

State of Florida



## Public Service Commission

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

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

---

**DATE:** August 29, 2007

**TO:** Office of Commission Clerk (Cole)

**FROM:** Division of Economic Regulation (Revell, Rendell, Bulecza-Banks)  
Office of the General Counsel (Brubaker)

**RE:** Docket No. 030106-SU – Application for staff-assisted rate case in Lee County by  
Environmental Protection Systems of Pine Island, Inc.  
County: Lee

**AGENDA:** 09/11/07 – Regular Agenda – Interested Persons May Participate

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** McMurrian

**CRITICAL DATES:** None

**SPECIAL INSTRUCTIONS:** None

**FILE NAME AND LOCATION:** S:\PSC\ECR\WP\030106.RCM.DOC

---

### Case Background

Environmental Protection Systems of Pine Island, Inc. (EPS or utility) is a Class C wastewater utility serving approximately 462 customers in Cherry Estates and R.V. Park in St. James City, which is located at the southern end of Pine Island, approximately 30 miles from Fort Myers. On January 30, 2003, EPS filed an application for a staff-assisted rate case (SARC). By Order No. PSC-03-1119-PAA-SU (SARC Order), the Commission approved the utility's current rates, charges, and rate base on October 7, 2003.<sup>1</sup> A portion of the approved rate base included pro forma additions to plant.

---

<sup>1</sup> Order No. PSC-03-1119-PAA-SU, issued October 7, 2003, in Docket No. 030106-SU, In re: Application for staff-assisted rate case in Lee County by Environmental Protection Systems of Pine Island, Inc.

Prior to filing its rate case in 2003, the Florida Department of Environmental Protection (DEP) renewed EPS's operating permit. However, the DEP advised the utility that future renewals could be in jeopardy due to the environmentally sensitive location of the utility's plant. Staff believed that due to the advanced age of the facility, DEP would require costly repairs and replacements before any additional operating permits would be granted.

At the time the utility filed its SARC, it considered two options in determining the most prudent and cost effective method of meeting future requirements. These options were to interconnect with Pine Island Regional Treatment System (PIRTS), or to construct a new wastewater treatment facility off-site. In the SARC Order, the Commission calculated the revenue requirement for each option, and determined the interconnection to the county facility was the most prudent and cost effective option. EPS reached an agreement with Lee County Utilities whereby EPS's treatment facility would be taken off line and EPS would interconnect with PIRTS.

At the time of the rate case, the utility expected to interconnect with PIRTS four to six months after the Commission approved its rate increase. As construction had not begun on the facilities needed to interconnect, the Commission Order was based on the necessary projected plant, retirements, cost of removal and expenses to interconnect. In Order No. PSC-03-1119A-PAA-SU (Amendatory SARC Order),<sup>2</sup> the Commission required the utility to complete the construction and interconnection within nine months of the issuance date of the Consummating Order, i.e., August 10, 2004. According to the utility, it encountered many problems and delays and the interconnection did not occur until September 20, 2005.

By letter dated November 16, 2004, the utility agreed to hold revenues from the date of the Order subject to refund pending a true up of the actual construction costs versus the projected costs in the Order. By Order No. PSC-07-0426-PAA-SU (Refund Order), issued May 15, 2007, the Commission ordered the utility to make certain refunds of revenues collected since the company failed to place the interconnect facility in service in the projected timeframe. Refunds were ordered that covered the period from November 15, 2003, through the date rates were changed.

On June 1, 2007, the utility filed a timely protest of the Refund Order. On June 19, 2007, the utility submitted its initial Settlement Proposal (Initial Proposal). On July 20, 2007, after additional discussions with Commission staff, the utility submitted a revised Settlement Proposal (Revised Proposal).

This recommendation addresses the revised settlement proposal. The Commission has the authority to consider this case pursuant to Section 367.0814, Florida Statutes.

---

<sup>2</sup> Order No. PSC-03-1119A-PAA-SU, issued November 10, 2003, in Docket No. 030106-SU, In re: Application for staff-assisted rate case in Lee County by Environmental Protection Systems of Pine Island, Inc.

