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Public Service Commission

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

DATE: July 28, 2011

TO: Office of Commission Clerk (Cole)

FROM: Division of Economic Regulation (Buys, Cicchetti, Daniel, Fletcher, Lingo, Maurey, Stallcup, Thompson, Williams)
Office of the General Counsel (Young)

RE: Docket No. 100426-WS – Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc.

AGENDA: 08/09/11 – Regular Agenda – Proposed Agency Action – Except for Issue Nos. 29 & 30 - Interested Persons May Participate

COMMISSIONERS ASSIGNED: ~~All Commissioners~~ ~~Graham, Balbis, Brown~~ All Commissioners - hws 8/02/11

PREHEARING OFFICER: Balbis

CRITICAL DATES: 5-Month Effective Date Waived Through 08/09/11

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\100426.RCM.DOC

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Case Background

Utilities, Inc. (UI or Parent) is an Illinois corporation which owns approximately 75 subsidiaries throughout 15 states including 15 water and wastewater utilities within the State of Florida. This is one of two UI rate case dockets pending before the Commission (Eagle Ridge, Docket No. 110153-SU). Lake Utility Services, Inc. (LUSI or Utility) is a Class A utility providing water and wastewater service to approximately 8,746 water and 2,827 wastewater customers in Lake County. LUSI is a wholly-owned subsidiary of UI. Water and wastewater rates were last established for this Utility in 2009.[1]

On December 27, 2010, LUSI filed its application for approval of final and interim rate increases in the instant docket. The Utility had a few deficiencies in the Minimum Filing Requirements (MFRs). The deficiencies were corrected and February 18, 2011, was established as the official filing date. The Utility requested that the application be processed using the Proposed Agency Action (PAA) procedure. The test year established for interim and final rates is the historical 13-month average period ended June 30, 2010.

LUSI's last rate case proceeding and review of rate base was in Docket No. 070693-WS, utilizing a projected test year ended June 30, 2009, which culminated in Order No. PSC-09-0101-PAA-WS. The Utility's revenue requirement established in that rate case was based on projected customer growth which failed to materialize. As a result, water consumption has decreased by approximately 35 percent over the past 3 years which translates into lower than anticipated water revenues. The Utility is also requesting recovery of capital costs related to improvements to the Lake Groves wastewater treatment plant and the Oranges-to-Vistas raw water line. LUSI further explained that its costs have increased significantly since the last rate case and is requesting recovery of those costs, including the cost of obtaining a consumptive use permit from the St. John's River Water Management District (SJRWMD). As such, the Utility filed the instant rate case which it believes would allow it to recover all the expenses LUSI will incur on a going-forward basis, and generate a fair rate of return on its investment on all property considered used and useful in the public service.

By Order No. PSC-11-0149-PCO-WS, issued March 4, 2011, the Commission approved interim rates designed to generate annual water revenues of $5,502,978, an increase of $1,332,875 or approximately 32 percent. The Utility did not request an interim rate increase for the wastewater system.

The Utility requested final rates designed to generate annual water revenues of $5,840,432, an increase of $1,606,673 or approximately 38 percent, and annual wastewater revenues of $2,344,226, an increase of $247,262 or approximately 12 percent.

On March 2, 2011, the Office of Public Counsel filed a Notice of Intervention in this docket, and an order acknowledging intervention was issued on March 8, 2011.[2]

[1] See Order No. PSC-09-0101-PAA-WS, issued February 16, 2009, in Docket No. 070693-WS, In re: Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc.
[2] See Order PSC-11-0161-PCO-WS.

On June 6, 2011, the Utility filed a letter waiving the Commission's requirement pursuant to Section 367.081(8), Florida Statutes (F.S.), through August 9, 2011, to process the rate case within five months of the official filing date. This recommendation addresses the Utility's final requested rates. The Commission has jurisdiction pursuant to Sections 367.081 and 367.082, F.S.

Discussion of Issues

QUALITY OF SERVICE

Issue 1: Is the quality of service provided by Lake Utility Services, Inc. satisfactory?

Recommendation: Yes. The overall quality of service provided by the Utility is satisfactory. (Williams)

Staff Analysis: Pursuant to Rule 25-30.433(1), Florida Administrative Code (F.A.C.), in a rate case proceeding, the Commission determines the overall quality of service provided by a utility by evaluating the quality of the utility's product, the operating condition of the utility's plant and facilities, and the utility's attempt to address customer satisfaction. The utility's compliance history with the Department of Environmental Protection (DEP) and the SJRWMD, as well as comments or complaints received from the customers, are also reviewed.

Quality of the Product and Operational Conditions of the Plants and Facilities

LUSI provides water service to approximately 8,800 customers and wastewater service to approximately 2,900 customers in Lake County. The Utility's water service territory is made up of three separate areas. The largest part of the service territory is in Clermont and consists of the interconnected LUSI North and Lake Groves service areas. The LUSI North system provides water service to mostly residential customers, and consists of several small, interconnected systems. In addition, LUSI North is connected to the Lake Groves area via a water main along U.S. Highway 27. Four Lakes and Lake Saunders are two separate water-only systems that are also part of LUSI's service territory. They both serve small residential areas and have their own water treatment facilities. The only system that provides wastewater service is the Lake Groves system.

Environmental regulation of LUSI's water and wastewater plants is by the DEP. The Utility is current in all of the required chemical analyses and is meeting all applicable rules and regulations related to water quality, wastewater treatment, and facility operations. There are no outstanding environmental compliance issues with DEP. The most recent inspection reports from DEP indicate that most of the water facilities are in compliance. However, LUSI was cited for deficiencies, including failing to operate water plants within the maximum operating capacity and for corrosion on well casings. The Utility subsequently responded to and corrected these deficiencies. In addition, staff conducted a field investigation of the plant facilities on April 26 and 27, 2011. All water and wastewater facilities were in good operating condition.

LUSI is located in an area known as the Central Florida Coordination Area, which, because of the potential for population growth and issues related to water supply, is monitored closely by the SJRWMD. LUSI is under an active Consent Order from the SJRWMD for several actions, including exceeding ground water withdrawal limitations and failing to comply with various other conditions of its consumptive use permits. The Consent Order was issued in December 2010 and requires the Utility to take corrective actions that include staffing a full-time water conservation coordinator. This coordinator was hired by LUSI in February 2009 in response to the ongoing negotiations with the WMD.

In summary, the Utility's water and wastewater facilities are in compliance with applicable DEP rules and regulations. The plant facilities are being maintained appropriately and the water produced meets all testing requirements. While there is an ongoing compliance issue with the SJRWMD, LUSI is complying with the provisions of the Consent Order and is attempting to resolve the issues. Therefore, staff recommends that the quality of the product and the operational conditions of the water and wastewater facilities be considered satisfactory.

The Utility's Attempt to Address Customer Satisfaction

To assess the Utility's attempt to address customer satisfaction, staff reviewed the complaints filed with LUSI, complaints filed with the Commission, correspondence received from the customers in response to the rate case, and customer comments received during the customer meeting.

A customer meeting was held on April 27, 2011, in the LUSI service territory. Approximately 60 customers attended the meeting and 20 spoke. All of the customers spoke in opposition to the rate increase. Many customers expressed opposition to the rate increase because of the short time since the last increase,[3] the magnitude of the proposed increase, and the financial hardship that increased rates would cause. Several customers complained that reuse water for irrigation was not available and expressed a desire to install private wells for irrigation use. Many customers also expressed displeasure with wastewater charges for water that was not returned to the wastewater system because of irrigation use.

In response to a data request, the Utility addressed some of the concerns that were raised at the customer meeting. LUSI asserts that the delay in initiating reuse service was primarily due to a lack of performance of the two micro-screen filters that are part of the treatment process. The Utility received and installed replacement filters from the manufacturer in June 2011, and after satisfactory equipment tests, plans to begin the process of providing reuse service to certain customers within the Lake Groves service area.

The Commission also received approximately 36 letters and emails from customers in opposition to the rate case. Much of the correspondence opposes the rate increase because of the same reasons presented by the customers at the customer meeting, including the short time since the last rate increase and the financial hardship that increased rates would create. There are two petitions from various customer groups with approximately 90 signatures of customers that are in opposition to the rate increase.

As of July 12, 2011, the Commission has received 28 complaints through the Complaint Activity Tracking System (CATS) since 2008, all of which have been addressed and closed. Most of the complaints involved billing issues, water outages, and water quality complaints. The Utility also submitted a record of the complaints that were filed with LUSI by their customers during the test year. Most of the complaints filed with the Utility involved meter reading and

[3] See Order Nos. PSC-09-0101-PAA-WS, issued February 16, 2009, in Docket No. 070693-WS, In re: Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc.

billing issues. In response to complaints, LUSI appears to take appropriate and timely actions, including re-reading the water meter or having it tested for accuracy for billing complaints, or testing the chlorine residual or flushing the lines for water quality complaints. Therefore staff recommends that the Utility's attempt to address customer satisfaction be considered satisfactory.

Overall Quality of Service

In summary, staff recommends that the overall quality of service provided by LUSI be considered satisfactory. The Utility's water and wastewater facilities are in substantial compliance with DEP rules and are in good operational condition. LUSI is also addressing the open Consent Order with the SJRWMD and attempting to achieve compliance. The Utility also appears to be appropriately responding to customer complaints and concerns. Therefore, staff recommends that the overall quality of service provided by the Utility be considered satisfactory.

RATE BASE

Issue 2: Should the audit adjustments to rate base and net operating income to which the Utility agrees be made?

Recommendation: Yes. Based on the audit adjustments agreed to by the Utility, the following adjustments should be made to rate base and net operating income as set forth in staff's analysis below. (Buys, Fletcher)

Staff Analysis: In its response to the staff's audit report and other correspondence, LUSI agreed to the audit adjustments as set forth in the tables below. As such, staff recommends that those adjustments be made.

Table 2-1

LUSI Audit Adjustments	Description of Adjustments
Finding No. 1	Reclassify expenses recorded as plant.
Finding No. 2	Reflect appropriate plant retirements.
Finding No. 5	Reflect supported plant not included in MFRs.
Finding No. 6	Correct errors in the Utility's accumulated depreciation balance.
Finding No. 7	Correct errors in Utility's CIAC and amortization of CIAC.
Finding No. 10	Correct misclassification of revenues recorded in other accounts.
Finding No. 11	Remove non-recurring expenses that have been fully amortized.
Finding No. 12	Reflect a prior Commission-ordered adjustment.
Finding No. 13	Reclassify plant items that were recorded as expenses.
Finding No. 14	Remove all lobbying expenses.
Finding No. 15	Reflect the appropriate allocation of property taxes.
Affiliate Audit Adjustments	Description of Adjustments
Finding No. 1	Reclassify expenses recorded as plant.
Finding No. 4	Correct errors in the Utility's prepaid expenses.
Finding No. 7	Correct errors in the Utility's capitalized salaries.
Finding No. 9	Remove non-utility expenses.

Based on the audit adjustments agreed to by the Utility, staff recommends that the adjustments set forth in staff's analysis below should be made to rate base and net operating income.

Table 2-2

Water								
LUSI Audit Adjustment	Plant	Accum. Deprec.	Deprec. Expense	Contributions in Aid of Construction (CIAC)	Amort. of CIAC	CIAC Amort. Expense	Revenue	O & M Expenses
Finding No. 1	($8,709)	$658	($442)	$0	$0	$0	$0	$0
Finding No. 2	(123,772)	129,035	(4,435)	0	0	0	0	0
Finding No. 5	219	0	0	0	0	0	0	0
Finding No. 6	0	170,515	0	0	0	0	0	0
Finding No. 7	0	0	0	(10,646)	104	288	0	0
Finding No. 10	0	0	0	0	0	0	1,946	0
Finding No. 11	0	0	0	0	0	0	0	(8,733)
Finding No. 12	0	0	0	0	0	0	0	(104,984)
Finding No. 13	236	705	6	0	0	0	0	(2,450)
Finding No. 14	0	0	0	0	0	0	0	(654)
Finding No. 15	0	0	0	0	0	0	0	(45,551)
Affiliate Audit Adjustment	Plant	Accum. Deprec.	Deprec. Expense	CIAC	Amort. of CIAC	Amort. Expense	Revenue	O & M Expenses
Finding No. 1	(171)	8	(16)	0	0	0	0	0
Finding No. 4	0	0	0	0	0	0	0	(3,930)
Finding No. 7	(25,662)	695	(1,390)	0	0	0	0	0
Finding No. 9	0	0	0	0	0	0	0	(3,629)
Adjustment Totals	($157,859)	$185,516	($6,277)	($10,646)	$104	$288	$1,946	($169,931)

Table 2-3

Wastewater								
LUSI Audit Adjustment	Plant	Accum. Deprec.	Deprec. Expense	CIAC	Amort. of CIAC	CIAC Amort. Expense	Revenue	O & M Expenses
Finding No. 1	($19,175)	$1,034	($1,048)	$0	$0	$0	$0	$0
Finding No. 2	(24,150)	25,581	(1,389)	0	0	0	0	0
Finding No. 7	0	0	0	32,579	(2,402)	(1,134)	0	0
Finding No. 11	0	0	0	0	0	0	0	(1,698)
Finding No. 12	0	0	0	0	0	0	0	(62,290)
Finding No. 14	0	0	0	0	0	0	0	(103)
Finding No. 15	0	0	0	0	0	0	0	45,551
Affiliate Audit Adjustment	Plant	Accum. Deprec.	Deprec. Expense	CIAC	Amort. of CIAC	Amort. Expense	Revenue	O & M Expenses
Finding No. 1	(56)	3	(5)	0	0	0	0	0
Finding No. 4	0	0	0	0	0	0	0	(1,297)
Finding No. 7	(8,468)	227	(455)	0	0	0	0	0
Finding No. 9	0	0	0	0	0	0	0	(1,197)
Adjustment Totals	($51,849)	$26,845	($2,897)	$32,579	($2,402)	($1,134)	$0	($21,035)

Issue 3: Should any adjustment be made to the Utility's Project Phoenix Financial/Customer Care Billing System (Phoenix Project)?

Recommendation: Yes. Plant should be reduced by $192,226 for water and $63,427 for wastewater. In addition, accumulated depreciation should be reduced by $47,090 for water and $15,537 for wastewater. Accordingly, depreciation expense should be decreased by $38,052 for water and $12,556 for wastewater. (Buys, Fletcher)

Staff Analysis: The purpose of the Phoenix Project is to improve accounting, customer service, customer billing, and financial and regulatory reporting functions of UI and its subsidiaries. The Phoenix Project became operational in December 2008. During 2009, the Commission approved recovery of the cost of the Phoenix Project in 11 UI rate cases.[4] In those cases, UI allocated the Phoenix Project costs based on each subsidiary's equivalent residential connections (ERCs) to UI's total ERCs.

Allocation of Phoenix Project Costs

In the instant case, UI allocated 4.51 percent of its costs to LUSI based on the ratio of LUSI's total ERCs to UI's total ERCs as of June 30, 2010. LUSI then allocated the cost from UI between its water and wastewater systems using the ERC percentage of 75.19 percent for water and 24.81 percent for wastewater. Based on total Phoenix Project costs of $21,545,555, LUSI calculated its allocated share to be 4.51 percent, or $971,705. Of this amount, 75.19 percent or $730,625 was assigned to the water system, and 24.81 percent or $241,080 was assigned to the wastewater system.

2009 Divestitures of UI Subsidiaries

In 2009, UI divested several Florida subsidiaries including Miles Grant Water and Sewer Company, Utilities, Inc. of Hutchinson Island, and Wedgefield Utilities, Inc., as well as other subsidiaries in other states. In Order No. PSC-10-0585-PAA-WS, the Commission found that allocating costs according to ERCs is an appropriate methodology to spread the cost of the Phoenix Project, but it did not believe the Phoenix Project costs previously allocated to the divested subsidiaries should be reallocated to the surviving utilities. Because no added benefit was realized by the remaining subsidiaries, the Commission found that it is not fair, just or reasonable for ratepayers to bear any additional allocated Phoenix Project costs. Thus, the Commission ruled that the divested subsidiaries' allocation amounts shall be deducted from the total cost of the Phoenix Project before any such costs are allocated to the remaining UI subsidiaries.

