

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: November 23, 2004

TO: Director, Division of the Commission Clerk & Administrative Services (Bayó)

FROM: Division of Economic Regulation (Clapp, Lester, Walden)
Office of the General Counsel (Rodan)

RE: Docket No. 041141-WS – Application for certificates to provide water and wastewater service in Lake County by Hidden Valley SPE LLC d/b/a Orange Lake.
County: Lake

AGENDA: 12/07/04 – Regular Agenda – Proposed Agency Action for Issues 2 and 3 – Interested Persons May Participate

CRITICAL DATES: 12/23/04 - Statutory deadline for original certificate pursuant to Section 367.031, Florida Statutes)

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\041141.RCM.DOC

Case Background

On September 24, 2004, Hidden Valley SPE, LLC d/b/a Orange Lake (Orange Lake or utility) filed its application for original water and wastewater certificates in Lake County. The proposed area is located in the St. Johns River Water Management District (SJRWMD). Water use restrictions have been imposed district wide to encourage conservation. The water and wastewater systems at Orange Lake have been operated as part of a mobile home community with no separate charge for water service since 1985. In order to promote water conservation, Orange Lake was required by the SJRWMD to form a private utility capable of charging for water use. Orange Lake decided that this would be an appropriate time to begin charging for wastewater service. The utility is currently serving a total of 250 equivalent residential connections (ERCs). Orange Lake is at build out and has no plans for expansion.

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The utility's initial application met all of the filing requirements. Therefore, the application date of September 24, 2004, is the official filing date of the application. Pursuant to Section 367.031, Florida Statutes, the Commission shall grant or deny an application for certificates of authorization within 90 days after the official filing date of the completed application.

Orange Lake owns and operates the utility and the manufactured housing community that is located at 15840 State Road 50, Clermont, Florida, in Lake County. The utility has been providing water and wastewater service solely to the rental community tenants as a part of the rent, and was therefore exempt from Commission regulation pursuant to Section 367.022(5), Florida Statutes.

This recommendation addresses the application for original water and wastewater certificates and initial rates and charges. The Commission has jurisdiction pursuant to Sections 367.031 and 367.045, Florida Statutes.

Discussion of Issues

Issue 1: Should the Hidden Valley SPE LLC d/b/a Orange Lake application for water and wastewater certificates be granted?

Recommendation: Yes, Hidden Valley SPE LLC d/b/a Orange Lake should be granted Certificate Nos. 625-W and 536-S to serve the territory described in Attachment A effective the date of the Commission's vote. (Clapp, Walden, Romig)

Staff Analysis: As stated in the case background, Orange Lake filed its completed application for original water and wastewater certificates on September 24, 2004. The application is in compliance with the governing statute, Section 367.045, Florida Statutes, and Rule 25-30.033, Florida Administrative Code, and other administrative rules concerning an application for original certificate and initial rates and charges.

The notice of application for initial certificates was mailed to the customers on September 24, 2004. The Commission received responses from three customers. One could not be followed-up on because it was sent anonymously. However, the writer did not want to pay for water service. The second customer stated that the residents strongly objected to the application since they were informed when they moved in that the land rent included the cost of water and wastewater service. On October 13, 2004, staff sent a certified letter to the customer asking for a response by November 10, 2004, if the customer objected to the certification and wanted to go to hearing. The customer did not respond to staff's letter. The third customer expressed concern that the rates may be higher than the City of Clermont's. On November 1, 2004, staff sent a certified letter to the customer asking for a response by December 1, 2004, if the customer objected to the certification and wanted to go to hearing. At the time of the filing of this recommendation, the customer had not responded to staff's letter. Staff will continue to keep the customers informed of events scheduled in this docket.

The utility has provided adequate service territory and system maps and an adequate description of the territory requested. A description of the territory is appended to this memorandum as Attachment A. In addition, the application includes a recorded warranty deed as evidence that the utility owns the land upon which the utility facilities are located as required by Rule 25-30.033(1)(j), Florida Administrative Code.

As evidence of its financial and technical ability to provide water and wastewater service to the proposed area, Orange Lake has provided a statement from its grandparent corporation, Hometown America which has \$2.8 billion in assets, that it has and will continue to provide the financial stability required to maintain the utility in accordance with PSC standards and environmental regulations. Hometown America has acquired several mobile home parks by way of a merger with Chateau Communities, Inc., which include utilities that are regulated by this Commission, and are being processed as transfers of majority organizational control in Docket No. 030998-WS.