### Discussion of Issues

**Issue 1:** Should the Commission approve the Environmental Protection Systems of Pine Island, Inc.'s Revised Settlement Proposal?

**Recommendation:** Yes. The Revised Proposal filed by Environmental Protection Systems of Pine Island, Inc. should be approved. The utility should be required to refund the percentage reductions set forth in the Settlement Proposal. The refunds should be made within 90 days of the effective date of the Consummating Order finalizing the Order for refunds and include interest as required by Rule 25-30.360(4), Florida Administrative Code (F.A.C.) The utility should be required to submit the proper refund reports pursuant to Rule 25-30.260(7), F.A.C. The refund should be made to customers of record as of the date of the Consummating Order pursuant to Rule 25-30.360(3), F.A.C. The utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C. In no instance should the maintenance and administrative costs associated with a refund be borne by the customers. These costs are the responsibility of, and should be borne by the utility. (Revell, Brubaker)

**Staff Analysis:** As discussed in the case background, the utility was required to complete a pro forma interconnection project within nine months of the issuance date of the Consummating Order. In the Amendatory SARC Order, the Commission specified that the docket remain open pending staff's verification that the utility completed the pro forma interconnection. The utility provided staff with cost verification of the completed items.

According to the utility, numerous problems and delays prevented the interconnection from occurring in the time period set out in the Amendatory SARC Order. The tariffs implementing the rate increase to recover the interconnection costs were effective November 15, 2003; however, the interconnection did not occur until September 20, 2005. Therefore, from November 15, 2003, through September 20, 2005, customers paid for costs the utility had not incurred. In addition, actual costs for the project were less than the costs projected in the rate case. Thus, the Commission found that refunds to customers and a rate reduction was necessary. The following is a comparison of Commission-approved pro forma plant and actual cost:

PRO FORMA PROJECTS	Per Order 12/31/2003	Actual 12/31/2006	Difference
LIFT STATION NO. 2	\$38,225	\$15,152	(\$23,073)
MASTER LIFT STATION	86,625	105,471	18,846
CONNECTION FEES less non-U&U	657,218	569,920	(87,298)
VIDEO OF LINES	23,771	28,570	4,799
LEGAL & ENG FEES	28,865	38,368	9,503
OFFICE EQUIPMENT	4,774	8,964	4,190
COST OF REMOVAL included in Early Loss calc	30,237	30,700	463
TOTAL	\$869,715	\$797,145	(\$72,570)

### **Previous Commission Action**

Pursuant to the Refund Order, the Commission identified three periods of time over which refunds should be calculated: (1) the period November 15, 2003, through August 4, 2004; (2) the period August 5, 2004, through December 31, 2004; and (3) the period January 1, 2005, through the date rates are changed. These timeframes are discussed in more detail below.

November 15, 2003 – August 4, 2004: During this period, little if any construction had taken place on the interconnection. Thus, from November 15, 2003 through August 4, 2004, the utility collected revenues to which it was not entitled. In the SARC, the Commission approved the revenue requirement impact of the interconnection in the utility's rates. However, in the Refund Order, adjustments to the utility's revenue requirement were necessary because the SARC contemplated the interconnection would be complete by August 10, 2004. Because the interconnection was not completed by that time, the utility continued to operate its treatment facilities. The Commission reversed certain operation and maintenance (O&M) adjustments that were made in the SARC to the projected 2003 test year. This included a new expense for purchased wastewater treatment, and excluded certain O&M expenses that would no longer be incurred by the utility after the interconnection was completed. The resulting revenue requirement impact is \$107,112. In the SARC, the Commission-approved wastewater rates were designed to recover \$230,802. Therefore, the Commission calculated a refund to customers of 46.41 percent ( $\$107,112/\$230,802$ ) of revenues collected between November 15, 2003, and August 4, 2004.

