

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 9, 2009

TO: Office of Commission Clerk (Cole)

FROM: Division of Economic Regulation (Buys, Bulecza-Banks, Daniel, Fletcher, Maurey, Walden)
Office of the General Counsel (Young)

RE: Docket No. 080248-SU – Application for increase in wastewater rates in Pinellas County by Tierra Verde Utilities, Inc.

AGENDA: 04/21/09 – Regular Agenda – Proposed Agency Action Except Issues 15 and 16 - Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Argenziano

CRITICAL DATES: 04/24/09 (5-Month Effective Date (PAA Rate Case))

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\080248.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 4 separate rate case dockets pending before the Public Service Commission (Commission). These dockets are as follows:

| <u>Docket No.</u> | <u>Utility Subsidiary</u> |
|-------------------|-------------------------------|
| 080247-SU | Utilities Inc. of Eagle Ridge |
| 080248-SU | Tierra Verde Utilities, Inc. |
| 080249-WS | Labrador Utilities, Inc. |
| 080250-SU | Mid-County Services, Inc. |

This recommendation addresses Docket No. 080248-SU, Tierra Verde Utilities, Inc. (Tierra Verde or Utility). Tierra Verde is a Class B utility providing wastewater service to approximately 1,033 customers in Pinellas County. The Utility is a wholly-owned subsidiary of UI. Tierra Verde's service area is located entirely on a barrier island at the mouth of Tampa Bay. All the Utility's sewage treatment service is purchased from the City of St. Petersburg. Wastewater rates were last established for Tierra Verde in its 2006 rate proceeding.¹

On August 27, 2008, Tierra Verde filed its application for a rate increase. The Utility requested that the application be processed using the Proposed Agency Action (PAA) procedure. Tierra Verde had deficiencies in the Minimum Filing Requirements (MFRs). The deficiencies were corrected and November 26, 2008, was established as the official filing date. The test year established for interim and final rates is the historical twelve-month period ended December 31, 2007.

Tierra Verde requested interim rates designed to generate annual wastewater revenues of \$923,677, an increase of \$142,978 or 18.31 percent. By Order No. PSC-08-0762-PCO-SU, issued November 17, 2008, the Commission approved interim rates designed to generate annual wastewater revenues of \$903,210, an increase of \$151,404 or 20.20%.² The Utility requested final rates designed to generate wastewater revenues of \$1,132,684, an increase of \$351,954 or 45.08 percent.

This recommendation addresses the revenue requirement and rates to be approved on a prospective basis. The Commission has jurisdiction pursuant to Section 367.081, Florida Statutes (F.S.).

¹ See Order No. PSC-07-0082-PAA-SU, issued January 29, 2007, in Docket No. 060255-SU, In Re: Application for increase in wastewater rates in Pinellas County by Tierra Verde Utilities, Inc. Consummating Order No. PSC-07-0164-CO-SU, issued February 23, 2007, made Order No. PSC-07-0082-PAA-SU final and effective.

² See Order No. PSC-08-0762-PCO-SU, issued November 17, 2008, in Docket No. 080248-SU, In re: Application for increase in wastewater rates in Pinellas County by Tierra Verde Utilities, Inc.

Discussion of Issues

QUALITY OF SERVICE

Issue 1: Is the quality of service provided by Tierra Verde Utilities, Inc. satisfactory?

Recommendation: Yes. The overall quality of service provided by the Utility is satisfactory. (Walden)

Staff Analysis: Pursuant to Rule 25-30.433,(1), Florida Administrative Code (F.A.C.), the Commission shall determine the overall quality of service provided by the Utility. Items considered are the quality of the product, the operating conditions of the plant, and customer satisfaction. Tierra Verde is a wastewater collection system only, with purchased wastewater treatment provided by the City of St. Petersburg (City). Therefore, Quality of the Product and Operating Conditions of the Plant would not be at issue in this case.

Customer Satisfaction

The filing contained sixteen customer complaints during the test year. Most complaints involved a wastewater back up or a lift station problem. The Utility dispatched a service representative in each case and resolved the problem. If the issue was not the Utility's responsibility, the customer was so informed. One customer e-mailed the Office of the Governor, and that e-mail was forwarded to the Commission for review and response. The substance of the e-mail was to state opposition to the rate increase, noting that these are difficult times for the Utility's customers.

The Commission scheduled an informal customer meeting in St. Petersburg Beach on February 26, 2009, to allow customers to provide input to staff concerning the Utility's application for a rate increase. No customers attended the meeting.

After a review of the complaints in the filing, the correspondence received by the Commission, and attendance at the customer meeting, it appears that the service provided to customers is adequate. Staff therefore recommends that the Commission find that customer satisfaction is satisfactory.

RATE BASE

Issue 2: Should the audit adjustments to rate base and operating expense to which the Utility and staff agree, be made?

