MERRITT ISLAND UTILITY COMPANY

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FPSC - COMMISSION CLERK

August 8, 2019

Office of Commission Clerk
Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399

Re: Docket No. 20190116-SU – Application for staff assisted rate case in Brevard County by Merritt Island Utility Company

Dear Commission Clerk,

Merritt Island Utility Company (Merritt Island) submits additional information related to its Outside Contractual Services in response to previous concerns brought forth by the Commission at previous agenda conferences. Several questions were expressed on comparative contracts with affiliated parties.

The wastewater system acquired from Colony Park experienced years of neglect. Merritt Island contracted with US Water Service Corporation (USWSC) for administrative management, operations, maintenance, and customer service. The President and majority shareholder of Merritt Island has been in the water and wastewater utility management, operations and maintenance related industry for over thirty (30) years bringing a level of Florida specific expertise that is not typical to private utility ownership within the State. The Vice President of Investor Owned Utilities also has over thirty (30) years experience in regulated utilities and will provide direct management oversight to Merritt Island. Further, through its contract with USWSC, Merritt Island has made significantly plant improvements that have resulted in improved quality of service to its wastewater. USWSC is the largest service provider of operations, maintenance, customer service and billing in the State of Florida. USWSC currently provides service in 60 of the 67 counties in Florida providing service to over 1,000 utility systems. Currently, USWSC provides water service to over 1,000,000 customers daily. USWSC has over 400 operational and maintenance employees throughout the State of Florida, and has over 99.95% compliance success record. USWSC also currently has numerous water and wastewater clients in close proximity to Merritt Island, thereby providing consistent reliable service in close proximity.

USWSC also provides more than 100,000 meter reading services per month and responds to over 25,000 service calls per month. Through its contract with USWSC, Merritt Island has already made significant operational changes that will improve the quality of service, as well as reduce overall operating expenses.

Through USWSC, professional and experienced managerial, financial, technical and operational resources are provided to twenty (20) other relate investor-owned utilities (IOUs) regulated by the Commission. The majority shareholder and president of Merritt Island is also the majority shareholder and president of the other related IOUs as well as USWSC. This provides for significant synergies and cost savings to all of the IOUs' customers. This technical and operational skills and knowledge can be used to further improve the operational performance of Merritt Island.

Merritt Island Waterworks, Inc.
Additional Information on Outside Contractual Services

Past Commission Decisions

Merritt Island has researched past Commission decisions on similar contractual services and offers the following relative to the existing contract.

A similar relationship exists with several regulated utilities in Marion County. However, these relationships are not exactly like Merritt Island contract. The following regulated water and wastewater utilities have similar services provided by a related party:

Tradewinds Utilities, Inc.
Residential Water Systems, Inc.
C.F.A.T. H20, Inc.
BFF Corp

These utilities have Outside Contractual Services with MIRA International, Inc. (MIRA). All of the above regulated utilities, as well as MIRA are owned by the same owners and have affiliated relations. MIRA provides the following services to the regulated utilities:

Billing/Computer Services
Administrative Services
Payroll
Meter Reading
Insurance
Office Space
Materials & Supplies
Repair & Service Equipment
Customer Relations
Customer Services
Annual PSC Reporting
Hospitalization Benefits

Testing expenses and operation and maintenance expenses are covered under separate contracts discussed below.

In review of the Annual Reports, as well as past Commission orders on previous rate cases, these utilities also have utility Employee Salaries and Employee Pensions and Benefits. In Order No. PSC-11-0385-PAA-WS, issued September 13, 2011, the Commission approved a rate increase for Tradewinds Utilities, Inc. (Tradewinds). In review of the documentation in the Commission's docket file, the Commission approved Tradewinds' Outside Contractual Services with MIRA, an affiliated company. Specifically, in the Commission's audit – Audit Control No: 10-175-2-1 dated December 17, 2010, the Commission's auditor disclosed the following in Audit Finding 8:

> The Utility's filing includes $100,276 and $131,475 of charges from MIRA International, Inc. (MIRA), an administrative Service Company, which is a related party. The charges are for employee and officer payroll, payroll tax expenses, employee benefits, office space and support for customer billing and collections, general maintenance materials and supplies, and other general administrative support operations as needed for utility

> operations. The Utility has no employees of its own and all administrative and general maintenance services are provided by MIRA.

The auditor recommended adjustments based on recommended amounts for affiliated charges as follows:

Tradewinds:	$93,228 – water $55,754 – wastewater
Residential:	$146,849 – water
C.F.A.T.:	$34,580 – water $33,666 - wastewater
BFF Corp:	$16,300 – wastewater

In addition, in reviewing Document No. 09572-10 in the docket file of Docket No. 100127-WS, Tradewinds also has an additional contract for operations with Pro-Tech for $600/month, or $7,200 annually. There were also additional expenses for Testing included in the operating expenses. The amount requested by Tradewinds in its MFRs for Pro-Tech was $4,400 for water and $5,250 for wastewater. In addition, there was additional testing in the amount of $3,630 for wastewater for Aqua Pure Water.

In Order No. PSC-11-0385-PAA-WS, the Commission approved Tradewind's Operation & Maintenance Expense with minor adjustments for Pro Forma Salary Increase and Bad Debt Expense. Tradewinds had requested O&M in the amount of $125,421 for water and $187,846 for wastewater. The Commission approved O&M in the amount of $120,654 for water and $176,895 for wastewater.

Tradewind's MFRs also reflected plant in service amounts for Transportation; Office Furniture and Equipment; and Power Operated Equipment which were included in rate base. These items are included in the contract with U.S. Water Services Corporation with Merritt Island and are not included in plant-in-service.

In another related rate case in Docket No. 200100126-WU for C.F.A.T. H2O, Inc. (CFAT), the Commission approved the utility's request for a rate increase. In reviewing the Commission audit in Audit Control No: 10-274-2-1 dated December 15, 2010, the Commission's auditor disclosed the following in Audit Finding 5:

> The Utility's filing includes $16,718 of charges to water O&M expenses from MIRA International, Inc. (MIRA), an administrative Service Company, which is a related party. The charges are for employee and officer payroll, payroll tax expenses, employee benefits, office space and support for customer billing and collections, general maintenance materials and supplies, and other general administrative support operations as needed for utility operations. CFAT has no employees of its own and all administrative and general maintenance services are provided MIRA. (sic)

Merritt Island Waterworks, Inc.
Additional Information on Outside Contractual Services

The auditor recommended that "The Utility's O&M expense balance should be increased by $17,862 for the 12-month period ending December 31, 2009." This would bring the MIRA recoverable amount to $34,580 for water. In addition, Document No. 09566-10 in the docket file contained an operations contract for Pro-Tech in the amount of $595 a month or $7,140 annually. The amount included in the Utility's MFRs and requested O&M expense for Pro-Tech was $8,197. These additional amounts were allowed by the Commission, for a total outside services amount of $49,917 for water.

In Order No. PSC-11-0366-PAA-WU, issued August 31, 2011, the Commission made minor adjustments to CFAT's O&M expenses primarily for Pro Forma salaries and bad debt expenses. This rate case was only for CFAT's water utility and did not include its wastewater utility.

In another similar rate case, the Commission approved total outside services for K.W. Resort Utilities Corp in Order No. PSC-09-0057-FOF-WS, issued January 27, 2009. In that rate case, the utility had several Outside Contractual Services with several affiliated parties. The first was for operations services with Keys Environmental, Inc. (KEI), an affiliated party. The utility recorded expenses in the amount $450,776 for KEI during the test year. The Commission reduced this amount by $71,053 for an allowed amount of $379,723. This represented the operations portion of the utility services. However, KEI employees utilized the transportation equipment (vehicles) owned by the utility. In addition, KEI does not provide accounting services or initial customer contacts. These services are provided by Key West Golf Course (KWGC), another affiliate company. The utility paid KWGC an amount of $8,000 a month or $96,000 annually. The Commission reduced this amount by $12,038 for a total allowed amount of $83,962. Finally, the utility was charged $60,000 annually for "management" of the utility paid to Green Fairways (an affiliated company). The Commission reduced this amount by $30,000 and allowed the remaining $30,000 annually. The total amount of these three contractual services was a total of $493,683. This is a wastewater only utility providing service to 1,556 customers during the test year. The total amount of the Commission allowed affiliated transactions equates to $317 per connection. In addition the utility also was allowed $65,289 in ongoing engineering charges in Contractual Services – Engineering in the approved revenue requirement. It should be noted that the KEI contract provides that the contractor provide the chemicals and sludge hauling in the contract.

It should also be noted, that in the rate cases cited above, the Commission approved rate case expense in its orders. In Merritt Island's filing, there is very minimal rate case expense requested.

Merritt Island contract with U.S. Water Service Corporation (USWSC) include the following services:

Wastewater Operations
System Maintenance
Flushing – distribution system
Customer Service
Service Orders
Regulatory - PSC, WMD, DEP
Permits – DEP, DOH, WMD, etc.
Testing – ***all*** normal required for and wastewater (abnormal events not included)
DMRs, MORs - monthly reporting
PSC Annual Reports
Accounting ***- all*** bookkeeping, record keeping, AR, AP, etc.

Merritt Island Waterworks, Inc.
Additional Information on Outside Contractual Services

Line break repairs
Minor repairs and/or replacements – up to $400
Locates
Meter calibrations
New connections
Disconnections
Generator Maintenance
Vehicles
Office (also equipment, phones, etc.)

The USWSC contract was revised on October 1, 2017 in the amount of $45,277.04 for wastewater. This equates to $286.56 per ERC. This contract amount has increased by an index increase and the current amount is $47,211.24 for wastewater, which equates to $298.81 per ERC.

