

State of Florida



Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

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

DATE: August 20, 2020

TO: Office of Commission Clerk (Teitzman)

FROM: Division of Engineering (Lewis, Ramos) *TB*
Division of Accounting and Finance (Richards, D. Brown) *MC ALM*
Division of Economics (Bethea) *JGH*
Office of the General Counsel (Dziechciarz) *TLI*

RE: Docket No. 20200168-WU – Application for staff-assisted rate case in Polk County, and request for interim rate increase, by McLeod Gardens Utilities, LLC.

AGENDA: 09/01/20 – Regular Agenda – Decision on Interim Rates – Participation is at the Discretion of the Commission

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Brown

CRITICAL DATES: 11/12/21 (15-Month Effective Date (Staff-assisted rate case))

SPECIAL INSTRUCTIONS: None

Case Background

McLeod Gardens Utilities, LLC (McLeod or Utility) is a Class C utility serving approximately 96 residential water customers in Polk County. The Utility was transferred to the present operator in 2016.¹ McLeod's rates and charges were approved in its last staff-assisted rate case in 2002 when the Utility was known as McLeod Gardens Water Company.² Subsequent to the

¹Order No. PSC-2017-0367-PAA-WU, issued September 29, 2017, in Docket No. 20160193-WU, *In re: Application for approval of transfer of certain water facilities and Certificate No. 619-W from McLeod Gardens Water Company to McLeod Gardens Utilities, LLC, in Polk County.*

²Order No. PSC-02-1733-PAA-WU, issued December 9, 2002, in Docket No. 20011677-WU, *In re: Application for staff-assisted rate case in Polk County by Tevalo, Inc. d/b/a McLeod Gardens Water Company.*

Docket No. 20200168-WU

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Utility's last rate case, its rates have been amended through five price index increases. According to McLeod's 2019 Annual Report, total gross revenue was \$33,563 and total operating expense was \$41,418.

On June 19, 2020, McLeod filed an application for a staff-assisted rate case. A test year ended December 31, 2019, has been established for the purposes of interim and final rates.

This recommendation addresses the Utility's request for interim rates. The Commission has jurisdiction pursuant to Sections 367.082 and 367.0814(4), Florida Statutes (F.S).

Discussion of Issues

Issue 1: Should an interim revenue increase be approved?

Recommendation: Yes. McLeod should be authorized to collect interim revenues as indicated below:

	Test Year Revenues	\$ Increase	Revenue Requirement	% Increase
Water	\$33,563	\$2,608	\$36,171	7.77%

(Richards, D. Brown)

Staff Analysis: On June 19, 2020, McLeod filed an application requesting an interim revenue increase in its water rates. Section 367.0814(4), F.S., details the criteria for evaluating a request for an interim rate increase for staff-assisted rate cases.

Section 367.0814(4), F.S., states:

The Commission may, upon its own motion, or upon petition from the regulated utility, authorized the collection of interim rates until the effective date of the final order. Such interim rates may be based upon a test period different from the test period used in the request for permanent rate relief. To establish interim relief, there must be a demonstration that the operation and maintenance expenses exceed the revenues of the regulated utility, and interim rates shall not exceed the level necessary to cover operation and maintenance expenses as defined by the Uniform System of Accounts for Class C Water and Wastewater Utilities (1996) of the National Association of Regulatory Utility Commissioners.

Staff has reviewed the Utility's operation and maintenance (O&M) expenses in relation to its revenues. Based on the Utility's filing, staff recommends that McLeod has demonstrated a *prima facie* entitlement to an interim rate increase in accordance with Section 367.0814(4), F.S.

Revenue Increase

In order to establish interim rate relief as prescribed by Section 367.0814(4), F.S., staff used the Utility's revenues reflected in its 2019 Annual Report for the test year ended December 31, 2019. The test year revenues are \$33,563, which includes \$31,790 from water service rates and \$1,773 from miscellaneous service revenues. The test year O&M expenses are \$36,054. The difference between the Utility's reported revenues and O&M expenses is \$2,491.