Recommendation: Yes. Based on the audit adjustments agreed to by the Utility and staff, the following adjustments should be made to rate base and operating expenses. (Buys)

| Audit Finding | Wastewater |
|---|-------------------|
| No. 1 - Increase CIAC | \$25,425 |
| No. 1 - Increase Amortization Expense (CIAC) | \$1,228 |
| No. 1 - Increase Accumulated Amortization of CIAC | \$614 |
| No. 2 - Decrease Accumulated Depreciation | \$75,829 |
| No. 2 - Decrease Accumulated Amortization of CIAC | \$107,686 |
| No. 2 - Decrease Amortization Expense (CIAC) | \$67,203 |
| No. 2 - Decrease CIAC | \$1 |
| No. 3 - Decrease Contractual Services – Legal | \$114 |
| No. 3 - Decrease Rate Case Expense Adjustment | \$2,829 |
| No. 4 - Decrease Accumulated Depreciation | \$1,517 |
| No. 4 - Increase Accumulated Amortization of CIAC | \$1,209 |
| No. 4 - Decrease Depreciation Expense | \$8,074 |
| No. 4 - Increase Amortization Expense (CIAC) | \$1,209 |
| AT No. 5 - Increase Transportation Expense | \$3,138 |

Staff Analysis: Tierra Verde either agreed to the audit findings and adjustments in staff's audit report or proposed alternative adjustments to which staff agrees. Those adjustments are listed below.

| Audit Finding | Wastewater |
|---|-------------------|
| No. 1 - Increase CIAC | \$25,425 |
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| No. 4 - Decrease Depreciation Expense | \$8,074 |
| No. 4 - Increase Amortization Expense (CIAC) | \$1,209 |

In addition, staff auditors performed an affiliate transactions (AT) audit of UI, the parent company of Tierra Verde and its sister companies. Based on AT Audit Finding No. 5, transportation expense should be increased by \$3,138. The aforementioned adjustments related to rate base and operating expenses are reflected on Schedules 1-B and 3-B.

Issue 3: What are the used and useful percentages of the Utility's wastewater collection system?

Recommendation: The collection system is 100 percent used and useful. (Walden)

Staff Analysis: In the last three rate cases for Tierra Verde, the Commission found the system to be 100 percent used and useful. Customer billing is performed by the City, and the used and useful determination in the last case was evaluated from the number of lots and meters rather than equivalent residential connections (ERCs). In the prior case, Order No. PSC-07-0082-PAA-SU stated that the number of meters was 1,003, and projected growth of 12 connections per year.

The current docket shows 1,095 total lots with 986 active, occupied connections. A detailed lot identification survey was made by the Utility. The number of total annual bills was provided, which indicates growth of 1.28 percent. It appears that the number of customers in the test year is essentially the same as in the prior docket. Based upon staff's review of the filing and prior Commission orders, it is recommended that the Commission find the wastewater collection system 100 percent used and useful because the collection system in place is needed to serve the current customers.

Issue 4: What is the appropriate working capital allowance?

Recommendation: The appropriate working capital allowance is \$91,724. (Buys)

Staff Analysis: Rule 25-30.433(2), F.A.C., requires that Class B utilities use the formula method, or one-eighth of operation and maintenance (O&M) expenses, to calculate the working capital allowance. Tierra Verde properly filed its allowance for working capital using the formula method. Staff has recommended adjustments to the Utility's O&M expenses. As a result, staff recommends that working capital of \$91,724 be approved. This reflects a decrease of \$14,892 to Tierra Verde's requested working capital allowance of \$106,616.

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Issue 5: What is the appropriate rate base for the December 31, 2007, test year?

Recommendation: Consistent with other recommended adjustments, the appropriate simple average rate base for the test year ending December 31, 2007, is \$1,502,918. (Buys)

Staff Analysis: Consistent with other recommended adjustments, the appropriate simple average rate base for the test year ending December 31, 2007, is \$1,502,918. Staff's rate base is shown on Schedule 1-A. The adjustments are shown on Schedule 1-B.

COST OF CAPITAL

Issue 6: What is the appropriate return on common equity?

Recommendation: The appropriate return on common equity is 12.34 percent based on the Commission's leverage formula currently in effect. Staff recommends an allowed range of plus or minus 100 basis points be recognized for ratemaking purposes. (Buys)

Staff Analysis: The return on equity (ROE) included in the Utility's filing is 11.7 percent. This return is based on the application of the Commission's leverage formula in effect at the time of the Utility's filing and an equity ratio of 42.59 percent.³

Based on the current leverage formula approved in Order No. PSC-08-0846-FOF-WS and an equity ratio of 42.59 percent, the appropriate ROE is 12.34 percent.⁴ Staff recommends an allowed range of plus or minus 100 basis points be recognized for ratemaking purposes.

³ See Order No. PSC-07-0472-PAA-WS, issued June 1, 2007, in Docket No. 070006-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.

⁴ See Order No. PSC-08-0846-FOF-WS, issued December 31, 2008, in Docket No. 080006-WS, In re: Water and Wastewater industry annual reestablishment of authorized range of return on common equity for water and wastewater utilities pursuant to Section 367.081(4)(f), F.S., Florida Statutes.

Issue 7: 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, 2007?

Recommendation: The appropriate weighted average cost of capital for the test year ended December 31, 2007, is 8.29 percent. (Buys)

Staff Analysis: Based upon the proper components, amounts, and cost rates associated with the capital structure for the test year ended December 31, 2007, staff recommends a weighted average cost of capital of 8.29 percent. The weighted average cost of capital included in the Utility's filing is 8.07 percent. Staff revised the respective cost rate for common equity. The appropriate cost rate for common equity of 12.34 percent is discussed in Issue 6. Schedule No. 2 details staff's recommendation.

NET OPERATING INCOME

Issue 8: Should an adjustment be made to Purchased Wastewater Treatment due to excessive infiltration and inflow?

