

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: October 29, 2009

TO: Office of Commission Clerk (Cole)

FROM: Division of Regulatory Compliance (Brown, Deamer)
Division of Economic Regulation (Bruce, Rieger)
Office of the General Counsel (Brubaker)

RE: Docket No. 090060-WU – Application for staff-assisted rate case in Duval County by Neighborhood Utilities.
County: Duval County

AGENDA: 11/10/09 – Regular Agenda – Proposed Agency Action - Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Skop

CRITICAL DATES: 06/28/10 (15-Month Effective Date (SARC))

SPECIAL INSTRUCTIONS: None

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Case Background

Neighborhood Utilities, Inc. (Neighborhood or Utility) is a Class C utility serving 429 water customers in Duval County. According to the Utility's 2008 Annual Report, total gross revenues were \$86,556 for water. The Utility's operating expenses were \$121,837 for water.

The Utility was granted water Certificate No. 430-W in 1984, in Docket No. 840063-WU.¹ Rate Base was also established in that docket. On January 30, 2009, the Utility filed a request for a staff-assisted rate case (SARC). Neighborhood Utilities, Inc. has not filed for an index or a pass through since the certificate was granted in 1984.

The Commission has the authority to consider this rate case pursuant to Section 367.0814, Florida Statutes (F.S.)

¹ Order No. 13723, issued September 28, 1984, in Docket No. 840063-WU, In Re: Application of Neighborhood Utilities, Inc. for a certificate to operate a water utility in Duval County, Florida.

Discussion of Issues

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

Recommendation: No. The overall quality of service provided by Neighborhood Utilities, Inc. is marginal. In order to monitor the customers' concerns about the precautionary "boil water" notices as required by the Department of Environmental Protection (DEP), it is recommended that the Utility provide the Commission with a copy of both the initial and rescinding boil water notifications for a period of one year after the Commission order concerning the rate case. (Rieger)

Staff Analysis: Pursuant to Rule 25-30.433(1), Florida Administrative Code (F.A.C.), the Commission determines the overall quality of service provided by a utility by evaluating three separate components of water operations, including the quality of the utility's product, the operational condition of the utility's plants and facilities, and the utility's attempt to address customer satisfaction. Comments or complaints received by the Commission from customers are reviewed. The utility's current compliance with the Department of Environmental Regulation (DEP) is also considered.

Quality of Utility's Product and Operational Condition of Plant and Facilities

Neighborhood is currently in compliance with DEP rules and regulations; however, there are several problems that the Utility needs to address which appear to result from the owner's failure to provide routine maintenance upkeep of Utility property. There have been sporadic compliance problems related to maintaining chlorine residuals at points furthest from the water treatment plant. DEP has indicated that as recently as August of this year, tests showed coliform bacteria to be positive. The Utility has addressed the situation through increased line flushing. DEP now considers the Utility's system to be operating in normal condition.

According to a 2008 DEP Sanitary Survey, it was noted that there was excessive rusting and corrosion on structures and equipment. A Commission staff investigation of Neighborhood was conducted on May 14, 2009. As noted by DEP, Commission staff also found rusting and corrosion to exist throughout the facility. In addition, one of the three high service pumps and one of the two wells at the water treatment plant were out of service. Because of its relatively small pumping capability, the Utility does not intend to reactivate the well. The Utility's owner indicated to staff that the deferred maintenance to the facility is the result of inadequate funds. The Utility has provided staff with a reliable cost estimate to address the rusting and corrosion situation which Commission staff is recommending to be included in the proforma adjustments discussed in Issue 12. The Utility has not produced sufficient documentation to support the cost of repair or replacement of the high service pump. Although there is no proforma cost estimate for high service pumping repair or replacement considered in this recommendation, staff believes that an existing interconnection with JEA provides adequate backup reliability in case of further equipment failure.

System reliability is maintained through an auxiliary power source (generator) and an emergency backup connection with a water system owned by JEA. As a result of a hydropneumatic tank malfunction, which occurred in April of 2009, the Utility purchased water from JEA while a replacement tank was manufactured and placed into service. The replacement tank was installed and the Utility's water treatment plant put back into service on July 9, 2009.

Summary. Staff believes that quality of the Utility's product and the operating condition of the Utility's water plant are marginal based on the utility's failure to provide routine maintenance of its facilities. Staff recommends that proforma plant improvements be included in rate base to address the operational and maintenance needs of this facility.

The Utility's Attempt to Address Customer Satisfaction

Customer Meeting. A customer meeting was held on September 16, 2009, at the West Regional Library in Jacksonville, Florida. Six customers attended the evening meeting. All of the attendees brought up concerns about the quality of service provided by the Utility. The customers were primarily upset over inconveniences related to the issuances of precautionary "boil water" notices as required by the DEP. These notices are usually issued in response to possible health risks related to low pressure due to line breakage or equipment failure and inadequate chlorine residuals. The customers believe that the incidences requiring notices occur much too frequently. In addition to the inconvenience of having to boil water, the customers were also concerned about how the Utility delivers notices. They noted that these hand delivered notices often fall off mail boxes to the ground and that some customers may never become aware of the situation. Also, follow-up rescinding notifications which indicate the "all clear" rarely happen.

Given what is considered unreliable service, the customers are distressed over health concerns related to the Utility's water quality. One customer spoke of problems regarding sulfuric odors and the Utility having difficulty maintaining chlorine residuals on his street. He pointed out that the Utility tries to sustain appropriate chlorine residuals through line flushing and expressed concern about the cost of the water used. Other customers spoke of problems with water pressure and being unable to contact the Utility to get information. Aware of JEA's existing backup supply connection with the Utility's system, all customers who provided comments would prefer to receive water service from JEA because of their perception that JEA has a better product and more reliable service.

Customer Complaints. Since 2003, there have been five customer complaints logged with the Commission. Four complaints were related to billing and have since been closed. A fifth closed complaint was about frequent outages, Utility contact problems, and the placement of boil water notices. It should be noted that this complainant spoke of the very same issues at the customer meeting.

Neighborhood's Response To Quality of Service Concerns. The Utility has noted that its equipment is over 25 years old and needs to be replaced. Neighborhood points out that the current rates are too low to generate revenues needed to pay for needed equipment replacements and upgrades, or to allow for staff to be hired to respond adequately to the customer calls. In reference to the noticing concerns, the Utility believes that it delivers the notices by the quickest and most effective method. It states that the best location for placement of individual notices is determined on a case by case basis by the person delivering the notices. However, DEP records do reflect incomplete information regarding the Utility's rescinding boil water notices.

Summary. The ability of the customers to more efficiently contact the Utility should improve with additional office staffing, as recommended in the proforma adjustments discussed in Issue 12. Given the current status of the above mentioned customer service problems, staff believes that the Utility's ability to address customer satisfaction is marginal.

Conclusion

The Utility's quality of service efforts with respect to corrosion control and increased staffing should improve with the proforma improvements recommended in Issue 12 of this recommendation. However, given our review, we are concerned that even with the improvements, systems reliability, as well as the general quality of service provided to the customers, may continue to be plagued with sporadic problems. In response to the concerns of the customers, staff has considered the possibility of JEA being a bulk water provider in lieu of having the Utility continue to operate its water treatment facility. Staff contacted JEA about the possibility of providing wholesale water service to Neighborhood. JEA indicated that it is willing and possibly able (pending additional pressure studies) to provide water supply. Initial costs associated with this service would include a meter set fee, gross capacity fee, and a plant capacity fee totaling approximately \$108,000. However, the expenses associated with converting to use an alternate water supply source would result in higher rates. In addition, an interconnection has not been mandated by DEP, and is not desired by the Utility.