Staff Affiliate Audit Finding No. 2

In Order No. PSC-10-0407-PAA-SU, the Commission established the total cost of the Phoenix Project as of December 31, 2008, at $21,617,487 and required UI to deduct $1,724,166 from the total cost of the Phoenix Project to account for the divestiture of several subsidiaries

[4] See Docket Nos. 090531-WS, 090462-WS, 090402-WS, 090392-WS, 080250-SU, 080249-WS, 080248-SU, 080247-SU, 070695-WS, 070694-WS, and 070693-WS.

resulting in a remaining balance of $19,893,321.[5] In this case, staff auditors determined that the Utility did not make the adjustment for the Phoenix Project that the Commission ordered in PSC-10-0407-PAA-WS. According to Affiliate Audit Finding No. 2, LUSI showed the Phoenix Project balance at December 31, 2008, to be $21,545,555. The difference between the Utility's balance and the Commission ordered balance is $1,652,234 ($21,545,555 - $19,893,321). Therefore, the UI balance for the Phoenix Project should be reduced by $1,652,234 to account for the divestiture of subsidiary utilities through 2009. The effect on the filing is a decrease to water and wastewater plant by $56,028 and $18,487, respectively. Corresponding adjustments should also be made to decrease both accumulated depreciation and depreciation expense by $5,603 for water and $1,849 for wastewater. The depreciation calculation is based on a depreciation life of ten years for the Phoenix Project.

In the Utility's response to Affiliate Audit Finding No. 2, LUSI disagreed with the finding and argued that the full balance of the Phoenix Project should be included at the UI level, with 4.51 percent allocated to LUSI. The Utility contends that Order No. PSC-10-0407-PAA-WS does not apply to future filings such as the instant case because it is a violation of Section 367.0813, F.S. LUSI wrote that it believes that it is a violation of Section 367.0813, F.S. to use the gains received by the shareholders on the sale of the divested systems to reduce the rate base of the remaining systems. The Utility stated that reducing the Phoenix Project balance for the remaining subsidiaries creates an improper gain on sale situation in the amount of $1,652,234 because it effectively includes the allocated amount of the Phoenix Project costs with the sale of the divested utilities. LUSI contends that none of the Phoenix Project assets were included in any of the sales and staff's position resulted in stranded assets on which the Utility will never recover. LUSI maintains that the total Phoenix Project balance is currently in-service and benefiting current ratepayers and it is arbitrary and inappropriate to reduce the balance.

In response to LUSI's objection to this adjustment, staff points out that the Commission has already determined in prior UI rate cases that the Phoenix Project balance should be reduced to account for the divestitures of subsidiary UI systems. Staff believes a departure from this practice would result in unfair and inconsistent treatment between UI's subsidiary utilities. If the adjustment is not made in this case, one could argue that LUSI customers would effectively be subsidizing part of the cost of the Phoenix Project for the customers of UI's other subsidiaries.

2010 Divestitures of UI Subsidiaries

In 2010, UI divested four additional subsidiaries as listed below.

Table 3-1

Date	Subsidiary	ERCs
March 1, 2010	Bio Tech Admin. (North Carolina)	281
March 15, 2010	Carolina Water Serv., Inc. of North Carolina	40,055
July 19, 2010	South Carolina Utilities, Inc.	1,322
September 19, 2010	Alafaya Utilities, Inc. (Florida)	8,916

[5] See Docket No. 090381-SU.

These four subsidiaries collectively represent 50,574 ERCs, or approximately 19 percent of the total ERCs for all of UI's subsidiaries. In the interest of consistency, the same Commission-ordered adjustment to deduct the proportional amount of the divested companies from the total cost of the Phoenix Project should also be made for the four subsequent divestitures. As such, staff calculated that the total cost of the Phoenix Project for UI should be reduced by an additional 18.592 percent, or $4,016,359 ($21,617,487 x 18.592 percent), to account for the divestiture of subsidiaries through 2010. The effect on the filing is a decrease to water and wastewater plant of $136,198 and $44,940, respectively. Corresponding adjustments should also be made to decrease both accumulated depreciation and depreciation expense by $13,360 for water and $4,494 for wastewater.

Amortization / Depreciation Period

In Staff Affiliate Audit Finding No. 3, staff auditors discovered that the Utility did not change the depreciation life for the Phoenix Project from eight to ten years as directed in Order No. PSC-10-0407-PAA-SU. In its response to Affiliate Audit Finding No. 3, LUSI disagreed with staff's finding based on the depreciation period used in the previous LUSI rate case in Docket No. 070693-WS. The Utility stated that the Commission previously established a depreciation life of eight years with respect to LUSI and that a departure from this practice would result in an inconsistency between successive rate cases.

In previous UI cases, the Commission approved a 6-year amortization period for the Phoenix Project.[6] In subsequent UI cases, the Commission found that an 8-year amortization period was more appropriate for a software project of this magnitude.[7] In 2010, the Commission set the amortization period for the Phoenix Project to ten years in four separate rate cases involving LUSI sister companies.[8] There were three factors the Commission considered in its decision to increase the amortization period. First, the Phoenix Project was specifically tailor-made to meet all of UI's needs. This project is not "off the shelf" software, but software designed to fulfill long-term accounting, billing, and customer service needs specific to UI and its affiliates and subsidiaries. Second, the Commission concluded that Phoenix Project software will be used for at least ten years. UI's former Legacy accounting system had been used for 21 years. Third, in a recent docket involving a UI subsidiary in Nevada,[9] UI responded that any amortization period between four and ten years would be in compliance with Generally Accepted Accounting Principles (GAAP). Similarly, UI stated to this Commission that its own research revealed that computer software could be amortized over a period of anywhere from four to ten

[6] See Docket Nos. 070695-WS, 070694-WS, and 070693-WS.
[7] See Docket Nos. 080250-SU, 080249-WS, 080248-SU, and 080247-SU.
[8] See Order Nos. PSC-10-0407-PAA-SU, issued June 21, 2010, in Docket No. 090381-SU, In re: Application for Increase in wastewater rates in Seminole County by Utilities Inc. of Longwood; and PSC-10-0400-PAA-WS, issued June 18, 2010, in Docket No. 090392-WS, In re: Application for increase in water and wastewater rates in Lake County by Utilities Inc. of Pennbrooke; and PSC-10-0423-PAA-WS, issued July 1, 2010, in Docket No. 090402-WS, In re: Application for increase in water and wastewater rates in Seminole County by Sanlando Utilities Corporation; and PSC-10-0585-PAA-WS, issued September 22, 2010, In re: Application for increase in water and wastewater rates in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida.
[9] Modified Final Order, issued January 15, 2009, in Docket No. 08-06036.

years.[10] As such, staff believes ten years is the appropriate amortization period for the instant case.

Based on the aforementioned, staff recommends that the appropriate depreciation period for LUSI is ten years which results in a necessary reduction to accumulated depreciation of $27,867 and $9,194 for water and wastewater, respectively. Accordingly, depreciation expense should be reduced by $18,829 for water and $6,213 for wastewater.

Conclusion

Based on the Phoenix Project balance for LUSI and the adjustment for the divestitures as ordered by the Commission in Docket Nos. 090381-SU and 090462-WS, staff believes the total cost of the Phoenix Project for UI should be reduced by the sum of $1,652,234 and $4,016,459 or $5,668,693. The resulting UI Phoenix Project balance for ratemaking purposes is $15,876,961. The appropriate amount of LUSI's allocated share of the Phoenix Project is $716,051 ($15,876,961 x 4.51 percent). Staff's recommended adjustments to LUSI's Phoenix Project balances are outlined in the following table.

Table 3-2

Staff Adjustment	13-Month Average Plant		13-Month Average Accumulated Depreciation		Depreciation Expense	
	Water	Wastewater	Water	Wastewater	Water	Wastewater
Affiliate Audit Finding No. 2	($56,028)	($18,487)	$5,603	$1,849	($5,603)	($1,849)
2010 Divestitures Adjustment	(136,198)	(44,940)	13,620	4,494	(13,620)	(4,494)
Affiliate Audit Finding No. 3	0	0	27,867	9,194	(18,829)	(6,213)
Total	($192,226)	($63,427)	$47,090	$15,537	($38,052)	($12,556)

Accordingly, staff recommends that plant be reduced by $192,226 for water and $63,427 for wastewater. In addition, accumulated depreciation should be reduced by $47,090 for water and $15,537 for wastewater. Depreciation expense should also be decreased by $38,052 for water and $12,556 for wastewater.

[10] See December 2, 2008, Commission Conference Transcript, Page 26, Line 3, through Page 27, Line 19.

Issue 4: Should any adjustments be made to the Utility's requested pro forma plant additions?

Recommendation: Yes. Plant and accumulated depreciation for water should both be reduced by $39,011 to reflect the appropriate retirement amount. Corresponding adjustments for water should be made to decrease depreciation expense and property taxes by $907 and $589, respectively. To reflect the actual supported cost, plant and accumulated depreciation for wastewater should be increased by $4,698 and $261, respectively. Corresponding adjustments for wastewater should be made to increase depreciation expense and property taxes by $261 and $4, respectively. (Buys, Fletcher)

Staff Analysis: LUSI's filing reflected pro forma plant additions, net of retirements, of $633,619 for water and $60,000 for wastewater, as shown in the table below.

Table 4-1

Pro Forma Plant Addition	Water	Wastewater
US Highway 27 Main Relocation	$453,619	$0
Retirement for U.S. Highway 27 Main Relocation	(70,000)	0
Oranges to Vistas Raw Water Main Installation	250,000	0
Treatment Equipment at Lake Groves WWTP	0	60,000
Total Pro Forma Plant Additions	$633,619	$60,000

In response to a staff data request, the Utility stated that the Florida Department of Transportation is widening U.S. Highway 27 North between Lake Louisa Road and SR 50 in Clermont. This roadway project impacted a 16-inch water main located in the right-of-way of U.S. Highway 27 that had to be relocated due to conflicts with storm water and roadway structures. With regard to the Oranges to Vistas Raw Water Main Installation, LUSI asserted that, in order to increase permitted water treatment capacity within the LUSI North community water system to meet current and future demand, a raw water main is proposed to be constructed to convey groundwater from the existing well at the Oranges WTP to the existing piping at the Vitas WTP. Also, the Utility contended that, upon completion of the expansion of its Lake Groves WWTP in December 2009, it was discovered that the installation of the new static screens at the head works resulted in a reduction in the pumping capacity of the Savannas lift station. As a result, LUSI stated that additional pumps were needed at the Savannas lift station to correct the pumping capacity issue.

Based on a review of the support documentation provided by the Utility, staff believes two adjustments are necessary. First, according to the journal entries and other support provided by LUSI, the retirement for U..S Highway 27 Main Relocation was $109,011, instead of the $70,000 included in the Utility's original estimate. As such, plant and accumulated depreciation for water should both be reduced by $39,011 to reflect the appropriate retirement amount.

Accordingly, corresponding adjustments should be made to decrease depreciation expense and property taxes by $907 and $589, respectively. Second, to reflect the actual supported cost for Treatment Equipment at the Lake Groves WWTP, plant and accumulated depreciation for wastewater should be increased by $4,698 and $261, respectively. Accordingly, corresponding adjustments for wastewater should be made to increase depreciation expense and property taxes by $261 and $4, respectively.

Issue 5: What are the used and useful percentages of the Utility's water system?

Recommendation: The water treatment plants for all three water systems are 100 percent used and useful (U&U). The storage facilities for the LUSI North and Lake Groves system are 100 percent U&U. The distribution systems in all three service areas are 100 percent U&U. Staff also recommends that O&M expenses related to chemicals and purchased power be reduced by a total of $30,604 to account for 5.41 percent excessive unaccounted for water (EUW). (Williams, Buys, Fletcher)

Staff Analysis: Rule 25-30.4325, F.A.C., provides that the U&U percentage for a water treatment plant (WTP) is determined by dividing the peak customer demand, less EUW, plus fire flow, and a growth allowance by the firm reliable capacity (FRC) of the wells. For systems with storage facilities, the FRC is based on 16 hours of pumping and the units are referenced in gallons per day (gpd). For systems without storage facilities, the units are referenced in gallons per minute (gpm).

Four Lakes WTP and Lake Saunders WTP

LUSI's service area is made up of three different service areas within Lake County. Four Lakes is a small service area near Montverde that serves approximately 66 customers. Lake Saunders is another small service area near Tavares that serves approximately 44 customers. Both of these areas serve residential customers and are built out with no growth during the past 5 years. The Four Lakes water treatment plant has 2 wells, no storage, and a FRC of 90 gpm. The maximum day demand during the test year was 72,000 gpd, while the peak hour demand was 100 gpm; excessive unaccounted for water of 1 gpm, and the fire flow requirement of 500 gpm, results in a U&U percentage above 100 percent. The Lake Saunders water treatment plant also has 2 wells, with a FRC of 300 gpm, and no storage capacity. The maximum day demand was 29,000 gpd, with a peak hour demand of 40 gpm, excessive unaccounted for water of 0.81 gpm, and a fire flow requirement of 500 gpm. The resulting U&U calculation for the Lake Saunders WTP exceeds 100 percent. Staff therefore recommends that both the Four Lakes and Lake Saunders water plants be considered 100 percent U&U.

LUSI North and Lake Groves

LUSI North and Lake Groves serve approximately 8,800 residential and commercial customers in Clermont. The area is still experiencing growth, with most of the growth occurring in the Lake Groves region. The LUSI North system has 18 small wells that have been interconnected for reliability. The Lake Groves system has 3 wells and is interconnected to the LUSI North system via a water main along U.S. Highway 27. The total FRC for the LUSI North and Lake Groves system is 9,340 gpm, or 8,966,400 gpd. This is less than the FRC from the previous case because of smaller pumps installed on 2 of the Lake Groves wells as a result of restrictions placed on the wells by the SJRWMD requiring those wells to be used only for back up and maintenance purposes. The maximum day demand was 9,955,000 gpd; there was 261,845 gpd of excessive unaccounted for water, and a fire flow requirement of 60,000 gpd. LUSI included a growth allowance of 488,407 gpd, pursuant to Section 367.081(2)(a)2.c., F.S., and

Rule 25-30.431, F.A.C. The resulting U&U calculation exceeds 100 percent, and staff therefore recommends that the LUSI North and Lake Groves WTP be considered 100 percent U&U.

Storage and Distribution Systems

The LUSI North and Lake Groves system has a total usable storage capacity of 3,015,000 gallons. However, the total usable storage capacity is less than the 9,955,000 gallons of peak demand. Therefore, pursuant to Rule 25-30.4325(8), F.A.C., the storage should be considered 100 percent used and useful. Essentially, all of the distribution lines are contributed to the Utility. Therefore, staff recommends that the water distribution systems in all three service areas be considered 100 percent U&U.

Excessive Unaccounted for Water

In its filing, LUSI indicated that all three water systems, Lake Saunders, Four Lakes, and LUSI North and Lake Groves, experienced a 7.65 composite percentage of EUW during the test year. This composite percentage was utilized because the O&M expenses for the three systems are combined. Unaccounted for water is the difference between water produced or purchased and water sold or used in line flushing or for fire fighting. Unaccounted for water typically results from water lost due to line leaks or inaccurate customer meters. Pursuant to Rule 25-30.4325(1)(e), F.A.C., unaccounted for water is considered excessive when it exceeds ten percent of the total volume of water produced or purchased. The Utility was found to have EUW in the previous rate case and an adjustment to O&M expenses was made.[11]

LUSI stated that it stopped using a contracted meter reader and began using Utility employees for meter reading. As a result, the meters are now read more accurately which will decrease EUW. The Utility also began testing customer meter accuracy, and is being required to initiate a meter replacement program by the SJRWMD. For the Lake Saunders system, operational changes were made that decreased the frequency of the iron filter backwash cycles. LUSI also recently replaced the well meter register because of accuracy issues. After reviewing post test year water consumption and pumping data and adjusting for meter reading inaccuracies, it appears that the Utility was able to reduce the amounts of EUW from 7.65 percent to 5.41 percent. Therefore, staff recommends that water O&M expenses related to chemicals and purchased power be reduced by a total of $30,604 to account for EUW of 5.41 percent. In addition, as discussed in Issues 13 and 22, staff recommends adjustments be made to test year water revenues and billing determinants to account for changes implemented by the Utility to more accurately measure customer usage.

[11] See Order Nos. PSC-09-0101-PAA-WS, issued February 16, 2009, in Docket No. 070693-WS, In re: Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc.