Recommendation: Yes. Purchased Wastewater Treatment Expense should be decreased by \$84,119 due to excessive infiltration and inflow. (Walden)

Staff Analysis: The Utility had approximately 14.87 percent excess infiltration and inflow (I & I) during the test year. It is an industry standard and Commission practice to allow 500 gallons per day per inch diameter pipe per mile for infiltration plus 10 percent of water sold as inflow.⁵ Based upon data supplied by the Utility, when comparing gallons billed to wastewater customers to the amount of wastewater treated, there is 57,554,200 gallons of estimated I & I. The total allowable amount for I & I was calculated to be 27,632,117 gallons per year; therefore, excessive I & I was calculated to be 29,922,083 gallons per year, or 14.87 percent of total flows.

The City's billing for purchased wastewater was \$532,690 for the test year. Removing 14.87 percent of this cost is a disallowance of \$79,211. Further, the Utility included a proforma expense of \$33,007 for purchased wastewater due to an increase in the rate per million gallons from the City. The same removal of 14.87 percent due to excess I & I results in a reduction of \$4,908 from this proforma expense. Therefore, staff recommends that Purchased Wastewater Treatment Expense be reduced by a total of \$84,119.

⁵ See Order No. PSC-05-0624-PAA-WS, issued June 5, 2005, in Docket No. 040450-WS, In re: Application for rate increase in Martin County by Indiantown Company, Inc.

Issue 9: Should an adjustment be made to operation and maintenance expense?

Recommendation: Yes. Operation and maintenance expense should be decreased by \$1,570.
(Buys)

Staff Analysis: On MFR Schedule B-11, Line 1, Tierra Verde reflected \$76,452 for a major maintenance project titled "TV Sewer Mains." The amount is amortized over a five-year period resulting in \$15,290 included in the test year operation and maintenance (O&M) expenses under Materials and Supplies. In response to staff's data request regarding the project, the Utility indicated that it could not locate \$7,850 of supporting documentation, so the total project cost now amounts to \$68,602. The correct amount of the five-year amortization included in test year expenses should be \$13,720 ($\$68,602 \div 5$). Therefore, staff recommends that O&M expenses be decreased by \$1,570 ($\$15,290$ less $\$13,720$). The aforementioned adjustment is reflected on Schedule 3-B.

Issue 10: Should an adjustment to Contractual Services-Other be made?

Recommendation: Yes. Contractual Services-Other should be decreased by \$14,536. (Buys)

Staff Analysis: On MFR Schedule B-8, the Utility reflected an adjusted test year amount of \$17,046 for Contractual Services-Other, which represents an increase of \$14,536 or 579.11 percent over the prior test year. Tierra Verde noted that the reason for this increase was due to “[t]emporary employment has increased the cost of other contractual services.” In addition, on MFR Schedule B-8, Lines 1 through 3, the Utility reflects an increase of \$30,001 or 60.11 percent for Salaries & Wages-Employees and \$8,983 or 77.50 percent for Employee Pensions & Benefits. Tierra Verde noted that the reason for these increases are due to "annualization, cost of living increases, and the need for additional employees.”

In its first data request, staff requested that the Utility provide support for its increase in temporary employment by indentifying each temporary position employed during the test year and providing a detail of the duties performed and the associated cost. In its response, Tierra Verde failed to provide a detail of the duties performed and the associated cost. The Utility stated that \$10,573 of the difference between the prior test year and the current test year results from an allocation adjustment to allocate costs on an ERC basis and not a customer equivalent (CE) basis. The remaining \$6,473 is what was actually booked to the general ledger during the current test year. Tierra Verde stated that only \$2,046 (\$1,242 booked plus the debit adjustment of \$804 from the allocation adjustment) of the \$17,046 is related to temporary employment.

By Order No. PSC-03-1440-FOF-WS, issued December 22, 2003, the Commission found that Water Service Corp.’s (WSC’s) method of allocating costs based on CEs was unsupported and unreasonable. The Commission ordered UI to use ERCs, measured at the end of the test year, as a basis for allocating costs in Florida.⁶ The support documentation listing the \$1,242 in temporary employment was presented as an allocated amount using CEs, and consequently staff was unable to determine the actual amount of expenses that were related to temporary employment for Tierra Verde. Although the Utility reported that \$10,573 of the increase is due to an allocation adjustment, Tierra Verde did not provide the requested documentation to support the \$6,473 that was actually booked to the general ledger for Contractual Services-Other during the current test year which gave rise to the allocation adjustment.

Based on the aforementioned, staff believes that the Utility’s increase in Contractual Services-Other for the test year, in addition to an increase in salaries and wages, is unsupported and excessive. Therefore, staff recommends that Contractual Services-Other be decreased by \$14,536. The aforementioned adjustment is reflected on Schedule 3-B.

⁶ See 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.

Issue 11: What is the appropriate amount of rate case expense?

Recommendation: The appropriate rate case expense is \$91,558. This expense should be recovered over four years for an annual expense of \$22,890. Thus, rate case expense should be reduced by \$19,107. (Buys)

Staff Analysis: In its MFRs, Tierra Verde recorded \$26,351 for prior rate case amortization for the test year ended December 31, 2007. The authorized amount of annual rate case amortization from the prior rate case is \$23,522. To correct the overstatement, an adjustment was made in Issue 2 to decrease the rate case expense adjustment for the previous filing by \$2,829.

In its MFRs, Tierra Verde requested total rate case expense of \$258,303. The Utility's total rate case expense included \$90,317 for prior unamortized rate case expense and \$167,986 for current rate case expense. It is Commission practice to remove the unamortized balance of prior rate cases from the rate case expense for the current case.⁷ Therefore, staff recommends that total rate case expense should be reduced by \$90,317.

