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June 14, 2001

Ms. Blanca S. Bayo, Director  
Division of Records and Reporting  
Florida Public Service Commission  
2540 Shumard Oak Boulevard  
Betty Easley Conference Center, Room 110  
Tallahassee, Florida 32399-0850

**HAND DELIVERY**

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01 JUN 22 PM 3:22  
RECORDS AND REPORTING

Re: Docket No. 010006-WS

Dear Ms. Bayo:

Enclosed herewith for filing in the above-referenced docket on behalf of Florida Waterworks Association ("FWA") are the original and fifteen copies of Florida Waterwork's Petition Protesting Proposed Agency Action Order No. PSC-01-1226-PAA-WS and Request for Formal Administrative Hearing.

Please acknowledge receipt of these documents by stamping the extra copy of this letter "filed" and returning the copy to me.

Thank you for your assistance with this filing.

Sincerely,

*J. Stephen Menton*  
J. Stephen Menton

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07782 JUN 22 01

FPSC-RECORDS/REPORTING

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

ORIGINAL

In re: Petition of Florida Waterworks Association for a Formal Administrative Proceeding on the proposed continuation of the leverage formula methodology for calculating a reasonable range of returns on common equity for water and wastewater utilities.

Docket No. 010006-WS
Filed: June 22, 2001

PETITION PROTESTING PROPOSED AGENCY ACTION ORDER NO. PSC-01-1226-PAA-WS AND REQUEST FOR FORMAL ADMINISTRATIVE PROCEEDING

Petitioner, Florida Waterworks Association, by and through its undersigned counsel and pursuant to Rule 28-106.201, Florida Administrative Code, hereby files this Petition Protesting Proposed Agency Action Order No. PSC-01-1226-PAA-WS (the "PAA Order") issued June 1, 2001. The PAA Order proposes a continuation with only a minor correction and a minor modification of the existing leverage formula methodology used for calculating a reasonable range of returns on equity for water and wastewater utilities. For the reasons set forth herein, the Florida Waterworks Association seeks a formal administrative hearing to address the assumptions and conclusions of the PAA Order. In support of its Petition, FWA states as follows:

- 1. The Petitioner is the Florida Waterworks Association ("FWA"). For purposes of this proceeding, the address and telephone number for FWA shall be that of its representatives:

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07782 JUN 22 01
FPSC-RECORDS/REPORTING

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2. The FWA is a non-profit association comprised of investor-owned water and/or wastewater utility companies providing service in the state of Florida. The FWA is the Florida Chapter of the National Association of Water Companies, Inc. The FWA exists to assist its members with legal, regulatory, technical and operational matters and participates in administrative and legal proceedings of common interest to its membership. A substantial number of the members of the FWA are water and wastewater utilities regulated by the Florida Public Service Commission and such utilities are therefore subject to the Commission's rules, regulations and policies, which would include the leverage formula methodology set forth in the PAA Order if it becomes final. The FWA received notice of the PAA Order upon its issuance on June 1, 2001.

3. The affected agency is the Florida Public Service Commission (the "Commission"), at the address of 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850. The Commission's docket number for this matter is set forth above.

4. Pursuant to Section 367.01(4)(f), Florida Statutes, the Commission is authorized to establish, not less than once each year, a leverage formula to calculate a reasonable range of returns on equity for water and wastewater utilities. Pursuant to the PAA Order, the Commission proposes to continue its current leverage formula methodology for water and wastewater utilities with only a minor correction and minor modification. The current leverage formula methodology has essentially been followed by the Commission for several years without any significant modifications

to reflect changes in the industry. The current leverage formula was renewed last year by the Commission in Proposed Agency Action Order No. PSC-00-1162-PAA-WS, which was made final by Consummating Order No. PSC-00-1299-CO-WS, issued on July 18, 2000 in Docket No. 000006.