Pursuant to the Contract, Merritt Island employed the services of USWSC in distinct functions; administrative management, operation, maintenance and billing/collection of the utility. This includes (a) Management and Financial Oversight; (b) Wastewater System Operations; and (d) Maintenance; and (d) Customer Service. For a listing of serviced provided to Merritt Island, see USWSC's Scope of Services – Base Contract Service, Section 2, as well as the cost responsibilities on Table 4 of the contract for water.

WetCon Study

In 2013, the Florida Governmental Utility Authority (FGUA) hired WetCon Utility and Management Consultants to review charges by USWSC in comparison to similar water and wastewater utilities throughout the United States. The Wetcon study was issued in July 2013. The WetCon study concluded that the USWSC costs on a per account bases fell within the top quartile of other utilities. These were charges to FGUA by USWSC.

Upon further analysis of the WetCon benchmarking study, there was a flaw in their data table. The underlying data for the "South" was obtained from the AWWA 2011 Benchmarking Performance Indicators. Upon further analysis, it was discovered that the costs in WetCon's table were an average of the two water and wastewater costs. Further, the WetCon Benchmarking report states, "It is virtually impossible to find any two water utilities that are comparable, given their unique treatment systems, customer bases, permit requirements, operational procedures, capital needs and rate structures. This is particularly true when comparing other systems to FGUA, with its' geographic spread, diverse customer base and broad range of treatment technologies."

AWWA Benchmark

Another reputable study often used in the water and wastewater industry is the American Water Works Association (AWWA) Benchmarking Performance Indicators. This is the same benchmarking used in the WetCon study. Utilizing the 2016 Edition for water and wastewater, below is the actual costs contained in the AWWA 2016 Benchmarking Analysis:

Merritt Island Waterworks, Inc.
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2016 AWWA:	Top	Medium	Bottom
O&M cost per customer			
Water - O&M	$ 300	$ 386	$ 573
Wastewater - O&M	$ 333	$ 346	$ 360
Total O&M	$ 633	$ 732	$ 933

Customer Service Cost	Top	Medium	Bottom
Water	$ 31.25	$ 44.71	$ 66.82
Wastewater	$ 11.99	$ 21.91	$ 30.11

Total Cost:			
Water:	$ 331.25	$ 430.71	$ 639.82
Wastewater:	$ 344.99	$ 367.91	$ 390.11
Total	$ 676.24	$ 798.62	$1,029.93

Compared to Merritt Island:
Water **$ 298.81**

Also, in the 2016 AWWA, there was a further analysis based on company size. When compared to utilities in this study for Population from 0 -10,000 customers, the contrast is much more striking. Below are the numbers from the AWWA study:

Population 0 – 10,000:

O&M cost per customer			
Water - O&M	$ 353	$ 573	$ 679
Wastewater O&M	$ 195	$ 278	$ 381
Total O&M	$ 548	$ 851	$1,060

Customer Service Cost	Top	Medium	Bottom
Average	$ 35.81	$ 48.09	$ 66.38

Total Cost per customer:	$ 583.81	$ 899.09	$ 1,126.38

Both of these independent studies provide third party independent verification that the USWSC operation and maintenance costs are well below the market rate. The "market" comparison is drawn on by both the 2016 AWWA benchmark as well as the Wetzell Benchmarking Report. This market comparison is paramount in providing finality to Merritt Island's unrefuted evidence that these costs are well below market, and not above as required by the Florida Supreme Court as discussed below.

Each of the Administrative Management, Operation, Maintenance, and Customer Service contracts that USWC enters into with a party are different and are priced differently depending on numerous factors. This includes the number of utility operation employees needed (Facility Operators and Maintenance Mechanic) and the number of hours required per system for operation. Also whether the contractor provides the cost of the sludge hauling, chemicals, power, offices, vehicles, etc. or if those costs are

borne by the owner. Also for the regulated utilities, the Utility Manager and Accountant are spread over all ERCs of the investor owned utilities. The contractual monthly charges for these utilities include the operations, accounting, and operation management positions. For the "Administrative Services" portion, this is derived at by using all currently owned or purchased investor owned utilities and dividing these amounts by the existing. The Administrative portion of the contract covers the accounting and utility oversight, including office space and equipment. These amounts are to cover the monthly operational and administrative expenses for all the investor owned utilities.

The Utilities Manager oversees the daily operational items of each regulated utility, as well as the future capital improvement requirements. This individual also interacts with the field employees of the Department of Environmental Protection, local Health Departments, Public Service Commission, and the various Water Management Districts. The Utility Manager also interacts with the customers of the various regulated utilities. The Accountant performs all accounting and reporting requirements of the regulated utilities. This includes daily transactions in accounts payable, accounts receivable, bookkeeping, financial statements, etc. The Vice President oversees all aspects of each regulated utility and supervises both the Utility Manager and Accountant. The Vice President also is responsible for all governmental reporting with the various agencies, including the Public Service Commission.

Merritt Island respectfully submits that the comparison of these non-related contracts, although useful and informational, should not be the sole basis of any disallowance of prudently incurred operating expenses. If Merritt Island was required to establish a stand-alone utility with personnel for maintenance, customer service, accounting, regulatory compliance, etc. the costs would far exceed the amount in the current USWSC contract. These operation and maintenance expenses would be incurred regardless of the size of the customer base.

It should be noted that the Commission has previously considered this approach at analyzing affiliated transactions of related parties and stated the following in Order No. PSC-12-0102-FOF-WS, issued March 5, 2012:

> In evaluating whether and how much affiliate costs should be included in rates, we are aware of the relevant statutes and cases on rates and affiliate transactions. Section 367.081(2)(a)1., F.S., sets forth our responsibility in rate setting, and specifically states:
>
> The commission shall, either upon request or upon its own motion, fix rates which are just, reasonable, compensatory, and not unfairly discriminatory. In every such proceeding, the commission shall consider the value and quality of the service and the cost of providing the service, which shall include, but not be limited to, debt interest; the requirements of the utility for working capital; maintenance, depreciation, tax, and operating expenses incurred in the operation of all property used and useful in the public service; and a fair return on the investment of the utility in property used and useful in the public service. . . .
>
> As reflected in the statute cited above, we are required to set reasonable rates, but we must also set rates that are compensatory. The provisions in the statute require that we consider the cost of providing service, which includes operating expenses incurred in the

operation of all property used and useful in the public service, as well as a fair return on the investment of the Utility in property used and useful in the public service. In conducting our analysis of the appropriate operating expenses to be included, we are mindful of two Florida Supreme Court cases. In the case of **Keystone Water Co v. Bevis**, 278 So. 2d 606 (Fla. 1973), the Court held that a utility is entitled to a fair rate of return on property used or useful in public service. In **Keystone**, the Court further found that rates which do not yield a fair rate of return are unjust, unreasonable, and confiscatory and their enforcement deprives a utility of due process.[1] Additionally, in **GTE v. Deason**, 642 So. 2d 545 (Fla. 1994), the Florida Supreme Court laid out the standard of review for affiliate transactions, stating:

> The mere fact that a utility is doing business with an affiliate does not mean that unfair or excess profits are being generated, without more. Charles F. Phillips, Jr., *The Regulation of Public Utilities* 254-55 (1988). We believe the standard must be whether the transactions exceed the going market rate or are otherwise inherently unfair. . . . If the answer is "no," then the PSC may not reject the utility's position.

GTE v. Deason, 645 So. 2d at 547-548. We have reviewed the record evidence and applied the holdings in **Keystone v. Bevis** and **GTE v. Deason** as appropriate. (pages 99 – 100)

The Commission, in arriving at its final decision stated:

> While we agree with OPC witness Dismukes that AUF's Market Based Study does not offer a realistic comparison of market based rates, we also agree with AUF witness Szyzgiel that the peer group analysis presented by witness Dismukes does not provide an adequate comparison. We note that in AUF's 2008 rate case we also disagreed with witness Dismukes' previous recommendation to use a comparison of Commission-regulated utilities to AUF in evaluating affiliate-provided services. In the Utility's 2008 rate case, we specifically found "[t]hat the comparison analysis proposed by witness Dismukes does not provide an appropriate basis to warrant an adjustment being made."[2] As acknowledged by witness Dismukes, there are complexities associated with determining the reasonableness of affiliate transactions. To that point, we find that witness Dismukes' peer group comparison does not adequately compare the duties, activities, and responsibilities for the Utility's affiliate-provided services.

The Commission further stated:

> Moreover, just because the costs to operate a utility are high, this does not necessarily mean that a utility is operating inefficiently. Other factors may influence the costs to provide service to customers. Therefore, we believe a review of this particular Utility's history is helpful in understanding the costs associated with providing service.

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[1] See Keystone Water Co. v. Bevis, 278 So. 2d 606, 609 (Fla. 1973).
[2] See Order No. PSC-09-0385-FOF-WS, p. 78.

Merritt Island also offers that in the alternative, certain utility expenses may be excluded from the contract amount with the mutual understanding that these expenses will still be incurred but recorded in other expense accounts. The amounts of these prudently incurred expenses, such as testing, would also need to be included in overall approved revenue requirement.

Previous Commission Decision – USWSC

The Commission has previously reviewed the reasonableness of the USWSC contract in several rate cases of "sister" utilities. Specifically, in Order No. PSC-15-0013-PAA-WS, issue January 2, 2015, the Commission stated:

> We understand that the U.S Water contract is a significant operating expense. However, the U.S Water contract is comprehensive in nature, and provides the Utility's customers with services that prior owners/operators did not. We recognize that such services in rates is the primary reason that the water and wastewater expenses have increased. Upon review, we shall approve contractual services – other expenses of $38,197 for water and $35,730 for wastewater.

Again in Order No. PSC-15-0282-PAA-WS, issued July 8, 2015, the Commission stated:

> The USWSC provided its costing and allocation model to this Commission and OPC. We reviewed the model and its inputs and allocation procedures and, with the exception of the items for which we made adjustments, found the model to be reasonable.

