

State of Florida



Public Service Commission  
-M-E-M-O-R-A-N-D-U-M-

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**DATE:** November 27, 2001  
**TO:** Jane Faurot, Chief of Reporting  
**FROM:** Ralph R. Jaeger, Senior Attorney, Legal Division  
**RE:** Docket No. 010006-WS - Water and wastewater industry annual reestablishment of authorized range of return on common equity of water and wastewater utilities pursuant to Section 367.081(4)(f), F.S.

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Attached is Late Filed Exhibit 2 to Roger A. Morin's deposition taken on October 23, 2001. Dr. Morin's deposition on October 23, 2001, with all exhibits, along with his November 1, 2001 deposition, were identified as Composite Exhibit 1 at the hearing on November 5, 2001, and admitted into evidence. Therefore, this Late-Filed Exhibit 2 should be attached to the October 23, 2001 deposition and be made a part of the record of this case, i.e. as a part of Exhibit No. 1.

RRJ/lw

cc: Division of the Commission Clerk and Administrative Services  
Division of Economic Regulation (Draper, Maurey)

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FPSC-COMMISSION CLERK

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November 16, 2001

Ralph Jaeger, Esquire  
Florida Public Service Commission  
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TELECOPIER

RE: In re: Petition of Florida Waterworks Association, et al.  
Docket No.: 010006-WS  
Late Filed Exhibit to Dr. Morin's Deposition

Dear Ralph:

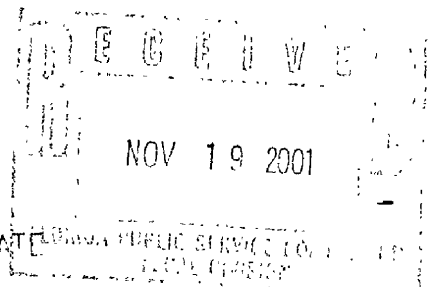
Enclosed please find the updated recommendation of Dr. Morin which was requested during his deposition. This document was identified during Dr. Morin's deposition as a late filed exhibit 2. I will hand deliver to you the original on Monday, but wanted to provide you and Steve Burgess a copy for use in preparation of the post-hearing briefs.

Sincerely,

  
J. Stephen Menton

JSM/knb  
Enclosure  
cc: Steve Burgess (with enclosure)

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FPSC-COMMISSION CLERK

**BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**

In re: Water and wastewater )  
industry annual reestablishment )  
of authorized range of return on )  
on common equity for water and )  
wastewater utilities pursuant to )  
Section 367.081(4)(f), F.S. )  
\_\_\_\_\_ )

Docket No. 010006-WS

**UPDATED RECOMMENDATION**

**OF**

**DR. ROGER A. MORIN**

**ON BEHALF OF**

**FLORIDA WATERWORKS ASSOCIATION**

DOCUMENT NUMBER-DATE

14942 NOV 27 06

FPSC-COMMISSION CLERK

## UPDATED RECOMMENDATION

Appreciable changes have occurred in long-term interest rates and stock prices since I prepared my original testimony earlier this year. As of early November 2001, long-term Treasury bonds are yielding about 5.0%, compared to 5.8% last June when I prepared my direct testimony, that is, a decrease of 80 basis points. Hence, the risk premium and CAPM results will change accordingly, although not proportionately. The DCF results have changed modestly in view of the change in dividend yields and analysts' growth forecasts, some of which are offsetting.

As was the case in my direct testimony, I performed the same six risk premium analyses. For the first two risk premium studies, I applied the CAPM and an empirical approximation of the CAPM using more recent market data, namely, a risk-free rate of 5.0%, a beta of 0.65, and a market risk premium of 7.5%. I updated my historical and allowed risk premium analyses. I also updated my DCF analyses on the same three surrogates for Florida water and wastewater utilities using more recent stock price and growth forecasts. The results are summarized in the following updated version of the summary table contained in my direct testimony:

<b>STUDY</b>	<b>ROE</b>
CAPM	10.2%
ECAPM	10.8%
Historical Risk Premium Electric	11.0%
Historical Risk Premium Natural Gas	11.5%
Allowed Risk Premium Electric Utilities	10.7%
Allowed Risk Premium Natural Gas Utilities	10.6%
Water Utilities IBES Growth	10.2%
Water Utilities Value Line Growth	11.6%
Water Utilities Historical Growth	11.4%
Transmission – Distribution Electrics IBES Growth	10.8%
Transmission – Distribution Electrics Value Line Growth	12.3%

Natural Gas Distribution IBES Growth	12.7%
Natural Gas Distribution Value Line Growth	14.5%

The DCF analysis performed on the natural gas distributors using Value Line's growth forecast might be considered an outlier, and I have accorded it little weight. The remaining results range from 10.2% to 12.7%, with a midpoint of 11.5% for a typical Florida water and wastewater utility with an average capital structure. Based on the results of all my analyses, the application of my professional judgment, and the risk circumstances of the industry, it is my opinion that a just and reasonable range of returns on common equity is 10.2% to 12.7% with a midpoint of 11.5% for a typical FWU with an average capital structure.

The 11.5% midpoint of my recommended range should be adjusted to reflect a particular FWU's capital structure in accordance to the directives provided in my direct testimony. For typical capital structures that range from a 60% common equity ratio to a 30% common equity ratio, the cost of common equity varies from about 10% to 13%.