In addition, the interim water increase should be grossed up to include regulatory assessment fees (RAFs). The Commission has previously determined that it would be inappropriate to approve an increase in a utility's rates to cover its operating expenses and deny that same utility the funds to pay RAFs.³ Furthermore, by approving an interim rate increase that allows for the

³Order No. PSC-01-1654-FOF-WS, issued August 13, 2001, in Docket No. 20010396-WS, *In re: Application for staff-assisted rate case in Brevard County by Burkim Enterprises, Inc.*

payment of RAFs, the Utility should be able to fully cover its O&M expenses. The RAFs associated with the interim increase equal \$117.

In total, McLeod should be allowed an interim water revenue increase of \$2,608 (\$2,491 + \$117) to produce revenues sufficient to cover O&M expenses and additional RAFs. Thus, staff recommends the appropriate interim revenue requirement should be \$36,171. This is a 7.77 percent increase above the Utility's test year revenues. Table 1-1 illustrates staff's interim increase calculation.

**Table 1-1
Determination of Interim Increase**

	Water
1. Utility Test Year O&M Expenses	\$36,054
2. Less: Utility Test Year Revenues	\$33,563
3. Revenues to Cover O&M Expenses	<u>\$2,491</u>
4. Interim Revenue Increase	\$2,491
5. RAFs on Interim Rate Increase	\$117
6. Total Interim Revenue Increase (\$)	<u>\$2,608</u>
7. Total Interim Revenue Increase (%)	7.77%

Source: Utility's 2019 Annual Report and staff's calculations.

Issue 2: What are the appropriate interim water rates?

Recommendation: The recommended interim rate increase of 8.20 percent for water should be applied as an across-the-board increase to the service rates in effect as of December 31, 2019. The rates, as shown on Schedule No. 1, should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code (F.A.C.). The Utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. In addition, the approved rates should not be implemented until the required security has been filed, staff has approved the proposed customer notice, and the notice has been received by the customers. The Utility should provide proof of the date notice was given within 10 days of the date of the notice. (Bethea)

Staff Analysis: Staff recommends that interim service rates for McLeod be designed to allow the Utility the opportunity to generate annual operating revenues of \$36,171 for water. Before removal of miscellaneous revenues, this would result in an increase of \$2,608 (7.77 percent). To determine the appropriate increase to apply to the service rates, miscellaneous revenues should be removed from the test year revenues. The calculation is as follows:

**Table 2-1
Percentage Service Rate Increase**

	<u>Water</u>
1 Total Test Year Revenues	\$33,563
2 Less: Miscellaneous Revenues	<u>\$1,773</u>
3 Test Year Revenues from Service Rates	\$31,790
4 Revenue Increase	<u>\$2,608</u>
5 Percentage Service Rate Increase (Line 4/Line 3)	8.20%

Source: Staff's Interim Recommended Revenue Requirement

Staff recommends that the interim rate increase of 8.20 percent for water be applied as an across-the-board increase to the service rates in effect as of December 31, 2019.⁴ The rates, as shown on Schedule No. 1 should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), F.A.C. The Utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. In addition, the approved rates should not be implemented until the required security has been filed, staff has approved the proposed customer notice, and the notice has been received by the customers. The Utility should provide proof of the date notice was given within 10 days of the date of the notice.

⁴The Utility had a 2020 price index effective June 5, 2020. Interim rate increases are applied to rates in effect at the end of the test year.

Issue 3: What is the appropriate security to guarantee the interim increase?

Recommendation: The Utility should be required to open an escrow account or secure a surety bond or letter of credit to guarantee any potential refund of revenues collected under interim conditions. If the security provided is an escrow account, the Utility should deposit \$217 into the escrow account each month. Otherwise, the surety bond or letter of credit should be in the amount of \$1,736. Pursuant to Rule 25-30.360(6), F.A.C., the Utility should provide a report by the 20th of each month indicating the monthly and total revenue collected subject to refund. Should a refund be required, the refund should be with interest and in accordance with Rule 25-30.360, F.A.C. (Richards, D. Brown)

Staff Analysis: Pursuant to Section 367.082, F.S., revenues collected under interim rates shall be placed under bond, escrow, letter of credit, or corporate undertaking subject to refund with interest at a rate ordered by the Commission. As recommended in Issue 1, the interim increase for water is \$2,608. In accordance with Rule 25-30.360, F.A.C., staff calculated the potential refund of revenues and interest collected under interim conditions to be \$1,736. This amount is based on an estimated eight months of revenue being collected under the recommended interim rates shown on Schedule No. 1.