Staff requested an update of the actual rate case expense incurred, with supporting documentation, as well as the estimated amount necessary to complete the case. On March 6, 2009, the Utility submitted a revised MFR Schedule B-10 reflecting actual and estimated rate case expense through completion of the PAA process of \$100,171, or when amortized over four years, \$25,043 annual rate case expense.

| | MFR | | Additional | |
|-------------------------|------------------|-----------------|------------------|------------------|
| | <u>Estimated</u> | <u>Actual</u> | <u>Estimated</u> | <u>Total</u> |
| Legal and Filing Fees | \$ 45,200 | \$14,487 | \$15,470 | \$29,957 |
| Consultant Fees – MS&A | 38,100 | 41,050 | 370 | 41,420 |
| Consultant Fees – M&R | 3,050 | 717 | 1,885 | 2,602 |
| Consultant Fees – CPH | 0 | 1,000 | 0 | 1,000 |
| WSC Fees – In House | 60,700 | 16,854 | 7,074 | 23,928 |
| Filing Fee | 3,500 | 0 | 0 | 0 |
| Travel – WSC | 3,200 | 54 | 0 | 54 |
| Miscellaneous | 12,000 | 246 | 0 | 246 |
| Notices | <u>2,236</u> | <u>482</u> | <u>482</u> | <u>964</u> |
| Total Rate Case Expense | <u>\$167,986</u> | <u>\$74,890</u> | <u>\$25,281</u> | <u>\$100,171</u> |

Pursuant to Section 367.081(7), F.S., the Commission shall determine the reasonableness of rate case expenses and shall disallow all rate case expenses determined to be unreasonable. In those cases where rate case expense has not been supported by detailed documentation,

⁷ See Order No. PSC-97-1225-FOF-WU, p. 17, issued October 10, 1997, in Docket No. 970164-WU, In re: Application for increase in rates in Martin County by Hobe Sound Water Company.

Commission practice has been to disallow some portion or remove all unsupported amounts.⁸ It is the Utility's burden to justify its requested costs. Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982). 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 Tierra Verde's 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 Rose, Sundstrom & Bently, LLP, a combined amount of \$825 was billed for correcting the MFR deficiencies and revising the Utility's filing. The Commission has previously disallowed rate case expense associated with correcting MFR deficiencies because of duplicate filing costs.⁹ Accordingly, staff recommends that \$825 be removed from legal fees.

The second adjustment relates to the Utility's estimated legal fees for Rose, Sundstrom & Bently, LLP to complete the rate case. As of March 12, 2009, Rose, Sundstrom & Bently, LLP estimated 47.6 hours or \$15,470 (47.6 hours x \$325) to complete the rate case. On March 31, 2009, Mr. Martin Freidman of Rose Sundstrom & Bently, LLP informed staff via email that his hourly rate as of January 1, 2009, is \$320 per hour. Accordingly, the estimated cost to complete the case should be reduced by \$5 per hour or \$238 (47.6 hours x \$5). Of the 47.6 hours estimated to complete the case, fifteen hours is to prepare for and attend Agenda Conference and discuss the agenda with client and staff. Commission practice has been to allow fourteen hours to travel and attend Agenda Conference. In this case, Tierra Verde's counsel is representing another UI company, Mid-County Services, Inc., at the same Agenda Conference. Therefore, staff believes the cost to attend Agenda Conference should be shared by both utilities and the estimated fifteen hours should be reduced to seven for each Utility. Accordingly, legal fees should be reduced by \$2,560 (8 x \$320). Staff believes that the remaining 39.6 hours is a reasonable amount of time to respond to data requests, conference with the client and consultants, review staff's recommendation, travel to the customer meeting, and attend to miscellaneous post-PAA matters. In total, staff recommends that the estimated legal fees should be reduced by an additional \$2,798 (\$238 + \$2,560).

The third adjustment relates to the Utility's estimated consultant fees for Mr. Frank Seidman with Management & Regulatory Consultants, Inc., to complete the rate case. As of March 12, 2009, Mr. Seidman estimated thirteen hours or \$1,885 (13 hours X \$145) to complete the rate case. Of the thirteen hours estimated, nine hours is to "assist with responses to data requests," and the remaining four hours is to prepare for and attend the Agenda Conference. At

⁸ See Order Nos. 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.; 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 PSC-96-0860-FOF-SU, issued July 2, 1996, in Docket No. 950967-SU, In re: Application for staff-assisted rate case in Highlands County by Fairmount Utilities, the 2nd, Inc. Staff notes that, in all of these cases, the Commission removed the entire unsupported amounts.

⁹ See Order Nos. 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.; and 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.

this time in the rate case process, there are no outstanding data requests that require a response. Staff believes that the nine hours estimated to assist with responses to data requests is unreasonable. Staff believes that four hours is a reasonable amount of time to prepare for and attend the Agenda Conference 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.¹⁰ Therefore, staff recommends that the consultant fees in the rate case expense be decreased by \$1,305 (9 hours x \$145).

The fourth adjustment relates to the actual charges to date related to WSC employees. Revised MFR Schedule B-10 reflecting the updated rate case expense includes hours and charges for Josephine Eblacas Ratliff and Michael A. Wilson of \$2,171 and \$455 respectively. The Utility also estimated additional charges to complete the PAA for Michael A. Wilson of \$759. However, the capitalized time report and work hours log provided as support for the charges incurred to date did not include an entry for either person. Thus, Tierra Verde's requested rate case expense for WSC employees of \$23,928 should be decreased by \$3,385 (\$2,171 + \$455 + \$759).