Staff believes that Neighborhood's quality of product, operational condition of its water treatment plant and facilities, and its attempt to address customer satisfaction are marginal. The Utility's deferred maintenance to its water treatment plant and distribution system has caused sporadic substandard service to its customers. While the Utility may have deferred improvements due to the lack of funds, these problems are the management's responsibility to correct, rather than the customers' fault. However, implementing fines and penalties on this small Utility would most likely be counterproductive.

Staff recommends that the overall quality of service provided by Neighborhood be considered marginal. In order to monitor the customers' concerns about the precautionary "boil water" notices as required by the DEP, we recommend that the Utility provide the Commission with a copy of both the initial and rescinding boil water notifications for a period of one year after the Commission order concerning the rate case is issued. In addition, the Utility should be put on notice that the customers should have reasonable access to contact the Utility during normal business hours as well as a means of emergency, after-hours contact.

Issue 2: What are the used and useful percentages of the Utility's water system?

Recommendation: The treatment plant and distribution system is considered 100 percent used and useful. (Rieger)

Staff Analysis: The Utility serves 429 customers. The water treatment system has two wells rated at 257 gpm and 90 gpm, although the smaller well is inactive. Raw water is treated with liquid chlorine for disinfection purposes. This facility has two storage tanks totaling 40,000 gallons. There are twenty-two fire hydrants located throughout the service area. There has been no prior rate case for this Utility; therefore, used and useful has not been previously established by the Commission. Pursuant to Rule 25-30.4325, F.A.C., with only ten lots left to be built upon, staff believes that the service territory the treatment plant and distribution system are designed to serve is built out. Therefore, it is recommended that the treatment plant and distribution system be considered 100 percent used and useful.

Issue 3: What is the appropriate average test year rate base for the Utility?

Recommendation: The appropriate average test year rate base for the Utility is \$660 for water. (Brown)

Staff Analysis: The appropriate components of the Utility's rate base include, Utility Plant in Service (UPIS), Contributions-In-Aid-of-Construction (CIAC), Accumulated Depreciation, Accumulated Amortization of CIAC, and a Working Capital allowance.

Staff selected a test year ended December 31, 2008, for this rate case. Rate base for this Utility was established as of September 28, 1984, in Docket No. 840063-WU.² Sufficient records of the original construction and expansion of plant and subsequent additions were available and were included within the audit. A summary of each component and the adjustments follows.

Utility Plant in Service: The Utility recorded \$617,959 of UPIS for the test year ended December 31, 2008, for water. Staff has made an adjustment to increase UPIS by \$47,927 to reflect the appropriate plant balances per company documentation. This \$47,927 adjustment consists of the following: 1) increase of \$9,560 to reflect the reclassification plant improvements that were previously expensed; 2) decrease of \$3,350 to reflect the retirement of a turbine motor; 3) increase of \$28,317 to reflect hydro tank replacement in 2009; 4) decrease of \$90 to reflect averaging adjustment; 5) an increase of \$18,130 to reflect invoices that were not recorded; and 6) a decrease of \$4,640 to reflect unsupported invoices.

Staff's net adjustment to UPIS is an increase of \$47,927 ($\$9,560 - \$3,350 + \$28,317 - \$90 + \$18,130 - \$4,640$). Staff's recommended UPIS balance is \$665,886.

Non-used and Useful Plant: As discussed in Issue No. 2, the Utility's water treatment plant should be considered 100 percent used and useful. Therefore, a used and useful adjustment is unnecessary.

Contribution in Aid of Construction (CIAC): The Utility recorded CIAC of \$786,578 for water, for the test year ended December 31, 2008. Staff reviewed necessary documentation and believes CIAC to be reasonable. Therefore, staff did not make an adjustment to this account.

Accumulated Depreciation: The Utility recorded a balance for accumulated depreciation of \$381,217 for water for the test year. Staff has calculated accumulated depreciation using the prescribed rates set forth in Rule 25-30.140, F.A.C. As a result, staff has decreased this account by \$88,397 for water to reflect depreciation calculated per staff. Included within this amount is a decrease of \$7,020 to reflect averaging adjustments for water. Staff's recommended Accumulated Depreciation balance is \$292,820.

² Order No. 13723, In Re: Application of Neighborhood Utilities, Inc. for a certificate to operate a water utility in Duval County, Florida.

Accumulated Amortization of CIAC: The Utility recorded \$462,313 for accumulated amortization of CIAC for water. Accumulated Amortization of CIAC has been recalculated by staff using composite depreciation rates. In order to reflect accumulated amortization of CIAC as calculated by staff, this account has been decreased by \$63,665. Included within this amount is a decrease of \$10,126 to reflect averaging adjustments. Staff's net adjustments to this account results in Accumulated Amortization of CIAC of \$398,648.

Working Capital Allowance: Working capital is defined as the investor-supplied funds necessary to meet operating expenses or going-concern requirements of the Utility. Consistent with Rule 25-30.433(2), F.A.C., staff used the one-eighth of the Operations and Maintenance (O&M) expense formula approach for calculating working capital allowance. Applying this formula, staff recommends a working capital allowance of \$14,523 (based on O&M expense of \$116,187). Working capital has been increased by \$14,523 to reflect one-eighth of staff's recommended O&M expenses.

Rate Base Summary: Based on the forgoing, staff recommends that the appropriate test year average rate base is \$660 for water. Rate base is shown on Schedule No. 1-A, and staff's adjustments are shown on Schedule 1-B.

Docket No. 090060-WU

Date: October 29, 2009

Issue 4: What is the appropriate rate of return on equity and overall rate of return for this Utility?

Recommendation: The appropriate return on equity is 11.30 percent with a range of 10.30 - 12.30 percent. The appropriate overall rate of return is 9.65 percent. (Brown)

Staff Analysis: The Utility recorded long term debt of \$94,761 and customer deposits of \$9,127 in its capital structure for the test year.

Using the leverage formula established by Order No. PSC-09-0430-PAA-WS, issued June 19, 2009, in Docket No. 090006-WS, In re: Water and wastewater industry annual reestablishment of authorized range of return on common equity for water and wastewater utilities pursuant to Section 367.081(4)(f), F.S., the appropriate return on equity is 11.30 percent.

The Utility has \$94,761 in long term debt payable to various banks. The average interest rate for these loans is 10 percent. The Utility did not pay interest in 2008.

Staff recommends a return on equity of 11.30 percent with a range of 10.30 - 12.30 percent, and an overall rate of return of 9.65 percent. The return on equity and overall rate of return are shown on Schedule No. 2.

Docket No. 090060-WU

Date: October 29, 2009

Issue 5: What are the appropriate amount of test year revenues?

Recommendation: The appropriate test year revenue for this Utility is \$89,675 for water.
(Bruce, Brown)

Staff Analysis: Neighborhood Utilities recorded total revenues of \$88,344 for water for the 12-month period ended December 31, 2008. Staff analyzed the Utility's reported revenues and determined that the water revenues were understated by \$1,331. Based on the above, staff recommends test year revenue of \$89,675 for water. Test year revenue is shown on Schedule 3-A. The related adjustments are shown on Schedule 3-B.

Issue 6: What is the appropriate amount of test year operating expense?

Recommendation: The appropriate amount of operating expense for the Utility is \$118,465 for water. (Brown)

Staff Analysis: Per Schedule 3-A, the Utility recorded total Operating Expenses of \$127,843. The test year expenses have been reviewed; and invoices, canceled checks, and other supporting documentation have been examined. Recalculations have been used when necessary. Staff made several adjustments to the Utility's operating expenses, as summarized below:

Operation and Maintenance Expenses (O&M)

Salaries and Wages – Employees – (601) – The Utility recorded salaries and wages – employees as \$0 for the test year. Staff recommends a test year balance of \$0.