The Commission continued by stating:

> In conclusion, we find that the adjusted cost of the management services contract with USWSC is reasonable. The contract cost is comparable to the cost allowed in Lakeside Waterworks, Inc.'s rate case, Docket No. 130194-WS, and is lower than similar contract costs that have been identified. USWSC and its managers bring considerable management and operator experience and expertise at a comparably reasonable cost. By spreading costs over
> multiple systems, and adding ERCs to recognize potential future growth, HC Waterworks' customers are realizing operational and cost benefits that would not be available if the Utility operated on a stand-alone basis. The adjusted total cost of the management services contract of $194,847 for water and $57,566 for wastewater is hereby approved.

Finally, in Order No. PSC-16-0305-PAA-WU, issued July 28, 2016, the Commission stated:

> Lake Idlewild receives all of its operational and administrative services under a contract with an affiliated company, U.S. Water Services Corporation (USWSC). We previously reviewed and approved expenses related to the USWSC management services contracts for six of Lake Idlewild's sister utilities.[3] In the four most recent related dockets, we

[3]Order No. PSC-14-0413-PAA-WS, issued August 14, 2014, in Docket No. 130153-WS, *In re: Application for staff-assisted rate case in Highlands County, by L.P. Utilities Corporation c/o LP Waterworks, Inc.*; Order No. PSC-15-

> found USWSC's costing and allocation model to be reasonable with the exception of some allocated expenses related to salary overtime, fuel, and vehicle maintenance which were adjusted in those dockets.[4]

The Commission approved the USWSC contract by stating:

> In addition to the cost subsidy resulting from USWSC's cost model, we find that Lake Idlewild is experiencing additional cost savings related to expenses such as chemicals, testing, and miscellaneous expenses that are attributable to economies of scale achieved through operations provided under the USWSC contract.
>
> USWSC and its managers bring considerable management and operator experience and expertise at a comparably reasonable cost. By spreading costs over multiple systems, and adding ERCs to recognize potential future growth, Lake Idlewild's customers are realizing operational and cost benefits that would not be available if the Utility operated on a stand-alone basis. We find that the adjusted cost of the USWSC management services contract is reasonable.

If you have any additional questions or concerns, please do not hesitate to contact me at (727) 848-8292, ext. 245.

Sincerely,

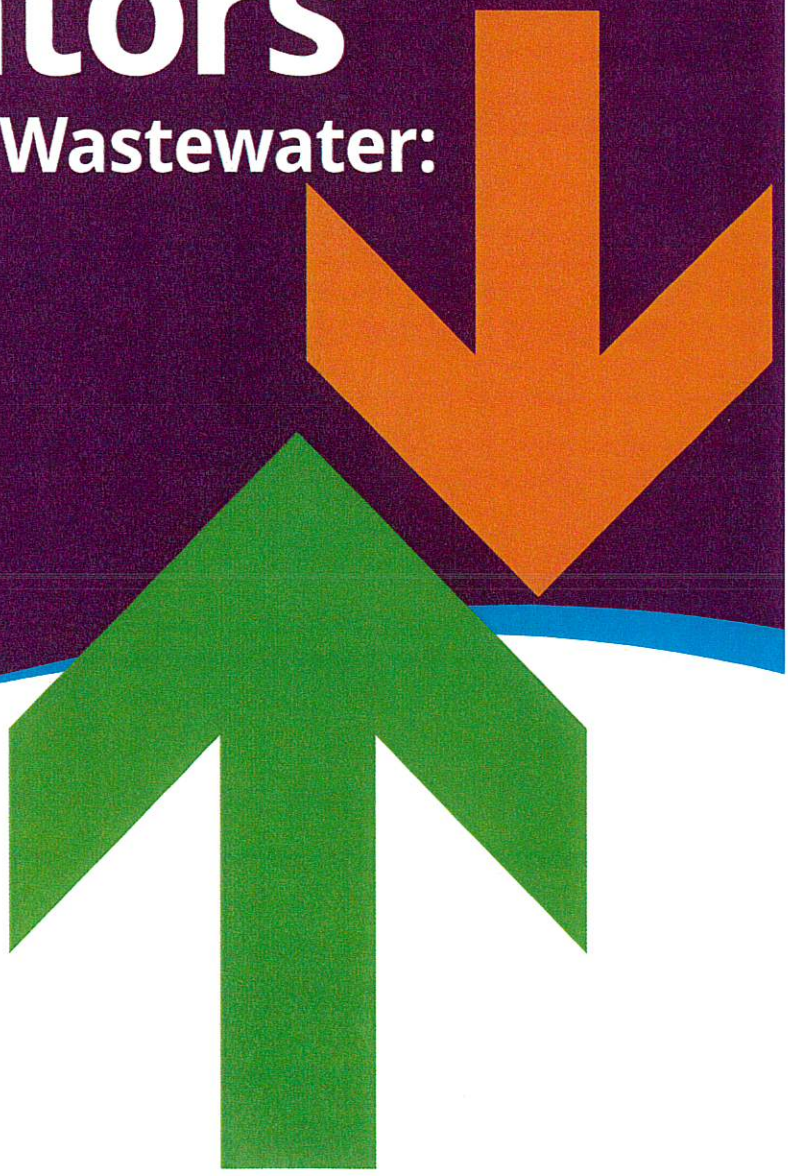
Troy Rendell
Vice President
Investor Owned Utilities
// for Merritt Island Waterworks, Inc.

0013-PAA-WS, issued January 2, 2015, in Docket No. 130194-WS, *In re: Application for staff-assisted rate case in Lake County by Lakeside Waterworks, Inc.*; Order No. PSC-15-0282-PAA-WS, issued July 8, 2015, in Docket No. 140158-WS, *In re: Application for increase in water/wastewater rates in Highlands County by HC Waterworks, Inc.*; Order No. PSC-15-0329-PAA-WU, issued August 14, 2015, in Docket No. 140186-WU, *In re: Application for staff-assisted rate case in Brevard County by Brevard Waterworks, Inc.*; Order No. PSC-15-0335-PAA-WS, issued August 20, 2015, in Docket No. 140147-WS, *In re: Application for staff-assisted rate case in Sumter County by Jumper Creek Utility Company*. In addition, we approved similar expenses in Docket No. 150199-WU, *In re: Application for staff-assisted rate case in Lake County by Raintree Waterworks, Inc.*, Order No. PSC-16-0256-PAA-WS, issued June 30, 2016

[4]Order Nos. PSC-15-0282-PAA-WS, PSC-15-0329-PAA-WU, and PSC-15-0335-PAA-WS. This Commission again found USWSC's costing and allocation model to be reasonable, with the exception of some allocated expenses related to fuel and vehicle maintenance, in Docket No. 150199-WU, *In re: Application for staff-assisted rate case in Lake County by Raintree Waterworks, Inc.*, Order No. PSC-16-0256-PAA-WS, issued June 30, 2016.

Benchmarking Performance Indicators

for Water and Wastewater: 2016 Edition



American Water Works Association

Dedicated to the World's Most Important Resource®

CUSTOMER SERVICE COST PER ACCOUNT

This indicator, which measures the amount of resources a utility applies to its customer service program over the course of a year, is expressed as the cost of managing a single customer account for one year. Customer service costs are all direct salaries, employee benefits, and direct costs including contracts that are associated with providing the following services to customers, plus a proportional share of total utility indirect costs:

- New account activation
- Meter reads, maintenance, repair, or replacement
- Bill preparation and delivery
- Payment receipt and processing
- Records maintenance
- Delinquent account collections
- Bankruptcy processing
- Provision of turn-on/turn-off services
- Receipt, investigation, and resolution of complaints
- Preparation and provision of outreach and education materials, including the Consumer Confidence Report

For a given reporting period, this indicator is calculated as follows:

$$\text{Customer Service Cost per Account (annual \$/account)} = \frac{\text{Total annual customer service costs}}{\text{Number of active residential accounts} + \text{Number of nonresidential accounts}}$$

Specifically excluded are all costs associated with maintaining service lines and customer plumbing on the customer side of the meter or service property line if no meter is present. If water and wastewater services are billed together, the following options for providing the data were recommended:

- The preferred option is to separate costs associated with each service and provide separate summaries of active customer accounts.
- An acceptable alternative is to provide aggregate cost for both services and provide separate counts of active customer accounts for water and wastewater services represented by those costs.
- A third alternative is to report single numbers for total costs and active customer accounts.

Tables 3-6A through 3-6C present the aggregate data for the Customer Service Cost per Account indicator by service from the 2015 data set.

Table 3-6A Aggregate data for the customer service cost per account—Water (annual $/account)

	Top Quartile	Median	Bottom Quartile	Sample Size
Water Operations	$31.25	$44.71	$66.82	39
Combined Operations—Water	$21.74	$32.03	$50.83	41

Table 3-6B Aggregate data for the annual customer service cost per account—Wastewater (annual $/account)

	Top Quartile	Median	Bottom Quartile	Sample Size
Wastewater Operations	$11.99	$14.71	$30.11	9
Combined Operations—Wastewater	$14.60	$21.91	$32.05	40

Table 3-6C Aggregate data for the annual customer service cost per account—Combined (annual $/account)

	Top Quartile	Median	Bottom Quartile	Sample Size
Combined Operations	$19.29	$24.91	$37.89	71

O&M COSTS FOR POTABLE WATER SERVICES

The operations and maintenance (O&M) costs for potable water service can be compared between utilities once normalized by water production to give a unit cost ($/MG) or on the basis of the number of accounts served or miles of distribution pipeline. For utilities following Governmental Accounting Standards Board (GASB) or Financial Accounting Standards Board (FASB) practices, the required total O&M cost information can be found on the audited financial statement. Depreciation is not included in the total operations and maintenance cost.

