

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Rule 25-30.4575, F.A.C.,
Operating Ratio Methodology.

UNDOCKETED
January 29, 2018

**OFFICE OF PUBLIC COUNSEL'S INITIAL COMMENTS REGARDING
FLORIDA PUBLIC SERVICE COMMISSION STAFF'S
NOTICE OF DEVELOPMENT OF RULEMAKING**

Pursuant to the Florida Public Service Commission ("PSC" or "Commission") Staff's Notice of Development of Rulemaking to create Rule 25-30.4575, Florida Administrative Code ("F.A.C."), issued, as updated, on December 12, 2017, the Office of Public Counsel ("OPC") supports the Commission initiating rulemaking and offers the following initial comments below.

In general, the OPC urged that the agency's operating ratio policy be adopted into a rule since the policy had been clearly and consistently applied over 21 years and was no longer incipient. The purpose was not to initiate the development of a new policy based on non-existent difficulties. There is absolutely no evidence reflected in the long line of Commission orders implementing the policy that it has been ineffective and thus there is no basis to depart from this policy since any proposed departure cannot be explained or supported by evidence.

1. Proposed Rule Paragraph (1), Lines 4-5, attempt to define the operating ratio as 15 percent of the utility's operation and maintenance expenses. For 21 years the PSC has used 10% as the basis for the operating ratio as defined in the seminal Commission Order No. PSC-96-0357-FOF-WU, issued March 13, 1996 (Lake Osborne Order). Nowhere in any of the subsequent orders has there been any discussion whether this is insufficient or needs to be readdressed. The 10% calculation is not a fixed amount and should remain unaffected by the CPI index or other inflationary factors. As it is a percentage, it allows the operating ratio to increase as the expenses increase. Therefore, the rule should continue the use of the establish policy of 10%. In the two

decades of incipient policymaking, this limitation has been consistently applied with no evidence that it is ineffective or causing harm. There is certainly no evidence that circumstances have changed since the last application of this aspect of the policy in 2017.

2. Proposed Rule Paragraph (1) does not include a cap on the approval of an operating ratio-based award. The Lake Osborne Order set a cap on the operating ratio of \$10,000. Nowhere in any of the subsequent orders explicating the Commission's longstanding policy has there been any discussion or finding supporting the notion that the \$10,000 cap is insufficient or needed to be readdressed. A cap should continue to be used to limit the amount of the operating ratio. There is certainly no evidence that circumstances have changed since the last application of this aspect of the policy in 2017.

3. Proposed Rule Paragraph (1), Line 4 includes the phrase "operation and maintenance expenses." This should be replaced by the phrase "operating expenses." The revenue requirement includes all operating expenses (operation and maintenance (O&M), depreciation, taxes other than income taxes, and income taxes). However, the operating ratio is only applied to the O&M expenses as indicated on Line 5.

4. Proposed Rule Paragraph (2) defines when the operating ratio methodology shall be used. When the PSC first considered the use of an Operating Ratio in Order No. PSC-96-0357-FOF-WU, issued March 13, 1996 (Lake Osborne Order) it listed five threshold criteria. However, the proposed rule excludes the threshold criteria that addresses whether the utility is developer owned. This is an important criteria that should be included in the proposed rule. The Lake Osborne Order states that:

[B]eing developer-owned shall not, in itself, disqualify a utility from the operating ratio method. However, if a developer-owned utility is in the early stages of growth, it may be inappropriate to grant the operating ratio. Other

factors to consider would be the rate of customer growth, the developer's financial condition (sources of developer funds), the utility's financial and operational condition, government mandated improvements and/or other unanticipated expenses. The level of CIAC collected or plant written off for tax purposes shall also be considered.”

In the past cases that have considered an operating ratio, the Commission has denied the operating ratio due to the status as a developer-owned utility¹. The order states because (1) Indian River was a developer-owned utility, (2) there was significant non-used and useful plant and (3) there was potential development property in the service territory, this utility was a borderline candidate for the alternative operating ratio methodology. Therefore, the Commission denied the inclusion of the ratio in setting rates. However, this criteria has not been an issue in other cases as the systems were built-out or there was no substantial growth. Most of the water and wastewater utilities in the state have seen little to no growth during the period that the operating ratio was tested. However, the one case where a developer-owned utility experienced substantial growth was the one case where the Commission saw sufficient justification to withhold application of the alternative methodology. We agree with this and recommend that the proposed language include an exception for developer-owned utilities that are not built out or are experiencing substantial growth. There has been no Commission history regarding the other factors for developer-owned utilities as listed in the Lake Osborne Order. For this reason, the Commission could omit the remaining criteria from a rule.