Issue 6: What are the used and useful percentages of the Utility's wastewater system?

Recommendation: The wastewater treatment plant is 53 percent U&U. The portions of the plant designated as providing reuse are 100 percent U&U. The collection system is 100 percent U&U. Accordingly, rate base, depreciation expense, and property taxes should be reduced by $685,825, $47,256, and $6,616, respectively. (Williams, Fletcher)

Staff Analysis: Rule 25-30.432, F.A.C., provides that the U&U percentage for a wastewater treatment plant is determined by dividing the customer demand, less excessive infiltration and inflow, plus a growth allowance by the permitted capacity. The rule also contains a provision for consideration of other factors, such as whether the service area is built out, whether the permitted capacity differs from design capacity, and whether flows have decreased due to conservation or reduction in the number of customers. Pursuant to Section 367.0817(3), F.S., this rule does not apply to reuse projects. In addition, pursuant to Section 367.081(2), F.S., a growth allowance is limited to 5 percent per year for 5 years, or a maximum of 25 percent.

In 2007, the treatment capacity of the Lake Groves wastewater treatment plant (WWTP) was expanded from 0.5 million gallons per day (mgd) to 1.0 mgd. It was also upgraded in order to provide reuse for irrigation purposes. In the last rate case, the plant was found to be 52.42 percent U&U, which recognized the potential for additional customer growth that could be handled by the system. The plant facilities associated with the reuse system were found to be 100 percent U&U, consistent with Section 367.0817(3), F.S. The collection system was also found to be 100 percent U&U, because essentially all of the collection lines have been contributed to the Utility.

Subsequent to receiving the wastewater plant permit in August 2007, DEP granted LUSI's request to modify portions of the Operation and Maintenance Requirements provisions of the wastewater plant permit in October 2007. This modification allowed LUSI to reduce the compliance staffing requirements and the number of monthly composite samples collected. The modification decreases the amount of hours that a Class C or higher wastewater plant operator must be on site, as long as the plant flows remain less than 0.500 mgd.

The average annual flow at the plant during the test year was approximately 0.374 mgd. The WWTP flows have slightly increased each year for the past four years, although there has been a fluctuation in customers and a decrease in water demand over that same period. An analysis for infiltration and inflow (I&I) shows that there is no excessive I&I and no adjustment is necessary. A total growth allowance of 19,719 gpd was included pursuant to Section 367.081(2)(a)2.c., F.S., and Rule 25-30.431, F.A.C. Based on the permitted capacity of 1.0 mgd, the calculation results in a 40 percent U&U percentage.

In its application, the Utility requested that the wastewater plant be considered 79 percent U&U based on the modified permit conditions. This modification to the permit is a temporary provision that allowed LUSI to reduce certain staffing and reporting requirements and this modification only lasts as long as the plant flows do not exceed 0.500 mgd. Once flows exceed 0.500 mgd, the staffing and reporting requirements associated with the full 1.0 mgd capacity of the plant go into effect.

Staff believes that the plant has the capacity to handle additional customer growth. However, in order to account for factors such as conservation and a reduction in customers, staff recommends that, consistent with previous Commission decisions,[12] the Lake Groves WWTP be found 53 percent U&U, the U&U percentage from the last case. In addition, similar to the Commission's decision in the Utility's last rate case, staff recommends that all of the collection lines and all plant facilities associated with providing reuse be considered 100 percent U&U. Accordingly, staff recommends that rate base, depreciation expense, and property taxes be reduced by $685,825, $47,256, and $6,616, respectively.

[12] See Order Nos. PSC-09-0385-FOF-WS, issued May 29, 2009, in Docket No. 080121-WS, In re: Application for increase in water and wastewater rates in Alachua, Brevard, DeSoto, Highlands, Lake, Lee, Marion, Orange, Palm Beach, Pasco, Polk, Putnam, Seminole, Sumter, Volusia, and Washington Counties by Aqua Utilities Florida Inc., pp. 36-38; PSC-10-0585-PAA-WS, issued September 22, 2010, in Docket No. 090462-WS, In re: Application for increase in water and wastewater rates in Marion, Orange, Pasco, Pinellas, and Seminole Counties by Utilities Inc. of Florida, pp. 14-15; and PSC-03-1440-FOF-WS, issued December 22, 2003, in Docket No. 020071-WS, In re: Application for increase in Marion, Orange, Pasco, Pinellas, and Seminole Counties by Utilities Inc. of Florida, pp. 36-38, 64-66.

Issue 7: Should any adjustment be made to deferred rate case expense?

Recommendation: Yes. Consistent with the annual amortization amount approved in the Utility's last rate case and Commission practice, deferred rate case expense (DRCE) included in the working capital allowance should be decreased by $263,719, or $198,290 for water and $65,429 for wastewater. (Buys)

Staff Analysis: In its filing, LUSI included $486,749 in its working capital allowance for DRCE. Of that amount, $317,784 is the 13-month average balance of DRCE from the Utility's 2009 rate case. LUSI made an adjustment of $55,386 to correct the actual expense per books to the Commission allowed rate case expense, for a net 13-month balance of $262,398. The remainder of the amount is one-half of the estimated DRCE for the current rate case, or $224,351. Staff is recommending two adjustments. The first adjustment is a reduction in the DRCE from the 2009 case and the second adjustment is related to the DRCE for the current case.

Deferred Rate Case Expense – 2009 Rate Case

In LUSI's 2009 rate case, the Commission approved rate case expense of $331,450 to be amortized over four years.[13] The rates and rate case expense amortization from that case went into effect on March 23, 2009. Recognizing that rates for the instant rate case will not go into effect before September 2011, staff calculated a 13-month average balance of $165,725 for the beginning of the first year the new rates will go into effect. Commission practice is to include one-half of rate case expense in working capital.[14] As such, one-half of the 13-month average balance of $165,725, or $82,863, should be included in the working capital allowance. Therefore, staff believes the Utility's prior-case DRCE 13-month average net balance of $262,398 should be reduced by $179,535 to $82,863. This adjustment is consistent with the Commission's recent decision in the Aqua Utilities Florida, Inc. (AUF) rate case.[15] Staff notes that while the Commission's PAA decision in the AUF case on the level of rate case expense has been protested, this adjustment was not protested and therefore is now deemed stipulated pursuant to Section 120.80 (13)(b), F.S.

Deferred Rate Case Expense-Current Rate Case

The Utility included a pro forma adjustment of $224,351 in the working capital allowance for DRCE from the current rate case. In Issue 18, staff is recommending rate case expense of $288,327 for the current rate case. Consistent with long-standing Commission practice, one-half of the total rate case expense, or $144,164, should be included in the working

[13] See Order No. PSC-09-0101-PAA-WS, issued February 16, 2009, in Docket No. 070693-WS, In re: Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc. at pp. 11-14.
[14] See Order Nos. PSC-09-0375-PAA-GU, issued May 27, 2009, in Docket No. 080366-GU, In re: Petition for rate increase by Florida Public Utilities Company, at p. 21; and PSC-00-0248-PAA-WU, issued February 7, 2000, in Docket No. 990535-WU, In re: Request for approval of increase in water rates in Nassau County by Florida Public Utilities Company (Fernandina Beach System), at pp. 13-14.
[15] See Order No. PSC-11-0256-PAA-WS, issued June 13, 2011, in Docket No. 100330-WS, In re: Application for increase in water/wastewater rates in Alachua, Brevard, DeSoto, Hardee, Highlands, Lake, Lee, Marion, Orange, Palm Beach, Pasco, Polk, Putnam, Seminole, Sumter, Volusia, and Washington Counties by Aqua Utilities Florida, Inc. at pp. 56-58.

capital allowance. As such, staff believes an adjustment of $80,187 should be made to reduce LUSI's pro forma adjustment of $224,351 to $144,164.

Conclusion

Based on the above, staff believes the Utility's DRCE should be decreased by $179,535 to reflect the appropriate amount for the 2009 rate case, and decreased by $84,184 to reflect the appropriate amount for the current rate case. The appropriate total amount of DRCE is $224,351. Consistent with the annual amortization amount approved in LUSI's last rate case and Commission practice, staff recommends that DRCE included in the working capital allowance should be decreased by $263,719, or $198,290 for water and $65,429 for wastewater.

<u>**Issue 8**</u>: What is the appropriate working capital allowance?

<u>**Recommendation**</u>: The appropriate amount of working capital is $573,484 for water and $205,058 for wastewater. Accordingly, the working capital allowance for water should be reduced by $47,972 in addition to the adjustments recommended in Issue 7. (Buys)

<u>**Staff Analysis**</u>: Rule 25-30.433(2), F.A.C., requires that Class A utilities use the balance sheet method to calculate the working capital allowance. The balance sheet approach generally defines working capital as current assets and deferred debits that are utility-related and do not already earn a return, less current liabilities, deferred credits and operating reserves that are utility-related and upon which a utility does not already pay a return. The Utility has properly filed its allowance for working capital using the balance sheet method. In its filing, LUSI reflected a working capital allowance of $1,090,233 ($819,746 for water and $270,487 or wastewater) using the balance sheet approach.

<u>Deferred Rate Case Expense</u>

It is Commission practice to include the 13-month average approved amount of rate case expense from prior cases and one half of the approved amount from the instant case in the working capital calculation for Class A water and wastewater utilities.[16] As discussed in Issue 7, staff believes the appropriate amount of DRCE to include in the working capital allowance is $224,351. The Utility included $486,749 for the 2009 and current rate case expense. Staff recommends that the DRCE included in the working capital should be decreased by $263,719 ($486,749 - $224,351).

<u>Miscellaneous Deferred Debits</u>

The Utility included miscellaneous deferred debits of $250,704 in the working capital. The cost of obtaining a consumptive use permit (CUP) renewal from the SJRWMD of $239,862 is included in miscellaneous deferred debits. In Issue 14, staff recommends that the CUP renewal expense of $239,862 be amortized over five years and include one-fifth of the expense, or $47,972, in water O&M expenses for the test year. The same amount should be deducted from the amount for the CUP renewal that is included in the water working capital to prevent double recovery of $47,972. Accordingly, staff believes that a corresponding adjustment should be made to reduce the working capital for water by $47,972.

Based on the above, staff believes DRCE should be reduced by a total of $262,398, or $197,297 for water and $65,101 for wastewater. The working capital for water should be further reduced by $47,972 for the adjustment related to the pro forma CUP renewal expense. Thus, staff recommends the appropriate working capital is $573,484 for water and $205,058 for wastewater.

[16] <u>See</u> Order Nos. PSC-08-0327-FOF-EI, issued May 19, 2008, in Docket No. 070304-EI, <u>In re: Review of 2007 Electric Infrastructure Storm Hardening Plan filed pursuant to Rule 25-6.0342, F.A.C., submitted by Florida Public Utilities Company.</u>; PSC-01-0326-FOF-SU, issued February 6, 2001, in Docket No. 991643-SU, <u>In re: Application for increase in wastewater rates in Seven Springs System in Pasco County by Aloha Utilities, Inc.</u>; and PSC-97-1225-FOF-WU, issued October 10, 1997, in Docket No. 970164-WU, <u>In re: Application for increase in rates in Martin County by Hobe Sound Water Company</u>.

Issue 9: What is the appropriate rate base for the historical test year ended June 30, 2010?

Recommendation: The appropriate rate base for the historical test year ended June 30, 2010, is $17,882,426 for water and $5,433,507 for wastewater. (Buys)

Staff Analysis: In its MFRs, the Utility recorded rate base of $18,140,810 for water and $6,223,040 for wastewater. Staff has calculated LUSI's water and wastewater rate bases using the Utility's MFRs with adjustments as recommended in the preceding issues. Accordingly, staff recommends that the appropriate rate base for the historical test year ended June 30, 2010, is $17,882,426 for water and $5,433,507 for wastewater. Staff's recommended schedules for rate base are shown on Schedules Nos. 1-A and 1-B, respectively. The adjustments are shown on Schedule No. 1-C.

Issue 10: What is the appropriate return on equity?

Recommendation: Based on the Commission leverage formula currently in effect, the appropriate return on equity (ROE) is 10.80 percent. Staff recommends an allowed range of plus or minus 100 basis points be recognized for ratemaking purposes. (Buys)

Staff Analysis: The ROE included in the Utility's filing is 10.55 percent based on the 2010 leverage formula. Based on the 2011 leverage formula and an equity ratio of 43.41 percent, the appropriate ROE is 10.80 percent.[17] Staff recommends an allowed range of plus or minus 100 basis points be recognized for ratemaking purposes.

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[17] See Order Nos. PSC-11-0287-PAA-WS, issued July 5, 2011, in Docket No. 110006-WS, In re: Water and Wastewater Industry Annual Reestablishment of Authorized Range of Return on Common Equity for Water and Wastewater Utilities Pursuant to Section 367.081(4)(f), Florida Statutes.

Issue 11: What is the appropriate cost rate for short-term debt?

Recommendation: The appropriate cost rate for short-term debt is 3.17 percent. (Buys)

Staff Analysis: The cost rate for short-term debt included in the Utility's filing was 4.28 percent. According to Audit Finding No. 5, LUSI could not provide supporting documentation for the total interest expense to substantiate the cost rate listed on the short-term debt schedule. Staff auditors recalculated the cost rate for short-term debt to be 3.17 percent. The Utility did not object to Staff Audit Finding No. 5. As such, staff recommends that the appropriate cost rate for short-term debt is 3.17 percent.

Issue 12: What is the appropriate weighted average cost of capital including the proper components, amounts, and cost rates associated with the capital structure for the historical test year ended June 30, 2010?

Recommendation: The appropriate weighted average cost of capital for the historical test year ended June 30, 2010, is 8.13 percent. (Buys)

Staff Analysis: The weighted average cost of capital included in the Utility's filing is 8.12 percent. With the exception of the cost rate for short-term debt and ROE, staff calculated the weighted average cost of capital based on the test year components, amounts, and cost rates listed in LUSI's MFR Schedule D-2. The cost rate for short-term debt was addressed in Issue 11 and the ROE was addressed in Issue 10. Based upon the proper components, amounts, and cost rates associated with the test year ended June 30, 2010, staff recommends a weighted average cost of capital of 8.13 percent. Schedule No. 2 details staff's recommendation.

NET OPERATING INCOME

Issue 13: Should any further adjustments be made to test year revenues?

Recommendation: Yes. To reflect income from plant leased to others, revenues should be increased by $12,261 and $4,045 for water and wastewater, respectively. In addition, to reflect additional revenues from improved meter reading of customer usage, water revenue should be further increased by $60,074. (Buys, Fletcher, Lingo)

Staff Analysis: In its filing, LUSI reflected adjusted test year revenues of $4,233,759 for water and $2,096,964 for wastewater. Based on a review of the MFRs and the Utility's recent annual report, staff discovered LUSI failed to include revenues associated with income received from plant leased to others. As will be discussed in greater detail in Issue 22, staff recommends that the test year kgals sold for the water system be increased by 27,571 kgals. This adjustment reflects an approximate 1.9 percent increase in the number of kgals pumped that are captured for billing purposes. This results in an increase in test year revenues for the water system of $60,704. Accordingly, staff recommends that revenues be increased by $72,335 and $4,045 for water and wastewater, respectively.

Issue 14: Should any adjustment be made to the Utility's pro forma O&M expense related to the amortization of LUSI's cost to obtain a consumptive use permit?

Recommendation: Yes. The amortization of the cost to obtain the CUP should be increased from 30 months to 60 months and water pro forma O&M expense should reduced by $47,972. (Buys)

Staff Analysis: On MFR Schedule B-3, the Utility recorded a pro forma adjustment to O&M expense of $95,945 to recover the cost of obtaining a CUP from the SJRWMD. The cost incurred to obtain the permit was $239,862. Staff reviewed the invoices and verified the cost was incurred. The CUP will expire at the end of 2013, or approximately 30 months from the date of issue. Based on the time period between the approval date and the expiration date, the Utility estimated the amortization period to be 30 months. However, the application process has been ongoing since November 2006 and incurred several delays before obtaining the permit in May 2011. It is Commission practice to amortize expenses over the time in which they are incurred in accordance with GAAP matching principles. In this case, LUSI has incurred costs related to the application since 2006. Further, staff believes the cost of the permit is atypically high due to the multiple delays incurred by the Utility and that cost should not be borne by the ratepayers over a shortened amortization period. Hence, staff believes a 5-year amortization period is more appropriate and reasonable than a 30-month period. Based on a 5-year amortization period, staff believes the appropriate amount of amortization is $47,973 ($239,862 ÷ 60 months x 12). Accordingly, staff recommends that the amortization of the CUP renewal should be increased from 30 months to 60 months and water pro forma O&M expense should reduced by $47,972.

