

State of Florida



Public Service Commission

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

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

DATE: April 26, 2007

TO: Commission Clerk (Cole)

FROM: Division of Economic Regulation (Revell, Rendell, Springer)
Office of the General Counsel (Fleming)

RE: Docket No. 060257-WS – Application for increase in water and wastewater rates in Polk County by Cypress Lakes Utilities, Inc.

AGENDA: 05/08/07 – Regular Agenda – Acknowledging Implementation of Proposed Agency Action Rates - Participation is at the Discretion of the Commission

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Pending

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: Place next to Docket No. 060258-WS

FILE NAME AND LOCATION: S:\PSC\ECR\WP\060257.RCM.DOC

Case Background

Cypress Lakes Utilities, Inc. (Cypress Lakes or utility) is a Class B utility providing water and wastewater service to approximately 1,287 residential and 43 general service customers in Polk County. The utility is a wholly-owned subsidiary of Utilities, Inc. (UI). Water and wastewater rates were last established for this utility in its 2002 proceeding.¹

On May 15, 2006, Cypress Lakes filed the Application for Rate Case at issue in the instant docket. By Order No. PSC-07-0199-PAA-WS (PAA Order), issued March 5, 2007, the

¹ See Order No. PSC-03-0647-PAA-WS, issued May 28, 2003, in Docket No. 020407-WS, In re: Application for rate increase in Polk County by Cypress Lakes Utilities, Inc.

Commission approved rates that were designed to generate a water revenue requirement of \$297,976 and a wastewater revenue requirement of \$508,186.

On March 26, 2007, Cypress Lakes Associates, Ltd., a developer, timely filed a protest of the proposed service availability charges proposed by this order. On April 6, 2007, the Office of Public Counsel (OPC) filed a cross-petition to protest the PAA order pursuant to Rule 25-22.029(3), Florida Administrative Code (F.A.C.). By letter dated April 9, 2007, Cypress Lakes stated that it intends to put the PAA Order rates in effect during the pendency of the administrative hearing.

The Commission will also be considering whether to acknowledge the implementation of the PAA rates of another UI subsidiary at the May 8, 2007, Agenda Conference. Sanlando Utilities Corporation (Sanlando) also filed an Application for Rate Increase in Docket No. 060258-WS on May 15, 2006. By Order No. PSC-07-0205-PAA-WS ("Sanlando PAA Order"), issued March 6, 2007, the Commission approved increased PAA rates and charges, which included annual revenue increases of \$404,581 for water and \$664,394 for wastewater. On March 27, 2007, the OPC filed a protest of the PAA Order. On April 5, 2007, Sanlando timely filed a cross-protest of the Sanlando PAA Order. By letter dated April 9, 2007, Sanlando stated that it also intends to put the Sanlando PAA Order rates in effect during the pendency of the administrative hearing.

This recommendation addresses the implementation of the PAA rates and the security to guarantee the increased revenues collected under the PAA rates for Cypress Lakes. The Commission has jurisdiction pursuant to Section 367.081, Florida Statutes, (F.S.).

Discussion of Issues

Issue 1: Should the Commission acknowledge the implementation of the proposed agency action rates by Cypress Lakes Utilities, Inc.?

Recommendation: Yes. The Commission should acknowledge the utility's implementation of the proposed agency action rates on a temporary basis pending the outcome of this rate proceeding. (Revell, Fleming)

Staff Analysis: As discussed in the Case Background, the PAA order was protested by a developer and a cross petition was filed by the OPC. On April 9, 2007, Cypress Lakes submitted its notice of intent to implement rates pursuant to Section 367.081(8), F.S., pending the resolution of the protest filed in this docket. The utility also submitted tariff sheets and a proposed customer notice.

Section 367.081(8), F.S., states:

At the expiration of 5 months following the official filing date, if the commission has not taken action or, if the commission's action is protested by a party other than the utility, the utility may place its requested rates into effect under bond, escrow, or corporate undertaking subject to refund, upon notice to the commission and upon filing the appropriate tariffs.

The filing of OPC's objection triggers the applicability of subsection 367.081(8), F.S., and the utility should be allowed to implement the PAA rates as requested by the utility. Although the utility has the right to implement its requested final rates, Cypress Lakes has elected to implement the rates approved by the Commission in the PAA order. These Commission-approved rates are lower than the rates requested by the utility in its filing.

Staff reviewed the tariff sheets and the proposed customer notice. Once the utility has provided the appropriate security, the effective date can be established and incorporated in the tariff sheets and customer notice. The security for the rate increase is discussed further in Issue 2. Based on the above, staff recommends that the Commission acknowledge the utility's implementation of the PAA rates on a temporary basis pending the outcome of this rate proceeding.