Salaries and Wages – Officers – (603) – The Utility owner claims a salary of \$24,000 per year, but paid himself less than \$24,000 in the test year. Staff believes owner is entitled to the \$24,000 per year and that the amount is reasonable; therefore, no adjustment was made to the account.

Purchased Power – (615) – The Utility provided invoices that indicated the purchased power for the test year was \$7,671 for water. Staff believes the purchased power amounts are reasonable and no adjustments were made to this account.

Chemicals – (618) – The Utility provided invoices that indicated the chemicals for the test year were \$3,423 for water. Staff believes the chemical amounts are reasonable and no adjustments were made to this account.

Materials and Supplies – (620) – The Utility provided invoices that indicate material and supplies for the test year was \$3,711 for water. To facilitate the Utility to go from quarterly billing to monthly billing, staff made an adjustment to increase materials and supplies by \$3,440. Staff's recommended materials and supplies is \$7,151.

Contractual Services - Professional – (631) – The Utility provided invoices indicating its accounting services for the test year was \$5,284. The accounting services consisted of the year-end closing of the books and the preparation of the Utility's annual report and tax return. Staff believes this amount is reasonable and no adjustments were made to this account.

Contractual Services – Testing – (635) – The Utility provided invoices indicating its contractual services for testing services for the test year was \$2,973. State and local authorities require that several analyses be submitted in accordance with Chapter 62-550, F.A.C. Testing costs incurred during the test year did not include these non-annual testing costs. Staff recommends that an additional annualized expense of \$785(\$2,356/3) be included in account 635 - Contractual Services - Testing for additional testing requirements. These tests are required by DEP every three or more years. Staff's recommended contractual services – testing is \$3,758 (\$2,973+\$785).

Contractual Services – Other – (636) – The Utility provided invoices that indicate contractual services – other for the test year was \$34,015. Staff’s recommended contractual services – other is \$34,015.

Rents – (640) – The Utility recorded \$8,479 in this account during the test year. A staff adjustment of \$257 was made to remove parking fees at the utility office in downtown Jacksonville for weekend parking. Staff’s recommended rent is \$8,222.

Transportation – (650) – The Utility recorded \$1,826 in this account during the test year. The Utility provided invoices that indicated that transportation for the test year was \$1,826. Staff believes the transportation amounts are reasonable and no adjustment was made to this account.

Insurance Expense – (655) – The Utility recorded \$5,349 in this account during the test year. The audit staff made a decreasing adjustment of \$3,346 to remove the non-utility life insurance coverage. Staff’s recommended insurance expense is \$2,003.

Regulatory Commission Expense – (665) – The Utility recorded \$1,200 in this account during the test year. Pursuant to Section 367.0816, F.S., rate case expense is amortized over a 4-year period. In addition, the Utility is also required by Rule 25-22.0407, F.A.C., to mail notices of the customer meeting and notices of final rates in this case to its customers. For these notices, staff has adjusted this account by \$856 to include these notices that will be amortized over four years. Staff also made an increasing adjustment of \$250 ($\$1,000/4$) for a filing fee that will be amortized over four years. Therefore, staff recommends that total regulatory commission expense is \$764 ($\$1,200 + \$1,000 + \856)/4.

Miscellaneous Expense – (675) – The Utility recorded \$25,585 for miscellaneous expense for the test year. Audit staff made a decreasing adjustment of \$7,516 for the test year. Staff recommends that total miscellaneous expense is \$18,069. The related adjustments are shown on Schedule 3-B.

Operation and Maintenance Expense (O & M) Summary – The Utility recorded \$123,516 for total O&M expense. Staff’s recommended O&M expenses are \$116,187. O&M expense adjustments are shown on Schedule 3-B.

Depreciation Expense

Depreciation Expense – The Utility recorded \$17,417 for depreciation expense. Staff has calculated depreciation expense using the prescribed rates set forth in Rule 25-30.140, F.A.C. Staff decreased depreciation expense by \$3,399 to reflect the changes in rates and for \$383 to reflect the depreciation on reclassified plant additions and retirements. Staff calculated depreciation expense for the hydrotank item paid for in 2009 to be \$943. Staff’s recommended depreciation expense is \$14,578.

Amortization of Contributions in Aid of Construction CIAC

Amortization of CIAC – The Utility recorded \$31,463 for amortization of CIAC. Staff has calculated amortization of CIAC using composite rates from the prescribed rates set forth in Rule 25-30.140, F.A.C. Staff's recommended amortization of CIAC is \$19,900.

Taxes Other Than Income

Taxes Other Than Income (TOTI) – The Utility recorded \$18,373 for taxes other than income. Staff's adjustments to TOTI are as follows: 1) decrease TOTI by \$14,808 to remove Right of Way and Public Service Utility taxes. These taxes are 10 and 5 percent respectively. These are stated separately on the customer bill and are established by the county. 2) increase by \$3,975 to reflect Regulatory Assessment Fees (RAF) on test year per Utility; and 3) increase by \$60 to reflect RAF on test year revenues per audit. The recommended taxes other than income is \$7,600.

Operating Expenses Summary – The application of staff's recommended adjustments to the audited test year operating expenses results in staff's calculated operating expenses of \$118,465. Operating expenses are shown on Schedule No. 3-A. The related adjustments are shown on Schedule 3-B.

Issue 7: Should the Commission utilize the operating ratio methodology as an alternative means to calculate the revenue requirement for Neighborhood Utilities, Inc. and, if so, what is the appropriate margin?

Recommendation: Yes, the Commission should utilize the operating ratio methodology for calculating the revenue requirement for the Utility water system. The margin should be 10 percent of O&M expense. (Brown)

Staff Analysis: Section 367.0814(9), F.S., provides that the Commission may, by rule, establish standards and procedures for setting rates and charges of small utilities using criteria other than those set forth in Sections 367.081(1), (2)(a), and (3), F.S. Pursuant to Rule 25-30.455, F.A.C., utilities whose total gross annual operating revenues are \$250,000 or less per system may petition the Commission for staff assistance in alternative rate settings.

Although Neighborhood did not petition the Commission for alternative rate setting under the aforementioned rule, staff believes that the Commission should exercise its discretion to employ the operating ratio methodology as an alternative means to set rates in this case. The operating ratio methodology is an alternative to the traditional calculation of revenue requirements. Under this methodology, instead of applying a rate of return on the Utility's rate base, the revenue requirement is based on the margin of Neighborhood's O&M expenses. This methodology has been applied in cases where the traditional calculation of revenue requirements would not provide sufficient revenues to protect against potential variances in revenues and expenses.

By Order No. PSC-96-0357-FOF-WU, issued March 13, 1996, in Docket No. 950641-WU, In re: Application for staff-assisted rate case in Palm Beach County by Lake Osborne Utilities Company, Inc., the Commission, for the first time, utilized the operating ratio methodology as an alternative means for setting rates. This order also established criteria to determine the use of the operating ratio methodology and a guideline margin of 10 percent of O&M expense.

In addition, by Order No. PSC-97-0130-FOF-SU, issued February 10, 1997, in Docket No. 960561-WU, In re: Application for staff-assisted rate case in Citrus County by Indian Springs Utilities, Inc., the Commission utilized the operating ratio methodology for setting rates. The same criteria and 10 percent margin of O&M expense was approved as in Order No. PSC-96-0357-FOF-WU.

In Order No. PSC-96-0357-FOF-WU, the Commission established criteria to determine whether to utilize the operating ratio methodology for those utilities with low or non-existent rate base. The following discusses the qualifying criteria established by Order No. PSC-96-0357-FOF-WU, and how they apply to the Utility.

