

State of Florida



Public Service Commission

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RECORDS AND REPORTING

DATE: JANUARY 4, 2001

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

FROM: DIVISION OF ECONOMIC REGULATION (FLETCHER, BINFORD, 198
WETHERINGTON, CROUCH, LINGO, WILLIS)
DIVISION OF LEGAL SERVICES (FUDGE, JAEGER)

RE: DOCKET NO. 991643-SU - APPLICATION FOR INCREASE IN
WASTEWATER RATES IN SEVEN SPRINGS SYSTEM IN PASCO COUNTY
BY ALOHA UTILITIES, INC.
COUNTY: PASCO

AGENDA: JANUARY 16, 2001 - REGULAR AGENDA - POST HEARING DECISION
- PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF

CRITICAL DATES: 8-MONTH STATUTORY DATE: DECEMBER 4, 2000
12-MONTH DEADLINE DATE: APRIL 4, 2001

SPECIAL INSTRUCTIONS: NONE

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FPSC-RECORDS/REPORTING

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CASE BACKGROUND

Aloha Utilities, Inc. (Aloha or utility), is a Class A water and wastewater utility in Pasco County. The utility consists of two distinct service areas, Aloha Gardens and Seven Springs. These service areas are physically divided by U.S. Highway 19, the major north/south highway through Pinellas and Pasco County. The utility's service area is located within the Northern Tampa Bay Water Use Caution Area as designed by the Southwest Florida Water Management District (SWFWMD). Critical water supply concerns have been identified by SWFWMD within this area. The following was obtained from Aloha's 1999 annual report for the Seven Springs systems:

	<u>Number of Customers</u>	<u>Operating Revenues</u>
Water	9,242	\$1,726,029
Wastewater	8,866	\$2,493,675

Rate base was last established for Aloha's Seven Springs wastewater system by Order No. PSC-99-1917-PAA-WS, issued September 28, 1999, in Dockets Nos. 970536-WS and 980245-WS. This Order was consummated by Order No. PSC-99-2083-CO-WS, issued October 21, 1999.

On February 9, 2000, Aloha filed an application for an increase in rates for its Seven Springs wastewater system. The utility was notified of several deficiencies in the minimum filing requirements (MFRs) by staff. Those deficiencies were corrected and the official filing date was established as April 4, 2000, pursuant to Section 367.083, Florida Statutes.

Aloha's requested test year for interim purposes is the historical year ended September 30, 1999. The utility's requested test year for the setting of final rates is the projected year ended September 30, 2001. Also, the utility requested that this application be directly set for hearing. Two days of hearings were held on October 2 and 3, 2000, at the Spartan Manor in New Port Richey, Florida. A third day of hearing was held in Tallahassee on November 2, 2000.

In its MFRs, the utility requested annual interim revenues of \$2,568,801. This represents a revenue increase of \$48,532 (or 1.92%). For final consideration, the utility has requested total revenues of \$4,374,495. This represents a revenue increase of

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\$1,593,501 (or 57.29%). The final revenues are based on the utility's request for an overall rate of return of 9.24%.

On May 3, 2000, the Commission issued its Order Establishing Procedure, Order No. PSC-00-0872-PCO-SU. That Order set the dates for the filing of testimony and other documents and the procedures to be followed in this case. That Order initially required intervenors and staff to prefile their testimony on July 17, 2000 and August 14, 2000, respectively.

By Order No. PSC-00-1065-PCO-SU, issued June 5, 2000, the Commission denied interim rates and suspended the utility's proposed rates.

On June 27, 2000, the Office of Public Counsel (OPC) filed its Notice of Intervention. By Order No. PSC-00-1175-PCO-SU, issued June 29, 2000, the Commission acknowledged OPC's intervention.

Because of a discovery dispute, both OPC and staff requested a two-week extension in which to prefile their testimony. By Order No. PSC-00-1288-PCO-SU, issued July 17, 2000, the Prehearing Officer granted staff's and OPC's request for extension of time. Because that Order contained several sentences that were not necessary for the ruling, by Order No. PSC-00-1636-PCO-SU, issued September 13, 2000, the Commission vacated Order No. PSC-00-1288-PCO-SU and allowed OPC and staff a two-week extension of time to prefile their testimony.

OPC timely filed its testimony on July 31, 2000, and staff timely filed its testimony on August 28, 2000. OPC and staff also timely filed their prehearing statements on September 5, 2000. However, by Order No. PSC-00-1609-PCO-SU, issued September 8, 2000, the Prehearing Officer granted Aloha an extension of time to file its prehearing statement which it did on September 8, 2000.

OPC timely filed the rebuttal testimony of Mr. Ted L. Bidy on September 11, 2000. By Order No. PSC-00-1642-PCO-SU, issued September 14, 2000, the Prehearing Officer granted Aloha's Motion for Extension of Time to prefile rebuttal testimony until September 17, 2000.

On September 18, 2000, Aloha filed its Motion to Strike "Rebuttal" Testimony of OPC witness Bidy. On September 25, 2000, OPC timely filed its Response to Aloha's Motion to Strike Rebuttal Testimony. By Order No. PSC-00-1779-PCO-SU, issued September 29, 2000, the Prehearing Officer granted Aloha's motion.

On September 14, 2000, Aloha filed a Motion to Allow Filing of Supplemental Direct Testimony with the Supplemental Direct Testimony of Stephen G. Watford attached as Attachment A with exhibit SGW-1. This testimony addressed the issue of a new office building that was not originally included in Aloha's MFRs and on which neither the utility, OPC nor staff had filed direct testimony.

The Prehearing Conference was held on September 18, 2000. The Prehearing Order and Order Revising Order Establishing Procedure, Order No. PSC-00-1747-PHO-SU, was issued on September 26, 2000. This Order granted Aloha's Motion to Allow Filing of Supplemental Direct Testimony with the Supplemental Direct Testimony of Mr. Watford attached as Attachment A with exhibit SGW-1 and allowed the addition of a new issue stated as follows: Should the Commission consider the new office building cost for the utility in this rate proceeding. The Order also allowed the Executed Contract for Sale of New Office Building submitted on September 15, 2000, to be identified as exhibit SGW-2. The Order also struck the rebuttal testimony of Mr. Stephen G. Watford, concerning the new office building, beginning at page 2, line 20, and going through page 6, line 15.

Also, staff was allowed to file supplemental direct testimony on this issue on October 18, 2000, and Aloha was allowed to file supplemental rebuttal testimony on this issue on October 23, 2000.

The formal hearing on all the other issues was held on October 2 and 3, 2000, but the Commission was unable to conclude the hearing on those issues by October 3, 2000. Therefore, the hearing on all the issues, plus the new issue was continued on November 2, 2000, and concluded on that date.

The eight-month deadline for the suspension of the requested rates expired on December 4, 2000. The twelve-month deadline for the Commission to take final action in this docket expires on April 4, 2001. On December 1, 2000, Aloha filed a notice of intent to implement its final proposed rates, along with revised tariff sheets, a proposed customer notice, and a corporate undertaking of the utility. However, upon being advised by staff that it appeared Aloha could not support a corporate undertaking, Aloha filed an escrow agreement on December 8, 2000. Section 367.081(6), Florida Statutes, states that "[s]uch consent shall not be withheld for a period longer than 8 months following the date of filing." At the January 2, 2001 agenda conference, the Commission acknowledged the utility's implementation of rates.

Approved Stipulations

The Commission found that the stipulations reached by the parties and supported by staff were reasonable, and accepted the stipulated matters set forth below at the hearing.

Category One Stipulations

Those stipulations which the utility and OPC agreed and staff supported, are set forth below:

1. David MacColeman's prefiled testimony shall be inserted into the record as though read, and he will be excused from attending the hearing and being subject to cross-examination.
2. For the wastewater treatment plant expansion from 1999 to 2000, plant-in-service should be reduced by \$122,524 which reflects the appropriate allowance for funds used during construction rate of 9.08%. Corresponding adjustments should be made to reduce accumulated depreciation by \$8,159 and depreciation expense by \$5,903.
3. For items that were erroneously expensed during the historical September 30, 1999 base year, Account 720 - Materials and Supplies, should be reduced by \$13,072. This adjustment is consistent with staff Audit Exception No. 3, and also reflects removal of the company's escalation of the expense. 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.
4. 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.
5. Utility charges recorded as transportation expenses in the amount of \$280 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.

6. Expenses related to errors resulting from Aloha's computer system conversion should be allocated to all of the utility's systems. Consistent with staff Audit Disclosure No. 5, Account 718 -- Chemicals, and Account 720 -- Materials and Supplies, 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 of \$136 should also be removed for a total adjustment of \$1,223.
7. Certain loan costs were expensed that should have been capitalized and amortized. Consistent with staff Audit Disclosure No. 9, Account 732 - Contractual Services - Legal, should be reduced by \$2,581.
8. Seven Springs wastewater land should be reduced by \$12,120 and Aloha Gardens wastewater land should be increased by \$12,120.
9. Income tax deposits should be removed from the working capital calculation because the utility does not anticipate paying any income tax.
10. In 1999, the utility expensed above-the-line \$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.
11. Accounts payable on Construction-Work-in-Progress (CWIP) provide a 30-day cost-free source of capital, and plant-in-service should be reduced by \$20,124. Also, accumulated depreciation and depreciation expense should be reduced by \$568.
12. The Allowance for Funds Used During Construction (AFUDC) should be calculated based on the overall cost of capital approved in this rate case. The effective date will be October 1, 2001, and the monthly discount rate will be calculated in accordance with the appropriate rule.

13. Retained earnings should be reduced by \$172,806 because of an overstatement of the 13-month average balanced by the utility. In addition, the final projected September 30, 2001, customer deposits balance should be \$438,412 resulting in a \$345,117 reduction in retained earnings.
14. The appropriate mileage rate to project tangible personal property taxes is 1.990754 percent or 19.90754 mils. (Issue 33)

Category Two Stipulations

Those stipulations which the utility offered and staff supported, but upon which OPC took no position, are set forth below:

15. None of the revenue requirement associated with reuse and approved in this docket should be allocated to the utility's water customers as allowed by Section 367.0817(3), Florida Statutes. This is consistent with Order No. PSC-97-0280-FOF-WS.
16. The extension of the Mitchell agreement dated March 19, 1999 should be approved. However, any further extension of the contract after this current term expires should be approved by the Commission before such an extension is executed.
17. For the base year ended September 30, 1999, the depreciation rate for computer equipment should be 16.67 percent. Adjustments should be made to correct the base, intermediate and projected test year accumulated depreciation and depreciation expense.

This recommendation addresses all issues related to Aloha's requested final rate increase and the appropriate amount of refunds. The Commission has jurisdiction pursuant to Sections 367.011(2) and 367.081, Florida Statutes.

RULINGS ON MOTIONS

- I. OPC's Motion for Reconsideration of Order Striking OPC Witness Biddy's Rebuttal Testimony

At the hearing on October 2, 2000, OPC made an ore tenus motion for the Commission to reconsider that portion of Order No. PSC-00-1779-PCO-SU, which struck OPC witness Bidy's rebuttal testimony concerning the existence of excessive infiltration and inflow (I&I). After hearing argument of counsel, the Commission found that there was no mistake of fact or law contained in Order No. PSC-00-1779-PCO-SU. Therefore, the Commission denied OPC's Motion for Reconsideration of the Order striking that portion of witness Bidy's rebuttal testimony which concerned the existence of excessive I&I.

II. OPC's Motion to Strike Portions of Supplemental Rebuttal Testimony of Exhibits and Utility Witnesses Nixon and Watford

At the hearing on November 2, 2000, OPC made an ore tenus motion for the Commission to strike major portions of the supplemental rebuttal testimony and exhibits of utility witnesses Nixon and Watford. Specifically, OPC moved to strike the supplemental rebuttal testimony of utility witness Watford as follows: from page 4, line 20 through page 22, line 5; from page 22, line 17 through page 24, line 11; from page 25, line 13 through page 28, line 3; from page 28, line 22 through page 29, line 3; from page 29, line 7 through page 29, line 13; from page 30, line 3 through page 30, line 5; from page 32, line 22 through page 36, line 8; from page 36, line 22 through page 37, line 11; and from page 40, line 25 through page 41, line 17. Moreover, OPC moved to strike Exhibits Nos. SGW-SR2 through SGW-SR7 which were attached to utility witness Watford's supplemental rebuttal testimony.

Similarly, OPC moved to strike all of utility witness Nixon's supplemental rebuttal testimony except the testimony beginning at page 1, line 23 through page 3, line 5. OPC also requested that Exhibits Nos. RCN-18 through RCN-20, which were attached to utility witness Nixon's supplemental rebuttal testimony, be stricken.

In moving to strike the above-noted testimony and exhibits, OPC stated that the utility should be held to the same standard to which OPC was held when, by Order No. PSC-00-1779-PCO-SU, the Commission struck OPC witness Bidy's rebuttal testimony. In that Order, the Prehearing Officer found that the rebuttal testimony filed by Mr. Bidy was "direct testimony that OPC could have or should have filed in its direct testimony." Moreover, the Order noted that the issues had been identified, and should have been addressed in OPC's direct testimony. OPC argues that a great deal of evidence that the utility provided in response to the listing of perceived deficiencies by staff witness Merchant could have or

should have been included in the utility's direct testimony and was not proper rebuttal testimony. In responding to the perceived deficiencies, OPC stated that the utility should have done one of two things: (a) it could have said "yes we did provide those things that you are looking for;" or (b) "we didn't provide those things, but we didn't need to because our justification lies elsewhere." Instead, OPC argues that Aloha merely filed additional evidence seeking to bolster its case, which evidence should have been submitted in the utility's direct testimony.

Aloha stated that the Order striking OPC witness Bidby's rebuttal testimony was based, at least in part, on the fact that Mr. Bidby was attempting to say what staff witness MacColeman meant to say or was attempting to put words in his mouth and that this was improper rebuttal. Aloha argued that its response to staff witness Merchant's criticisms is different from Mr. Bidby's rebuttal testimony. According to Aloha, its supplemental rebuttal testimony shows that it did the analysis and instructed the realtor on the requirements for a building, which staff witness Merchant stated was not evident in the utility's supplemental direct testimony.

Upon consideration of the above, the Commission found it appropriate to grant in its entirety the ore tenus motion of OPC to strike certain rebuttal testimony and exhibits of Aloha witnesses Watford and Nixon, and such testimony and exhibits, as indicated by OPC, were stricken from the record. The Commission noted that OPC did not move to strike all such testimony and that the utility proffered the prefiled supplemental rebuttal testimony and exhibits to the extent that they were stricken.

III. Motion of Aloha to Strike Supplemental Direct Testimony of Staff Witness Merchant

At the hearing on November 2, 2000, after initially stipulating that the supplemental direct testimony of staff witness Merchant could be inserted into the record as though read, and subsequent to the Commission having granted OPC's motion to strike major portions of Aloha's supplemental rebuttal testimony and exhibits, Aloha made an ore tenus motion to strike all of the supplemental direct testimony of staff witness Merchant. Aloha argued that staff witness Merchant failed to take a position on the prudence of the purchase of the office building and that her testimony was therefore irrelevant and immaterial.

OPC argued that because the utility had already stipulated that the testimony could be entered, that it was past the phase during which an objection could be entered.

Staff counsel noted that this testimony was not rebuttal and that the rationale supporting the striking of rebuttal testimony did not apply in this instance. Moreover, staff counsel noted that it was for the Commission to decide whether the testimony of staff witness Merchant would aid it in making a decision on the appropriateness of including the cost of the new building in calculating the appropriate rates for the utility. After hearing argument of counsel, the Commission denied Aloha's motion.

IV. Aloha's Motion for Reconsideration of the Commission's Decision to Strike Portions of the Utility's Supplemental Rebuttal Testimony

On November 15, 2000, Aloha filed a Motion for Reconsideration of the Commission's ruling granting the ore tenus motion of OPC to strike portions of the supplemental rebuttal testimony and exhibits of Aloha witnesses Robert C. Nixon and Stephen G. Watford. A timely response to the Motion was filed by OPC on November 29, 2000. By Order No. PSC-00-2534-PCO-SU, issued December 28, 2000, the Commission found that neither Rule 25-22.060 nor Rule 25-22.0376, Florida Administrative Code, was applicable at that time and that the Motion for Reconsideration was premature. Consequently, the Commission denied Aloha's Motion for Reconsideration without prejudice to refile, in accordance with Rule 25-22.060, Florida Administrative Code, after rendition of the Final Order memorializing our ruling.

V. OPC's Motion for Extension of Time to File Brief

On November 16, 2000, OPC filed a Motion for Extension of Time to File Brief. The Motion was granted by Order No. PSC-00-2191-PCO-SU, issued November 17, 2000, which made all briefs due on November 29, 2000.

Abbreviations and Technical Terms

The following is a list of acronyms and technical terms which have been used in the recommendation.

COMPANY AND PARTY NAMES:

Aloha or utility	Aloha Utilities, Inc.
OPC	Office of Public Counsel

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TECHNICAL TERMS:

AADF	Annual Average Daily Flow
AFUDC	Allowance for Funds Used During Construction
ARCFJ	Amended and Restated Consent Final Judgement
CIAC	Contribution in Aid of Construction
CTs	Contributed Taxes
DEP	Department of Environmental Protection
DTAs	Deferred Tax Assets
DTLs	Deferred Tax Liabilities
ERCs	Equivalent Residential Connections
F.A.C.	Florida Administrative Code
GPD	Gallons Per Day
GPM	Gallons Per Minute
I&I	Infiltration and Inflow
MFRs	Minimum Filing Requirements
MGD	Million Gallons Per Day
NARUC	National Association of Regulatory Utility Commissioners
SWFMD	Southwest Florida Water Management District
NOI	Net Operating Income
ROE	Return on Equity
TY	Test Year
U&U	Used and Useful
USOA	Uniform System of Accounts
WWTP	Wastewater Treatment Plant

QUALITY OF SERVICE

ISSUE 1: Is the quality of service satisfactory?

RECOMMENDATION: Yes. Staff recommends that the quality of service provided by Aloha Utilities, Inc. at its Seven Springs Wastewater Treatment Plant is satisfactory. (CROUCH)

POSITION OF PARTIES

ALOHA: Yes. The utility is providing a service in conformance with all applicable standards, including full compliance with the requirements of the Consent Agreement entered into between the utility and DEP.

OPC: No. Aloha's authorized ROE should be reduced by 100 basis points to reflect substandard customer treatment.

STAFF ANALYSIS: Quality of Service provided by the utility is an issue considered by the Commission in virtually every rate case. Rule 25-30.433(1) F.A.C. states that:

The Commission in every rate case shall make a determination of the quality of service provided by the utility. This shall be derived from an evaluation of three separate components of water and wastewater utility operations: quality of the utility's product (water and wastewater); operational conditions of the utility's plant and facilities; and the utility's attempt to address customer satisfaction. Sanitary surveys, outstanding citations, violations and consent orders on file with the Department of Environmental Protection (DEP) and the county health departments or lack thereof over the preceding 3-year period shall also be considered. DEP and county health officials' comments or testimony concerning quality of service as well as the complaints or testimony of utility's customers shall be considered.

Staff's analysis below addresses each of these three components.

Aloha is a Class A water and wastewater utility. Its service area is located in New Port Richey, Florida, which is in Pasco County. The utility consists of two distinct service areas - Aloha Gardens and Seven Springs. These service areas are physically divided by U.S. Highway 19. In its Seven Springs service area, it

provides water service to approximately 9,242 customers and wastewater service to approximately 8,866 customers. This case deals exclusively with the Seven Springs Wastewater Treatment Plant. Its current wastewater plant is permitted by DEP at 1.2 MGD based upon AADF. (EX 7) Aloha is currently under a ARCFJ with DEP which requires Aloha to expand the wastewater treatment plant and provide Class I Reliability so that the effluent can be reused and applied to areas where human contact is acceptable. (EX 5)

Quality of Utility's Product:

Aloha is not meeting the requirements specified by DEP for wastewater treatment at this time. (TR 497-499) The utility is currently operating under a ARCFJ in which DEP has ordered Aloha to increase the size of its plant; implement an Infiltration & Inflow reduction program; and produce a reusable effluent suitable for public access application. (EX 5) The surface water effluent now produced by the treatment plant is a major subject of the ARCFJ. (TR 498) According to staff witness MacColeman, an employee of DEP, Aloha is currently on schedule for meeting the demands of the ARCFJ. (TR 497) The interim, 1.6 MGD plant now under construction is designed to bring Aloha into compliance with DEP rules and regulations. Consequently, staff recommends that the quality of the utility's product be found satisfactory.

Operational Conditions of the Utility's Plant and Facilities:

As stated above, Aloha is currently operating under the guidelines of a ARCFJ in which DEP is requiring the plant capacity to be increased from 1.2 MGD to 1.6 MGD (interim) and eventually to 2.4 MGD with Class I reliability. According to staff witness MacColeman, an employee of DEP, Aloha has appropriate permits and is on schedule for meeting the demands of the ARCFJ. (TR 497-498) Therefore, staff recommends that the operational condition of the utility's plant and facilities be found satisfactory.

Utility's Attempt to Address Customer Satisfaction:

Customer satisfaction was addressed at the Hearing on October 2, 2000. The Presiding Officer at the Hearing explained that the Commission was seeking customer comments and testimony concerning wastewater service and wastewater issues and not issues related to water quality. (TR 14, 16, 17, 24, 282, 286) However, the Presiding Officer noted that the responsiveness of the company as a whole is quality of service issue. (TR 24) A total of 39 customers spoke at the morning and evening sessions, 15 of whom addressed only water quality complaints. Eight customers

complained about the proposed rate increase and the cost of their utilities. (TR 64, 72, 78, 83, 291, 306, 334, 340) One customer (Rosin) complained about the proposed rate increase but also testified that the utility personnel were "pretty good people". (TR 333-334) Mr. McMahon (TR 321-322), Mr. Dean (TR 312-313), Mr. Schermerhorn (TR 97-98), Mr. Reethof (TR 68), Mr. Lane (TR 74) and others asked about irrigation meters or the availability of treated effluent to reduce their water bills. Five customers spoke despite the fact that they did not live in the Seven Springs area and were not affected by the proposed wastewater treatment upgrade. (TR 51, 62, 290, 298, 348) (EX 2) Mr. Cifelli voiced concern over the size of his water bills in the past and inquired about getting his meter checked and/or replaced. (TR 299-302) While this was actually a water complaint, staff arranged for the utility to replace Mr. Cifelli's meter shortly after the completion of the Hearing. One customer stated that he had contempt for Aloha and even more contempt for the PSC, while another customer expressed frustration with the progress made by the PSC. (TR 323, 326) The utility has no record of either of these customers ever registering a complaint about wastewater service. (EX 2) Mr. LaMaire, a resident of Trinity Oaks, complained about the ability of Aloha to maintain its wastewater system, citing odor problems with pumping [lift] stations in his neighborhood. (TR 53-55) He further testified that the utility responded to complaints and put a cap over the end of a pipe. (TR 54) Aloha responded that a complaint had been received from another customer and that the utility responded and implemented odor control measures and capped off the pipe. No complaint was ever received from Mr. LaMaire and no other complaints were received from any customer after the odor control measures were implemented. (EX 2)

It should be pointed out that complaints related to water quality and service are currently being addressed in a separate docket, Docket No. 960545-WS, and are being thoroughly investigated by this Commission. Each of the specific customer complaints concerning Seven Springs wastewater were addressed by the utility in EX 2.

OPC has taken the position that the quality of service is unsatisfactory. OPC refers to the testimony of Ms. Doris Boyce, who stated that she went to the Aloha offices to lodge a complaint and to discuss the matter with Mr. Stephen Watford. When she attempted to speak with Mr. Watford, the utility had Ms. Boyce physically removed by the police. (TR 349) OPC states that such heavy-handed treatment of a captive customer is altogether inappropriate. OPC further states that it is clear that Aloha does not put forth sufficient effort to treat its customers' concerns

properly. OPC argues that Aloha's authorized ROE should be reduced to reflect this improper treatment (BR 1).

The utility responds that there was absolutely no evidence in this proceeding that Aloha has failed to appropriately respond to any customer's concern which even arguably relates to the provision of wastewater service. (EX 2) Additionally, there was absolutely no prefiled testimony in this case which even suggested or implied that the quality of Aloha's wastewater service is less than satisfactory or that Aloha is not in full compliance with the requirements of the Amended and Restated Consent Final Judgment. Ms. Boyce complained about a water bill which she received several years ago. (TR 348) Hers was not a wastewater complaint. Moreover, she is not a customer of the Seven Springs system since she lives in Holiday, Florida. (TR 348) OPC admits that Ms. Boyce lives in Aloha Gardens [and is therefore not a customer of the Seven Springs wastewater system] (BR 1). Neither OPC nor the utility questioned Ms. Boyce. Consequently, there is nothing in the record explaining this incident other than the fact that it was a water matter which happened several years ago at a different Aloha utility. (TR 349)

CONCLUSION:

Staff recommends that based on the record, the quality of the utility's wastewater product and the operational condition of Aloha's wastewater plant and facilities are both satisfactory. The utility is under an ARCFJ with DEP which ordered Aloha to expand its wastewater treatment facility and provide effluent capable of being applied to areas where human contact is acceptable. While 39 total customers spoke at the hearing, five were not customers of the Seven Springs area and 15 addressed only water related complaints. The only complaint referred to by OPC in its brief was several years old by a person who was not a customer of the Seven Springs system. All applicable customer complaints and comments were addressed by the utility in its late filed Exhibit No. 2. Upon consideration of the evidence in the record, staff recommends that the quality of service provided by Aloha Utilities, Inc. at its Seven Springs Wastewater Treatment plant is satisfactory.

RATE BASE

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

RECOMMENDATION: Yes. The proposed modifications and expansion of the treatment plant are prudent and justified. (WETHERINGTON)

POSITION OF PARTIES

ALOHA: Yes. They are not only prudent, but they are required pursuant to a Consent Final Judgement with the Florida Department of Environmental Protection and are prerequisites to the utility being allowed to provide reuse service to any paying customer.

OPC: The Citizens do not take issue with Aloha's construction decisions. The Citizens believe, however, that Aloha's modification and expansion projects are sized to serve substantial future growth. Accordingly, U&U adjustments must be made to properly allocate the cost of these projects.

STAFF ANALYSIS: In this case, Aloha is expanding the Seven Springs wastewater treatment plant from 1.2 MGD to 1.6 MGD with full Class I Reliability in order for the effluent to be used for public access reuse. This is being done in accordance with the ARCFJ between DEP and Aloha. (EX 5)

OPC witness Bidy agreed that DEP had instructed Aloha to upgrade the treatment plant for effluent reuse and that this type of reuse required Class I Reliability. (TR 481, 482) Mr. Bidy also agreed that all of the components of Aloha's application were required by DEP by virtue of the fact that DEP granted the permit. (TR 482) No OPC witness offered testimony that the modifications and expansion of the treatment plant were imprudent or unjustified.

Utility witness Porter stated that DEP required all the modifications to the treatment plant prior to allowing effluent reuse. (TR 916) Mr. Porter further stated that every process unit at the treatment plant is sized to provide Class I Reliability as required by DEP. (TR 915)

The ARCEJ required Aloha to comply with the requirements of the permit. (EX 5) Based on the ARCFJ, the DEP permit, the testimony of utility witness Porter and the fact that OPC does not

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take issue with the proposed modifications and expansion, staff concludes that the proposed modifications and expansion of the Aloha Seven Springs wastewater treatment plant are prudent and justified.

ISSUE 3: Are the costs of the utility's infiltration and inflow (I&I) reduction program prudent?

RECOMMENDATION: Yes. The costs of the utility's I&I reduction program are prudent. (WETHERINGTON)

POSITION OF PARTIES

ALOHA: Yes.

OPC: Because the entire costs (including projected future costs) of the I/I reduction program are included in the test year, fairness dictates that the entire effect of the I/I reduction also be recognized. If further I/I reductions are not recognized, neither should the expenditures that are incurred for the purpose of reducing I/I.

