rates should not be implemented until notice has been received by the customers. The utility should provide proof of the date notice was given within 10 days after the date of the notice. In addition, after the increased rates are in effect, pursuant to Rule 25-30.360(6), Florida Administrative Code, the utility should file reports with the Commission no later than 20 days after each monthly billing. These reports should indicate the amount of revenue collected under the increased rates. (KYLE)

STAFF ANALYSIS:

Using the additional revenue requirement of $82,707 recommended in Issue 8 and the "Present Metered Revenue" of $731,791 as recommended in Issue 7, staff recommends an increase in base facility charge and gallonage charges of approximately 11.3%.

As part of its analysis, staff compared the projected additional monthly revenue resulting from the above increase with the projected monthly debt service expenditures to be paid by the utility, and found the total amounts during the Phase 1 time-frame to be very similar.

Staff recommends that the approved Phase 1 rates should be effective for service rendered on or after the stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), Florida Administrative Code, and should be held subject to refund with interest pending the final decision in this docket. The Phase 1 rates should not be implemented until notice has been received by the customers. The utility should provide proof of the date notice was given within 10 days after the date of the notice. The recommended rates collected by the utility should be subject to the refund provisions discussed in Issue 12.

ISSUE 11: Should the recommended rates be approved for the utility on a temporary basis, subject to refund, in the event of a protest?

RECOMMENDATION: Yes, the recommended rates should be approved for the utility on a temporary basis in the event of a protest. The utility should be authorized to collect the temporary rates after staff's approval of the security for potential refund, the proposed customer notice, and the revised tariff sheets. (KYLE)

STAFF ANALYSIS: This recommendation proposes an increase in water rates. The Commission has approved temporary rates in the event of protest when a delay in what might be a justified rate increase would result in unrecoverable loss. See Order No. PSC-99-1883-PAA-SU, issued September 21, 1999, in Docket No. 980242-SU. Therefore, in the event of a protest, staff recommends that the recommended rates be approved as temporary rates. The recommended rates collected by the utility should be subject to the refund provisions discussed in Issue 12. In addition, after the increased rates are in effect, pursuant to Rule 25-30.360(6), Florida Administrative Code, the utility should file reports with the Commission no later than 20 days after each monthly billing. These reports should indicate the amount of revenue collected under the increased rates.

ISSUE 12: What is the appropriate security to guarantee the Phase 1 rate increase?

RECOMMENDATION: The utility should be required to open an escrow account, file a security bond or a letter of credit to guarantee any potential refunds of revenues collected under interim conditions. The escrow account, security bond or letter of credit should be in the amount of $145,000. Pursuant to Rule 25-30.360(6), Florida Administrative Code, the utility should provide a report by the 20th of each month indicating the monthly and total revenue collected subject to refund. Should a refund be required, the refund should be with interest and undertaken in accordance with Rule 25-30.360, Florida Administrative Code. (D. DRAPER, KYLE)

STAFF ANALYSIS: As recommended in Issue 8, the total annual interim increase is $82,707 for the water system on an annual basis. Staff has calculated the potential refunds of water revenues and interest collected, in accordance with Rule 25-30.360, Florida Administrative Code, to be $145,000. This amount is based on an estimated nineteen months of revenue being collected from staff's recommended Phase 1 rates over the previously authorized rates.

Staff has reviewed the financial data of the utility. The criteria for a corporate undertaking includes sufficient liquidity, ownership equity, profitability, and interest coverage to guarantee any potential refund. The 1997, 1998 and 1999 annual reports of WMSI were used to determine the financial condition of the Company. Staff's analysis concludes that WMSI has shown minimal liquidity and negative equity for the three-year period. In addition, WMSI has had minimal interest coverage and negative profitability over the last three years. Based upon this analysis, staff recommends that WMSI cannot support a corporate undertaking in the amount of $145,000. Therefore, staff recommends that the utility provide a letter of credit, bond or escrow agreement to guarantee the funds collected subject to refund.