Regarding the applicant's technical ability, Orange Lake indicated that it will make the financial and operating commitment necessary for the utility to be successful in providing water and wastewater service to the residents within its service territory. The utility will continue to

retain the local management team that has operated the water and wastewater system for approximately 10 years. The utility is staffed with licensed and trained personnel and is committed to providing safe and reliable water and wastewater service to its customers.

The Orange Lake water treatment facility is made up of three wells with aeration and chlorination. One well is a low production well that will be taken off line and abandoned. Staff has contacted the Department of Environmental Protection (DEP) regarding the status of the water system. The DEP representative stated that the water system is in compliance with DEP regulations.

The utility's wastewater treatment facility is made up of collection lines, a 50,000 gallons per day treatment plant, and effluent disposal. Wastewater effluent is treated with chlorine and percolation ponds are used for disposal. The percolation ponds are two rapid infiltration basins on approximately 0.33 acres. DEP reported that the wastewater facilities are in compliance with DEP's requirements.

Based on the above information, staff believes it is in the public interest to grant the application for original water and wastewater certificates. Accordingly, staff recommends that Orange Lake be granted Certificate Nos. 625-W and 536-S to serve the territory described in Attachment A effective the date of the Commission's vote.

Issue 2: What are the appropriate initial water and wastewater rates and return on investment for this utility?

Recommendation: The utility's proposed water and wastewater rates and miscellaneous service charges described in the staff analysis should be approved. Orange Lake should charge the approved rates and charges until authorized to change them by this Commission in a subsequent proceeding. The utility should be required to notice all customers of the approved rates prior to billing for monthly water and wastewater service. The utility should also be required to file a proposed customer notice reflecting the Commission-approved rates within ten days of the date of the consummating order. The approved rates 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. A return on equity of 11.40% plus or minus 100 basis points should be approved. (Clapp, Walden, Lester)

Staff Analysis: Orange Lake submitted an original cost study for the water and wastewater systems in support of its proposed rates and charges. Orange Lake's proposed rates are based on its proposed rate base, cost of capital, customer growth, and operating and maintenance expenses. In reviewing the utility's proposed rates and charges, it appears that the utility's calculations are reasonable and consistent with those normally used by the Commission in setting initial rates and charges for a utility in existence, but not currently charging for service. The analysis below describes the utility's proposed initial rates and charges and return on investment for water and wastewater service.

PROJECTED RATE BASE

The utility's proposed rate base of \$220,440 for water and \$4,328 for wastewater are shown on Schedule No. 1. The rate base schedule is for informational purposes to establish initial rates and is not intended to formally establish rate base. This is consistent with Commission practice in original certificate applications.

Utility Plant in Service (UPIS) and Land

The proposed water UPIS of \$531,087 includes \$4,600 for approximately .92 acre of land and \$526,487 for structures and improvements, power generation equipment, wells and springs, supply mains, pumping equipment, treatment and distribution facilities, services, meters, hydrants, and backflow prevention devices. The utility indicated that the UPIS balances are the estimated original cost of the assets through December 31, 2004. The facilities are designed to serve the total build out of 250 ERCs.

The proposed wastewater UPIS of \$362,499 includes \$3,750 for approximately .75 acres of land and \$358,749 for structures and improvements, collection sewers, pumping equipment, treatment and disposal equipment, and services to customers. The utility indicated that the UPIS balances reflect the estimated original cost of the assets. The facilities are designed to serve total build out of the manufactured housing community.

Staff has reviewed the utility's UPIS costs and, based on the supporting documentation provided, the amounts appear reasonable. Therefore, staff recommends that the utility's

proposed balances of \$526,487 with \$4,600 for land and \$358,749 with \$3,750 for land for water and wastewater, respectively, be included in the UPIS and land accounts.

Accumulated Depreciation

The utility's proposed accumulated depreciation balances are \$255,976 and \$274,715 for water and wastewater, respectively, as of December 31, 2004. The accumulated depreciation balance was calculated using the guidelines for average service lives as set forth in Rule 25-30.140, Florida Administrative Code. Therefore, staff recommends that the utility's proposed balances of \$255,976 for water and \$274,715 for wastewater should be included in the accumulated depreciation accounts.