STAFF ANALYSIS: The ARCFJ between DEP and Aloha requires Aloha to have an I&I program designed to reduce the collection system infiltration and inflows to the treatment plant. This program is to run until the compliance date described in the ARCFJ. The compliance date is 365 days after the completion date. The completion date is 18 months after the date of the ARCFJ (3/9/99) or the completion of construction, whichever comes first. As a consequence of this program, Aloha receives additional capacity at the treatment plant for the reduction of I&I flows. (EX 5)

OPC did not produce any witnesses who questioned the prudence of the costs of the I&I program. OPC's case of nonprudence is from its brief, in which OPC argues that utility witness Porter testified that the I&I program will result in no further I&I reductions beyond the 140,000 GPD already achieved. It is the pinnacle of imprudent spending to spend \$15,000 per month on a program to reduce I&I that will not reduce I&I. (BR 3)

OPC also states in its brief that if Aloha was convinced that there would be no further I&I reductions resulting from the I&I reduction program, it should have ceased the \$15,000 monthly expenditures immediately. The customers should not bear such wasteful expenditures. If, however, the Commission includes this expenditure in rates, then it should impute further I&I reduction. The Commission should adjust the used and useful (U&U), the electric expense and the chemical expense to reflect the reduced I&I, or it should remove the program expenditures. (BR 3)

The utility states that the cost of the I&I reduction program are prudent and the program was required by the DEP through the ARCFJ. (EX 5) Utility witness Porter testified that there was an additional 30,000 GPD of I&I still in the system. (TR 913)

In the opinion of Mr. Porter, this agreement with DEP was prudent on the part of Aloha, not only because it allowed Aloha to more efficiently provide service to new wastewater customers without constructing new treatment facilities, but also because I&I analysis and reduction is a normal, necessary and prudent part of operating a wastewater collection system. (TR 910) This is why Aloha has, as do all properly managed wastewater utility systems, a program to inspect and repair wastewater line and manhole defects on an ongoing basis. (TR 911)

It is unclear why OPC has stated that Mr. Porter testified that the program will result in no further I&I reductions beyond the 140,000 GPD already achieved when he clearly testified that an additional 30,000 GPD still exists in the system.

Utility witness Porter based his statement of an additional 30,000 GPD of I&I in the system on total system flow isolation studies. (TR 913) OPC witness Bidy stated that he assumed that there was another 140,000 GPD of excessive I&I in the collection system. (TR 416) Since Mr. Porter's testimony is based on actual studies and Mr. Bidy's testimony is based on an assumption, staff believes that the 30,000 GPD figure is more reliable. The 30,000 GPD of I&I is a relatively negligible amount and is not a justification for reducing operation and maintenance costs.

Staff agrees with the utility witness that a properly managed wastewater utility system will have an ongoing program to inspect and repair wastewater line and manhole defects. This, coupled with the requirement for an I&I reduction program in the ARCFJ, leads staff to conclude that the costs of the I&I reduction program are prudent.

ISSUE 4: Should the utility be allowed to capitalize invoices previously expensed?

RECOMMENDATION: 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 depreciation should be reduced by \$73,211. Depreciation expense should also be reduced by \$6,675. (FLETCHER)

POSITION OF PARTIES

ALOHA: Yes, in keeping with longstanding Commission policy and appropriate accounting treatment, these items should be capitalized. The utility did not overearn, even with this change, during any of the years the items were expensed.

OPC: No. The capitalization of these previously expensed items would constitute double recovery and should be disallowed. The Seven Springs wastewater system's plant should be reduced by \$127,232 and accumulated depreciation should be reduced by \$76,548. Depreciation expense should also be reduced by \$6,675.

STAFF ANALYSIS: As indicated in Audit Exception No. 1 of the audit report for this rate case, in 1997, the utility made an adjustment to capitalize certain transactions which were originally classified as O&M expense between the years 1980 and 1991. (EX 11, JAM-1, Page 5; EX 13, TES-1, Page 5) The effect of this adjustment was to add \$232,262 to plant accounts, \$68,671 to accumulated depreciation and to increase the 1997 depreciation by \$9,961. (EX 11, JAM-1, Page 5; EX 13, TES-1, Page 5) Aloha's Seven Springs wastewater system accounted for \$127,232 of the total items capitalized. (EX 13, TES-1, Page 5) By Order No. PSC-99-1917-PAA-WS, issued September 28, 1999, in Dockets Nos. 970536-WS and 980245-WS, the Commission disallowed the utility's capitalization of the items that were expensed prior to the 1997 test year. In the PAA order, the Commission found that the utility shall be allowed to fully contest or litigate its objections to the Commission's decision in its next rate case. According to the audit report for this rate case, the utility did not make any adjustment to remove these items from rate base. (EX 13, TES-1, Page 5)

Staff witness McPherson testified that the utility has already recovered the costs of these items expensed prior to the test year.

(TR 530, 552)(EX 11) Mr. McPherson stated that it is the utility's responsibility to file an application if it is underearning and that the Commission can not open an earnings investigation for prior years due to the prohibition against retroactive ratemaking. (TR 552-553) Mr. McPherson testified that on numerous occasions the Commission has allowed the capitalization of items that were expensed during the test year, but that he did not believe that the Commission had approved such accounting on numerous occasions in years prior to the test year. (TR 532)

Staff witness Stambaugh pointed out that in Order No. PSC-99-1917-PAA-WS, issued September 28, 1999, the Commission found the following:

Pursuant to Rule 25-30.110(5)(d), Florida Administrative Code, the utility certified that its annual reports from 1980 to 1991 fairly presented the financial condition and results of operations for each of those years. We believe that it is inappropriate to capitalize these amounts several years after the fact. We have relied on these reports for purposes of monitoring the utility's earnings level and are precluded by the prohibition against retroactive ratemaking from going back and looking at those prior years to determine if overearnings existed. Therefore, the utility shall be precluded from taking previously expensed items from prior years and changing its accounting treatment. (TR 573)

Mr. Stambaugh testified that the effect of expensing these items in previous years was a reduction of the utility's NOI in those years. (TR 574)(EX 13, TES-1, Page 5) Mr. Stambaugh also testified that, if the utility is permitted to recover the depreciation expense related to this capitalization of previous years expenses, the utility will in a sense be recovering these costs twice, using depreciation expense as the recovery vehicle this time, as compared to O&M expense used in previous years. (TR 574)(EX 13, TES-1, Page 5) Further, Mr. Stambaugh argued that allowing the capitalization of these items would be giving a green light for any utility to manipulate its annual reports in years that it is over earning and then capitalizing such items in future years. (TR 574)

Mr. Stambaugh stated that the Commission often corrects accounting errors in plant additions, but it is not Commission practice to restate prior years earnings. (TR 574) Mr. Stambaugh explained that during audit field work, Commission auditors analyze plant additions since the most recent audit of rate base to verify

the accuracy of the additions; however, expenses for the test year only are analyzed to verify the accuracy of the O&M expenses as a component of NOI for the test year. (TR 574)

OPC witness Larkin agrees with Mr. Stambaugh and Mr. McPherson that the utility has already recovered the costs of the items expensed prior to the test year. (TR 369-370) Mr. Larkin further agrees with Mr. Stambaugh and Mr. McPherson that the Commission can not open an earnings investigation for prior years due to the prohibition of retroactive ratemaking. (TR 371)

Utility witness Nixon explained that the utility's capitalization of items expensed prior to the historical test year was a correction of an error. (TR 779) Mr. Nixon argued that if these items had originally been capitalized in prior years that the earnings would not have pushed Aloha outside the range of its established rate of return. (TR 779)(EX 22, RCN-5) Mr. Nixon testified that the Commission, in Orders Nos. PSC-95-0363-FOF-WS, 10285, and 22150, allowed the capitalization of items expensed prior to the test year on at least three occasions. (TR 802-803)(EX 22, RCN-10) In its brief, the utility stated that in Order No. 24733, issued July 1, 1991, in Docket No. 900521-WS, in the last general rate increase for FFEC-Six Limited, a Class B utility with an average of over \$300,000 in annual revenues each for its water and wastewater systems, adjustments to capitalize previously expensed items were clearly made without any regard to prior year earnings or the other issues addressed by Mr. McPherson or Mr. Stambaugh. (BR 10) Through cross-examination by the utility, Mr. McPherson testified that he was not aware of any rule or Commission order that called for differential treatment by making this type of adjustment based on the size of the utility. (TR 564-565)

Through cross-examination by staff, Mr. Larkin testified that the accounting systems and record keeping of Class C water and wastewater utilities are less sophisticated than Class A or B water and wastewater utilities. (TR 371) Mr. Larkin further testified that Class A or B utilities are more likely to retain accounting consultants than Class C utilities; in fact, he concluded that Class A or B utilities would have a higher level of compliance with the NARUC uniform system of accounts than Class C utilities. (TR 371-372)

Based on arguments of witnesses McPherson, Stambaugh, and Larkin, staff believes that the utility has already recovered the costs of the items expensed prior to the test year and would result in double recovery if these items were allowed to be capitalized. This position is supported by Westwood Lake, Inc. v. Metropolitan

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Dade County Water and Sewer Board, 203 So. 2d 363, 367 (Fla. 3d DCA 1967), in which the court noted that:

Ordinarily, a utility may not capitalize and include in its rate base items which have been accounted for and charged off as operating expenses. This is true because expensed items have been paid for and their costs recovered and the utilities are estopped therefore to capitalize those items which they have already expensed. See *Re Mondovi Telephone Company*, PUR 1933 D 142 (Wisc.Pub.Serv.Com.1932); *RE Los Angeles Gas & Electric Corp.*, PUR 1931 A 132 (Cal.R.R.Com.1930); *Horton v. Badger State Teleph. & Teleg. Co.*, 1 PUR (NS) 409 (Wisc.Pub.Serv.Com.1933).

Further, as indicated on utility witness Nixon's rebuttal exhibit RCN-5, Aloha had a positive return in those priors when the items were expensed. In fact, staff witness McPherson indicated that, for three of the years in question, the utility may have overearned, assuming a 10% authorized rate of return. (TR 552) As such, staff believes this is further support of our position.

Rule 25-30.115, F.A.C., states: "Water and wastewater utilities shall, effective January 1, 1998, maintain their accounts and records in conformity with the 1996 NARUC Uniform System of Accounts adopted by the National Association of Regulatory Utility Commissioners." Staff agrees with Mr. Larkin that Class A or B utilities would have a higher level of compliance with the NARUC uniform system of accounts than Class C utilities. For example, in the Indian Springs Utilities, Inc.'s (Indian or ISUI) 1990 staff-assisted rate case, the Commission found the following: "The utility does not maintain its books and records in conformity with 1984 NARUC Uniform System of Accounts. This resulted in our making numerous adjustments to each account." Order No. 24211, issued March 11, 1991, in Docket No. 900604-WS. Further, in this order, the Commission ordered Indian to comply with Rule 25-30.115, F.A.C., but did not fine this utility for its non-compliance with the NARUC USOA.

In ISUI's 1992 staff-assisted rate case, the Commission once again found that Indian did not maintain its books in conformance with the NARUC USOA during the test year. See Order No. PSC-93-1823-FOF-WS, issued December 23, 1993, in Docket No. 920767-WS. Specifically in Order No. PSC-93-1823-FOF-WS, the Commission found the following:

The utility is relatively small, serving less than 100 customers per system. Although the utility has failed to comply with the previous Commission order regarding its compliance with the USOA, the utility has stated that it now employs a bookkeeper with the expertise necessary to convert and maintain the utility's records in conformity with the above-referenced rule. Based on the foregoing, we hereby admonish the utility for failing to comply with the previous Commission Order regarding USOA,....

Based on staff's reading of Section 367.0814, Florida Statutes, staff believes the legislative intent of this statute was to provide more regulatory assistance to Class C utilities. Subsection 1 of this statute states that "the commission may establish rules by which a water or wastewater utility whose gross annual revenues are \$150,000 or less may request and obtain staff assistance for the purpose of changing its rates and charges." Rule 25-30.115, F.A.C., defines a Class C utility to be a water or wastewater utility having annual water or wastewater revenues of less than \$200,000. Based on the above, staff believes that by statute and through Commission practice, Class C utilities are given differential treatment due to their size and level of regulatory sophistication.

With regard to the three orders referenced by utility witness Nixon's exhibit RCN-10, staff agrees that the Commission did capitalize items that were expensed prior to the test year in those proceedings. However, staff notes that these three orders involved Class C utilities. Although it was not discussed in these three orders, as stated above, staff believes differential treatment is given to Class C utilities due to their size and level of regulatory sophistication. As such, staff believes it was appropriate to make those adjustments because they are Class C utilities.

The first order involved a staff-assisted rate case by Fisherman's Cove of Stuart, Inc. (Fisherman or FCOSI) in Marion County. In this docket, FCOSI reported test year-end water rate base of \$205,658 and a test year-end wastewater rate base of \$190,652. Further, the Commission noted that Fisherman only had total water revenues of \$94,842, with an operating income of \$3,985, and total wastewater revenues of \$132,860, with an operating income of \$942 for the test year. See Order No. PSC-95-0363-FOF-WS, issued March 14, 1995, in Docket No. 940768-WS.

The second order involved a rate case by Gulf Coast Utility Company, Inc. (Gulf or GCUCI) in Hernando County. In this docket,

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GCUCI reported a test year-end water rate base of \$46,163 and a test year-end wastewater rate base of \$29,355. Further, the Commission noted that for the water and wastewater systems combined, Gulf was operating at a loss of \$22,156 which reflects that Gulf was not recovering all of its expenses. See Order No. 10285, issued September 9, 1981, in Docket No. 790789-WS.

The third order involved a certificate transfer case by Point O' Woods Utilities, Inc. (Point or POW) in Citrus County. In this docket, POW reported a test year-end water rate base of \$144,146 and a test year-end wastewater rate base of \$200,377. Point was serving only 312 water customers and 74 wastewater customers. See Order No. 22150, issued November 6, 1989, in Docket No. 890233-WS.

As stated earlier, the utility argued that the Commission allowed the capitalization of expensed items prior to the test year in the last general rate increase for FFEC-Six Limited, a Class B utility with average revenue of over \$300,000 in annual revenues each for its water and wastewater systems. According to Order No. 24733, FFEC-Six Limited reported a test year-end water rate base of \$1,093,793 and reported a test year-end wastewater rate base of \$1,606,752. Based on the forgoing, the total water and wastewater rate base reported by Fisherman, Gulf and Point is \$816,351. Given the size of FFEC-Six Limited, staff believes that it should have been held to a higher standard than Fisherman, Gulf or Point with regard to the capitalization of the items expensed prior to the test year. As a result, staff believes that the adjustment should not have been allowed.

Based on the above, staff recommends that the capitalization of these previously expensed items would constitute double recovery and should be disallowed. See Westwood Lake, Inc., 203 So. 2d at 367. Thus, the Seven Springs wastewater system's plant should be reduced by \$127,232 and accumulated depreciation should be reduced by \$73,211. Depreciation expense should also be reduced by \$6,675.

ISSUE 5: Should the Commission consider the new office building cost for the utility in this rate proceeding?

RECOMMENDATION: No. Based on the evidence in the record, staff cannot determine that the purchase of the building was the most cost effective alternative. As such, staff recommends that all the requested costs associated with the purchase of the building should not be considered in this rate proceeding. (FLETCHER, WILLIS)

POSITION OF PARTIES

ALOHA: Yes. Because of the unforeseen requirement of the utility to vacate its main office building, the utility will incur substantially higher costs for obtaining new office space. This change was unknown and unforeseeable at the time the application and direct testimony were filed. The need and reasonableness of the price paid have been demonstrated. This known change should be recognized.

OPC: The Commission should not allow Aloha to recover the cost of the new office building because the utility has not justified the costs. The Commission gave the utility more than ample opportunity but Aloha failed to carry its burden of proof.

STAFF ANALYSIS: In its MFRs, the utility requested recovery of rental expense of its office building from a related party. (EX 5, MFRs Vol. I, Schedule B-12, Pages 58 and 59) By Order No. PSC-00-1747-PHO-SU, the Prehearing Officer granted Aloha's Motion to Allow Filing of Supplemental Direct Testimony with the Supplemental Direct Testimony of Stephen G. Watford attached as Attachment A with exhibit SGW-1. The Order also allowed the Executed Contract for Sale of New Office Building submitted on September 15, 2000, to be identified as exhibit SGW-2. The Order also struck the rebuttal testimony of Stephen G. Watford, concerning the new office building, beginning at page 2, line 20, and going through page 6, line 15.

In his supplemental direct testimony, Mr. Watford explained the reasons why Aloha needed to change office location, including: 1) its related party from whom Aloha was renting the old office building, informed the utility in June, 2000 that it would not be renewing Aloha's lease at the end of the December 31, 2000 calendar year; 2) an American Disabilities Act lawsuit had been filed against the utility stating that the current building did not comply with the Act and which Aloha asserts was not modifiable to

comply with the Act; and 3) Aloha was short of space needed to house its current staff and its expected future employee needs. (TR 988-989) Mr. Watford provided an executed contract for the purchase of the building and estimated the costs of real estate taxes, insurance, and maintenance expenses associated with the purchase. (TR 989-992)(EX 23)

In her supplemental direct testimony, staff witness Merchant stated that she could not support a position on the prudence of the purchase of the building or whether the utility's requested costs represent the most cost effective alternative. (TR 680) Ms. Merchant explained that her basis for this was as follows: 1) no information or costs related to the new building was in its MFRs; 2) in Aloha's response to staff Interrogatory No. 10(a), Aloha informed staff, three months after the official filing of this docket, that the utility was going to relocate its office and stated that the estimated costs for the relocation of its building would be substantially greater than its current rent expense; and 3) the utility only suggested that the Commission should consider the new building in this rate case, but Aloha made no formal request for such recovery. (TR 680-681) Ms. Merchant noted that in staff Interrogatory No. 10(a) the utility listed several different areas where property was available for either lease or purchase, but she was unable to determine the cost of all the properties and why the utility determined that these locations were not suitable for the utility. (TR 681-682)

Ms. Merchant stated that, on October 5, 2000, staff propounded Interrogatory No. 58 and Request for Production of Documents Request No. 13 which asked if the utility had performed any cost benefit analysis to determine whether it should purchase or lease a building. (TR 682) She noted that the utility's initial response through its attorney, by letter dated October 9, 2000, stated that no such cost benefit has been performed by the utility in writing and that the utility's review did not rise to the level of a cost benefit analysis. In the utility's formal response to staff's Interrogatory No. 58 and Request for Production of Documents Request No. 13, Ms. Merchant noted that Aloha stated that an analysis was performed at the request of the utility's president. (TR 682) She stated that this analysis compared its incremental cost of the purchased building to the old lease cost with its related party. (TR 683) Further, Ms. Merchant stated that this analysis also compared the incremental cost of the purchased building to an average cost to lease comparable space, but the utility did not provide any actual comparisons of property that were available for lease or purchase. (TR 683) As a result, she concluded that there was no reasonable basis on which to determine

whether the utility made a prudent and cost effective choice in deciding to buy this building. (TR 683)

Ms. Merchant testified that she does not believe it was prudent for the utility to purchase a building without performing a cost benefit analysis. She believed that Aloha should have documented the minimum requirements for its new office location. Further, Ms. Merchant stated that examples of the minimum requirements were as follows: 1) size, location, availability, cost and whether the property was available for purchase or lease; 2) research and compile a list of all the available properties that fit the minimum criteria established; 3) compare each of the alternatives and document the advantages and disadvantages of each property; 4) any found to be unsatisfactory should have been documented and removed from the list; 5) all the attributes of the acceptable locations should have been detailed and documented so that an appropriate decision could have been made based on these facts. (TR 683-684)

Ms. Merchant expressed additional concerns that the costs in the utility's response to staff's Production of Documents Request No. 13 were in excess of those costs in the supplemental direct testimony of utility witness Watford. (TR 684) She also testified that the utility's additional requested costs associated with the building for improvements, new furniture, relocation of its phone system, maintenance, real estate taxes, and insurance were not supported. (TR 684-685) Lastly, with regard to the utility's value of land associated with this building in its calculation of the revenue impact, Ms. Merchant disagreed with Aloha's estimation of land using the prior property tax assessed value escalated by 25%. She noted that Aloha did not provide the reason why it used this methodology, nor did it provide a copy of the prior property tax bill. (TR 685) Ms. Merchant stated that this method is not a reliable method for determining the current market value of the land and that the appraisal of the land that is required for financing the property would support the amount the utility paid for the land and the building. (TR 685)

In his supplemental rebuttal testimony, Mr. Watford noted that the letter from their attorney initially responding to staff's discovery regarding a cost benefit analysis was a courtesy letter attempting to help the staff with as much information as quickly as possible. (TR 1102) He further noted that, in an attempt to provide the best information, he instructed a subsequent cost analysis be performed. (TR 1103) In their supplemental testimony, utility witnesses Nixon and Watford noted that the utility's

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detailed cost analysis supports the purchase of the building. (TR 1054, 1102-1103)

Through cross examination by the utility, Ms. Merchant stated that a cost benefit analysis is not required, but that if the utility wants a major item in its rate case, then the utility should submit documentation to show that the steps the utility went through and its final actions were prudent. (TR 740-741)

Staff agrees with the utility that the utility has to relocate its office due the non-renewal of its lease. However, it is the utility's burden to prove that its costs are reasonable. Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982). Staff is persuaded by Ms. Merchant's testimony. There is insufficient evidence to determine that the purchase of the building was the most cost effective alternative. As such, staff recommends that all the requested costs associated with the purchase of the building should not be considered in this rate proceeding.

ISSUE 6: Does Aloha have excessive infiltration and inflow?

RECOMMENDATION: Aloha does not have excessive I&I. (WETHERINGTON)

POSITION OF PARTIES

ALOHA: No. The utility's infiltration and inflow is minimal, well below engineering standards and deemed by DEP to be not excessive.

OPC: Yes, Aloha does have excessive infiltration and inflow (I/I), and is currently undertaking a project to reduce its I/I. The entire costs (including projected future costs) have been included in the projected test year. Accordingly, the results of the I/I reduction should also be considered in the flows for calculating U&U.

STAFF ANALYSIS: In his testimony OPC witness Bidy stated that it is not unreasonable to assume that another 140,000 GPD of I&I exists in the Aloha system beyond the 140,000 GPD already found. (TR 408) He further assumed that after the system was repaired and the total 280,000 GPD of excessive I&I had been removed, an allowable I&I of 56,000 GPD would remain in the system. (TR 417) Mr. Bidy's calculation of the allowable I&I in the system was based on the standard in the Ten State Standards document which stated the allowable I&I was 200 GPD per inch of diameter per mile of pipe. (TR 406, 407) Mr. Bidy stated that this standard is enforced by DEP for both new construction and rehabilitated systems. (TR 434)

Utility witness Porter testified that 140,000 GPD of I&I had been identified in the system by flow isolation studies and removed. (TR 913) He further stated that the flow isolation studies indicated that a maximum of 30,000 GPD may remain in the system. (TR. 913)

DEP witness MacColeman when asked if Aloha had excessive I&I stated that DEP has no opinion as to whether or not the I&I in the Aloha system was excessive. (TR 499)

Staff notes that Mr. Bidy's testimony concerning excessive I&I is admittedly a simple doubling of the known 140,000 GPD figure and then the addition of the calculated 56,000 GPD amount. None of these figures or assumptions is supported by field study. Mr. Porter's testimony showing 140,000 GPD of I&I, since removed from

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the system, and an additional 30,000 GPD of I&I remaining in the system is supported by field study.

DEP witness MacColeman when asked about excessive I&I in the Aloha system did not make reference to the Ten State Standards which Mr. Biddy stated was enforced by DEP as the applied standard in this case. Under cross-examination, Mr. Biddy testified that the section of the Ten State Standards that he was applying to the Aloha system was entitled Design of Sewers. (TR 433) In Order No. PSC-96-1320-FOF-WS, Mr. Biddy was reported to have stated that the Ten State Standards guideline is a more appropriate guideline for new systems. These facts and testimony lead staff to believe that the Ten State Standards document is not the standard for excessive I&I enforced by DEP in this case.

Staff believes that the 30,000 GPD of I&I remaining in the system documented by Mr. Porter's field studies is the most reliable figure presented in the testimony. For a collection system the size of Aloha's this is a negligible figure and does not even violate the calculated standard for new systems (56,000 GPD) shown in the Ten State Standards. Staff recommends that this indicates that there is no excessive I&I in the Aloha collection system.

ISSUE 7: What is the used and useful percentage of the wastewater treatment plant and the wastewater collection system?

RECOMMENDATION: Staff recommends that the wastewater treatment plant and the wastewater collection system are both 100% U&U. (CROUCH)

POSITION OF PARTIES

ALOHA: Both the wastewater treatment facilities and the collection system are 100% U&U, along with all trunk lines and associated maintenance expenses. The entire wastewater treatment plant is an integral part of the reuse facilities and the collection system is 100% contributed.

OPC: The WWTP should be considered 72.97% U&U, with the exception of the equalization tank and the new headworks, which should be considered 48.65%. The wastewater collection system should be considered 78.7% U&U.

STAFF ANALYSIS: Chapter 367.081(2)(a)1., Florida Statutes, states that:

The commission shall, either upon request or upon its own motion, fix rates which are just, reasonable, compensatory, and not unfairly discriminatory. In every such proceeding, the commission shall consider . . . operating expenses incurred in the operation of all property used and useful in the public service; and a fair return on the investment of the utility in property used and useful in the public service.

Further, Chapter 367.081 (2)(a)2.c. states that:

Notwithstanding the provisions of this paragraph, the commission shall approve rates for service which allow a utility to recover from customers the full amount of environmental compliance costs. Such rates may not include charges for allowances for funds prudently invested or similar charges. For the purpose of this requirement, the term "environmental compliance costs" are defined as all reasonable expenses and fair return on any prudent investment incurred by a utility in complying with the requirements or conditions contained in any permitting enforcement or similar decision of the United

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States Environmental Protection Agency, the Department of Environmental Protection, a water management district, or any other governmental entity with similar regulatory jurisdiction. (Emphasis added)

Wastewater Treatment Plant

Aloha's existing 1.2 MGD wastewater treatment system was not capable of handling the existing customer load. Consequently, Aloha was not in compliance with its permit. (TR 497) Aloha was ordered by DEP through the ARCFJ to build a wastewater treatment plant providing Class I Reliability and effluent capable of reuse in areas where human contact is authorized. (EX 5, Vol. III, Pg 184) The utility submitted plans, which DEP approved, to build an interim plant with 1.6 MGD capacity to replace the existing 1.2 MGD plant. (EX 7, SCH F-6) Eventually, this interim plant will be expanded to 2.4 MGD under the requirements of the ARCFJ.

According to Section 367.081, Florida Statutes, the Commission shall consider the utility's investment in property U&U in the public service [its customers], and the Commission shall approve rates to recover all prudent investment by the utility. It is staff's recommendation that the construction of the new wastewater treatment plant with Class I Reliability and capable of providing effluent reusable in areas with human contact was ordered by DEP. Environmental Protection Agency's document EPA-430-99-74-001, Design Criteria for Mechanical, Electric, and Fluid System and Component Reliability, page 15, states that a Wastewater Treatment System includes all components from and including the bar screen and wastewater pumps to and including the works outfall. Pages 19-24 detail the specific requirements for Class I Reliability. Summarizing the EPA document: Class I Reliability essentially requires 100% backup for all primary components in the treatment chain.

OPC argues that the equalization tanks and the new headworks are two new plant components that were designed for the ultimate capacity of 2.4 MGD (TR 409) which is more than twice the capacity that will be needed even five years after the projected test year. OPC recommends a U&U percentage of 48.65 for those two components. (TR 410) OPC also argues that the treatment plant is sized to serve customers which will come on line after the five-year growth required by statute; therefore, the plant should be considered 72.97% U&U. (TR 409) OPC witness Bidy testified that, in his opinion, anything regarding this project that is designed and implemented but will not be used until after the five-year horizon is automatically imprudent. (TR 455) Mr. Bidy bases much of his

U&U argument on the claim that the utility has excessive I&I. Therefore, adjustments in operating expenses and U&U percentages for the treatment plant are required. (TR 407-409) The I&I quantity is discussed in Issue 6.