- 1) Whether the utility's O&M expense exceeds rate base. In the instant case, the rate base is substantially lower than the level of O&M expense. Based on the staff audit, the adjusted rate base for the test year is \$660, while adjusted O&M expenses are \$116,187.

- 2) Whether the utility is expected to become a Class B in the foreseeable future. According to Chapter 367.0814(9), F.S., the alternative forms of regulation being considered in this case only apply to small utilities whose gross annual revenues are \$150,000 or less. Neighborhood is a Class C utility and the recommended revenue requirement of \$131,987 is substantially below the threshold level for Class B status (\$200,000 per system). The Utility's service area has not had any growth in the last five years and is essentially built out. Therefore, the Utility will not become a Class B utility in the foreseeable future.
- 3) Quality of service and condition of plant. A review of the DEP records shows no compliance problems. The quality of service appears marginal.
- 4) Whether the utility is developer owned. Although the current Utility owner is a developer, the service territory is not in the early stages of growth, and there has not been any customer growth in the last five years.
- 5) Whether the utility operates treatment facilities or is simply a distribution and/or collection system. Neighborhood operates its own treatment facilities.

By Order No. PSC-96-357-FOF-WS, the Commission determined that a margin of 10 percent shall be used unless unique circumstances justify the use of a greater or lesser margin. The Commission settled on the 10 percent margin due to lack of economic guidance on developing an operating ratio method rate of return. The Commission believed that it would be futile and unwarranted exercise to try to establish a precise return applicable to all small utilities. The important question was not what the return percentage should be, but what level of operating margin will allow the utility to provide safe and reliable service and remain a viable entity. The answer to this question requires a great deal of judgment based upon the particular circumstances of the utility.

Several factors must be considered in determining the reasonableness of a margin. First, the margin must provide sufficient revenues for the Utility to cover its interest expense. Neighborhood did not pay interest expense in 2008 on its outstanding loans. Staff's recommended operating margin of \$11,619 is sufficient to cover interest expense.

Second, use of the operating ratio methodology rests on the contention that the principal risk to the Utility resides in operating cost rather than in capital cost of the plant. The fair return on a small rate base may not adequately compensate the Utility owner for incurring the risk associated with covering the much larger operating cost. Therefore, the margin should adequately compensate the Utility owner for that risk. Under the rate of return method, the return to Neighborhood, amounts to only \$64, which is enough to cover only a 0.06 percent variance in O&M expenses. Given this Utility's circumstances, staff believes that using the rate of return method would not be beneficial to the utility.

Third, if the rate of return method were applied, a normal return would generate such a small level of revenues that in the event staff estimates revenues or expenses incorrectly, Neighborhood could be left with insufficient funds to cover operating expenses. Therefore, the margin should provide adequate revenues to protect against potential variability in revenues and

expenses. The rate of return method would provide the Utility only \$64 in operating income to cover revenue and expense variances.

In conclusion, staff believes the above factors show that the Utility needs a higher margin of revenues over operating expenses than the traditional rate of return method would allow. Therefore, in order to provide Neighborhood with adequate cash flow to satisfy environmental requirements and to provide some assurance of safe and reliable service, staff recommends application of the operating ratio methodology at a margin of 10 percent of O&M expenses.

Issue 8: What is the appropriate revenue requirement?

Recommendation: The appropriate revenue requirement using the operating ratio methodology for calculating the revenue requirement is \$131,988. (Brown)

Staff Analysis: Using the operating ratio method for calculating the revenue requirement, the Utility should be allowed an annual increase in revenue of \$42,313 (47.18 percent). This will allow the Utility the opportunity to recover its expenses and earn a 10 percent operating margin on its adjusted operation and maintenance expense. The calculations are as follows:

	<u>Water</u>
Adjusted O&M Expenses	\$116,187
Less Purchased Water	0
Adjusted O&M less purchased water	<hr/> \$116,187
Rate of Return	x .10
Operating Margin	<hr/> \$11,619
Adjusted O&M expense	\$116,187
Depreciation expense (Net)	\$14,578
Amortization	(\$19,900)
Taxes Other Than Income	\$9,504
Income Taxes	\$0
Revenue Requirement	<hr/> \$131,988
Less Test Year Revenues	\$89,675
Annual Increase	<hr/> \$42,313
Percent Increase/(Decrease)	<hr/> 47.18%

Issue 9: Should the Utility's current rate structure be changed, and if so, what is the appropriate rate structure for the Utility's water system?

Recommendation: Yes. The Utility's current base facility charge (BFC)/uniform gallonage charge rate structure, which is billed on a quarterly basis, should be changed to a monthly three-tier inclining block rate structure with usage blocks set at: a) 0-5 kgals; b) 5-10 kgals; c) usage in excess of 10 kgals, with appropriate usage block rate factors of 1.0, 1.5, 2.0 respectively for water system's residential class. The appropriate rate structure for the water system's non-residential class is a traditional BFC/uniform gallonage charge. The billing system should be changed to a monthly basis. The water system's BFC cost recovery should be set at 35%. (Bruce)

Staff Analysis: Neighborhood currently has a BFC/uniform gallonage charge rate structure for the water system's residential and non-residential class. The BFC is \$28.45 and is billed on a quarterly basis. The monthly usage charge is \$1.14 per Kgal.

Water Rates: As mentioned above, the Utility's current rate structure consists of a BFC/uniform gallonage charge rate structure which is billed quarterly. In prior cases, it has been Commission practice to convert the Utility's billing system to a monthly system. By billing on a monthly basis, customers receive a more timely price signal that will allow them to adjust their consumption accordingly. Therefore, in order to promote a rate design that is consistent with past Commission practice, staff recommends changing the Utility's quarterly billing to monthly.

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 goals and practices.

Neighborhood is located in Duval County in the St. Johns River Water Management District (SJRWMD) or District. In its consumptive use permit (CUP), Condition No. 26 states the next rate case brought before the Commission must include a request for approval of a District approved-rate structure that is designed to encourage water conservation. Staff contacted the District in regards to an approved rate structure for the Utility and District staff indicated, if possible, that an inclining block rate structure be implemented for a water conserving rate structure.

Based on staff's analysis of the billing data, the customer's overall average monthly consumption is 6.7 Kgals. As indicated in the staff report, staff's preliminary recommended rate structure consisted of a two-tier inclining block rate structure with usage blocks set at 0-6 kgals and usage in excess of 6 kgal. However, staff re-evaluated the billing data and it indicates that seventeen percent of the gallons are at 10 kgals and above. This is an indication there is a significant amount of discretionary usage. Therefore, staff recommends a three-tier inclining block rate structure with usage blocks set at: a) 0-5 kgals; b) 5-10 kgals, c) usage in excess of 10 kgals, with usage block rate of 1.0, 1.5, and 2.0, respectively.

Furthermore, the utility's service area is comprised of a mobile home park and two subdivisions that consist of single family homes. Also, according to the utility owner, the utility serves retirees, single young adults, and families that consist of at least three to four people. For this reason, staff believes it is appropriate to increase the threshold for a customer's essential usage to approximately 3,375 gallons per month. This number is derived based on the average number of persons per household, gallons per day, days per month ($2.25 \times 50 \times 30$). Staff's recommended rate structure is designed to minimize the price increase for customers with low consumption in the first block; the second block is designed to target working families' consumption; and the third block is designed to target customers with consumption over 10 kgals.

Staff's recommended rate design for the water system is presented in Attachment A. Staff also presented two alternative rate structures to illustrate other recovery methodologies.

Staff recommends that the fixed cost recovery be reduced to 35 percent from the initial allocation of 57.82 percent. This shifts more of the cost recovery to the gallonage charge thereby making rates more conservation oriented.