This brief financial analysis is only appropriate for deciding if the utility can support a corporate undertaking in the amount proposed and should not be considered a finding regarding staff's position on other issues in the rate case.

If the security provided is an escrow account, said account should be established between the utility and an independent financial institution pursuant to a written escrow agreement. The Commission should be a party to the written escrow agreement and a

signatory to the escrow account. The written escrow agreement should state the following: that the account is established at the direction of this Commission for the purpose set forth above; that no withdrawals of funds shall occur without the prior approval of the Commission through the Director of the Division of Records and Reporting; that the account shall be interest bearing; that information concerning that escrow account shall be available from the institution to the Commission or its representative at all times; that the amount of revenue subject to refund shall be deposited in the escrow account within seven days of receipt; and that pursuant to Cosentino v. Elson, 263 So. 2d 253 (Fla 3d, DCA 1972), escrow accounts are not subject to garnishments.

The utility should deposit $6,900 into the escrow account each month for possible refund. The escrow agreement should also state the following: that if a refund to the customers is required, all interest earned on the escrow account shall be distributed to the customers; and if a refund to the customers is not required, the interest earned on the escrow account shall revert to the utility.

If the security provided is a bond or a letter of credit, said instrument should be in the amount of $145,000. If the utility chooses a bond as security, the bond should state that it will be released or should terminate only upon subsequent order of the Commission. If the utility chooses to provide a letter of credit as security, the letter of credit should state that it is irrevocable for the period it is in effect and that it will be in effect until a final Commission order is rendered releasing the funds to the utility or requiring a refund.

Irrespective of the type of security provided, the utility should keep an accurate and detailed account of all monies it receives. Pursuant to Rule 25-30.360(6), Florida Administrative Code, the utility shall provide a report by the 20th day of each month indicating the monthly and total revenue collected subject to refund. Should a refund be required, the refund should be with interest and undertaken in accordance with Rule 25-30.360, Florida Administrative Code.

In no instance should maintenance and administrative costs associated with any refund be borne by the customers. The costs are the responsibility of, and should be borne by, the utility.

ISSUE 13: Should these dockets be closed?

RECOMMENDATION: No further action is necessary in Docket No. 940109-WU. Therefore, Docket No. 940109-WU should be closed. With respect to Docket No. 000694-WU, if no timely protest is received upon the expiration of the protest period, the PAA Order will become final upon the issuance of a Consummating Order. However, Docket No. 000694-WU should remain open pending Commission action on the utility's request for increased rates for Phases 2 and 3. (GERVASI, FUDGE)

STAFF ANALYSIS: No further action is necessary in Docket No. 940109-WU. Therefore, Docket No. 940109-WU should be closed. With respect to Docket No. 000694-WU, if no timely protest is received upon the expiration of the protest period, the PAA Order will become final upon the issuance of a Consummating Order. However, Docket No. 000694-WU should remain open pending Commission action on the utility's request for increased rates for Phases 2 and 3.

Attachment A

Water Management Services, Inc. — Schedule of Monthly Rates

Residential and General Service:

Meter Size	Existing Rates * BFC per month	Utility Requested Phase 1 Rates (Original) BFC per month	Utility Requested Phase 1 Rates (Amended) BFC per month	Staff Recommended Phase 1 Rates BFC per month
5/8" x 3/4"	$20.90	$33.69	$25.26	$23.26
1"	$52.25	$84.24	$63.14	$58.15
1 ½"	$104.51	$168.49	$126.29	$116.32
2"	$167.20	$269.56	$202.05	$186.09
3" Compound	$334.40	$539.11	$404.10	$372.18
3" Turbine	$365.77	$589.69	$442.01	$407.10
4" Turbine	$627.02	$1,010.87	$757.71	$697.87
6" Turbine	$1,306.30	$2,105.99	$1,578.58	$1,453.90
Gallonage Charge, per 1,000 Gallons	$1.98	$3.19	$2.39	$2.20

* BFC = Base Facility Charge