Aloha states in its brief that there is no credible evidence in this proceeding that a U&U adjustment for either the wastewater treatment plant or the wastewater collection system is appropriate or justified. (BR 19) The utility's position, as stated by witness Porter, is that each and every process unit provided at the wastewater treatment plant was sized to provide Class I Reliability as required by DEP rules. (TR 915)(SCH F-6, EX 7) In addition, these process units are also considered part of a reuse system and therefore were 100% U&U (TR 915) under Section 367.0817(3), Florida Statutes, which states: All prudent costs of a reuse project shall be recovered in rates.

When asked if the [existing 1.2 MGD] wastewater collection, treatment and disposal facilities were adequate to serve present customers based upon permitted capacities, staff witness MacColeman, an employee of DEP, stated that the interim [1.6 MGD] wastewater plant improvements which are being constructed will increase the plant capacity to meet current flows from the present customers. (TR 497) In other words, the existing 1.2 MGD plant could not meet existing demand. The new, interim, 1.6 MGD plant ordered under the ARCFJ will meet existing demands.

From the evidence in the record, it is obvious that DEP ordered Aloha to build a new plant with Class I Reliability and capable of providing effluent which could be reused in areas with human contact. Aloha submitted plans, which DEP approved and permitted, for an interim 1.6 MGD plant. According to Section 367.081(2)(a)2.c, Florida Statutes, these improvements should be considered 100% U&U because they were mandated by DEP. These improvements would also be considered 100% U&U under Section 367.081(3), Florida Statutes, since the improvements were made to provide reuse. Therefore, because this system is properly sized and prudent, staff recommends that it be considered 100% U&U.

Collection System

The majority of the wastewater collection system was contributed by the developers of the individual subdivisions to the utility. (EX 7, SCH F-7)(TR 901-902) It is Commission practice that contributed lines are considered 100% U&U. In addition, staff normally considers the lift stations and force mains which carry the wastewater from each subdivision back to the treatment plant

to be 100% U&U because they are required to serve an established development or subdivision and are sized according to DEP requirements in order to support the contributed lines. (See Order No. PSC-97-0847-FOF-WS, Docket No. 960329-WS, Issued July 15, 1997)

OPC witness Bidy argues that the Commission should apply the ratio of "currently connected" lots to total available lots that can be served by existing lines. (TR 405) According to OPC, the collection system should be 78.7% U&U.

Utility witness Porter, in his rebuttal testimony, gives considerable explanation as to the fact that the vast majority of the collection system is contributed and therefore 100% U&U (TR 901-902). Utility witness Porter further explains that it would be imprudent to attempt to build sewer lines for anything less than the total expected number of customers. The marginal cost of increasing the size of the line is small whereas the cost of adding a parallel sewer line to the first line would be very large. (TR 904) Aloha states that the collection system is essentially 100% contributed and therefore 100% U&U. (EX 7, SCH F-7)(TR 901-902)

Since the collection system is either contributed or consists of force mains back to the treatment plant, no lot count or ERC to ERC ratio is required. Contrary to the position of OPC, the ratio of "currently connected" lots to total available lots that can be served by existing lines (TR 405) is neither necessary nor appropriate.

Conclusion

From the evidence presented, Aloha has shown that the utility has installed a 1.6 MGD interim plant which meets Class I Reliability requirements and provides high quality, reusable effluent in accordance with DEP orders and the ARCFJ. The utility has shown that both the improvements and expansion were required pursuant to the ARCFJ and that they are for the provision of reuse. Moreover, the utility has shown that the plant was prudent and properly sized and approved and permitted by DEP. Therefore, pursuant to the requirements of Section 367.081(2)(a)2.c. and 367.0817(2), Florida Statutes, staff recommends that the wastewater treatment plant is 100% U&U. The collection system is essentially contributed. Staff also recommends that the wastewater collection system be considered 100% U&U.

ISSUE 8: Should a used and useful adjustment be applied to the reuse facilities?

RECOMMENDATION: No. Section 367.0817(3) Florida Statutes requires that "All prudent costs of a reuse project shall be recovered in rates". (CROUCH)

POSITION OF PARTIES

ALOHA: No. All reuse facilities are required to be recovered in rates, pursuant to Section 367.0817, Florida Statutes and Section 403.064, Florida Statutes. In addition, even by traditional methods applied to non-reuse facilities (sic) were applied to these reuse facilities they are still 100% U&U.

OPC: Although the Citizens are philosophically opposed to requiring current customers to subsidize Aloha's anticipated growth, OPC is no longer seeking a U&U adjustment for the reuse facilities.

STAFF ANALYSIS: Staff agrees with OPC and the utility that no adjustments should be made to the reuse facilities. Pursuant to Section 367.0817(3), Florida Statutes, "[a]ll prudent costs of a reuse project shall be recovered in rates."

Section 403.064(10)., Florida Statutes states:

Pursuant to Chapter 367, the Florida Public Service Commission shall allow entities under its jurisdiction which conduct studies or implement reuse projects, including, but not limited to, any study required by subsection (2) or facilities used for reliability purposes for a reclaimed water reuse system, to recover the full, prudently incurred cost of such studies and facilities through their rate structure.

No party proposes a U&U adjustment to the reuse facilities in this rate case. Staff, therefore, recommends that no U&U adjustment be applied to Aloha's reuse facilities.

ISSUE 9: Are any adjustments necessary to test year CIAC and accumulated amortization of CIAC for changes in projection methodology?

RECOMMENDATION: Consistent with staff's recommendation in Issue 18, CIAC and accumulated amortization of CIAC should be increased by \$7,387 and \$273, respectively. (FLETCHER)

POSITION OF PARTIES

ALOHA: No such adjustments are appropriate unless the Commission accepts Mr. Stallcup's testimony.

OPC: The Citizens take no position on this issue.

STAFF ANALYSIS: The utility projected its CIAC through the September 30, 2000 intermediate test year and the September 30, 2001 final test year, based on its current approved plant capacity charge and estimated growth of 370 ERCs for the intermediate period and 349 ERCs for the final test period. (EX 5, MFRs Vol. I, Schedule G-1, page 135) The growth in the ERCs was based on the utility's regression analysis, which yielded a customer growth factor of 1.04812. (EX 5, MFRs Vol. I, Schedules F-10 and G-1, pages 133 and 135) As discussed in Issue 18, staff has recommended that the appropriate growth factor is 1.03486, which represents 316 ERCs for the intermediate period and 368 ERCs for the final test year. As a result, staff recommends that CIAC should be reduced by \$7,387 and accumulated amortization of CIAC should be reduced by \$273.

ISSUE 10: What is the appropriate regulatory treatment of contributed taxes (CTs) and accumulated deferred income taxes?

RECOMMENDATION: Consistent with staff's recommendation in Issue 32, staff recommends that the September 30, 2001 13-month average test year should be adjusted as follows: 1) CTs of \$1,544,865 for the Seven Springs wastewater system should be reflected as CIAC and included in rate base; 2) the amortization of these CTs of \$295,878 should be reflected as accumulated amortization of CIAC and also included in rate base; 3) the Seven Springs wastewater system's U&U debit deferred income taxes of \$1,084,985 should be offset with its U&U credit deferred income taxes of \$578,619; 4) the net debit balance of \$506,367 should be included as an addition item to rate base for the Seven Springs wastewater system. Staff also recommends that credit deferred income taxes of \$770,040 should be removed from the capital structure. (FLETCHER)

POSITION OF PARTIES

ALOHA: These should be given the treatment required by PSC Orders 23541 and 16971 and as per Nixon's Rebuttal Testimony.

OPC: The Citizens agree with the testimony of Mr. McPherson that the CTs should be reflected as CIAC and fully included for the calculation of rate base.

STAFF ANALYSIS: The utility grossed-up CIAC to pay tax on CIAC from 1987 to 1996 for its Seven Springs water and wastewater systems. (EX 5, MFRs Vol. I, Schedules G-6, page 160) As indicated in Audit Disclosure No. 7 of this rate case, the utility included the \$475,501 of deferred tax liabilities in its capital structure for the 13-month average year-end September 30, 1999, but the utility did not include the deferred tax assets (DTAs) or CIAC that was grossed up for income taxes in either its capital structure or rate base schedules. (EX 13, TES-1, Page 16)

Staff witness McPherson pointed out that Rule 25-30.433(3), F.A.C., states:

Used and useful debit deferred taxes shall be offset against used and useful credit deferred taxes in the capital structure. Any resulting net debit deferred taxes shall be included as a separate line item in the rate base calculation. Any net credit deferred taxes

shall be included in the capital structure calculation.
(TR 509)

Under the heading Accounting/Regulatory Treatment With Gross-Up of Order 23541, issued October 1, 1990, in Docket No. 860814-PU, Mr. McPherson pointed out that the Order states that all witnesses who testified agreed that normalization accounting should be followed when a utility does gross-up. (TR 509-510) Under the same heading, Mr. McPherson noted that the Order states in part the following:

We still believe that full normalization accounting should be utilized. This would result in consistent treatment between utilities that are not grossing-up and those that are. In addition, those utilities that switch from grossing-up to not grossing-up will maintain the same normalization methodology. . . . As discussed above, normalization involves offsetting debit deferred taxes against credit deferred taxes in the capital structure with any net debit deferred balance included in rate base. (TR 509-510)

Mr. McPherson also noted that Order No. 11487, issued January 5, 1983, in Docket No. 820014-WS, states in part the following:

. . . the utility has also reduced CIAC by the amount of income taxes paid on connection fees, which were included as income for tax purposes. We believe that connection and tap fees should be considered CIAC, not revenue. Therefore, we have increased CIAC for the water system by \$26,690 and \$26,199 for the sewer system. (TR 510-511)

Mr. McPherson stated that the USOA for Class A wastewater utilities describes the amounts that should be recorded in Account 271 for CIAC. (TR 511) Specifically, under item 4 of the USOA's description of CIAC, it states in part the following:

Any amount of money received by a utility, any portion of which is provided at no cost to the utility, which represents an addition or transfer to the capital of the utility and which is utilized to offset the federal, state or local income tax effect of taxable contributions in aid of construction . . . shall be reflected in a sub-account of this account.

Mr. McPherson testified that the utility did not include the gross-up portion of CIAC with the other CIAC in its MFRs rate base

schedule and did not net DTAs (debits) against deferred tax liabilities (DTLs) (credits) in its capital structure as required by the USOA and Commission orders. (TR 511) Mr. McPherson believes all CIAC, whether grossed-up for tax or not, should be treated consistently, which means it should be included in rate base. (TR 511) In addition, he believes Aloha's DTAs should be offset against its DTLs in the utility's capital structure with any net debit balance included in rate base. (TR 511) Using the percentage of the Seven Springs water system CTs and the Seven Springs wastewater system CTs to total CTs, Mr. McPherson allocated the net DTAs. (TR 512)(EX 11, JAM-2) Based on the above, Mr. McPherson recommended that the September 30, 1999 13-month average balance of Aloha's Seven Springs wastewater system should be adjusted as follows: CIAC should be increased by \$1,544,865, accumulated amortization of CIAC should be increased by \$171,681, and the net DTAs of 1,003,170 should be included in rate base. (TR 512)(EX 11, JAM-2)

Utility witness Nixon argued that Order No. 16971, issued December 18, 1986, in Docket No. 860184-PU, states in part "The amount of CIAC Tax Impact collected by a utility shall not be treated as CIAC for ratemaking." (TR 807) He stated that Order No. 23541 is silent on the issue of CTs on CIAC for ratemaking. (TR 809) Mr. Nixon asserted that Mr. McPherson's reliance on Order No. 11487 is misplaced support of his position because meter fees have always been taxable forms of CIAC and that Aloha has never reduced any form of CIAC for taxes paid as was done by the utility in that Order. (TR 510-511, 809-810)

In light of the Commission's finding in Order No. 16971 that contributed tax is not CIAC for ratemaking, Mr. Nixon testified that Rule 25-30.433(3), F.A.C., should be modified in the interest of customer fairness. (TR 807, 811-812) Mr. Nixon asserted that the DTAs created by the taxation of CIAC should not be included as a separate rate base item or used to reduce DTLs because a full gross-up company does not have any basis in these DTAs. (TR 817) Mr. Nixon stated that Order No. 23541 states that "Under the full gross-up method, the debit-deferred taxes would be fully offset by the contributed taxes." He contended that what this language does is eliminate any DTAs which were paid for with CTs from the ratemaking equation. (TR 812) Further, Mr. Nixon testified that Order No. 23541 requires that the benefits of tax depreciation on CIAC should be passed back to the ratepayers and that the mechanism by which these benefits are passed back is through DTLs in the capital structure.

Mr. Nixon testified that the utility's CTs do not offset the DTAs created by the taxation of CIAC because the utility did not begin amortization of CTs until Aloha received an Order from the Commission as to the appropriate amount of the refund pursuant to Order No. 23541. (TR 814) He asserted that if the amortization of CTs had begun in the year received, without waiting for a Commission order, then the amounts in the two accounts would virtually offset each other. (TR 814)(EX 22, RCN-11, pages 6 and 34) In addition, Mr. Nixon argued that since this is a wastewater rate case only DTAs on meter fees should be ignored. (EX 22, RCN-11, pages 5)

In its brief, the utility pointed out that, through cross-examination by the utility, Mr. McPherson agreed that he was not involved in the docket or hearings that led up to the issuance of Order No. 23541, that he did not review the records of those proceedings other than orders themselves, and that the wording in Order No. 16971 was directly contrary to his proposal. (TR 540-541)(BR 23) The utility further argued that its tariffs approved by the Commission during the period of time Aloha was authorized to gross-up and after the issuance of Order No. 23541 contained the language in Order No. 16971 barring treatment of CTs as CIAC for ratemaking purposes. (TR 543-547, 807)(EX 12)(BR 24)

Through redirect examination, staff witness McPherson testified that Order No. 23541 superseded Order No. 16971 and that Order No. 23541 is the binding order regarding the accounting and regulatory treatment for utilities that grossed-up CIAC. (TR 557-559) Mr. McPherson stated that the issuance of Order No. 16971 was expedited because the tax law was set to take effect January 1st of the following year. (TR 558) In fact, Mr. McPherson noted that the Commission stated in Order No. 16971 that "[t]his docket shall remain open to handle any generic problems that arise in accounting for the CIAC." (TR 558, Lines 6-8) In addition, Mr. McPherson pointed out that Order No. 21266, issued May 22, 1989, specifically states "[s]ince Order 16971 was issued on an expedited, emergency basis, we instructed the staff of this Commission to continue to investigate the necessity and appropriateness of the gross-up." (TR 558, Lines 11-15)

In addition to his direct testimony, Mr. McPherson pointed out three additional findings in Order No. 23541 that he believed bolsters his recommended treatment. (TR 558-560) First, he noted that, on page 18, it states in part the following: "[h]owever, in order to identify the different contributions and to properly normalize, utilities will have to, and we find it appropriate to require them to record the gross-up in a separate subaccount." (TR

558, Line 23 through TR 559, Line 2)(EX 3, Order No. 23541) Mr. McPherson contended that if CTs were required to be in the same account as other contributions, that implies, at least, that they should be treated the same as other contributions. (TR 559) Second, he noted that, on page 8, it states in part the following: "Further, in a rate proceeding, all CIAC will be considered in the reduction of the utility's rate base." (TR 559, Lines 10-13) Mr. McPherson argued that it did not provide for any exception for grossed-up CIAC to be included. (TR 559) Finally, he noted that, on page 17, it states in part the following: "Under the full gross-up method, the debit-deferred taxes would be fully offset by the contributed taxes." (TR 559; TR 560, Lines 5-7) Mr. McPherson contended that the only place the CTs can offset deferred taxes is in rate base which means that the CTs have to be included in rate base. (TR 560)

Based on its review of Orders Nos. 16971, 21266, and 23541 and the arguments presented by Mr. McPherson, staff agrees that his proposed treatment is appropriate. Further, since Mr. McPherson's adjustments are reflected for the historical September 30, 1999 13-month average balances, any adjustments should be based on the September 30, 2001 13-month average balances because that is the test year upon which final rates will be set. Staff agrees with Mr. Nixon that the effect of the full gross-up method would result in no ratemaking impact because the CTs included as CIAC in rate base would be virtually offset by the debit-DTAs related to the CTs included in rate base.

However, for this utility, staff points out that the primary reason why the debit-DTAs related to grossed-up CIAC and CTs do not offset is because the utility did not begin amortizing its CTs in the year they were received. (TR 814, 842-843) With regard to Mr. Nixon's argument that Aloha was waiting to receive an order from the Commission as to the appropriate amount of the refund pursuant to Order No. 23541, staff notes that there is no Commission directive in that Order requiring a utility to wait for a refund order before amortizing CTs. Further, as discussed in Issue 32, the utility amortized its CTs at a 2.5% rate, instead of 3.06%. This resulted in a lesser annual amortization amount than the ratepayers were entitled to. Both of these actions are contrary to the Commission's directive in Order No. 23541 that the benefits of CTs shall be passed back to the ratepayers over the lives of the related assets.

With regard to Mr. Nixon's proposed exclusion of DTAs on meter fees because this is a wastewater rate case only, staff agrees in part. However, staff is unable to remove these DTAs because the

record does not reflect what the corresponding DTLs associated with the DTAs on meter fees are. Moreover, staff believes that it would be more appropriate to determine any net debit or credit deferred tax balance for the Seven Springs wastewater system, using only the deferred tax associated with this system. Further, Exhibit 24 is the utility's breakdown of deferred tax assets and deferred liabilities for each of Aloha's divisions. Using Exhibit 24, staff is able to determine any net debit or credit deferred tax balance specifically associated with the Seven Springs wastewater system.

Based on the above and consistent with staff's recommendation in Issue 32, staff recommends that the September 30, 2001 13-month average test year should be adjusted as follows: 1) CTs of \$1,544,865 for the Seven Springs wastewater system should be reflected as CIAC and included in rate base; 2) the amortization of these CTs of \$295,878 should be reflected as accumulated amortization of CIAC and also included in rate base; 3) the Seven Springs wastewater system's U&U debit deferred income taxes of \$1,084,985 should be offset with its U&U credit deferred income taxes of \$578,619; 4) the net debit balance of \$506,367 should be included as an additional item to rate base for the Seven Springs wastewater system. The following schedules illustrates our adjustments. Further, the utility prorated its total company deferred tax credits of \$770,040 to the Seven Springs wastewater system's rate base. (EX 5, MFRs Vol. I, Schedule D-2(A), page 93) As such, consistent with our recommendations above, staff also recommends that credit deferred income taxes of \$770,040 should be removed from the capital structure. This adjustment is depicted on Schedules 2-A and 2-B.

Contributed Taxes

Purpose: To calculate September 30, 2001 13-Month Average Balance of Contributed Taxes, using staff's recommended amortization rate in Issue 32.

	<u>Contributed Taxes</u>	<u>Amortization Rate</u>	<u>Annual Amortization</u>
Seven Springs Water System (SS W)	\$1,175,890	3.06%	\$35,982
Seven Springs Wastewater System (SS WW)	<u>1,544,865 (1)</u>	3.06%	<u>47,273</u>
	<u>\$2,720,755</u>		<u>\$83,255</u>
Total			
<u>Intermediate Projected Test Year</u>	<u>Utility</u>	<u>SS W</u>	<u>SS WW</u>
9/30/99	\$2,325,180 (2)	\$170,607	\$224,968
10/31/99	2,318,242	173,606	228,908
11/30/99	2,311,304	176,604	232,847
12/31/99	2,304,366	179,603	236,786
01/31/00	2,297,428	182,601	240,726
02/28/00	2,290,490	185,600	244,665
03/31/00	2,283,552	188,598	248,605
04/30/00	2,276,614	191,597	252,544
5/31/00	2,269,676	194,595	256,483
6/30/00	2,262,738	197,594	260,423
7/31/00	2,255,801	200,592	264,362
08/31/00	2,248,863	203,591	268,302
9/30/00	<u>2,241,925</u>	<u>206,589</u>	<u>272,241</u>
13-month avg	<u>\$2,283,552</u>	<u>\$188,598</u>	<u>\$248,605</u>
Total			
<u>Final Projected Test Year</u>	<u>09/30/2001</u>	<u>SS W</u>	<u>SS WW</u>
9/30/00	2,241,925	206,589	272,241
10/31/00	2,234,987	209,588	276,181
11/30/00	2,228,049	212,586	280,120
12/31/00	2,221,111	215,585	284,059
01/31/01	2,214,173	218,583	287,999
02/28/01	2,207,235	221,582	291,938
03/31/01	2,200,297	224,580	295,878
04/30/01	2,193,359	227,579	299,817
5/31/01	2,186,421	230,577	303,756
6/30/01	2,179,483	233,576	307,696
7/31/01	2,172,545	236,574	311,635
08/31/01	2,165,607	239,573	315,575
9/30/01	<u>2,158,670</u>	<u>242,571</u>	<u>319,514</u>
13-month avg	<u>\$2,200,297</u>	<u>\$224,580</u>	<u>\$295,878</u>

Footnotes:

(1) (EX 11, JAM-2)

(2) 9/30/99 balance includes \$2,340,416 amount that agrees with McPherson's 9/30/99 balance (TR 509)(EX 24, Schedule D, page 7)

Schedule of Deferred Taxes for the Seven Springs Wastewater System

Purpose: To calculate September 30, 2001 13-Month Average Balance of the Net Debit Deferred Tax Balance, using staff's recommended amortization rate in Issue 32.

	Contributed Taxes	Amortization Rate	Annual Amortization
Seven Springs Wastewater System (SSWW)	1,544,865	3.06%	47,273
Staff's recommended annual amortization (Issue 32)			\$47,273
Less: Annual amortization per utility (EX 5, MFRs Vol. I, Sch. G-6, page 1)			<u>38,622</u>
<u>Residual of old rate and staff's recommended rate</u>			<u>\$8,651</u>

Note:

Since we are increasing the amortization rate of contributed taxes, we should also increase SSWW's Accumulated Amortization of DTAs by the residual effect of the staff recommended rate in Issue 32 and old rate. Plus, we are allocating amortization evenly over each month, consistent with Stipulation No. 13. (TR 505-506)

<u>Accumulated Amortization of DTAs for SSWW</u>				<u>DTLs for SSWW</u>		
	Intermediate		Final		Final	
Month	Test Year		Month	Test Year	Month	Test Year
9/30/99	\$414,232 (1)		9/30/00	\$489,122	9/30/00	\$474,110 (2)
10/31/99	417,596		10/31/00	489,610	10/31/00	491,528
11/30/99	420,960		11/30/00	490,098	11/30/00	508,946
12/31/99	424,325		12/31/00	490,585	12/31/00	526,364
01/31/00	427,689		1/31/01	491,073	1/31/01	543,782
02/28/00	431,053		2/28/01	491,561	2/28/01	561,200
03/31/00	434,417		3/31/01	492,049	3/31/01	578,619
04/30/00	437,782		4/30/01	492,536	4/30/01	596,037
5/31/00	441,146		5/31/01	493,024	5/31/01	613,455
6/30/00	444,510		6/30/01	493,512	6/30/01	630,873
7/31/00	447,874		7/31/01	493,999	7/31/01	648,291
08/31/00	485,758		8/31/01	494,487	8/31/01	665,709
9/30/00	<u>489,122</u> (1)		9/30/01	<u>494,975</u>	9/30/01	<u>683,127</u> (2)
13-month avg	<u>\$439,728</u>		13-month avg	<u>\$492,049</u>	13-month avg	<u>\$578,619</u>
Total DTAs for SSWW				\$1,577,034		
Less: Accumulated Amortization of DTAs for SSWW				<u>492,049</u>		
Total U&U Unamortized DTAs for SSWW				\$1,084,985		
Less: DTLs for SSWW				<u>578,619</u>		
<u>Net U&U Debit Deferred Balance for SSWW</u>				<u>\$506,367</u>		

Footnotes:

(1) EX 24, Schedule B, page 3

(2) EX 24, Schedule C, page 5

ISSUE 11: Should the cash operating account balance be removed from the working capital calculation?

RECOMMENDATION: No. The cash operating account balance should be included in the working capital calculation. (FLETCHER)

POSITION OF PARTIES

ALOHA: No. The interest is reported above-the-line and to penalize the utility in the working capital calculation would result in this and all other Utilities' refusal to use interest bearing sweep accounts that benefit the customers. The staff auditors concurred with this treatment.

OPC: Yes, the balance is excessive and has not been adequately explained.

STAFF ANALYSIS: The utility used the balance sheet approach to calculate working capital. (EX 5, Vol. I, Schedules Nos. A-17, page 28 and G-1, page 136) In its MFRs, the utility reflected a total cash balance of \$557,243 for the projected September 30, 2001 test year. (EX 5, Vol. I, Schedules Nos. A-17(A), page 28 and A-18(A), page 34) The utility included this \$557,243 cash balance in its working capital calculation. (EX 5, Vol. I, Schedule No. A-17(A), page 28) The interest income on the utility's cash balance was included in above-the-line revenues. (EX 5, Vol. I, Schedules Nos. B-4(A) and G-1, pages 46 and 136)

OPC witness Larkin testified that consistent with the Commission's decision in the utility's last rate proceeding, Aloha's cash operating account balance should be excluded from the working capital allowance. (TR 230) Mr. Larkin further testified that the utility has failed to put forward any proof of the need or prudence of maintaining a half-million-dollar cash balance. (TR 230) Mr. Larkin stated that unless the utility can demonstrate providing services to ratepayers requires the maintenance of a bank account with a \$500,000 balance it should not be included as working capital. (TR 230) Mr. Larkin argued that regardless of whether the interest associated with this account is included in revenues, the customer would still be subsidizing the balance because the interest return is less than the rate of return of rate base. (TR 230-231)

In his rebuttal testimony, utility witness Nixon noted that the removal of the cash operating account balance from working

capital was made in Aloha's last rate proceeding because the utility had recorded the interest income below-the-line. (TR 793) Mr. Nixon pointed out that, in this rate case, the interest income was recorded above-the-line, which effectively makes cash a cost-free current asset. (TR 793) Further, Mr. Nixon testified that the return on cash operating account is not a subsidization, but a generally recognized cost of providing service, pursuant to Section 367.081(2)(a), Florida Statutes. (TR 793)

Mr. Nixon explained that the utility entered into a sweep arrangement with its bank whereby the bank utilizes the cash in the account to make over-night investments. (TR 792) Mr. Nixon noted that during the historical test year bank charges totaled \$19,289, while interest earnings totaled \$26,588 and that of these amounts, \$6,944 of bank charges and \$9,572 of interest income were allocated to the Seven Springs wastewater division. (TR 792) Mr. Nixon argued that the arrangement benefits Aloha's customer since the interest earnings help offset the charges from the bank. (TR 792)

Mr. Nixon testified that, in assessing working capital, one should review the total net working capital to determine its sufficiency or reasonableness, instead of one component, such as the cash operating account. (TR 974) Mr. Nixon noted that to merely look at one component is misleading. (TR 974) Mr. Nixon argued the sufficiency or reasonableness of the utility's requested working capital should be determined by: 1) a comparison of utility's current ratio to a lender's benchmark; and 2) a comparison of Aloha's requested working capital and the average test-year monthly O&M expense, plus accrued taxes. (TR 794) Mr. Nixon stated that lenders view a current ratio of 2 times as the generally acceptable benchmark for a healthy company and that Aloha's current ratio in this case is 1.96 times. (TR 794) Mr. Nixon pointed out that, according to Schedules Nos. B-6(A) and A-17(A), the average monthly O&M expenses are \$181,314 (\$2,175,762/12) and accrued taxes are \$268,823, totaling \$450,137 and that the working capital requested before adjusting for current rate case expense is \$347,100. (TR 794)

Based on the above, Mr. Nixon concluded that the utility's cash balance was sufficient and reasonable to include in the working capital calculation. (TR 793-795) Lastly, in its brief, the utility argued that Mr. Larkin provided no support for his statement that the cash balance maintained by the utility is excessive. (BR 26)

It is a utility's burden to prove that its costs are reasonable. Florida Power Corporation v. Cresce, 413 So. 2d 1187,

1191 (Fla. 1982). Staff believes that both of Mr. Nixon's comparison approaches are reasonable to evaluate working capital. In fact, Mr. Nixon's comparison of Aloha's requested working capital and the average test-year monthly O&M expense, plus accrued taxes is conservative because Mr. Nixon only recognized the O&M expenses for the Seven Springs wastewater system, instead of the total O&M expenses of the total company which is significantly greater. Staff agrees with the utility that Mr. Larkin did not provide any support that the cash balance maintained by the utility is excessive.

