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COMMISSION
CLERK

July 15, 2011

Via Hand Delivery

Honorable Art Graham
Chairman
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, Florida 32399-0850

110226-WS

Re: Aqua Utilities Florida, Inc. - Request for Test Year Approval Pursuant to Rule 25-30.430, Florida Administrative Code, for Chuluota Water and Wastewater Systems in Seminole County.

Dear Chairman Graham:

Aqua Utilities Florida, Inc. ("AUF" or "Company"), is committed to providing safe and reliable water and wastewater services to the customers of its Chuluota water and wastewater systems in Seminole County ("Chuluota Systems"). To do so, the Company has spent and continues to spend significant resources and money to strengthen, operate, and maintain those systems.

Based on the Company's financial records, adjustments must be made to its current rates in order for the Company to continue to adequately serve its Chuluota customers and to maintain its financial integrity. Accordingly, the Company intends to submit an application for general rate relief to the Commission for its Chuluota Systems, including minimum filing requirements ("MFRs"), on or before September 30, 2011.¹ For purposes of this request for rate relief, AUF is proposing to use an historic test year ending March 31, 2011.

¹ The Commission has specified that the Chuluota Systems "shall be considered as stand-alone systems for rate design purposes." See Order No. PSC-09-0385-FOF-WS.

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The Company's decision to seek rate relief was made only after careful and thorough consideration. The last base rate increase for the Chuluota Systems was in 1996 -- fifteen years ago. Since acquiring the systems in 2004, AUF has made substantial capital investments in plant and equipment to improve the quality of water and wastewater service in the Chuluota service area. Although AUF has made serious effort to avoid a rate increase for as long as possible, the costs of providing service to Chuluota customers have increased at a rate that dramatically outpaces the Company's revenues. Consequently, the Company must seek rate relief to fulfill its public service requirements and meet the needs of its customers.

In accordance with Florida Administrative Code Rule 25-30.430, AUF submits the following information:

Improvements to the Chuluota Water System

AUF has made significant improvements to the Chuluota water system. Specifically, the Company has made more than \$4.4 million in capital improvements, \$2.3 million of which relate to an ion exchange system to address issues related to disinfection byproducts (i.e., TTHMs). As a result of those improvements, the Chuluota water system has been in compliance with TTHM standards for all of 2010, and continues to be in compliance. Moreover, there are no open consent orders relating to the Chuluota water system.

Improvements to the Chuluota Wastewater System

AUF also has made significant improvements to its Chuluota wastewater system. Specifically, AUF has made more than \$1 million in capital investments in the wastewater system, which include substantial investments in an innovative reuse project to address effluent disposal requirements.² AUF undertook the reuse project because of constraints placed on effluent disposal by the Florida Department of Environmental Protection ("FDEP"). Previously, the wastewater treatment plant's permitted capacity was limited to the effluent disposal capacity of the spray fields. AUF initially entered into discussions with the former Alafaya Utilities, Inc. ("Alafaya"), to determine whether it could deliver reuse water to this neighboring utility. After thorough review and analysis, AUF determined that delivery of reuse water to Alafaya was the environmentally preferred and the least cost alternative to address the Company's effluent disposal needs. Thus, instead of buying and building a new disposal site, AUF entered into a contract to build a reuse line and provide treated reuse water to Alafaya.³ AUF has completed construction of the reuse line and will place this reuse line into service by the end of June 2011.

²The Florida Legislature has expressly recognized that reuse water projects benefit water, wastewater and reuse customers and thus should be encouraged. See §§373.250 and 367.0817, Florida Statutes.

³Alafaya was subsequently purchased by the City of Oviedo.

Pro Forma Projects

AUF continues to make improvements to its Chuluota Systems, and intends to include the cost of those ongoing projects in the rate base as pro forma plant additions. With respect to the Chuluota wastewater system, AUF will include as pro forma plant approximately \$279,750 in additional costs related to the above-described reuse project. With respect to the Chuluota water system, AUF will include as pro forma plant approximately \$73,000 in additional costs related to optimizing the ion exchange system. AUF will also include as pro forma plant \$60,000 in additional costs related to a Seminole County storm system relocation project, which involves replacing existing water lines with new water lines.