5. Proposed Rule Paragraph (2), Line 10 limits the use of the methodology to those utilities whose rate base is no greater than 125% of O&M expenses. For 21 years in the incipient development of the operating ration policy the PSC has utilized the threshold of whether rate base

¹ See Order No. PSC-1996-0286-FOF-WS, issued February 27, 1996 in Docket No. 19950631-WS, In re: Application for Staff-Assisted Rate Case in Volusia County by Indian River Utilities, Inc.

is less than or equal to O&M expenses as defined in the Lake Osborne Order in determining eligibility for the rate setting treatment. Nowhere in any of the subsequent orders developing or elucidating the established policy has there been any discussion whether this is insufficient or needed to be readdressed. The determination is not a fixed amount and should remain unaffected by the CPI index or other inflationary factors. As it is based on justified expenses, it allows the threshold to increase as the expenses increase. Therefore, without any evidence as to inadequacy of, or harm caused by, the eligibility threshold policy, the rule should continue to use the established criteria. There is certainly no evidence that circumstances have changed since the last application of this aspect of the policy in 2017.

6. The Proposed Rule inexplicably abandons the express criteria in the Lake Osborne Order that the operating ration methodology is limited to Class C utilities as discussed therein on page 5 and again in a separate ordering paragraph at 23. Absent any evidence that such a limitation embedded in the longstanding agency policy is inadequate or causing hardship, such an expansion of the limited exception to the rate base, rate-of-return ratemaking should not be included in the proposed rule. There is certainly no evidence that circumstances have changed since the last application of this aspect of the policy in 2017.

7. Many of our comments above are based on a concern that was expressed in a dissent to the Lake Osborne Order by Commissioner Deason on page 26. As succinctly stated by Commissioner Deason, how does this methodology “impact our policy of seeking to encourage equity investment and, hence, a sense of ownership and responsibility by the owners?” Staff has expressed concern that none of the utilities want to be in this position. However, many of these utilities are in such a position as a result of their own actions, such as its failure to invest in needed infrastructure. We also recognize that some utilities are in this position due to the actions of prior

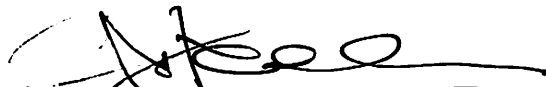
owners. Because there is no one-size-fits-all rule that can address this concern, we believe that taking the moderate approach contained in the longstanding policy allows utilities to obtain the additional margin necessary to operate, but does not remove all incentives from a utility to invest in needed infrastructure.

8. These comments are preliminary and the OPC reserves the right to supplement and amend them as the rulemaking proceeds forth, including to hearing if necessary.

CONCLUSION

OPC respectfully requests the Commission consider these comments as it proceeds to review Staff's Notice of Development of Rulemaking to create Rule 25-30.4575, F.A.C.

Sincerely,



J.R. Kelly
Public Counsel

Charles J. Rehwinkel
Deputy Public Counsel

CERTIFICATE OF SERVICE
UNDOCKETED

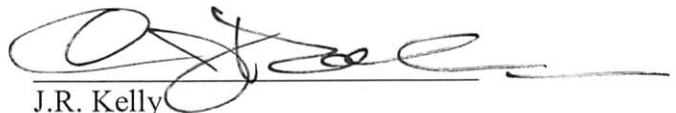
I HEREBY CERTIFY that a true and correct copy of the foregoing **OFFICE OF PUBLIC COUNSEL'S COMMENTS REGARDING FLORIDA PUBLIC SERVICE COMMISSION STAFF'S NOTICE OF DEVELOPMENT OF RULEMAKING** has been furnished by electronic mail to the following parties on this 29th day of January, 2018.

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