

State of Florida



## Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

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

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**DATE:** March 1, 2007

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

**FROM:** Division of Economic Regulation (Rendell, Rieger, Lingo, Springer, Kyle)  
Office of the General Counsel (Fleming)

**RE:** Docket No. 060260-WS – Application for increase in water and wastewater rates in Highlands County by Lake Placid Utilities, Inc.

**AGENDA:** 03/13/07 – Regular Agenda – Proposed Agency Action Except Issues 20 and 22 - Interested Persons May Participate

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** Pending

**CRITICAL DATES:** 03/13/07 (5-Month Effective Date (PAA Rate Case))

**SPECIAL INSTRUCTIONS:** None

**FILE NAME AND LOCATION:** S:\PSC\ECR\WP\060260.RCM.DOC

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### Case Background

Utilities, Inc. (UI or parent) is an Illinois corporation which owns approximately 80 utility subsidiaries throughout 16 states including 16 water and wastewater utilities within the State of Florida. Currently UI has ten separate rate case dockets pending before the Public Service Commission (Commission). These dockets are as follows:

<u>Docket No.</u>	<u>UI Subsidiary</u>
060253-WS	Utilities Inc. of Florida
060254-SU	Mid-County Services, Inc.
060255-SU	Tierra Verde Utilities, Inc.
060256-SU	Alafaya Utilities, Inc.
060257-WS	Cypress Lakes Utilities, Inc.
060258-WS	Sanlando Utilities, Inc.
060260-WS	Lake Placid Utilities, Inc.
060261-WS	Utilities Inc. of Pennbroke
060262-WS	Labrador Utilities, Inc.
060285-SU	Utilities Inc. of Sandalhaven

This recommendation addresses Docket No. 060260-WS.

Lake Placid Utilities, Inc. (Lake Placid or utility) is a Class C utility providing water and wastewater service to approximately 125 water and 194 wastewater customers in Highlands County. According to its 2005 annual report, Lake Placid reported revenues of \$45,173 and \$70,362 for water and wastewater, respectively. Lake Placid reported a net operating income of \$29,387 for water and a net operating loss of \$14,944 for wastewater.

On May 15, 2006, the utility filed its application for approval of a final and interim rate increase in this docket and requested that the Commission process the case under the Proposed Agency Action (PAA) procedure. After review of the Minimum Filing Requirements (MFRs), staff determined that the MFRs contained a number of deficiencies that required revisions by the utility. Those revisions were filed, and the official filing date for the utility's final rate increase was established as August 22, 2006.

The utility's requested test year for interim and final purposes is the historical test year ended December 31, 2005. Lake Placid requested an annual interim revenue increase of \$49,376 or 70.12% for wastewater only. On July 19, 2006, the wastewater interim revenue increase was denied. The utility has requested final revenue increases of \$30,017 or 66.12% for water and \$71,902 or 102.12% for wastewater. Water and wastewater rates were last established for this utility in its 1995 rate proceeding.<sup>1</sup> In that case, Lake Placid was granted revenue increases of 69.41% and 118.43% for water and wastewater, respectively.

This recommendation addresses Lake Placid's final rates. The Commission has jurisdiction pursuant to Sections 367.081, Florida Statutes.

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<sup>1</sup> See Order No. PSC-96-0910-FOF-WS, issued July 15, 1996, in Docket No. 951027-WS, In re: Application for rate increase in Highlands County by Utilities, Inc.

## Discussion of Issues

### Quality of Service

**Issue 1:** Is the quality of service provided by Lake Placid Utilities, Inc. considered satisfactory?

**Recommendation:** Yes. The utility's overall quality of service is satisfactory. (Rieger)

**Staff Analysis:** Pursuant to Rule 25-30.433(1), Florida Administrative Code (F.A.C.), in every water and/or wastewater rate case, the Commission shall determine the overall quality of service provided by the utility by evaluating three separate components of water and/or wastewater operations. The components are: 1) quality of utility's product; 2) the operational conditions of the utility's plant and facilities; and, 3) the utility's attempt to address customer satisfaction. The rule further states that sanitary surveys, outstanding citations, violations and consent orders on file with the Department of Environmental Protection (DEP) and the county health department over the preceding 3-year period shall also be considered, along with input from the DEP and health department officials and consideration of customer comments and complaints.

Our analysis of the overall quality of service provided by the utility is derived from the quality of the utility's water and wastewater product, operational condition of the utility's plants or facilities, and customer satisfaction. Comments or complaints received by the Commission from customers are reviewed. Staff has also considered the utility's current compliance with the DEP.

### Quality of the product

In Highlands County, the water and wastewater programs are regulated by the DEP South District Office located in Fort Myers. The utility is current in all of the required chemical analyses and the utility has met all required standards for both water and wastewater. The quality of drinking water delivered to the customers and the wastewater effluent quality are both considered to be satisfactory by the DEP.

### Condition of Plants and Facilities

A field investigation for Lake Placid was conducted on August 17-18, 2006. The water and wastewater treatment facilities appeared to be operating adequately at the time of the field investigation. However, due to continued safety and reliability concerns, the utility was beginning preparations at that time to replace a hydropneumatic tank, internal plant piping and defective check valves at the water treatment plant. Replacements have been completed and the conditions of these facilities (water and wastewater) are currently in compliance with the DEP rules and regulations. A review of the maintenance records and the general condition of the plants appear to be adequate.

A review of flow data during the test year indicates there is excessive unaccounted for water. Staff believes that for water, the utility has adequately addressed the excessive unaccounted for water situation with the recent replacement of leaking check valves at the water

treatment plant. Therefore, staff believes that the quality of service concerning the condition of the facilities is satisfactory.

### Customer Satisfaction

**Test Year Complaints.** The utility provided in its filing copies of customer complaints received during the test year. Although there appeared to be no water quality complaints, there were a few complaints concerning customer billing and consumption and various water leaks. For wastewater, there were several complaints concerning liftstation alarms and liftstation overflows. A review of these complaints found that the utility satisfactorily addressed the above mentioned concerns in a proper fashion.

**Correspondence.** The Commission received no correspondence concerning quality of service from customers of the utility.

**Customer Meeting.** A customer meeting was held within the utility's service area on November 8, 2006, in the DeeAnn Lakefront Estates Clubhouse near Lake Placid, Florida. The 10 customers who attended the meeting had no specific comments about the quality of service provided by the utility.

**Complaints on file.** The PSC Complaint Tracking System (CATS) was reviewed. There are currently no active or recently closed complaints on file.

### Staff's Conclusion

The overall quality of service provided by the utility should be considered satisfactory. Staff believes the quality of product and the condition of the plants are adequate when it comes to regulatory compliance standards. Also, after review of the complaint records, and the fact that no one brought up any quality of service concerns during the customer meeting, the utility appears to be adequately addressing customer concerns in an acceptable matter.

**Rate Base**

**Issue 2:** Should the audit rate base adjustments to which the utility agrees be made?

**Recommendation:** Yes. Based on audit adjustments which the utility agrees with, plant should be reduced by \$14,150 for water and \$3,093 for wastewater. In addition, accumulated depreciation should be increased by \$4,555 for water and \$4,424 for wastewater. (Rendell)

**Staff Analysis:** Staff auditors recommended the following adjustments to the utility's average rate base:

Audit Adjustment	<u>Plant</u>		<u>Accumulated Depreciation</u>	
	<u>Water</u>	<u>Wastewater</u>	<u>Water</u>	<u>Wastewater</u>
Audit Findings 1& 2	<u>(\$14,150)</u>	<u>(\$3,093)</u>	<u>\$4,555</u>	<u>\$4,424</u>

The utility agrees with all of the above audit adjustments. Therefore, staff recommends that plant be reduced by \$14,150 for water and \$3,093 for wastewater and accumulated depreciation be increased by \$4,555 for water and \$4,424 for wastewater.

**Issue 3:** What is the appropriate Water Service Corporation (WSC) and Utilities, Inc. of Florida (UIF) rate base allocations for Lake Placid?

**Recommendation:** The appropriate WSC net rate base allocation for Lake Placid is \$824 for water and \$1,591 for wastewater. This represents an increase of \$197 and \$308 for water and wastewater, respectively. WSC depreciation expense should also be increased by \$12 and \$16, for water and wastewater, respectively. Further, the appropriate UIF rate base allocation for Lake Placid is \$4,781 for water and \$4,837 for wastewater. This represents water plant and accumulated depreciation decreases of \$12,591 and \$7,350, respectively, and wastewater plant and accumulated depreciation increases of \$12,582 and \$7,745, respectively. In addition, depreciation expense should be decreased by \$764 for water and increased by \$1,656 for wastewater. (Fletcher)

**Staff Analysis:** On MFR Schedule A-3, the utility reflected a WSC rate base allocation of \$845 for water and \$1,065 for wastewater. Lake Placid also recorded UIF rate base allocation of \$10,022 for water only. Staff performed an affiliate transactions (AT) audit of Utilities, Inc., the parent company of Lake Placid and its sister companies. WSC (a subsidiary service company of UI) supplies most of accounting, billing, and other services required by UI's other subsidiaries. UIF (a subsidiary of UI) provides administrative support to its sister companies in Florida. As discussed below, staff believes several adjustments are necessary to the WSC and UIF rate bases before they are allocated to the utility. These adjustments include recommended audit adjustments and the use of an ERC-only methodology for several WSC allocation codes.

### Audit Adjustments

In Audit Finding No. 1 of the AT audit, the staff auditor recommended adjustments to WSC's rate base consistent with Order No. PSC-03-1440-FOF-WS.<sup>2</sup> First, deferred income taxes were removed because they should be a component of the capital structure. Second, the net computer plant balances were set to zero because WSC was unable to provide sufficient supporting evidence for inter-company transfers of computers and was unable to locate several missing invoices requested. Third, the office structure and furniture balances were adjusted because WSC was unable to locate several missing invoices requested. In its response to the AT audit, UI agreed with the above recommended audit adjustments. Based on the above, staff recommends that the appropriate simple average WSC rate base before any allocation is \$2,122,628. As there were no audit findings in the AT audit regarding UIF's rate base, staff recommends that the appropriate simple average UIF rate base before any allocation is \$1,113,433 as reflected in UIF's general ledger.

### ERC Methodology

WSC utilizes 11 different allocation factors to allocate its rate base and expenses. Prior to January 1, 2004, WSC's allocation codes one, two, three, and five were based on customer equivalents (CEs). By Order No. PSC-03-1440-FOF-WS, pp. 23-30, the Commission found that that WSC's method of allocating its common costs based on CEs is unsupported and

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<sup>2</sup> Order No. PSC-03-1440-FOF-WS, issued December 22, 2003, in Docket No. 020071-WS, In re: Application for rate increase in Marion, Orange, Pasco, Pinellas, and Seminole Counties by Utilities, Inc. of Florida.



unreasonable. Further, the Commission found that UI shall use ERCs, measured at the end of the applicable test year, as the primary factor in allocating affiliate costs in Florida as of January 1, 2004.

In Audit Finding No. 4 of the AT Audit, staff auditors stated that WSC allocates its common plant and expenses quarterly as of June 30, 2005. In addition, WSC utilizes the following: “(1) If the operating system has both water and wastewater, the wastewater customer is counted as one and one-half; (2) If the customer is an availability customer only, the customer is counted as one-half; (3) If the water company is a distribution company only, the customer is counted as one-half; and, (4) If the wastewater company is a collection company only, the customer is counted as one-half.” Staff believes that these additional four factors unnecessarily complicate the allocation process versus the use of an ERC-only methodology. With this additional methodology, staff notes that WSC’s ERC count will not conform to the ERC count in each Florida subsidiaries’ annual report filed with the Commission. Further, the use of an ERC-only methodology is consistent with the methodology used by the Commission to set rates for water and wastewater utilities. Accordingly, staff recommends that UI should use the ERC-only methodology for its allocation codes one, two, three, and five.