For a given reporting period, these indicators are calculated as follows:

$$\text{Total O\&M Cost of Potable Water Services (\$/account)} = \frac{\text{Total O\&M cost}}{\text{Number of residential accounts + Number of nonresidential accounts}}$$

$$\text{Total O\&M Cost of Potable Water Services (\$/MG)} = \frac{\text{Total O\&M cost}}{\text{Average daily production} \times 365 \text{ days}}$$

$$\text{Total O\&M Cost of Potable Water Services (\$/100 miles of pipe)} = \frac{\text{Total O\&M cost} \times 100}{\text{Total miles of distribution system piping}}$$

$$\text{Treatment O\&M Cost of Potable Water Services (\$/MG)} = \frac{\text{Treatment O\&M cost}}{\text{Average demand in MGD} \times 365}$$

$$\text{Distribution O\&M Cost of Potable Water Services (\$/100 miles of pipe)} = \frac{\text{Distribution O\&M cost} \times 100}{\text{Total length of distribution system piping}}$$

$$\text{Specific O\&M Percentage of Water Services (\% of total)} = \frac{\text{Specific O\&M cost}}{\text{Total O\&M Cost}}$$

Tables 4-5A through 4-5I present the aggregate data for the O&M Cost of Potable Water Services indicators for water and combined utilities from the 2015 data set. O&M percentage of water services is calculated in four separate ways: water supply, water treatment, water transmission and distribution, and water support series provided by others.

Table 4-5A Aggregate data for the O&M cost of potable water services indicators—Total annual O&M cost per account ($/account)

	Top Quartile	Median	Bottom Quartile	Sample Size
Water Operations	$300	$386	$573	44
Combined Operations—Water	$294	$410	$669	85

Table 4-5B Aggregate data for the O&M cost of potable water services indicators—Total annual O&M cost per MG

	Top Quartile	Median	Bottom Quartile	Sample Size
Water Operations	$1,769	$2,417	$3,515	44
Combined Operations—Water	$1,726	$2,305	$3,683	76

Table 4-5C Aggregate data for the O&M cost of potable water services indicators—Total annual O&M cost per 100 miles of pipe

	Top Quartile	Median	Bottom Quartile	Sample Size
Water Operations	$1,800,664	$2,487,492	$3,729,519	45
Combined Operations—Water	$1,668,654	$2,598,590	$4,049,861	86

Table 4-5D Aggregate data for the O&M cost of potable water services indicators—Treatment O&M cost per MG

	Top Quartile	Median	Bottom Quartile	Sample Size
Water Operations	$378	$512	$765	35
Combined Operations—Water	$452	$661	$850	50

Table 4-5E Aggregate data for the O&M cost of potable water services indicators—Distribution O&M cost per 100 miles of pipe

	Top Quartile	Median	Bottom Quartile	Sample Size
Water Operations	$421,547	$587,945	$948,905	37
Combined Operations—Water	$383,869	$577,512	$763,520	61

O&M COSTS FOR WASTEWATER SERVICES

The operations and maintenance (O&M) costs for wastewater services can be compared between utilities once normalized by production rate to give a unit cost ($/MG) or on the basis of the number of accounts served or the length of the collection pipe network. For utilities following Governmental Accounting Standards Board (GASB) or Financial Accounting Standards Board (FASB) practices, the required total O&M cost information can be found on the audited financial statement. Depreciation is not included in the total operations and maintenance cost.

For a given reporting period, these indicators are calculated as follows:

$$\text{Total O\&M Cost of Wastewater Services (\$/account)} = \frac{\text{Total O\&M cost}}{\text{Number of residential accounts + Number of nonresidential accounts}}$$

$$\text{Total O\&M Cost of Wastewater Services (\$/MG)} = \frac{\text{Total O\&M cost}}{\text{Average daily production} \times 365 \text{ days}}$$

$$\text{Total O\&M Cost of Wastewater Services (\$/100 miles of pipe)} = \frac{\text{Total O\&M cost} \times 100}{\text{Total miles of collection system piping}}$$

$$\text{Collection O\&M Cost of Wastewater Services (\$/100 miles of pipe)} = \frac{\text{Collection O\&M cost} \times 100}{\text{Total miles of collection system piping}}$$

$$\text{Treatment O\&M Cost of Wastewater Services (\$/MG)} = \frac{\text{Treatment O\&M cost}}{\text{Average daily production} \times 365 \text{ days}}$$

$$\text{O\&M Percentage of Wastewater Services (\% of total)} = \frac{\text{Specific O\&M cost}}{\text{Total O\&M Cost}}$$

Tables 5-5A through 5-5H present the aggregate data of O&M Cost of Wastewater Services indicators for wastewater and combined operations from the 2015 data set. The percentage of O&M services to total wastewater O&M services provided is shown for wastewater collection, wastewater treatment, and wastewater support services provided by others.

Table 5-5A Aggregate data for O&M cost of wastewater services indicators—Total annual O&M cost per account ($/Account)

	Top Quartile	Median	Bottom Quartile	Sample Size
Wastewater Operations	$333	$346	$360	8
Combined Operations—Wastewater	$249	$355	$494	75

Table 5-5B Aggregate data for O&M cost of wastewater services indicators—Total annual O&M cost per MG

	Top Quartile	Median	Bottom Quartile	Sample Size
Wastewater Operations	$1,360	$2,609	$3,489	11
Combined Operations—Wastewater	$1,727	$2,597	$3,904	69

Table 5-5C Aggregate data for annual O&M cost of wastewater services indicators—Total annual O&M cost per 100 miles of pipe

	Top Quartile	Median	Bottom Quartile	Sample Size
Wastewater Operations	$1,879,576	$3,485,961	$4,751,973	10
Combined Operations—Wastewater	$1,796,332	$2,412,263	$3,335,791	76

Table 5-5D Aggregate data for annual O&M cost of wastewater services indicators—Collection O&M cost per 100 miles of pipe

	Top Quartile	Median	Bottom Quartile	Sample Size
Wastewater Operations	$508,664	$1,026,267	$1,136,943	10
Combined Operations—Wastewater	$368,562	$513,699	$791,276	57

Performance Indicator	0–10,000				10,001–50,000				50,001–100,000			
	Top Quartile	Median	Bottom Quartile	Count	Top Quartile	Median	Bottom Quartile	Count	Top Quartile	Median	Bottom Quartile	Count
Residential Cost of Water Service—Average Monthly Bill ($)	$30.75	$43.53	$58.68	7	$29.69	$38.75	$56.50	23	$22.71	$28.74	$36.78	22
Residential Cost of Water Service—Average monthly usage (gallons)	5,758	7,000	9,067	7	5,000	5,984	8,231	23	4,100	5,882	7,600	21
Residential Cost of Wastewater Service—7,500 gallons per month	$46.04	$49.34	$56.88	6	$25.41	$47.96	$61.21	13	$34.15	$51.00	$55.90	17
Residential Cost of Wastewater Service—Average monthly residential bill	$37.14	$46.09	$55.30	6	$25.38	$37.36	$48.28	13	$31.02	$35.87	$41.17	18
Residential Cost of Wastewater Service—Average Monthly flow (gallons)	6,020	6,540	7,150	6	4,458	5,250	6,709	12	4,000	5,800	6,000	17
Residential Cost of Stormwater Service—Average monthly residential bill ($ per month)	na	na	na	0	$2.69	$4.10	$9.09	6	$4.00	$7.00	$9.75	5
Customer Service Cost per Account ($)—COMBINED	$40.18	$55.55	$102.54	3	$14.83	$22.92	$34.93	11	$22.11	$27.27	$40.64	12
Customer Service Cost per Account ($)—WATER	$46.13	$70.81	$82.36	6	$20.94	$59.11	$90.39	15	$25.95	$27.96	$44.42	11
Customer Service Cost per Account ($)—WASTEWATER	$35.81	$48.09	$66.38	4	$35.98	$78.35	$80.89	6	$11.21	$20.47	$27.69	9
Billing Accuracy (per 10,000 bills generated)—COMBINED	0.9	1.3	1.9	3	0.7	2.9	8.9	10	3.4	12.4	19.4	10
Billing Accuracy (per 10,000 bills generated)—WATER	1.3	2.1	3.5	6	1.1	3.0	6.5	14	0.9	14.0	34.2	7
Billing Accuracy (per 10,000 bills generated)—WASTEWATER	0.9	1.3	2.7	3	0.7	0.9	4.4	6	0.0	5.5	14.4	4
Total per capita consumption (gallons per capita per day)	79.6	88.3	181.6	7	89.0	97.0	139.4	23	100.4	116.7	160.1	21
Domestic per capita consumption (gallons per capita per day)	56.4	73.6	153.3	5	48.4	69.9	103.9	23	57.5	66.2	86.1	20
Service Affordability (%)—WATER	0.70%	0.79%	0.88%	6	0.55%	0.65%	1.09%	19	0.53%	0.66%	0.80%	19
Service Affordability (%)—WASTEWATER	0.37%	0.58%	0.96%	4	0.43%	0.65%	0.97%	12	0.59%	0.80%	0.99%	15
Service Affordability (%)—STORMWATER	na	na	na	0	0.06%	0.09%	0.24%	6	0.08%	0.10%	0.27%	5
Stakeholder Outreach Index (%)	60%	38%	25%	10	67%	33%	33%	17	98%	75%	58%	22
Water Operations												
Regulatory Compliance—WATER (%)	100.0%	100.0%	100.0%	7	100.0%	100.0%	100.0%	23	100.0%	100.0%	100.0%	20