Based on the foregoing, staff recommends that the Utility's current rate structure which includes a quarterly BFC be changed to a monthly three-tier inclining block rate structure with usage blocks set at: a) 0-5 kgal; b) 5-10 kgal; c) usage in excess of 10 Kgals, with usage block rate factors of 1.0, 1.5, 2.0, respectively for water system's residential class. The appropriate rate structure for the water system's non-residential class is a traditional BFC/uniform gallonage charge. The billing system should be changed to a monthly basis. The water system's BFC cost recovery should be set at 35 percent.

Issue 10: Is a repression adjustment appropriate in this case, and if so, what are the appropriate adjustments to make for this Utility, what are the appropriate corresponding expense adjustments to make, and what are the final revenue requirements?

Recommendation: Yes, a repression adjustment is appropriate for this Utility. Test year consumption should be reduced by 3,499 Kgals or 10.2 percent. Purchased power expense should be reduced by \$785, chemical expense should be reduced by \$350, and regulatory assessment fees (RAFs) should be reduced by \$53. The final post-repression revenue requirement for the water system should be \$130,799.

In order to monitor the effect of the changes to rate structure and revenue, the Utility should be ordered to file reports detailing the number of bills rendered, the consumption billed and the revenues billed on a monthly basis. In addition, the reports should be prepared, by customer class and meter size. The reports should be filed with staff, on a semi-annual basis, for a period of two years beginning the first billing period after the approved rates go into effect. To the extent the Utility makes adjustments to consumption in any month during the reporting period, the Utility should be ordered to file a revised monthly report for that month within 30 days of any revision (Bruce)

Staff Analysis: The price elasticity of demand is defined as the anticipated change in quantity demanded resulting from a change in price. All other things equal, as price increases, the quantity demanded decreases.

Staff conducted a detailed analysis of the consumption patterns of the Utility's residential customers as well as the effect of increased revenue requirements on the amount paid by residential customers at varying levels of consumption. As discussed in Issue 8, staff's analysis showed that average residential monthly consumption per customer was 6.7 Kgal. Also, as discussed in Issue 8, staff believes it is appropriate to set the threshold for the customer's essential usage to approximately 3,375 gallons per month. Staff's recommended repression adjustment therefore only applies to water consumption about 3,375 gallons per month.

Using our database of utilities that have previously had repression adjustments made, staff calculated a repression adjustment for this Utility based upon the recommended increase in revenues from monthly service in this case, and the historically observed response rates of consumption to changes in price. This is the same methodology for calculating repression adjustments that the Commission has approved in prior cases. Based on this methodology, staff calculated that test year residential water sold should be reduced by 785, chemical expense should be reduced by \$350, and regulatory assessment fee (RAFs) should be reduced by \$53. The final post-repression revenue requirement for the water system should be \$130,799.

In order to monitor the effect of the changes to rate structure and revenue, the Utility should be ordered to file reports detailing the number of bills rendered, the consumption billed and the revenues billed on a monthly basis. In addition, the reports should be prepared, by customer class and meter size. The reports should be filed with staff, on a semi-annual basis, for a period of two years beginning the first billing period after the approved rates go into effect. To the extent the Utility makes adjustments to consumption in any month during the reporting

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Date: October 29, 2009

period, the Utility should be ordered to file a revised monthly report for that month within 30 days of any revision.

Issue 11: What are the appropriate rates for this Utility?

Recommendation: The appropriate monthly water rates are shown on Schedules Nos. 4-A. The recommended rates should be designed to produce revenue in the amount of \$130,799 for water, excluding miscellaneous service 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 on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved rates should not be implemented until staff has approved the proposed customer notice and the notice has been received by the customers. The Utility should provide proof of the date notice was given no less than 10 days after the date of the notice. (Bruce, Brown)

Staff Analysis: Excluding miscellaneous service revenues, the recommended rates should be designed to produce of revenue \$130,799 for the water system.

As discussed in Issue 8, staff recommends that the Utility's current rate structure which includes a quarterly BFC be changed to a three-tier inclining block rate structure with usage blocks set at: a) 0-5 kgal; b) 5-10 kgal; c) usage in excess of 10 kgal, with appropriate usage block rate factors of 1.0, 1.5, 2.0 respectively for water system's residential class for the water system's residential class. The appropriate rate structure for the water system's nonresidential class is a traditional BFC/uniform gallonage charge. The water system's BFC cost recovery should be set at 35 percent.

The approved rates should be effective for service rendered on or after stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved rates should not be implemented until staff has approved the proposed customer notice and the notice has been received by the customers. The Utility should provide proof of the date notice was given no less than 10 days after the date of the notice.

If the effective date of the new rates falls within a regular billing cycle, the initial bills at the new rate may be prorated. The old charge shall be prorated based on the number of days in the billing cycle before the effective date of the new rates. The new charge shall be prorated based on the number of days in the billing cycle on and after the effective date of the new rates. In no event shall the rates be effective for service rendered prior to the stamped approval date.

Based on the foregoing, the appropriate rates for monthly service for the water is shown on Schedules 4-A.

Issue 12: Should the Commission approve proforma plant and expenses for the Utility, and if so, what is the appropriate return on equity, overall rate of return, revenue requirement and when should the resulting rates be implemented?

Recommendation: Yes. The Commission should approve a Phase II revenue requirement associated with proforma plant improvements. The Utility’s revenue requirement should be \$166,672. Neighborhood should complete the proforma improvements within no more than 12 months of the issuance of the consummating order. The Utility should be allowed to implement the resulting rates once the proforma improvements have been completed and verified by staff. However, Neighborhood should not implement the revised rates until it has submitted a revised tariff and a proposed customer notice reflecting the Commission-approved rates. The rates should be effective for service rendered on or after the stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. The rates should not be implemented until notice has been received by the customers. Neighborhood should provide proof of the date notice was given within 10 days after the date of the notice. If the Utility encounters any unforeseen events that will impede the completion of the proforma improvements, the Utility should immediately notify the Commission immediately. (Brown)

Staff Analysis: The Utility requested additional proforma plant and expenses that it intends to complete. The following is a chart summarizing the proforma item, the cost, and staff’s recommended treatment:

<u>Proforma</u>	<u>Staff Recommended</u>
Meter replacement program – 40 meters per year	\$5,255
Office Staff	\$20,000
Painting and Repairing of Facilities – 1/5 amortization of total	\$3,467
Total	\$28,722

Meter Replacement Program. To replace aging meters, the Utility intends to replace 40 meters per year at a cost of \$5,255 annually. This proforma improvement will enhance customer billing accuracy.

Part-time Employee. The Utility intends to hire additional office staffing to aid in increased customer billing as a result of going from quarterly billing to monthly billing. This \$20,000 proforma expense will also help improve on customer service by providing reasonable access to the Utility during normal business hours. To reflect the appropriate payroll taxes that will result from the hire of an additional employee, the staff has adjusted TOTI by \$1,530 to account for this future employee.

Painting of Facilities. To eliminate a rusting and corrosion situation on structures and equipment at the water treatment plant, the Utility requested \$17,334.20 for painting and related improvements. This proforma improvement will help extend the operating life of these structures and is amortized over five years. The amount per year is \$3,467(\$17,334.20/5).

Staff believes Neighborhood's proposed proforma improvement items are reasonable and prudent because they will allow the Utility to provide improved quality of service. With the proforma items, Neighborhood's appropriate return on equity should be 11.30 percent with a range of 10.30 percent to 12.30 percent. The appropriate overall rate of return is 9.65 percent. The Utility's revenue requirement should be \$166,672. Neighborhood should complete the proforma improvements within no more than 12 months of the issuance of the consummating order. Phase II rate base is shown on Schedule Nos. 5A and 5B. The capital structure for Phase II is shown on Schedule No. 6. Finally, the revenue requirement is shown on Schedule Nos. 7A and 7B. The resulting rates are on the chart on page 24.