### Conclusion

Based on the above, staff recommends that the appropriate WSC net rate base allocation for Lake Placid is \$824 for water and \$1,591 for wastewater. This represents an increase of \$197 and \$308 for water and wastewater, respectively. WSC depreciation expense should also be increased by \$12 and \$16, for water and wastewater, respectively. Further, the appropriate UIF rate base allocation for Lake Placid is \$4,781 for water and \$4,837 for wastewater. This represents water plant and accumulated depreciation decreases of \$12,591 and \$7,350, respectively, and wastewater plant and accumulated depreciation increases of \$12,582 and \$7,745, respectively. In addition, depreciation expense should be decreased by \$764 for water and increased by \$1,656 for wastewater.

**Issue 4:** Should other rate base adjustments be made?

**Recommendation:** Yes. Pro forma plant should be reduced by \$22,424 for water and \$1,343 for wastewater. Corresponding adjustments should be made to increase accumulated depreciation by \$17,036 for water, decrease accumulated depreciation by \$30 for wastewater and decrease depreciation expense by \$1,083 and \$30 for water and wastewater, respectively. Accumulated Amortization of Acquisition should be decreased by \$9,204 for water. Historical plant should be increased by \$17,900 for wastewater. (Rendell)

**Staff Analysis:** In Schedule A-3 of its MFRs, the utility requested the inclusion of \$71,331 in pro forma plant additions. Also included was \$1,914 of related accumulated amortization and depreciation expense. In its first data request, staff asked the utility to provide invoices and signed contracts for the requested pro forma plant. In its response, the utility provided three invoices related to the requested pro forma projects.

After an examination of the company-provided invoices, staff determined the invoices totaling \$30,788 related to pro forma projects. Staff recommends disallowance of all requested costs that the utility did not provide sufficient documentation in response to data requests from staff. Staff has verified the recommended projects are specific in nature and are necessary and prudent for this utility. These pro forma plant additions are not for non-specific projects.

Overall, staff recommends that pro forma plant be reduced by \$22,424 and \$1,343 for water and wastewater, respectively. Corresponding adjustments should be made to increase accumulated depreciation by \$17,036 for water and reduce accumulated depreciation by \$30 for wastewater. Adjustments should also be made to reduce depreciation expense by \$1,083 and \$30 for water and wastewater, respectively.

In schedule A-1 of its MFRs, the utility included a \$9,204 Accumulated Amortization of Acquisition Adjustment. The utility has not booked an acquisition adjustment for the test year, nor has one been approved by this Commission. Therefore, staff has remove this amount from its rate base calculation.

Staff believes the utility erred by reducing plant in service by \$17,900. As such, staff has increased plant in service by this amount.

In conclusion, staff recommends that pro forma plant should be reduced by \$22,424 for water and \$1,343 for wastewater. Corresponding adjustments should be made to increase accumulated depreciation by \$17,036 for water, decrease accumulated depreciation by \$30 for wastewater and decrease depreciation expense by \$1,083 and \$30 for water and wastewater, respectively. Accumulated Amortization of Acquisition should be decreased by \$9,204 for water. Historical plant should be increased by \$17,900 for wastewater.

**Issue 5:** What is the used and useful percentage for the water treatment plant, the wastewater treatment plant, the water distribution system and the wastewater collection system?

**Recommendation:** Lake Placid's water treatment plant should be considered 100% used and useful. The wastewater treatment plant should be considered 30.46% used and useful, and the water distribution system and wastewater collection system, with the exception of Account 354, should be considered 100% used and useful as reflected in Attachment A. As a result of the above adjustments, net wastewater rate base should be reduced by \$94,585. Corresponding adjustments should also be made to reduce wastewater depreciation expense by \$8,206 and property taxes by \$589. An adjustment should be made to reduce O&M expense by \$681 for excessive unaccounted for water. (Rieger, Rendell)

**Staff Analysis:** In its application, the utility requests that the water treatment plant be considered 100% used and useful, and the wastewater treatment plant be considered 86% used and useful. In addition, the utility requests the water distribution and wastewater collection systems be considered 100% used and useful. Attachment A contains a used and useful analysis for the water and wastewater plants.

#### Water Treatment Plant

In its application, the utility calculated the water treatment plant to be 100% used and useful, the wastewater treatment plant to be 43% used and useful, and the water distribution and wastewater collection systems to be 100% used and useful. However, the utility has requested the wastewater treatment plant be considered 86% used and useful. The Commission recognized in the prior rate case, Order No. PSC-96-0910-FOF-WS, that the used and useful calculation was 40.36% for the water treatment plant, 30.46% for the wastewater treatment plant, 100% for water distribution, 100% for wastewater collection gravity lines, and 84% for force mains.

Because this is a system without storage, the used and useful calculation of the water treatment plant is determined by dividing the peak demand in gallons per minute by the firm reliable capacity of the water treatment system in gallons per minute. Consideration is given to fireflow, unaccounted for water, and growth. In accordance with the American Waterworks Association Manual of Water Supply Practices, the highest capacity well should be removed from the calculation to determine the plant's reliability. In this case, the firm reliable capacity is determined by assuming that one of the utility's two wells, rated at 200 gpm each, is out of service. As indicated in Attachment A, since it does not appear to be an anomaly, the peak usage day of 91 gpm (March 1, 2005) should be used. The local fire flow requirement is 500 gpm for 2 hours.

Total unaccounted for water is 2.612 million gallons for the test year or 4.84 gpm (26.92%). Therefore, excessive unaccounted for water (in excess of 10% of average daily flow) is 16.92% or 3.04 gpm. As noted in the application, excessive unaccounted for water during the test year is attributed to two defective water valves located at the water treatment plant. These valves, which were replaced in the fall of 2006, allowed pumped and metered water to seep back into the wells. In the prior rate case, a 47% adjustment was made for excessive unaccounted for

water. In this case, in addition to the above plant gallonage adjustment, it is also appropriate to make a 16.92% operation and maintenance (O&M) adjustment for excessive unaccounted for water to Account Nos. 615 (purchased power) and 618 (chemicals). As a result, staff recommends an adjustment should be made to reduce O&M expense by \$681 for excessive unaccounted for water.

In reference to growth, a 9.4 gpm allowance based on annual customer growth of 5 ERCs should be used. As reflected in Attachment A, the water treatment plant is 100% used and useful based on a peaking factor of two times the peak day demand of 91 gpm minus 3.04 gpm excessive unaccounted for water and a growth allowance of 9.4 gpm, plus the required fireflow of 500 gpm, divided by the firm reliable plant capacity of 200 gpm.

It should be noted that the utility does not have sufficient total well capacity (400 gpm) to meet the fire flow requirement of 500 gpm. Staff considered a used and useful analysis based on gallons per day instead of gallons per minute, even though the utility does not have storage capacity. However, even using a gallons per day analysis, the utility's water system does not have sufficient capacity (144,000 gallons) to meet the fire flow requirement for two hours (60,000 gallons) plus the peak day demand (131,000 gallons).

### Wastewater Treatment Plant

Pursuant to Rule 25-30.432, F.A.C., the used and useful calculation of a wastewater treatment plant is based on the customer demand and permitted capacity of the plant. The rule provides that customer demand should be determined using the same basis as the permitted capacity. Consideration is also given for growth, infiltration and inflow, and other relevant factors.

Lake Placid's wastewater treatment plant is permitted for 90,000 gpd based on annual average daily flows (AADF) and the customer demand based on AADF is 15,597 gpd.<sup>3</sup> The utility has a small amount of growth, but no excessive infiltration or inflow. Based on these factors, the utility would be 18.68% used and useful. However, in the utility's last rate case, the wastewater treatment plant was found to be 30.46% used and useful.

Staff recommends that, given the age of the system, the limited growth potential, and the higher used and useful percentage allowed in the last rate case, the wastewater treatment plant should be considered 30.46% used and useful. Staff notes that using seasonal flows during the test year would result in a used and useful of approximately 30%.

However, in a review of Schedule A-6 of the MFRs, staff discovered that the utility appears to have transferred a large portion of the balance in Account 380 to Account 354. This transfer occurred during the test year. This transfer has the effect of decreasing the average balance in Account 380, Treatment and Disposal, while increasing the average balance in

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<sup>3</sup> The utility originally reported average annual daily flows for the test year of 35,200 gpd. However, the utility subsequently filed additional information which indicated that during the test year the plant flow meter was found to be inaccurate and was recalibrated. The flows for the twelve months following the recalibration reflect customer demand of 15,597 average annual gallons per day.

Account 354, Structures and Improvements. In some situations, a transfer of this type would have no effect on rate base, but it does here. In this case, staff has applied a 69.54% non-used and useful adjustment to Account 380. No adjustment was approved in the last case for Account 354. Therefore, a transfer from Account 380 to Account 354 in December 2005, has the effect of increasing rate base and revenue requirement.

Furthermore, Account 380 is the primary account used by the utility for its facilities used in its wastewater treatment operations, while Account 354 is normally used for such items as the utility offices, landscaping, or out-buildings. Account 354 does not usually contain costs for treatment plant. The utility has not justified this transfer. Therefore, staff has applied the same 30.46% used and useful percentage recommended by staff for Account 380 to the amount of plant staff calculated was transferred to Account 354.

Overall, the utility's wastewater treatment plant should be considered 30.46% used and useful. As discussed below, the wastewater collection system, with the exception of Account 354, should be considered 100% used and useful. A portion of plant in Account 354 should be considered 69.54% non-used and useful. As a result of the above adjustments, net wastewater rate base should be reduced by \$94,585. Corresponding adjustments should also be made to reduce wastewater depreciation expense by \$8,206 and property taxes by \$589.

#### Water Distribution and Wastewater Collection Systems

The used and useful calculations for the water distribution and wastewater collection systems are determined by the number of customers connected to the systems divided by the capacity of the systems. Consideration is given for growth. In this case, with only five vacant lots remaining that have mains available for service, the water distribution and wastewater collection systems are considered built out. Therefore, the water distribution and wastewater collection systems are recommended to be 100% used and useful.

**Issue 6:** What is the appropriate working capital allowance?

**Recommendation:** The appropriate amount of working capital is \$3,181 for water and \$7,952 for wastewater based on the formula method. (Rendell)

**Staff Analysis:** Rule 25-30.433(2), F.A.C., requires that Class C utilities use the formula method, or one-eighth of operation and maintenance (O&M) expenses, to calculate the working capital allowance. The utility has properly filed its allowance for working capital using the formula method. Staff has recommended several adjustments to the utility's balance of O&M expenses. Due to the adjustments recommended in other issues, staff recommends that working capital of \$3,181 and \$7,952 should be approved for water and wastewater, respectively. This reflects a decrease of \$992 to the utility's requested working capital allowance of \$4,173 for water and a decrease of \$1,438 from the utility's request of \$9,390 for wastewater.

Docket No. 060260-WS

Date: March 1, 2007

**Issue 7:** What is the appropriate water and wastewater rate base?

**Recommendation:** The appropriate water rate base for the test year ending December 31, 2005, is \$160,656. The appropriate wastewater rate base for the period ending December 31, 2005, is \$104,686. (Rendell)

**Staff Analysis:** Staff has calculated Lake Placid's water and wastewater rate base using the utility's MFRs with adjustments as recommended in the proceeding issues, as \$160,656 and \$104,686, respectively.

## **Capital Structure**

**Issue 8:** What is the appropriate return on common equity?

**Recommendation:** The appropriate return on common equity is 11.45% based on the Commission leverage formula currently in effect. Staff recommends an allowed range of plus or minus 100 basis points be recognized for ratemaking purposes. (Springer)

**Staff Analysis:** The return on equity (ROE) included in the utility's filing is 11.77%. This return is based on the application of the Commission's leverage formula approved in Order No. PSC-05-0680-PAA-WS and an equity ratio of 40.14%.<sup>4</sup>

As noted in Audit Finding No. 11, Utilities, Inc.'s average common equity balance of \$90,787,422 should be adjusted upward by \$3,093,004 to \$93,880,426. Per its response to the Audit Report, the utility is in agreement with the audit opinion. This adjustment increased the equity ratio as a percentage of investor-supplied capital from 40.14% to 40.95%.