It is the Commission's practice to either exclude interest bearing accounts from working capital or to include them provided that the interest income is included in the above-the-line revenues. See Orders Nos.: PSC-99-1917-PAA-WS, issued September 28, 1999, in Dockets Nos. 970536-WS and 980245-WS; PSC-99-2083-CO-WS, issued October 21, 1999, in Dockets Nos. 970536-WS and 980245-WS; PSC-94-0170-EI, issued February 10, 1999, in Docket No. 930400-EI; PSC-97-1487-FOF-EI, issued November 24, 1997, in Docket No. 971228-EI; 11498, issued January 11, 1983, in Docket No. 820150-GU(CR); PSC-93-1637-FOF-TL, issued November 8, 1993, in Docket No. 920196-TL; PSC-96-1404-FOF-GU, issued November 20, 1996, in Docket No. 960502-GU; PSC-97-1225-FOF-WU, issued October 10, 1997, in Docket No. 970164-WU. Based on the Commission's past practice and arguments presented by Mr. Nixon, staff believes that the utility has met its burden of proof that the inclusion of cash in working capital is appropriate. Therefore, staff recommends that the cash operating account balance should be included in the working capital calculation.

ISSUE 12: Are any adjustments necessary to the working capital allowance for rate case expense?

RECOMMENDATION: Yes. Working capital should be adjusted to reflect the average unamortized balance of rate case expense approved by the Commission. (BINFORD)

POSITION OF PARTIES

ALOHA: Yes, the full investment in rate case expenses must be recognized in the working capital calculation.

OPC: This should be a fall-out issue, depending on the adjustments that are made to rate case expense.

STAFF ANALYSIS: This issue is a fall-out of Issue 31. Accordingly, this issue should be considered after Issue 31. The working capital recommended should be adjusted to reflect the average unamortized balance of rate case expense approved by the Commission in Issue 31.

Prior Commission practice regarding rate case expense in the working capital calculation was to include the average unamortized balance of the total allowed rate case expense as a debit. In its MFRs, the utility, in accordance with prior Commission practice, added the average balance of the current rate case expense to the working capital allowance. No parties in this proceeding filed testimony disagreeing with this treatment.

Based on the rate case expense recommended in Issue 31 and following Commission practice, and the utility's treatment, staff recommends that working capital include \$213,338 [$\$426,676/2$] for the average unamortized balance of rate case expense.

ISSUE 13: What is the appropriate working capital allowance?

RECOMMENDATION: The issue is a fall-out of Issues 11, 12, 18, and 31. The appropriate working capital allowance for the utility's Seven Springs wastewater system is \$546,232. (FLETCHER)

POSITION OF PARTIES

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

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

STAFF ANALYSIS: The utility used the balance sheet approach to calculate working capital. (EX 5, Vol. I, Schedules Nos. A-17(A) and G-1, pages 28 and 136) According to its MFRs, the utility calculated its total company balance sheet working capital and allocated it to each of the utility's system based on their prorata share of Aloha's total O&M expenses. (EX 5, Vol. I, Schedule No. A-17(A), pages 28-29) To determine the Seven Springs wastewater system's total working capital allowance, the utility added the average balance of Aloha's estimated costs of this rate case. (EX 5, Vol. I, Schedules No. A-3(A), page 4) Based on the utility's calculation, the total company balance sheet working capital is \$726,402. (EX 5, Vol. I, Schedule No. A-17(A), page 28)

The utility projected its intermediate September 30, 2000 13-month average test year balances of cash, accounts receivable, and accounts payable by multiplying the historical September 30, 1999 13-month average balances of these accounts by the utility's 1.04812 customer growth factor. (EX 5, MFRs Vol. I, Schedule G-6, page 155) Further, the utility projected its final September 30, 2001 13-month average test year balances of cash, accounts receivable, and accounts payable by multiplying the intermediate September 30, 2000 13-month average balances of these accounts by the utility's 1.04812 customer growth factor. (EX 5, MFRs Vol. I, Schedule G-6, page 155) According to its MFRs, the utility indicated that its projected September 30, 2000 and September 30, 2001 balances for accounts payable are slightly understated due to typographical errors. (EX 5, MFRs Vol. I, Schedule G-6, page 161)

Rule 25-30.115, F.A.C., defines a Class A utility as a water or wastewater utility having annual water or wastewater revenues of \$1,000,000 or more. According to its MFRs, the projected September 30, 2001 year-end revenues for Seven Springs wastewater is

\$2,780,994. (EX 5, Vol. I, Schedule No. B-2(A), page 40) Pursuant to Rule 25-30.115, F.A.C., Aloha is a Class A utility system. Rule 25-30.433(2), F.A.C., states in part that "Working capital for Class A utilities shall be calculated using the balance sheet approach." No testimony was presented to dispute the use of the balance sheet approach. As such, staff believes the record supports the use the balance sheet approach.

As discussed in Issue 18, staff is recommending that the appropriate customer growth factor is 1.03486. Using the 1.03486 customer growth factor and being consistent with the utility's projection method, staff has calculated a final September 30, 2001 13-month average test year balances of cash, accounts receivable, and accounts payable. In addition, because the balances were recalculated, staff was able to correct the typographical errors, indicated by the utility, for the accounts payable account. (EX 5, MFRs Vol. I, Schedule G-6, page 161) As a result, staff recommends that the following adjustments to the final September 30, 2001 13-month average test year balances of cash, accounts receivable, and accounts payable should be made.

<u>Account</u>	Per Sch. A-17 Utility's Final Projected Balance	Staff's Final Projected Balance	Staff Adjustment
Cash	\$557,243	\$549,620	(\$7,623)
Accounts Receivable	\$706,239	\$696,991	(\$9,248)
Accounts Payable	\$410,482	\$407,287	(\$3,195)

Based on these adjustments and others that are addressed in other related issues, staff recommends that the appropriate working capital allowance for the utility's Seven Springs wastewater system is \$546,232. Staff's working capital calculation is illustrated in the following schedule.

ALOHA UTILITIES, INC. - SEVEN SPRINGS SYSTEM		DOCKET 991643-SU	
SCHEDULE OF WORKING CAPITAL ALLOWANCE			
FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01			
Account Title	Average Balance Per Utility @9/30/01	Staff Adjustments	Staff Adjusted Balance @9/30/01
Current Assets:			
Cash (Issue 11, Issue 13)	\$ 557,243	(\$7,623)	\$549,620
Customer Accts Receivable (Issue 13)	706,239	(9,248)	696,991
Accts. Rec. - Other (Income Tax Deposits) (Stip. 9)	16,294	(16,294)	0
Allowance for Bad Debts	(6,900)	0	(6,900)
Miscellaneous Current & Accrued Assets	1,154	0	1,154
Other Miscellaneous Deferred Debits	<u>152,116</u>	<u>0</u>	<u>152,116</u>
Total Current Assets and Deferred Debits	<u>\$1,426,146</u>	<u>(\$33,165)</u>	<u>\$1,392,981</u>
Current Liabilities:			
Accounts Payable - Trade (Issue 13)	\$ 410,482	(\$3,195)	\$407,287
Accrued Taxes	268,823	0	268,823
Miscellaneous Current & Accrued Liabilities	<u>20,439</u>	<u>0</u>	<u>20,439</u>
Total Liabilities and Deferred Credits	<u>\$ 699,744</u>	<u>(3,195)</u>	<u>696,549</u>
Net Allowance for Average Working Capital	<u>\$ 726,402</u>	<u>(\$29,970)</u>	<u>\$696,432</u>
	Sch A-17(A)	Allocated	
	O&M Exp	Working	
	Percentage	Capital	
O&M EXPENSE ALLOCATION			
Aloha Gardens Water System	6.75%	\$47,009	
Aloha Gardens Wastewater System	16.01%	111,499	
Seven Springs Water System	29.44%	205,030	
Seven Springs Wastewater System	<u>47.80%</u>	<u>332,894</u>	
	<u>100.00%</u>	<u>\$696,432</u>	
	Amount	Amount	
	Per Utility	Per Staff	
Current Rate Case Expense (Issue 31)	\$472,817	\$426,676	
Average Balance of Current Rate Case Exp. (Issue 12)	\$236,409	\$213,338	
Allocated Working Capital based on O&M Expense		\$332,894	
Plus: Average balance of Current Rate Case Expense		<u>213,338</u>	
Total Working Allowance for Seven Springs Wastewater		<u>\$546,232</u>	

ISSUE 14: What is the appropriate projected rate base?

RECOMMENDATION: Consistent with other recommended adjustments, the appropriate projected rate base for the 13-month average is \$9,552,096. (FLETCHER)

POSITION OF PARTIES

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

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

STAFF ANALYSIS: Based upon the 13-month average test year balances and staff's recommended adjustments, staff recommends that the appropriate projected rate base for the 13-month average is \$9,552,096. Schedule 1-A depicts staff's rate base calculation. Staff's proposed adjustments to rate base are depicted on Schedule 1-B.

COST OF CAPITAL

ISSUE 16: What is the appropriate weighted average cost of capital for the projected test year ending September 30, 2001?

RECOMMENDATION: Based on Stipulation 4, Stipulation 13, and the recommended adjustments discussed in Issue 10, the weighted average cost of capital should be 9.92%. (BINFORD)

POSITION OF PARTIES

ALOHA: To the extent the Commission's leverage formula return on equity or variable interest rate on long term debt changes between the time of the original filing in this case and the Final Order, the returns should be updated.

OPC: The weighted average cost of capital will be a fall-out issue based on adjustments made by the Commission on various other issues.

STAFF ANALYSIS: This issue is a fall-out of Issue 10, Stipulation 4 (use of current leverage formula), and Stipulation 13. Based on Stipulation 4, Stipulation 13, and the recommended adjustments discussed in Issue 10, the weighted average cost of capital should be 9.92%. Schedule 2-A depicts staff's cost of capital calculation. Staff's proposed adjustments to cost of capital are depicted on Schedule 2-B.

ISSUE 17: What is the appropriate prospective Allowance for Funds Used During Construction rate for Aloha?

RECOMMENDATION: The calculation and the effective date of the AFUDC rate were stipulated to as discussed in the case background in Stipulation 12. The actual AFUDC rate should be approved by the Commission based on the approved cost of capital. Based on the staff recommended capital structure, the Commission should approve an AFUDC rate of 9.92% and a monthly discounted rate of 0.826185%. (BINFORD)

POSITION OF PARTIES

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

OPC: It is the Citizens' understanding that this is a stipulated issue.

STAFF ANALYSIS: The calculation and the effective date of the AFUDC rate were stipulated to as discussed in the case background in Stipulation 12. The rate is a fall-out of Issue 16. The actual AFUDC rate should be approved by the Commission based on the approved cost of capital. Based on the staff recommended capital structure, the Commission should approve an AFUDC rate of 9.92% and a monthly discounted rate of 0.826185%.

NET OPERATING INCOME

ISSUE 18: 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?

RECOMMENDATION: The appropriate method of projecting customers and consumption for the projected year ending September 30, 2001 is based on the utility's revised forecast as presented on MFR Schedule F-10, pages 1 and 2. There are two projected growth factors that would be affected by staff's recommended projection methodology. The projected growth factor used to escalate base year bills and gallons up to test year levels should be changed to 1.07093. The projected growth factor is used to account for the impact of forecasted ERC growth on selected O&M accounts should be changed to 1.03486. (LINGO)

POSITION OF PARTIES

ALOHA: The Commission should utilize those projection factors required pursuant to Commission Rule and as contained in Aloha's MFR filing, which is a simple regression over a historic five-year period.

OPC: The Citizens take no position on this issue.

STAFF ANALYSIS: Utility witness Nixon sponsored Schedule F-10, pages 1-4, which calculates the projected growth factors used to escalate bills, gallons and selected O&M accounts from 1999 to 2001. Pages 3 and 4 contain the ERC forecast that is based on total customers, while pages 1 and 2 contain the revised ERC forecast based on single family residential customers. (TR 195-196) The utility believes the regression analysis under either the single family or total customer ERC approach are virtually identical. Therefore, the utility used the original growth predicted on page 4 of Schedule F-10 as a basis of projection. (EX 5, MFRs Vol. 1, Schedule F-10, p. 1)

Staff witness Stallcup testified on the results of an analysis he conducted on the ERC forecasts to determine if the forecasts are identical and which forecast should be used. (TR 152-153) The utility's arguments, testifying staff's arguments and staff's analysis follow.

The projections on pages 3 and 4 of Schedule F-10 contain total ERCs, both residential and commercial, converted to ERCs based on meter size. Utility witness Nixon testified that these ERCs are more representative of the additional revenue and additional billing determinants, and, therefore, they should be used to calculate the projected factors used to escalate bills, gallons and selected O&M accounts from 1999 to 2001.

In the utility's original filing, the ERC forecast was based on total customer ERCs. Also, the utility used calendar year 1999 data instead of historical base year data as required by the MFRs. This forecast is contained on pages 3 and 4 of Schedule F-10. In response to staff's request to correct this MFR deficiency, the utility revised its forecast to one based on historical base year residential ERCs as required by the MFRs. This forecast is presented on pages 1 and 2 of Schedule F-10. (TR 152)

Witness Nixon testified that pages 1 and 2 containing the revised ERC forecast was filed to meet the minimum filing requirements, but does not present an accurate count of the total ERCs that will be billed. Therefore, he concluded that the projections, as originally filed, are appropriate to use in this case. (TR 195-196)

In particular, the utility's 1.08535 projection factor represents the escalation of 1999 bills and gallons to 2001 values. This factor was calculated by multiplying the growth in ERCs, as predicted by the five-year historic linear regression as originally filed, by 12 months to derive the total additional number of bills. This result was then divided by the total historic residential test year bills to arrive at the projection factor. The 1.08535 projection factor can be restated as an annual projection factor of 1.041801. (TR 197-198)

The projection factor to escalate selected O&M expenses to account for the effects of ERC growth was derived by taking the percentage growth rate shown on page 133 of the MFRs, which is a rounded value of 4.812. Generally, that growth factor was applied to the historic O&M expenses to yield the expenses in the intermediate year. The same 4.812 factor was used again to project expenses for 2001. An inflation factor was also used, with specific adjustments. (TR 198)

Staff witness Stallcup, an expert in the fields of statistics and econometrics, analyzed the ERC forecasts submitted by the utility for its Seven Springs system. To test the utility's belief that its original and revised forecasts are virtually identical,

and to determine which of the forecasts should be used, witness Stallcup conducted two evaluations of the forecasts. The first evaluation tested the utility's belief that the two forecasts are virtually identical. The second evaluation tested the utility's two forecasts against an independent projection of test year ERCs to determine which forecast would be likely to yield a more accurate result. Based on these analyses, witness Stallcup concluded that the two forecasts are not virtually identical, and that the revised forecast yields a more reliable test year ERC forecast. (TR 153)

In order to conclude that the two test year forecasts are not virtually identical, witness Stallcup used statistical techniques to determine if the projected test year ERCs produced by the two forecasts were sufficiently close to each other to deem the difference to be insignificant. "In this test, the difference between the forecasts is compared to each forecast model's inherent ability to explain ERC growth. If the difference is less than the models' inherent accuracy, one would conclude that one forecast is just as accurate as the other, or, in other words, that they produce virtually identical results. On the other hand, if the size of this difference is greater than the models' inherent range of accuracy, one would conclude that the two forecasts are not virtually identical." (TR 153 line 19-154 line 2)

"The results of these calculations show that the difference between the revised forecast of 10,330 ERCs in test year 2001 is significantly different from the originally filed forecast of 9,774.5 ERCs. That is, the difference between the forecasts can not be attributed simply to normal forecasting error. Therefore, [witness Stallcup] concluded that the two forecasts are not virtually identical." (TR 154 lines 4-9; EX 4, PWS-1)

The utility relied on a time trend to forecast ERC growth. "Forecasts derived from time trends incorporate within them the intrinsic assumption that the level of change in the future will be equal to the level of change observed in the historical data. This assumption ignores any other causal factors that may influence growth such as changes in economic and/or demographic conditions and forces the forecasts to grow at the same level as that observed in the historical data." (TR 154 line 21-TR 155 line 2)

Because the utility relied on a time trend to forecast ERC growth, witness Stallcup constructed a separate econometric model of ERC growth. "An econometric model differs from a time trend model in that it incorporates changes in economic and/or demographic conditions to explain growth." (TR 155 lines 3-5)

"This sensitivity to changing conditions can not be incorporated into a time trend forecast. Thus, econometric models tend to produce more reliable forecasts over a wider range of conditions."
(TR 155 lines 12-15)

Witness Stallcup's constructed model explains ERC growth using the rate of growth in the number of households in Pasco County as measured by the University of Florida's Bureau of Economic and Business Research. "The purpose of this model is to provide a benchmark projection that can be used to test the reasonableness of the utility's ERC forecasts." (TR 154 lines 17-19)

"[T]he econometric model produced a test year total ERC forecast of 10,229 compared to a revised utility forecast of 10,330. This difference of 101 ERCs does not represent a statistically significant difference. The utility's original forecast of 9,775 ERCs, on the other hand, did differ significantly from the econometric model's projection. These results led [witness Stallcup] to conclude that the utility's revised ERC forecast should be more reflective of the conditions expected to exist in the test year than the originally filed forecast." (TR 156 lines 17-25; EX 4, PWS-2)

There are two projected growth factors that are affected if the utility's revised forecast is used instead of its originally filed forecast. The first is the projected growth factor used in MFR Schedule E-13(A) to escalate base year bills and gallons up to test year levels. The utility's originally filed projection factor is 1.08535. The same factor, based on the revised forecast, is 1.07093. The second affected projected growth factor occurs in the MFR schedules used to account for the impact of forecasted ERC growth on selected O&M accounts. The utility used a factor of 1.04812 to escalate these accounts from the base year of 1999 to 2000, and then again from 2000 to 2001. This factor was calculated by averaging the observed percentage change in ERCs over the historical period from 1994 to 1999. Witness Stallcup's recommended factor, based on the percentage growth of projected ERCs from 1999 to 2000 using the revised forecast is 1.03486. (TR 157-158)

Utility witness Nixon reiterated on rebuttal that the utility used the projection as originally filed since it was the utility's belief that, for the purposes used in the MFRs, the two projections were virtually identical. (TR 799) After admitting he had no expertise in mathematics or statistics, and was therefore unable to test the validity of Mr. Stallcup's models, Mr. Nixon confined his testimony to "practical matters." (TR 798) Witness Nixon testified

that the original projection predicts an additional total increase of 718 ERCs by the end of the projected test year, while the revised forecast predicts an additional 684 ERCs by the end of the projected test year. This is a difference of 34 ERCs; "[t]herefore, from a practical basis, [witness Nixon does] not see any difference in the two projections presented in the MFRs." (TR 800 lines 13-14)

Witness Nixon further testified that, as he understands witness Stallcup's testimony, he (witness Stallcup) recommends using an annual projection factor of 1.03486 because he believes that the growth rate should be based on the three years ending September 30, 2001, as opposed to the historic five-year average growth rate. (TR 800-801, emphasis added) Witness Nixon believes that Mr. Stallcup has deviated from using the historic five-year average incorporated as rule on Schedule F-10 of the MFRs. He also states, "I believe the Commission has always believed that this was a better approach than simply using one or two years, much less actual and two projected years." (TR 801 lines 10-13) Finally, witness Nixon believes "that utility companies filing projected test year rate cases will need to hire a statistician in order to mathematically evaluate the various models which may exist," which will drive up the cost of rate case expense. (TR 801 lines 16-18)

As discussed above, there are several areas of disagreement between the utility and witness Stallcup. The first area of disagreement is whether the original and revised forecasts are virtually identical. While witness Stallcup presented a statistical analysis which indicated that the two forecasts are not identical, witness Nixon admitted that he is neither a mathematician nor a statistician, and that he is therefore unable to rebut a lot of witness Stallcup's testimony. (TR 192, 203) He also stated that he cannot comment credibly on the statistical analysis used, and that he is not qualified to present a detailed response as it relates to the statistical and econometric models referred to in Mr. Stallcup's testimony. "I have no expertise in mathematics or statistics and I am unable to test the validity of his models." (TR 798, 799)

Because witness Nixon has admitted that he cannot comment credibly on the statistical analysis used by Mr. Stallcup, staff believes it is impossible for witness Nixon to credibly rebut what we believe to be a statistically valid analysis presented by witness Stallcup. Therefore, staff recommends that the two forecasts are not virtually identical.

The second area of disagreement is whether the original or revised forecast provides a more reliable test year ERC forecast. "[I]t is important to verify that the ERC growth forecasts submitted by the utility are a proper reflection of the expected economic and demographic conditions in which the utility will be operating. This can be achieved by comparing the ERC forecasts produced by the time trend method to those produced by an econometric model. If the two approaches produce similar forecasts, the Commission can have additional assurance that the Company's projections are reasonable. If the two differ significantly, however, the Commission may take this as a signal that the trended forecasts called for by the MFRs may need to be adjusted." (TR 156 lines 4-14)

According to witness Nixon, because a comparison of the two forecasts yields a difference of 34 ERCs, from a practical basis, there is no difference in the two projections presented in the MFRs. (TR 800) Witness Stallcup conducted a more technical analysis by constructing an econometric model which explains ERC growth, and involves testing the utility's two forecasts against his model to determine which forecast would be likely to yield a more accurate result. Based on these analyses, witness Stallcup concluded that the two forecasts are not virtually identical, and that the revised forecast yields a more reliable test year ERC forecast. (TR 153-154)

Witness Nixon admitted that he has not read witness Stallcup's testimony, and is unable to provide credible rebuttal to the mathematical or statistical analysis. (TR 192, 203, 798, 799, 877, 882) Based on witness Nixon's admitted inability to rebut what we believe to be the credible testimony of witness Stallcup, staff recommends that the revised forecast yields a more reliable test year ERC forecast.

The third area of disagreement focuses on the appropriate application of the Commission's preferred linear regression methodology. According to witness Nixon, he believes the Commission's preferred method of applying a simple regression analysis has been to use the percentage increase represented by the slope over the entire five-year historic period as the growth percentage in projected years. In particular, he believes witness Stallcup has inappropriately used just the historic test year and then the two projected test years, which changes the percentage represented by the historic five-year regression line. (TR 202-203, 886)

However, witness Stallcup testified that his linear regression is based on five years of historical data, which produces the trend line to carry forward the number of ERCs to 2001. The years 2000 and 2001 are entirely derived from the five years of data. (TR 163) His growth factor was derived by calculating the actual change from 1999 to 2001. Furthermore, based on witness Stallcup's participation in countless projected test year cases based on linear regression, the methodology he proposes is the only methodology adopted by the Commission. (TR 170) The appropriate application of linear regression is not dependent upon a particular industry. (TR 171)

Once again witness Nixon is unable to credibly rebut witness Stallcup. He has admitted that he does not understand the significance of a slope in a linear regression equation. In fact, "[a]ll [he] knows how to do is plug the data into a linear regression formula in the computer and get a result." (EX 6, p. 7 lines 8-10; TR 877, 889) Therefore, based on witness Nixon's admitted lack of understanding of the subject matter, as well as the credible expert testimony of witness Stallcup in this matter, staff recommends that the revised forecast yields a more reliable test year ERC forecast.

The fourth area of disagreement is with regards to escalation factors before the application of an inflation factor. Although both rates of growth are attributable to the same ERC growth data, the utility is using a different escalation factor methodology for revenues than for expenses. The utility used the forecasted increase in customers to project revenues, but for the expenses, the utility used the percentage growth represented by the slope of the regression line over the historic five-year period. This results in selected O&M accounts being escalated roughly 9.8%, before inflation, over two years. However, the corresponding escalation for bills and gallons was only 8.5% over the same two year period. (TR 199-200)

Witness Stallcup believes that the methodology utilized to calculate the growth factor for bills and gallons should be the same for increased expenses. "One of the benefits of my methodology is, it applies the same growth rates to both revenues and expenses, which gives me comfort that if we carry our 1999 values forward to the test year of 2001, we will be growing them at the same rate and, therefore, have a more reliable estimate of what revenue requirements are required to be." (TR 171 lines 15-21)

Staff agrees with witness Stallcup. The utility has provided no credible evidence to support using different escalation factor

methodology; therefore, staff recommends that the same methodology and resulting escalation factor be used for bills, gallons and expenses.

A final area of disagreement concerns the use of statistical and econometric analysis in the evaluation of utility rate case filings. Witness Nixon testified that "utility companies filing projected test year rate cases will need to hire a statistician in order to mathematically evaluate the various forecasting models which may exist," resulting in an increase in rate case expense. (TR 801 lines 16-18)

Staff disagrees. It is true that the utility has the burden to file whatever additional information it believes necessary to meet its burden of proof regarding its requested rate increase. However, neither Chapter 367, Florida Statutes, nor Chapter 25-30, Florida Administrative Code, require that all possible variations of methodologies be examined by the utility prior to its filing. While it is important to verify that the ERC growth forecasts submitted by the utility are a proper reflection of the expected economic and demographic conditions in which the utility will be operating, it is staff's role in formulating our recommendation to verify and evaluate the utility's filing.

There is one area of partial agreement, however, between witnesses Nixon and Stallcup. Witness Nixon believes that "[w]hat is important is the projected increase in ERCs from the end of the historic test year to the end of the projected test year. These projected additional ERCs are those which will generate additional projected revenues and expenses." (TR 799 line 24-800 line 3) He reiterates that it is the increase between those two ERC values from 1999 to 2001 that is important. (TR 884) Witness Stallcup utilized the projected increase in ERCs from the end of the historic test year to the end of the projected test year to calculate his projection factors. (EX 4, PWS-1, p. 1)

Staff agrees with witnesses Nixon and Stallcup that the projected increase in ERCs from the end of the historic test year to the end of the projected test year is important. However, staff disagrees with witness Nixon regarding both the level of projected additional ERCs and the growth factors which will yield the appropriate results. As discussed earlier in this issue, staff recommends that the revised forecast yields a more reliable test year ERC forecast. The growth factors of witness Stallcup are the only factors which will yield the desired projected ERCs, as shown in the table below, further validating Mr. Stallcup's analysis.

ERC PROOF -- REVISED FORECAST

Base Year 1999 ERCs (Revised Forecast)	9,646
x Two-Year Projection Factor	1.07093
= Projected ERCs at 9/30/01	10,330

Base Year 1999 ERCs (Revised Forecast)	9,646
x Annual Projection Factor	1.03486
= Intermediate Year ERCs	9,982
x Annual Projection Factor	1.03486
= Projected ERCs at 9/30/01	10,330

Sources: EX 5, MFRs Vol. 1, Sch. F-10, p. 131; TR 157-158.

Witness Nixon has failed to rebut the testimony of witness Stallcup. Staff believes the testimony of witness Stallcup is credible, reasonable and consistent with Commission practice. (TR 151, 155, 170-171, EX 4) Based on the foregoing, the appropriate method of projecting customers and consumption for the projected year ending September 30, 2001 is based on the utility's revised forecast as presented in EX 5, MFRs Vol. 1, Schedule F-10, pages 1 and 2. There are two projected growth factors that are affected by staff's recommended projection methodology. The projected growth factor used to escalate base year bills and gallons up to test year levels should be 1.07093. The projected growth factor used to account for the impact of forecasted ERC growth on selected O&M accounts should be 1.03486.

ISSUE 19: 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?