The fifth adjustment addresses WSC travel expenses. In its updated rate case expense, Tierra Verde included \$54 for travel. Based on several previous UI rates cases, it is staff's understanding that for PAA rate cases UI does not send a representative from their Illinois office to attend the Agenda Conference. Therefore the entire amount of travel expense should be removed. Accordingly, staff recommends that rate case expense be decreased by \$54.

The sixth adjustment relates to WSC expenses for FedEx Corporation (FedEx), copies, and other miscellaneous costs. In its updated rate case expense, the Utility reflects actual total costs of \$246. The Utility did not provide a breakdown of these costs. UI has requested and received authorization from the Commission, to keep its records outside the state in Illinois, 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 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.¹¹ 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 requests, 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

¹⁰ See Order Nos. 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.; and 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.

¹¹ See Order Nos. 25821, issued February 27, 1991, in Docket No. 910020-WS, In re: Petition for rate increase in Pasco County by UTILITIES, INC. OF FLORIDA; and 20066, issued September 26, 1988, in Docket No. 870981-WS, In re: Application of MILES GRANT WATER AND SEWER COMPANY for an increase in Water and Sewer Rates in Martin County

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 miscellaneous rate case expense be decreased by \$246.

In summary, staff recommends that Tierra Verde's revised rate case expense of \$100,171 be decreased by \$8,613 for MFR deficiencies, and for unreasonable and unsupported rate case expense. The appropriate total rate case expense is \$91,558. A breakdown of rate case expense is as follows:

| <u>Description</u> | <u>MFR Estimated</u> | <u>Utility Revised Actual & Estimated</u> | <u>Staff Adjustments</u> | <u>Total</u> |
|---|--------------------------|---|------------------------------|-----------------|
| Legal Fees | \$45,200 | \$29,957 | (3,623) | \$26,334 |
| Consultant Fees-MS&A | 38,100 | 41,420 | 0 | 41,420 |
| Consultant Fees-M&R | 3,050 | 2,602 | (1,305) | 1,297 |
| Consultant Fees – CPH | 0 | 1,000 | 0 | 1,000 |
| WSC In-House Fees | 60,700 | 23,928 | (3,385) | 20,543 |
| Filing Fee (\$2,000 included in legal fees) | 3,500 | 0 | 0 | 0 |
| WSC Travel | 3,200 | 54 | (54) | 0 |
| Miscellaneous | 12,000 | 246 | (246) | 0 |
| Customer Notices & Postage | <u>2,236</u> | <u>964</u> | <u>0</u> | <u>964</u> |
| Total Rate Case Expense | <u>\$167,986</u> | <u>\$100,171</u> | <u>(8,613)</u> | <u>\$91,558</u> |
| Annual Amortization | <u>\$41,997</u> | <u>\$25,043</u> | <u>(2,153)</u> | <u>\$22,890</u> |

In its MFRs, Tierra Verde requested current rate case expense of \$167,986, which amortized over four years would be \$41,997. The recommended current rate case expense should be amortized over four years, pursuant to Section 367.016, F.S. Based on the data provided by the Utility and the staff-recommended adjustments discussed above, staff recommends annual rate case expense of \$22,890. Thus, staff recommends that rate case expense be reduced by \$19,107 (\$41,997 less \$22,890).

Docket No. 080248-SU

Date: April 9, 2009

Issue 12: What is the test year wastewater operating income or loss before any revenue increase?

Recommendation: The test year operating income is a net loss of \$46,891 for wastewater before any revenue increase. (Buys)

Staff Analysis: This issue is subject to resolution of other issues related to revenues and operating expenses and rate base, and is primarily a "fall-out" number. Based on the adjustments discussed in previous issues, staff recommends that the test year operating income before any provision for increased revenues should be a net loss of \$46,891 for wastewater. The schedule for wastewater operating income is attached as Schedule No. 3-A, and the adjustments are shown on Schedule No. 3-B.

REVENUE REQUIREMENT

Issue 13: What is the appropriate revenue requirement?

Recommendation: The following is the appropriate revenue requirement:

| | <u>Test Year</u> | | <u>Revenue</u> | |
|----------------------|------------------|--------------------|--------------------|-------------------|
| | <u>Revenues</u> | <u>\$ Increase</u> | <u>Requirement</u> | <u>% Increase</u> |
| Wastewater (Buys) | \$780,729 | \$287,930 | \$1,068,659 | 36.88% |

Staff Analysis: The issue is a summary computation that is subject to the resolution of other issues related to rate base, and cost of capital, and is primarily a “fall-out” number. The computation of the revenue requirement is shown on Schedule No. 3-A and is \$1,068,659 which represents an increase of \$287,930 or 36.88 percent.

RATES AND CHARGES

Issue 14: What are the appropriate wastewater rates for Tierra Verde?

Recommendation: The appropriate monthly rates are shown on Schedule No. 4. Staff's recommended rates are designed to produce revenues of \$1,068,659 excluding miscellaneous service charge revenues. The Utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(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 10 days after the date of the notice. (Buys)

Staff Analysis: Staff's recommended revenue requirement is \$1,068,659. After excluding miscellaneous service charges of \$450, the revenue to be recovered through rates is \$1,068,209. Tierra Verde's current wastewater rate structure is a flat rate for residential customers and a base facility charge and gallonage charge for general service customers.

The Utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. 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 10 days after the date of the notice.

A comparison of the Utility's original and requested rates, the Commission-approved interim rates, and staff's recommended PAA rates are shown on Schedule No. 4.

Issue 15: In determining whether any portion of the interim increase granted should be refunded, how should the refund be calculated, and what is the amount of the refund, if any?

Recommendation: The proper refund amount should be calculated by using the same data used to establish final rates, excluding rate case expense and other items not in effect during the interim period. This revised revenue requirement for the interim collection period should be compared to the amount of interim revenue requirement granted. Based on this calculation, no wastewater refunds are required. (Buys)

Staff Analysis: By Order No. PSC-08-0762-PCO-SU, issued November 17, 2008, the Commission authorized the collection of interim wastewater rates, subject to refund, pursuant to Section 367.082, F.S. The approved interim revenue requirement is \$903,210 for wastewater, which represents an increase of \$151,806 or 20.20 percent.

According to Section 367.082, F.S., any refund should be calculated to reduce the rate of return of the Utility during the pendency of the proceeding to the same level within the range of the newly authorized rate of return. Adjustments made in the rate case test period that do not relate to the period interim rates are in effect should be removed. Rate case expense is an example of an adjustment which is recovered only after final rates are established.

In this proceeding, the test period for establishment of interim and final rates is the simple average ending December 31, 2007. Tierra Verde's approved interim rates did not include any provisions for pro forma or projected operating expenses or plant. The interim increase was designed to allow recovery of actual interest costs and the floor of the last authorized range for equity earnings.

Using the principles discussed above, staff calculated a revised interim revenue requirement of \$1,044,240 utilizing the same data used to establish final rates. Rate case expense was excluded because this item is prospective in nature and did not occur during the interim collection period.

Because the \$903,210 interim wastewater revenue requirement granted in Order No. PSC-08-0762-PCO-SU for the test year is less than the revised revenue requirement for the interim collection period of \$1,044,240, staff recommends that no refund is required for wastewater revenues collected under interim rates.

Issue 16: 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?

Recommendation: The rates should be reduced as shown on Schedule No. 4 to remove \$23,969 for rate case expense, grossed-up for regulatory assessment fees (RAFs), which is being amortized over a four-year period. The decrease in 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. (Buys)

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 RAFs which is \$23,969 for wastewater. The decreased revenue will result in the rate reduction recommended by staff on Schedule No. 4.

The Utility should be required to file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. 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. Tierra Verde should provide proof of the date notice was given no less than 10 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 17: 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, Tierra Verde should provide proof, within 90 days of the final order in this docket, that the adjustments for all the applicable National Association of Regulatory Utility Commissioners Uniform System of Accounts primary accounts have been made. (Buys)

Staff Analysis: To ensure that the Utility adjusts its books in accordance with the Commission's decision, Tierra Verde should provide proof, within 90 days of the final order in this docket that the adjustments for all the applicable National Association of Regulatory Utility Commissioners Uniform System of Accounts primary accounts have been made.

Issue 18: Should this docket be closed?

Recommendation: No. If no person whose substantial interests are affected by the proposed agency action files a protest within twenty-one days of the issuance of the order, a consummating order will be issued. 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, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively, and the corporate undertaking should be released. (Buys)

Staff Analysis: No. If no person whose substantial interests are affected by the proposed agency action files a protest within twenty-one days of the issuance of the order, a consummating order will be issued. 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, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively, and the corporate undertaking should be released.

| Tierra Verde Utilities, Inc. Schedule of Wastewater Rate Base Test Year Ended 12/31/07 | | | Schedule No. 1-A Docket No. 080248-SU | | |
|--|-----------------------------|-----------------------------|--|---------------------------|--------------------------------|
| Description | Test Year Per Utility | Utility Adjust- ments | Adjusted Test Year Per Utility | Staff Adjust- ments | Staff Adjusted Test Year |
| 1 Plant in Service | \$3,901,999 | \$177,075 | \$4,079,074 | \$0 | \$4,079,074 |
| 2 Land and Land Rights | 234 | 0 | 234 | 0 | 234 |
| 3 Non-used and Useful Components | 0 | 0 | 0 | 0 | 0 |
| 4 Accumulated Depreciation | (2,135,206) | (17,501) | (2,152,707) | 77,346 | (2,075,361) |
| 5 CIAC | (1,687,658) | 0 | (1,687,658) | (25,424) | (1,713,082) |
| 6 Amortization of CIAC | 1,226,192 | 0 | 1,226,192 | (105,863) | 1,120,329 |
| 7 CWIP | 116,722 | (116,722) | 0 | 0 | 0 |
| 8 Acquisition Adjustment | 351,207 | (351,207) | 0 | 0 | 0 |
| 9 Accum. Amort. Of Acq. Adjustments | (81,247) | 81,247 | 0 | 0 | 0 |
| 10 Working Capital Allowance | <u>0</u> | <u>106,616</u> | <u>106,616</u> | <u>(14,892)</u> | <u>91,724</u> |
| 11 Rate Base | <u>\$1,692,243</u> | <u>(\$120,492)</u> | <u>\$1,571,751</u> | <u>(\$68,833)</u> | <u>\$1,502,918</u> |