Based on the current leverage formula approved in Order No. PSC-06-0476-PAA-WS and an equity ratio of 40.95%, the appropriate ROE is 11.45%.<sup>5</sup> Staff recommends an allowed range of plus or minus 100 basis points be recognized for ratemaking purposes.

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<sup>4</sup> Order No. PSC-05-0680-PAA-WS, issued June 20, 2005, in Docket No. 050006-WS, In Re: Water and Wastewater Industry Annual Reestablishment of Authorized Range of Return on Common Equity for Water and Wastewater Utilities Pursuant to Section 367.081(4)(f), Florida Statutes.

<sup>5</sup> Order No. PSC-06-0476-PAA-WS, issued June 5, 2006, in Docket No. 060006-WS, In Re: Water and Wastewater Industry Annual Reestablishment of Authorized Range of Return on Common Equity for Water and Wastewater Utilities Pursuant to Section 367.081(4)(f), Florida Statutes.



**Issue 9:** What is the appropriate weighted average cost of capital including the proper components, amounts, and cost rates associated with the capital structure for the test year ended December 31, 2005?

**Recommendation:** The appropriate weighted average cost of capital for the test year ended December 31, 2005 is 7.50%. (Springer, Kyle)

**Staff Analysis:** Based upon the proper components, amounts, and cost rates associated with the capital structure for the test year ended December 31, 2005, staff recommends a weighted average cost of capital of 7.50%. The weighted average cost of capital included in the utility's filing is 8.17%. Schedule No. 2 details staff's recommendation.

The test year per book amounts were taken directly from Lake Placid Utility's MFR filing Schedule D-2. Staff made specific adjustments to three components in the utility's proposed capital structure. As noted in Audit Finding No. 11, Utilities, Inc.'s average common equity balance should be adjusted upward by \$3,093,004. Also in Audit Finding No. 11, the staff auditors noted that an average balance of \$1,602 for customer deposits was reflected in the utility's general ledger but was not included in its filing. Staff made an adjustment of \$1,602 to recognize the amount of customer deposits in the capital structure. Finally, staff made an adjustment of \$8,996 to increase the balance of deferred income taxes.

In Audit Finding No. 12, staff auditors noted that the utility understated its calculation of deferred taxes for accelerated depreciation for state income tax purposes by \$3,564. Further, the auditors discovered that deferred taxes for intangible plant were understated by \$1,422 for state tax purposes and were understated by \$4,010 for federal tax purposes. Accordingly, staff recommends that the balance of deferred taxes be increased by \$8,996, the total of these amounts. Per its response to the Audit Report, the utility is in agreement with the audit opinion regarding these adjustments.

Staff revised the respective cost rates proposed by the utility. The appropriate cost rate for common equity of 11.45% is discussed in Issue 8. In addition, the auditors in staff Audit Finding No. 11 recommended an adjustment to the cost rate for long-term debt. The long-term debt cost rate was reduced from the utility proposed rate of 6.81% to 6.73%. Per its response to the Audit Report, the utility is in agreement with the audit opinion regarding these adjustments.

Based on the proper components, amounts, and cost rates associated with the capital structure for the test year ended December 31, 2005, staff recommends a weighted average cost of capital of 7.50%. Schedule No. 2 details staff's recommendation.

**Net Operating Income**

**Issue 10:** What adjustments, if any, should be made to the utility's test year revenue?

**Recommendation:** Water revenues should be increased by \$1,809 and wastewater revenues should be increased by \$1,631. (Rendell)

**Staff Analysis:** A utility is required to annualize test year revenues to reflect the effect of any rate increase that accrued during the test year. In its MFRs, the utility made annualized revenue adjustments of \$222 and \$50 for water and wastewater, respectively. However, staff determined the proper annualized adjustments for water and wastewater should be \$2,031 and \$1,881, respectively.

Therefore, staff recommends that annualized water test year revenues be increased by \$1,809 (\$2,031-\$222), and annualized wastewater revenues should be increased by \$1,831 (\$1,881-\$50).

**Issue 11:** Should audit net operating income adjustments to which the utility agrees be made?

**Recommendation:** Yes. Water O&M expense should be reduced by \$2,602. Taxes Other Than Income should be increased by \$468 and \$2,064 for water and wastewater, respectively. Additionally water depreciation expense should be increased by \$957, and wastewater depreciation expense should be increased by \$762. (Rendell)

**Staff Analysis:** The audit findings and recommended adjustments are listed in the table below:

<u>Audit Finding</u>	<u>O&amp;M Expense</u>		<u>Taxes Other Than Income</u>		<u>Depreciation Expense</u>	
	<u>Water</u>	<u>Wastewater</u>	<u>Water</u>	<u>Wastewater</u>	<u>Water</u>	<u>Wastewater</u>
AF 1					(\$725)	(\$71)
AF 2					\$371	\$306
AF 6		(\$2,602)				
AF 8					\$1,311	\$527
AF 9			\$468	\$2,064		
Total		<u>(\$2,602)</u>	<u>\$468</u>	<u>\$2,064</u>	<u>\$957</u>	<u>\$762</u>

The utility agrees with all of the above audit adjustments. Therefore, staff recommends that water O&M expense be reduced by \$2,602. Taxes Other Than Income should be increased by \$468 and \$2,064 for water and wastewater, respectively. Additionally water depreciation expense should be increased by \$957, and wastewater depreciation expense should be increased by \$762.

**Issue 12:** What is the appropriate amount of allocated WSC and UIF expenses for Lake Placid?

**Recommendation:** The appropriate WSC O&M expenses and taxes other than income for Lake Placid are \$2,825 and \$3,724, respectively. As such, water and wastewater O&M expenses should be increased by \$62 and \$81, respectively, and water and wastewater taxes other than income should be decreased by \$4 and \$6, respectively. Further, the appropriate UIF O&M expenses for Lake Placid are \$1,913 for water and \$2,522 for wastewater. As such, water and wastewater O&M expense should be increased by \$178 and \$235, respectively. (Fletcher)

**Staff Analysis:** On MFR Schedule B-12, the utility reflected total WSC allocated O&M expenses of \$6,406 and taxes other than income of \$338. Lake Placid also recorded total UIF allocated O&M expenses of \$4,021. As discussed below, staff believes adjustments are necessary to the WSC and UIF expenses before they are allocated to the utility. These adjustments include recommended audit adjustments and the use of an ERC-only methodology for several WSC allocation codes.

In Audit Finding No. 2 of the AT audit, the staff auditor recommended adjustments to WSC's expenses consistent with Order No. PSC-03-1440-FOF-WS, pp. 82-84. The auditor recommended removal of: (1) insurance premiums for former employee directors' life insurance policies; (2) fiduciary policies protecting directors and officers; and, (3) pension funds. The auditor believes these items should be eliminated because they were for the benefit of UI's shareholders. Second, the auditor recommended the removal of interest expense and interest income because they are included as components of UI's capital structure. In its response to the AT audit, UI agreed with the above recommended audit adjustments. Based on the above, staff recommends that the appropriate WSC expenses, before any allocation, are \$7,458,207. Further, there was no audit finding in the AT audit regarding UIF's expenses. Thus, staff recommends that the appropriate UIF O&M expenses before any allocation are \$266,650.

As recommended in Issue 3, UI should use the ERC-only methodology for its allocation codes one, two, three, and five. Based on the above audit adjustments and the ERC-only methodology, staff recommends that the appropriate WSC O&M expenses and taxes other than income for Lake Placid are \$2,825 and \$3,724, respectively. As such, water and wastewater O&M expenses should be increased by \$62 and \$81, respectively, and water and wastewater taxes other than income should be decreased by \$4 and \$6, respectively. Further, the appropriate UIF O&M expenses for Lake Placid are \$1,913 for water and \$2,522 for wastewater. As such, water and wastewater O&M expense should be increased by \$178 and \$235, respectively.

**Issue 13:** Should an adjustment be made to the utility's pro forma salaries and wages, pensions and benefits, and payroll taxes?

**Recommendation:** Yes. Lake Placid's salaries and wages should be decreased by \$705 for water and \$749 for wastewater. Accordingly, pensions and benefits should be reduced by \$48 for water and \$52 for wastewater, respectively, and payroll taxes should be reduced by \$78 and \$96 for water and wastewater, respectively. (Fletcher)

**Staff Analysis:** On MFR Schedule B-5, Lake Placid reflected historical water salaries and wages and pensions and benefits of \$925 and \$682, respectively. On MFR Schedule B-6, the utility reflected historical wastewater salaries and wages and pensions and benefits of \$4,266 and \$1,063, respectively. On MFR Schedule B-15, Lake Placid reflected historical payroll taxes of \$243 for water and \$378 for wastewater.

On MFR Schedule B-3, the utility requested pro forma increases in water salaries and wages, pensions and benefits, and payroll taxes of \$747, \$79, and \$89, respectively, and requested increases in wastewater salaries and wages, pensions and benefits, and payroll taxes of \$941, \$100, and \$113, respectively. The pro forma salaries and wages represents increases of 80.76% for water and 22.06% for wastewater. The pro forma pensions and benefits represents increases of 11.58% for water and 9.41% for wastewater.

In Staff's First Data Request in Docket No. 060261-WS, the utility was asked to explain why its pro forma salaries and wages increases were significantly greater than the Commission's 2006 price index of 2.74%. In its response, the utility explained that its increases include all new employees' salaries, payroll taxes, and benefits for office employees and operators. The utility also stated that the salaries were annualized to reflect a full year of costs and a cost of living increase was applied across the board to all Florida office employees and operators.

In Staff's Fifth Data Request in Docket No. 060256-SU, UI was asked to provide the total number of full-time and part-time employees for its Florida subsidiaries, their average salary, and average salary percentage increases for all Florida managerial and non-managerial employees through September 2006. According to the information provided, the historical average salary increases for all Florida Employees from 2001 to 2005 has been 4.51%. UI realized a net reduction of eight total Florida employees from 2005 to June 2006. The total average salaries from 2005 to 2006 increased \$74,616; however, staff notes the total requested pro forma salary increases in UI's current docketed rate cases in Florida is \$332,883. If the salary increases for all Florida employees were limited to an across the board increase of the 4.51% historical five-year average, the pro forma salary increases for all of UI's current docketed cases would be \$105,776.

From the information provided by UI, staff is unable to attribute the 2006 employee changes to the respective pro forma salary increases in the UI docketed cases. The utility has the burden of proving that its costs are reasonable. See, Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (1982). Staff believes that UI has not met its burden of proof of showing how the employee changes from 2005 to 2006 affect the respective rate cases.

On January 18, 2007, the utility hand delivered a two-page document reflecting the title and duties of two new employees. However, this document did not contain the annual salary for these two employees nor did it show the utility's calculation of how their respective salaries are allocated to the UI's Florida subsidiaries. Further, the utility has not provided any information regarding any other employee changes from July 1, 2006 to the present.

As such, with the exception of Sandalhaven<sup>6</sup> (a negative pro forma salary adjustment of \$573), staff believes the requested pro forma salary increases in UI's other respective rate cases are excessive. Staff notes the historical 5-year average salary increase of 4.51% is 177 basis points above the Commission's 2006 Price Index of 2.74%. With the exception of Sandalhaven, staff recommends that pro forma salary increases in all of UI's respective cases should be limited to the 4.51% above the 2005 historical salary amounts. The Commission has previously limited pro forma salary adjustments to a utility's historical average salary increases.<sup>7</sup> Thus, staff recommends that Lake Placid's salaries and wages should be decreased by \$705 for water and \$749 for wastewater. Accordingly, pensions and benefits should be reduced by \$48 for water and \$52 for wastewater, respectively, and payroll taxes should be reduced by \$78 and \$96 for water and wastewater, respectively.

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<sup>6</sup> Docket No. 060285-SU, In re: Application for increase in wastewater rates in Charlotte County by Utilities, Inc. of Sandalhaven.

<sup>7</sup> By Order No. PSC-05-0624-PAA-WS, issued June 7, 2005, in Docket No. 040450-WS, In re: Application for rate increase in Martin County by Indiantown Company, Inc., the Commission limited pro forma salaries to the utility's actual historical average wage increases of 3%.