RECOMMENDATION: Consistent with staff's recommendation in Issue 18, the appropriate projected test year ending September 30, 2001 bills and consumption are 108,266 and 633,079,000, respectively, for residential service customers and 1,696 and 61,822, respectively, for general service customers. The utility's test year revenues before any rate adjustment should be further reduced by \$36,194, and the utility's O&M expenses should be reduced by \$32,883. (FLETCHER)

POSITION OF PARTIES

ALOHA: As per the revised MFRs, adjustments may be necessary to the extent the Commission changes the utility's projected customer growth rate.

OPC: Any such adjustment should be consistent with the Commission's decision on the customer growth rate (Issue 18).

STAFF ANALYSIS: The utility calculated \$2,780,994 of projected test year revenues at Aloha's current rates, which includes miscellaneous service revenues, interest income, and reuse revenues. (EX 5, MFRs Vol. I, Sch. E-13(A), page 120) This \$2,780,994 amount also includes \$2,711,628 of projected revenues for residential and general service customers, which were calculated based on the utility's projection factor of 1.08535. (EX 5, MFRs Vol. I, Sch. E-13(A), page 120) In addition, the utility projected Sludge Removal, Purchased Power, Chemicals, Materials & Supplies, Contractual Services - Other, Rental of Equipment, and Miscellaneous Expense by its calculated projection factor of 1.04812. (EX 5, MFRs Vol. I, Sch. G-1, pages 139 and 141)

As discussed in Issue 18, staff has recommended that the projection factor 1.07093 should be used to project bills and consumption, instead of the utility's projection factor of 1.08535. In order to reflect projected test year revenues at the utility's current rates, staff first removed Aloha's requested increase in revenues calculated at the utility's requested rates. This results in a decrease in revenues of \$1,593,501 returning to the Aloha's projected test year revenues of \$2,780,994 before any residential and general service rate adjustment. Since staff's recommended projection factor is less than the utility's projection factor,

staff recommends that the utility's test year revenues before any rate adjustment should be further reduced by \$36,194. This \$36,194 amount represents the residual of Aloha's projected revenues for residential and general service and staff's projected revenues.

The following schedule illustrates staff's calculation of the appropriate projected test year ending September 30, 2001 bills and consumption for residential service customers and general service customers, as well as the resulting adjustment to the utility's test year revenues before any rate adjustment.

DOCKET NO. 991643-SU
 DATE: JANUARY 4, 2001

ALOHA UTILITIES, INC. - SEVEN SPRINGS WASTEWATER SYSTEM								DOCKET 991643-SU	
SCHEDULE OF PROJECTED TEST YEAR RESIDENTIAL & GENERAL SERVICE REVENUES AT CURRENT RATES									
FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01									
Line No.	Class/Meter Size	Historical Year Bills	Project Factor	Projected Test Year Bills	Test Year Consumption (000)	Project Factor	Projected TY Consumption (000)	Present Rates	Projected TY Revenue
1									
2	Residential								
3	5/8" X 3/4"	101,095	1.07093	108,266				\$8.99	\$973,308
4	M Gallons				591,149	1.07093	633,079	2.32	1,468,744
5	Total Residential	<u>101,095</u>		<u>108,266</u>	<u>591,149</u>		<u>633,079</u>		<u>\$2,442,052</u>
6									
7	General Service								
8	5/8" X 3/4"	975	1.07093	1,044				8.99	9,387
9	M Gallons				9,544	1.07093	10,221	2.78	28,414
10	1"	255	1.07093	273				22.48	6,139
11	M Gallons				4,288	1.07093	4,592	2.78	12,766
12	1 1/2"	108	1.07093	116				44.96	5,200
13	M Gallons				4,459	1.07093	4,775	2.78	13,275
14	2"	168	1.07093	180				71.94	12,943
15	M Gallons				20,295	1.07093	21,735	2.78	60,422
16	3"	12	1.07093	13				143.88	1,849
17	M Gallons				1,335	1.07093	1,430	2.78	3,975
18	4"	24	1.07093	26				224.75	5,777
19	M Gallons				2,707	1.07093	2,899	2.78	8,059
20	6"	42	1.07093	45				449.62	20,223
21	M Gallons				15,099	1.07093	16,170	2.78	44,953
22	Total General Service	<u>1,584</u>		<u>1,696</u>	<u>57,727</u>		<u>61,822</u>		<u>\$233,382</u>
23									
24	Total Projected Residential and General Service Revenues, per staff (Issue 19)								<u>\$2,675,434</u>
25									
26	Total Projected Residential and General Service Revenues, per utility (EX 5, Schedule E-13(A))								<u>\$2,711,628</u>
27									
28	RESIDUAL OF UTILITY'S PROJECTED REVENUES AND STAFF'S PROJECTED REVENUES								<u>(\$36,194)</u>

As discussed in Issue 18, staff has recommended that the projection factor of 1.03486 be used to project customers, instead of the utility's projection factor of 1.04812. As stated earlier, the utility projected Sludge Removal, Purchased Power, Chemicals, Materials & Supplies, Contractual Services - Other, Rental of Equipment, and Miscellaneous Expense by its calculated projection factor of 1.04812. With regard to the Chemicals and Materials & Supplies accounts, there are stipulated adjustments that have already been adjusted for the utility's 1.04812 customer growth factor. As discussed in Issues 26, 28, and 30, staff has made some adjustments to the Materials & Supplies and Miscellaneous expense accounts in which staff also adjusted for the utility's 1.04812 customer growth factor. Therefore, in order to calculate the remaining adjustment for the Chemicals, Materials & Supplies, and Miscellaneous expense accounts, staff removed the historical September 30, 1999 base year amounts of the stipulations and other issues.

Based on the above, staff recommends that the utility's projected O&M expenses should be reduced by \$32,883 to reflect the appropriate growth rate. The following table shows staff's adjustments by account.

<u>Account</u>	<u>Staff's Adjustments</u>
Sludge Removal	(\$16,880)
Purchased Power	(\$3,303)
Chemicals	(\$787)
Materials & Supplies	(\$4,846)
Contractual Services - Other	(\$2,978)
Rental of Equipment	(\$15)
Miscellaneous Expense	<u>(\$4,073)</u>
Total	<u>(\$32,883)</u>

ISSUE 20: What is the appropriate amount of reuse revenue to include in the test year?

RECOMMENDATION: Consistent with staff's recommendations in Issue 37, staff recommends that the appropriate amount of reuse revenue to include in the September 30, 2001 projected test year is \$28,474, which results in a \$18,885 reduction to test year revenues. (FLETCHER)

POSITION OF PARTIES

ALOHA: While the staff calculation is mathematically correct based on the information provided on gallons of reuse to be sold, the information concerning expected paying customers was in error. The \$60,620 calculated by the staff utilizing the new proposed rate is extremely optimistic, based on the fact that the Fox Hollow Golf Course will not be paying any reuse charges for the first four years of its receiving reuse water.

OPC: The Citizens do not dispute Ms. Merchant's position that the appropriate reuse rate should be \$0.32 per thousand gallons. The Citizens believe that because Aloha extended the Mitchell property contract without approval--in violation of Commission order--the \$0.32 should be imputed to the Mitchell property reuse.

STAFF ANALYSIS: The utility projected annual reuse consumption of 189,436,000 and annual revenues of \$47,359. (EX 5, MFRs Vol. I, Schedule E-13(A), page 120; EX 15) Exhibit 15 shows the utility's breakdown of its estimated reuse consumption by GPD and annual consumption for each customer. As indicated by utility witness Watford, the total GPD of 1,219,000 reflected on Exhibit 15 is a typographical error. (TR 634-635) Staff notes that the correct amount should be 519,000 GPD.

Further, based on staff's review, the utility had more typographical errors on Exhibit 15. First, the Pasco Middle & High Schools' annual consumption should be 21,900,000 (60,000 GPD multiplied by 365 days). Also, the total 189,436,000 gallon annual consumption is incorrect and overstated by 1,000 gallons. Using the correct total GPD, the total annual consumption is 189,435,000 (519,000 GPD multiplied by 365 days) gallons. Consistent with staff recommendations in Issue 37 (reuse rate of \$0.29 per thousand gallons and no charge for reuse water to the Mitchell Property and the Fox Hollow Golf Course), staff recommends that the appropriate

amount of reuse revenue to include in the September 30, 2001 projected test year is \$28,474, which results in a \$18,885 reduction to test year revenues. The following table illustrates staff's calculation of the appropriate amount of reuse revenue and reduction to test year revenues.

<u>Reuse Customers</u>	<u>GPD</u>	<u>Annual Consumption</u>
Fox Hollow Golf Course	250,000	91,250,000
Pasco Middle & High Schools	60,000	21,900,000
YMCA	13,500	4,927,500
Trinity College	8,000	2,920,000
Virgo Optics	19,500	7,117,500
Morton Plan Hospital	4,000	1,460,000
Heritage Springs Development	114,000	41,610,000
<u>Seven Springs Elementary School</u>	<u>50,000</u>	<u>18,250,000</u>
<u>Total reuse consumption</u>	<u>519,000</u>	<u>189,435,000</u>
Less: Fox Hollow Golf Course - <u>(Issue 37)</u>	<u>250,000</u>	<u>91,250,000</u>
Total reuse consumption for All <u>Other reuse customers - (Issue 37)</u>	<u>269,000</u>	<u>98,185,000</u>
Divided by 1,000		98,185
Reuse rate at a \$0.29 per thousand gallons for All Other reuse customers - (Issue 37)		X \$0.29
Total Reuse Revenue Per Staff		<u>\$28,474</u>
Utility's Reuse Revenue, Per Schedule E-13(A)		\$47,359
Staff's Adjustment to Test Year Revenues - Difference in Staff's Reuse Revenue and Aloha's		<u>(\$18,885)</u>

ISSUE 21: What is the appropriate salary for Aloha's vice-president?

RECOMMENDATION: The vice-president's salary should be 20% of the president's salary. As a result, Salary & Wages - Officers and Employee Benefits accounts 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. (FLETCHER)

POSITION OF PARTIES

ALOHA: The salary proposed in the MFRs and charged for the historic test year.

OPC: The Citizens agree with the staff that because the vice-president spends only 20% of her time with utility operations, her salary should be no higher than 20% of the president's salary.

STAFF ANALYSIS: As indicated in Audit Disclosure No. 4, the president's salary is \$122,595 for 100% of his time in this capacity, and the vice-president's salary is \$68,250 for 20 percent of her time in this capacity. (EX 13, TES-1, page 13) By Order No. PSC-99-1917-PAA-WS, issued September 28, 1999, the Commission found it appropriate to limit the maximum threshold of the vice-president's salary to 20% of the president's salary. In that Order, the Commission allowed the utility to fully contest or litigate its objections to the Commission's decision in the next rate case. According to the audit report, the utility did not make any adjustment to limit the vice-president's salary to 20% of the president's salary. (EX 13, TES-1, page 13)

Staff witness Stambaugh testified that "expanding the vice-president's salary to 100% [of her time in this capacity] equates to an annual rate of pay of \$341,250." (TR 579) Mr. Stambaugh pointed out that in Order No. PSC-99-1917-PAA-WS, issued September 28, 1999, the Commission found the following: "we do not believe that Aloha's vice-president warrants a greater annualized salary than the president." (TR 579, Lines 7-8)(EX 13, TES-1, Page 13) Mr. Stambaugh testified that the vice-president's salary should be capped at 20% of the president's salary because she still only spends 20% of her time in this capacity. (TR 579) As a result, Mr. Stambaugh concluded that the vice-president's salary should be reduced by \$43,731. (TR 579) Since this amount relates to the entire utility, Mr. Stambaugh used the utility's allocation of 35.46% in its MFRs which resulted in an adjustment of \$15,507 for

the Seven Springs wastewater system. (TR 579) By comparing the salary adjustment to total salaries and applying the result to benefits and payroll taxes, Mr. Stambaugh testified that benefits should be reduced by \$5,319 and payroll taxes should be reduced by \$1,392. (TR 579)(EX 13, TES-1, page 13)

Further, staff witness McPherson agrees with Mr. Stambaugh's adjustment. (EX 11, JAM-1, Page 11) Through redirect-examination by staff, Mr. McPherson testified that the duties of the vice-president had not significantly changed, since the utility's last rate proceeding. (TR 557)

OPC witness Larkin testified that he agreed with Mr. Stambaugh's recommended adjustment to the vice-president's salary. (TR 217-218) In its brief, OPC argued that the obvious intuitive conclusion is that a vice-president's salary should be significantly below the president's. OPC also posed the following question: "How many corporations pay the vice-president equal to the president?" (BR 17) OPC also argued that, conventionally, the president is paid substantially more than the vice-president. (BR 17) Lastly, OPC argued that allowing Aloha's vice-president's annualized salary equal to the president's, the Commission would be giving the utility the benefit of the doubt. (BR 17)

In his rebuttal testimony, utility witness Nixon noted that Mr. Stambaugh's adjustment rests on the theory that all employees are of equal worth. (TR 764) The utility argued in its brief that there is no support for this basis or contention. Mr. Nixon claimed Mr. Stambaugh ignored traditional tests contained in the Commission's Audit Manual. (TR 765) Specifically, Mr. Nixon stated that this manual lists seven different factors that should be considered and that the audit finding sponsored by Mr. Stambaugh did not consider any of them. (TR 765) Mr. Nixon noted that the "Vice-President is a successful, respected, and experienced businessperson whose time would command a higher salary than the President's on an annual basis." (TR 765, Lines 17-20)

Mr. Nixon noted that the duties of the vice-president include being on call 24 hours a day 7 days a week to provide advice and consultation to the utility with little or no notice. (TR 766) He also noted that because of the arrangement with the vice-president for part time services, Aloha does not have to provide her with administrative support or a separate office. (TR 766) Finally, Mr. Nixon noted that the total officers' compensation for Aloha is less than that for similar sized utilities, and that the alternative to the part time vice president is a full time vice president at a substantially higher cost. (TR 766)

In his rebuttal testimony, utility witness Watford testified that the vice-president has a bachelor's degree in accounting with a major in finance (brief says minor) and that her time devoted to the utility often exceeds the 20% the utility has indicated that she spends in this capacity. (TR 970-971)(BR 32) Further, through cross-examination by Aloha, Mr. Stambaugh testified that he did not undertake any analysis of the educational background and experience of the vice-president during the period of audit field work or after he drafted his testimony. (TR 588-589) However, Mr. Stambaugh did review it afterwards, and he did not change his recommendation. (TR 569, 589)

Based on arguments of witnesses Stambaugh, McPherson, and Larkin, staff believes that the vice-president's salary should be limited to 20% of the president's salary. With regard to Mr. Nixon's argument that Mr. Stambaugh ignored traditional tests contained in the Commission's Audit Manual, staff disagrees. According to Mr. Nixon's rebuttal testimony, one of the tests is to review the description of duties and responsibilities. In the last rate proceeding, the Commission reviewed the duties and responsibilities of the vice-president and other officers. See Order No. PSC-99-1917-PAA-WS, issued September 28, 1999. As stated earlier, Mr. McPherson testified that the duties of the vice-president had not significantly changed, since the utility's last rate proceeding. (TR 557)

As noted by Mr. Watford, the vice-president has a bachelor's degree in accounting with a major in finance. Staff believes that the educational background of the vice-president is beneficial to the utility because it is a qualifying factor that she possess qualifications adequate for this position. However, based on our review of Exhibit 32, which provides the duties and responsibilities of the utility's officers, staff notes that the president's duties and responsibilities are greater than those of the vice-president. Section 367.081(3), Florida Statutes, states in part that "[t]he commission, in fixing rates, may determine the prudent cost of providing service. . . ." Staff believes a comparison of the president's salary and his time spent in that capacity in relation to the vice-president's salary and her time spent in that capacity is a reasonable test to determine a prudent level of salary for the vice-president. Based on the above, staff recommends that Salary & Wages - Officers and Employee Benefits accounts 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.

ISSUE 22: Should an adjustment be made to remove expenses associated with an administrative employee?

RECOMMENDATION: No. This employee is needed due to the increased workload caused by reporting requirements imposed by DEP and the ARCFJ. (CROUCH)

POSITION OF PARTIES

ALOHA: No. That employee is a necessary addition to the staff of Aloha, not only because of under staffing during the test year, but additionally because of the requirements imposed by the DEP.

OPC: Yes. The utility stated that the justification for adding this particular position was that it was required by the CFJ. While the CFJ specifically identifies two other positions, which have been filled, it says nothing about the position in question.

STAFF ANALYSIS: Aloha hired a new administrative employee in late 1999 and included the annualized salary in the projected test year expenses. The utility's explanation in the MFR's was that this employee was "required to meet DEP staffing requirements." (EX 5, Sch G-1)

OPC witness Larkin testified that the ARCFJ did not require any additional administrative employees be added to the Company's employment rolls. Mr. Larkin further testified that, "I am removing from the projected salaries the administrative person that the Company has added under the purported justification that it was a requirement of the DEP." (TR 221)

Utility witness Nixon testified that although the position was not specifically required by the Consent Order, "the decision to add this position was made in connect with management's assessment of staffing requirements set forth in the Consent Order." (TR 771, Lines 11-13) Further, Aloha has provided evidence of the substantial increase in reporting requirements resulting from the ARCFJ. (TR 771, 795-796) In addition, Mr. Watford noted that the PSC's management audit team had informed them that they were recommending not only the need for this new administrative employee, but the possible need for three more administrative employees to handle the current workload at the utility. (TR 976) He further noted that the additional administrative employee was

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needed to handle other duties that were due to customer growth and demand. (TR 976)

Staff agrees that the additional reporting requirements levied by the ARCFJ and the additional workload due to customer growth and demand (TR 976) justify the new administrative position even though that position is not specifically called for in the ARCFJ.

Staff recommends that this administrative position is justified by the increased workload caused by the ARCFJ and DEP and that there should be no adjustment to remove the expenses associated with that position.

ISSUE 23: Should the cost of the annual financial audit be allocated to all of the utility's systems?

RECOMMENDATION: No. Staff recommends that no adjustment should be made. (FLETCHER)

POSITION OF PARTIES

ALOHA: No. The financial audit is required as part of the financing arrangement related to the Seven Springs wastewater system and relates solely to the financing for the improvements to that system. Allocating these costs to other systems is inappropriate.

OPC: Yes. This bank loan benefits all Aloha divisions with this cost source of capital. The audit is, in effect, simply a cost of debt. Since other divisions share the benefits of this low-cost capital, they should also share the cost.

STAFF ANALYSIS: The utility executed a loan with Bank of America for the construction financing of the Seven Springs wastewater system. (EX 5, MFRs Vol. I, Schedule No. D-5(A)) (EX 25, page 1) According to the loan covenants, all of the utility's systems are required to be audited annually. (TR 377-378, 844) (EX 25, page 44) The annual cost of auditing all the utility's systems is \$24,000, and was recorded in the Contractual Services - Accounting account. (TR 223) (EX 5, MFRs Vol. I, Schedule No. B-8(B), page 53) All of Aloha's systems revenues are guaranteed for this loan. (TR 844) (EX 25, page 44)

OPC witness Larkin testified that Aloha allocated a portion of this loan to the utility's other operating divisions, through the prorata allocation of the total company capital structure components to the rate base of the Seven Springs wastewater system. (TR 223) (EX 5, MFRs Vol. I, Schedule D-2(A), page 93) As a result, Mr. Larkin stated that because the benefit of the loan is being allocated in part to the utility's other systems, then these other systems should bear part of the cost of the annual audit. (TR 223) Mr. Larkin noted that the portion of the loan that is allocated to Aloha's other divisions is 14.35%. (TR 223) Mr. Nixon testified that the \$24,000 annual audit fee should be allocated in the same proportion as the debt, which results in a reduction to Contractual Services - Accounting account of \$3,444. (TR 223)

Utility witness Nixon testified that virtually all the utility's long-term debt, except for a minor amount of debt for transportation equipment, was incurred for the Seven Springs wastewater system. (TR 776) Mr. Nixon stated that the audit is required specifically for the loan to expand and modify the Seven Springs wastewater plant. (TR 776) Mr. Nixon also stated that "[t]he receipt of CIAC, Accumulated Depreciation, and CIAC Amortization cause the rate base [of the Seven Springs wastewater system] to differ from Capital Structure, requiring prorata reconciliation." (TR 776, Lines 7-10) Further, Mr. Nixon testified that the reconciliation of rate base is simply a mechanical adjustment and is totally unrelated to an expense specifically identified and matched with the utility's Seven Springs wastewater system. (TR 776)

According to Schedule D-5(A) of its MFRs, the utility's total 13-month average balance of long-term debt for the projected test year ended September 30, 2001 is as follows:

<u>Description</u>	<u>13-month Average Balance</u>
Bank of America (15 years)	\$5,064,090
Vehicle Notes (4.9%, 3 years)	24,926
Vehicle Note (9.25%, 3 years)	7,386
L.L. Speer - LOC (P+2, 30 years)	2,976,688
L.L. Speer - DOT (P+2, 30 years)	<u>541,672</u>
Total Long-term Debt	<u>\$8,614,742</u>

Both of the L.L. Speer debt issues are associated with Aloha's 1995 reuse project for its Seven Springs wastewater system. See Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, in Dockets Nos. 950615-SU and 960545-WS. As stated earlier, the loan with Bank of America was for the construction financing for the Seven Springs wastewater system. Thus, staff agrees with Mr. Nixon that virtually all the utility's long-term debt was incurred for the Seven Springs wastewater system and that the reconciliation of rate base is simply a mechanical adjustment and is totally unrelated to an expense specifically identified to the Seven Springs wastewater system. Based on the above, the cost causer of this annual audit fee is the Seven Springs wastewater system. Therefore, staff recommends that no adjustment should be made.

ISSUE 24: Should any additional adjustments be made to Contractual Services - Accounting, for non-recurring costs?

RECOMMENDATION: Yes. 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. (FLETCHER)

POSITION OF PARTIES

ALOHA: No adjustments should be made to reduce contractual services - accounting. The adjusted items are recurring expenses.

OPC: The Citizens agree with Mr. McPherson that accounting expenses should be reduced by \$1,113 to remove non-recurring fees associated with the implementation of the new accounting software system.

STAFF ANALYSIS: As indicated in Audit Disclosure No. 9 of the audit report for the Commission's earnings investigation, the utility replaced its general ledger and billing software systems in July of 1999 with a new accounting software system. (TR 506-507) (EX 11, page 11) The utility's accounting firm assisted Aloha with the implementation of the new system by reviewing system output, balancing accounts, and testing accuracy. (TR 507) (EX 11, page 11)

Staff witness McPherson testified that the replacement of billing and accounting systems is an infrequent event and expenses related to this event are non-recurring. (TR 507) Mr. McPherson pointed out that Rule 25-30.433(8), F.A.C., requires that non-recurring expenses be amortized over a 5-year period. As a result, Mr. McPherson testified that the accounting expenses for the Seven Springs wastewater system should be reduced by \$1,113. (TR 507)

In his rebuttal testimony, utility witness Nixon testified that these charges for services simply took the place of the accounting firm's ordinary charges for its semi-annual review of the company's financial statements. (TR 805-806) Mr. Nixon explained that the accounting firm's semi-annual review is simply an overview of the general ledger, financial statements and journal entries. (TR 806) Mr. Nixon stated that a review of quarterly financial statements is required in Aloha's financing agreement with Bank of America, and that the estimated cost of those services will equal or exceed the amount of Mr. McPherson's proposed adjustment. (TR 806)

Through cross-examination by staff, Mr. Nixon testified that "the change over in software prevented us from doing our semi-annual review. Instead, we were working with the client to produce financial statements on a general ledger." (TR 846, Lines 8-11) However, as indicated by Mr. Nixon, the accounting firm's semi-annual review is simply an overview of the general ledger, financial statements and journal entries. (TR 806) As such, staff believes these charges were in addition to the normal semi-annual review.

Regarding Mr. Nixon's testimony that the estimated cost of a review of quarterly financial statements required by the loan with Bank of America will equal or exceed the amount of Mr. McPherson's proposed adjustment, staff believes that the record is unclear whether the cost of these quarterly reviews is included in the utility's requested \$24,000 annual fee for a financial audit which is also required by the loan with Bank of America. If it is included the \$24,000 annual fee, it will be recovered. If it is not included, it is the utility's burden to prove that its costs are reasonable. Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982). Further, if it is not included, staff notes that the utility should have requested and provided supporting documentation for these costs. Regardless, staff believes the cost of reviews of quarterly financial statements is separate and apart from this issue. Therefore, staff recommends that the 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.

ISSUE 25: Should an adjustment be made to Contractual Services - Accounting, as a result of the Company hiring a new comptroller?

RECOMMENDATION: No adjustment is necessary. (FLETCHER)

POSITION OF PARTIES

ALOHA: No adjustment is appropriate. The new comptroller is less experienced than the old comptroller and less knowledgeable in utility matters. It would probably be appropriate to include additional outside accounting expenses for the first few years.

OPC: Yes. As a result of the comptroller's accounting expertise, Aloha has less need to rely on outside accounting services to maintain the company's books and records. Contractual Services should be reduced by \$7,449 to reflect the savings as a result of hiring this new employee.

STAFF ANALYSIS: The utility hired a new comptroller in June of 2000. (TR 774) OPC witness Larkin testified that "[t]he addition of the new comptroller should result in productivity gains related to keeping the Company's books and records." (TR 222, Lines 18-20) Mr. Larkin stated that the utility "will not have to rely as extensively as they have in the past on outside accounting services to maintain the books and records. . . ." (TR 222, Lines 20-21) As a result, Mr. Larkin further testified that the new comptroller's allocated salary for the Seven Springs wastewater system should be reduced for an estimated 50% productivity gain, which results in a reduction of Contractual Services - Accounting of \$7,449. (TR 223)

Through cross-examination by Aloha, Larkin stated that the old comptroller had approximately 18 years of experience with Aloha. (TR 254) Further, Mr. Larkin stated that the new comptroller had experience in accounting since 1973 and had been an assistant comptroller of Ryans Home, Inc. for 10 years and comptroller for one year with the same company. (TR 255) Utility witness Nixon noted that the new comptroller does not have an accounting degree and has no experience in the utility industry. (TR 774) Due to the inexperience of the new comptroller, Mr. Nixon asserted that Mr. Larkin should have logically concluded that, in the short-term, the outside accounting firm might have to assist the utility's new comptroller to a greater extent than the experienced former comptroller. (TR 775, 847, 891) In its brief, the utility argued that Mr. Larkin provided no basis for the 50% productivity gain.

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(BR 35) Lastly, the utility believes that Mr. Larkin's adjustment is neither appropriate nor supported by the record. (BR 35)

Based upon the evidence of record, staff agrees with the utility. In so recommending, staff notes that "it is the [Commission's] prerogative to evaluate the testimony of competing experts and accord whatever weight to the conflicting opinions it deems necessary." Gulf Power Co. v. FPSC, 453 So. 2d 799, 805 (Fla. 1984). Accordingly, staff recommends that no adjustment is necessary.

ISSUE 26: Should any adjustments be made to remove expenses associated with the settlement of the DEP enforcement action?

RECOMMENDATION: Yes. Legal expenses associated with a DEP enforcement action are non-recurring and should be amortized over five years, which results in a reduction to legal expenses of \$14,020. Also, miscellaneous expenses should be reduced by \$20,706. (FLETCHER)

POSITION OF PARTIES

ALOHA: Yes. Those related to the enforcement action should be amortized over five years. However, the initial audit position removed far more than were related to the enforcement action. Those expenses related to annual recurring functions should have been left in normal operating expenses.

OPC: Yes. Aloha's stockholders should bear this expense. Aloha paid a penalty for violations cited by DEP. Customers should not pay either the penalty or legal expense Aloha incurred to fight it.