5. The current regulatory treatment embodied in the existing leverage formula does not appropriately reflect the risks and issues facing the industry. The water and wastewater industry is a rising cost industry. As a result of uncertain and continually changing environmental regulations and conditions, water and wastewater utilities must assume greater business risks than in the past. The Commission's proposed continuation of the current formula fails to adequately recognize these risks and thereby jeopardizes the financial viability of the utilities and potentially compromises their ability to provide adequate, safe and reliable service.

6. The Commission's current leverage formula calculates a range of returns on equity ("ROE") based on certain financial models. Strict adherence to the Commission's models has resulted in rates of return that are significantly lower than the ROEs authorized for water and wastewater utilities in other states. Consequently, investment in Florida water and wastewater utilities is comparatively becoming less and less attractive.

7. The current leverage formula methodology for water and wastewater utilities produces ROEs that are significantly less than the composite authorized rate of return for Commission regulated electric and gas utilities. The primary recommendation set forth in the May 3, 2001 Staff Recommendation in this docket sought to reconcile this discrepancy and would have resulted in a significantly higher range of returns for water and wastewater utilities consistent with what the Commission has approved for electric and gas utilities in Florida. There is no basis for lower ROE's for water and wastewater utilities in comparison to other Commission regulated

utilities. If anything, a higher ROE is warranted for the water and wastewater industry due to the greater risks that are faced. The Commission's authorization of returns on equity in excess of the model projections for other regulated industries in Florida exacerbates the disincentives to investment in Florida water and wastewater utilities.

8. The proposed decision to continue the existing formula perpetuates the use of a sample of utilities that is not reflective of Commission regulated water and wastewater utilities. The sample is too small in size and utilizes a disproportionate number of utilities located out-of-state who operate in markets and circumstances which do not reflect the water and wastewater industry in Florida. Furthermore, the current leverage formula utilizes an index of out-of-state water utilities that have publicly traded stock. Some of the companies used in the sample have been the subject of merger talks and/or other market-influencing factors that distort or negate their usefulness for purposes of the formula. For these and other reasons, the sample does not accurately reflect the typical Florida water and wastewater company.

9. Disputed issues of material fact in this proceeding include the following:

(a) What is the appropriate manner to estimate a fair and reasonable return on a water and wastewater utility's common equity capital;

(b) Whether the current leverage formula methodology is appropriate in view of the business risks and market conditions facing the water and wastewater industry in Florida;

(c) Whether Florida water and wastewater utilities will be able to attract the capital funds needed to meet their service demands and to maintain financial integrity with the range of returns calculated using the current methodology with the proposed minor modifications;

(d) Whether adoption of the PAA Order will offer returns to capital suppliers that are comparable to those achieved on alternate competing investments of similar risk;

(e) Whether the existing leverage formula methodology is based upon an appropriate sample of utilities;

(f) Whether water and water utilities in Florida face more or less business risk than other rate- based regulated industries; and

(g) Whether there is any justification or basis for utilizing a leverage formula methodology that yields a lower return on equity for water and wastewater utilities as opposed to other rate-based regulated industries.

10. The Commission should modify the leverage formula methodology consistent with Staff's primary recommendation set forth in the May 3, 2001 Staff Recommendation in this docket. The leverage formula methodology should incorporate the use of an electric and gas composite authorized return on equity which would yield a higher return than under the current leverage formula.

11. The ultimate facts entitling FWA to relief include, but are not limited to, the following: The Commission's proposed continuation of the current leverage formula methodology mistakenly assumes that water and wastewater utilities are less risky than other rate- based regulated industries; changes in the water and wastewater industry and the stock market warrant modification of the current leverage formula to more accurately reflect the actual business risks and to create incentives for consolidations within the industry.

WHEREFORE, Petitioner Florida Waterworks Association requests the Commission:

(a) to grant FWA's Petition for a Formal Administrative Hearing;

- (b) to enter a Final Order modifying the current leverage formula methodology consistent with Staff's primary recommendation; and
- (c) to grant such further relief as may be deemed just and proper.

Respectfully submitted,



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