**Issue 14:** Should additional adjustments be made to Taxes Other Than Income?

**Recommendation:** Yes. Taxes other than income should be increased by \$931 and \$1,451 for water and wastewater, respectively to reflect the appropriate amount of test year regulatory assessment fees (RAFs). (Rendell)

**Staff Analysis:** Staff has reviewed Lake Placid's operating income and believes one adjustment is appropriate. The utility reflected test year RAFs of \$1,102 for water and \$1,715 for wastewater. Based on staff review, these amounts do not reflect 4.5% of test year revenues. To correct this, staff believes that RAFs should be increased by \$931 for water and \$1,451 for wastewater.

**Issue 15:** What is the appropriate amount of rate case expense?

**Recommendation:** The appropriate rate case expense is \$31,073 for water and \$39,547 for wastewater. This expense should be recovered over four years for an annual expense of \$7,768 for water and \$9,887 for wastewater. Thus annual rate case expense should be reduced by \$6,745 for water and \$8,415 for wastewater. (Rendell)

**Staff Analysis:** The utility included in its MFRs an estimate of \$131,261 for current rate case expense. Staff requested an update of the actual rate case expense incurred, with supporting documentation, as well as the estimated amount to complete the case. On November 22, 2006, the utility submitted a revised estimated rate case expense through completion of the PAA process of \$171,859. The components of the estimated rate case expense are as follows:

	<u>MFR Estimated</u>	<u>Actual</u>	<u>Additional Estimated</u>	<u>Total</u>
Legal and Filing Fees	51,000	16,421	48,500	66,921
Consultant Fees - VK	18,032	18,031	0	18,031
Consultant Fees - Seidman	5,000	2,794	3,025	5,819
WSC In-house Fees	41,600	15,919	28,242	44,161
Various Office Temp Fees	0	1,830	19,431	21,261
Travel – WSC	3,200	0	3,200	3,200
Miscellaneous	12,000	509	11,491	12,000
Notices	<u>429</u>	<u>88</u>	<u>378</u>	<u>466</u>
Total Rate Case Expense	<u>\$131,261</u>	<u>\$55,592</u>	<u>\$114,267</u>	<u>\$171,859</u>

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

The first adjustment relates to costs incurred to correct deficiencies in the MFR filing. Based on staff's review of invoices from the utility's consultants and the WSC employees, a combined amount of \$2,074 was billed for correcting the MFR deficiencies and revising the utility's filing. The amount associated with deficiency corrections (\$571) was easily identified in the consultants' invoices. However, the invoices and the documentation provided for WSC employees did not provide sufficient detail to specifically identify work done on corrections. Staff estimated the deficiency corrections by removing invoice amounts during the months of June through August when the corrections were in progress. This amounted to \$1,503 for WSC employees. The Commission has previously disallowed rate case expense associated with



correcting MFR deficiencies because of duplicate filing costs.<sup>8</sup> Accordingly, staff recommends that \$2,074 (\$571 + \$1,503) should be removed as duplicative and unreasonable rate case expense.

The second adjustment relates to the utility's estimated legal fees to complete the rate case. The utility's counsel estimated 150 hours or \$41,250 in fees plus \$6,000 in expenses to complete the rate case. A list of tasks to complete the case was provided by legal counsel, but no specific amount of time associated with each item. Counsel provided only a total number of hours and the total cost. While the descriptions of the activities or tasks appeared reasonable, staff had no basis to determine whether the individual hours estimated were reasonable. Staff reviewed these requested legal fees and expenses and believes these estimates reflect an overstatement. As noted in the case background, UI currently has ten pending rate cases with the Commission. In eight out of the ten rate cases, the same amount of estimated legal hours to complete was submitted for the estimated processing of each of the cases. Although the estimate to complete did not indicate the period of time it included, staff made the assumption it included November 2006 through February 2007. This would allow time for reviewing the recommendation, attending the agenda conference, reviewing the Commission's PAA order, and submitting the appropriate customer notice and tariffs for approval. The estimate for additional legal services for eight out of the ten rate cases was 150 hours for each rate case. Staff analyzed the reasonableness of this estimated time to complete each of these cases. Using the estimated amount of time to complete of four months for each of the eight rate cases, the legal office would have to work over 11 hours each day, including all holidays and all weekends. This would be exclusive work on just these cases. However, staff is aware of numerous other pending dockets, including the other two remaining UI rate cases, and undocketed projects also being worked on by this legal firm. Further, when the recognized holidays and weekends are removed, this firm would require work of approximately 18 hours everyday exclusively of these eight rate cases. Staff does not believe this is a reasonable assumption.

As discussed below, it is the utility's burden to justify its requested costs. Staff believes that 40 hours is a reasonable amount of time to respond to data requests, conference with the client and consultants, review staff's recommendation, travel to agenda and attend to miscellaneous post PAA matters. This is consistent with hours allowed for completion by the Commission in the 2004 Labrador Utilities, Inc. (Labrador) rate case.<sup>9</sup> This amounts to \$11,000 of rate case expense, a reduction of \$30,250.

There was no breakdown provided of the \$6,000 in disbursements required for legal counsel to complete the case. Thus, this amount is unsupported. However, staff calculated a reasonable travel allowance for this agenda conference. Staff believes that a reasonable cost for one person traveling from Altamonte Springs to Tallahassee, including meals, vehicle mileage and one day's lodging is \$489 in this instant docket. Staff notes this amount is greater than the

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<sup>8</sup> See Order No. PSC-05-0624-PAA-WS, issued Jun 7, 2005, in Docket No. 040450-WS, In re: Application for rate increase in Martin County by Indiantown Company, Inc.; and Order No. PSC-01-0326-FOF-SU, issued February 6, 2001, in Docket No. 991643-SU, In Re: Application for increase in wastewater rates in Seven Springs System in Pasco County by Aloha Utilities, Inc.

<sup>9</sup> See Order No. PSC-04-1281-PAA-WS, issued December 28, 2004, in Docket No. 030443-WS, In re: Application for rate increase in Pasco County by Labrador Utilities, Inc.

amount of travel expense the Commission allowed for this law firm in the 2004 Labrador rate case supra, as well as recent rate cases recently brought before this Commission. However, staff realizes the legislative session will have started and the hotel rates will increase. Based on staff's analysis, it calculated travel expenses of \$489, using the current state mileage rate (503 miles x \$.455 = \$224), hotel rates from websites (\$200) and a meal allowance (\$65). Therefore, staff believes \$489 is the appropriate travel expense in this docket. In addition to travel expense, staff calculated an amount for miscellaneous disbursements. Staff added the actual and unbilled legal disbursements less the filing fee, divided by eight, the number of months represented by the data, then multiplied by two, the time remaining until the agenda. Thus, staff believes \$1,236 is a reasonable amount for miscellaneous disbursements. Therefore, staff believes disbursements should be decreased by \$4,275 (\$6,000 - \$489 - \$1,236). Accordingly, staff recommends that rate case expense be decreased by \$34,525 (\$30,250 + \$4,275).

The third adjustment relates to the utility's estimated consultant fees for Mr. Seidman to complete the rate case. Mr. Seidman estimated 24 hours or \$3,000 plus \$25 in expenses to complete the rate case. Specifically, Mr. Seidman estimated 20 hours to assist with and respond to data requests and four hours to prepare for and attend the agenda. Staff believes that four hours is a reasonable amount of time to prepare for and attend the agenda for this docket. This is consistent with the hours allowed for completion by the Commission in the Indiantown Company, Inc. and the Mid-County Services, Inc. rate cases.<sup>10</sup> However, staff is aware only of one subsequent data request from OPC regarding the used and useful percentage. Staff believes that no more than two hours at \$125 per hour is reasonable for this data request. Therefore, staff recommends that rate case expense be decreased by \$2,250 (18 hours x \$125).

The fourth adjustment relates to the 491 hours and \$26,267 of estimated costs to complete this case by WSC employees. As of the November 22, 2006 date of the updated rate case expense, the audit was complete and there were no data requests outstanding. The utility failed to provide any detailed documentation of what tasks were involved in its estimate to complete the case for each employee. The utility simply stated that the \$26,267 was to assist with data requests and audit facilitation. The hours needed to complete data requests and audit facilitation was not broken down to estimate the hours needed to complete each item. In addition, there were no timesheets provided to show actual hours worked. Therefore, staff had no basis to determine whether the individual hours estimated were reasonable. As discussed below, it is the utility's burden to justify its requested costs. Thus, the utility's requested expense of \$26,267 should be removed in its entirety. In those cases where rate case expense has not been supported by detailed documentation, Commission practice has been to disallow some portion or remove all unsupported amounts.<sup>11</sup>

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<sup>10</sup> See Order No. PSC-05-0624-PAA-WS, issued June 7, 2005, in Docket No. 040450-WS, In re: Application for rate increase in Martin County by Indiantown Company, Inc.

Order No. PSC-04-0819-PAA-SU, issued August 23, 2004, in Docket No. 030446-SU, In re: Application for rate increase in Pinellas County by Mid-County Services, Inc.

<sup>11</sup> See Order No. PSC-94-0075-FOF-WS, issued January 21, 1994 in Docket No. 921261-WS, In re: Application for a Rate Increase in Lee County by Harbor Utilities Company, Inc.; Order No. PSC-96-0629-FOF-WS, issued May 10, 1996, in Docket No. 950515-WS, In re: Application for staff-assisted rate case in Martin County by Laniger Enterprises of America, Inc.; and Order No. PSC-96-0860-FOF-SU, issued July 2, 1996, in Docket No. 950967-SU,

It is the utility's burden to justify its requested costs. Florida Power Corp. v. Cresce, 413 So. 2d 1187, 1191 (Fla. 1982). Further, the Commission has broad discretion with respect to allowance of rate case expense. It would constitute an abuse of discretion to automatically award rate case expense without reference to the prudence of the costs incurred in the rate case proceedings. Meadowbrook Util. Sys., Inc. v. FPSC, 518 So. 2d 326, 327 (Fla. 1<sup>st</sup> DCA 1987), review denied by 529 So. 2d 694 (Fla. 1988).

The fifth adjustment relates to WSC expenses for the temporary office workers, Office Team. The utility did not include this expense in its MFRs; however, in its update, \$20,000 was estimated to assist with data and audit requests. The hours needed to complete data and audit requests was not broken down to estimate the hours needed to complete each item. Therefore, staff had no basis to determine whether the individual hours estimated were reasonable, although as mentioned above, the estimated hours appear to be excessive. As discussed above, it is the utility's burden to justify its requested costs. The utility indicated that it had incurred \$568 in expenses for Office Team, and provided invoices in support of this total. Staff believes that the additional \$19,432 estimated by Lake Placid is excessive, given the number of hours the utility estimated for the WSC employees, consultants and law firm to complete the case. Therefore, staff recommends that rate case expense be decreased by \$19,432.

The sixth adjustment addresses WSC travel expenses. In its MFRs, the utility estimated \$3,200 for travel. Staff believes that a reasonable cost for one person traveling round trip from Chicago to Tallahassee, airfare, car rental, parking and lodging is \$750. This was the amount of travel expense the Commission allowed for WSC in the Labrador rate case. However, staff does not believe an WSC employee will attend the agenda conference. In eight out of the ten UI current rate dockets currently before the Commission, the utilities have consistently requested this travel. In seven out of nine dockets decided at previous agenda conferences, the Commission has allowed this travel expense from Chicago. No WSC employee has attended any previous agenda conference for any of the seven dockets. Staff does not believe this current docket would warrant an WSC employee attending the agenda conference, as well. Therefore, staff believes no travel expense should be allowed. Accordingly, staff recommends that rate case expense be decreased by \$3,200.