The Utility should be allowed to implement the above rates once all proforma plant items and expense have been completed and verified. Once verified, the rates should be effective for service rendered on or after the stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. The rates should not be implemented until notice has been received by the customers. Neighborhood should provide proof of the date notice was given within ten days after the date of the notice. If the Utility encounters any unforeseen events that will impede the completion of the proforma improvements, the Utility should immediately notify the Commission.

NEIGHBORHOOD UTILITIES, INC.			SCHEDULE NO. 4-A	
TEST YEAR ENDING 12/31/08			DOCKET NO. 090060-WU	
MONTHLY WATER RATES – PHASE II				
	UTILITY'S EXISTING RATES *	UTILITY'S MONTHLY RATES**	STAFF RECOMMENDED RATES	4 YEAR RATE REDUCTION
-				
-				
<u>Residential Service</u>				
Base Facility Charge All Meter Sizes				
5/8"X3/4"	\$28.45	\$9.48	\$9.45	\$0.04
3/4"	\$0.00	\$0.00	\$14.18	\$0.07
1"	\$49.70	\$16.57	\$23.63	\$0.11
1-1/2"	\$87.09	\$29.03	\$47.25	\$0.22
2"	\$152.51	\$50.84	\$75.60	\$0.36
3"	\$266.79	\$88.93	\$151.20	\$0.72
4"	\$466.89	\$155.63	\$236.25	\$1.12
6"	\$816.97	\$272.32	\$472.50	\$2.24
<u>Residential Gallonage Charge</u>				
Per 1,000 Gallons, 0-5 kgal	\$1.14		\$4.18	\$0.02
Per 1,000 Gallons, 5-10 kgal			\$6.27	
Per 1,000 Gallons, 10+ kgal			\$8.36	
<u>General Service</u>				
Base Facility Charge by Meter Size:				
5/8"X3/4"	\$28.45	\$9.48	\$9.45	\$0.04
3/4"	\$0.00	\$0.00	\$14.18	\$0.07
1"	\$49.70	\$16.57	\$23.63	\$0.11
1-1/2"	\$87.09	\$29.03	\$47.25	\$0.22
2"	\$152.51	\$50.84	\$75.60	\$0.36
3"	\$266.79	\$88.93	\$151.20	\$0.72
4"	\$466.89	\$155.63	\$236.25	\$1.12
6"	\$816.97	\$272.32	\$472.50	\$2.24
Gallonage Charge (all gallons)	\$1.14		\$4.62	\$0.02
Per 1,000 Gallons				
* BCF Charge is billed quarterly				
** For comparison the Utility's quarterly rate converted to monthly				

Docket No. 090060-WU

Date: October 29, 2009

Issue 13: Should this docket be closed?

Recommendation: Yes, upon expiration of the protest period, if a timely protest is not received from a substantially affected person, this docket should be closed. (Brubaker)

Staff Analysis: If no protest is received within twenty-one days of the issue date of the Commission Order, no further action will be required and this docket should be closed.

WATER

	Current Rates		Current rates converted to Monthly	Staff Recommended	Alternate 1	Alternate 2
				BFC = 35% 3-Tier Inclining Block 0-5 Kgal; 5-10 Kgal; 10+Kgal 2nd Tier Rate Factor =1.50 3 rd Tier Rate Factor = 2.00	BFC = 40% 3-Tier Inclining Block 0-5 Kgal; 5-10 Kgal; 10+Kgal 2nd Tier Rate Factor =1.50 3 rd Tier Rate Factor = 2.00	BFC =40% 3-Tier Inclining Block 0-6 Kgal; 6-12 Kgal; 12+ Kgal 2nd Tier Rate Factor =1.50 3 rd Tier Rate Factor = 2.00
Quarterly BFC	\$28.45	BFC	\$9.48	\$7.59	\$8.69	\$8.69
Per kgal	\$1.14	Per Kgal	\$1.14	0-5 Kgal \$2.25 5-10 Kgal \$3.37 10+ \$4.49	0-5 Kgal \$2.01 5-10 Kgal \$3.02 10+ \$4.02	0-6 Kgal \$2.10 6-12 Kgal \$3.15 12+ \$4.20
	<u>Typical Quarterly Bills</u>		<u>Typical Monthly Bills</u>	<u>Typical Monthly Bills</u>	<u>Typical Monthly Bills</u>	<u>Typical Monthly Bills</u>
0 kgal	\$28.45	0 kgal	\$9.48	\$7.59	\$8.69	\$8.69
3 kgals	\$38.71	3 kgals	\$12.90	\$14.34	\$14.72	\$14.99
5 kgals	\$45.55	5 kgals	\$15.18	\$18.84	\$18.74	\$19.19
10 kgals	\$62.65	10 kgals	\$20.88	\$35.69	\$33.84	\$33.89
15 kgals	\$79.75	15 kgals	\$26.58	\$58.14	\$53.94	\$52.79

Note: All recommended and alternative rates are based on rate factors of 1.0, 1.50 and 2.00

**NEIGHBORHOOD UTILITIES INC.,
TEST YEAR ENDING 12/31/08
SCHEDULE OF RATE BASE – PHASE I**

**SCHEDULE NO. 1-A
DOCKET NO. 090060-WU**

DESCRIPTION	BALANCE PER UTILITY	STAFF ADJUST. TO UTIL. BAL.	BALANCE PER STAFF
1. UTILITY PLANT IN SERVICE	\$617,959	\$47,927	\$665,886
2. LAND & LAND RIGHTS	\$1,000	\$0	\$1,000
3. NON-USED AND USEFUL COMPONENTS	\$0	\$0	\$0
4. CIAC	(\$786,578)	\$0	(\$786,578)
5. ACCUMULATED DEPRECIATION	(\$381,217)	\$88,397	(\$292,820)
6. ACCUM. AMORTIZATION OF CIAC	\$462,313	(\$63,665)	\$398,648
7. WORKING CAPITAL ALLOWANCE	<u>\$0</u>	<u>\$14,523</u>	<u>\$14,523</u>
8. WATER RATE BASE	<u>(\$86,523)</u>	<u>\$87,183</u>	<u>\$660</u>

NEIGHBORHOOD UTILITIES, INC.
TEST YEAR ENDING 12/31/08
ADJUSTMENTS TO RATE BASE – PHASE I

SCHEDULE NO. 1-B
DOCKET NO. 090060-WU

		<u>WATER</u>
<u>UTILITY PLANT IN SERVICE</u>		
1.	To reflect plant balance as per utility as of as 12/31/2008	\$0
2.	To reclassify plant addition from Acct No. 636	4,467
3.	To reclassify plant addition from Acct No. 720	0
4.	To reclassify plant addition from Acct No. 675	1,717
5.	To reclassify plant addition from Acct No. 618	854
6.	To reclassify plant addition from Acct No. 620	2,522
7.	To reflect invoices that were not recorded	18,130
8.	To reflect the retirement of turbine motor	(3,350)
9.	To reflect proforma hydro tank replacement	28,317
10.	To reflect averaging adjustment	(90)
11.	To reflect non supported invoices	(4,640)
	Total	<u>\$47,927</u>
<u>LAND</u>		
1.	To reflect the appropriate land purchase price	<u>\$0</u>
<u>CIAC</u>		
1.	To reflect CIAC balance per utility as of 12/31/2008	\$0
2.	To reflect an averaging adjustment	0
	Total	<u>\$0</u>
		<u>WATER</u>
<u>ACCUMULATED DEPRECIATION</u>		
1.	To reflect accumulated depreciation per Rule 25-30.0140	\$81,377
2.	To reflect an averaging adjustment	7,020
	Total	<u>\$88,397</u>
<u>ACCUMULATED AMORTIZATION OF CIAC</u>		
1.	To reflect the appropriate amort of CIAC per utility as of 12/31/2008	(\$53,539)
2.	To reflect an averaging adjustment	(10,126)
	Total	<u>(\$63,665)</u>
<u>WORKING CAPITAL ALLOWANCE</u>		
1.	To reflect 1/8 of test year O & M expenses.	<u>\$14,523</u>