To evaluate the effect the refunds would have on the utility's 2004 and 2005 earnings, staff analyzed EPS's annual reports. Adjustments to amounts in the annual reports were made consistent with the utility's rate case. Based on the Commission's analysis in the Refund Order, the utility overearned by 35.64 percent in 2004. Therefore, the Commission ordered the utility refund to customers 35.64 percent of revenues collected between November 15, 2003, and August 4, 2004.

August 5, 2004 – December 31, 2004: It appeared from invoices that from August 5, 2004, the utility began spending substantial amounts for the interconnection project. However, the cost of the project was less than what was approved by the Commission. Further, during this time, the interconnection still was not completed, so the same O&M adjustments discussed above were made to this time period. In the Refund Order, the Commission calculated the difference between the revenue requirement impacts projected in the SARC and the actual costs. The Commission also made the reversing adjustments described above. The resulting revenue requirement impact was \$20,714. In the SARC, the Commission-approved wastewater rates were designed to recover \$230,802. Therefore, the Commission ordered the utility refund to customers 8.97 percent ( $\$20,714/\$230,802$ ) of revenues collected between August 5, 2004 – December 31, 2004.

Thus, by approving December 31, 2004, as the ending date for the 8.97 percent refund, the Commission allowed the full nine months for completion of the project. The interconnection occurred on September 20, 2005, and December 31, 2004, would be nine months prior to the interconnection date.

January 1, 2005 – Date Rates are Changed: As stated above, the utility interconnected with PIRTS on September 20, 2005. Because the actual cost of the interconnection was less than the amount projected in the rate case, the Commission found that the utility was collecting more in rates than is fair and just. Since the interconnection had occurred, no reversal of the O&M adjustments was made. As a result, the Commission calculated the difference in the revenue requirement impact of the interconnection approved in the rate case of \$97,401 and the actual costs incurred by the utility of \$86,398. The resulting \$11,003 was divided by the total revenue requirement from the rate case of \$230,802 to produce 4.77 percent. Therefore, the Commission ordered that the utility refund to customers 4.77 percent of revenues collected between January 1, 2005 and the date rates are changed.

### **Settlement Offer**

On June 1, 2007, the utility filed a timely protest of the Refund Order. On June 19, 2007, the utility filed its Initial Proposal. In its Initial Proposal, the utility indicated that the refund amounts were overstated because the wastewater rate base was understated for the test year ending December 31, 2006. Further, the utility stated that the amounts included as salary expense were in error, and the refund based on a period by period case was also erroneous.

After further discussions with staff, the utility filed its Revised Proposal on July 20, 2007. The Revised Proposal addressed only the reduction to salary expense. The adjustments ordered by the Commission and the utility's Revised Proposal is shown below:

<u>Period</u>	<u>% Reduction per PAA Order</u>	<u>% Reduction per Settlement</u>
11/15/03-8/04/04	35.64	20.79
8/05/04-12/31/04	8.97	1.03
1/01/05-8/01/07	4.77	0.00

In the SARC Order, the Commission calculated salary expense for the utility's two employees based on duties and responsibilities and the amount of total work hours related to EPS. Based on these calculations, Salaries and Wages-Officers was reduced.

The utility states that the salaries expense reported in its Annual Report includes the salary amounts approved in the SARC Order, as well as, the amount of benefits expense and payroll taxes. As a result, the salary account was overstated, as these expenses should have been included in Employee Pensions and Benefits, and Taxes Other than Income, respectively. In the Refund Order, the Commission's reduction of salary expense had the effect of removing the utility's total expense for pensions and benefits and taxes other than income, as well as the salary of a new employee.

The utility believes the reductions were excessive since the amount reported as salary expense actually includes an amount of benefit expense previously approved by the Commission in the SARC Order. Further, the utility indicated the Commission failed to address the appropriate amount of payroll taxes in its SARC Order. Staff reviewed the actual amount of salaries, benefits, and payroll taxes incurred by the utility, as well as the utility's calculations and

agrees with the Revised Proposal. If staff had initially been made aware of the utility's errors in booking the pensions and benefits, and taxes other than income expenses, staff would not have recommended an adjustment to salaries which were approved in the Refund Order. As a result of this recalculation, the utility's revenue requirement should be increased.