The seventh adjustment relates to WSC expenses for FedEx Corporation (FedEx), copies and other miscellaneous costs. In its MFRs, the utility estimated \$12,000 for these items. In support of this expense, the utility provided only \$577 in costs from FedEx invoices for services through October 16, 2006. There was no breakdown or support for the remaining \$11,423. Staff is also concerned with the amount of requested costs for FedEx expense. UI has requested and received authorization from the Commission to keep its records outside the state in Illinois. This is pursuant to Rule 25-30.110(2)(b), F.A.C. However, when a utility receives this authorization, it is required to reimburse the Commission for the reasonable travel expense incurred by each Commission representative during the review and audit of the books and records. Further, these costs are not included in rate case expense or recovered through rates. By Order No. PSC-93-1713-FOF-SU, p. 19, issued November 30, 1993, in Docket No. 921293-SU, In Re: Application

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In re: Application for staff-assisted rate case in Highlands County by Fairmount Utilities, the 2<sup>nd</sup>, Inc. Staff notes that, in all of these cases, the Commission removed the entire unsupported amounts.

for a Rate Increase in Pinellas County by Mid-County Services, Inc., the Commission found that the utility also requested recovery of the actual travel costs it paid for the Commission auditors. Because the utility's books are maintained out of state, the auditors had to travel out of state to perform the audit. The Commission has consistently disallowed this cost in rate case expense. See Order No. 25821, issued February 27, 1991, and Order No. 20066, issued September 26, 1988. Staff believes that the requested amount of shipping costs in this rate case directly relates to the records being retained out of state. The utility typically ships its MFRs, answers to data request, etc. to its law firm located in central Florida. Then the documents are submitted to the Commission. Staff does not believe that the ratepayers should bear the related costs of having the records located out of state. This is a decision of the shareholders of the utility, and therefore, they should bear the related costs. Therefore, staff recommends that rate case expense be decreased by \$12,000.

In summary, staff recommends that the utility's revised rate case expense be decreased by \$101,239 for MFR deficiencies, and for unsupported and unreasonable rate case expense. The appropriate total rate case expense is \$70,620. A breakdown of rate case expense is as follows:

	MFR Estimated	Utility Revised Actual & Estimated	Staff Adjustments	Total
Legal and Filing Fee	\$51,000	\$66,921	(\$36,794)	\$30,127
Consultant Fees - VK	18,032	18,032	2,180	20,212
Consultant Fees- Seidman	5,000	5,819	(2,250)	3,569
WSC In-house Fees	41,600	44,161	(29,745)	14,416
Various Office Temp Fees	0	21,262	(19,432)	1,830
WSC Travel	3,200	3,200	(3,200)	0
Miscellaneous	12,000	12,000	(12,000)	0
Notices	<u>429</u>	<u>466</u>	<u>0</u>	<u>466</u>
Total Rate Case Expense	<u>\$131,261</u>	<u>\$171,859</u>	<u>(\$101,239)</u>	<u>\$70,620</u>
Annual Amortization	<u>\$32,815</u>		<u>(\$15,160)</u>	<u>\$17,655</u>

In its MFRs, the utility requested total rate case expense of \$131,261, which amortized over four years would be \$32,815. The utility actually included in its MFRs \$14,513 and \$18,302 for rate case expense in the test year for water and wastewater, respectively. Thus rate case expense should be decreased by \$6,745 for water and \$8,415 for wastewater, respectively.

**Issue 16:** What is the test year operating income?

**Recommendation:** Based on the adjustments discussed in previous issues, the test year operating income before any provision for increased revenues is \$6,469 and (\$3,219) for water and wastewater, respectively. (Rendell)

**Staff Analysis:** As shown on Schedules 3-A and 3-B, after applying staff's adjustments, the test year net operating income before any revenue increase is \$6,469 and (\$3,219) for water and wastewater, respectively. Staff's adjustments to operating income and expenses are shown on Schedule 3-C.

**Issue 17:** What are the appropriate revenue requirements for water and wastewater?

**Recommendation:** The following revenue requirement should be approved. (Rendell)

	<u>Test Year Revenues</u>	<u>\$ Increase</u>	<u>Revenue Requirement</u>	<u>% Increase</u>
Water	\$47,204	\$9,375	\$56,579	19.86%
Wastewater	\$72,043	\$18,591	\$90,634	25.81%

**Staff Analysis:** Lake Placid's requested final rates are designed to generate annual revenues of \$75,413 and \$142,314 for water and wastewater, respectively. These revenues exceed test year revenues by \$30,017 (66.12%), and \$71,902 (102.12%) for water and wastewater, respectively.

Based on staff's recommendations concerning the underlying rate base, cost of capital, and operating income issues, staff recommends approval of rates that are designed to generate a water revenue requirement of \$56,579 and a wastewater revenue requirement of \$90,634. These revenues are an increase to staff's adjusted test year revenues of \$9,375, or 19.86% for water and \$18,591 or 25.81% for wastewater. These revenue requirement amounts are shown on attached Schedules 3-A and 3-B. These amounts allow the utility the opportunity to recover its expenses and earn an 7.50% return on its investment in water and wastewater rate base.

## **Rate and Rate Structure**

**Issue 18:** What are the appropriate rate structures for the water and wastewater systems?

**Recommendation:** The appropriate rate structure for the water system is a continuation of the current base facility charge (BFC)/uniform gallonage charge rate structure. The residential wastewater-only flat rate structure should be discontinued and replaced with a bulk wastewater rate based on a BFC/gallonage charge rate structure. The bulk customers' BFC should be based on 80% of the number of equivalent residential connections actually connected to the system, while the gallonage charge should be set at 80% of the general service gallonage charge. The traditional BFC/gallonage charge rate structure should be continued for the remaining wastewater customers. The BFC cost recovery should be set at 54.6% for the water system and 50% for the wastewater system. The multi-residential gallonage charge rate should be set at an amount equal to the general service gallonage charge rate. (Lingo)

**Staff Analysis:** The current rate structures for the utility's respective water and wastewater systems were approved in the utility's last rate case. In that case, the Commission approved a BFC/uniform gallonage charge rate structure for the water system. The Commission also found that the BFC/gallonage charge rate structure was appropriate for the wastewater system, with the exception of DeeAnn Estates, a 70-unit condominium facility (plus clubhouse) that was served by a water source other than the utility. Because these customers' water consumption data was not available, a flat monthly rate was approved by the Commission for each condominium customer.<sup>12</sup> Each DeeAnn Estates resident is currently billed a flat rate of \$23.51 per month for wastewater service.

Staff performed a detailed analysis of the utility's billing data in order to evaluate various BFC cost recovery percentages, usage blocks, and usage block rate factors for the residential rate class. The goal of the evaluation was to select the rate design parameters that: 1) allow the utility to recover its revenue requirement; 2) equitably distribute cost recovery among the utility's customers; and 3) implement, where appropriate, water conserving rate structures consistent with the Commission's Memorandum of Understanding with the state's five Water Management Districts. Based on staff's analysis, the average water consumption per residential customer is approximately 2,400 gallons (2.4 kgal) per month. Therefore, staff believes that changing the utility's water rate structure to a more aggressive inclining-block rate structure is unnecessary.

The utility is located within the Southwest Florida Water Management District (SWFWMD or District). On January 9, 2007, a public hearing was held at the headquarters of the SWFWMD. Specific data presented at the hearing included but was not limited to: 1) rainfall data indicating that the deficits in several counties, including Highlands County, were categorized as critically abnormal; 2) all 16 counties within the District were experiencing drought or drought-like conditions; and 3) the Long Term Palmer Index indicating that all 16 counties were experiencing severely abnormal conditions. Based upon the testimony, data,

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<sup>12</sup> See Order No. PSC-96-0910-FOF-WS, issued July 15, 1996 in Docket No. 951027-WS, In re: Application for a rate increase in Highlands County by Lake Placid Utilities, Inc., pp. 11-12.

District staff recommendations and public comments, the Executive Director of the SWFWMD ordered that a Phase II Severe Water Shortage be declared for all ground and surface waters within the District's 16 county area.<sup>13</sup>

Ordinarily, one method staff uses to make the rates more conservation-oriented is to shift some of the cost recovery from the BFC to the gallonage charge such that no more than 40% of the costs are recovered through the BFC. Based on initial accounting allocations, the BFC in this case would recover approximately 42.1% of the costs. This results in a BFC reduction of almost \$3 compared to the BFC prior to filing the case. However, staff does not believe a reduction to the current BFC is appropriate due to the seasonality of the utility's customer base – almost half of the bills are for consumption of 1 kgal or less. Instead, staff recommends that the water BFC be set at 54.6%, which results in no change compared to the BFC prior to filing.

Staff's recommended increase to the utility's water system is less than 20%. Based on the declared water shortage in the SWFWMD, and staff's recommendation that the BFC remain unchanged from its level prior to filing this case, it is appropriate to place all of the revenue requirement increase into the gallonage charge. This results in a pattern of increasingly greater percentage price increases at increasing levels of consumption, which is consistent with how the Commission typically sets water rates.

Based on staff's initial accounting allocations, the wastewater system's BFC would recover 44% of the cost of service. However, due to the capital-intensive nature of wastewater systems, staff recommends that the BFC be set at 50%.

Before the scheduled customer meeting in the instant case, staff met with several representatives of the DeeAnn Estates Homeowners Association (DEHOA). During that meeting, customers expressed their concerns that the revenues from the flat rate structure were disproportionately great compared to the revenues generated by the remaining wastewater rates. The customers suggested that, rather than continuing to bill each individual customer a flat rate every month, the DEHOA be billed each month based on a BFC/gallonage charge rate structure. The DEHOA would pay the bill, and subsequently bill each resident an equal portion of the total bill. Each resident of DeeAnn Estates (DeeAnn) is a member of the DEHOA.

Before recommending a BFC/gallonage charge rate for DeeAnn Estates, staff had to first determine whether the requisite water consumption data would be available to the utility each month. DeeAnn Estates receives water service from its own well, which is of sufficient size that monthly operating reports must be supplied to the Florida Department of Environmental Protection (DEP). Therefore, monthly consumption data is available. The utility may obtain this data in one of three ways: 1) directly reading the utility's water well meter each month; 2) obtaining the data from DEP; or 3) obtaining the monthly meter readings from Short Utility Services, the well operator contracted by DeeAnn Estates.

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<sup>13</sup> Southwest Florida Water Management District, Order No. SWF 07-02, In re: Declaration of Water Shortage, pp. 1-5.



In the original recommendation filed February 1, 2007 for the February 13, 2007 agenda conference, staff recommended, among other things, that the wastewater rate structure for the customers of DeeAnn be changed from a flat rate per unit per month to a traditional BFC/general service gallonage charge rate structure. In addition, the homeowners' association, rather than the individual customers, would become the single customer of record. The meter readings from DeeAnn's dedicated water well would be used for wastewater billing. In an email to staff dated February 12, 2007, the customers of DeeAnn Estates had reviewed staff's original recommendation and provided staff with additional information and comments which, they believe, should change staff's recommended wastewater rate design treatment of DeeAnn's customers. Staff will address the major points raised in the email.

The customers stated that each unit in DeeAnn Estates has a water service control switch plus an outside faucet to use as needed for car washing, shrub watering, etc. This results in a difference between water gallons pumped and gallons returned to the wastewater system. The customers also stated that Lake Grassy is the source of supply for the common area irrigation. Based on these factors, the customers believe that each unit is essentially an individual home deserving the residential, rather than general service, gallonage charge. Finally, at the customer meeting and reiterated in the email, DeeAnn's residents do not believe they should be charged a BFC "unless consideration is given for our added cost and over-head of the lift station."

Despite each DeeAnn resident having a separate outside faucet for some non-indoor needs, the residents nevertheless should be charged the general service gallonage charge. The differentiation between residential and general service gallonage charges is to recognize that while approximately 20% of residential metered water usage is not returned to the wastewater system (mostly due to irrigation and pool needs), virtually 100% of general service metered water is returned to the system. DeeAnn's 70 units are spread over 9 different buildings, and as previously stated, DeeAnn's common area irrigation needs are met by a nearby lake. Fully 100% of the water pumped from the customers' dedicated well may not be used for indoor purposes and returned to the wastewater system. Nevertheless, staff believes that the percentage of pumped water for residential indoor use is closer to 100% than 80%. Therefore, staff recommends that the general service gallonage charge is more appropriate for DeeAnn's residents than the residential gallonage charge.