NEIGHBORHOOD UTILITIES, INC.
 TEST YEAR ENDING 12/31/08
 SCHEDULE OF CAPITAL STRUCTURE
 PHASE I

SCHEDULE NO. 2
 DOCKET NO. 090060-WU

CAPITAL COMPONENT	PER UTILITY	SPECIFIC ADJUSTMENTS	BALANCE BEFORE PRO RATA ADJUSTMENTS	PRO RATA ADJUSTMENTS	BALANCE PER STAFF	PERCENT OF TOTAL	COST	WEIGHTED COST
1. COMMON STOCK	\$0	\$0	\$0					
2. RETAINED EARNINGS	\$0	\$0	\$0					
3. PAID IN CAPITAL	\$0	\$0	\$0					
4. TREASURY STOCK	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>					
5. TOTAL COMMON EQUITY	\$0	\$0	\$0	\$0	\$0	0.00%	0.00%	0.00%
6. LONG TERM DEBT	\$94,761	\$0	\$94,761	\$0	\$94,761	91.21%	10.00%	9.12%
7. LONG TERM DEBT	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	\$0	\$0	<u>0.00%</u>	0.00%	0.00%
TOTAL LONG TERM DEBT	\$94,761	\$0	\$94,761	\$0	\$94,761	91.21%		
8. CUSTOMER DEPOSITS	<u>\$9,127</u>	<u>\$0</u>	<u>\$9,127</u>	<u>\$0</u>	<u>\$9,127</u>	<u>8.79%</u>	6.00%	<u>0.53%</u>
9. TOTAL	<u>\$103,888</u>	<u>\$0</u>	<u>\$103,888</u>	<u>\$0</u>	<u>\$103,888</u>	<u>100.00%</u>		<u>9.65%</u>
RANGE OF REASONABLENESS						<u>LOW</u>	<u>HIGH</u>	
RETURN ON EQUITY						<u>10.30%</u>	<u>12.30%</u>	
OVERALL RATE OF RETURN						<u>9.65%</u>	<u>9.65%</u>	

NEIGHBORHOOD UTILITIES, INC. TEST YEAR ENDING 12/31/08 SCHEDULE OF WATER OPERATING INCOME PHASE I				SCHEDULE NO. 3-A DOCKET NO. 090060-WU	
	TEST YEAR PER UTILITY	STAFF ADJUSTMENTS	STAFF ADJUSTED TEST YEAR	ADJUST. FOR INCREASE	REVENUE REQUIREMENT
1. OPERATING REVENUES	<u>\$88,344</u>	<u>\$1,331</u>	<u>\$89,675</u>	<u>\$42,312</u> 47.18%	<u>\$131,987</u>
OPERATING EXPENSES:					
2. OPERATION & MAINTENANCE	123,516	(7,329)	116,187	0	116,187
3. DEPRECIATION	17,417	(2,839)	14,578	0	14,578
4. AMORTIZATION OF CIAC	(31,463)	11,563	(19,900)	0	(19,900)
5. TAXES OTHER THAN INCOME	18,373	(10,773)	7,600	1,904	9,504
6. INCOME TAXES	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>0</u>	\$0
7. TOTAL OPERATING EXPENSES	<u>\$127,843</u>	<u>(\$9,378)</u>	<u>\$118,465</u>	<u>\$1,904</u>	<u>\$120,369</u>
8. OPERATING MARGIN	<u>(\$39,499)</u>		<u>(\$28,790)</u>		<u>\$11,619</u>
9. WATER RATE BASE	<u>(\$86,523)</u>		<u>\$660</u>		<u>\$660</u>
10. OPERATING RATIO					<u>10.00%</u>

NEIGHBORHOOD UTILITIES, INC.
 TEST YEAR ENDING 12/31/08
 ADJUSTMENTS TO OPERATING INCOME - PHASE I

SCHEDULE NO. 3-B
 DOCKET NO. 090060-WU
 PAGE 1 OF 2

		<u>WATER</u>
OPERATING REVENUES		
1.	To reflect the appropriate test year revenues	\$1,331
	Subtotal	<u>\$1,331</u>
OPERATION AND MAINTENANCE EXPENSES		
1.	Salaries and Wages - Employees (601)	
	a. Not used	0
	Subtotal	<u>\$0</u>
2.	Salaries and Wages - Officers, Directors and Major Stockholders (603)	
	a. Not used	<u>\$0</u>
	Subtotal	<u>\$0</u>
3.	Purchased Power (615)	
	a. Not used	\$0
	Subtotal	<u>\$0</u>
4.	Chemicals (618)	
	a. Not used	\$0
	Subtotal	<u>\$0</u>
5.	Materials and Supplies (620)	
	a. To increase for mailing of bills to go from quarterly to monthly	<u>3,440</u>
	Subtotal	<u>\$3,440</u>
6.	Contractual Services - Professional (631)	
	a. Not used	\$0
	Subtotal	<u>\$0</u>
7.	Contractual Services - Testing (635)	
	a. To amortize tests required by DEP every three or more years	<u>785</u>
	Subtotal	<u>\$785</u>
8.	Contractual Services - Other (636)	
	a. Not used	\$0
	Subtotal	<u>\$0</u>
9.	Rents (640)	
	a. To remove parking fees associated with weekend parking	<u>(\$257)</u>
	Subtotal	<u>(\$257)</u>
10.	Transportation Expense (650)	
	b. Not used	0
	Subtotal	<u>\$0</u>
11.	Insurance Expense (655)	
	a. To remove non-utility life insurance coverage	(\$3,346)
	Subtotal	<u>(\$3,346)</u>
(O & M EXPENSES CONTINUED ON NEXT PAGE)		

NEIGHBORHOOD UTILITIES, INC.		SCHEDULE NO. 3-B
TEST YEAR ENDING 12/31/08		DOCKET NO. 090060-WU
ADJUSTMENTS TO OPERATING INCOME – PHASE I		PAGE 2 OF 2
12	Regulatory Commission Expense (665)	
	a. To adjust amount of consulting fee that should be amortized over four years	<u>(900)</u>
	b. To adjust amount to include filing fee that will be amortized over four years	<u>250</u>
	c. To adjust amount to include noticing expenses that will be amortized over four years	<u>214</u>
	Subtotal	<u>(\$436)</u>
13	Miscellaneous Expense (675)	
	a. To remove utility's finance charges	(2,950)
	b. To remove utility's late payments	(489)
	c. To remove utility's charge backs due to payments declared NSF	(2,256)
	d. To remove utility's returned deposited items	(180)
	e. To remove non utility Comcast Service Bundle - removed cable	(669)
	f. To remove non utility newspaper - Florida Time	(200)
	g. To remove non utility newspaper - Morris Paper	(16)
	h. To remove non utility dental visits - Scott Watson	(95)
	i. To remove non utility vitamin purchase - Swanson Health	(35)
1	j. To remove non utility Sunbiz payment - for Colt Development	(150)
	k. To remove non utility - Swamp Holly Shop - retail store	(266)
	l. To remove non utility - S&K Internet	(205)
	m. To remove no utility - late fee - Verizon	(5)
	Subtotal	<u>(\$7,516)</u>
2	TOTAL OPERATION & MAINTENANCE ADJUSTMENTS	<u>(\$7,329)</u>
	DEPRECIATION EXPENSE	
3	To reflect the adjustment due to rate changes over the years.	(3,399)
	To reflect the adjustment due to changes in pre 2008 additions and retirements	<u>(383)</u>
	To reflect the adjustment due to changes in post 2008 additions and retirements	<u>943</u>
	Subtotal	<u>(\$2,839)</u>
	AMORTIZATION of CIAC	
	To reflect the adjustment due to rate changes over the years.	<u>\$11,563</u>
	Subtotal	<u>\$11,563</u>
	TAXES OTHER THAN INCOME	
	To reflect the appropriate RAFs for the test year revenues per utility	\$3,975
	To reflect the appropriate RAFs for the test year revenues per audit	\$60
	To reflect the appropriate property taxes - Not used	0
	To reflect the appropriate payroll taxes	0
	To remove right of way and public service utility tax	<u>(14,808)</u>
		<u>(\$10,773)</u>
	<u>INCOME TAX</u>	
	Income Tax Per Staff	<u>\$0</u>