A number of customers have expressed concern over the proposed settlement and do not believe the Commission should reverse its decision or the amount of the refund. Staff understands these concerns; however, if the salary adjustments had not been made in the Refund Order, the utility would not have filed its protest. Additionally, staff believes that the extra rate case expense that would be incurred if this protest proceeded to hearing could lower or even eliminate the refunds.

Based on the above, staff believes the settlement is fair, just, and reasonable, and is in the public interest. Staff believes that the acceptance of the settlement will further the goal of administrative efficiency and is in the public interest. Therefore, staff recommends that the Commission approve the attached Revised Proposal and that the utility be required to refund the percentage reductions indicated in the table above.

The refunds should be made within 90 days of the effective date of the Consummating Order finalizing the Order for refunds and include interest as required by Rule 25-30.360(4), F.A.C. The utility should be required to submit the proper refund reports pursuant to Rule 25-30.260(7), F.A.C. The refund should be made to customers of record as of the date of the Consummating Order pursuant to Rule 25-30.360(3), F.A.C. The utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C. In no instance should the maintenance and administrative costs associated with a refund be borne by the customers. These costs are the responsibility of, and should be borne by the utility.

Docket No. 030106-SU

Date: August 29, 2007

**Issue 2:** Should this docket be closed?

**Recommendation:** No. If the Commission approves staff's recommendation in Issue 1, this docket should remain open for staff's verification that the appropriate refund has been completed. Once these actions are complete, this docket should be closed administratively. (Revell, Brubaker)

**Staff Analysis:** If the Commission approves staff's recommendation in Issue 1, this docket should remain open for staff's verification that the appropriate refund has been completed. Once these actions are complete, this docket should be closed administratively.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for staff-assisted  
rate case in Lee County, Florida by  
ENVIRONMENTAL PROTECTION  
SYSTEMS OF PINE ISLAND, INC.

DOCKET NO. 030106-SU

ENVIRONMENTAL PROTECTION SYSTEMS OF PINE ISLAND, INC.'S  
REVISED SETTLEMENT PROPOSAL

Applicant, ENVIRONMENTAL PROTECTION SYSTEMS OF PINE ISLAND, INC. ("EPS" or "Utility"), by and through its undersigned attorneys, files this Revised Settlement Proposal with regard to its Petition on Proposed Agency Action protesting Order No.: PSC-07-0426-PAA-SU.

1. In all years salary expense per the Utility was reduced by payroll taxes and benefits. The Utility added the benefits and salary allowed per the staff assisted rate case and added the payroll taxes to that amount. In a Subchapter "S" Corp, benefits to a 2% or more stockholder are considered salary and must go on W-2. The amount of payroll taxes of \$5,220 was left out of the Staff Assisted Rate Case so EPS added it as salary expense. This should have been posted as taxes other than income.

2. The following is a summary of the effect of this adjustment which is a reduction in the refund due EPS customers:

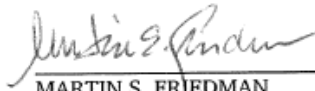
<u>Period</u>	<u>% Reduction per PAA Order</u>	<u>% Reduction per Settlement Offer</u>
11/15/03 - 8/04/04	35.64	20.79
8/05/04 - 12/31/04	8.97	1.03
1/01/05 - 8/01/07	4.77	-0-



In addition, EPS requests no adjustment to its current rates since it is not over earning on a prospective basis.

Respectfully submitted this 19<sup>th</sup> day of  
July, 2007, by:

ROSE, SUNDBSTROM & BENTLEY, LLP  
Sanlando Center  
2180 W. State Road 434, Suite 2118  
Longwood, FL 32799  
Telephone: (407) 830-6331  
Facsimile: (407) 830-8522



---

MARTIN S. FRIEDMAN  
Florida Bar Number: 0199060  
For the Firm