Staff researched prior cases to obtain guidance on the possible application of a bulk wastewater rate for the customers of DeeAnn Estates. In a 1984 case involving Martin Downs Utilities, Inc. and Martin County (County), the County was responsible for all water distribution beyond the point of delivery. The Commission approved a BFC for Martin County that was based on 80% of the number of ERCs actually connected to the system plus the tariff-approved usage charge. The Order states, "The 20% reduction in the base facility charge reflects the savings to the utility in billing and bookkeeping, as well as the maintenance responsibility for the mains on the discharged side of the meter."<sup>14</sup> In another case involving K W Resort Utilities Corporation, the Commission recognized that in K W Resort's prior rate case there were wastewater customers who owned their lift station. The Commission decided in that docket that

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<sup>14</sup> Order No. 17269, issued March 10, 1987 in Docket No. 840315-WS, In re: Application of Martin Downs Utilities, Inc., for increase in water and sewer rates in Martin County, Florida, p. 3.

the private lift station (PLS) customers should be charged the same BFC as other service classes, but that those customers should be charged only 80% of the gallonage charge to recognize the reduced costs of service to the PLS owners. The reduced cost of service stems from the PLS owners paying for their own electrical pumping power and maintenance of the lift station.<sup>15</sup>

Staff believes the circumstances in the instant case match those circumstances from both prior cases referenced above. As discussed previously, staff recommends that the homeowners' association, rather than the individual customers, be the customer of record. This would reflect savings to the utility in billing and bookkeeping. Furthermore, because the customers own their lift station, there is a reduced cost to serve the customers because the customers, not the utility, are paying for the electrical pumping power and maintenance of the lift station. Therefore, staff recommends that the appropriate wastewater rate structure for DeeAnn's residents is a bulk rate BFC/gallonage charge rate structure. The BFC should be based on 80% of the ERCs actually connected to the system, while the gallonage charge should be set at 20% less than the general service wastewater gallonage charge to reflect the fact that DeeAnn pays for all costs associated with its lift station. The resulting recommended gallonage charge for DeeAnn's residents is slightly less than staff's recommended residential gallonage charge. Staff's recommended bulk rate also gives consideration to DeeAnn's residents for their added cost and over-head of the lift station.

Staff noticed during its analysis that the current gallonage charge for multi-residential service is equal to the gallonage charge for residential service. This is incorrect – the multi-residential service gallonage charge should be set equal to the general service gallonage charge rate. This is to correctly reflect the anticipation that approximately 80% of residential water consumption is returned to the wastewater system, while approximately 100% of multi-residential and general service water consumption is returned to the wastewater system.

Staff obtained test year 2005 water flow data for DeeAnn Estates, and recalculated wastewater rates based on: 1) the application of the BFC/gallonage charge rate structure to all classes except for DeeAnn Estates; 2) the elimination of DeeAnn's residential wastewater-only flat rates replaced by a bulk rate BFC/gallonage charge rate structure; and 3) the correction of the multi-residential gallonage charge so that it was equal to the general service gallonage rate. Staff then calculated, by customer class and meter size, a comparison of typical bills based on average usage. The results, shown in Table 1 on the following page, indicate that the 71 residents at DeeAnn Estates have been subsidizing the remaining 117 customers of the utility.

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<sup>15</sup> Order No. PSC-02-1165-PAA-SU, issued August 26, 2002 in Docket No. 020520-SU, In re: Complaint by Safe Harbor marina against K W Resort Utilities Corp. and request for new class of service for bulk wastewater rate in Monroe County, p. 3; Order No. 13862, issued November 19, 1984 in Docket No. 830388-S, In re: Application of Stock Island Utility Company, Inc., for increased sewer rates to its customers in Monroe County, Florida, p. 3.

TABLE 1

<b>LAKE PLACID UTILITIES, INC.</b>					
<b>REVISED WASTEWATER RATE STRUCTURE:</b>					
<b>CUSTOMERS' CHANGE IN AVERAGE MONTHLY BILLS</b>					
<b>Customer Class</b>	<b>Average Kgal per Month</b>	<b>Bill Under Current Rate Structure</b>	<b>Bill Under Recom Rate Structure</b>	<b>Amt Chg in Bill</b>	<b>Pct Chg in Bill</b>
Residential 5/8"	2.100	\$19.73	\$27.28	\$7.55	38%
Gen Serv 5/8"	7.189	\$36.58	\$60.82	\$24.25	66%
Multi Resid 5/8"	0.833	\$16.45	\$21.62	\$5.17	31%
Gen Serv 1"	18.750	\$93.83	\$156.85	\$63.03	67%
Multi Resid 1"	8.250	\$57.07	\$92.09	\$35.02	61%
DeeAnn Estates / Multi Resid 2" (1)	140.667	\$23.51	\$17.68	(\$5.83)	(25%)
Gen Serv 4"	197.385	\$968.75	\$1,629.48	\$660.73	68%
Multi Resid 4"	20.792	\$410.71	\$540.26	\$129.55	32%

(1) DeeAnn Estates customers currently billed \$23.51 per unit per month. Bill under recommended rate structure is based on (monthly sum of charge for 2" BFC plus monthly charge for average water usage of 140.667 kgal.) divided by 71 units.

**Source:** Lake Placid Utility Company, MFRs, Schedule No. E-2; Short Utility Services, 2005 monthly water well flow data for DeeAnn Estates.

As shown on Schedule No. 3-B, staff recommends that the wastewater revenue requirement be increased by approximately 26%. As shown in Table 1, under staff's recommended wastewater rate structures, the average bill for a resident of DeeAnn Estates would decrease by 25 percent, while the average bills for all other customers would increase between 31% and 68%. The subsidization of the remaining wastewater customers by the residents of DeeAnn Estates represents a rate structure inequity. Staff believes such inequities, when discovered, must be corrected.

Based on the foregoing, the appropriate rate structure for the water system is a continuation of the current BFC/uniform gallonage charge rate structure. The residential wastewater-only flat rate structure should be discontinued and replaced with a bulk wastewater rate based on a BFC/gallonage charge rate structure. The bulk customers' BFC should be based on 80% of the number of equivalent residential connections actually connected to the system, while the gallonage charge should be set at 80% of the general service gallonage charge. The traditional BFC/gallonage charge rate structure should be continued for the remaining wastewater customers. The BFC cost recovery should be set at 54.6% for the water system and 50% for the wastewater system. The multi-residential gallonage charge rate should be set at an amount equal to the general service gallonage charge rate.

**Issue 19:** What are the appropriate rates for monthly service for the water and wastewater systems?

**Recommendation:** The appropriate water and wastewater rates are shown in Schedule Nos. 4-A and 4-B. (Rendell, Lingo)

**Staff Analysis:** As discussed in Issue 17, staff recommends that the appropriate revenue requirements are \$56,579 for the water system and \$90,634 for the wastewater system. Excluding miscellaneous service revenues of \$398 for the water system and \$0 for the wastewater system, the resulting revenues from monthly service \$56,181 for the water system and \$90,634 for the wastewater system.

As discussed in Issue 18, staff recommends that the appropriate rate structure for the water system is a continuation of the current BFC/uniform gallonage charge rate structure. The residential wastewater-only flat rate structure should be discontinued and replaced with a bulk wastewater rate based on a BFC/gallonage charge rate structure. The bulk customers' BFC should be based on 80% of the number of equivalent residential connections actually connected to the system, while the gallonage charge should be set at 80% of the general service gallonage charge. The traditional BFC/gallonage charge rate structure should be continued for the remaining wastewater customers. The BFC cost recovery should be set at 54.6% for the water system and 50% for the wastewater system. The multi-residential gallonage charge rate should be set at an amount equal to the general service gallonage charge rate.

Approximately 54.6% of the monthly service revenues for the water system (or \$30,667) and 50% of the corresponding wastewater system revenues (or \$45,304) are recovered through the base facility charges. Approximately 45.4% of the monthly service revenues for the water system (or \$25,517) and 50% of the corresponding wastewater system revenues (or \$45,327) represents revenue recovery through the consumption charges.

Based on the foregoing, the appropriate rates for monthly service for the water and wastewater systems are shown on Schedules Nos. 4-A and 4-B.

**Issue 20:** What is the appropriate amount by which rates should be reduced four years after the established effective date to reflect the removal of the amortized rate case expense as required by Section 367.0816, F.S.?

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

**Staff Analysis:** Section 367.0816, F.S., requires rates to be reduced immediately following the expiration of the four-year amortization period by the amount of the rate case expense previously included in the rates. The reduction will reflect the removal of revenues associated with the amortization of rate case expense and the gross-up for regulatory assessment fees. The decreased water and wastewater revenues will result in the rate reduction recommended by staff on Schedule Nos. 4-A and 4-B.

The utility should be required to file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The utility should be required to file revised tariffs and a proposed customer notice setting forth the lower rates and the reason for the reduction no later than one month prior to the actual date of the required rate reduction. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice. The utility should provide proof of the date notice was given no less than ten days after the date of the notice.

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

**Issue 21:** Should the utility be authorized to revise its miscellaneous service charges, and, if so, what are the appropriate charges?

**Recommendation:** Yes. The utility should be authorized to revise its miscellaneous service charges. The appropriate charges are reflected below. The utility should file a proposed customer notice to reflect the Commission-approved charges. The approved charges should be effective for service rendered on or after the stamped approval date of the tariff, pursuant to Rule 25-30.475(1), F.A.C., provided the notice has been approved by staff. Within 10 days of the date the order is final, the utility should be required to provide notice of the tariff changes to all customers. The utility should provide proof the customers have received notice within 10 days after the date that the notice was sent. (Rendell)

**Staff Analysis:** The miscellaneous service charges currently in effect were approved for Lake Placid in 1993, and have not changed since that date. Similar charges have been the standard charge in other cases since at least 1990 - a period of 16 years. Staff believes these charges should be updated to reflect current costs. Staff recommends that Lake Placid be allowed to increase its water and wastewater miscellaneous service charges from \$15 to \$21 for normal hours and from \$15 to \$42 for after hours, and to modify its Premises Visit (in lieu of disconnection) charge. If both water and wastewater services are provided, a single charge is appropriate unless circumstances beyond the control of the utility requires multiple actions. The current and recommended charges are shown below.

Water Miscellaneous Service Charges

	<u>Current Charges</u>		<u>Staff Recommended</u>	
	<u>Normal Hrs</u>	<u>After Hrs</u>	<u>Normal Hrs</u>	<u>After Hrs</u>
Initial Connection	\$15	N/A	\$21	N/A
Normal Reconnection	\$15	N/A	\$21	\$42
Violation Reconnection	\$15	N/A	\$21	\$42
Premises Visit (in lieu of disconnection)	\$10	N/A	N/A	N/A
Premises Visit	N/A	N/A	\$21	\$42

Wastewater Miscellaneous Service Charges

	<u>Current Charges</u>		<u>Staff Recommended</u>	
	<u>Normal Hrs</u>	<u>After Hrs</u>	<u>Normal Hrs</u>	<u>After Hrs</u>
Initial Connection	\$15	N/A	\$21	N/A
Normal Reconnection	\$15	N/A	\$21	\$42
Violation Reconnection	Actual Cost	N/A	Actual Cost	Actual Cost
Premises Visit (in lieu of disconnection)	\$10	N/A	N/A	N/A
Premises Visit	N/A	N/A	\$21	\$42

The general industry-wide miscellaneous service charges have not been updated in over 16 years and costs for fuel and labor have risen substantially since that time. Further, the Commission's price index has increased approximately 60% in that period of time. The Commission has expressed concern with miscellaneous service charges that fail to compensate utilities for the cost incurred. By Order No. PSC-96-1320-FOF-WS, issued October 30, 1996, involving Southern States Utilities Inc.,<sup>16</sup> the Commission expressed "concern that the rates [miscellaneous service charges] are eight years old and cannot possibly cover current costs" and directed staff to "examine whether miscellaneous service charges should be indexed in the future and included in index applications." Currently, miscellaneous service charges may be indexed if requested in price index applications pursuant to Rule 25-30.420, F.A.C. However, few utilities request their miscellaneous service charges be indexed. Staff believes a \$21 charge is reasonable and is cost based. By Order No. PSC-06-0684-PAA-WS, issued August 8, 2006,<sup>17</sup> and by Order No. PSC-05-0776-TRF-WS, issued July 26, 2005,<sup>18</sup> the Commission approved a \$20 charge for connection and reconnections during normal hours and a \$40 after hours charge.