| Tierra Verde Utilities, Inc. Adjustments to Rate Base Test Year Ended 12/31/07 | | Schedule No. 1-B Docket No. 080248-SU |
|---|--|--|
| Explanation | Wastewater | |
| <u>Accumulated Depreciation</u> | | |
| 1 | To reflect appropriate adjustment from prior rate case (AF No. 2) | \$75,829 |
| 2 | To adjust for use of incorrect depreciation rates (AF No. 4) | <u>1,517</u> |
| | Total | <u>\$77,346</u> |
| <u>CIAC</u> | | |
| 1 | To adjust for CIAC not included in MFRs (AF No. 1) | (\$25,425) |
| 2 | To reflect appropriate adjustment from prior rate case (AF No. 2) | <u>1</u> |
| | Total | <u>(\$25,424)</u> |
| <u>Accumulated Amortization of CIAC</u> | | |
| 1 | To reflect adjustment for CIAC not included in MFRs (AF No. 1) | \$614 |
| 2 | To reflect appropriate adjustment from prior rate case (AF No. 2) | (107,686) |
| 3 | To reflect adjustment for use of incorrect depreciation rates (AF No. 4) | <u>1,209</u> |
| | Total | <u>(\$105,863)</u> |
| <u>Working Capital</u> | | |
| | To reflect staff's recalculation of working capital | <u>(\$14,892)</u> |

Tierra Verde Utilities, Inc.
Capital Structure-Simple Average
Test Year Ended 12/31/07

Schedule No. 2
Docket No. 080248-SU

| Description | Total Capital | Specific Adjustments | Subtotal Adjusted Capital | Prorata Adjustments | Capital Reconciled to Rate Base | Ratio | Cost Rate | Weighted Cost |
|--------------------------|-----------------------------|----------------------|-----------------------------|-------------------------------|---------------------------------|-----------------------|--------------------|---------------------|
| Per Utility | | | | | | | | |
| 1 Long-term Debt | \$180,000,000 | \$0 | \$180,000,000 | (\$179,197,989) | \$802,011 | 51.03% | 6.65% | 3.39% |
| 2 Short-term Debt | 7,750,000 | 0 | 7,750,000 | (7,715,466) | 34,534 | 2.20% | 2.44% | 0.05% |
| 3 Preferred Stock | 0 | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% |
| 4 Common Equity | 139,282,132 | 0 | 139,282,132 | (138,661,535) | 620,597 | 39.48% | 11.70% | 4.62% |
| 5 Customer Deposits | 0 | 0 | 0 | 0 | 0 | 0.00% | 6.00% | 0.00% |
| 6 Deferred Income Taxes | <u>114,609</u> | <u>0</u> | <u>114,609</u> | <u>0</u> | <u>114,609</u> | <u>7.29%</u> | 0.00% | <u>0.00%</u> |
| 7 Total Capital | <u>\$327,146,741</u> | <u>\$0</u> | <u>\$327,146,741</u> | <u>(\$325,574,990)</u> | <u>\$1,571,751</u> | <u>100.00%</u> | | <u>8.07%</u> |
| Per Staff | | | | | | | | |
| 8 Long-term Debt | \$180,000,000 | \$0 | \$180,000,000 | (\$179,235,868) | \$764,132 | 50.84% | 6.65% | 3.38% |
| 9 Short-term Debt | 7,750,000 | 0 | 7,750,000 | (7,717,100) | 32,900 | 2.19% | 2.44% | 0.05% |
| 10 Preferred Stock | 0 | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% |
| 11 Common Equity | 139,282,132 | 0 | 139,282,132 | (138,690,854) | 591,278 | 38.34% | 12.34% | 4.86% |
| 12 Customer Deposits | 0 | 0 | 0 | 0 | 0 | 0.00% | 6.00% | 0.00% |
| 13 Deferred Income Taxes | <u>114,609</u> | <u>0</u> | <u>114,609</u> | <u>0</u> | <u>114,609</u> | <u>7.63%</u> | 0.00% | <u>0.00%</u> |
| 14 Total Capital | <u>\$327,146,741</u> | <u>\$0</u> | <u>\$327,146,741</u> | <u>(\$325,643,822)</u> | <u>\$1,502,919</u> | <u>100.00%</u> | | <u>8.29%</u> |
| | | | | | | <u>LOW</u> | <u>HIGH</u> | |
| | | | | | RETURN ON EQUITY | <u>11.34%</u> | <u>13.34%</u> | |
| | | | | | OVERALL RATE OF RETURN | <u>7.90%</u> | <u>8.68%</u> | |