Issue 15: Should any adjustments be made to the Utility's salaries and wages expense and employee pensions and benefits expense?

Recommendation: Yes. Salaries and wages expense should be reduced by $62,658 for water and $20,674 for wastewater. In addition, employee pensions and benefits expense should be reduced by $68,429 for water and $22,577 for wastewater. Corresponding adjustments should be made to reduce payroll taxes by $6,084 for water and $2,007 for wastewater. (Buys)

Staff Analysis:

Salaries and Wages Expense

In its MFRs, LUSI reflected water and wastewater salaries and wages of $607,603 and $200,477, respectfully. On MFR Schedules B-7 and B-8, LUSI explained the increase in the salaries and wages expense for water reflects the addition of a water conservation coordinator position that was required by the SJRWMD, and the increase for wastewater can be attributed to an additional wastewater system operator to staff the new wastewater reuse plant. The salaries for the water conservation coordinator and the additional wastewater system operator are included in the test year expenses and are not a pro forma or an annualization adjustment.

In its filing, LUSI made two adjustments to the salaries and wages expense for the current test year. The first adjustment annualized the salaries and wages expense, and the second adjustment was a pro forma increase to pay for a 3.5 percent salary increase in April 2011. Given the tumultuous state of the economy, staff believes that any pay increase at this time should not be borne by the ratepayers. As such, staff believes the Utility's annualization adjustment and pro forma pay increase should be disallowed. This is consistent with the Commission's recent decision in the AUF rate case.[18] Therefore, staff believes an adjustment to reduce LUSI's requested salaries and wages expense by the amount of the annualization and pro forma adjustments is appropriate. Staff notes, however, that this adjustment has been protested in the AUF case.

Based on the above, staff recommends that salaries and wages expense should be reduced by $62,658 for water and $20,674 for wastewater.

Pensions and Benefits Expense

In its filing, LUSI requested employee pensions and benefits expense of $176,077 for water and $58,095 for wastewater. In its last rate case, the Commission approved water and wastewater employee pension and benefit expense of $124,483 and $41,263, respectively. The amounts were 21.63 percent of the salaries and wages expense approved in the 2009 rate case. In the instant case, LUSI is requesting employee pension and benefit expense equal to 29.0 percent of the Utility's requested salaries and wages expense. The requested amount represents a

[18] See Order No. PSC-11-0256-PAA-WS, issued June 13, 2011, in Docket No. 100330-WS, In re: Application for increase in water/wastewater rates in Alachua, Brevard, DeSoto, Hardee, Highlands, Lake, Lee, Marion, Orange, Palm Beach, Pasco, Polk, Putnam, Seminole, Sumter, Volusia, and Washington Counties by Aqua Utilities Florida, Inc., at p. 80. (Staff notes, however, that this adjustment has been protested in the AUF case.)

34 percent increase over the amount approved in LUSI's last rate case. On MFR Schedules B-7 and B-8, for both water and wastewater, the Utility explained that the increase is a fallout from the increase in the number of full-time staff as well as adjustments in compensation levels. However, staff was unable to reconcile the requested increase in employee pensions and benefits expense with the information submitted by the Utility.

In LUSI's response to staff's data request dated January 4, 2011, the Utility provided a schedule that listed the UI employee benefit expenses from calendar year 2009 through June 2010. The schedule indicated a decrease in benefit expense from $3,823,675 in 2009 to $3,654,083 in the test year ended June 30, 2010. This represents a 4.43 percent decrease in the employee benefit expenses over that same period. In the Utility's response to another staff data request, LUSI provided a schedule that listed, by employee, all the employee expenses for UI and the allocated amounts for LUSI. The new positions for the water conservation coordinator and the wastewater system operator were included in the list. Based on the information provided by LUSI, staff calculated that the employee pension and benefit costs for LUSI equates to 23.43 percent of the salaries and wages expense. Therefore, staff believes it is reasonable and appropriate to base the amount of employee pension and benefit expense on 23.43 percent of employee salaries and wages expense. Accordingly, staff recommends that employee pension and benefit expense should be reduced by $68,429 for water and $22,577 for wastewater.

Conclusion

Based on the above, staff believes the requested salaries and wages expense, and employee pensions and benefits expense are excessive. The Utility has the burden of proving that its costs are reasonable.[19] Staff believes that the Utility has not met its burden of proof for the proposed increase in salaries and wages expense, and employee pensions and benefits expense. Accordingly, staff recommends that salaries and wages expense be reduced by $62,658 for water and $20,674 for wastewater. In addition, employee pensions and benefits expense should be reduced by $68,429 for water and $22,577 for wastewater. Corresponding adjustments should be made to reduce payroll taxes by $6,085 for water and $2,008 for wastewater.

[19] See Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (1982).

Issue 16: Should any further allocation expense adjustments be made?

Recommendation: Yes. To reflect the appropriate amount of allocated directors and officers (D&O) liability insurance expense, O&M expenses should be reduced by $1,828 for water and $603 for wastewater. (Buys, Fletcher)

Staff Analysis: In its filing, the Utility included allocated D&O liability insurance expense of $3,655 for water and $1,206 for wastewater. Staff notes that, in the recent Final Order in the Tampa Electric Company rate case, the Commission found the following:

> We find that DOL insurance is a part of doing business for a publicly-owned Company. It is necessary to attract and retain competent directors and officers. Corporate surveys indicate that virtually all public entities maintain DOL insurance, including investor-owned electric utilities.[20]

In addition, staff notes that, in the recent Progress Energy Florida, Inc. rate case, the Commission found the following:

> In summary, we believe that D&O liability insurance has become a necessary part of conducting business for any publicly owned company and it would be difficult for companies to attract and retain competent directors and officers without it. We also believe that ratepayers receive benefits from being part of a large public company including, among other things, easier access to capital. Because D&O liability insurance benefits both the ratepayer and the shareholder, it should be a shared cost. Thus, we find that O&M expense shall be reduced by $964,913 jurisdictional to reflect the sharing of costs between the ratepayers and the shareholders.[21]

Based on the above, staff recommends D&O liability insurance costs be shared between the ratepayers and the shareholders. Therefore, staff recommends that O&M expense should be reduced by $1,828 for water and $603 for wastewater.

[20] See Order No. PSC-09-0283-FOF-EI, issued April 30, 2009, in Docket No. 080317-EI, In re: Petition for rate increase by Tampa Electric Company, p. 64.
[21] See Order No. PSC-10-0131-FOF-EI, issued March 5, 2010, in Docket No. 090079-EI, In re: Petition for increase in rates by Progress Energy Florida, Inc., pp. 98-99.

<u>Issue 17</u>: Should any adjustments be made to the Utility's bad debt expense?

<u>Recommendation</u>: Yes. LUSI's bad debt expense should be based on a 3-year average. Accordingly, water and wastewater bad debt expense should be reduced by $36,454 and $12,058, respectively. (Buys)

<u>Staff Analysis</u>: The Utility recorded bad debt expense of $83,539 for water and $27,563 for wastewater in the test year. In numerous decisions, the Commission has set bad debt expense using the 3-year average in electric,[22] gas,[23] and water and wastewater cases.[24] The Commission approved a 3-year average in these cases based on the premise that a 3-year average fairly represented the expected bad debt expense. Overall, the basis for determining bad debt expense has been whether the amount is representative of the bad debt expense to be incurred by the Utility.

Staff calculated the 3-year average using the bad debt expense reported in the Utility's annual reports for 2008, 2009, and 2010. Based on the 3-year average calculation, LUSI should be entitled to bad debt expense of $47,085 for water and $15,505 for wastewater, which staff believes is representative of the Utility's bad debt expense. As a result, staff recommends that LUSI's bad debt expense of $83,539 for water and $27,563 for wastewater should be reduced by $36,454 and $12,058, respectively.

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[22]<u>See</u> Order Nos. PSC-94-0170-FOF-EI, issued February 10, 1994, in Docket No. 930400-EI, <u>In re: Application for a Rate Increase for Marianna electric operations by Florida Public Utilities Company</u>, at p. 20; PSC-93-0165-FOF-EI, issued February 2, 1993, in Docket No. 920324-EI, <u>In re: Application for a rate increase by Tampa Electric Company</u>, at pp. 69-70; and PSC-92-1197-FOF-EI, issued October 22, 1992, in Docket No. 910890-EI, <u>In re: Petition for a rate increase by Florida Power Corporation</u>, at p. 48.
[23] <u>See</u> Order Nos. PSC-92-0924-FOF-GU, issued September 3, 1992, in Docket No. 911150-GU, <u>In re: Application for a rate increase by Peoples Gas System, Inc.</u>, p. 6; and PSC-92-0580-FOF-GU, issued June 29, 1992, in Docket No. 910778-GU, <u>In re: Petition for a rate increase by West Florida Natural Gas Company</u>, pp. 30-31.
[24]<u>See</u> Order Nos. PSC-10-0407-PAA-SU, PSC-10-0423-PAA-WS, PSC-09-0385-FOF-WS, pp. 92-96; and PSC-10-0585-PAA-WS, pp. 43-44.

Issue 18: What is the appropriate amount of rate case expense?

Recommendation: The appropriate amount of rate case expense is $288,327. This expense should be recovered over four years for an annual expense of $72,082, or $54,199 for water and $17,883 for wastewater. Therefore, annual rate case expense should be reduced by $30,147 for water and $9,947 for wastewater. (Buys)

Staff Analysis: In its MFRs, the Utility included an estimate of $448,701 for current rate case expense. Staff requested an update of the actual rate case expense incurred, with supporting documentation, as well as the estimated amount to complete the case. On June 24, 2011, the Utility submitted a revised estimated rate case expense through completion of the PAA process of $380,103.

Table 18-1

	MFR Estimated	Actual as of June 9, 2011	Additional Estimated	Revised Total
Legal Fees	$66,300	$61,768	$15,556	$77,324
Accounting Consultant Fees	264,900	89,763	7,000	96,763
Engineering Consultant Fees	18,150	30,164	1,800	31,964
WSC In-house Fees	76,776	99,650	41,275	140,925
Filing Fee	4,000	7,000	0	7,000
Travel- WSC	3,200	353	2,847	3,200
Temp Employee Fees-WSC	0	2,707	500	3207
Miscellaneous	12,000	75	11,925	12,000
Notices	3,375	7,720	0	7,720
Total Rate Case Expense	$448,701	$299,200	$80,903	$380,103

Pursuant to Section 367.081(7), F.S., the Commission shall determine the reasonableness of rate case expense and shall disallow all rate case expense determined to be unreasonable. Staff has examined the requested actual expenses, supporting documentation, and estimated expenses as listed above for the current rate case. Based on our review, staff believes several adjustments are necessary to the revised rate case expense estimate.

MFR Deficiencies

The first adjustment relates to costs incurred to correct deficiencies in the MFR filing. Based on staff's review of invoices of the Utility's consultants, a combined amount of $5,850 was billed for correcting MFR deficiencies and revising the Utility's filing. Specifically, $3,535 related to legal fees, $538 related to accounting fees, and $150 related to engineering fees. In addition, WSC employees spent 40 hours and incurred an expense of $1,627 correcting MFR deficiencies. Accordingly, staff recommends that $5,850 be removed as duplicative and unreasonable rate case expense. The Commission has previously disallowed rate case expense associated with correcting MFR deficiencies because of duplicate filing costs.[25]

Legal Consultant Fees

The second adjustment relates to the legal fees billed for this case. The revised MFR Schedule B-10 reflected actual legal consulting charges of $61,768. The invoices provided to support the requested amount total $58,350. Hence, legal fees should be reduced by $3,418 for lack of support documentation ($61,768 - $58,350). The rate case filing fee of $7,000 was included in the total amount of the legal fees billed to the Utility. LUSI also included the $7,000 filing fee as a separate line item in the B-10 Schedule. Thus, legal fees should be reduced by $7,000 to remove the duplicate cost of the rate case filing fee. In addition, the Utility submitted two invoices for legal fees in the amounts of $528 and $817 that were not related to the instant rate case, and a third invoice in the amount of $817 was a duplicate. The charges billed on the three invoices totaled $2,163. Hence, legal fees should be further reduced by $2,163. The total amount of actual legal fees incurred that were supported by the Utility equals $49,187 ($58,350 - $7,000 - $2,163). Hence, the charges related to legal fees should be reduced by $12,581 ($61,768 - $49,187).

The third adjustment relates to the remaining estimated legal fees to complete the PAA process. In its breakdown of estimated legal fees of $15,675, the Utility applied an hourly rate of $330 for 47.5 estimated hours. The law firm representing LUSI has a partner billing at a rate of $340 per hour and an associate lawyer billing at a rate of $315 per hour. During the rate case, the associate lawyer billed 91 percent of the hours. Therefore, staff believes it is reasonable to assume that, with the exception of the fifteen hours estimated to prepare for and attend the Commission Conference, the associate lawyer will be working the remainder of the rate case which represents a total of 32.5 hours. As such, staff believes that legal fees should be recalculated and reduced by $338.

Accounting Consultant Fees

The fourth adjustment relates to the Utility's accounting consultant fees. The revised MFR Schedule B-10 reflected actual accounting consultant charges of $89,763. The invoices provided to support the requested amount totaled $87,850. Hence, accounting fees should be reduced by $1,913 for lack of support documentation ($89,763 - $87,850). In addition, LUSI

[25] See Order Nos. PSC-05-0624-PAA-WS, issued June 7, 2005, in Docket No. 040450-WS, In re: Application for rate increase in Martin County by Indiantown Company, Inc.; and PSC-01-0326-FOF-SU, issued February 6, 2001, in Docket No. 991643-SU, In re: Application for increase in wastewater rates in Seven Springs System in Pasco County by Aloha Utilities, Inc.

included an estimate of $7,000 for additional work to complete this case. The only support provided for the work to be performed was "Assist w/MFRs, data requests, and audit facilitation." Staff notes that there would be no work remaining for MFRs and audit facilitation. Also, staff believes any remaining data requests would be more appropriately addressed by WSC in-house employees. As such, staff believes that $7,000 should be removed as unreasonable and unsupported rate case expense. Accordingly, staff recommends that accounting consultant fees be reduced by $8,913 ($7,000 + $1,913).

Engineering Consultant Fees

The fifth adjustment relates to the Utility's actual engineering consulting fees and its estimated engineering consultant fees to complete the rate case. LUSI requested total engineering fees of $31,964 which was comprised of $30,164 in actual costs and $1,800 in estimated remaining fees through the PAA process. The estimated remaining hours to complete the PAA process for engineering consulting fees totaled 12 hours or $1,800. The only support provided for the work to be performed was ten hours to "Assist w/& Respond to Data Req. & New Info." and two hours to "Prepare for and Attend Agenda." Staff notes that there would be no work remaining for responding to data requests and new information and the engineering consultant rarely attends the Commission Conference. Also, staff believes any remaining data requests would be more appropriately addressed by WSC in-house employees. Accordingly, staff recommends that engineering consultant fees be reduced by $1,800.

WSC In-house Employee Fees

The sixth adjustment relates to WSC in-house employee fees. In its rate case expense update, the Utility reported that the total number of actual hours incurred by WSC in-house employees as of June 9, 2011, was 2,543, and estimated an additional 813 hours remaining to complete the rate case, for a total of 3,356 hours. Staff believes the number of hours proposed by LUSI for WSC in-house employee fees is excessive, unreasonable, and unsupported. In the Utility's 2009 rate case, the total number of hours incurred by all the consultants and WSC in-house employees combined was 3,219. In this case, the Utility estimated the total number of hours incurred by all the consultants and WSC in-house employees to prepare the MFRs, respond to all audit requests, data requests, discovery, and complete the rate case through the PAA process is 4,242.