STAFF ANALYSIS: On March 9, 1999, the utility executed an ARCFJ with DEP in which the utility was required to pay \$18,400 in settlement of alleged violations. (EX 5, MFRs Vol. III, Page 196) The \$18,400 amount was recorded as miscellaneous expenses during the historical September 30, 1999 test year. (TR 778-779) (EX 22, RCN-4, Page 1) According to Audit Disclosure No. 6, the utility incurred \$27,400 in legal fees related to DEP's enforcement action during the historical September 30, 1999 test year. (EX 13, TES-1, Page 15)

OPC witness Larkin testified that stockholders should have borne the \$27,400 in legal expenses associated with DEP's enforcement action because ratepayers have no influence over the utility's operation of the plant or discharge of effluent, which caused the conflict with the DEP. (TR 220) Mr. Larkin asserted that "ratepayers should not be held responsible for violations, either alleged or otherwise, associated with the operation of the plant." (TR 220, Lines 14-16) Further, Mr. Larkin noted that to allow the recovery of these legal fees and the payment for alleged violations would move the responsibility of plant operations in conformity with DEP regulation, from the utility's management to the utility's ratepayers. (TR 220)

In its brief, OPC noted that page 7 of the ARCFJ states: "following compliance with all the terms of this judgement, including the payment of any stipulated penalties due to the requirements of this judgement shall be deemed satisfied." (TR 246, Lines 8-11)(EX 5, MFRs Vol. III, page 190)(BR 21) OPC pointed out that page 10 of the ARCFJ states: "Within 10 days of the execution of this judgement Aloha shall pay the department \$18,400 in settlement of alleged violations." (TR 246, Line 25 through TR 247, Line 2)(EX 5, MFRs Vol. III, page 193)(BR 22) Further, OPC argued that one need only ask two questions: "1) If there is no 'stipulated penalty' [in the ARCFJ], then why would that term be included in the ARCFJ at all?, . . . and 2) What is the purpose of the \$18,400 payment to DEP, if it is not a penalty." (BR 22) As a result, Mr. Larkin believes that legal expenses should be reduced by \$27,400 and miscellaneous expense should be reduced by \$20,244, which represents the \$18,400 amount plus \$1,844 attributed to the utility's escalation of these expenses by its customer growth factor. (TR 220)(EX 5, MFRs Vol. I, Schedule G-1, page 139)

In its response to this audit disclosure, Utility witness Nixon asserted that Aloha had submitted invoices which indicated that \$9,875 of the \$27,400 in legal expenses were for routine matters not associated with the ARCFJ. (EX 22, RCN-11, pages 4 and 13-33) Further, Mr. Nixon pointed out that in Order No. PSC-97-0618-FOF-WS, issued May 30, 1997, in Docket No. 960451-WS, the Commission found the following:

Although we find that fines associated with violations of DEP and EPA should be borne by the shareholders of the utility, we believe it is reasonable for UWF to recover the costs of defending such fines. As the Commission previously concluded, the legal expenses incurred for defending fines from DEP and EPA could facilitate avoided or a reduced amount of fines. Therefore, we find that no such adjustments are necessary to test year expenses. (TR 769, Line 25 through TR 770, Line 8)(EX 22, RCN-2, page 2)

Mr. Nixon testified that this is not a fine and pointed out that the Commission staff audit report stated that the \$27,400 in legal expenses and the \$18,400 payment appear to be legitimate utility expenses because in the ARCFJ there was no finding of wrong doing by the utility. (TR 769)(EX 13, page 15) As a result, Mr. Nixon asserted that these expenses should be amortized over 5 years and that the appropriate amount of annual amortization to include is \$7,185 [(\$27,400 less \$9,875 plus \$18,400)/5 years]. (TR 770)

Based on his review of the legal invoices submitted by the utility, staff witness Stambaugh agreed with Mr. Nixon that \$9,875 of the \$27,400 in legal expenses were not related to the ARCFJ, but were normal, recurring expenses. (TR 580-581) Mr. Stambaugh also agreed with Mr. Nixon that the remaining legal expenses of \$17,525 associated with the DEP enforcement action and the \$18,400 for the utility's payment of DEP's legal expenses should be amortized over 5 years and that the appropriate amount of annual amortization to include is \$7,185. (TR 581)(EX 13, page 15)

Based on its review of the legal invoices submitted by the utility, staff agrees that \$9,875 of the \$27,400 in legal expenses were not related to the ARCFJ. Staff believes the legal expenses associated with the ARCFJ are non-recurring in nature. Rule 25-30.433(8), F.A.C., states that "[n]on-recurring expenses shall be amortized over a 5-year period unless a shorter or longer period of time can be justified." According to Schedule G-1, pages 139 of Volume I of its MFRs, the utility did not escalate legal expenses by customer growth or inflation. As such, staff agrees with Mr. Nixon and Mr. Stambaugh and recommends that the \$17,525 in legal expenses in connection with the ARCFJ should be amortized over 5 years. This results in a reduction to legal expenses of \$14,020 [\$17,525 less (\$17,525 divided by 5 years)].

Based on the arguments of OPC and our review of the ARCFJ, staff believes that the payment of \$18,400 for alleged violations are stipulated penalties or fines. As pointed out by Mr. Nixon, the Commission practice is that fines associated with violations of DEP and EPA should be borne by the shareholders of the utility. See Order No. PSC-97-0618-FOF-WS, issued May 30, 1997, in Docket No. 960451-WS. Accordingly, staff believes that the \$18,400 payment should be borne by the utility's shareholders. As stated earlier, the payment was recorded as miscellaneous expenses. According to Schedule G-1, page 139 of Volume I of its MFRs, the utility escalated miscellaneous expenses by customer growth and inflation. As such, the utility's escalation of this amount should be removed. As a result, staff recommends that miscellaneous expenses should be reduced by \$20,706. The following table illustrates staff's adjustments.

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	<u>Intermediate Projected Amount</u>	<u>Final Projected Test Year Amount</u>
Historical TY Amount	\$18,400	\$19,519
Aloha's Growth Factor	<u>X 1.04812</u>	<u>X 1.04812</u>
	\$19,285	\$20,458
Inflation Factor	<u>X 1.0121</u>	<u>X 1.0121</u>
	<u>\$19,519</u>	<u>\$20,706</u>

ISSUE 27: Is an adjustment necessary to chemicals and purchased power expenses as a result of the utility's infiltration and inflow reduction program?

RECOMMENDATION: No, an adjustment is not necessary because there is no excessive I&I. (WETHERINGTON)

POSITION OF PARTIES

ALOHA: No. There is no significant change in these accounts as a result of this infiltration and inflow reduction.

OPC: Yes, Aloha has included future costs for an I/I reduction program that is ongoing. If future costs are recognized, fairness dictates that the corresponding I/I reduction also be recognized. Chemicals and purchased power should be reduced by 23.37% to reflect the lower I/I resulting from the program.

STAFF ANALYSIS: In Issue 6, OPC and the utility argued the case for whether or not Aloha had excessive I&I. After a review of those arguments, staff recommended that the Aloha collection system did not have excessive I&I. Since it is the practice of the Commission not to adjust operation and maintenance expenses in these cases unless there is excessive I&I (See Docket No. 950495-WS, Order No. PSC-96-1320-FOF-WS, Issued October 30, 1996, and Docket No. 990937-SU, Order No. PSC-00-1163-PAA-SU, Issued June 26, 2000), staff recommends that no adjustments to chemicals and purchased power be made.

ISSUE 28: Should any adjustments be made to the utility's base year ended 9/30/99 balance for Account 720 - Materials & Supplies?

RECOMMENDATION: No adjustment should be made. (FLETCHER)

POSITION OF PARTIES

ALOHA: Yes, an adjustment to capitalize \$11,606 should be made as proposed by Audit Exception No. 3, and the effect of Stipulation No. 6. However, no other adjustments to the base year materials and supplies account are appropriate.

OPC: Yes. The utility has incurred a drastic increase which has not been adequately explained. This account should be reduced by \$17,179 to reflect indexing of this account for customer growth and inflation from the 1998 level.

STAFF ANALYSIS: The utility's year-end December 31, 1998 balance for materials & supplies was \$48,406, and its year-end September 30, 1999 balance was \$78,582. (EX 5, MFRs Vol. I, Schedule B-8(C), page 54) OPC witness Larkin testified that the Materials & Supplies Account had increased approximately 62% from December 31, 1998 year-end to the test year ended September 30, 1999. (TR 222) After removing audit adjustments of \$12,703 which have been stipulated, Mr. Larkin stated that the balance still increased by approximately 36% and that the utility had not accounted for this dramatic increase. (TR 222) As a result, Mr. Larkin proposed that the appropriate balance for September 30, 1999 should be equal to the 1998 calendar year-end balance escalated by customer growth and inflation for nine months, which results in a reduction of \$15,266. (TR 222) Lastly, OPC noted in its brief that Exhibit 23 still does not show that the utility's historical base year Material & Supplies are normal and expected to continue at that level in the future. (BR 25)

In its MFRs, the utility stated that the increase to Materials & Supplies was a result of increased routine maintenance of the treatment plant. (EX 5, MFRs Vol. I, Schedule B-8(C), page 54) In his rebuttal testimony, utility witness Nixon stated that he had reviewed the materials & supplies account, and based on this review, he provided an exhibit which listed the specific increases from the 1998 calendar year-end to the September 30, 1999 historical base year. (TR 773)(EX 22, RCN-3) In its brief, the utility argued that Mr. Nixon's rebuttal exhibit RCN-3 and Exhibit

23 fully explains the increase of the historical base year Materials & Supplies. (BR 37)

Exhibit 23 shows an itemized breakdown of the Materials & Supplies for the 1998 calendar year-end and the historical September 30, 1999 historical base year. In its brief, OPC stated that it does not doubt that the money was spent. (BR 25) However, through cross-examination by the utility, staff witness Stambaugh testified that, other than Audit Exception No. 3, no other adjustments to the Material & Supplies were recommended in the audit report. (TR 593) Staff agrees with the utility that the increase of the historical base year Materials & Supplies has been fully explained. Therefore, staff recommends that no adjustment should be made.

ISSUE 29: Should an adjustment be made to Contractual Services - Other, to remove the projected maintenance expense for the new plant?

RECOMMENDATION: No. No adjustment should be made to Contractual Services-Other, Account 736, to remove the projected maintenance expense for the new plant. (CROUCH)

POSITION OF PARTIES

ALOHA: No. There will be no savings as the warranty provided with the new plant has nothing to do with the normal operation and maintenance expenses related to that plant.

OPC: Yes. Aloha has made no adjustment to reflect the manufacturer's guarantee on new equipment. Unless this is addressed, Account 736 - Contractual Services - Other, should be reduced by \$175,000 (the 5% expense factor), since this is new plant that is guaranteed by the manufacturer.

STAFF ANALYSIS: Aloha and OPC agree that the 1.6 MGD wastewater treatment facility is basically a new plant and as such, the equipment comes with a manufacturer's warranty or guarantee on that new equipment for the first year. (TR 409, 914) However, Aloha and OPC disagree as to what maintenance expenses remain and which expenses should be allowed under Account 736 - Contractual Services-Other. The utility estimated \$175,000 in preventative maintenance expense for the test year. (TR 210-211)

OPC witness Bidy, when asked whether Aloha would encounter \$175,000 of preventative maintenance for the new plant, responded:

No, it wouldn't be nowhere close to \$175,000 simply because it's brand new equipment. The only maintenance you will be doing will be preventative maintenance that the operator will do as he goes about his normal duties, and most of those are lubrication-type things. If there is a breakdown, it's covered by the warranties, so it would be a very small percentage of that 175. (TR 489, Lines 10-17)

Utility witness Porter testified that his estimate, representing 5% of the value of the new equipment, was a figure that he had used in previous rate cases and was based on his

experience. (TR 211) He also recalled that the 5% was initially used by EPA in published documents related to operation and maintenance costs that would be associated with facilities built under the 201 program. (TR 211) Another Aloha witness, Mr. Nixon, thought that OPC's witnesses had confused the manufacturer's warranty on equipment failure with the cost of routine maintenance necessary for the proper functioning of the equipment. (TR 777) Mr. Nixon considered it incredible that OPC's witnesses were assuming a manufacturer would pay for all maintenance just because the equipment is guaranteed for one year. (TR 777) Mr. Porter specifically noted that the system must be 100% reliable under DEP Rule 62-610, F.A.C., and that the system required a great deal of preventative maintenance to maintain that 100% reliability. (TR 915)

OPC does not argue that there will be maintenance expense, they merely argue that it will not be near the 5% or \$175,000 figure. They believe that it is Aloha's burden to bring forward an accurate figure that is applicable to the first few years of plant life. (BR 26-27) Mr. Porter, on the other hand, countered that the 5% projected maintenance expense was "certainly fair and reasonable and, if anything, it is understated." (TR 930, Lines 12-13)

CONCLUSION:

A projected maintenance expense is exactly that: projected. There is no crystal ball to reveal what the exact expenses will be for the next year. OPC gave no estimates of its own; it only stated that the utility should produce an accurate figure. (BR 27) From the testimony presented by utility witnesses' Porter and Nixon, it seems evident that the utility used appropriate guidelines (EPA publications) and 25 years' experience (TR 930) in arriving at the 5% estimate. Under cross-examination, OPC witness Bidy acknowledged that he had no experience in the startup or ongoing operation and maintenance of such a wastewater treatment plant. (TR 483)

Staff believes that the projected maintenance costs comply with EPA's guidelines and are justified. Therefore, staff recommends that no adjustment be made to Account 775, Contractual Services-Other, to remove the projected maintenance expense for the new plant.

ISSUE 30: Should any adjustments be made to the base year ended September 30, 1999 balance for miscellaneous expenses?

RECOMMENDATION: Yes. In addition to the adjustments made in Issue 19 and 26, miscellaneous expenses should be reduced by \$7,593 for non-recurring advertising expenses and by \$162 for a misclassification error by the utility, which represents a total reduction of \$7,755. (FLETCHER)

POSITION OF PARTIES

ALOHA: No adjustments are appropriate, other than those agreed to in Issue 26.

OPC: Yes. Aloha incurred a significant increase in Miscellaneous Expenses, which has not been adequately explained. Accordingly, the account should be reduced by \$16,155, and would then reflect the historical average indexed for infiltration and customer growth.

STAFF ANALYSIS: The utility's year-end December 31, 1998 balance for miscellaneous expenses was \$21,406, and its adjusted year-end September 30, 1999 balance was \$57,861. (EX 5, MFRs Vol. I, Schedule B-8(C), page 54) OPC witness Larkin testified that the utility has incurred approximately \$24,000 in miscellaneous expenses based on its average calendar year-end levels from 1996-1998. (TR 224) After removing the utility's \$18,400 payment to DEP resulting from the ARCFJ, Mr. Larkin stated that the balance still increased by approximately 67% and that the utility has not explained this dramatic increase. (TR 224-225) As a result, Mr. Larkin proposed that the appropriate balance for September 30, 1999 should be equal to the average 1996-1998 calendar year-end balance escalated by customer growth and inflation for nine months. (TR 224)

In its MFRs, the utility stated that the increase to miscellaneous expenses was a result of additional advertising costs for new employees and miscellaneous operating costs for DEP compliance. (EX 5, MFRs Vol. I, Schedule B-8(C), page 54) In his rebuttal testimony, utility witness Nixon stated that he had reviewed all of the miscellaneous expense account, and based on this review, he provided an exhibit which listed the specific increases from the 1998 calendar year-end to the September 30, 1999 historical base year. (TR 778-779) (EX 22, RCN-4) In its brief, the utility argued that Mr. Nixon's rebuttal exhibit RCN-4 fully

explains the increase of the historical base year miscellaneous expense. (BR 40)

As stated earlier, on March 9, 1999, the utility executed an ARCFJ with DEP. Both OPC witness Larkin and utility witness Nixon testified that the expense items listed as advertising expenses on Nixon's rebuttal exhibit RCN-4 are for the new employees required by the ARCFJ. (TR 385, 848-849) (EX 5, MFRs Vol. III, pages 184-197) Staff believes that the execution of a ARCFJ with DEP is not likely to occur every year. As such, staff believes that the advertising expenses resulting from the ARCFJ are non-recurring expenses. As stated earlier in Issue 26, staff notes that utility witness Nixon testified that the legal expenses associated with the ARCFJ were non-recurring and should be amortized over 5 years. (EX 13, TES-1, page 15) (EX 22, RCN-11, page 4) Rule 25-30.433(8), F.A.C., states that "[n]on-recurring expenses shall be amortized over a 5-year period unless a shorter or longer period of time can be justified." As such, staff believes the total advertising expenses of \$8,206 that is listed on Mr. Nixon rebuttal exhibit RCN-4 should be amortized over 5 years.

In addition, Mr. Nixon's rebuttal exhibit RCN-4 indicated that an insurance premium payment of \$1,296 was misclassified by the utility as a miscellaneous expense and that it should have been recorded in Account 757, Insurance - General Liability. According to Schedule G-1, pages 139-140 of Volume I of its MFRs, the utility escalated miscellaneous expenses by customer growth and inflation, but did not escalate Account 757, Insurance - General Liability. Thus, staff believes that one year's amortization of the total advertising expenses of \$8,206 should be recognized, but the utility's escalation of the \$8,206 for customer growth and inflation should be removed because it is a non-recurring expense. Further, staff believes that Account 757, Insurance - General Liability should be increased by \$1,296 and that miscellaneous expenses should be decreased by that amount plus the amount for the utility's escalation of the \$1,296 for customer growth and inflation.

Based on the above, staff agrees with the utility that the increase of the historical base year miscellaneous expenses has been fully explained; however, staff recommends that miscellaneous expenses be reduced by \$7,593 for non-recurring advertising expenses and by \$162 for a misclassification error by the utility, which represents a total reduction of \$7,755. The following table illustrates staff's adjustments.

Advertising Expense Adjustment

	<u>Intermediate Projected Amount</u>	<u>Final Projected Test Year Amount</u>
Historical TY Amount	\$8,206	\$8,705
Aloha's Growth Factor	<u>X 1.04812</u>	<u>X 1.04812</u>
	\$8,601	\$9,124
Inflation Factor	<u>X 1.0121</u>	<u>X 1.0121</u>
	<u>\$8,705</u>	<u>\$9,234</u>

Final Projected TY Amount - Advertising Expense	\$9,234
Less: Historical Teat Year Amount	<u>\$8,206</u>
Customer Growth and Inflation Adjustment	<u>\$1,028</u>
Total Amount of Non-recurring Advertising Exp.	(\$8,206)
Plus: One Year's Amortization (\$8,206/5 years)	1,641
<u>Less: Customer Growth and Inflation Adjustment</u>	<u>(1,028)</u>
<u>Total Adjustment for Non-recurring Advert. Exp.</u>	<u>(\$7,593)</u>

Misclassification Adjustment

	<u>Intermediate Projected Amount</u>	<u>Final Projected Test Year Amount</u>
Historical TY Amount	\$1,296	\$1,374
Aloha's Growth Factor	<u>X 1.04812</u>	<u>X 1.04812</u>
	\$1,358	\$1,440
Inflation Factor	<u>X 1.0121</u>	<u>X 1.0121</u>
	<u>\$1,374</u>	<u>\$1,458</u>

Final Projected TY Amount - Advertising Expense	\$1,458
<u>Less: Historical Teat Year Amount</u>	<u>\$1,296</u>
<u>Customer Growth and Inflation Adjustment</u>	<u>\$ 162</u>

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

RECOMMENDATION: Total current rate case expense of \$426,676 should be allowed. This results in an increase of \$126,676 above the revised estimate in the MFRs and a decrease of \$46,139 to the updated rate case expense per Exhibit 22. (BINFORD)

POSITION OF PARTIES

ALOHA: The appropriate allowable rate case expense is the amount shown in Mr. Nixon's updated rebuttal exhibits.

OPC: Only prudently incurred rate case expense should be allowed and amortized over four years.

STAFF ANALYSIS: In its revised MFRs, the utility requested an estimate of rate case expense of \$300,000 for this case. (EX 5, MFRs Vol. I, Schedule B-10, page 56) Aloha originally requested \$275,000 in rate case expense, but increased that amount to \$300,000 after filing revised MFRs. According to utility witness Nixon, rate case expense was increased by \$25,000 in order to cover the costs of preparing additional new information required by staff. (TR 189)

In Exhibit 22, Aloha updated its actual rate case expense figures as of October 6, 2000, with a revised estimate to complete. That exhibit indicates total rate case expense (actual expenses and estimates to complete) to be \$472,815 for the current rate proceeding. The components of total rate case expense are summarized as follows:

	<u>PER MFRs</u>	<u>PER EX 22</u>
Cronin, Jackson, Nixon, and Wilson, CPAs	\$125,000	\$185,879
Rose, Sundstrom, and Bentley	110,000	229,031
David Porter, PE	50,000	33,220
In House	<u>15,000</u>	<u>24,685</u>
Total	\$300,000	\$472,815

Section 367.081(7), Florida Statutes states that "[t]he Commission shall determine the reasonableness of rate case expenses

and shall disallow all rate case expenses determined to be unreasonable. No rate case expense determined to be unreasonable shall be paid by a consumer."

There are five adjustments that are addressed in this issue concerning rate case expense for this proceeding. The adjustments are as follows: (1) legal expenses associated with filing the emergency variance or waiver, (2) costs associated with filing revisions to the MFRs, (3) filing fee that was double charged, (4) accounting and legal expenses associated with supplemental rebuttal testimony disallowed, and (5) legal and engineering fees that were estimated for reconsideration.

Emergency Variance

In addressing the issue of legal expenses associated with the emergency variance, staff witness Merchant testified that if the utility had addressed this need early on during the test year approval the utility could have determined whether it could comply with the rule on a timely basis and avoided the cost of any rule waiver, whether emergency or not. (TR 688) She further stated that if the utility had looked at their circumstances in October 1999, they could have spent seven to ten to 21 days getting information to comply with the MFRs and would not have needed a waiver at all. (TR 704)

Ms. Merchant testified that after the utility saw staff's recommendation on the emergency variance, they completed the requirement within a week. The utility then withdrew its emergency request for variance. In her experience in dealing with waivers, Ms. Merchant testified that when the Commission has disallowed the waiver, the rate case costs associated with that waiver have also been disallowed. (TR 714-715) Concerning the emergency request for waiver filed by the utility, there was no decision made due to the fact that the utility withdrew its request. (TR 747) Ms. Merchant proposed removing \$10,014 from rate case expense for legal fees related to filing the emergency request for variance. (TR 674)

In his rebuttal testimony, utility witness Deterding testified that prior to filing its Application on February 9, 2000, the utility had planned to copy all of its hundreds of maps and provide them to staff. (TR 938) Mr. Deterding testified that the facts did not come to light concerning the specifics of this issue until shortly before the date of the rate case filing. (TR 940)

Approximately one to two weeks before the Application was filed, the utility contacted Mr. Crouch, chief staff engineer.

They discussed the issue of what maps were needed in order to comply with the Commission's minimum filing requirements as contained in Rule 25-30.436(6), F.A.C. According to Mr. Deterding's testimony, Mr. Crouch agreed that if the utility's facilities were contributed he did not need maps of the systems at all and that a waiver would be appropriate. (TR 938) In his testimony, Mr. Deterding stated that the utility simply "called the person for whom the information was requested, who would utilize the information, who would determine whether or not it was appropriate to waive the rule requirement, and inquired of them whether they thought it was appropriate under these circumstances for the utility to seek a waiver." (TR 952, Line 21 through TR 953, Line 1)

Mr. Deterding testified that the actions of the utility were an attempt to spend the least amount of money complying with the rule. Once it became apparent that action on the waiver or variance would, at a minimum, be delayed, if not rejected altogether, plus additional legal time in dealing with the waiver issue, the utility decided that the cheapest alternative was to try and come up with something that would comply with the rule as judged by the staff engineer. (TR 943) Mr. Deterding sponsored an exhibit with his testimony that detailed the portion of the February 2000 bill related to the rule waiver. According to Exhibit 30, FMD-2, the amount is \$6,205.

Staff agrees with Ms. Merchant's testimony. Given the time frame in which the utility provided maps after reading the recommendation, staff believes that the filing of the emergency request for variance was imprudent. Because the utility chose to not proceed with its waiver request and no waiver was ever obtained, staff believes the costs associated with that waiver request should be disallowed. Since Mr. Deterding provided a detail exhibit of the actual cost associated with the rule waiver, staff recommends reducing rate case expense by the amount that Mr. Deterding sponsored in his exhibit which was \$6,205.

In its updated rate case expense, utility witness Watford included the cost of the maps. (EX 22) Since the utility did provide the maps, staff believes that the cost of the maps should be included in rate case expense.

MFR Deficiencies

In addressing the issue of costs associated with filing revisions to the MFRs, staff witness Merchant testified that "rate case expense associated with fixing MFR deficiencies should be

disallowed to the extent the costs duplicated or corrected information that was previously filed in the MFRs." (TR 688, Lines 22-25) Ms. Merchant testified that one of the deficiencies that staff identified was the lack of support for projection methodologies. Rule 25-30.437(3), F.A.C., states in part that "(a) schedule shall also be included which describes in detail all methods and bases of projection, explaining the justification for each method or basis employed." She continued to explain that staff has interpreted this rule to mean that all items and accounts projected in a projected test year rate base should be explained fully so that the Commission and parties can take an historical balance reflected in the MFRs and calculate both the intermediate and projected test year amounts. She further stated that this does not mean the utility should provide all specific calculations, but that the user should be able to follow the utility's logic and get similar projected results. (TR 677-678)

Ms. Merchant testified that, especially for a projected test year, as one comes up with assumptions for the projections, they should write down the assumptions as they are developed (or decided on) before one forgets them. "If you are writing them down, you might as well design a document that can be submitted with the minimum filing requirements. . . ." (TR 724, Lines 19-21) Ms. Merchant further states that one has to think through things when planning a projected year. Every single account needs to be looked at to determine whether it is going to be projected or not. Ms. Merchant states that what she has seen in a lot of different cases is that the notes concerning projections are created as they go along. (TR 727) She has stated that a utility has the responsibility to provide the necessary information to the Commission so that the filing can be processed within the statutory deadline. Ms. Merchant proposed removing a total of \$21,725 from rate case expense for accounting fees of \$18,669 and legal fees of \$3,056 associated with the deficiencies. (TR 679)

In his rebuttal testimony, Mr. Nixon stated that staff was requiring additional information as a deficiency. Therefore, they had to reproduce their work papers to show how each account was projected. (TR 189) Mr. Nixon testified that the calculation of the specific amounts by month could have been verified by the PSC auditors. (TR 189)

Concerning the time to develop the schedule, Mr. Nixon states that it would be incurred whether the schedule was created with the original filing or after the deficiency letter was issued. (TR 830) The utility considers the deficiencies as additional information

for the filing and also argues that this is not duplication or a correction due to the fact the information did not exist.

Concerning errors identified, Mr. Nixon stated that he believed no more than 8 to 10 hours of work was required to correct the items that he identified as errors. He testified that he wrote off and discounted fees totaling \$6,237 of rate case expense to reflect the correction of errors. (TR 795, TR 830)

Staff notes that disagreement exists as to whether the items identified as deficiencies were actually deficiencies. During his testimony, Mr. Nixon admitted that there were specific items that may not have been completely explained in the MFRs, but he considered these items minor points or items that the PSC auditors could have calculated. (TR 861-863) Ms. Merchant testified that she did not believe it was an audit function to obtain information that should be filed in the MFRs. (TR 676-677) Pursuant to Rule 25-30.437(3), F.A.C., it appears that a utility must provide a schedule which describes in detail all methods and bases of projections.

Staff agrees with Ms. Merchant's testimony. Although Ms. Merchant has not prepared MFRs, she has been involved in reviewing and analyzing filed MFRs for over 15 years. (TR 732) In considering a projected test year, one would logically think that some kind of workpapers were developed as the MFRs were developed to determine what projection methodology would be applied and how the projection methodology would be applied.

Staff recommends disallowing the rate case expense related to the MFR deficiencies. As stated earlier, Mr. Nixon testified that he wrote off and discounted fees totaling \$6,237 of rate case expense to reflect the correction of errors. Further, rate case expense should be reduced by the amount of \$18,669 for accounting fees associated with the MFR deficiencies after Mr. Nixon's adjustment for errors/corrections. (EX 22, RCN-9) Rate case expense should also be reduced by \$3,056 for legal fees associated with the MFR deficiencies. Therefore, staff recommends reducing rate case expense by a total of \$21,725 for costs related to MFR deficiencies. The follow table illustrates staff's adjustment for MFR deficiencies.