Performance Indicator	0–10,000				10,001–50,000				50,001–100,000			
	Top Quartile	Median	Bottom Quartile	Count	Top Quartile	Median	Bottom Quartile	Count	Top Quartile	Median	Bottom Quartile	Count
Water Produced (MGD per Employee)	0.11	0.09	0.08	7	0.30	0.19	0.11	21	0.25	0.17	0.13	21
Current Water Demand (%)	22%	39%	43%	5	36%	40%	58%	17	35%	47%	69%	16
Available Water Supply (years)	66	48	35	4	65	32	22	17	58	39	19	14
Energy Consumption Efficiency for Water (kBtu/yr./MG)	3,248	5,345	14,757	5	1,235	4,561	7,785	20	4,835	6,408	8,153	16
TOTAL O&M Cost of Potable Water Services ($/Account)	$353	$573	$679	7	$294	$376	$693	21	$234	$349	$499	19
TOTAL O&M Cost of Potable Water Services ($/MGD)	$3,149	$3,806	$4,386	6	$1,602	$2,006	$5,139	17	$1,942	$2,957	$4,436	16
TOTAL O&M Cost of Potable Water Services ($/100 miles of pipe)	$1,139,168	$2,722,222	$3,426,379	7	$1,031,954	$1,990,797	$3,592,191	20	$1,482,692	$1,950,201	$3,066,074	19
Treatment O&M Cost of Water Service ($/MG)	$488	$727	$1,082	4	$426	$628	$1,229	12	$506	$572	$1,293	11
Distribution O&M Cost of Water Service ($/100 miles of pipe)	$150,884	$313,755	$462,726	6	$370,748	$546,595	$771,494	14	$426,785	$671,630	$842,206	14
O&M %—Water Supply	4.6%	6.9%	19.7%	4	16.3%	33.5%	51.5%	12	8.4%	13.0%	20.9%	8
O&M %—Water Treatment	18.5%	29.2%	49.4%	4	12.2%	28.6%	54.0%	13	12.4%	24.9%	33.9%	12
O&M %—Water Transmission and Distribution	10.5%	12.3%	15.2%	6	19.2%	31.5%	58.0%	16	22.9%	34.2%	39.7%	13
O&M %—Water Support Services provided by others	9.4%	48.8%	61.6%	5	4.9%	10.3%	24.8%	7	27.3%	33.4%	42.3%	8
Planned maintenance Ratio (as % of total maintenance)—WATER	71%	62%	51%	6	80%	67%	42%	19	77%	67%	58%	13
Corrective maintenance to Water Production (hrs/MG)	0.5	1.0	1.8	6	0.5	1.6	3.1	19	0.2	0.5	0.9	13
Planned maintenance to Water Production (hrs/MG)	2.4	2.1	1.7	6	8.1	3.9	0.3	19	2.6	1.1	0.5	13
Corrective maintenance to Water Distribution (hrs/100 miles)	229	906	1,513	6	766	1,677	2,266	18	253	339	853	13
Planned maintenance to Water Distribution (hrs/100 miles)	2,092	1,146	621	6	4,836	2,016	482	16	3,715	972	647	13
Water Distribution System Integrity (leaks per 100 miles of pipe)	2.1	3.9	9.9	6	1.9	5.2	10.5	11	3.1	4.4	19.1	12
Water Distribution System Integrity (breaks per 100 miles of pipe)	6.5	10.4	17.9	6	1.8	5.3	9.0	14	2.7	5.7	11.4	12
Combined Leaks and Breaks (per 100 miles of pipe)	7.2	15.4	24.0	6	4.1	13.0	41.1	19	5.1	7.9	32.6	18

Metrics you can use

Water and wastewater utility managers need useful metrics to gauge how their organization is currently performing, and to set reasonable targets for future performance. The benchmarking data and analyses in this report are chosen for their usefulness in helping utilities track and improve both operational efficiency and managerial effectiveness.

Benchmarks for all operations

Utility managers can use the data and analyses in this report to determine how their utility's performance compares to the water or wastewater industry in five areas of operations: Organizational Development, Customer Relations, Business Operations, Water Operations, and Wastewater Operations. The report provides benchmarking data for 43 key performance indicators.

Compare your utility

Aggregate data are provided from 35 US states, the District of Columbia, 4 Canadian provinces, Guam, American Samoa, and Puerto Rico. Participating utilities range in size from under 10,000 population served to over 500,000 population served, summarizing performance data for the fiscal year 2015. Where data are available, historical trends from previous AWWA utility benchmarking surveys are also provided.

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Contract and Benchmarking Review

for the

Florida Governmental Utility Authority

July 2013

Utility and Management Consultants

Contract and Benchmarking Review

Florida Governmental Utility Authority

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A- Benchmarking calculations

B- FGUA Board presentation (June 20, 2013)

Section 1
Introduction and Purpose

Introduction

The Florida Governmental Utility Authority (FGUA) is a 15-county water and wastewater utility serving approximately 120,000 residential, commercial and industrial customers throughout the State of Florida. The FGUA was initially formed in 1999 through the acquisition of Avatar Utilities, and has grown over the past 14 years through additional acquisitions of primarily investor-owned utility systems. The current FGUA system, including the recently-acquired Florida operations of Aqua Utilities, is shown on Figure 1 below.

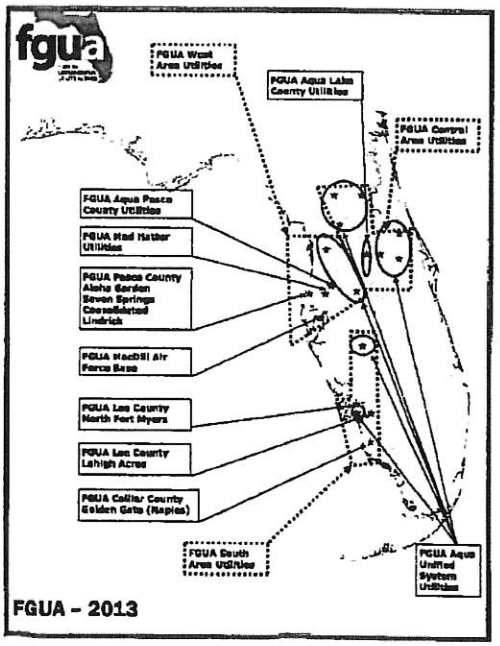

Figure 1
FGUA Operating Systems

The FGUA is managed by a six-member board comprised of key staff members from six counties across the state. The FGUA Board meets monthly either in person or via webcast. A unique feature of the FGUA is that it employs no permanent or temporary staff members, but rather contracts for all services, including management, operation and maintenance, legal support, accounting and rate review.

During the Board's annual strategic planning workshop held in February of 2013, the Board felt it necessary to assess the cost-effectiveness of the FGUA business model. Specifically, the Board asked for an independent, third-party review of the U.S. Water/Wade Trim (USWWT) Operations and Maintenance, Customer Service and Billing agreements and the Government Services Group (GSG)

Management Services Agreement, as well as benchmark operational metrics against similar water and wastewater systems across the United States. A review of the USWWT agreements are timely since the Aloha and Consolidated system contracts are scheduled for renewal in September of this year. In response to the Board request, Wetzel Consulting, LLC (WetCon) was contracted in March of 2013 to perform the independent review as requested.

Purpose of the Review

The two primary objectives of the review process conducted by WetCon were to:

1. Review the USWWT and GSG agreements and recommend changes that will improve workability, contract management efficiency and accountability; and
2. Benchmark the FGUA operations against similar water/wastewater utilities in order to assess cost-effectiveness and operational efficiency to insure that the customers are being well-served.

Scope of Services

The scope of services of the engagement involved six specific tasks as outlined below:

Task 1- Review of current USWWT and GSG agreements
Task 2- Meetings with GSG, USW and the FGUA Board
Task 3- Industry Benchmarking using AWWA QualServe methodology
Task 4- Develop and review recommendations with GSG staff, Utility and General Counsel and USW
Task 5- FGUA Board presentation
Task 6- Draft and Final Report

A presentation of preliminary results and recommendations was made to the FGUA Board at their monthly meeting on June 20, 2013 in Ft. Myers, FL. At that time, the Board authorized GSG and the attorneys to initiate negotiations with USW on the contract renewal based on the recommendations contained in the WetCon presentation, as attached in Appendix B.

This report does not analyze each agreement on a line-by-line basis, nor does it attempt to re-write the agreements, but rather leaves that to the negotiation process between the FGUA, USWWT and GSG. However, this report does identify significant issues with the agreements, and makes both short and long-term recommendations for contract improvement.

Section 2
U.S. Water/Wade Trim Contracts Review

Background

The joint venture of U.S. Water/Wade Trim LLC (USWWT) first became a service provider for the FGUA upon acquisition of the Aloha system in Pasco County. Subsequently, Lindrick, Consolidated, and North Ft. Myers joined the FGUA and then USWWT succeeded Severn Trent Services when their contracts for Lehigh and Golden Gate expired. The primary agreement that details the general terms and conditions of the USWWT service contract is entitled "*General Terms Agreement for Utility Operations, Maintenance, Billing and Customer Service*" (dated October 8, 2008 as amended on February 9, 2009), and includes a number of appendices that outline specific performance standards, reporting and insurance requirements, and pricing information. This agreement forms the basis for the individual Compensation Agreements unique to each system under contract to the FGUA. In addition, whenever USWWT undertakes construction activity related to system renewals and replacements or capital project implementation, a separate construction agreement is executed between the FGUA and USWWT for that specific project.

WetCon's review of these agreements included the General Terms Agreement, a representative sampling of the Compensation Agreements, and the Standard Construction Agreement dated October 27, 2005.