In the 2009 rate case, the Utility used the projected test year ended June 30, 2009, which required additional MFR preparation and auditing as compared to this rate case which used only the historical test year ended June 30, 2010. It stands to reason that the hours incurred to process the entire rate case by WSC in-house employees in this rate case would be less than the 2009 rate case. In comparison, LUSI reported that the accounting consultant incurred 1,427 hours in the 2009 rate case, but reported that 588 total hours had been incurred in this rate case as of June 9, 2011. This equates to a 59 percent decrease in the number of hours incurred by the accounting consultant to prepare the MFRs and respond to the audit and data requests. As such, staff expected to see a decrease in the number of hours incurred by WSC in-house employees to prepare the MFRs in this case as compared to the prior rate case. The total number of hours incurred by WSC in-house employees in LUSI's last rate case was 1,585. In the instant case, LUSI reported that 2,543 hours had been incurred as of June 9, 2011. Staff believes the number of hours is unreasonable and excessive.

Based on the detailed timesheets provided by LUSI, staff determined that WSC in-house employees spent 1,199 of the 2,543 hours preparing the MFRs for filing. Staff believes the number of hours spent on preparing the MFRs is excessive. UI has made the decision to not keep its books and records in accordance with NARUC system of accounts. As a result, WSC in-house employees spend additional time re-stating depreciation, making "roll-forward" adjustments to account for regulatory accounting and Commission-ordered adjustments, and re-calculating the 13-month average balance. For example, one WSC in-house employee recorded 162 hours working on a depreciation re-statement and correcting the 13-month average balance. The hourly rate for the employee is $50 for a total expense of $8,100. In response to staff's data request regarding the purpose for the work, LUSI explained:

> This file is created to account for Commission-ordered adjustments as well as correct depreciation errors and coding reclassifications that need to be made. These corrections must be made in order to prepare accurate MFRs. In addition, the Company's regulatory ledger currently does not depreciate, and this file must be created in order to depreciate any items that are on that ledger that should be depreciating.

Staff believes the Utility's ratepayers should not be required to bear the added cost of correcting errors and re-calculating depreciation as part of rate case expense. Accordingly, staff recommends that rate case expense should be decreased by $8,100.

In addition, a second WSC in-house employee recorded 64 hours for correcting errors, assisting other employees, correcting formatting errors, and re-running data. The 64 hours of work performed by this employee appears to be duplicative of the work performed by co-workers, and as such, should be removed from rate case expense. The hourly rate for this employee is $41 for a total expense of $2,624. Accordingly, staff recommends that rate case expense be reduced by $2,624.

A third WSC In-house employee recorded 24 hours reconciling the PDF files for the 2007, 2008, and 2009 annual reports to the Excel file versions. The employee also recorded 23 hours correcting the placed in-service dates on the computer file restatement and re-reconciling the corrected annual report to the trial balance. The work performed appears to be time incurred correcting errors and is duplicative in nature. The hourly rate for this employee is $40 for a total expense of $1,880. Accordingly, staff recommends that rate case expense be reduced by $1,880.

A fourth WSC employee recorded 46 hours for "Supporting production of MFRs. Additional engineering data provided." Staff believes the activities listed do not contain sufficient detail to support the expense. The hourly rate for this employee is $39.36 for a total expense of $1,838. Accordingly, staff recommends that rate case expense be reduced by $1,838.

A fifth WSC employee recorded 38 hours for "Pull Invoices for Audit Requests" and "Scan Invoices for Audit Requests." The time period for the hours recorded preceded the dates of the staff audit for LUSI. Hence, it appears the activities were not related to the LUSI rate case. The hourly rate for this employee is $24 for a total expense of $912. Accordingly, staff recommends that rate case expense be reduced by $912.

Based on the aforementioned, staff believes that 357 hours associated with WSC in-house fees of $15,327 related to the preparation of the MFRs should be disallowed. This results in 842 hours for MFR preparation which staff believes is more reasonable.

The remaining 1,344 hours reportedly incurred by WSC in-house employees was related to responding to staff data requests, staff audit requests, and OPC discovery. In the instant case, staff sent out data requests totaling 87 questions and sub-parts. In LUSI's 2009 rate case, staff sent out data requests totaling 66 questions and sub-parts. In both cases, OPC intervened and requested discovery and staff performed audits on the Utility and Affiliates. As such, the number of hours incurred to respond to data requests, audit requests and discovery in this rate case should be reasonably close to the number of hours incurred in the Utility's 2009 rate case. The total number of hours incurred by WSC in-house employees in the 2009 rate case was 1,585. Therefore, the total number of hours incurred as of June 9, 2011, should not be greater than the 2009 rate case. Staff recommends 842 hours for MFR preparation and filing the rate case. Hence, no more than 743 hours should be allowed for WSC in-house employees responding to staff data requests, staff audit requests, and OPC discovery. Therefore, staff believes 601 hours should be disallowed as excessive and unreasonable rate case expense. According to the supporting data provided by the Utility, six WSC employees recorded time for responding to data requests, audit requests, and OPC's discovery. The average hourly rate for the six employees is $37.73. Accordingly, staff recommends that rate case expense be reduced by $22,674 (601 hours x $37.73 per hour).

The Utility estimated an additional 813 hours for WSC in-house employees to complete the rate case through the PAA process for an expense of $41,276. LUSI explained the additional hours are related to assistance with MFRs, data requests, audit facilitation, billing analysis, implementation of rates, and customer notice mailings. Staff has concerns regarding these estimated hours. First, as stated earlier, there should be no hours related to the MFRs or the audit in this case because the Utility has already completed the MFRs and has responded to the audit requests and those associated hours are reflected in the actual hours. Second, in those cases where rate case expense has not been supported by detailed documentation, the Commission's practice has been to disallow some portion or remove all unsupported amounts.[26] Staff believes a reasonable method to estimate WSC employee hours to complete the rate case is to utilize the average monthly hours of WSC employees incurred to date and carry the monthly average forward until the PAA process is complete.

The Utility began to incur charges related to the rate case in August 2010 and submitted an updated rate case expense as of June 9, 2011, which represents a period of ten months. Staff is recommending the appropriate number of hours incurred as of June 9, 2011 is 1,585. Based on

[26] See Order No. PSC-94-0075-FOF-WS, issued January 21, 1994 in Docket No. 921261-WS, In re: Application for a Rate Increase in Lee County by Harbor Utilities Company, Inc.; Order No. PSC-96-0629-FOF-WS, issued May 10, 1996, in Docket No. 950515-WS, In re: Application for staff-assisted rate case in Martin County by Laniger Enterprises of America, Inc.; and Order No. PSC-96-0860-FOF-SU, issued July 2, 1996, in Docket No. 950967-SU, In re: Application for staff-assisted rate case in Highlands County by Fairmount Utilities, the 2nd, Inc. Staff notes that, in all of these cases, the Commission removed the entire unsupported amounts.

1,585 hours incurred over ten months staff calculated the average number of hours worked per month to be 158.5. The anticipated implementation of the rates will occur in September 2011 or four months from June 9, 2011. Staff believes a reasonable estimate for WSC employees to complete the case is 634 hours (158.5 hours per month x 4 months). The Utility reported that 19 WSC In-house employees would incur charges to complete the rate case. The average hourly rate of the WSC in-house employees is $50. Accordingly, staff believes the appropriate amount of rate case expense should be $31,700 ($50 x 634). Therefore, staff recommends that rate case expense be decreased by $9,576 ($41,276 - $31,700).

In Issue 15, staff is recommending that all salary increases be disallowed. In the Utility's rate case expense estimates and incurred charges, LUSI calculates hourly rate increases for WSC employees. To be consistent, staff re-calculated the charges for the WSC in-house employees based on the lowest reported hourly rate in MFR Schedule B-10 for each employee. The result is a reduction of $3,812 due to the removal of the salary increases proposed by the Utility. As such, staff recommends rate case expense be decreased by $3,812. In total, staff recommends that WSC in-house employee charges be reduced by $53,015 ($3,812 + $1,627 + $15,327 + $22,674 + $9,576) for unreasonable and excessive expense. Staff notes that all preceding adjustments to WSC in-house employees fees were calculated using the lowest hourly rates in the MFR schedule.

WSC Travel Expenses

The eighth adjustment addresses WSC travel expenses. In its MFRs, LUSI estimated $3,200 for travel. However, the documentation the Utility provided to support this expense did not demonstrate that this expense was related to this rate case. The time of travel on the receipts and invoices did not correlate to the time during which the informal meeting and the customer meeting took place. Furthermore, based on several previous UI rates cases, it is staff's experience that for PAA rate cases UI does not send a representative from their Illinois office to attend the Agenda Conference. Therefore, staff recommends that rate case expense be decreased by $3,200.

WSC FedEx Expenses

The ninth adjustment relates to WSC expenses for FedEx Corporation (FedEx) and other miscellaneous costs. In its MFRs, the Utility estimated $12,000 for these items. UI has requested and received authorization from the Commission to keep its records outside the state in Illinois. This authorization was made pursuant to Rule 25-30.110(1)(c), F.A.C. However, when a utility receives this authorization, it is required to reimburse the Commission for the reasonable travel expense incurred by each Commission representative during the review and audit of the books and records. Further, these costs are not included in rate case expense or recovered through rates. In a 1993 rate case for Mid-County Service, Inc. (another UI subsidiary), the Commission found the following:

> The Utility also requested recovery of the actual travel costs it paid for the Commission auditors. Because the Utility's books are maintained out of state, the auditors had to travel out of state to perform the audit. We have consistently

> disallowed this cost in rate case expense. See Order No. 25821, issued February 27, 1991, and Order No. 20066, issued September 26, 1988.[27]

Staff believes that the requested amount of shipping costs in this rate case directly relates to the records being retained out of state. The Utility typically ships its MFRs, answers to data and audit requests, and other rate case correspondence to its law firm located in central Florida. The documents are then submitted to the Commission. Staff does not believe that ratepayers should bear the related costs of having LUSI's records located out of state. This is a decision by the management of the Utility, and, thus, the shareholders should bear the related costs. Accordingly, staff recommends that rate case expense be decreased by $12,000.

Customer Notices and Postage

The seventh adjustment relates to WSC expenses for customer notices and postage. The Utility estimated charges of $3,375 for these expenses, but reflected actual charges incurred of $7,720 in its revised Schedule B-10. In 2009 UI rate cases, the Commission has allowed expenses of $0.05 per envelope, $0.34 for postage,[28] and $0.10 per copy. The charges appear to be reasonable based on approximately 8,746 customers to whom notices were mailed. In addition, LUSI did not include costs for customer notices and postage for the final notice. Accordingly, staff recommends rate case expense be increased by $4,294 to account for the cost of mailing the final notice to customers.

Conclusion

It is the Utility's burden to justify its requested costs.[29] Further, the Commission has broad discretion with respect to the allowance of rate case expense. It would constitute an abuse of discretion to automatically award rate case expense without reference to the prudence of the costs incurred in the rate case proceedings.[30] In summary, staff recommends that LUSI's revised rate case expense be decreased by $91,776 for MFR deficiencies and for unsupported and unreasonable rate case expense. The appropriate total rate case expense is $288,327. That amount includes charges for a total of 3,000 hours for all consultants and WSC in-house employees. Staff believes 3,000 hours is reasonable and appropriate based on the 3,219 hours charged in LUSI's 2009 rate case, which was more complex. A breakdown of rate case expense is as follows:

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[27] See Order No. PSC-93-1713-FOF-SU, p. 19., issued November 30, 1993, in Docket No. 921293-SU, In re: Application for a Rate Increase in Pinellas County by Mid-County Services, Inc.
[28] UI has a presorted postage rate of $0.34.
[29] See Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982)
[30] See Meadowbrook Util. Sys., Inc. v. FPSC, 518 So. 2d 326, 327 (Fla. 1st DCA 1987), rev. den., 529 So. 2d 694 (Fla. 1988)

Table 18-2

Description	MFR Estimated	Utility Revised Actual & Estimated	Staff Adjustments	Total
Legal Fees	$66,300	$77,324	($16,454)	$60,869
Accounting Consultant Fees	264,900	96,763	(9,451)	87,312
Engineering Consultant Fees	18,150	31,964	(1,950)	30,014
WSC in-house Fees	76,776	140,925	(53,015)	87,911
Filing Fee	4,000	7,000	0	7,000
Travel- WSC	3,200	3,200	(3,200)	0
Temp Employee Fees-WSC	0	3,207	0	3,207
Miscellaneous	12,000	12,000	(12,000)	0
Notices	3,375	7,720	4,294	12,014
Total Rate Case Expense	$448,701	$380,103	($91,776)	$288,327
Annual Amortization	$112,175	$95,026	($22,944)	$72,082

In its MFRs, LUSI requested total rate case expense of $448,701, which amortized over four years is $112,175. The Utility included a pro forma adjustment of $112,175 in its MFRs for rate case expense, or $84,346 for water and $27,829 for wastewater. Based on the adjustments recommended above, total rate case expense should be decreased by $160,374 (448,701 - $288,327), or $40,093 ($112,175 – $72,082) per year, which equates to a reduction of $30,147 for water and $9,947 for wastewater.

The recommended total rate case expense should be amortized over four years, pursuant to Section 367.0816, F.S. Based on the data provided by LUSI and the recommended adjustments discussed above, staff recommends the appropriate amount of rate case expense is $288,327. This expense should be recovered over four years for an annual expense of $72,082, or $54,199 for water and $17,883 for wastewater. Therefore, annual rate case expense should be reduced by $30,147 for water and $9,947 for wastewater.

Issue 19: How should the net gain on sale of land be treated?

Recommendation: The net gain on sale of land realized by LUSI should be amortized over five years and deducted from the Utility's expenses. The annual amortization should be $13,417 for water and $14,238 for wastewater. (Buys)

Staff Analysis: Staff auditors determined that in 2009, the Utility sold 5 of the 180 acres of land at Lake Groves to Sumter Electric for $244,439 net of closing costs. This amount was recorded in account 7690 (414 NARUC), Gain or Loss from Sale of Property, which is below-the-line and was not included in the rate case filing. It is a longstanding Commission practice to amortize capital gains from the sale of specific assets, such as land, over a five-year period to the benefit of the ratepayers.[31] However, if the sale results in a loss of customers, the gain flows to the shareholders.

In the 2002 rate case for Utilities Inc., of Florida (UIF), the Commission ordered that gains on the sale of facilities to separate municipalities shall be attributable to the shareholders.[32] However, staff believes that LUSI's sale of its land is distinguishable from UIF's gain on sale. First, UIF's sale involved the transfer of all facilities and the customer bases to the separate municipalities. As UIF's witness Gower testified, the remaining UIF customers should not benefit from the sale of a system when the customers who paid for the facilities are now gone.[33] Further, as the Office of Public Counsel's witness Dismukes testified, the Commission has recognized that future profits are lost for systems sold along with the customers of a system, and that the Commission has therefore found it appropriate to assign the gain to shareholders.[34]

LUSI's sale of its land does not result in any revenue stream loss associated with a loss of the Utility's customer base. The sale of land was strictly a sale of real property. Across the rate base-regulated water, wastewater, gas, and electric industries, the Commission has consistently approved the amortization of a gain on sale of property to the benefit of the ratepayers.[35]

[31] See Order Nos. PSC-07-0205-PAA-WS, issued March 6, 2007, in Docket No. 060258-WS, In re: Application for increase in water and wastewater rates in Seminole County by Sanlando Utilities Corp., PSC-04-0947-PAA-SU, issued September 28, 2004, in Docket No. 040733-SU, In re: Disposition of gain on sale of land held for future use in Marion County by BFF Corp.; Order No. PSC-02-1159-PAA-GU, issued August 23, 2002, in Docket No. 020521-GU, In re: Petition for approval to amortize gain on sale of property over five-year period by Florida Public Utilities Company; and Order No. PSC-98-0451-FOF-EI, issued March 30, 1998, in Docket No. 970537-EI, In re: 1997 depreciation study by Florida Public Utilities Company, Marianna Division.

[32] See Order No. PSC-03-1140-FOF-WS, pp. 117-131, issued December 22, 2003, in Docket No. 020071-WS, In re: Application for rate increase in Marion, Orange, Pasco, Pinellas, and Seminole Counties by Utilities, Inc. of Florida.

[33] See Order No. 03-1140-FOF-WS, p. 130.

[34] See Order No. 03-1140-FOF-WS, p. 130.