In summary, staff recommends the utility's miscellaneous service charges for normal hours of \$21 and after hours charges of \$42, be approved because the increased charges are cost-based, reasonable, and consistent with fees the Commission has approved for other utilities. The utility should file a proposed customer notice to reflect the Commission-approved charges. The approved charges should be effective for service rendered on or after the stamped approval date of the tariff, pursuant to Rule 25-30.475(1), F.A.C., provided the notice has been approved by staff. Within ten days of the date the order is final, the utility should be required to provide notice of the tariff changes to all customers. The utility should provide proof the customers have received notice within ten days after the date the notice was sent.

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<sup>16</sup> Docket No. 950495-WS, In Re: Application for rate increase and increase in service availability charges by Southern States Utilities, Inc. for Orange-Osceola Utilities, Inc. in Osceola County, and in Bradford, Brevard, Charlotte, Citrus, Clay, Collier, Duval, Highlands, Lake, Lee, Marion, Martin, Nassau, Orange, Osceola, Pasco, Putnam, Seminole, St. Johns, St. Lucie, Volusia, and Washington Counties.

<sup>17</sup> Docket 050587-WS, In re: Application for staff-assisted rate case in Charlotte County by MSM Utilities, LLC.

<sup>18</sup> Docket No. 050369-TRF-WS, In re: Request for approval of change in meter installation fees and proposed changes in miscellaneous services charges in Pasco County by Mad Hatter Utility, Inc.

**Other Issues**

**Issue 22:** Should the utility be required to provide proof that it has adjusted its books for all Commission approved adjustments?

**Recommendation:** Yes. To ensure that the utility adjusts its books in accordance with the Commission's decision, Lake Placid should provide proof, within 90 days of the issuance of the Consummating Order, that the adjustments for all the applicable NARUC USOA primary accounts have been made. (Rendell)

**Staff Analysis:** To ensure that the utility adjusts its books in accordance with the Commission's decision, staff recommends that Lake Placid should provide proof, within 90 days of the issuance of the Consummating Order, that the adjustments for all the applicable NARUC USOA primary accounts have been made.



**Issue 23:** Should this docket be closed?

**Recommendation:** No. If no person whose substantial interests are affected by the proposed agency action issues files a protest within 21 days of the issuance of the order, a Consummating Order will be issued. However, the docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the utility and approved by staff. When the PAA issues are final and the tariff and notice actions are complete, this docket may be closed administratively. (Fleming, Rendell)

**Staff Analysis:** No. If no person whose substantial interests are affected by the proposed agency action issues files a protest within 21 days of the issuance of the order, a Consummating Order will be issued. However, the docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the utility and approved by staff. When the PAA issues are final and the tariff and notice actions are complete, this docket may be closed administratively.

Lake Placid Utilities Inc. of Florida  
Water Treatment System Without Storage  
Used and Useful Analysis

1	Firm Reliable Capacity		200 gpm
2	Demand		91 gpm
	a Maximum Day (131,000 gpd)	91 gpm	
	b 5 Max Day Average (76,600 gpd)	53 gpm	
	c Average Daily Flow (25,584 gpd)	18 gpm	
3	Excessive Unaccounted for Water = a-b		3.04 gpm
	a Total Unaccounted for Water (26.92%)	4.84 gpm	
	b 10% of Average Daily Flow	1.80 gpm	
4	Required Fire Flow		500 gpm
5	Growth = $((2/5a) \times 5b \times 5 \text{ yrs})$		9.4 gpm
	a Average Test Year Customers	243 ERCs	
	b Annual Customer Growth	5	
6	Used and Useful = $[2^{19} \times (2 - 3 + 5) + 4]/1$		100+%
	$[(2(91 - 3.04 + 9.4) + 500)/200]$		

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<sup>19</sup> Peak Factor

Lake Placid Utilities Inc. of Florida  
Wastewater Treatment System  
Used and Useful Analysis

1	Permitted Capacity (AADF)		90,000 gpd
2	Demand (AADF)		15,597 gpd
3	Excessive Infiltration and Inflow (I&I)		0 gpd
	a Water demand per ERC	70.6 gpd	
	b AADF per ERC	48.7 gpd	
4	Growth = ((70.6 x 4b x 5 yrs)		1,218 gpd
	a Average Test Year Customers	320 ERCs	
	b Customer Growth	5 ERCs	
5	Used and Useful = (2 – 3 + 4)/1		18.68%
	Staff recommended		30.46%

Note – Staff recommends that the used and useful percentage (30.46%) approved in the utility's last rate case in Order No. PSC-96-0910-FOF-WS be used because of the age of the system and the limited growth possibilities for the service area.

Lake Placid Utilities, Inc. Schedule of Water Rate Base Test Year Ended 12/31/05		Schedule No. 1-A Docket No. 060260-WS				
		Test Year	Utility	Adjusted	Staff	Staff
		Per	Adjust-	Test Year	Adjust-	Adjusted
	Description	Utility	ments	Per Utility	ments	Test Year
1	Plant in Service	<u>\$320,753</u>	<u>\$39,279</u>	\$360,032	(\$48,968)	\$311,064
2	Utility Land & Land Rights	<u>\$2,707</u>	<u>\$0</u>	\$2,707	\$0	\$2,707
3	Construction Work in Progress	<u>\$14,528</u>	<u>(\$14,528)</u>	\$0	\$0	
4	Non-used and Useful Components	<u>\$0</u>	<u>\$0</u>	\$0	\$0	\$0
5	Accumulated Depreciation	<u>(\$123,370)</u>	<u>\$30,983</u>	(\$92,387)	(\$14,241)	(\$106,628)
6	CIAC	<u>(\$89,440)</u>	<u>\$0</u>	(\$89,440)	\$0	(\$89,440)
7	Amortization of CIAC	<u>\$39,772</u>	<u>\$0</u>	\$39,772	\$0	\$39,772
8	Acquisition Adjustment	<u>\$0</u>	<u>\$0</u>	\$0	\$0	\$0
9	Accum Amort of Acq Adjustment	<u>\$9,204</u>	<u>\$0</u>	\$9,204	(\$9,204)	\$0
10	Working Capital Allowance	<u>\$0</u>	<u>\$4,173</u>	\$4,173	(\$992)	\$3,181
11	Other	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
12	<b>Rate Base</b>	<u>\$174,154</u>	<u>\$59,907</u>	<u>\$234,061</u>	<u>(\$73,405)</u>	<u>\$160,656</u>

Lake Placid Utilities, Inc. Schedule of Wastewater Rate Base Test Year Ended 12/31/05			Schedule No. 1-B Docket No. 060260-WS		
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Staff Adjust- ments	Staff Adjusted Test Year
1 Plant in Service	<u>\$560,019</u>	<u>(\$15,492)</u>	\$544,527	\$26,354	\$570,881
2 Utility Land & Land Rights	<u>\$21,665</u>	<u>\$0</u>	\$21,665	\$0	\$0
3 Construction Work in Progress	<u>\$0</u>	<u>(\$13,188)</u>	(\$13,188)	\$0	(\$13,188)
4 Non-used and Useful Components	<u>\$0</u>	<u>\$0</u>	\$0	(\$94,585)	(\$94,585)
5 Accumulated Depreciation	<u>(\$302,910)</u>	<u>(\$30)</u>	(\$302,940)	(\$12,139)	(\$315,079)
6 CIAC	<u>(\$154,466)</u>	<u>\$0</u>	(\$154,466)	\$0	(\$154,466)
7 Amortization of CIAC	<u>\$103,172</u>	<u>\$0</u>	\$103,172	\$0	\$103,172
8 CWIP	<u>\$0</u>	<u>\$0</u>	\$0	\$0	\$0
9 Advances for Construction	<u>\$0</u>	<u>\$0</u>	\$0	\$0	\$0
10 Working Capital Allowance	<u>\$0</u>	<u>\$9,390</u>	\$9,390	(\$1,438)	\$7,952
11 Other	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>
12 <b>Rate Base</b>	<u>\$227,480</u>	<u>(\$19,320)</u>	<u>\$208,160</u>	<u>(\$81,809)</u>	<u>\$104,686</u>

Lake Placid Utilities, Inc. Adjustments to Rate Base Test Year Ended 12/31/05		Schedule No. 1-C Docket No. 060260-WS	
Explanation	Water	Wastewater	
<u>Plant In Service</u>			
1	Unsupported Plant Additions (AF-1)	(\$14,150)	(\$3,093)
2	To reflect appropriate amount of historical plant	\$0	\$17,900
3	To adjust for unsupported Pro Forma Plant	(\$22,424)	(\$1,343)
4	Reflect appropriate WSC rate base allocation.	\$197	\$308
5	Reflect appropriate UIF rate base allocation.	<u>(\$12,591)</u>	<u>\$12,582</u>
	Total	<u>(\$48,968)</u>	<u>\$26,354</u>
<u>Non-used and Useful</u>			
	To reflect net non-used and useful adjustment	<u>\$0</u>	<u>(\$94,585)</u>
<u>Accumulated Depreciation</u>			
1	Unrecorded A/D (AF-2)	(\$4,555)	(\$4,424)
2	Reflect appropriate UIF rate base allocation.	\$7,350	(\$7,745)
3	To adjust for unsupported Pro Forma Plant	(\$17,036)	\$30
	Total	<u>(\$14,241)</u>	<u>(\$12,139)</u>
<u>Accum Amort of Acq Adjustment</u>			
	Remove Accum Amort of Acq Adj	<u>(\$9,204)</u>	<u>\$0</u>
	Total	<u>(\$9,204)</u>	<u>\$0</u>
<u>Working Capital</u>			
		<u>(\$992)</u>	<u>(\$1,438)</u>

Lake Placid Utilities, Inc.  
 Capital Structure-Simple Average  
 Test Year Ended 12/31/05

Schedule No. 2  
 Docket No. 060260-WS

Description	Total Capital	Specific Adjustments	Subtotal Adjusted Capital	Prorata Adjustments	Capital Reconciled to Rate Base	Ratio	Cost Rate	Weighted Cost
<b>Per Utility</b>								
1 Long-term Debt	\$124,044,203	\$0	\$124,044,203	(\$123,817,501)	\$226,702	52.35%	6.81%	3.57%
2 Short-term Debt	\$11,347,000	\$0	\$11,347,000	(11,326,262)	\$20,738	4.79%	2.00%	0.10%
3 Preferred Stock	\$0	\$0	\$0	0	\$0	0.00%	0.00%	0.00%
4 Common Equity	\$90,787,422	\$0	\$90,787,422	(90,621,500)	\$165,922	38.32%	11.77%	4.51%
5 Customer Deposits	\$0	\$0	\$0	0	\$0	0.00%	6.00%	0.00%
6 Deferred Income Taxes	<u>\$19,655</u>	<u>\$0</u>	<u>\$19,655</u>	<u>0</u>	<u>\$19,655</u>	<u>4.54%</u>	0.00%	<u>0.00%</u>
10 <b>Total Capital</b>	<u>\$226,198,280</u>	<u>\$0</u>	<u>\$226,198,280</u>	<u>(\$225,765,263)</u>	<u>\$433,017</u>	<u>100.00%</u>		<u>8.17%</u>
<b>Per Staff</b>								
11 Long-term Debt	\$124,044,203	\$0	\$124,044,203	(\$123,917,011)	\$127,192	47.93%	6.73%	3.23%
12 Short-term Debt	\$11,347,000	\$0	\$11,347,000	(\$11,335,365)	\$11,635	4.38%	2.00%	0.09%
13 Preferred Stock	\$0	\$0	\$0	\$0	\$0	0.00%	0.00%	0.00%
14 Common Equity	\$90,787,422	\$3,093,004	\$93,880,426	(\$93,784,163)	\$96,263	36.28%	11.45%	4.15%
15 Customer Deposits	\$0	\$1,602	\$1,602	\$0	\$1,602	0.60%	6.00%	0.04%
16 Deferred Income Taxes	<u>\$19,655</u>	<u>\$8,996</u>	<u>\$28,651</u>	<u>\$0</u>	<u>\$28,651</u>	<u>10.80%</u>	0.00%	<u>0.00%</u>
20 <b>Total Capital</b>	<u>\$226,198,280</u>	<u>\$3,103,602</u>	<u>\$229,301,882</u>	<u>(\$229,056,629)</u>	<u>\$265,342</u>	<u>100.00%</u>		<u>7.50%</u>
						<b>LOW</b>	<b>HIGH</b>	
					RETURN ON EQUITY	<u>10.45%</u>	<u>12.45%</u>	
					OVERALL RATE OF RETURN	<u>7.14%</u>	<u>7.87%</u>	