The criteria for a corporate undertaking include sufficient liquidity, ownership equity, profitability, and interest coverage to guarantee any potential refund. Staff reviewed McLeod's financial condition. Because the Utility has no meaningful liquidity, has negative interest coverage, has reported significant net losses year over year, and has negative ownership equity, staff does not believe the Utility has the financial capability to support a corporate undertaking in the amount requested at this time. Instead, staff recommends that the Utility be required to secure a surety bond, letter of credit, or escrow agreement to guarantee any potential refund.

If security is provided through an escrow agreement, the following conditions should be part of the agreement:

- 1) The Commission Clerk, or his or her designee, must be a signatory to the escrow agreement.
- 2) No monies in the escrow account may be withdrawn by the Utility without the express approval of the Commission Clerk, or his or her designee.
- 3) The escrow account shall be an interest bearing account.
- 4) If a refund to the customers is required, all interest earned by the escrow account shall be distributed to the customers.
- 5) If a refund to the customers is not required, the interest earned by the escrow account shall revert to the Utility.
- 6) All information on the escrow account shall be available from the holder of the escrow account to a Commission representative at all times.
- 7) The amount of revenue subject to refund shall be deposited in the escrow account within seven days of receipt.
- 8) This escrow account is established by the direction of the Florida Public Service Commission for the purpose(s) set forth in its order requiring such account. Pursuant to *Cosentino v. Elson*, 263 So. 2d 253 (Fla. 3d DCA 1972), escrow accounts are not subject to garnishments.

- 9) The account must specify by whom and on whose behalf such monies were paid.

If the security provided is a surety bond or a letter of credit, said instrument should be in the amount of \$1,736. If the Utility chooses a surety bond as security, the surety bond should state that it will be released or terminated only upon subsequent order of the Commission. If the Utility chooses to provide a letter of credit as security, the letter of credit should state that it is irrevocable for the period it is in effect and that it will be in effect until a final Commission order is rendered releasing the funds to the Utility or requiring a refund.

In no instance should the maintenance and administrative costs associated with the refund be borne by the customers. These costs are the responsibility of, and should be borne by, the Utility. Irrespective of the form of security chosen by the Utility, an account of all monies received as a result of the rate increase should be maintained by the Utility. If a refund is ultimately required, it should be paid with interest calculated pursuant to Rule 25-30.360(4), F.A.C.

Issue 4: Should this docket be closed?

Recommendation: No. Staff recommends that this docket should remain open to address the merits of McLeod's staff-assisted rate case. (Dziechciarz)

Staff Analysis: Staff recommends that this docket should remain open to address the merits of McLeod's staff-assisted rate case.

MCLEOD GARDENS UTILITIES, LLC.		SCHEDULE NO. 1	
TEST YEAR ENDED DECEMBER 31, 2019		DOCKET NO. 20200168-WU	
MONTHLY WATER RATES			
	RATES IN EFFECT AS OF 12/31/2019 (1)	CURRENT RATES (2)	STAFF RECOMMENDED INTERIM RATES
<u>Residential and General Service</u>			
Base Facility Charge by Meter Size			
5/8"X3/4"	\$11.65	\$11.88	\$12.61
3/4"	\$17.48	\$17.82	\$18.92
1"	\$29.13	\$29.70	\$31.53
1-1/2"	\$58.25	\$59.40	\$63.05
2"	\$93.20	\$95.04	\$100.88
3"	\$186.40	\$190.08	\$201.76
4"	\$291.25	\$297.00	\$315.25
6"	\$582.50	\$594.03	\$630.50
Gallonage Charge			
Charge per 1,000 gallons - Residential and General Service	\$2.91	\$2.97	\$3.15
<u>Typical Residential 5/8" x 3/4" Meter Bill Comparison</u>			
2,000 Gallons	\$17.47	\$17.82	\$18.91
4,000 Gallons	\$23.29	\$23.76	\$25.21
6,000 Gallons	\$29.11	\$29.70	\$31.51
(1) The interim rate increase was applied to the rates in effect as of 12/31/2019.			
(2) The current rates became effective June 5, 2020 as a result of a price index.			