[35] See Order No. 24225, issued March 12, 1991, in Docket No. 900688-WS, In re: Application for staff-assisted rate case in Pasco County by Betmar Utilities, Inc.; Order No. PSC-04-0947-PAA-SU, issued September 28, 2004, in Docket No. 040733-SU, In re: Disposition of gain on sale of land held for future use in Marion County by BFF Corp.; Order No. PSC-02-1159-PAA-GU, issued August 23, 2002, in Docket No. 020521-GU, In re: Petition for approval to amortize gain on sale of property over five-year period by Florida Public Utilities Company.; and Order No. 970537-EI, issued March 30, 1998, in Docket No. 970537-EI, In re: 1997 depreciation study by Florida Public Utilities Company, Marianna Division.

Staff's calculation of the amortization of the gain on sale and the resulting reduction in expenses is reflected in the following table.

Table 19-1

AMORTIZATION OF GAIN ON SALE CALCULATION	Water	Wastewater	Total
Proceeds net of closing costs	$118,594	$125,845	$244,439
Book basis of land (a)	(11,684)	(12,399)	(24,083)
Pre-tax Gain	$106,909	$113,446	$220,356
Less: Taxes (Composite tax rate of 37.25%)(b)	(39,824)	(42,259)	(82,101)
Net Gain	$67,086	$71,188	$138,255
Five-Year Amortization	($13,417)	($14,238)	($27,651)

(a) As recorded in rate base per staff audit
(b) Per MFR Schedule C-2

Based on the above, staff recommends that the $244,439 net gain on the sale of land realized by LUSI should be amortized over five years and deducted from the Utility's expenses. The annual amortization should be $13,417 for water and $14,238 for wastewater

Issue 20: What is the test year water and wastewater operating income before any revenue increase?

Recommendation: Based on the adjustments discussed in previous issues, the test year operating income is $871,412 for water and $456,309 for wastewater. (Buys)

Staff Analysis: As shown on Schedule Nos. 3-A and 3-B, after applying staff's recommended adjustments, the Utility's net operating income is $871,412 for water and $456,309 for wastewater. Staff's adjustments to operating income are shown on Schedule No. 3-C.

REVENUE REQUIREMENT

Issue 21: What is the appropriate revenue requirement for the historical test year ended June 30, 2010?

Recommendation: The following revenue requirement should be approved. (Buys, Fletcher)

	Test Year Revenues	($ Decrease) $ Increase	Revenue Requirement	(% Decrease) % Increase
Water	$4,308,670	$977,509	$5,286,178	22.69%
Wastewater	$2,101,009	($24,551)	$2,076,458	(1.17%)

Staff Analysis: LUSI's requested revenue requirements should generate annual revenues of $5,840,432 and $1,606,673 for water and wastewater, respectively. These requested revenue requirements represent revenue increases of $1,606,673 or approximately 38 percent for water and $247,262 or approximately 12 percent for wastewater.

Consistent with staff's recommendations concerning the underlying rate base, cost of capital, and operating income issues, staff recommends approval of rates that are designed to generate a water revenue requirement of and a wastewater revenue requirement of $2,076,458. The recommended water revenue requirement exceeds staff's adjusted test year revenues by $977,509, or 22.69 percent, for water. The recommended wastewater revenue requirement is below staff's adjusted test year revenues by $24,551, or 1.17 percent, for wastewater. These recommended pre-repression revenue requirements will allow the Utility the opportunity to recover its expenses and earn an 8.13 percent return on its investment in water and wastewater rate base.

RATE STRUCTURE AND RATES

Issue 22: What are the appropriate numbers of bills, ERCs and consumption for the Utility's water, wastewater and reuse systems for the historical test year ending June 30, 2010?

Recommendation: The appropriate numbers of bills, ERCs and consumption for the Utility's water, wastewater and reuse systems for the historical test year ending June 30, 2010 are shown in Table 22-1 below. (Lingo)

Table 22-1

LAKE UTILITY SERVICES, INC.
STAFF'S RECOMMENDED
TEST YEAR BILLING DETERMINANTS
FOR THE HISTORICAL TEST YEAR ENDING JUNE 30, 2010

Water System		Wastewater System		Reuse System	
Bills	102,813	Bills	33,456	Bills	0
ERCs	111,368	ERCs	37,843.5	ERCs	0
Consumption (kgals)	1,471,056	Consumption (kgals)	254,416	Consump	0

Staff Analysis: According to the Utility's MFRs, there were 102,813 bills, 111,368 ERCs and 1,443,485 kgals associated with the water system, and 33,456 bills, 37,843.5 ERCs and 254,416 kgals associated with the wastewater system during the historical test year ending June 30,2010. The Utility reported no billing determinants associated with its reuse system during the test year.

As discussed in Issues 1 and 5, the Utility submitted a record of customer complaints filed with LUSI during the test year. The majority of these complaints involved meter reading and billing issues. LUSI also received numerous high bill complaints as a result of curb reading, and the Utility found numerous meters that either did not function at all or were under-registering. In response to these complaints, the Utility undertook meter testing and meter replacement programs. The Utility was asked to provide staff with further details of the meter replacement initiative, and its anticipated impact on test year billing determinants. The Utility responded that approximately 10 out of the 100 oldest meters tested had accuracy levels of less than 95 percent, which is below the minimum requirement set by the SJRWMD. These meters were replaced. Furthermore, the function of meter reading is now being serviced in house.[36]

In a conference call held between the parties on January 31, 2011, the Utility offered to provide staff with post-test year data in order to evaluate whether, as a result of the changes the Utility had made with meter reading and meter replacements, there had been a reduction in the EUW. Based on staff's review of 10 months of post test year data, there has been an improvement in the percentage of kgals captured for billing purposes. A comparison of the Utility's post test year kgals billed relative to the number of kgals pumped (yielding the percentage of kgals that are revenue generating) indicated an approximate 1.9 percent increase in

[36] Lake Utility Services, Inc., response to staff's second data request, question no. 3.

the number of kgals pumped that are captured for billing purposes. Therefore, staff believes it is appropriate to increase the water system's test year kgals sold by 1.9 percent to recognize this improvement in billing accuracy on a forward-going basis. This results in an increase in test year consumption of 27,571 kgals, yielding total adjusted water system sales of 1,471,056 kgals.

Staff evaluated the recommended increase in water test year consumption to determine whether a corresponding increase should be made to wastewater system consumption. Based on staff's analysis, the resulting increase in wastewater consumption is immaterial; therefore, no corresponding increase in kgals sold is recommended for the Utility's wastewater system. The Utility had no sales of reuse during the test year; therefore, no adjustments are needed.

Based on the foregoing, the appropriate numbers of bills, ERCs and consumption for the Utility's water, wastewater and reuse systems for the historical test year ending June 30, 2010 are shown in Table 22-1 below.

Table 22-1

**LAKE UTILITY SERVICES, INC.
STAFF'S RECOMMENDED
TEST YEAR BILLING DETERMINANTS
FOR THE HISTORICAL TEST YEAR ENDING JUNE 30, 2010**

Water System		**Wastewater System**		**Reuse System**	
Bills	102,813	Bills	33,456	Bills	0
ERCs	111,368	ERCs	37,843.5	ERCs	0
Consumption (kgals)	1,471,056	Consumption (kgals)	254,416	Consump	0

Issue 23: What are the appropriate rate structures for the Utility's water, wastewater and reuse systems?

Recommendation: The appropriate water system rate structure for the Utility's residential water system is a continuation a three-tiered inclining block rate structure, with usage blocks for monthly usage of: a) 0-5 kgals; b) 5.001-10 kgals; and c) for usage in excess of 10 kgals. The appropriate water system rate structure for the Utility's remaining customer classes is a continuation of the BFC/uniform gallonage charge rate structure. The pre-repression BFC cost recovery percentage should be set at 20 percent.

As discussed in Issue 21, staff recommends a 1.17 percent revenue requirement reduction to the Utility's wastewater system. Staff recommends that this revenue requirement decrease be applied across the board to the Utility's wastewater rates, thereby keeping the wastewater system's current BFC/gallonage charge rate structure intact. The residential customers' billing for monthly consumption should continue to be capped at 10 kgal. The general service gallonage charge should be 1.2 times greater than the corresponding residential gallonage charge. The appropriate rate structure for the Utility's reuse system is a continuation of the BFC/uniform gallonage charge rate structure. (Lingo)

Staff Analysis: In the Utility's last rate case, due to very high average residential consumption per month, the Commission implemented an aggressive three-tiered inclining block rate structure for the residential water customers, with usage blocks for monthly consumption of a) 0-5 kgal; b) 5.001-10 kgal; and c) greater than 10 kgal. The BFC cost recovery was set at 20 percent. An analysis of the Utility's residential test year billing data in the instant proceeding indicates that, despite reductions in residential customers' average monthly consumption, there continues to be greater than average usage by its residential customers. For example, less than 20 percent of the residential kgals billed are at consumption levels of 5 kgal or less, and approximately 50 percent of the kgals billed are at consumption levels of 10 kgal or less. In addition, the average residential consumption per month remains high, at approximately 13.9 kgal per month. Therefore, staff recommends that the current water system rate structure remain in place. The Utility's current water system rate structure, along with staff's recommended rate structure and two alternative rate structures, are shown on Table 23-1 on the following page.

Table 23-1

LAKE UTILITY SERVICES, INC.
STAFF'S RECOMMENDED AND ALTERNATIVE RATE STRUCTURES
FOR THE WATER SYSTEM'S RESIDENTIAL CUSTOMERS
POST-REPRESSION ANALYSIS

Rate Structure and Rates at End of Test Year
Three-tiered inclining block rate structure
Usage blocks of: 0-5 kgal, 5.001-10 kgal, 10+ kgals
BFC = 20 percent

BFC for 5/8" x 3/4" meter	$8.36
0-5 kgals	$1.69
5.001-10 kgals	$2.12
10+ kgals	$2.54
Typical Monthly Bills	
Cons (kgal)	
0	$8.36
5	$16.81
10	$27.41
15	$40.11
20	$52.81
25	$65.51

Recommended Rate Structure and Rates
Three-tiered inclining block rate structure
Usage blocks of: 0-5 kgal, 5.001-10 kgal, 10+ kgals
BFC = 20 percent

BFC for 5/8" x 3/4" meter	$9.25
0-5 kgals	$2.26
5.001-10 kgals	$2.55
10+ kgals	$3.82
Typical Monthly Bills	
Cons (kgal)	
0	$9.25
5	$20.53
10	$33.25
15	$52.34
20	$71.43
25	$90.53

Alternative 1
Three-tiered inclining block rate structure
Usage blocks of: 0-5 kgal, 5.001-10 kgal, 10+ kgals
BFC = 25 percent

BFC for 5/8" x 3/4" meter	$11.57
0-5 kgals	$1.76
5.001-10 kgals	$1.98
10+ kgals	$3.96
Typical Monthly Bills	
Cons (kgal)	
0	$11.57
5	$20.37
10	$30.27
15	$50.08
20	$69.89
25	$89.69

Alternative 2
Three-tiered inclining block rate structure
Usage blocks of: 0-5 kgal, 5.001-10 kgal, 10+ kgals
BFC = 30 percent

BFC for 5/8" x 3/4" meter	$13.89
0-5 kgals	$1.97
5.001-10 kgals	$2.18
10+ kgals	$3.26
Typical Monthly Bills	
Cons (kgal)	
0	$13.89
5	$23.76
10	$34.63
15	$50.95
20	$67.27
25	$83.58

Staff believes the recommended rate structure accomplishes two things. First, the prices are reduced at lower, nondiscretionary levels of consumption. This avoids penalizing those customers whose usage is essential in nature. Second, since customers are sent more aggressive price signals at greater consumption levels, a greater level of conservation can be achieved.

As discussed in Issue 21, staff is recommending a revenue decrease to the Utility's wastewater system. Therefore, staff does not believe a change in rate structure is appropriate. The Utility's reuse rates were set in the Utility's last rate proceeding, but no reuse kgals have been sold. Therefore, staff recommends no change to the reuse system rate structure at this time.

Therefore, the appropriate water system rate structure for the Utility's residential water system is a continuation a three-tiered inclining block rate structure, with usage blocks for monthly usage of: a) 0-5 kgals; b) 5.001-10 kgals; and c) for usage in excess of 10 kgals. The appropriate water system rate structure for the Utility's remaining customer classes is a continuation of the BFC/uniform gallonage charge rate structure. The pre-repression BFC cost recovery percentage should be set at 20 percent.

As discussed in Issue 21, staff recommends a 1.17 percent revenue requirement reduction to the Utility's wastewater system. Staff recommends that this revenue requirement decrease be applied across the board to the Utility's wastewater rates, thereby keeping the wastewater system's current BFC/gallonage charge rate structure intact. The residential customers' billing for monthly consumption should continue to be capped at 10 kgal. The general service gallonage charge should be 1.2 times greater than the corresponding residential gallonage charge. The appropriate rate structure for the Utility's reuse system is a continuation of the BFC/uniform gallonage charge rate structure.

Issue 24: Are repression adjustments appropriate for the Utility's water and wastewater systems, and, if so, what are the appropriate adjustments for the respective systems?

Recommendation: A repression adjustment is appropriate for the water system only. Residential water consumption should be reduced by 8.7 percent, resulting in a consumption reduction of approximately 122,361 kgals. Total water consumption for ratesetting is 1,348,695 kgals, which represents an 8.3 percent reduction in overall consumption. The resulting water system reductions to revenue requirements are $32,874 in purchased power expense, $11,635 in chemicals expense, and $2,097 in regulatory assessment fees (RAFs). The post-repression revenue requirement for the water system is $5,148,630. As discussed in Issue 21, staff recommends a revenue requirement reduction to the wastewater system. Therefore, no repression adjustment is recommended for that system.

In order to monitor the effect of the rate change, the Utility should be ordered to file reports for its respective water and wastewater systems, detailing the number of bills rendered, the consumption billed and the revenues billed on a monthly basis. In addition, the reports should be prepared by customer class, usage block and meter size. The reports should be filed with staff, on a semi-annual basis, for a period of two years beginning with the first billing period after the approved rates go into effect. To the extent the Utility makes adjustments to consumption in any month during the reporting period, the Utility should be ordered to file a revised monthly report for that month within 30 days of any revision. (Lingo)

Staff Analysis: A repression adjustment quantifies changes in consumption patterns in response to an increase in prices. Customers will typically reduce their non-essential consumption (i.e. outdoor irrigation, etc.) in response to price changes, while essential consumption (i.e. indoor uses such as cooking, cleaning, drinking, bathing, etc.) remains relatively unresponsive to price changes.

As discussed in Issue 23, less than 20 percent of the residential kgals billed are at consumption levels of 5 kgal or less, and approximately 50 percent of the kgals billed are at consumption levels of 10 kgal or less. In addition, the average residential consumption per month remains high, at approximately 13.9 kgal per month. This represents a high degree of non-essential consumption that should be responsive to changes in price.

Therefore, staff recommends that a repression adjustment for the water system is appropriate in this case. Based on staff's analysis and the application of staff's recommended water system rate structure for the residential class, residential water consumption should be reduced by 8.7 percent. The resulting consumption reduction is approximately 122,361 kgals. Total water consumption for ratesetting is 1,348,695 kgals, which represents an 8.3 percent reduction in overall consumption. The resulting water system reductions to revenue requirements are $32,874 in purchased power expense, $11,635 in chemicals expense, and $2,097 in RAFs. The post-repression revenue requirement for the water system is $5,148,630. As discussed in Issue 21, staff recommends a revenue requirement reduction to the wastewater system. Therefore, no repression adjustment is recommended for that system.

In order to monitor the effect of the rate changes, the Utility should be ordered to file reports detailing the number of bills rendered, the consumption billed and the revenues billed on a monthly basis. In addition, the reports should be prepared by customer class and meter size. The reports should be filed with staff, on a semi-annual basis, for a period of two years beginning with the first billing period after the approved rates go into effect. To the extent the Utility makes adjustments to consumption in any month during the reporting period, the Utility should be ordered to file a revised monthly report for that month within 30 days of any revision.

Issue 25: What are the appropriate rates for the Utility's water, wastewater and reuse systems?