The Need for Rate Relief

As explained above, there has not been a general base rate increase for the Chuluota Systems since 1996 even though AUF has made significant capital investments to improve those systems. Without a rate increase, the Company's 2011 return on equity ("ROE") is anticipated to be negative 3.03 percent for its Chuluota water system and negative 2.18 percent for its wastewater system. The Company's combined 2011 ROE is expected to be approximately 1,151 basis points below the Commission's established 8.75% ROE midpoint for the Chuluota Systems. At this earnings level, the Company cannot realistically maintain a stable financial position and simultaneously meet the needs of its customers and provide safe and reliable water and wastewater services. Furthermore, without rate relief, the Company's rate of return will continue to lag significantly below the returns that the Commission has awarded to other water and wastewater utilities. These factors have left the Company with no alternative but to seek rate relief for its Chuluota Systems.

AUF respectfully submits that there may be efficiencies in processing this case using the Commission's proposed agency action ("PAA") procedures set forth in Section 367.081(8), Florida Statutes. However, at this juncture it is difficult to predict whether a PAA order is likely to be protested. Accordingly, AUF will defer to the Commission as to whether the PAA or formal hearing process should be utilized.⁴

Water Year-End Rate Base

Due to the significant capital improvements to the Chuluota water system during the test year, AUF is requesting to use a year-end (rather than an average) rate base for its water system. The Company has made more than \$4.4 million in capital improvements to its Chuluota water system. \$2.3 million of those improvements related to an ion exchange system to address the TTHM issue. These system improvements increase water plant in service during the test year by

⁴ Order No. PSC-96-1147-FOF-WS makes it clear that "the discretion to opt between the PAA or hearing procedures resides with the Commission."

approximately 30 percent. The courts and the Commission have consistently found that, in cases such as this, a significant increase in plant in service during a test year constitutes an extraordinary circumstance which justifies the use of a year-end rate base.⁵ Furthermore, a year-end rate base would allow AUF an opportunity to earn a fair return on investments made during the test year to comply with FDEP environmental requirements,⁶ and ensure that there will be compensatory rates on a prospective basis. Moreover, pursuant to Section 367.081(2)(a)1., Florida Statutes, the Commission is required to consider the investment in plant made by the utility in the public service. For the foregoing reasons, AUF respectfully requests that the Commission approve the use of a year-end rate base in AUF's MFRs for its water system.

The Test Year

Finally, pursuant to Rule 25-30.430, Florida Administrative Code, AUF requests approval of an historic test year ending March 31, 2011. That historic test year is representative of a normal, full year of operation for the Chuluota Systems, and will best fulfill the purpose of a test year, which is to set rates based on costs and revenues that are representative of the period when new rates will be in effect. AUF has not experienced any significant changes in its operations since March 31, 2011, and does not anticipate any such changes prospectively. The Company will also request interim rates based on the same historic test year.

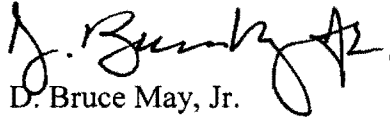
As I hope is evident from this letter, AUF's decision to seek rate relief was made only after long and serious deliberation. An increase in base rate revenues is necessary to maintain safe and reliable water and wastewater systems for the Chuluota customers, and to preserve the Company's financial integrity. Meanwhile, AUF continues to strive to provide excellent service to its customers.

⁵ See *Citizens of Florida v. Hawkins*, 356 So. 2d 254, 257 (Fla. 1978); see also Order No. PSC-06-0378-PAA-WU (May 8, 2006) (improvements representing 33% of the total plant warrant year-end rate base); Order No. PSC-98-0763-FOF-SU (June 3, 1998) (improvements representing 36.07% of total plant warrant year-end rate base).
⁶ Florida law provides that "the [C]ommission shall approve rates for service which allow a utility to recover from customers the full amount of environmental compliance cost." § 367.081(2)(a)2., Fla. Stat., (emphasis added).

Should you or members of the Staff have any questions regarding this request, please do not hesitate to contact me.

Sincerely,

HOLLAND & KNIGHT LLP


D. Bruce May, Jr.

DBM:kjg

cc: Hon. Lisa Polak Edgar, Commissioner
Hon. Ronald A. Brisé, Commissioner
Hon. Eduardo E. Balbis, Commissioner
Hon. Julie Imanuel Brown, Commissioner
S. Curtis Kiser, General Counsel (Via Hand Delivery)
Charles Hill, Deputy Executive Director (Via Hand Delivery)
Marshall Willis, Director, Division of Economic Regulation (Via Hand Delivery)
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