Issue 2: What is the appropriate security to guarantee the increased revenues collected under the temporary proposed agency action rates?

Recommendation: The utility should be required to open an escrow account or file a surety bond to guarantee any potential refund of revenues collected under interim conditions. If the security provided is an escrow account, the utility should deposit 16.81% of water and 39.22% of wastewater revenues into the escrow account each month. Otherwise, the surety bond should be in the amount of \$158,475. Pursuant to Rule 25-30.360(6), F.A.C., the utility should provide a report by the 20th of each month indicating the monthly and total revenue collected subject to refund. Should a refund be required, the refund should be with interest and undertaken in accordance with Rule 25-30.360, F.A.C. (Revell, Springer)

Staff Analysis: As discussed in Issue 1, the utility may place its requested rates into effect under bond, escrow, or corporate undertaking subject to refund pursuant to Section 367.081(8), F.S. In addition to allowing the utility to implement its requested rates, the statute requires that “[t]he utility shall keep accurate records of amounts received as provided by subsection (6).” Subsection (6) specifies that “[t]he utility shall keep accurate, detailed accounts of all amounts received because of such rates becoming effective under bond, escrow, or corporate undertaking subject to refund, specifying by whom and in whose behalf such amounts were paid.”

Pursuant to the PAA Order, the Commission approved PAA rates and charges for Cypress Lakes, which included an annual revenue increase of \$42,874 for water and \$143,167 for wastewater. In addition, by Order No. PSC-07-0205-PAA-WS, issued March 6, 2007, the Commission approved PAA rates and charges for Sanlando Utilities Corporation (Sanlando), which included an annual revenue increase of \$404,581 for water and \$664,394 for wastewater. By letter dated April 9, 2007, Sanlando also stated that it intends to put the PAA Order rates in effect during the pendency of the administrative hearing in Docket No. 060258-WS.

Cypress Lakes and Sanlando are wholly-owned subsidiaries of UI, which provides all investor capital to its subsidiaries. UI’s present cumulative corporate undertaking amount is \$1,784,788. UI has requested an additional corporate undertaking to secure the implementation of temporary PAA rates granted for Cypress Lakes and Sanlando. In accordance with Rule 25-30.360, F.A.C., staff has calculated the potential refund of revenues and interest collected to be \$158,475 for Cypress Lakes and \$910,583 for Sanlando. The total incremental amount of \$1,069,057 is based on an estimated ten months of revenue being collected. Adding the total incremental amount for Cypress Lakes and Sanlando, the total cumulative corporate undertaking amount would be \$2,853,845 (\$1,784,788 plus \$1,069,057).

The criteria for a corporate undertaking includes sufficient liquidity, ownership equity, profitability, and interest coverage to guarantee any potential refund. Staff reviewed the financial statements of the parent company to determine if UI can support an additional corporate undertaking on behalf of its subsidiaries. UI’s 2004, 2005, and 2006 financial statements were used to determine the financial condition of the Company. UI’s average equity ratio over the most recent three-year period has remained stable at 40%. In addition, UI’s relative level of liquidity has improved compared to 2005. However, both the Company’s interest coverage and relative level of net income have declined over the three year review period. In addition, if granted, UI’s total cumulative corporate undertaking outstanding of approximately \$2.9 million

would represent 78% of the parent Company's average annual net income in 2005 and 2006. Based upon this analysis, staff recommends that UI cannot support any incremental amount of corporate undertaking above the current cumulative amount of \$1,784,788. Therefore, staff recommends that the utility provide a surety bond or escrow agreement to guarantee the funds collected subject to refund.

If the security provided is an escrow account, the utility should deposit 16.81% of water and 39.22% of wastewater revenues into the escrow account each month. In addition, the following conditions shall be part of the agreement:

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

If the security provided is a surety bond, said instrument should be in the amount of \$158,475. In addition, the surety bond should state that it will be released or should terminate only upon subsequent order of the Commission.

Docket No. 060257-WS

Date: April 26, 2007

Regardless of the type of security provided, the utility should keep an accurate and detailed account of all monies it receives. Pursuant to Rule 25-30.360(6), F.A.C., the utility shall provide a report by the 20th day of each month indicating the monthly and total revenue collected subject to refund. Should a refund be required, the refund should be with interest and undertaken in accordance with Rule 25-30.340, F.A.C. In no instance should maintenance and administrative costs associated with any refund be borne by the customers. The costs are the responsibility of, and should be borne by, the utility.

Docket No. 060257-WS

Date: April 26, 2007

Issue 3: Should this docket be closed?

Recommendation: No. This docket should remain open to complete the hearing process.
(Fleming, Revell)

Staff Analysis: Because a protest has been filed to the Proposed Agency Action Order No. PSC-07-0199-PAA-WS, the docket should remain open to complete the hearing process.