Lake Placid Utilities, Inc. Statement of Water Operations Test Year Ended 12/31/05						Schedule No. 3-A Docket No. 060260-WS	
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Staff Adjust- ments	Staff Adjusted Test Year	Revenue Increase	Revenue Requirement
1 <b>Operating Revenues:</b>	<u>\$45,173</u>	<u>\$30,239</u>	<u>\$75,412</u>	<u>(\$28,208)</u>	<u>\$47,204</u>	<u>\$9,375</u> 19.86%	<u>\$56,579</u>
<b>Operating Expenses</b>							
2 Operation & Maintenance	\$17,676	\$15,711	\$33,387	(\$7,939)	\$25,448		\$25,448
3 Depreciation	\$8,722	\$1,914	\$10,636	(\$878)	\$9,758		\$9,758
4 Amortization	(\$7,894)	\$7,894	\$0	\$0	\$0		\$0
5 Taxes Other Than Income	\$3,386	\$1,440	\$4,826	\$47	\$4,873	\$422	\$5,295
6 Income Taxes	(\$14,339)	\$20,868	\$6,529	(\$5,873)	\$656	\$3,369	\$4,025
7 <b>Total Operating Expense</b>	<u>\$7,551</u>	<u>\$47,827</u>	<u>\$55,378</u>	<u>(\$14,643)</u>	<u>\$40,735</u>	<u>\$3,791</u>	<u>\$44,526</u>
8 <b>Operating Income</b>	<u>\$37,622</u>	<u>(\$17,588)</u>	<u>\$20,034</u>	<u>(\$13,565)</u>	<u>\$6,469</u>	<u>\$5,584</u>	<u>\$12,053</u>
9 <b>Rate Base</b>	<u>\$174,154</u>		<u>\$234,061</u>		<u>\$160,656</u>		<u>\$160,656</u>
10 <b>Rate of Return</b>	<u>21.60%</u>		<u>8.56%</u>		<u>4.03%</u>		<u>7.50%</u>



Lake Placid Utilities, Inc.  
 Statement of Wastewater  
 Operations  
 Test Year Ended 12/31/05

		Test Year	Utility	Adjusted	Staff	Staff	Revenue	Revenue
		Per	Adjust-	Test Year	Adjust-	Adjusted	Increase	Requirement
Description		Utility	ments	Per Utility	ments	Test Year		
1	<b>Operating Revenues:</b>	<u>\$70,362</u>	<u>\$71,952</u>	<u>\$142,314</u>	<u>(\$70,271)</u>	<u>\$72,043</u>	<u>\$18,591</u> 25.81%	<u>\$90,637</u>
	<b>Operating Expenses</b>							
2	Operation & Maintenance	\$52,976	\$22,147	\$75,123	(\$11,506)	\$63,617		\$63,617
3	Depreciation	\$13,194	\$30	\$13,224	(\$5,802)	\$7,422		\$7,422
4	Amortization	\$529	(\$529)	\$0	\$0	\$0		\$0
5	Taxes Other Than Income	\$5,271	\$3,348	\$8,619	(\$337)	\$8,282	\$837	\$9,118
6	Income Taxes	<u>\$13,559</u>	<u>\$13,971</u>	<u>\$27,530</u>	<u>(\$31,588)</u>	<u>(\$4,058)</u>	<u>\$6,681</u>	<u>\$2,623</u>
7	<b>Total Operating Expense</b>	<u>\$85,529</u>	<u>\$38,967</u>	<u>\$124,496</u>	<u>(\$49,234)</u>	<u>\$75,262</u>	<u>\$7,518</u>	<u>\$82,780</u>
8	<b>Operating Income</b>	<u>(\$15,167)</u>	<u>\$32,985</u>	<u>\$17,818</u>	<u>(\$21,037)</u>	<u>(\$3,219)</u>	<u>\$11,073</u>	<u>\$7,854</u>
9	<b>Rate Base</b>	<u>\$227,480</u>		<u>\$208,160</u>		<u>\$104,686</u>		<u>\$104,686</u>
10	<b>Rate of Return</b>	<u>-6.67%</u>		<u>8.56%</u>		<u>-3.08%</u>		<u>7.50%</u>

<b>Lake Placid Utilities, Inc.</b>		<b>Schedule 3-C</b>	
<b>Adjustment to Operating Income</b>		<b>Docket No. 060260-WS</b>	
<b>Test Year Ended 12/31/05</b>			
<b>Explanation</b>	<b>Water</b>	<b>Wastewater</b>	
<u>Operating Revenues</u>			
1 Remove requested final revenue increase	(\$30,017)	(\$71,902)	
2 To reflect the appropriate amount of annualized revenues.	<u>\$1,809</u>	<u>\$1,631</u>	
Total	<u>(\$28,208)</u>	<u>(\$70,271)</u>	
<u>Operation and Maintenance Expense</u>			
1 To properly record the utility's misc exp (AF-6)	\$0	(\$2,606)	
2 Adjustment to Proforma Salaries and Benefits	(\$753)	(\$801)	
3 Adjustment to Rate Case Expense	(\$6,745)	(\$8,415)	
4 To reflect the appropriate WSC allocated expenses.	\$62	\$81	
5 To reflect the appropriate UIF allocated expenses.	\$178	\$235	
6 Adjustment for excessive accounted for water	(\$681)	\$0	
Total	<u>(\$7,939)</u>	<u>(\$11,506)</u>	
<u>Depreciation Expense – Net</u>			
1 Unsupported Plant Additions (AF-1)	(\$725)	(\$71)	
2 Unrecorded A/D (AF-2)	\$371	\$306	
3 To adjust understated DE (AF-8)	\$1,311	\$527	
4 To remove net depreciation on non-U&U adjustment above.	\$0	(\$8,206)	
5 Reflect appropriate WSC rate base allocation.	\$12	\$16	
6 Reflect appropriate UIF rate base allocation.	(\$764)	\$1,656	
7 To adjust for unsupported Pro Forma Plant	<u>(\$1,083)</u>	<u>(\$30)</u>	
Total	<u>(\$878)</u>	<u>(\$5,802)</u>	
<u>Taxes Other Than Income</u>			
1 RAFs on revenue adjustments above	(\$1,269)	(\$3,162)	
2 To adjust understated TOTI (AF-9)	\$468	\$2,064	
3 To the appropriate WSC allocated property taxes.	(\$4)	(\$6)	
4 Adjustment to Payroll Taxes	(\$78)	(\$96)	
5 To reflect reduced property taxes on NU & U Property.	\$0	(\$589)	
6 To reflect appropriate TY RAFs	<u>\$931</u>	<u>\$1,451</u>	
Total	<u>\$47</u>	<u>(\$337)</u>	

<b>Lake Placid Utilities, Inc.</b>					<b>Schedule No. 4-A</b>
<b>Water Monthly Service Rates</b>					<b>Docket No. 060260-WS</b>
<b>Test Year Ended 12/31/05</b>					
	<b>Rates Prior to Filing</b>	<b>Commission Approved Interim</b>	<b>Utility Requested Final</b>	<b>Staff Recomm. Final</b>	<b>Four-year Rate Reduction</b>
<b><u>Residential, Multi-Residential and General Service</u></b>					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	\$12.59	\$0.00	\$12.20	\$12.59	\$ 1.81
3/4"	\$18.87	\$0.00	\$18.30	\$18.89	\$ 2.72
1"	\$31.45	\$0.00	\$30.51	\$31.48	\$ 4.53
1 1/2"	\$62.92	\$0.00	\$61.01	\$62.95	\$ 9.05
2"	\$100.67	\$0.00	\$97.62	\$100.72	\$14.48
3"	\$201.33	\$0.00	\$195.24	\$201.44	\$28.96
4"	\$315.61	\$0.00	\$305.06	\$314.75	\$45.25
6"	\$629.15	\$0.00	\$610.12	\$629.50	\$90.50
Gallorage Charge, per 1,000 Gallons	\$2.29	\$0.00	\$6.34	\$3.64	\$ 0.52
<b><u>Typical Residential Bills 5/8" x 3/4" Meter</u></b>					
3,000 Gallons	\$19.46	\$0.00	\$31.22	\$23.51	
5,000 Gallons	\$24.04	\$0.00	\$43.90	\$30.79	
10,000 Gallons	\$35.49	\$0.00	\$75.60	\$48.99	

<b>Lake Placid Utilities, Inc.</b>		<b>SCHEDULE NO. 4-B</b>			
<b>Wastewater Monthly Service Rates</b>		<b>Docket No. 060260-WS</b>			
<b>Test Year Ended 12/31/05</b>					
	<b>Rates</b>	<b>Commission</b>	<b>Utility</b>	<b>Staff</b>	<b>Four-year</b>
	<b>Prior to</b>	<b>Approved</b>	<b>Requested</b>	<b>Recomm.</b>	<b>Rate</b>
	<b>Filing</b>	<b>Interim</b>	<b>Final</b>	<b>Final</b>	<b>Reduction</b>
<b><u>Residential</u></b>					
Base Facility Charge :					
5/8"	\$14.29	\$0.00	\$15.41	\$16.48	\$ 1.88
All other meter sizes	--	--	--	\$16.48	\$1.88
DeeAnn Estates (flat rate per unit)	\$23.51	\$0.00	\$25.35	--	--
Gallonage Charge - Per 1,000 gallons					
(6,000 gallon cap)	\$2.59	\$0.00	\$12.10	\$5.14	\$0.59
<b><u>General Service/Multi-Residential</u></b>					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	\$14.29	\$0.00	\$15.41	\$16.48	\$1.88
3/4"	\$21.39	\$0.00	\$23.11	\$24.72	\$2.82
1	\$35.70	\$0.00	\$38.52	\$41.20	\$4.71
1-1/2"	\$71.37	\$0.00	\$77.04	\$82.40	\$9.41
2"	\$114.20	\$0.00	\$123.27	\$131.84	\$15.06
3"	\$228.39	\$0.00	\$246.53	\$263.68	\$30.12
4"	\$356.86	\$0.00	\$385.21	\$412.01	\$47.06
6"	\$713.74	\$0.00	\$770.41	\$824.03	\$94.13
DeeAnn Estates HOA (bulk rate)	--	--	--	\$561.66	\$64.16
Gallonage Charge (GS/MS), per 1,000 gallons	\$3.10	\$0.00	\$14.52	\$6.17	\$0.70
Gallonage Charge – DeeAnn Estates HOA (bulk rate) per 1,000 gallons	--	--	--	\$4.93	\$0.56
<b><u>Typical Residential Bills 5/8" x 3/4" Meter</u></b>					
3,000 Gallons	\$31.28	\$0.00	\$58.97	\$31.90	
5,000 Gallons	\$36.46	\$0.00	\$88.01	\$42.18	
10,000 Gallons	\$39.05	\$0.00	\$102.53	\$47.32	
(Wastewater Gallonage Cap - 6,000 Gallons)					