Contributions In Aid of Construction (CIAC)

Pursuant to Rule 25-30.570, Florida Administrative Code, if the amount of CIAC has not been recorded on the utility's books and the utility does not submit competent substantial evidence as to the amount of CIAC, the amount of CIAC shall be imputed to be the amount of plant costs charged to the cost of land sales for tax purposes if available, or the portion of the cost of the facilities and plant attributable to the water transmission and distribution system and the sewage collection system. The utility proposed CIAC balances of \$107,789 and \$178,699 for water and wastewater, respectively, based on the cost of the water transmission and distribution system and the wastewater collection system included in UPIS. Therefore, staff recommends CIAC balances of \$107,789 and \$178,699 for water and wastewater, respectively, should be included in rate base.

Accumulated Amortization of Contributions In Aid of Construction

The utility's proposed accumulated amortization of CIAC balances are \$53,118 and \$95,243 for water and wastewater, respectively. The accumulated amortization balance was calculated using the guidelines for average service lives as set forth in Rule 25-30.140, Florida Administrative Code. The proposed accumulated amortization balances appear to be reasonable. Therefore, staff recommends that accumulated amortization of CIAC of \$53,118 for water and \$95,243 for wastewater be included in rate base.

SUMMARY OF RATE BASE

Staff recommends that for purposes of setting initial rates and charges, the utility's proposed rate base of \$220,440 and \$4,328 for water and wastewater, respectively, as itemized above, appears to be reasonable and should be used to set initial rates for Orange Lake. The schedule of rate base is for informational purposes to establish initial rates and is not intended to formally establish rate base.

COST OF CAPITAL

The proposed capital structure for Oak Springs is shown on Schedule No. 2. Orange Lake proposed a cost of capital of 7.38% based on a cost of debt of 5.37%, a cost of equity of 11.40%, and a capital structure consisting of 33.35% equity and 66.65% debt. The cost rate for

common equity is based on the current leverage formula. (See Order No. PSC-04-0587-PAA-WS issued June 10, 2004 in Docket No. 040006-WS, In Re: Water and wastewater industry annual reestablishment of authorized range of return on common equity for water and wastewater utilities pursuant to Section 367.081(4)(f), F.S.). The capital structure and debt cost rate are based on the capital structure and debt cost of the parent company, Hometown America Holdings, LLC. Staff recommends that the utility's proposed cost of capital of 7.38% is reasonable. Further, staff recommends that the Commission establish Orange Lake's authorized return on equity at 11.40% with a range of plus or minus 100 basis points.

RETURN ON INVESTMENT

The utility's proposed return on investment is \$16,268 for water and \$319 for wastewater, as shown on Schedule No. 3. Staff recommends that a return on investment of \$16,268 for water and \$319 for wastewater be included in the utility's revenue requirement for setting initial rates.

REVENUE REQUIREMENT

The utility's proposed revenue requirements of \$56,454 and \$58,252 for water and wastewater, respectively, are based on its proposed rate base, cost of capital, operating and maintenance expenses, and customer base. The following analysis describes the utility's proposed revenue requirement.

Operating and Maintenance Expense

The utility's proposed operating and maintenance expenses for its water system of \$25,751 are based on current costs for purchased power, chemicals, materials and supplies, bad debt, miscellaneous expenses, and contractual services. Staff recommends that the amount appears to be reasonable and, therefore, \$25,751 should be included in the revenue requirement for operating and maintenance expense for water.

The utility's proposed operating and maintenance expenses for its wastewater system of \$53,463 are based on current costs for sludge removal, purchased power, chemicals, materials and supplies, bad debt, miscellaneous expenses, and contractual services. Staff recommends that the amount appears to be reasonable and, therefore, \$53,463 should be included in the revenue requirement for operating and maintenance expense for wastewater.

Net Depreciation and Amortization Expenses

The utility's proposed net depreciation and amortization expenses of \$9,919 for water and \$68 for wastewater are based on the guideline rates reflected in Rule 25-30.140, Florida Administrative Code. Staff recommends that the utility's net proposed depreciation and amortization expenses of \$9,919 and \$68 for water and wastewater, respectively, are reasonable and should be included in the revenue requirement.