| Tierra Verde Utilities, Inc. Statement of Wastewater Operations Test Year Ended 12/31/07 | | | | | | Schedule No. 3-A Docket No. 080248-SU | |
|--|-----------------------------|-----------------------------|--------------------------------------|---------------------------|--------------------------------|--|------------------------|
| 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 Operating Revenues: | <u>\$690,922</u> | <u>\$441,761</u> | <u>\$1,132,683</u> | <u>(\$351,954)</u> | <u>\$780,729</u> | <u>\$287,930</u> 36.88% | <u>\$1,068,659</u> |
| Operating Expenses | | | | | | | |
| 2 Operation & Maintenance | \$45,324 | \$207,606 | \$852,930 | (\$119,137) | \$733,793 | | \$733,793 |
| 3 Depreciation | 14,180 | 34,614 | 48,794 | 59,110 | 107,904 | | 107,904 |
| 4 Amortization | 0 | 0 | 0 | 0 | 0 | | 0 |
| 5 Taxes Other Than Income | 35,338 | 25,189 | 60,527 | (15,170) | 45,357 | 12,957 | 58,314 |
| 6 Income Taxes | <u>(43,791)</u> | <u>87,541</u> | <u>43,750</u> | <u>(103,184)</u> | <u>(59,434)</u> | <u>103,472</u> | <u>44,039</u> |
| 7 Total Operating Expense | <u>\$651,051</u> | <u>\$354,950</u> | <u>\$1,006,001</u> | <u>(\$178,381)</u> | <u>\$827,620</u> | <u>\$116,429</u> | <u>\$944,049</u> |
| 8 Operating Income | <u>\$39,871</u> | <u>\$86,811</u> | <u>\$126,682</u> | <u>(\$173,573)</u> | <u>(\$46,891)</u> | <u>\$171,501</u> | <u>\$124,609</u> |
| 9 Rate Base | <u>\$1,692,243</u> | | <u>\$1,571,751</u> | | <u>\$1,502,918</u> | | <u>\$1,502,918</u> |
| 10 Rate of Return | <u>2.36%</u> | | <u>8.06%</u> | | <u>-3.12%</u> | | <u>8.29%</u> |

| Tierra Verde Utilities, Inc. | | Schedule 3-B |
|--|-------------------|-----------------------------|
| Adjustment to Operating Income | | Docket No. 080248-SU |
| Test Year Ended 12/31/07 | | |
| Explanation | Wastewater | |
| <u>Operating Revenues</u> | | |
| Remove requested final revenue increase | | <u>(\$351,954)</u> |
| <u>Operation and Maintenance Expense</u> | | |
| 1 To reduce Contractual Services - Legal (AF No. 3) | | (\$114) |
| 2 To reflect the appropriate adjustment to prior rate case expense (AF No. 3) | | (2,829) |
| 3 To reflect adjustment to Transportation Expense (Allocation AF No. 5) | | 3,138 |
| 4 To reduce Purchased Sewer Treatment Expense due to I&I | | (84,119) |
| 5 To reflect the appropriate amount of expense for TV Sewer Mains project | | (1,570) |
| 6 To remove unsupported temporary employment in Contractual Services - Other | | (14,536) |
| 7 To reflect the appropriate amount of rate case expense | | <u>(19,107)</u> |
| Total | | <u>(\$119,137)</u> |
| <u>Depreciation Expense - Net</u> | | |
| 1 To reflect the appropriate amount of amortization expense for CIAC (AF No. 1) | | (\$1,228) |
| 2 To reflect the appropriate depreciation rates (AF No. 4) | | (8,074) |
| 3 To reflect the appropriate amount of amortization expense for CIAC (AF No. 2) | | 67,203 |
| 4 To reflect the appropriate amount of amortization expense for CIAC (AF No. 4) | | <u>1,209</u> |
| Total | | <u>(\$59,110)</u> |
| <u>Taxes Other Than Income</u> | | |
| 1 RAFs on revenue adjustments above | | (\$15,838) |
| 2 To reflect appropriate amount of RAFs in test year (AF No. 4) | | 3,251 |
| 3 To reflect appropriate amount of property tax in test year (AF No. 4) | | <u>(2,583)</u> |
| Total | | <u>(\$15,170)</u> |

| Tierra Verde Utilities, Inc. | | | | Schedule No. 4 | |
|---|-----------------|-------------------|------------------|-----------------------------|------------------|
| Wastewater Bi-Monthly Service Rates | | | | Docket No. 080248-SU | |
| Test Year Ended 12/31/07 | | | | | |
| | Rates | Commission | Utility | Staff | Four-year |
| | Prior to | Approved | Requested | Recomm. | Rate |
| | Filing | Interim | Final | Final | Reduction |
| <u>Residential Flat Rate</u> | \$74.23 | \$86.90 | \$107.69 | \$100.53 | \$2.25 |
| <u>General Service</u> | | | | | |
| Base Facility Charge by Meter Size: | | | | | |
| 5/8" x 3/4" | \$48.28 | \$56.25 | \$70.04 | \$63.66 | \$1.43 |
| 1" | \$120.71 | \$140.64 | \$175.13 | \$159.15 | \$3.57 |
| 1-1/2" | \$241.40 | \$281.26 | \$350.22 | \$318.29 | \$7.14 |
| 2" | \$386.24 | \$450.01 | \$560.36 | \$509.27 | \$11.42 |
| 3" | \$772.48 | \$900.01 | \$1,120.71 | \$1,018.54 | \$22.84 |
| 4" | \$1,207.00 | \$1,406.28 | \$1,751.12 | \$1,591.47 | \$35.69 |
| 6" | \$2,414.00 | \$2,812.55 | \$3,502.23 | \$3,182.93 | \$71.39 |
| Gallonge Charge, per 1,000 Gallons | \$2.37 | \$2.76 | \$3.44 | \$3.39 | \$0.08 |
| <u>Typical Residential Bills 5/8" x 3/4" Meter</u> | | | | | |
| 3,000 Gallons | \$74.23 | \$86.90 | \$107.69 | \$100.53 | |
| 5,000 Gallons | \$74.23 | \$86.90 | \$107.69 | \$100.53 | |
| 10,000 Gallons | \$74.23 | \$86.90 | \$107.69 | \$100.53 | |
| (Wastewater Gallonge Cap - 10,000 Gallons) | | | | | |