	<u>Amounts</u>
Total Cost for MFR Deficiencies (Per EX 22, RCN-9)	\$24,909
Write-Offs/Discount by Nixon	<u>(6,237)</u>
Net Accounting Bill to Revise MFRs	\$18,669
Legal Cost for MFR Deficiencies	<u>3,056</u>
Total Adjustment for MFR Deficiencies	\$21,725

Filing Fee

In the invoices filed to support rate case expense, the utility included the filing fee of \$4,500 as an in-house cost and as a legal expense. Mr. Nixon acknowledged that to the extent the fee is in there twice, it should be taken out. (TR 875) Staff recommends rate case expense be reduced by \$4,500.

Supplemental Rebuttal Testimony

The utility filed supplemental rebuttal testimony much of which was ultimately disallowed as improper rebuttal. Because much of the testimony was disallowed as improper, staff believes that rate case expense should be reduced for the accounting and legal fees associated with filing the stricken supplemental rebuttal testimony. Since the rate case expense was updated with actual expenditures through October 6, 2000 and estimates to complete, staff did not have an actual amount to make an adjustment for the disallowed testimony which was filed October 23, 2000.

The Commission has broad discretion with regard to rate case expense. Florida Crown Utility Services, Inc. v. Utility Regulatory Bd. of Jacksonville, 274 So. 2d 597, 598 (Fla. 1st DCA 1973). Staff recommends adjusting rate case expense for the disallowed testimony. Staff made an adjustment as described below:

$$A = (B/C) * (D * ((F/G) * E))$$

where A is the adjustment amount
B is the number of lines of Nixon's supplemental
rebuttal testimony disallowed
C is the total number of lines of Nixon's supplemental
rebuttal testimony
D is the hourly rate charged by Mr. Nixon

E is the number of pages of Nixon's supplemental
rebuttal testimony filed
F is the number of hours charged by Mr. Nixon for his
rebuttal testimony
G is the number of pages of Nixon's rebuttal testimony

Numerically, the adjustment is as follows:

$$144.36 = (100/133)*(160*((14/70)*6))$$

Staff used the rebuttal testimony filed to approximate the number of hours per page Mr. Nixon used for his supplemental rebuttal testimony. Staff also made an adjustment for the exhibits that Mr. Nixon filed with his supplementary rebuttal testimony. Again, staff didn't have an actual amount associated with the exhibit. After analyzing the complexity of the information contained in the exhibit, staff made a conservative estimate that Mr. Nixon spent about 10 hours preparing the exhibit. This results in an adjustment of \$1,744 (\$144 + (\$160*10)) for Mr. Nixon's disallowed supplemental rebuttal testimony.

To be consistent, staff also reduced legal fees associated with filing the supplemental rebuttal testimony. Staff used the rebuttal testimony filed to approximate the number of hours per page Mr. Deterding used for the review of the supplemental rebuttal testimony. Staff made an adjustment as described below:

$$A = (B/C)*(D*((F/G)*E))$$

where A is the adjustment amount

B is the number of lines of Nixon's supplemental
rebuttal testimony disallowed

C is the total number of lines of Nixon's supplemental
rebuttal testimony

D is the hourly rate charged by Mr. Deterding

E is the number of pages of Nixon's supplemental
rebuttal testimony filed

F is the number of hours charged by Mr. Deterding for
his review of the rebuttal testimony for Porter,
Nixon, Deterding, and Watford

G is the total number of pages of rebuttal testimony
for Porter, Nixon, Deterding, and Watford

Numerically, the adjustment is as follows:

$$45.11 = (100/133)*(200*((6.42/117)*6))$$

Therefore, staff recommends decreasing rate case expense by a total of \$1,794 for accounting and legal cost related to the filing of the disallowed supplemental rebuttal testimony and exhibits.

Reconsideration

As discussed earlier, in Exhibit 22, Aloha updated its actual rate case expense figures as of October 6, 2000, with a revised estimate to complete. As part of the estimate to complete, legal fees of \$10,500 and engineering fees of \$1,600 were included for reconsideration. Because it is not known whether the utility will request reconsideration of the Order arising from this proceeding, it would be premature to include this cost in rate case expense. It has been the Commission's practice not to include the allowance of cost estimates for reconsideration or appeals in rate case expense. (See Orders Nos.: 22226, issued November 27, 1989, in Docket No. 880882-WU; PSC-97-0280-FOF-WS, issued March 12, 1997, in Docket Nos. 950615-SU and 960545-WS; and PSC-93-0295-FOF-WS, issued February 24, 1993, in Docket No. 910637-WS.) Since reconsideration is considered a possibility, not a certainty, rate case expense should be reduced by \$12,100. If a motion for reconsideration is filed, a determination should be made at that time as to the reasonableness of the amounts requested and whether inclusion of those amounts are appropriate.

Summary

After a thorough evaluation of the record, staff recommends that the appropriate total rate case expense for this proceeding is \$426,676.

	<u>PER MFR</u> <u>ESTIMATED</u>	<u>PER EX 22</u> <u>UTILITY</u> <u>REVISED</u> <u>ACTUAL</u>	<u>STAFF</u> <u>ADJUSTMENTS</u>	<u>STAFF</u> <u>ADJUSTED</u> <u>BALANCE</u>
Cronin, Jackson, Nixon, and Wilson, CPAs	\$125,000	\$185,879	(\$20,413)	\$165,466
Rose, Sundstrom, and Bently	110,000	229,031	(24,126)	204,905
David Porter, PE	50,000	33,220	(1,600)	31,620
In House	<u>15,000</u>	<u>24,685</u>	<u>0</u>	<u>24,685</u>
Total	<u>\$300,000</u>	<u>\$472,815</u>	<u>(\$46,139)</u>	<u>\$426,676</u>

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Based on the record and the staff recommended adjustments discussed above, staff recommends that current rate case expense of \$426,676 be allowed. This results in an increase of \$126,676 above the revised estimate in the MFRs and a decrease of \$46,139 to the updated rate case expense per Exhibit 22.

ISSUE 32: What is the appropriate amortization period and amount of contributed taxes (CTs) associated with the Seven Springs wastewater system?

RECOMMENDATION: The appropriate amortization period is 32.68 years or 3.06%, and the appropriate annual amortization amount is \$47,273. Thus, the utility's annual amortization amount should be increased by \$8,651. (FLETCHER)

POSITIONS

ALOHA: Aloha agrees an adjustment is appropriate to utilize a 32.68 year life. This equates to a composite rate of 3.06 percent, which is the composite rate for all CIAC during the period CIAC was taxable (1987-1996).

OPC: The composite life of 26.9 years for the CIAC assets should be used. This results in an increase in amortization of the tax by \$18,808.

STAFF ANALYSIS: In its MFRs, the utility stated that Aloha uses a 2.5% rate to amortize CTs for its Seven Springs water and wastewater systems. (EX 5, MFRs Vol. I, Schedule G-6, page 160) OPC witness Larkin testified that, consistent with staff audit workpapers, the CTs for the Seven Springs wastewater system should be amortized over 26.9 years or a 3.2% rate, which is the composite rate for Aloha's CIAC assets for the calendar year-end 1998. (TR 226, 385)

In his rebuttal testimony, utility witness Nixon agreed that its 2.5% amortization rate should be changed and asserted that the appropriate amortization rate is 3.06%, which represent the composite CIAC amortization rate for CIAC assets acquired for Aloha's Seven Springs wastewater system during the period of 1987 to 1996 when CIAC was taxable. (TR 782-783)(EX 22, RCN-6) Mr. Nixon stated that to use the current rate distorts the true depreciable life of these assets because of the addition of significant amounts of assets with shorter lives after 1996. (TR 782-783)

Consistent with the theory of normalization, the Commission determined that the benefits of CTs shall be passed back to the ratepayers over the lives of the related assets. See Order No. 23541, issued October 1, 1990, in Docket No. 860184-PU. Staff believes Mr. Nixon's recommended 3.06% composite amortization rate complies with the Commission's directive in Order No. 23541 that

the utility pass back the benefits of CTs to ratepayers over the lives of related assets. According to Schedule G-6, page 160 of Volume I of its MFRs, the annual amortization of CTs for its Seven Springs wastewater system was \$38,622. The 3.06% amortization rate yields an annual amortization of \$47,273. Therefore, staff recommends that the utility's annual amortization amount should be increased by \$8,651 (\$47,273 less \$38,622).

ISSUE 34: What is the test year operating income before any revenue increase?

RECOMMENDATION: The test year operating income should be \$131,673 for wastewater before any revenue increase. (BINFORD)

POSITIONS

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

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

STAFF ANALYSIS: The issue is subject to resolution of other issues related to revenues and operating expenses and rate base, and is primarily a "fall-out" number.

Based on the adjustments discussed in previous issues, staff recommends that the test year operating income before any provision for increased revenues should be \$131,673 for wastewater. The schedule for wastewater operating income is attached as Schedule No. 3-A and the adjustments are shown on Schedule No. 3-B.

REVENUE REQUIREMENT

ISSUE 35: What is the appropriate revenue requirement?

RECOMMENDATION: The following revenue requirement should be approved: (BINFORD)

	<u>TOTAL</u>	<u>\$ INCREASE</u>	<u>% INCREASE</u>
Wastewater	\$4,095,504	\$1,369,589	50.24%

POSITIONS

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

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

STAFF ANALYSIS: The issue is a summary computation that is subject to the resolution of other issues related to rate base, cost of capital, and rate base, and is primarily a "fall-out" number. The computation of the revenue requirement is shown on Schedule 3-A and is \$4,095,504 which represents an increase of \$1,369,589 or 50.24%.

RATES

ISSUE 36: What are the appropriate final wastewater rates?

RECOMMENDATION: Consistent with staff's recommendations in Issues 18 and 19, the recommended rates should be designed to allow the utility the opportunity to generate annual operating revenues of \$4,059,430 for its Seven Springs wastewater system, excluding miscellaneous service revenues, interest income on its cash operating account, and reuse revenues. The utility should be required to file revised tariff sheets and proposed customer notice to reflect the appropriate rates pursuant to Rule 25-22.0407(10), F.A.C. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), F.A.C., provided the customers have received notice. The rates should not be implemented until proper 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. (FLETCHER)

POSITIONS

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

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

STAFF ANALYSIS: The final rates requested by the utility are designed to produce revenues of \$4,374,495 for its Seven Springs wastewater system. The requested revenues represent an increase of \$1,593,501 or 57.29%.

Consistent with staff's recommendations in Issues 18 and 19, the final rates approved for the utility's Seven Springs wastewater system should be designed to produce annual revenues of \$4,059,504 for its Seven Springs wastewater system, which is an increase of \$1,369,589 or 50.24%. This recommended increase excludes miscellaneous service revenues, interest income on its cash operating account, and reuse revenues.

The utility should be required to file revised tariff sheets and a proposed customer notice to reflect the appropriate rates pursuant to Rule 25-22.0407(10), F.A.C. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), F.A.C.,

provided the customers have received notice. The rates should not be implemented until proper 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.

A comparison of the utility's present rates, Aloha's requested rates, and staff's recommended final rates are shown on Schedule No. 4.

ISSUE 37: Should the Commission determine a reuse rate in this proceeding, and if so, what is the appropriate rate?

RECOMMENDATION: Yes. Staff recommends no charge for the Fox Hollow Golf Course from the date it begins receiving reuse service from Aloha to exactly four years from that date, at which time, the utility should begin charging the approved charge for all other reuse customers. In addition, staff recommends that, in the future, the utility should file an application for new reuse rates or changes in reuse rates, pursuant to Section 367.091, Florida Statutes. Further, staff recommends that the utility's current reuse rate of \$0.25 per thousand gallons should be increased to \$0.29 per thousand gallons and that the zero rate for the Mitchell property be continued. The utility should be required to file revised tariff sheets and proposed customer notice to reflect the appropriate rates pursuant to Rule 25-22.0407(10), F.A.C. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), F.A.C., provided the customers have received notice. The rates should not be implemented until proper 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. (FLETCHER, JAEGER)

POSITIONS

ALOHA: Yes. However, it should be kept in mind that the higher the rate, the less likely Aloha will be able to sell the effluent in the first place.

OPC: The Citizens take no position on this issue.

STAFF ANALYSIS: The utility currently charges the Mitchell Property a zero rate and all others a \$0.25 rate per thousand gallons. (EX 5, MFRs Vol. I, Schedules E-1 and G-1, pages 109 and 138) In Aloha's 1995 reuse proceeding, the Commission agreed with the utility that the reuse rate should be market-based to encourage new customers. Since Pasco County was the nearest utility that provided reuse service and had a rate of \$0.28 per thousand gallons, the Commission agreed that the utility's proposed rate of \$0.25 per thousand gallons was market-based. Further, the Commission stated that this rate was just, fair and reasonable for the inception of the reuse system, with the knowledge that the rate is subject to increase in subsequent proceedings. See Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, in Docket No. 950615-SU and 960545-WS. Consequently, the Commission required Aloha's next

rate filing to contain information sufficient to enable the Commission to address reuse rates for all reuse customers.

Staff witness Merchant stated that "Aloha did not provide information in its application, that [she has] found, supporting any reuse determination." (TR 669, Lines 1-2) Aloha used the current \$.025 rate, but did not provide any support as to whether the current or any other reuse rate was appropriate.

Also, Ms. Merchant, in her direct testimony, agreed with the Commission's decision in the 1995 reuse proceeding to establish market-based reuse rates. (TR 669) Since the Commission used the reuse rate for Pasco County as a benchmark, Ms. Merchant believed that it was appropriate to review its rate in determining whether Aloha's reuse rate should be changed. (TR 669) Ms. Merchant stated that according to the DEP's 1999 Reuse Inventory Report, Appendix H, the Central Pasco County Reuse System has a non-residential reuse gallonage charge of \$0.32 per thousand gallons, which represents a \$0.04 per thousand gallon increase from the 1995 reuse proceeding. (TR 668-669) (EX 18, PWM-2, Page 4) As a result, Ms. Merchant believes that Aloha's rate should be increased. (TR 669) In fact, Ms. Merchant testified that Aloha's rate should be equal to Pasco County's rate because the two providers are not in competition. (TR 669)

Through cross-examination by staff, utility witness Watford, the utility's president, testified that the goal of Aloha's reuse system should be to get the system utilized and that successful reuse systems initially make it free or set a \$0.05 per thousand gallon rate. (TR 611) Mr. Watford noted that Pasco County's reuse system is in a much different situation than Aloha, in that the County's system runs dry during certain periods of the year. Therefore, the County has already built up a clientele with sufficient demand to take all the effluent the County's system can generate. (TR 610) Mr. Watford asserted that increasing the rate is counterproductive to the ultimate purpose of effluent disposal and secondly to encourage participation in the system. (TR 612, 613) (BR 45) In its brief, the utility argued that the reuse rate should be lowered, rather than increased for the short-term. (BR 45)

As stated above, the utility in its initial filing did not provide any information to support a change in the current reuse rate. However, for the first time in his rebuttal testimony, utility witness Porter testified that the utility's MFRs were in error in assuming that revenue will be derived from the Fox Hollow Golf Course because this customer is not required to pay for reuse

water until four years after it begins receiving reuse. Mr. Watford noted that the utility had to give concessions to Rexbo Reality, Inc., the owner of the Fox Hollow Golf Course and Aloha's largest anticipated reuse user. (TR 615-617, 621) Mr. Watford explained that the concessions were that it would not pay for reuse for the first four years; otherwise, the golf course would have been lost to Pasco County and Aloha would not have had a place for its effluent. (TR 615-617, 621)(EX 16) Mr. Watford stated that in its prior case (over three years ago) that Mr. Bramlett from Pasco County testified that the vast majority of the County's effluent is given away to golf courses. (TR 617) Lastly, Mr. Watford testified that Pasco County has the ability to distribute reuse county-wide. (TR 618)

Staff notes that the utility did not include in its MFRs a request for a zero rate for the Fox Hollow Golf Course. However, based on the arguments presented by Mr. Watford, staff believes the utility's decision to offer the concession of a zero rate for the first four years to the Fox Hollow Golf Course was appropriate. Therefore, staff recommends no charge for the Fox Hollow Golf Course from the date it begins receiving reuse from Aloha to exactly four years from that date, at which time, the utility should begin charging the approved charge for all other reuse customers. In addition, staff recommends that in the future the utility should file an application for new reuse rates or changes in reuse rates, pursuant to Section 367.091, Florida Statutes.

Based upon a review of the record, staff agrees with Ms. Merchant to the extent that it appears that competition does not exist at this time between the utility and the County with respect to the provision of reuse service to Aloha's customers. The concessions agreed to by the utility which amount to the utility not charging the Fox Hollow Golf Course for reuse service for the first four years of service provides assurance to the utility that it has secured this reuse customer, at least for the time being. Moreover, there is no evidence in the record to suggest that the utility and the County are competing for any other reuse customer(s) at this time.

Nevertheless, Mr. Watford testified that the County could have provided reuse to the Fox Hollow Golf Course and that the County has the ability to distribute reuse on a County-wide basis. Additionally, staff notes that the Commission has found that a utility's wastewater certificate does not carry with it any exclusive right to provide reuse within that territory and that Chapter 367, Florida Statutes, does not address certification for separate reuse service territory. Order No. PSC-98-0391-FOF-SU,

issued March 16, 1998, in Docket No. 960288-SU (In re: Application for approval of reuse project plan in Seminole County by Alafaya Utilities, Inc.).

A utility's water territory might be, and often is, different than its wastewater territory. The same can and will be true of wastewater service and reuse service. Potential reuse customers can be located within a utility's wastewater territory, its water territory, or in some other utility's territory which might be unable to provide reuse to the customer.

Id. At 26. The Commission also found that "[a]s more utilities enter the reuse arena or seek to expand their existing reuse customer base, it will be increasingly important that the issue of reuse territory be addressed." Id. For the foregoing reasons, staff believes that competition does or will exist between the utility and the County for future reuse customers, although the extent of such competition cannot be determined from the evidence of record.

As stated in the case background, the utility's service area is located within the Northern Tampa Bay Water Use Caution Area as designated by SWFWMD. Critical water supply concerns have been identified by SWFWMD within this area. Moreover, the Legislature has recognized the benefit of reuse to the State, as evidenced by Sections 367.0817(3), 403.064(1), and 373.250(1), Florida Statutes. For these reasons, staff believes that it is appropriate to set a reuse rate in this case that will attract reuse buyers.

As stated earlier, Ms. Merchant recommended a reuse rate of \$0.32 per thousand gallons for all reuse customers with the exception of the Mitchell property, and Mr. Watford suggested no charge or a reuse rate of \$0.05 per thousand gallons for all reuse customers. Consistent with the Commission's decision in the utility's last reuse proceeding to set Aloha's rate three cents lower than Pasco County's rate, staff believes that a reuse gallonage charge of \$0.29 per thousand gallons for the reuse customers is appropriate. Thus, staff recommends that the utility's current reuse rate of \$0.25 per thousand gallons for all reuse customers except the Mitchell property and the Fox Hollow Golf Course should be increased to \$0.29 per thousand gallons. Staff notes that this recommended increase represents a \$0.04 per thousand gallon increase, which corresponds to the level of increase experienced by the County's reuse customers. In so recommending, staff again notes that "it is the [Commission's] prerogative to evaluate the testimony of competing experts and

accord whatever weight to the conflicting opinions it deems necessary." Gulf Power Co. v. FPSC, 453 So. 2d 799, 805 (Fla. 1984). Staff also notes that not charging the Fox Hollow Golf Course for reuse service for four years results in differing rates being charged among reuse customers. Given that the Legislature has recognized the benefit of reuse to the state and that the Commission encourages reuse, staff does not believe that charging differing reuse rates among reuse customers is unfairly discriminatory. See 367.081(2)(a)1., Florida Statutes (2000).

For the foregoing reasons, staff recommends that the Fox Hollow Golf Course not be charged for reuse from the date it begins receiving reuse service from Aloha to exactly four years from that date, at which time, the utility should begin charging the approved charge for all other reuse customers. In addition, staff recommends that, in the future, the utility should file an application for new reuse rates or changes in reuse rates, pursuant to Section 367.091, Florida Statutes. Further, staff recommends that the utility's current reuse rate of \$0.25 per thousand gallons should be increased to \$0.29 per thousand gallons.

The utility should be required to file revised tariff sheets and a proposed customer notice to reflect the appropriate rates pursuant to Rule 25-22.0407(10), F.A.C.. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), F.A.C., provided the customers have received notice. The rates should not be implemented until proper 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.

ISSUE 37A: Should any portion of the utility's proposed final rates implemented pursuant to Section 367.081(6), Florida Statutes, be refunded?

RECOMMENDATION: Yes. Consistent with staff's recommendation in Issue 36, staff recommends that the utility should refund 6.03% of the service rates collected during the period of time Aloha collects revenues under its proposed final rates. Further, staff recommends that the utility administer this refund, pursuant to Rule 25-30.360, F.A.C. (FLETCHER)

STAFF ANALYSIS: At the January 2, 2001 Agenda Conference, the Commission acknowledged Aloha's implementation of its proposed final rates, pursuant to Section 367.081(6), Florida Statutes. The increased revenues from Aloha's proposed final rates were held subject to refund. As stated in Issue 36, the final rates requested by the utility are designed to produce revenues of \$4,374,495 for its Seven Springs wastewater system. The requested revenues represent an increase of \$1,593,501 or 57.29%. In addition, as discussed in Issue 36, the final rates approved for the utility's Seven Springs wastewater system should be designed to produce annual revenues of \$4,095,504 for its Seven Springs wastewater system, which is an increase of \$1,369,589 or 50.24%. The result is a revenue level that is less than the utility's final proposed revenue requirement. However, since the utility's requested reuse rate is less than staff's recommended rate of \$0.29 per thousand gallons and because there were no projected changes in the historical balances of miscellaneous service revenues or interest income on the cash operating account, the only comparison for refund purposes should be the utility's requested final revenues for residential and general service and staff's recommended final revenues for residential and general service.

Based on the above and consistent with staff's recommendation in Issue 36, staff recommends that the utility should refund the percentage of the difference of the utility's proposed final revenue requirement for residential and general service and staff's recommended final revenue requirement for residential and general service divided by Aloha's proposed final revenue requirement for residential and general service, during the period of time Aloha collected revenues under its proposed final rates. As indicated on Schedule E-13(A) of MFRs Volume I on page 120 (EX 5), the utility's projected final revenue requirement for residential and general service is \$4,305,036 (\$3,937,227 plus \$367,809). As illustrated on the following schedule, staff's recommended projected final revenue requirement for residential and general service is \$4,063,033. This results in a 6.03% ((\$4,305,036 less \$4,045,358)

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divided by \$4,305,036) that should be applied to the revenues collected under Aloha's proposed final rates for residential and general service, in order to determine the appropriate amount of refund. Further, staff recommends that the utility administer this refund pursuant to Rule 25-30.360, F.A.C.

ALOHA UTILITIES, INC. - SEVEN SPRINGS SYSTEM								DOCKET 991643-SU		
SCHEDULE OF PROJECTED TEST YEAR RESIDENTIAL & GENERAL SERVICE REVENUES AT STAFF'S RECOMMENDED FINAL RATES										
FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01										
Line No.	Class/Meter Size	Historical Year Bills	Staff's Project Factor	Projected Test Year Bills	Test Year Consumption (000)	Staff's Project Factor	Projected TY Consumption (000)	Staff's Recommend Final Rates	Staff's Projected Revenues Requirement	
1	Residential									
2	5/8" X 3/4"	101,095	1.07093	108,266				\$14.06	\$1,522,215	
3	M Gallons				591,149	1.07093	633,079	3.43	2,172,402	
4	Total Residential	<u>101,095</u>		<u>108,266</u>	<u>591,149</u>		<u>633,079</u>		<u>\$3,710,740</u>	
5	General Service									
6	5/8" X 3/4"	975	1.07093	1,044				14.06	14,681	
7	M Gallons				9,544	1.07093	10,221	4.12	42,088	
8	1"	255	1.07093	273				35.14	9,596	
9	M Gallons				4,288	1.07093	4,592	4.12	18,909	
10	1 1/2"	108	1.07093	116				70.28	8,129	
11	M Gallons				4,459	1.07093	4,775	4.12	19,664	
12	2"	168	1.07093	180				112.45	20,232	
13	M Gallons				20,295	1.07093	21,735	4.12	89,498	
14	3"	12	1.07093	13				224.90	2,890	
15	M Gallons				1,335	1.07093	1,430	4.12	5,887	
16	4"	24	1.07093	26				351.41	9,032	
17	M Gallons				2,707	1.07093	2,899	4.12	11,937	
18	6"	42	1.07093	45				702.83	31,613	
19	M Gallons				15,099	1.07093	16,170	4.12	66,584	
20	Total General Service	<u>1,584</u>		<u>1,696</u>	<u>57,727</u>		<u>61,822</u>		<u>\$350,740</u>	
21	Total Projected Residential and General Service Revenues, per staff (Issue 19)									\$4,045,358
22	Total Projected Residential and General Service Revenues, per utility (Schedule E-13(A))									\$4,305,036
23	RESIDUAL OF UTILITY'S PROJECTED REVENUE AND STAFF'S PROJECTED REVENUES									(\$259,678)
24	Refund Percentage ((\$4,305,036 less \$4,063,033) divided by \$4,305,036)									6.03%

ISSUE 38: Who should bear the risk that the company will not find buyers for its reclaimed water?

RECOMMENDATION: Consistent with staff's recommendations in Issues 20 and 37, staff recommends that the risk that Aloha will not find buyers for its reclaimed water should be limited to the anticipated reuse customers for the final September 30, 2001 projected test year. Further, staff recommends that 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 and the revenue collected for the year. (FLETCHER)

POSITIONS

ALOHA: Since these are required improvements to the wastewater system, it is inappropriate for the utility to bear this risk, and contrary to the provisions of Chapter 367 and 403 related to reuse systems.

OPC: The Citizens agree with staff that the utility should bear the risk that it will not find buyers for its reclaimed water.

STAFF ANALYSIS: By Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, in Dockets Nos. 950615-SU and 960545-WS, the Commission found the following:

Upon completion of the project, Aloha will have available to sell 438,000,000 gallons of annual reuse. Based upon a 25% annual growth in reuse sales, coupled with a rate of \$.25 cents per thousand gallons, we have projected reuse revenue of \$27,375, \$54,750, \$82,125 and \$109,500 for the initial four years of the operation of the reuse system upon completion of phase III. Based upon the above reuse revenue, we find that, after implementation of Phase III, the rates shall decrease each year based upon projected reuse revenue. . . . By considering future reuse revenue at this time, the cost of the reuse system is properly shared between the parties that benefit -- the wastewater and reuse customers -- without further action by the utility or this Commission. In this way, the risk associated with finding paying reuse customers would be borne, as it should, by the utility.

Staff witness Merchant testified that the imputed reuse revenues beyond the final September 30, 2001 projected test year is not an appropriate mechanism to reflect the risk of finding new reuse buyers. (TR 671) She asserted that the utility has supported its position that, for the projected test year, it will only be able to sell 189,436,000 gallons (now corrected to 189,435,000 gallons). (TR 671) Ms. Merchant contended that the Commission should not impute revenues for the total amount of reuse disposal capacity in this proceeding. She explained that it is only appropriate to project to the extent that there will be reuse customers during the projected test year because "any imputation beyond that does not consider the increased expenses associated with transmitting the reuse to the customers premises." (TR 671, Lines 12-14)

Further, Ms. Merchant testified that the Commission should monitor the utility's reuse revenue and customers by requiring Aloha to submit additional information in its annual report regarding its reuse service. (TR 671) She explained that "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." (TR 671, Lines 19-21) Further, Ms. Merchant stated that, [f]or residential reuse service, Aloha should provide the number of residential customers by development, the number of gallons sold and the revenue collected for the year." (TR 671, Lines 21-23)

Utility witness Watford testified that Aloha requires all developers along the corridor where its reuse line is located to put in pipes for reuse water in their subdivisions. (TR 609) Mr. Watford asserted that the burden on the utility to locate reuse customers to comply with the ARCFJ is the real issue. (TR 608)(BR 45) In his rebuttal testimony, utility witness Porter agreed with Ms. Merchant that no reuse revenue beyond the projected test year should be imputed and that it is appropriate to monitor the number of reuse customers and the revenue that it generates. (TR 925)

Based on the arguments of Ms. Merchant and consistent with staff's recommendations in Issues 20 and 37, staff recommends that the risk that Aloha will not find buyers for its reclaimed water should be limited to the anticipated reuse customers for the final September 30, 2001 projected test year. Further, staff recommends that 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

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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 and the revenue collected for the year.