Recommendation: The appropriate monthly water rates are shown on Schedule 4-A, and the appropriate monthly wastewater and reuse rates are shown on Schedule 4-B. Excluding miscellaneous service charges, and after the effects of repression, the recommended water rates produce revenues of $5,148,630. After staff's recommended revenue requirement decrease and excluding miscellaneous service charges, the recommended wastewater rates produce revenues of $2,064,513. The Utility should file revised water and wastewater tariff sheets and a proposed customer notice to reflect the Commission-approved rates for the respective systems. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved rates should not be implemented until staff has approved the proposed customer notice. The Utility should provide proof of the date notice was given no less than ten days after the date of the notice. (Lingo, Buys, Fletcher)

Staff Analysis: The appropriate water system revenue requirement, excluding miscellaneous service charges, is $5,195,235. As discussed in Issue 23, staff recommends that the appropriate rate structure for the residential customer class is the continuation of the three-tiered inclining block rate structure, with usage blocks for monthly consumption of: a) 0-5 kgals; b) 5.001-10 kgals; and c) usage in excess of 10 kgals. Staff recommends that the traditional BFC/uniform kgal charge rate structure be applied to the Utility's remaining water system customer classes. The BFC cost recovery percentage for the water system should be set at 20 percent. As discussed in Issue 24, staff recommends that a repression adjustment reduction of 122,361 kgals be made. Applying these recommendations results in the final rates contained in Schedule 4-A. These rates are designed to recover annual revenues, excluding miscellaneous service charges, of $5,148,630.

The appropriate wastewater system revenue requirement, after staff's recommended reduction and excluding miscellaneous service charges, is $2,064,513. As discussed in Issue 23, staff recommends that the appropriate rate structure is a continuation of the Utility's current traditional BFC/kgal charge rate structure for all classes. As discussed in Issue 24, staff recommends that no repression adjustment be made. Applying these recommendations results in the final rates contained in Schedule 4-B. These rates are designed to recover annual revenues, excluding miscellaneous service charges, of $2,064,513. Staff recommends no change to the Utility's current reuse rate structure or rates.

The Utility should file revised water and wastewater tariff sheets and a proposed customer notice to reflect the Commission-approved rates for the respective systems. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved rates should not be implemented until staff has approved the proposed customer notice. The Utility should provide proof of the date notice was given no less than 10 days after the date of the notice.

OTHER ISSUES

Issue 26: Should the Utility be authorized to revise its water service availability charges, and if so, what are the appropriate charges?

Recommendation: Yes. LUSI's water service availability charges should be revised. The recommended charges are reasonable and consistent with the guidelines set forth in Rule 25-30.580, F.A.C., and should be approved. The approved charges should be effective for service rendered on or after the stamped approval date of the tariff, pursuant to Rule 25-30.475, F.A.C. The appropriate revised water service availability charges are reflected below.

Main Extension Charge	$1,426
Plant Capacity Charge	$1,157
Meter Installation Charges:	
5/8" x 3/4"	$150
1"	$250

(Buys)

Staff Analysis: LUSI requested to revise its water service availability charges to increase the main extension charge from $270 to $800, and the plant capacity charge from $270 to $1,783. For Lake Groves, the Utility is requesting to increase the main extension charge from "negotiable" to $800, and the plant capacity charge from $707 to $1,783. In addition, for Lake Groves, LUSI is requesting to increase its meter installation charges for a 5/8" x 3/4" meter from $67 to $150, and for a 1" meter from $114 to $250, so that the charges mirror the present meter installation charges of the other LUSI systems. Service availability charges for water were last approved for LUSI on May 15, 1999. Rule 25-30.580, F.A.C., establishes guidelines for designing service availability policy. Pursuant to the rule, the maximum amount of contributions-in-aid-of-construction (CIAC), net of amortization, should not exceed 75 percent 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. The minimum amount of CIAC 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.

Main Extension Charge

The main extension charge is used to pay for the original cost of the water transmission and distribution plant. In the instant case, LUSI's service availability policy requires that additional customers contribute property or donate lines to pay for the cost of the water transmission and distribution plant. However, the main extension charge would allow the Utility to collect the appropriate CIAC from a single property owner in lieu of donating lines in addition to developers who may be installing and donating lines.

In its filing, the Utility listed $18,227,478 for the original cost of the water transmission and distribution plant. This amount represents the minimum amount of CIAC that should be included in total plant. Hence, according to Rule 25-30.580, F.A.C., the main extension charge should be designed to collect $18,227,478. Although the total amount of LUSI's proposed service availability charges fall within the guidelines set forth in Rule 25-30.580, F.A.C., staff believes the charges should be designed so that the total amount of the original cost of the transmission and distribution plant is allocated to the main extension charge. This cost should be equally allocated to all ERCs. Using a methodology staff believes to be reasonable, LUSI determined that the water plant has a design capacity of 12,781 ERCs. As such, staff believes the appropriate main extension charge should be $1,426 per ERC ($18,227,478 ÷ 12,781). The recommended main extension charge of $1,426 is consistent with the guidelines in Rule 25-30.580, F.A.C., which require at a minimum the cost of the lines should be contributed.

Plant Capacity Charge

The remainder of the CIAC received by the Utility should be obtained through the plant capacity charge. The balance of CIAC for all of the water plant in service as of June 30, 2010, is $17,040,299. LUSI's proposed service availability charges (both main extension and plant capacity charges) are projected to collect approximately $9,032,750 in additional CIAC through December 31, 2023, which will increase the total amount of CIAC to $26,073,050. The total amount of CIAC, less projected amortization of $13,251,450, is 12,821,600 or 69 percent of the total original cost, less accumulated depreciation, of the Utility's water facilities and plant at its designed capacity. The total amount of revised service availability charges requested by LUSI is $2,583 per ERC. Staff is recommending a main extension charge of $1,426 per ERC. Therefore, the plant capacity charge should be the difference between the total amount of CIAC and the main extension charge, or $1,157 ($2,583 - $1,426). The recommended plant capacity charge of $1,157 is consistent with the guidelines in Rule 25-30.580, F.A.C.

Meter Installation Charges

LUSI is requesting to increase the meter installation charge in Lake Groves for a 5/8" x 3/4" meter from $67 to $150, and for a 1" meter from $114 to $250. Current meter installation charges in the other LUSI systems are $150 for a 5/8" x 3/4" meter and $250 for a 1" meter. The Utility is requesting an increase for only Lake Groves so that the charges mirror the meter installation charges of the other LUSI systems. Staff believes the meter installation charges are reasonable and should be approved.

Conclusion

Staff recommends that the Commission authorize the Utility to revise its water service availability charges. The recommended charges are reasonable and consistent with the guidelines set forth in Rule 25-30.580, F.A.C., and should be approved. The approved charges should be effective for service rendered on or after the stamped approval date of the tariff, pursuant to Rule 25-30.475, F.A.C. The appropriate revised water service availability charges are reflected below.

Table 26-1

Type of Charge	Current	Requested	Recommended
Main Extension Charge	$270	$800	$1,426
Plant Capacity Charge	$270	$1,783	$1,157
Lake Groves Meter Installation			
5/8" x 3/4"	$67	$150	$150
1"	$114	$250	$250

Issue 27: Should the Utility's wastewater service availability charges be revised, and if so, what are the appropriate charges?

Recommendation: Yes. LUSI's wastewater service availability charges should be revised. The recommended charges are reasonable and consistent with the guidelines set forth in Rule 25-30.580, F.A.C., and should be approved. The approved charges should be effective for service rendered on or after the stamped approval date of the tariff, pursuant to Rule 25-30.475, F.A.C. The appropriate revised wastewater service availability charges are reflected below.

Main Extension Charge	$1,243
Plant Capacity Charge	$558

(Buys)

Staff Analysis: In its filing, LUSI did not request to revise its wastewater service availability charges. The Utility's current wastewater service availability charges are set at a negotiable rate for the main extension charge and $558 for the plant capacity charge. Staff believes that the Utility's wastewater main extension charge should be revised to include a dollar amount of $1,243. Rule 25-30.580, F.A.C., establishes guidelines for designing service availability policy. Pursuant to the rule, the maximum amount of CIAC, net of amortization, should not exceed 75 percent 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. The minimum amount of CIAC 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. The main extension charge is used to pay for the original cost of the wastewater sewer collection system. According to LUSI's wastewater service availability policy, the sewer collection system is installed by the developer and contributed to the Utility. However, a main extension charge would allow the Utility to collect the appropriate CIAC from a single property owner in lieu of donating lines in addition to developers who may be installing and donating sewer collection lines.

Main Extension Charge

In response to a staff data request, LUSI provided the necessary information to calculate the appropriate wastewater main extension charge. The Utility listed $5,242,654 for the original cost of the sewer collection system. The majority of this amount was contributed by the developer. This amount represents the minimum amount of CIAC that should be included in total plant. Hence, according to the guidelines in Rule 25-30.580, F.A.C., the main extension charge should be designed to collect $5,242,654. This cost should be equally allocated to all ERCs. Using a methodology staff believes to be reasonable, LUSI determined that the wastewater plant has a design capacity of 4,217 ERCs. As such, staff believes the appropriate wastewater main extension charge should be $1,243 per ERC ($5,242,654 ÷ 4,217). The recommended main extension charge of $1,243 is consistent with the guidelines in Rule 25-30.580, F.A.C., which require at a minimum the cost of the lines should be contributed.

Plant Capacity Charge

The remainder of the CIAC received by the Utility should be obtained through the plant capacity charge. LUSI's wastewater plant capacity charge is currently $558. Staff is recommending no change to the plant capacity charge. The recommended wastewater service availability charges (both main extension and plant capacity charges) are projected to collect approximately $1,916,497 in additional CIAC through October 30, 2021, which will increase the total amount of CIAC to $12,856,179. The total amount of the wastewater service availability charges recommended by staff is $1,801 per ERC. The total amount of CIAC, less projected amortization of $8,731,071, is $4,125,108 or 70 percent of the total original cost, less accumulated depreciation, of the Utility's wastewater facilities and plant at its designed capacity. The current wastewater plant capacity charge of $558 is consistent with the guidelines in Rule 25-30.580, F.A.C.

Conclusion

Staff recommends that the Commission revise LUSI's wastewater service availability charges. The recommended charges are reasonable and consistent with the guidelines set forth in Rule 25-30.580, F.A.C., and should be approved. The approved charges should be effective for service rendered on or after the stamped approval date of the tariff, pursuant to Rule 25-30.475, F.A.C. The appropriate revised water service availability charges are reflected below.

Table 27-1

Type of Charge	Current	Recommended
Main Extension Charge	Negotiable	$1,243
Plant Capacity Charge	$558	$558

Issue 28: In determining whether any portion of the interim water revenue increase granted should be refunded, how should the refund be calculated, and what is the amount of the refund, if any?

Recommendation: The proper refund amount should be calculated by using the same data used to establish final rates, excluding rate case expense and other items not in effect during the interim period. This revised water revenue requirement for the interim collection period should be compared to the amount of interim water revenue requirement granted. This results in a refund of 6.10 percent. The refunds should be made with interest in accordance with Rule 25-30.360(4), F.A.C. The Utility should be required to submit proper refund reports pursuant to Rule 25-30.360(7), F.A.C. The Utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C. Further, the corporate undertaking should be released upon staff's verification that the required refunds have been made. (Buys)

Staff Analysis: By Order No. PSC-11-0149-PCO-WU,[37] the Commission authorized the collection of interim water rates, subject to refund, pursuant to Section 367.082, F.S. The approved interim water revenue requirement was $5,502,978, which represented an increase in annual water revenue of $1,332,875 or approximately 32 percent. This interim increase was effective for service rendered after March 6, 2011, and was protected by a corporate undertaking.

According to Section 367.082, F.S., any refund should be calculated to reduce the rate of return of the Utility during the pendency of the proceeding to the same level within the range of the newly authorized rate of return. Adjustments made in the rate case test period that do not relate to the period interim rates are in effect should be removed. Rate case expense is an example of an adjustment which is recovered only after final rates are established.

In this proceeding, the test period for establishment of interim and final rates is the 12-month period ended June 30, 2010. LUSI's approved interim water rates did not include any provisions for pro forma or projected operating expenses or plant. The interim increase was designed to allow recovery of actual interest costs, and the floor of the last authorized range of return on equity.

To establish the proper refund amount, staff has calculated a revised interim revenue requirement utilizing the same data used to establish final rates. Rate case expense was excluded because this item is prospective in nature and did not occur during the interim collection period.

Using the principles discussed above, the $5,502,978 revenue requirement granted in Order No. PSC-11-0149-PCO-WU for the interim test year is greater than the revised revenue requirement for the interim collection period of $5,164,184. This results in a refund of 6.10 percent. The refund should be made with interest in accordance with Rule 25-30.360(4), F.A.C. The Utility should be required to submit proper refund reports pursuant to Rule 25-30.360(7), F.A.C. The Utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C.

[37] See Order No. PSC-11-0149-PCO-WU.

Issue 29: What is the appropriate amount by which rates should be reduced four years after the established effective date to reflect the removal of the amortized rate case expense as required by Section 367.0816, Florida Statutes?

Recommendation: The rates should be reduced as shown on Schedule Nos. 4-A and 4-B to remove $131,221 for water and $43,296 for wastewater related the annual rate case expense, grossed-up for RAFs, which is being amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the four-year rate case expense recovery period, pursuant to Section 367.0816, F.S. The Utility should be required to file revised tariffs and a proposed customer notice setting forth the lower rates and the reason for the reduction no later than one month prior to the actual date of the required rate reduction. (Buys)

Staff Analysis: Section 367.0816, F.S., requires rates to be reduced immediately following the expiration of the four-year amortization period by the amount of the rate case expense previously included in the rates. The reduction will reflect the removal of revenues associated with the amortization of rate case expense, the associated return included in working capital, and the gross-up for RAFs, which is $131,221 for water and $43,296 for wastewater. The decreased revenue will result in the rate reduction recommended by staff on Schedule Nos. 4-A and 4-B.

The Utility should be required to file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice. LUSI should provide proof of the date notice was given within 10 days after the date of the notice.

If the Utility files this reduction in conjunction with a price index or pass-through rate adjustment, separate data should be filed for the price index and/or pass-through increase or decrease, and for the reduction in the rates due to the amortized rate case expense.

Issue 30: Should the Utility be required to provide proof, within 90 days of an effective order finalizing this docket, that it has adjusted its books for all the applicable National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts (USOA) primary accounts associated with the Commission approved adjustments?

Recommendation: Yes. To ensure that the Utility adjusts its books in accordance with the Commission's decision, LUSI should provide proof, within 90 days of the final order in this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made. (Buys)

Staff Analysis: To ensure that the Utility adjusts its books in accordance with the Commission's decision, LUSI should provide proof, within 90 days of the final order in this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made.

Issue 31: Should this docket be closed?

Recommendation: No. If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the Utility and approved by staff, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively. (Young, Buys)

Staff Analysis: If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the Utility and approved by staff, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively.