Taxes Other Than Income and Income Taxes

The utility proposed taxes other than income for Orange Lake's water system of \$4,516 which includes regulatory assessment fees (RAFs) of 4.5% of gross revenues, payroll taxes of \$930, and property taxes of \$1,046. The utility's proposed payroll taxes, property taxes, and RAFs appear reasonable. Orange Lake's parent company is a limited partnership. The utility operation does not incur an income tax liability; therefore, no income tax expense was included in the proposed revenue requirement. Therefore, staff recommends that taxes other than income for water of \$4,516 should be included in the revenue requirement.

The proposed balance for taxes other than income for Orange Lake's wastewater system is \$4,402 which includes RAFs of 4.5% of gross revenues, payroll taxes of \$912 and property taxes of \$869. The utility's proposed payroll taxes, property taxes and RAFs appear reasonable. Orange Lake's parent company is a limited partnership. The utility operation does not incur an income tax liability; therefore, no income tax expense was included in the proposed revenue requirement. Therefore, staff recommends that taxes other than income for wastewater of \$4,402 should be included in the revenue requirement.

SUMMARY OF REVENUE REQUIREMENT

In summary, based on staff's analysis of the utility's proposed operating and maintenance expenses, depreciation, taxes other than income, and return on investment, staff recommends that the utility's proposed revenue requirement of \$56,454 and \$58,252 for water and wastewater, respectively, should be used in setting initial rates for Orange Lake.

RATES

As stated in the case background, as a part of its consumptive use permit, the SJRWMD required Orange Lake to form a private utility capable of charging for water use. Orange Lake decided that this would be an appropriate time to also begin charging for wastewater service. The utility's proposed residential and general service rates are based on a revenue requirement of \$56,454 for water and \$58,252 for wastewater. The requested rates include a base facility charge and gallonage charge which is considered a conservation rate structure. Since 2002, the utility has been separately metering all water use at each point of connection and providing that information to residents monthly without charging for the water service. Therefore, staff recommends that the utility's proposed water and wastewater rates for residential and general service customers be approved. The utility's requested monthly rates, along with a comparison of typical monthly bills, are shown on Schedule 4.

Miscellaneous Service Charges

The application contains a request for miscellaneous service charges. The utility's proposed miscellaneous service charges are in compliance with Rule 25-30.460, Florida Administrative Code, which defines four categories of miscellaneous service charges. Staff recommends that the proposed miscellaneous service charges for the utility are consistent with Commission rules and should be approved.

SUMMARY

The utility's proposed and staff recommended water and wastewater rates and miscellaneous service charges, as shown on Schedule No. 4 should be approved. Orange Lake should charge these rates and charges until authorized to change them by this Commission in a subsequent proceeding. The utility should be required to notice all customers of the approved rates prior to billing for monthly water and wastewater service. The utility should also be required to file a proposed customer notice reflecting the Commission-approved rates within ten days of the date of the order becoming final. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), Florida Administrative Code. A return on equity of 11.40% plus or minus 100 basis points should be approved.

Issue 3: What are the appropriate service availability charges for Hidden Valley SPE LLC d/b/a Orange Lake?

Recommendation: The proposed meter installation charge of \$200 should be approved for new connections made on or after the stamped approval date on the tariff sheets. (Clapp, Walden)

Staff Analysis: Rule 25-30.580(1)(a), Florida Administrative Code, provides that the maximum amount of contributions-in-aid-of-construction (CIAC), net of amortization, should not exceed 75% of the total original cost, net of accumulated depreciation, of the utility's facilities and plant when the facilities and plant are at their designed capacity. Rule 25-30.580(1)(b), Florida Administrative Code, provides that the minimum amount of CIAC should not be less than the percentage of such facilities and plant that is represented by the water transmission and distribution systems or the wastewater treatment and disposal systems.

The utility built all of the plant, distribution system, and disposal facilities within the existing territory. In 2002, the utility installed meters for all of its existing customers. The utility requested approval of a meter installation charge of \$200 for a 5/8"x3/4" meter. No other service availability charges were requested because the utility is near build out. The proposed meter installation charge appears reasonable. Therefore, staff recommends that the proposed meter installation charge of \$200 be approved for new connections made on or after the stamped approval date on the tariff sheets.