ISSUE 39: Should the three-step rate reduction required by Order No. PSC-97-0280-FOF-WS be implemented, modified, or canceled?

RECOMMENDATION: Consistent with staff's recommendation in Issue 38, the three-step rate reduction should not be implemented.
(FLETCHER)

POSITIONS

ALOHA: The three step rate reduction should not be implemented. The Commission should instead monitor Aloha's reuse revenue and customers by requiring the utility to submit additional information in its Annual Report.

OPC: The Citizens take no position on this issue.

STAFF ANALYSIS: Consistent with staff's recommendation in Issue 38, staff recommends the three-step rate reduction should not be implemented.

SERVICE AVAILABILITY CHARGES

ISSUE 40: Should Aloha's Seven Springs wastewater plant capacity charge be revised?

RECOMMENDATION: Yes. Staff recommends that the appropriate plant capacity charge for the utility's Seven Springs wastewater system be set at \$1,650 per residential ERC and \$12.79 per gallon for all others. Further, staff recommends that the utility should file an appropriate revised tariff sheet within twenty days of the date of the Order, and staff should be given administrative authority to approve the revised tariff sheet upon staff's verification that the tariffs are consistent with the Commission's decision. If a revised tariff sheet is filed and approved, the service availability charges should become effective for connections made on or after the stamped approval date of the revised tariff sheet pursuant to Rule 25-30.475(2), F.A.C.. (FLETCHER)

POSITIONS

ALOHA: Yes, to the maximum authorized by the Commission rule. However, if the staff auditor's position on Issue 12 is adopted, application of the rule would likely result in a reduction or elimination of Aloha's service availability charges.

OPC: The Citizens take no position on this issue.

STAFF ANALYSIS: According to Aloha's MFRs, the historical September 30, 1999 balances of plant-in-service, accumulated depreciation, CIAC, and accumulated amortization of CIAC for the Seven Springs wastewater system yielded a CIAC ratio of 61.82%. Based on the utility's MFRs, the CIAC ratio for the projected final test year was 44.42%.

Rules 25-30.580(1) and (2), F.A.C., provide that:

(1) The maximum amount of contributions-in-aid-of-construction, net of amortization, should not exceed 75% of the total original cost, net of accumulated depreciation, of the utility's facilities and plant when the facilities and plant are at their designed capacity; and

(2) The minimum amount of contributions-in-aid-of-construction should not be less than the percentage of such facilities and plant that is represented by the

water transmission and distribution and sewage collection systems.

Through cross-examination by the utility, staff witness McPherson testified that it might be an option to exclude gross-up CIAC from the determination of the 75% maximum level required by Rule 25-30.580(1), F.A.C. (TR 548-549) Staff disagrees that this is an option because this rule makes no exception for this, and without such an exception, all CIAC should be taken into account to determine the CIAC ratio.

Through cross-examination by staff, Mr. Nixon agreed that the Seven Springs wastewater system upgrade was to enable the utility to serve future customers. (TR 840) In addition, he agreed that if the utility's projected CIAC ratio as of September 30, 2001 is less than 75%, then it would be appropriate for the Commission to revise the utility's plant capacity charge to achieve a 75% ratio for the 1.6 MGD plant capacity. (TR 841)

Pursuant to Section 367.101(1), Florida Statutes, "[t]he commission shall set just and reasonable charges and conditions for service availability." Since this construction phase will increase the capacity of the plant to accommodate future growth, the current plant capacity charges should be increased. Consistent with the plant, land, accumulated depreciation, CIAC, and accumulated amortization of CIAC adjustments in other issues, staff utilized the projected calendar year-end September 30, 2001 balances to calculate plant capacity charges. Staff notes that we also included CTs and the net debit-DTAs in our calculation, consistent with staff's recommendation in Issue 10. Based on a January 16, 2001 Agenda Conference, staff assumed that the utility would not begin charging a revised plant capacity charge until the middle of February, 2001. Thus, before proceeding with its calculation of a new charge, staff adjusted the projected year-end September 30, 2001 balances to remove the additions from plant capacity charges at the utility's existing charge of \$206.75 from the middle of February, 2001 to September 30, 2001.

Staff utilized the same composite depreciation/amortization rates that the utility used to calculate its September 30, 2001 year-end depreciation of plant, amortization of plant capacity fees, and amortization of contributed lines. For future growth, staff assumed the same customer growth rate as recommended in Issue 18. With regard to future additions of donated property, staff continued to use the utility's projection of \$390,527 reflected on Schedule G-4 of MFRs Volume I on page 153.

According to the utility's permit for its Seven Springs wastewater system, DEP permitted this system based on AADF. (EX 5, MFRs Vol. III, page 96) In determining the GPD per ERC to reflect the appropriate demand on the system, staff utilized the utility's Discharge Monitoring Reports filed with DEP from September 30, 1999 to August 31, 2000 for the Seven Springs wastewater system in Exhibit 3. Based on these reports, this system reported the AADF of 1,285,000 gallons. As reported on Schedule F-10 of MFRs Volume I on page 131 (EX 5), the utility reported 9,646 ERCs as of September 30, 1999. To equate the total ERCs as of August 31, 2000, staff utilized the recommended growth of 316 ERCs discussed in Issue 18. Specifically, staff used the reported September 30, 1999 balance of 9,646 and added 11 months growth of 290 ERCs ((316 ERCs divided 12 months) multiplied by 11 months), which represents a total of 9,936 ERCs for the year ending August 31, 2000. As a result, staff calculated a GPD per ERC of 129 GPD (1,285,000 AADF divided by 9,936 ERCs).

Based on the above, staff believes that the appropriate plant capacity charge for the utility's Seven Springs wastewater system is \$1,650 per residential ERC and \$12.79 (\$1,650 divided by 129 GPD per ERC) per gallon for all others, and recommends that this charge be approved by the Commission. Staff's analysis is depicted on the following schedule. Further, staff recommends that the utility should file an appropriate revised tariff sheet within twenty days of the date of the Order, and staff should be given administrative authority to approve the revised tariff sheet upon staff's verification that the tariffs are consistent with the Commission's decision. If a revised tariff sheet is filed and approved, the service availability charges should become effective for connections made on or after the stamped approval date of the revised tariff sheet pursuant to Rule 25-30.475(2), F.A.C.

ALOHA UTILITIES, INC. - SEVEN SPRINGS WASTEWATER SYSTEM					DOCKET 991643-SU	
Schedule of Staff's Plant Capacity Charge Calculation						
Plant Capacity Charge:		\$1,650		1,285,000 ADDF From 9/99 to 8/00 9,936 ERCs at 8/31/00 129 GPD per ERC		
	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Capacity	1,600,000	1,600,000	1,600,000	1,600,000	1,600,000	1,600,000
Demand	1,336,000	1,385,253	1,436,224	1,488,971	1,543,557	1,600,045
% Used	83.50%	86.58%	89.76%	93.06%	96.47%	100.00%
Growth	230	381	394	408	422	437
Utility	23,432,345	23,822,872	24,213,399	24,603,926	24,994,453	25,384,980
Accumulated Depreciation	<u>(5,052,977)</u>	<u>(5,888,416)</u>	<u>(6,737,322)</u>	<u>(7,599,695)</u>	<u>(8,475,536)</u>	<u>(9,359,382)</u>
Net Plant	<u>18,379,368</u>	<u>17,934,456</u>	<u>17,476,077</u>	<u>17,004,231</u>	<u>16,518,917</u>	<u>16,025,598</u>
CIAC	13,452,582	14,471,476	15,512,275	16,575,742	17,662,668	18,726,135
Accumulated Amortization	<u>(3,836,837)</u>	<u>(4,338,632)</u>	<u>(4,877,924)</u>	<u>(5,455,551)</u>	<u>(6,072,380)</u>	<u>(6,708,319)</u>
Net CIAC	<u>9,615,744</u>	<u>10,132,843</u>	<u>10,634,350</u>	<u>11,120,190</u>	<u>11,590,288</u>	<u>12,017,817</u>
Net Investment	<u>8,763,624</u>	<u>7,801,613</u>	<u>6,841,727</u>	<u>5,884,040</u>	<u>4,928,629</u>	<u>4,007,781</u>
CIAC Ratio	<u>52.32%</u>	<u>56.50%</u>	<u>60.85%</u>	<u>65.40%</u>	<u>70.16%</u>	<u>74.99%</u>

LEGAL ISSUES

ISSUE 41: Should Aloha be fined in the amount of \$250 for its apparent violation of Order No. PSC-97-0280-FOF-WS for its failure to timely file the extension of the Mitchell agreement with the Commission for approval?

RECOMMENDATION: Yes, pursuant to Section 367.161, Florida Statutes, Aloha should be fined \$250 for its failure to timely comply with Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, which required any extension of the Mitchell contract to be filed with the Commission for approval. The Commission should approve the renewed contract after the fact, but no further extension of the contract after this current term expires should take place until the utility has Commission approval. Moreover, Aloha should either obtain approval of the Commission for another extension of the Mitchell agreement, or charge the Mitchell property the approved system-wide reuse rate upon expiration of this latest extension. (FLETCHER, JAEGER)

POSITIONS

ALOHA: No. The delay in filing this agreement was merely an oversight and the utility had no choice but to extend the Mitchell agreement in order to allow it to continue to dispose of treated effluent or face being in violation of DEP and EPA requirements.

OPC: The Citizens agree with staff on this issue.

STAFF ANALYSIS: Order No. PSC-97-0280-FOF-WS, issued March 12, 1997, noted that the reuse rate for the Mitchell property was zero, but required any extension of the Mitchell contract to be filed with the Commission for approval (TR 677). Although an extension agreement was entered into on March 19, 1999, the utility did not submit the agreement until March 10, 2000, after a request by staff. (TR 677) (EX 17).

Aloha argues in its brief that this was a mere oversight, and that the utility had no choice but to extend the Mitchell agreement in order to allow it to dispose of treated effluent or face being in violation of DEP and ERA requirements. OPC merely states that it agrees that a \$250 fine is appropriate.

The evidence shows that Aloha violated the requirements of Order No. PSC-97-0280-FOF-WS by not timely submitting the extension

of the Mitchell contract to the Commission for approval. 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, or any lawful rule or order of the Commission.

Utilities are charged with the knowledge of the Commission's rules, statutes, and orders. In Order No. 24306, issued April 1, 1991, in Docket No. 890216-TL, entitled In Re: Investigation Into The Proper Application of Rule 25-14.003, F.A.C., 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 "'willful' implies an intent to do an act, and this is distinct from an intent to violate a statute or rule." Id. at 6. Additionally, "[i]t is a common maxim, familiar to all minds that 'ignorance of the law' will not excuse any person, either civilly or criminally." Barlow v. United States, 32 U.S. 404, 411 (1833).

Therefore, in accordance with Section 367.161, Florida Statutes, the utility could be fined up to \$5,000 for its failure to submit the extension of the Mitchell contract to the Commission for approval. However, because of the exigencies of this case and the need of Aloha to enter into this extension, staff believes that Aloha should be fined \$250 for its failure to timely submit the Mitchell contract for approval as required by the Order. The Commission should approve the renewed contract after the fact, but no further extension of the contract after this current term expires should take place until the utility has Commission approval. Staff further recommends that Aloha should either obtain approval of the Commission for another extension of the Mitchell agreement, or charge the Mitchell property the approved system-wide reuse rate upon expiration of this latest extension.

ISSUE 42: Should Aloha be fined for its apparent violation of Order No. PSC-97-0280-FOF-WS for 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?

RECOMMENDATION: The utility should not be fined for its apparent failure to file the directed information in violation of the Order. (FLETCHER, JAEGER)

POSITIONS

ALOHA: No. As was stated in the reuse case, it is the utility's position that none of the costs should be allocated to its water customers.

OPC: No position.

STAFF ANALYSIS: 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. However, Order No. PSC-97-0280-FOF-WS specifically stated 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 Docket No. 960545-WS is still open, and 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 either be made to show cause or be fined for its failure to file the directed information in apparent violation of the Order.

ISSUE 43: Should this docket be closed?

RECOMMENDATION: No, this docket should remain open pending staff's verification that the utility's revised tariff sheets are consistent with the Commission's decision and that the utility has properly administered the refund. Upon staff's verification, this docket should be administratively closed. (FLETCHER, JAEGER)

POSITIONS

ALOHA: Yes, upon approval of final rates.

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

STAFF ANALYSIS: This docket should remain open pending staff's verification that the utility's revised tariff sheets are consistent with the Commission's decision and that the utility has properly administered the refund. Upon staff's verification, this docket should be administratively closed.

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**ALOHA UTILITIES, INC. - SEVEN SPRINGS SYSTEM
 SCHEDULE OF WASTEWATER RATE BASE
 FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01**

**SCHEDULE NO. 1-A
 DOCKET 991643-SU**

DESCRIPTION	TEST YEAR PER UTILITY	UTILITY ADJUST- MENTS	ADJUSTED TEST YEAR PER UTILITY	STAFF ADJUST- MENTS	STAFF ADJUSTED TEST YEAR
1 UTILITY PLANT IN SERVICE	\$22,229,056	\$0	\$22,229,056	(\$244,164)	\$21,984,892
2 LAND	\$548,944	\$0	\$548,944	(\$12,120)	\$536,824
3 NON-USED & USEFUL	\$0	\$0	\$0	\$0	\$0
4 ACCUMULATED DEPRECIATION	(\$4,742,735)	\$0	(\$4,742,735)	\$80,647	(\$4,662,088)
5 CIAC	(\$11,337,945)	\$0	(\$11,337,945)	(\$1,646,425)	(\$12,984,370)
6 AMORTIZATION OF CIAC	\$3,324,608	\$0	\$3,324,608	\$299,631	\$3,624,239
7 DEFERRED INCOME TAXES	\$0	\$0	\$0	\$506,367	\$506,367
8 WORKING CAPITAL ALLOWANCE	<u>\$0</u>	<u>\$497,220</u>	<u>\$497,220</u>	<u>\$49,012</u>	<u>\$546,232</u>
RATE BASE	<u>\$10,021,928</u>	<u>\$497,220</u>	<u>\$10,519,148</u>	<u>(\$967,052)</u>	<u>\$9,552,096</u>

**ALOHA UTILITIES, INC. - SEVEN SPRINGS SYSTEM
 ADJUSTMENTS TO RATE BASE
 FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01**

**DOC. 991643-SU
 SCH. NO. 1-B**

EXPLANATION	WASTEWATER
<u>PLANT IN SERVICE</u>	
1 Reduce plant for items capitalized prior to the test year. (Issue 4)	(\$127,232)
2 To reduce for using incorrect AFUDC rate. (Audit Excep. No. 2) (Stip. 2)	(\$122,524)
3 Reclassify items expensed that should be capitalized. (Audit Ex. No. 3) (Stip. 3)	\$11,616
4 To recognize 30-day zero cost of accounts payables on CWIP. (Stip. 11)	(\$20,124)
5 To reflect the utility's capitalization of materials and supplies. (Issue 28)	\$14,100
Total	<u>(\$244,164)</u>
<u>LAND</u>	
Correct error made in Order No. PSC-99-1917-PAA-WS. (Audit Dis. No. 1) (Stip 8)	<u>(\$12,120)</u>
<u>NON-USED AND USEFUL</u>	
None	<u>\$0</u>
<u>ACCUMULATED DEPRECIATION</u>	
1 Reduce plant for items capitalized prior to the test year. (Issue 4)	\$73,211
2 To reduce for using incorrect AFUDC rate. (Audit Excep. No. 2) (Stip. 2)	\$8,159
3 Reclassify items expensed that should be capitalized. (Audit Ex. No. 3) (Stip. 3)	(\$1,291)
4 To recognize 30-day zero cost of accounts payables on CWIP. (Stip. 11)	\$568
Total	<u>\$80,647</u>
<u>CIAC</u>	
1 Reflect appropriate treatment of CTs & DTAs. (Issue 10)	(\$1,544,865)
2 Reduce to reflect the appropriate growth rate. (Issue 18)	\$7,387
3 To reflect increase in plant capacity charges. (Issue 40)	(\$108,947)
Total	<u>(\$1,646,425)</u>
<u>ACCUM. AMORT. OF CIAC</u>	
1 Reflect appropriate treatment of CTs & DTAs. (Issue 10)	\$295,878
2 Reduce to reflect the appropriate growth rate. (Issue 18)	(\$273)
3 To reflect increase in plant capacity charges. (Issue 40)	\$4,026
Total	<u>\$299,631</u>
<u>DEFERRED INCOME TAXES</u>	
Reflect appropriate treatment of CTs & DTAs. (Issue 10)	<u>\$506,367</u>
<u>WORKING CAPITAL</u>	
To reflect the appropriate working capital. (Issues 11, 12, 13, & Stip. 9)	<u>\$49,012</u>

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**ALOHA UTILITIES, INC. - SEVEN SPRINGS WASTEWATER SYSTEM
 CAPITAL STRUCTURE
 FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01**

**SCHEDULE NO. 2-A
 DOCKET 991643-SU**

DESCRIPTION	TOTAL CAPITAL	SPECIFIC ADJUSTMENTS (EXPLAIN)	PRO RATA ADJUSTMENTS	CAPITAL RECONCILED TO RATE BASE	RATIO	COST RATE	WEIGHTED COST
PER UTILITY AVERAGE							
1 LONG TERM DEBT	\$8,614,742	\$0	(\$1,236,366)	\$7,378,376	70.14%	9.84%	6.90%
2 SHORT-TERM DEBT	\$0	\$0	\$0	\$0	0.00%	0.00%	0.00%
3 PREFERRED STOCK	\$600,000	\$0	(\$86,005)	\$513,995	4.89%	10.12%	0.49%
4 COMMON EQUITY	\$2,188,637	\$0	(\$314,069)	\$1,874,568	17.82%	10.12%	1.80%
5 CUSTOMER DEPOSITS	\$93,295	\$0	\$0	\$93,295	0.89%	6.00%	0.05%
6 DEFERRED INCOME TAXES	<u>\$770,040</u>	<u>\$0</u>	<u>(\$111,126)</u>	<u>\$658,914</u>	<u>6.26%</u>	0.00%	<u>0.00%</u>
7 TOTAL CAPITAL	<u>\$12,266,714</u>	<u>\$0</u>	<u>(\$1,747,566)</u>	<u>\$10,519,148</u>	<u>100.00%</u>		<u>9.25%</u>
PER STAFF AVERAGE							
8 LONG TERM DEBT	\$8,614,742	\$0	(\$1,347,892)	\$7,266,850	76.08%	10.12%	7.70%
9 SHORT-TERM DEBT	\$0	\$0	\$0	\$0	0.00%	0.00%	0.00%
10 PREFERRED STOCK	\$600,000	\$0	(\$93,878)	\$506,122	5.30%	9.93%	0.53%
11 COMMON EQUITY	\$2,188,637	(\$517,923)	(\$261,406)	\$1,409,308	14.75%	9.93%	1.47%
12 CUSTOMER DEPOSITS	\$93,295	\$345,117	(\$68,595)	\$369,817	3.87%	6.00%	0.23%
13 DEFERRED INCOME TAXES	<u>\$770,040</u>	<u>(\$770,040)</u>	<u>\$0</u>	<u>\$0</u>	<u>0.00%</u>	0.00%	<u>0.00%</u>
14 TOTAL CAPITAL	<u>\$12,266,714</u>	<u>(\$942,846)</u>	<u>(\$1,771,772)</u>	<u>\$9,552,096</u>	<u>100.00%</u>		<u>9.92%</u>
						LOW	HIGH
						<u>7.93%</u>	<u>10.93%</u>
						<u>9.62%</u>	<u>10.07%</u>

**ALOHA UTILITIES, INC. - SEVEN SPRINGS WASTEWATER SYSTEM
ADJUSTMENTS TO CAPITAL STRUCTURE
FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01**

**DOC. 991643-SU
SCH. NO. 2-B**

EXPLANATION	
<u>COMMON EQUITY</u>	
Reflect appropriate balance of retained earnings and customer deposits. (Stip. 13)	<u>(\$517,923)</u>
<u>CUSTOMER DEPOSITS</u>	
Reflect appropriate balance of retained earnings and customer deposits. (Stip. 13)	<u>\$345,117</u>
<u>DEFERRED INCOME TAXES</u>	
Reflect appropriate treatment of CTs & DTAs. (Issue 10)	<u>(\$770,000)</u>

DOCKET NO. 991643-SU
 DATE: JANUARY 4, 2001

**ALOHA UTILITIES, INC. - SEVEN SPRINGS SYSTEM
 STATEMENT OF WASTEWATER OPERATIONS
 FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01**

**SCHEDULE NO. 3-A
 DOCKET 991643-SU**

DESCRIPTION	TEST YEAR PER UTILITY	UTILITY ADJUST- MENTS	ADJUSTED TEST YEAR PER UTILITY	STAFF ADJUST- MENTS	STAFF ADJUSTED TEST YEAR	REVENUE INCREASE	REVENUE REQUIREMENT
1 OPERATING REVENUES	<u>\$2,780,994</u>	<u>\$1,593,501</u>	<u>\$4,374,495</u>	<u>(\$1,648,580)</u>	<u>\$2,725,915</u>	<u>\$1,369,589</u> 50.24%	<u>\$4,095,504</u>
2 OPERATING EXPENSES OPERATION &	\$2,175,762	\$75,000	\$2,250,762	(\$111,708)	\$2,139,054	\$0	\$2,139,054
3 DEPRECIATION	\$383,390	\$0	\$383,390	(\$12,501)	\$370,889	\$0	\$370,889
4 AMORTIZATION	(\$38,622)	\$0	(\$38,622)	(\$8,651)	(\$47,273)	\$0	(\$47,273)
5 TAXES OTHER THAN	\$527,189	\$71,707	\$598,896	(\$89,896)	\$509,000	\$61,632	\$570,632
6 INCOME TAXES	<u>\$208,100</u>	<u>\$0</u>	<u>\$208,100</u>	<u>(\$585,529)</u>	<u>(\$377,429)</u>	<u>\$492,184</u>	<u>\$114,756</u>
7 TOTAL OPERATING	<u>\$3,255,819</u>	<u>\$146,707</u>	<u>\$3,402,526</u>	<u>(\$808,284)</u>	<u>\$2,594,242</u>	<u>\$553,816</u>	<u>\$3,148,058</u>
8 OPERATING INCOME	<u>(\$474,825)</u>	<u>\$1,446,794</u>	<u>\$971,969</u>	<u>(\$840,296)</u>	<u>\$131,673</u>	<u>\$815,773</u>	<u>\$947,447</u>
9 RATE BASE	<u>\$10,021,928</u>		<u>\$10,519,148</u>		<u>\$9,552,096</u>		<u>\$9,552,096</u>
10 RATE OF RETURN	<u>-4.74%</u>		<u>9.24%</u>		<u>1.38%</u>		<u>9.92%</u>

**ALOHA UTILITIES, INC. - SEVEN SPRINGS SYSTEM
 ADJUSTMENTS TO OPERATING INCOME
 FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01**

**SCH. NO. 3-B
 DOC. 991643-SU**

EXPLANATION	WASTEWATER
<u>OPERATING REVENUES</u>	
1 Remove utility requested revenue increase.	(\$1,593,501)
2 To reduce projected revenues at current rates based on staff's recommended factor for bills and consumption. (Issue 19)	(\$36,194)
3 To reflect the appropriate reuse revenue. (Issue 20)	(18,885)
Total	<u>(\$1,648,580)</u>
<u>OPERATION & MAINTENANCE EXPENSE</u>	
1 Reduce expense accounts to reflect the appropriate growth rate. (Issue 19)	(\$32,883)
2 Reduce vice-president's salary. (Issue 21)	(15,507)
3 Reduce pensions & benefits associated w/ disallowed VP's salary. (Issue 21)	(5,319)
4 To reclassify items expensed that should be capitalized. (Audit Ex. # 3) (Stip. 3)	(13,072)
5 Reduce O&M that should be allocated to other systems. (A. Dis. # 6) (Stip. 6)	(2,446)
6 Reclassify legal expense as prepaid bank loan costs. (Audit Dis. No. 9) (Stip. 7)	(2,581)
7 To remove excess rate case expense of Doc. # 950615-SU. (Audit Ex. # 4) (Stip. 10)	(31,401)
8 Reduce Contractual Services - Acctg acct. for non-recurring costs. (Issue 24)	(1,113)
9 Reduce O&M expenses associated w/ DEP Enforcement Action. (Issue 26)	(34,726)
10 Reduce Miscell. exp. for non-recurring exp. & misclassification error. (Issue 30)	(7,755)
11 To reflect the appropriate amount of current rate expense. (Issue 31)	35,095
Total	<u>(\$111,708)</u>
<u>DEPRECIATION EXPENSE-NET</u>	
1 Reduce depreciation expense for disallowed plant. (Issue 4)	(\$6,675)
2 To reduce for using incorrect AFUDC rate. (Audit Ex. No. 2) (Stip. 2)	(5,903)
3 Reclassify items expensed that should be capitalized. (Audit Ex. No. 3) (Stip. 3)	645
4 To recognize 30-day zero cost of accounts payables on CWIP. (Stip 11)	(568)
Total	<u>(\$12,501)</u>
<u>AMORTIZATION EXPENSE</u>	
To reflect the appropriate amortization rate of contributed taxes. (Issue 32)	<u>(\$8,651)</u>
<u>TAXES OTHER THAN INCOME</u>	
1 RAFs on corrected test year revenues.	(\$74,186)
2 Reduce payroll taxes. (Issue 21)	(1,392)
3 Reflect appropriate millage rate for tangible estate property taxes. (Stip. 14)	(14,318)
Total	<u>(\$89,896)</u>
<u>INCOME TAXES</u>	
To adjust to test year income tax expense.	<u>(\$585,529)</u>

**ALOHA UTILITIES, INC. - SEVEN SPRINGS SYSTEM
 WASTEWATER MONTHLY SERVICE RATES
 FINAL 13-MONTH AVERAGE TEST YEAR ENDED 09/30/01**

**SCH. NO. 4
 DOCKET 991643-SU**

		Rates As of 01/18/200	Utility Requested Final	Staff Recomm. Final
<u>Residential</u>				
Base Facility Charge: Meter Size 5/8"X3/4"	5	\$8.99	\$14.54	\$14.06
Gallorage Charge - Per 1,000 gallons (10,000 gallon cap)		\$2.32	\$3.65	\$3.43
<u>General Service</u>				
Base Facility Charge: Meter Size 5/8"X3/4"	5	\$8.99	\$14.54	\$14.06
1"	1	\$22.48	\$36.35	\$35.14
1 1/2"	1	\$44.96	\$72.70	\$70.28
2"	2	\$71.94	\$116.32	\$112.45
3"	3	\$143.88	\$218.10	\$224.90
4"	4	\$224.75	\$363.50	\$351.41
6"	6	\$449.62	\$727.00	\$702.83
8"	8	\$719.39	\$1,163.20	\$1,124.52
Gallorage Charge, per 1,000 Gallons		\$2.78	4.26	\$4.12
<u>Reclaimed Water</u>				
Mitchell Property		\$0.00	\$0.00	\$0.00
Follow Hollow Golf Course		\$0.25	\$0.25	\$0.00
All Others		\$0.25	\$0.25	\$0.29
5/8" Meter Size 3,000 Gallons		\$15.95	\$25.49	\$24.35
5,000 Gallons		\$20.59	\$32.79	\$31.22
10,000 Gallons (Wastewater Gallorage Cap - 10,000 Gallons)		\$32.19	\$51.04	\$48.37