General Observations

While there are no "standard" contract operations agreements for the water and wastewater utility industry, the terms and conditions contained within the USWWT General Terms agreement are reasonably consistent with similar agreements WetCon has observed in the past, although the comprehensive nature of the services provided by USWWT makes this agreement a bit longer than is typical. The proof of success for such agreements has more to do with how they stand the test of time rather than the words contained within the document. In this case, these agreements have served the FGUA well over the past five years, as evidenced by:

- No significant contract disputes since initial contract execution in 2008;
- USWWT has maintained regulatory permit compliance throughout the time period;
- Customer surveys have been generally positive, particularly with respect to customer service, despite the high user rates inherent with the FGUA systems;
- Demonstrated ability to add and subtract systems to FGUA without service interruption;
- Favorable results from the benchmarking exercise included in this study and discussed in Section 4 of this report; and
- Successful completion of numerous projects utilizing the Standard Construction Agreement.

Contract Issues

A number of contract issues were identified and categorized into five major topic areas, as outlined below.

1. **Timeframe and Scope.** Currently, each new agreement between USWWT and the FGUA is given a five-year term from the date of contract execution. This results in a series of agreements with staggered timeframes, requiring individual renewals at the end dates of each contract. The agreements include a very comprehensive set of services, including operation and maintenance, customer service, meter reading, billing, and a right of first refusal for system renewals and replacement projects. The staggered timeframes limits FGUA's flexibility with regard to combining systems into larger service areas to achieve economies of scale or potentially segregating services into individual contracts.
2. **Repairs, Renewals and Replacements.** Most of the USWWT agreements combine repairs with renewals and replacements (R&R), and defines two categories (Basic and Major) of Renewals, Replacements and Repairs. Major Renewals, Replacements and Repairs are those where the contractor's direct costs exceed $7,500, while the basic category falls below that threshold. The $7,500 is treated as a deductible (unless the item was previously identified in a capital needs budget or pre-existing deficiency), and according to both USWWT and GSG personnel, represents the most contentious and time-consuming aspect of the agreements. More typically, repairs are included as part of a "Maintenance and Repair" budget and are generally considered the responsibility of the contractor, whereas R&R is treated as "Maintenance Capital", and is usually the responsibility of the utility owner. In fact, the recently executed Compensation Agreements for the Aqua systems separately defines repairs and R&R, and uses a $1,000 threshold to distinguish between a basic and major R&R project, while retaining the $7,500 direct cost threshold for major vs. basic repairs.
3. **Compensation.** There are a number of aspects of the FGUA operational model and the various contractual elements that impact the compensation received by USWWT. The first is that each system and its customers must be treated separately from a rates and fees perspective, thereby requiring allocation of all operating expenses across the various systems. This feature of FGUA will grow in complexity over time as additional utilities are added in the future. A second aspect of FGUA that impacts compensation is the lack of any reserve accounts to use for due diligence of potential acquisitions, thereby requiring at-risk due diligence services from USSWT, the cost of which is reimbursed through subsequent bond financing if and when the deal closes. A third aspect involves the use of the Consumer Price Index (CPI) for pricing adjustments on a yearly basis, but the particular CPI index varies across the various Compensation Agreements. A fourth compensation element involves the markup USWWT receives on direct costs for R&R projects, emergency repairs and other miscellaneous aspects of the agreements, currently calculated using 10% overhead and 8% profit (18% total markup). These numbers are on the high side of typical industry standards for such markups, which more commonly fall within the 12 to 15% range for the combined number. Finally, the agreements contain a number of hourly rates that although adjusted annually per the CPI adjustment, have not been reviewed since the initial contract execution in 2008.
4. **Performance and Stipulated Penalties.** Appendices A and B of the General Terms Agreement outline a series of performance standards for both O&M and Customer Service, while Section

5.01 details a number of stipulated penalties for specific non-performance issues. While the USWWT performance is evaluated on an ongoing basis by GSG, there is no annual, formal Performance Review process with pre-established Key Performance Indicators (KPIs) that can be articulated to the FGUA Board and reported back on an annual or semi-annual basis. In addition, a number of the stipulated penalties (referred to in the agreement as "liquidated damages") have limited relevance to FGUA system operation, have not been utilized during the past five years, and contain no justification for the dollar amounts specified in the agreement.

5. **Consumables.** Consumables in an O&M contract refer to the power, chemicals, water and fuel required to operate and maintain the utility system. The USWWT contracts generally make the contractor responsible for all consumables except power, which is a pass-through expense to the FGUA. Many utility owners prefer to take advantage of their own purchasing power and tax status to bulk-purchase chemicals and perhaps fuel. In fact, FGUA is engaging in a pilot study right now for this purpose.

In addition to the major categories identified above, there were also a few miscellaneous observations from the contracts that could be addressed in a renegotiation:

- The dispute resolution clause in the O&M agreement calls for mediation followed by litigation, rather than either binding or non-binding arbitration.
- There is no termination for convenience clause in the agreements.
- Meter testing and replacement clauses are confusing, as it is not clear which meters are to be replaced and which are to be tested on an annual basis.
- Training and safety programs are identified, but without detail as to number of training hours required of new employees and safety performance metrics expected from the contractor.

Short-term Recommendations

Given the immediate need to begin renegotiating the Aloha and Consolidated agreements, the recommendations are divided into two categories. The short-term recommendations are intended to be addressed as part of the current negotiations, while the long-term recommendations can be addressed over the next five years of operations or as deemed appropriate by the FGUA Board.

The recommendations below generally follow the issues as outlined above.

1. *Timeframe and Scope*- Reset all new agreements to the end date of the renewed Aloha and Consolidated agreements, which would be September 30, 2018 if tied to the FGUA fiscal calendar. The agreements can either be renewed with the Aloha and Consolidated agreements, or as they expire over the next few years. Consistent contract expiration dates will provide the FGUA flexibility in regionalizing the systems or segregating the services as 2018 approaches. There are no short-term recommendations to alter the scope of the USWWT engagement, nor to eliminate the right of first refusal for contract R&R, although we do encourage the FGUA to procure on-call contractors as appropriate for specialty R&R work.
2. *Repairs, Renewals and Replacements*- Clarify definitions consistent with industry standards, making repairs a contractor responsibility and R&R (as Maintenance Capital) the responsibility of FGUA. In this instance, capital expenditures are defined as those investments that significantly

extend the useful life of the asset (beyond one or two years), while repairs do not necessarily extend the useful life. The new agreements could adopt the recently executed Aqua agreements language, although that language does not eliminate the $7,500 deductible problem. An alternative approach used in other contracts is the establishment of a Maintenance and Repair Fund (as a subset of the O&M service fee) that is separately tracked during the year, with a shared penalty or benefit depending on whether the budget is exceeded or under-spent in any given year.

3. *Compensation-* A number of specific recommendations are made with respect to the various compensation issues identified:
    a. Continue cost allocations as per bond indenture requirements until such time as systems can be combined for future operational synergy and cost savings.
    b. Standardize pricing adjustments to the Consumer Price Index- U.S. City Average- All Urban Customers as published annually by the Bureau of Labor Statistics, U.S. Department of Labor, but include an annual cap of 4.5% consistent with the GSG contract (as discussed later in this report).
    c. Continue using Equivalent Residential Connection (ERC) as the growth metric upon which any increased/decreased base compensation will be received for any given system.
    d. Review and renegotiate as appropriate the 18% markup on direct expenses.
    e. Review all hourly rate schedules for consistency with industry standards.
4. *Performance and Stipulated Penalties-* Establish 5 to 10 Key Performance Indicators (KPIs) at the initiation of each contract year, and conduct a formal mid-year and end-of-year review to track performance against the established KPIs. Example KPIs might include year over year operating cost reductions, safety performance metrics (e.g. no lost time accidents), reduced energy consumption, reduced water loss rate or sewer overflow rate, improved billing accuracy and reduced number of customer complaints. The annual reviews can be used to monitor progress and establish a scorecard that can be used by the Board when deciding whether to renew or procure operational support services in the future. Eliminate the stipulated penalties clauses where possible, and replace where appropriate with more typical "cost to correct" language.
5. *Consumables-* Continue evaluating the bulk purchase of chemicals and other consumables. Create incentives for the contractor to monitor and reduce energy consumption, likely as part of the KPI process.
6. *Miscellaneous-* A few other general recommendations to address these issues include:
    a. Consider replacing litigation with arbitration, or at least including arbitration as an intermediate step between mediation and litigation in the process.
    b. Consider adding a termination for convenience clause into the contract, although such clauses tend to include a "termination fee" to compensate a contractor for mobilization costs that are generally amortized over the life of the contract. In the case of renewals, such mobilization costs are not relevant, but would be for any new acquisitions during the five-year renewal period.
    c. Clarify meter testing and replacement language such that residential meters are replaced on a 10-year cycle, and wholesale/commercial/industrial meters are calibrated annually and replaced when necessary.

Long-term Recommendations

A few long-term recommendations are provided for FGUA consideration over the next five years. These topic areas can be discussed as part of the utility's annual strategic planning process, or as needs dictate during the course of the year.