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Issue 4: Should this docket be closed?

Recommendation: Yes. If no timely protest is filed by a substantially affected person to proposed agency action Issues 2 and 3, a consummating order should be issued upon expiration of the protest period and the docket should be closed. (Rodan)

Staff Analysis: If no timely protest is filed by a substantially affected person to proposed agency action Issues 2 and 3, a consummating order should be issued upon expiration of the protest period and the docket should be closed.

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ATTACHMENT A

Hidden Valley SPE LLC d/b/a Orange Lake
Water and Wastewater Territory Description
Lake County

The Southeast 1/4 of the Northeast 1/4 of Section 27, Township 22 South, Range 26 East, Lake County, Florida, less the right of way for State Road 50.

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Hidden Valley SPE LLC d/b/a Orange Lake
Schedule of Water Rate Base

Schedule No. 1A

<u>DESCRIPTION</u>	<u>PROPOSED BY UTILITY</u>
Utility Plant in Service and Land	\$531,087
Accumulated Depreciation	(255,976)
CIAC	(107,789)
Accumulated Amortization of CIAC	<u>53,118</u>
RATE BASE	\$220,440

Hidden Valley SPE LLC d/b/a Orange Lake
Schedule of Wastewater Rate Base

Schedule No. 1B

<u>DESCRIPTION</u>	<u>PROPOSED BY UTILITY</u>
Utility Plant in Service	\$362,499
Accumulated Depreciation	(274,715)
CIAC	(178,699)
Accumulated Amortization of CIAC	<u>95,243</u>
RATE BASE	\$ 4,328

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Hidden Valley SPE LLC d/b/a Orange Lake
Capital Structure for Hometown America, LLC
Schedule of Cost of Capital

Schedule No. 2

<u>DESCRIPTION</u>	<u>BALANCE PER UTILITY</u>	<u>WEIGHT</u>	<u>COST RATE</u>	<u>WEIGHTED COST</u>
Common Equity	\$ 74,960	33.35%	11.40%	3.80%
Long - Term Debt	149,808	66.65%	5.37%	3.58%
Customer Deposits	0	0.0%	8.00%	0.00%
	\$224,768	100.0%		7.38%
Range of Reasonableness	High	Low		
Common Equity	12.40%	10.40%		

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Hidden Valley SPE LLC d/b/a Orange Lake
Schedule of Water and Wastewater Rate Base

Schedule No. 3

<u>DESCRIPTION</u>	<u>UTILITY PROPOSED WATER</u>	<u>UTILITY PROPOSED WASTEWATER</u>
Operating Revenues	<u>\$56,454</u>	<u>\$ 58,252</u>
Operating and Maintenance	25,751	53,463
Depreciation/Amortization Expense	9,919	68
Taxes Other Than Income	4,516	4,402
Income Taxes	<u>0</u>	<u>0</u>
Total Operating Expense	<u>40,186</u>	<u>57,933</u>
Return on Net Investment	<u>\$16,268</u>	<u>\$319</u>
Rate Base	\$220,440	\$4,328
Rate of Return	7.38%	7.38%

Hidden Valley SPE LLC d/b/a Orange Lake
 Schedule of Monthly Rates and Charges

Schedule No. 4

Monthly Service Rates
Residential & General Service

WATER

<u>Base Facility Charge</u>	
5/8" x 3/4"	\$ 8.62
Charge per 1,000 gallons	\$1.29

WASTEWATER

<u>Base Facility Charge</u>	
5/8" x 3/4"	\$7.99
Charge per 1,000 gallons	\$1.51
Residential cap of 8,000 gallons	

Typical Residential Bills

<u>5/8" x 3/4" meter</u>	Water	Wastewater
3,000 gallons	\$ 12.49	\$12.52
5,000 gallons	\$ 15.07	15.54
10,000 gallons	\$ 21.52	23.09

MISCELLANEOUS SERVICE CHARGES

	Water	Wastewater
Initial Connection	\$ 15.00	\$ 15.00
Normal Reconnection	15.00	15.00
Violation Reconnection	15.00	Actual
Premises Visit (in lieu of disconnection)	10.00	10.00