	Lake Utility Services, Inc. Schedule of Water Rate Base Test Year Ended 6/30/10				Schedule No. 1-A Docket No. 100426-WS	
	Description	**Test Year Per Utility**	**Utility Adjust-ments**	**Adjusted Test Year Per Utility**	**Staff Adjust-ments**	**Staff Adjusted Test Year**
1	Plant in Service	$43,784,217	($7,354,922)	$36,429,295	($389,095)	$36,040,200
2	Land and Land Rights	117,081	(975)	116,106	0	116,106
3	Construction Work in Progress	636,275	(636,275)	0	0	0
4	Accumulated Depreciation	(6,457,866)	410,111	(6,047,755)	387,716	(5,660,039)
5	CIAC	(17,058,144)	17,845	(17,040,299)	(10,646)	(17,050,945)
6	Amortization of CIAC	3,866,668	(3,151)	3,863,517	104	3,863,621
7	Working Capital Allowance	0	819,746	819,746	(246,262)	573,484
8	Rate Base	$24,888,231	($6,747,621)	$18,140,610	($258,184)	$17,882,426

Lake Utility Services, Inc.
Schedule of Wastewater Rate Base
Test Year Ended 6/30/2010

Schedule No. 1-B
Docket No. 100426-WS

	Description	Test Year Per Utility	Utility Adjust-ments	Adjusted Test Year Per Utility	Staff Adjust-ments	Staff Adjusted Test Year
1	Plant in Service	$13,650,545	$4,438,937	$18,089,482	($110,577)	$17,978,905
2	Land and Land Rights	397,641	(371,396)	26,245	0	26,245
3	Non-used and Useful Components	0	(343,626)	(343,626)	(685,825)	(1,029,451)
4	Accumulated Depreciation	(2,707,904)	(133,904)	(2,841,808)	42,121	(2,799,687)
5	CIAC	(10,894,397)	(45,285)	(10,939,682)	32,579	(10,907,103)
6	Amortization of CIAC	1,767,524	194,418	1,961,942	(2,402)	1,959,540
7	CWIP	(398,327)	398,327	0	0	0
8	Advances for Construction	(38,400)	38,400	0	0	0
9	Working Capital Allowance	0	270,487	270,487	(65,429)	205,058
10	Rate Base	$1,776,682	$4,446,358	$6,223,040	($789,533)	$5,433,507

	Lake Utility Services, Inc. Adjustments to Rate Base Test Year Ended 6/30/10	Schedule No. 1-C Docket No. 100426-WS	
	Explanation	**Water**	**Wastewater**
	Plant In Service		
1	Audit Finding No. 1 - Expenses recorded as plant. (Issue 2)	($8,709)	($19,175)
2	Audit Finding No. 2 - Reflect plant retirements. (Issue 2)	(123,772)	(24,150)
3	Audit Finding No. 5 - Correct plant error. (Issue 2)	219	0
4	Audit Finding No. 13 - Capital projects expensed. (Issue 2)	236	0
5	Affiliated Audit Finding No. 1 - (Issue 2)	(171)	(56)
6	Affiliated Audit Finding No. 2 - Phoenix Project (Issue 3)	(56,028)	(18,487)
7	Affiliated Audit Finding No. 7 - Capitalized salaries. (Issue 2)	(25,662)	(8,468)
8	Reflect appropriate amount for Phoenix Project. (Issue 3)	(136,198)	(44,940)
9	Reflect appropriate pro forma plant items. (Issue 4)	(39,011)	4,698
	Total	($389,095)	($110,577)
	Non-used and Useful		
	To reflect net non-used and useful adjustment. (Issue 6)	$0	($685,825)
	Accumulated Depreciation		
1	Audit Finding No. 1 - Expenses recorded as plant. (Issue 2)	$658	$1,034
2	Audit Finding No. 2 - Reflect plant retirements. (Issue 2)	129,035	25,581
3	Audit Finding No. 6 - Correct accum. depr. error. (Issue 2)	170,515	0
4	Audit Finding No. 13 - Capital projects expensed. (Issue 2)	705	0
5	Affiliated Audit Finding No. 1 - Expenses recorded as plant. (Issue 2)	8	3
6	Affiliated Audit Finding No. 7 - Capitalized salaries. (Issue 2)	695	227
7	Affiliated Audit Finding No. 2 - Phoenix Project Adjustment. (Issue 3)	5,603	1,849
8	Affiliated Audit Finding No. 3 - Depreciation of Phoenix Project. (Issue 3)	27,867	9,194
9	Adjust Phoenix Project for 2010 Divestures. (Issue 3)	13,620	4,494
10	Reflect appropriate pro forma accumulated depreciation. (Issue 4)	39,011	(261)
	Total	$387,716	$42,121
	CIAC		
	Audit Finding No. 7 – Correct Utility errors in CIAC (Issue 2)	($10,646)	$32,579
	Accumulated Amortization of CIAC		
	Audit Finding No. 7 - Correct Utility errors in CIAC amort. (Issue 2)	$104	($2,402)
	Working Capital		
1	Average Deferred Rate Case Expense. (Issue 7)	($198,290)	($65,429)
2	Appropriate Miscellaneous Deferred Debits. (Issue 8)	(47,972)	0
	Total	($246,262)	($65,429)

Lake Utility Services, Inc.
Capital Structure-Simple Average
Test Year Ended 6/30/10

Schedule No. 2
Docket No. 100426-WS

	Description	Total Capital	Specific Adjust-ments	Subtotal Adjusted Capital	Pro rata Adjust-ments	Capital Reconciled to Rate Base	Ratio	Cost Rate	Weighted Cost
Per Utility									
1	Long-term Debt	$180,000,000	$0	$180,000,000	($168,398,745)	$11,601,255	47.62%	6.65%	3.17%
2	Short-term Debt	29,629,231	0	29,629,231	(27,718,578)	1,910,653	7.84%	4.28%	0.34%
3	Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%
4	Common Equity	164,142,503	0	164,142,503	(153,560,424)	10,582,079	43.43%	10.55%	4.58%
5	Customer Deposits	111,811	0	111,811	0	111,811	0.46%	6.00%	0.03%
6	Deferred Income Taxes	157,852	0	157,852	0	157,852	0.65%	0.00%	0.00%
7	**Total Capital**	$374,041,397	$0	$374,041,397	($349,677,747)	$24,363,650	100.00%		8.12%
Per Staff									
8	Long-term Debt	$180,000,000	$0	$180,000,000	($168,856,664)	$11,143,336	47.60%	6.65%	3.17%
9	Short-term Debt	29,629,231	0	29,629,231	(27,794,962)	1,834,269	7.84%	3.17%	0.25%
10	Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%
11	Common Equity	164,142,503	0	164,142,503	(153,980,864)	10,161,639	43.41%	10.80%	4.69%
12	Customer Deposits	111,811	0	111,811	0	111,811	0.48%	6.00%	0.03%
13	Deferred Income Taxes	157,852	0	157,852	0	157,852	0.67%	0.00%	0.00%
14	**Total Capital**	$374,041,397	$0	$374,041,397	($350,632,489)	$23,408,908	100.00%		8.13%

	LOW	HIGH
RETURN ON EQUITY	9.80%	11.80%
OVERALL RATE OF RETURN	7.70%	8.56%

Lake Utility Services, Inc.
Statement of Water Operations
Test Year Ended 6/30/10

Schedule No. 3-A
Docket No. 100426-WS

	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:**	$4,185,151	$1,655,281	$5,840,432	($1,531,762)	$4,308,670	$977,509	$5,286,178
							22.69%	
	Operating Expenses							
2	Operation & Maintenance	$2,583,569	($176,677)	$2,406,892	($402,471)	$2,004,421		$2,004,421
3	Depreciation	705,108	79,473	784,581	(44,947)	739,634		739,634
4	Amortization	0	0	0	(13,417)	(13,417)		(13,417)
5	Taxes Other Than Income	845,645	(172,199)	673,446	(121,153)	552,293	43,988	596,281
6	Income Taxes	(7,906)	510,336	502,430	(348,103)	154,327	351,284	505,611
7	**Total Operating Expense**	$4,126,416	$240,933	$4,367,349	($930,091)	$3,437,258	$395,272	$3,832,529
8	**Operating Income**	$58,735	$1,414,348	$1,473,083	($601,671)	$871,412	$582,237	$1,453,649
9	**Rate Base**	$24,888,231		$18,140,610		$17,882,426		$17,882,426
10	**Rate of Return**	0.24%		8.12%		4.87%		8.13%

	Lake Utility Services, Inc. Statement of Wastewater Operations Test Year Ended 6/30/10							Schedule No. 3-B Docket No. 100426-WS
	Description	**Test Year Per Utility**	**Utility Adjust-ments**	**Adjusted Test Year Per Utility**	**Staff Adjust-ments**	**Staff Adjusted Test Year**	**Revenue Decrease**	**Revenue Requirement**
1	**Operating Revenues:**	$2,059,060	$285,166	$2,344,226	($243,217)	$2,101,009	($24,551) -1.17%	$2,076,458
	Operating Expenses							
2	Operation & Maintenance	$358,331	$545,880	$904,211	($132,443)	$771,768		$771,768
3	Depreciation	617,123	(76,277)	540,846	(63,583)	477,263		477,263
4	Amortization	0	0	0	(14,238)	(14,238)		(14,238)
5	Taxes Other Than Income	0	221,481	221,481	25,975	247,456	(1,105)	246,351
6	Income Taxes	(2,609)	174,974	172,365	(9,914)	162,451	(8,823)	153,628
7	**Total Operating Expense**	$972,845	$866,058	$1,838,903	($194,203)	$1,644,700	($9,928)	$1,634,772
8	**Operating Income**	$1,086,215	($580,892)	$505,323	($49,014)	$456,309	($14,624)	$441,686
9	**Rate Base**	$1,776,682		$6,223,040		$5,433,507		$5,433,507
10	**Rate of Return**	61.14%		8.12%		8.40%		8.13%

	Lake Utility Services, Inc. Adjustment to Operating Income Test Year Ended 6/30/10	Schedule No. 3-C Docket No. 100426-WS	
	Explanation	**Water**	**Wastewater**
	Operating Revenues		
1	Remove requested final revenue increase.	($1,606,673)	($247,262)
2	Audit Finding No. 10 - Correct misclassification of revenues (Issue 2)	1,946	0
3	Income from Utility Plant Leased to Others (Issue 13)	12,261	4,045
4	Revenue adjustment for improved metering accuracy (Issue 13)	60,704	0
	Total	($1,531,762)	($243,217)
	Operation and Maintenance Expense		
1	Audit Finding No . 11 - Remove non-recurring (Issue 2)	($8,733)	($1,698)
2	Audit Finding No. 12 - Prior Commission-ordered adjustment (Issue 2)	(104,984)	(62,290)
3	Audit Finding No. 13 - Reclassify plant items (Issue 2)	(2,450)	0
4	Audit Finding No. 14 - Remove all lobbying expenses (Issue 2)	(654)	(103)
5	Affiliated Audit Finding No. 4 - Prepaid - Other Expenses. (Issue 2)	(3,930)	(1,297)
6	Affiliated Audit Finding No. 9 - Removal of Operating Expenses. (Issue 2)	(3,629)	(1,197)
7	Reflect appropriate amortization of CUP expenses. (Issue 14)	(47,972)	0
8	Reflect appropriate O&M expenses due to EUW adjustment (Issue 5)	(30,604)	0
9	Reflect appropriate salaries. (Issue 15)	(62,658)	(20,674)
10	Reflect appropriate pension & benefits. (Issue 15)	(68,429)	(22,577)
11	Reflect appropriate amount for D&O liability insurance (Issue 16)	(1,828)	(603)
12	Reflect appropriate amount of bad debt expense. (Issue 17)	(36,454)	(12,058)
13	Reflect appropriate amount of rate case expense. (Issue 18)	(30,147)	(9,947)
	Total	($402,471)	($132,443)
	Depreciation Expense - Net		
1	Audit Finding No. 1 - Expenses recorded as plant. (Issue 2)	($442)	($1,048)
2	Audit Finding No. 2 - Reflect plant retirements. (Issue 2)	(4,435)	(1,389)
3	Audit Finding No. 7 - Correct Utility errors in CIAC amort. (Issue 2)	288	(1,134)
4	Audit Finding No. 13 - Capital projects expensed. (Issue 2)	6	0
5	Affiliated Audit Finding No. 1 - Expenses recorded as plant. (Issue 2)	(16)	(5)
6	Affiliated Audit Finding No. 7 - Capitalized salaries. (Issue 2)	(1,390)	(455)
7	Affiliated Audit Finding No. 2 - Phoenix Project Adjustment. (Issue 3)	(5,603)	(1,849)
8	Affiliated Audit Finding No. 3 - Depreciation of Phoenix Project. (Issue 3)	(18,829)	(6,213)
9	Adjust Phoenix Project for 2010 Divestures. (Issue 3)	(13,620)	(4,494)
10	Reflect appropriate pro forma depreciation expense. (Issue 4)	(907)	261
11	Remove net depreciation on non-U&U adjustment above. (Issue 6)	0	(47,256)
	Total	($44,947)	($63,583)
	Amortization-Other Expense		
	Reflect gain of sale of land. (Issue 19)	($13,417)	($14,238)
	Taxes Other Than Income		
1	RAFs on revenue adjustments above.	($68,372)	($10,945)
2	Audit Finding No. 15 - Allocation of Personal Property. (Issue 2)	(45,551)	45,551
3	Reflect appropriate pro forma property taxes. (Issue 4)	(589)	4
4	To remove non-U&U property taxes. (Issue 6)	0	(6,616)
5	Reflect appropriate payroll taxes. (Issue 15)	(6,084)	(2,007)
	Total	($120,595)	$25,987

Lake Utility Services, Inc. | **Schedule No. 4-A**
Water Monthly Service Rates | **Docket No. 100426-WS**
Test Year Ended 6/30/10

	Rates Prior to Filing	Commission Approved Interim	Utility Requested Final	Staff Recomm. Final	4-Year Rate Reduction
Residential and Multi-Family					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	$8.48	$11.08	$11.74	$9.25	$0.23
1"	$21.21	$27.71	$29.36	$23.13	$0.57
1-1/2"	$42.41	$55.40	$58.71	$46.25	$1.15
2"	$67.85	$88.63	$93.93	$74.00	$1.84
3"	$135.71	$177.27	$187.88	$148.00	$3.67
4"	$212.03	$276.97	$293.53	$231.25	$5.74
6"	$424.06	$553.95	$587.07	$462.50	$11.48
8"	$763.32	$997.12	$1,056.74	$832.50	$20.67
10"	$1,229.73	$1,606.45	$1,702.52	$1,341.25	$33.29
Gallonage Charge (per 1,000)					
0 - 5,000 Gallons	$1.72	$2.24	$2.38	$2.26	$0.06
5,001 - 10,000 Gallons	$2.15	$2.81	$2.98	$2.55	$0.06
Over 10,000 Gallons	$2.58	$3.37	$3.57	$3.82	$0.09
General Service					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	$8.48	$11.08	$11.74	$9.25	$0.23
1"	$21.21	$27.71	$29.36	$23.13	$0.57
1-1/2"	$42.41	$55.40	$58.71	$46.25	$1.15
2"	$67.85	$88.63	$93.93	$74.00	$1.84
3"	$135.71	$177.27	$187.88	$148.00	$3.67
4"	$212.03	$276.97	$293.53	$231.25	$5.74
6"	$424.06	$553.95	$587.07	$462.50	$11.48
8"	$763.32	$997.12	$1,056.74	$832.50	$20.67
10"	$1,229.73	$1,606.45	$1,702.52	$1,341.25	$33.29
Gallonage Charge (per 1,000)	$2.32	$3.04	$3.21	$3.05	$0.08
	Typical Residential Bills 5/8" x 3/4" Meter				
3,000 Gallons	$13.64	$17.80	$18.88	$16.03	
5,000 Gallons	$17.08	$22.28	$23.64	$20.55	
10,000 Gallons	$25.68	$33.48	$41.54	$33.30	

Lake Utility Services, Inc. **Schedule No. 4-B**
Wastewater Monthly Service Rates **Docket No. 100426-WS**
Test Year Ended 6/30/10

	Rates Prior to Filing	Commission Approved Interim	Utility Requested Final	Staff Recomm. Final	4-Year Rate Reduction
Residential					
Base Facility Charge - all meter sizes	$24.57	n/a	$27.48	$24.28	$0.51
Gallonage Charge - Per kgal (10 kgal cap)	$4.48	n/a	$5.01	$4.43	$0.09
Multi-Family and General Service					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	$24.57	n/a	$27.48	$24.28	$0.51
1"	$61.44	n/a	$68.71	$60.72	$1.27
1-1/2"	$122.87	n/a	$137.41	$121.43	$2.53
2"	$196.60	n/a	$219.86	$194.29	$4.05
3"	$393.21	n/a	$439.73	$388.59	$8.10
4"	$614.38	n/a	$687.06	$607.16	$12.66
6"	$1,228.78	n/a	$1,374.14	$1,214.34	$25.32
8"	$2,211.79	n/a	$2,473.44	$2,185.80	$45.58
10"	$3,563.46	n/a	$3,985.02	$3,521.58	$73.43
Gallonage Charge - Per 1,000 gallons (10,000 gallon cap)	$5.39	n/a	$6.02	$5.33	$0.11
Irrigation Quality Reuse Services					
Base Facility Charge					
Residential Service - all meter sizes	$7.36	n/a	$8.23	$7.36	$0.15
General Service - all meter sizes	$7.36	n/a	$8.23	$7.36	$0.15
Irrigation Quality Reuse - Residential	$1.10	n/a	$1.23	$1.10	$0.02
Irrigation Quality Reuse - General Service	$1.10	n/a	$1.23	$1.10	$0.02
	Typical Residential Bills 5/8" x 3/4" Meter				
3,000 Gallons	$38.01	n/a	$42.51	$37.56	
5,000 Gallons	$46.97	n/a	$52.53	$46.42	
10,000 Gallons	$69.37	n/a	$77.58	$68.55	
(Wastewater Gallonage Cap - 10,000 Gallons)					