1. *Create flexibility for future procurements.* By establishing 2018 as the consistent end date for the renewed USWWT contracts, the FGUA Board can consider procuring services on a regional basis rather than through individual compensation agreements, or issuing separate contracts for various services. It is not unusual for utilities to contract for meter reading and billing or even all of customer service as a separate service, rather than have it included as part of the O&M service agreement. By implementing a formal performance review process, the FGUA Board can monitor performance against established KPIs, and thereby make a more informed decision about USWWT contract renewal as 2018 approaches.
2. *Establish regional systems to the extent possible.* Since it is likely that FGUA will continue to grow and add systems over the next five years, it would be prudent to consider consolidation of systems to benefit from operational synergies and reduce the number of rate tariffs and cost allocation requirements. We understand that such consolidation may be limited by bond requirements and the potential loss of systems to host counties, but continue to believe that this would be in the best long-term interests of the customers.
3. *Implement performance-based compensation.* The natural extension of a formal performance review process is the implementation of performance-based compensation. This might involve having a range of profit percentages earned by the contractor depending on their annual KPI scorecard results, or the establishment of a bonus pool funded out of a shared savings fund created through cost saving measures, such as energy reduction or staff reductions attained through technology enhancements.
4. *Consider Advanced Metering Infrastructure (AMI).* Since only a portion of the Aqua system currently uses Automatic Meter Reading (AMR) technology, the FGUA systems are prime candidates for AMI, a satellite-based metering approach that can reduce meter reading labor costs and improve billing accuracy. An initial step might be a business case analysis looking at AMI for all or a portion of the FGUA systems, and perhaps a pilot implementation step for one or more of the systems under consideration.
5. *Reduce at-risk due diligence.* While we understand the need for at-risk due diligence given the unique bond and financial constraints of the FGUA, reducing the utility's reliance on this process is encouraged. Creation of regional entities might allow for the creation of a reserve fund for each entity for future acquisition considerations. In the interim, it seems prudent to continue down the at-risk due diligence path with USWWT for potential acquisitions that are either large or within current FGUA service area boundaries. For smaller systems, especially those in more remote locations, there are other operations firms that would bid on operations contracts at their expense as part of an RFP process, thereby transferring the due diligence cost and operational risk to those contractors.

Section 3
Government Services Group Contract Review

Background

The Government Services Group, Inc. (GSG) has provided administration, management and other support services to the FGUA since the creation of the utility in 1999. With the exception of MacDill AFB, the current contract is dated February 19, 2009, and as amended on January 17, 2013, now extends to September 30, 2019. Unlike the multiple compensation agreements that exist with the USWWT contracts, GSG's contract is one document that must be amended each time new systems are added, deleted or additional services are incorporated.

The WetCon review of the GSG contract included three specific areas:

- Timeframe
- Compensation and Pricing Adjustments
- Contract Oversight

Timeframe

With the extension of the GSG contract to September 30, 2019, this contract is now set at one year past the recommended end date for the renegotiated USWWT agreements. In our judgment, establishing the GSG contract end date one year past the O&M contract is a prudent strategy and is recommended for the future.

Compensation and Pricing Adjustments

There are a number of separate pricing elements contained within the GSG contract, including the management fee, CIP administration fee, inspection services, developer review and additional services. Each of these service fees are considered below.

1. **Management Fee.** The Management Fee is calculated from a staffing plan developed each year, with raw salary marked up by fringe benefits, overhead and profit, yielding a lump sum fee spread across all FGUA systems, which is then allocated to each system proportional to the number of customers. Although the profit percentage used in the calculation is a bit high at 20%, the overall multiplier of 2.42 is below industry standards for these types of services. *We are therefore recommending no change in this component of the GSG compensation package.*
2. **CIP Administration Fee.** The same basic approach to determination of a lump sum fee is used for CIP Administration as is used for the Management Fee, except that the staffing plan is adjusted based on the anticipated capital needs of the systems in any given year. These costs are

then allocated to each system proportional to the size of their individual CIP. *No change is recommended to the current approach to CIP administration fees.*

3. **Inspection Services.** Inspection services are charged on an hourly rate basis based on timesheet entries by the individual inspectors assigned to each individual project. Charging to each project based on the actual time spent in the field looking at the construction is the appropriate approach and should be continued. However, the formula used to determine the hourly rates results in a labor multiplier of 3.91, which is above market rate for field inspection services. *We therefore recommend that these rates be reviewed and renegotiated as appropriate.*
4. **Development Review Services.** GSG staff provide developer review services in much the same way as any utility would review the plans and specifications for developer-built utility systems (pipelines, service laterals, lift stations, etc). The fees charged to the developers are market-based fees consistent with other utilities across central Florida, but the costs incurred by GSG typically exceed the recovered fees. GSG may request supplemental funding for these services, but has chosen not to do so in the past. *No change is recommended to the current approach to Development Review Services.*
5. **Additional Services.** Any additional services charged to the FGUA by GSG utilize a standard hourly rate schedule, which like the schedule contained within the USWWT agreements, has been adjusted but not reviewed since 2009. *This schedule should be reviewed for its appropriateness and consistency with local engineering rate schedules.*

The GSG contract allows for pricing adjustments for two primary purposes:

- Annual increases in unit rates based on the same CPI adjustment included in the USWWT contract, with the 4.5% cap included.
- Increase (or decrease) in the Management Fee to accommodate system growth calculated at 75% of the average change in the number of water and wastewater accounts.

Each of these approaches is reasonable and should be continued into the future.

Contract Oversight

A basic philosophy of the FGUA is to operate the utility systems with no full-time staff members, but rather to contract for all services, including utility administration and management. As System Manager, GSG provides all of the typical management, procurement, administration, financial planning and accounting, engineering review, capital planning and oversight, and inspection services normally provided by utility staff members. In that capacity, they provide ongoing oversight to the USWWT contracts, as well as other contract service providers such as the engineering designers, construction contractors, rate consultants and others. An important question is therefore who and how does the FGUA provide oversight of the GSG contract?

The most important answer to the question of GSG contract oversight is that all GSG task orders, irrespective of size, must be approved by the FGUA Board. In addition, pricing discussions are held in advance with the FGUA General Counsel. WetCon interviewed Mr. Pelham during the course of this study, and determined that he is generally satisfied with the process and his ability to review each task

order for scope and fee appropriateness. One area of concern as articulated by Mr. Pelham is distinguishing between what should be included in the basic services vs. the need for additional services task authorizations. The most common example of this is the public outreach component of system management, the scope of which consistently exceeds the scope as anticipated and described in the basic services agreement. The higher levels of service are a function of ongoing acquisition activity and high levels of customer interaction required within the FGUA customer base. If costs are consistently above those anticipated by the basic services agreement for any particular service type, the FGUA should consider amending the basic service fee rather than requiring additional task orders each year for those services.

The FGUA Board may deem it prudent to enhance the oversight element of the GSG contract in the future, particularly as the utility continues to grow and add customers over time. There are a number of ways to accomplish this, with varying levels of cost and commitment. Alternatives range from the hiring of full-time staff (an Executive Director, for example), to engaging a "trust consultant" on an ongoing basis, to performing an annual review of system management similar to the financial audit conducted by the audit firm each year. Hiring an Executive Director would represent a significant commitment of funds with limited benefit, as there is no guarantee that such a person would be any more qualified than the GSG System Manager, and in the event of systems being taken back by their county governments, the salary and fringe benefit costs for such a person would need to be spread across a smaller customer base. Trust consultants or bond engineers are often employed when bond indentures require an annual, independent review of the system operations and CIP execution, in order to represent the best interests of the bondholders. FGUA has recently retained Brown and Caldwell as Engineer for Indenture Compliance for their 2010 bond issue, but they are not specifically tasked with reviewing the GSG contract or system management. *The simplest and most cost-effective approach to providing additional oversight would be to retain an individual or firm to provide an annual Management Review of the FGUA, to insure that the services provided by GSG are in accordance with their contract and are consistent with the best interests of the FGUA customer base.*

Finally, as in the case of the USWWT agreements, the GSG contract has no provision for a formal, annual performance review based on a pre-established set of KPIs. We believe this would be a valuable exercise, and *recommend such an annual performance review process be incorporated into the GSG service contract going forward.*

Section 4
Utility Industry Benchmarking

Objectives and Approach

The primary objective of any benchmarking initiative is to build a performance measurement system specific to water and wastewater utilities, and utilize that measurement system and database to help other utilities improve operational efficiency and performance. There are a number of benchmarking algorithms and products in the utility marketplace, but many are specific to either water or wastewater, or to a component of the utility operations like treatment plants or pump stations. In 2005, the American Water Works Association (AWWA) teamed with the Water Environment Federation (WEF) and the AWWA Research Foundation to develop a benchmarking methodology and database applicable to both water and wastewater utilities across North America. The approach incorporated the QualServe business system previously developed for utility audits as an organizing framework, with an initial database of 350 water and wastewater utilities.

The original report entitled *2005 Benchmarking Performance Indicators for Water and Wastewater Utilities: Survey Data and Analyses Report* was published by AWWA and WEF, with annual updates prepared in 2006 and 2007. No updates to the 2007 document were available until late 2012, when the 2011 version of the document with the same name as above was published by the AWWA. It is this 2011 version that was used for the benchmarking exercise outlined in this section of the report.

The AWWA benchmarking process includes 38 performance indicators (22 indicators in 2005) and 102 total utility participants, with 59 of those being both water and wastewater utility systems. Of the 38 performance indicators, we selected 11 for evaluation of FGUA compared with the 59 water/wastewater systems nationwide. The FGUA data were also compared with a subset of the total pool of participants representing the Southern Region of the US, including Florida. The database presents the results for the participants as the top quartile (top 25% of the surveyed utilities), median and bottom quartile. FGUA data were compiled for the Western systems (including Pasco, Mad Hatter, Lindrick, Consolidated and Aloha), the Southern systems (Golden Gate, Lehigh Acres and North Ft. Myers) and the combined systems. The Aqua systems were not included given the limited data available at this time from these new acquisitions, but it will be interesting to perform this exercise again in a year or two to contrast the Aqua systems with the other existing systems in FGUA.

Benchmarking Results

The results of the FGUA benchmarking exercise are summarized on Table 1 on the following page.

Table 1

FGUA Benchmarking Summary

Metric	Basis	All Utilities			South Utilities			FGUA		
		Top	Median	Bottom	Top	Median	Bottom	South	West	Total
Customer Service Cost	$/account	39.43	48.34	64.16	36.43	41.16	52.38	50.58	38.51	44.55
O&M Cost	$/account-water	210	340	470	233	257	331	213	225	219
	$/account-sewer	271	344	468	259	345	426			
	$/MG processed-water	1540	2002	2596	1627	1843	1939	2365	2914	2633
	$/MG processed-sewer	1535	2784	3673	954	1198	1280			
Debt ratio	%	17.9	31.6	47.8	22.2	41	53.1	65.4	99.4	78.8
Water rates	$/month	20.17	25.86	33.59	20.2	22.47	25.14	58.89	54.80	56.54
Sewer rates	$/month	21.59	28.54	38.81	21.26	27.73	29.51	71.38	68.18	69.91
No. of employees	Accounts/employee-water	730	479	389	789	718	493	562	1004	783
	Accounts/employee-sewer	849	504	388	648	535	460			
	MGD/employee-water	0.36	0.25	0.19	0.32	0.26	0.18	0.15	0.19	0.17
	MGD/employee-sewer	0.32	0.2	0.15	0.48	0.37	0.25			
Water loss rate	%	1.14	4.99	7.85	0.76	5.4	13.9	12.9	11.9	12.4
Sewer overflow rate	Overflows/100 miles pipe	0.9	1.7	4.2	1.53	3.05	11.5	2.53	3.74	3.14
Customer complaints	#/1000 customers	2.63	11.4	30.4	1.35	3.09	12.6	4.27	22.1	14

Analysis and Recommendations

It is virtually impossible to find any two water utilities that are comparable, given their unique treatment systems, customer bases, permit requirements, operational procedures, capital needs and rate structures. This is particularly true when comparing other systems to FGUA, with its' geographic spread, diverse customer base and broad range of treatment technologies. Nevertheless, comparing performance metrics of the FGUA with other utilities has value, at least in determining whether the operational metrics fall within reasonable ranges of values.

An analysis of the various performance metrics for FGUA as compared with other systems nationwide provides the following conclusions:

1. **Customer Service Costs-** FGUA's costs are comparable to those of the participating utilities both nationally and across the south. The FGUA numbers are actually skewed a bit on the high side by the South systems, where three Customer Service Centers are operated compared with only one center in the west.
2. **O&M Costs-** The FGUA O&M cost on a per account basis falls within the top quartile of other utilities, but toward the bottom quartile on a cost per million gallons processed basis. The best explanation for this phenomenon is that FGUA customers use about 4500 gallons per month on average, while the average usage for the benchmarked utilities in closer to 6500 gallons per month.
3. **Debt ratio-** The average debt ratio (total liabilities/total assets) across all FGUA systems exceeds 78%, substantially above the bottom quartile across the US and the South. This was an expected result, given the high price of the FGUA acquisitions, deteriorated asset condition, and recent timing of many of those acquisitions, especially for the Western systems in Pasco County. Over time, this ratio will reduce as bonds are paid down for any particular system, but may not help FGUA overall as it continues to acquire new systems each year.
4. **Water/Sewer rates-** It is also not surprising that the average water and sewer rates for the FGUA systems exceed the bottom quartile for rates from the surveyed utilities. However, since we've discovered that the average operating cost per account is low to average, the high rates are being driven by the high debt service from acquisition and capital improvement needs.
5. **Number of Employees-** This metric attempts to evaluate whether a utility is being operated with the correct number of employees. The results in this instance are very similar to the operating cost comparison (not surprising since labor costs are the biggest driver of operational expense), where the number of accounts served per employee is within the top quartile of performance, but the number of MGDs produced per employee is in the bottom quartile. Once again this difference is driven by the average water usage per customer being 40% lower for the FGUA systems.
6. **Water Loss Rate-** The numbers on Table 1 would appear to indicate that water loss in FGUA is in the bottom quartile of performance. However, previous experience in Florida (where bacterial regrowth requires excessive hydrant flushing) indicates that an apparent loss rate (non-revenue water percentage) of between 10 and 15% is excellent.
7. **Sewer Overflow Rate-** Overflow rates of around 3 overflows per 100 miles of pipe per month is right around the median number for the benchmarked utilities. It should be noted that wet weather

conditions resulting in flooding and system infiltration/inflow are excluded from these calculations.

8. **Customer complaints**- The benchmarking data actually separate complaints into two separate categories—customer service complaints resulting from billing errors or customer service problems and technical quality complaints resulting from water quality, odors or other technically-based issues. The FGUA customer service call centers do not distinguish between these types of complaints, hence we have combined the two types from the data base and compared the sum of the two with the FGUA complaint results. In this case, while the overall number is toward the bottom quartile of performance, there is a dramatic difference between the South and West systems, with the West showing five times the number of complaints than the South. This difference is believed to be the result of higher rates and newer acquisitions in the West, and the fact that the call centers do not differentiate between an "inquiry" and a "complaint". This metric require improved data collection for accurate assessment in the future.

In addition to the metrics discussed above, there were other metrics of interest to the FGUA for which the operational data does not exist at this time. Specifically, it would be interesting to track the billing accuracy (number of adjustments per 10,000 bills sent), and the system renewal and replacement (R&R) rate as a percentage of total system assets. Current contractor billing adjustment data do not distinguish errors from other routine adjustments, such as deposit referrals.

It is recommended that FGUA revisit the benchmarking effort in another year or two when the Aqua systems are fully integrated and the operational processes stabilized. It is further recommended that any of the benchmarking data of interest to the FGUA be collected consistent with the numerical values reported for inclusion in future analyses.

Section 5
Conclusions and Recommendations

Conclusions

The following summarizes the fundamental conclusions from the Contract and Benchmarking Review conducted by WetCon.

- The USWWT team and the various agreements outlining the services provided have served the FGUA and its' customers well over the past five years.
- A number of issues have been identified through our review of the USWWT agreements and discussions with GSG, USW, General Counsel and Utility Counsel, including:
    - Staggered timeframes for each system agreement
    - Limited flexibility in pricing
    - Utilizing one contractor for comprehensive set of services (O&M, customer service, meter reading, billing, R&R)
    - Individual systems require complicated cost allocation
    - At-risk due diligence
    - Responsibility/payment for consumables (power, chemicals, fuel)
    - Stipulated penalties generally not practical
    - No formal annual performance review process (KPIs)
    - No "termination for convenience" clause
    - Inconsistent application of CPI adjustments
    - Contractor mark-ups (10% + 8%) on the high side
    - Hourly rates not reviewed in five years
- A series of short-term and long-term recommendations have been made to address the above contract issues.
- GSG has been a valuable partner to the FGUA since 1999, and its current agreement extends through September 30, 2019. It has been recognized for providing quality management services by both independent bond rating agencies and annual FGUA Board reviews.
- The GSG agreement was reviewed and a series of recommendations presented related to timeframe, compensation, pricing adjustments and oversight.
- A benchmarking exercise was completed, comparing a number of FGUA operational metrics with water and wastewater utilities both across the U.S. and the southern states.
- FGUA compares favorably with the benchmarked utilities in the areas of customer service cost, O&M cost, number of employees, water loss rate and sewer overflow rate.
- FGUA compares less favorably with the other utilities in the areas of debt ratio, water and sewer rates and customer complaints, although the customer complaint data may be skewed by inquiry calls being labeled as complaints.

Summary of Recommendations

A number of recommendations are included throughout the previous sections of this report. Those recommendations are summarized below for ease of review and tracking of the implementation process moving forward.

USWWT Agreements (Short-term)

1. Reset all subsequent contract end dates to the renegotiated Aloha and Consolidated agreements, likely sometime in the fall of 2018.
2. Redefine "repairs" as distinct from "renewals and replacements", and simplify the $7,500 deductible issue, either by adopting the language in the Aqua agreements or establishing new contract language.
3. Do not modify "right of first refusal" language for R&R implementation, but proceed with procurement of on-call specialty contractors as appropriate.
4. Consistently apply the CPI- U.S. City Average-All Urban Customers to index pricing adjustments across all compensation agreements, and add a 4.5% cap consistent with the GSG agreement.
5. Review and renegotiate the 18% markup on direct costs.
6. Review hourly rates for consistency with local marketplace and adjust as necessary.
7. Develop a formal annual performance review process to include 5 to 10 mutually acceptable Key Performance Indicators (KPIs) as part of an ongoing monitoring and continuous improvement business process.
8. Eliminate stipulated penalties (liquidated damages) where appropriate, and clarify for workability.
9. Continue investigation of bulk chemical purchasing and incentivize operational energy savings.
10. Add a "termination for convenience" clause.
11. Clarify meter testing and replacement language.

USWWT Agreements (Long-term)

1. Create flexibility for future procurements by looking at regional operations and/or segregation of services.
2. Consider regional consolidation of systems to enhance efficiencies and improve customer service to the extent practical and permitted by bond covenants.
3. Implement performance-based compensation as a natural outgrowth of the KPIs and annual performance review process.
4. Consider implementation of Advanced Metering Infrastructure (AMI) to reduce field services costs and improve reliability and billing accuracy.
5. Reduce FGUA dependence on at-risk due diligence for future acquisitions.

GSG Agreement

1. Maintain GSG contract timeframe end date at one year past end date for O&M agreement.
2. Retain current pricing model for Management Fee, CIP Administration Fee and Developer Review services.

3. Review and renegotiate pricing for inspection services.
4. Review hourly rate schedule for consistency with local marketplace.
5. Maintain current approach to pricing adjustments for both inflation and system growth.
6. Conduct an annual Management Review of GSG services to ensure consistency with the contract requirements.
7. Develop an annual performance review process to include 5 to 10 KPIs, similar to the USWWT recommendations.

Benchmarking

1. Conduct a similar benchmarking analysis in one to two years to include the recently acquired Aqua systems.
2. Collect customer complaint data (both customer service and technical quality) consistent with the AWWA approach for future benchmarking activities.
3. Collect billing accuracy data consistent with AWWA approach and add metric to future benchmarking analyses