NEIGHBORHOOD UTILITIES, INC.		SCHEDULE NO: 3-C	
TEST YEAR ENDING 12/31/08		DOCKET NO. 090060-WU	
ANALYSIS OF WATER OPERATION AND MAINTENANCE EXPENSE – PHASE I			
	TOTAL PER PER UTILITY	STAFF PER ADJUST.	TOTAL PER PER STAFF
(601) SALARIES AND WAGES - EMPLOYEES	\$0	0	\$0
(603) SALARIES AND WAGES - OFFICERS	24,000	0	24,000
(604) EMPLOYEE PENSIONS AND BENEFITS	0	0	0
(610) PURCHASED WATER	0	0	0
(615) PURCHASED POWER	7,671	0	7,671
(616) FUEL FOR POWER PRODUCTION	0	0	0
(618) CHEMICALS	3,423	0	3,423
(620) MATERIALS AND SUPPLIES	3,711	3,440	7,151
(630) CONTRACTUAL SERVICES - BILLING	0	0	0
(631) CONTRACTUAL SERVICES - PROFESSIONAL	5,284	0	5,284
(635) CONTRACTUAL SERVICES - TESTING	2,973	785	3,758
(636) CONTRACTUAL SERVICES - OTHER	34,015	0	34,015
(640) RENTS	8,479	(257)	8,222
(650) TRANSPORTATION EXPENSE	1,826	0	1,826
(655) INSURANCE EXPENSE	5,349	(3,346)	2,003
(665) REGULATORY COMMISSION EXPENSE	1,200	(436)	764
(670) BAD DEBT EXPENSE	0	0	0
(675) MISCELLANEOUS EXPENSES	<u>25,585</u>	<u>(7,516)</u>	<u>18,069</u>
	\$123,516	(\$7,329)	\$116,187

NEIGHBORHOOD UTILITIES, INC.			SCHEDULE NO. 4	
TEST YEAR ENDING 12/31/08			DOCKET NO. 090060-WU	
MONTHLY WATER RATES – PHASE I				
	UTILITY'S EXISTING RATES *	UTILITY'S MONTHLY RATES**	STAFF RECOMMENDED RATES	4 YEAR RATE REDUCTION
<u>Residential Service</u>				
Base Facility Charge All Meter Sizes				
5/8"X3/4"	\$28.45	\$9.48	\$7.59	\$0.05
3/4"	\$0.00	\$0.00	\$11.39	\$0.07
1"	\$49.70	\$16.57	\$18.98	\$0.11
1-1/2"	\$87.09	\$29.03	\$37.95	\$0.23
2"	\$152.51	\$50.84	\$60.72	\$0.36
3"	\$266.79	\$88.93	\$121.44	\$0.73
4"	\$466.89	\$155.63	\$189.75	\$1.14
6"	\$816.97	\$272.32	\$379.50	\$2.27
<u>Residential Gallonage Charge</u>				
Per 1,000 Gallons, 0-5 kgal	\$1.14	\$1.14	\$2.25	\$0.01
Per 1,000 Gallons, 5-10 kgal			\$3.37	
Per 1,000 Gallons, 10 + kgal			\$4.49	
<u>General Service</u>				
Base Facility Charge by Meter Size:				
5/8"X3/4"	\$28.45	\$9.48	\$7.59	\$0.05
3/4"	\$0.00	\$0.00	\$11.39	\$0.07
1"	\$49.70	\$16.57	\$18.98	\$0.11
1-1/2"	\$87.09	\$29.03	\$37.95	\$0.23
2"	\$152.51	\$50.84	\$60.72	\$0.36
3"	\$266.79	\$88.93	\$121.44	\$0.73
4"	\$466.89	\$155.63	\$189.75	\$1.14
6"	\$816.97	\$272.32	\$379.50	\$2.27
Gallonage Charge (all gallons)	\$1.14	\$1.14	\$2.77	\$0.02
Per 1,000 Gallons				
* BCF Charge is billed quarterly				
** For comparison the Utility's quarterly rate converted to monthly				

NEIGHBORHOOD UTILITIES, INC..
 TEST YEAR ENDING 12/31/08
 SCHEDULE OF RATE BASE – PHASE II

SCHEDULE NO. 5-A
 DOCKET NO. 090060-WU

DESCRIPTION	BALANCE PER UTILITY	STAFF ADJUST. TO UTIL. BAL.	BALANCE PER STAFF
1. UTILITY PLANT IN SERVICE	\$617,959	\$47,927	\$665,886
2. LAND & LAND RIGHTS	\$1,000	\$0	\$1,000
3. NON-USED AND USEFUL COMPONENTS	\$0	\$0	\$0
4. CIAC	(\$786,578)	\$0	(\$786,578)
5. ACCUMULATED DEPRECIATION	(\$381,217)	\$88,397	(\$292,820)
6. ACCUM. AMORTIZATION OF CIAC	\$462,313	(\$63,665)	\$398,648
7. WORKING CAPITAL ALLOWANCE	<u>\$0</u>	<u>\$18,114</u>	<u>\$18,114</u>
8. WATER RATE BASE	<u>(\$86,523)</u>	<u>\$90,773</u>	<u>\$4,250</u>

NEIGHBORHOOD UTILITIES, INC.

SCHEDULE NO. 5-B

TEST YEAR ENDING 12/31/08

DOCKET NO. 090060-WU

ADJUSTMENTS TO RATE BASE - PHASE II

	<u>WATER</u>
<u>UTILITY PLANT IN SERVICE</u>	
1. To reflect plant balance as per utility as of as 12/31/2008	\$0
2. To reclassify plant addition from Acct No. 636	4,467
3. To reclassify plant addition from Acct No. 720	0
4. To reclassify plant addition from Acct No. 675	1,717
5. To reclassify plant addition from Acct No. 618	854
6. To reclassify plant addition from Acct No. 620	2,522
7. To reflect invoices that were not recorded	18,130
8. To reflect the retirement of turbine motor	(3,350)
9. To reflect proforma hydro tank replacement	28,317
10. To reflect averaging adjustment	(90)
11. To reflect non supported invoices	(4,640)
Total	<u>\$47,927</u>
<u>LAND</u>	
1. To reflect the appropriate land purchase price	<u>\$0</u>
<u>CIAC</u>	
1. To reflect CIAC balance per utility as of 12/31/2008	\$0
2. To reflect an averaging adjustment	0
Total	<u>\$0</u>
<u>WATER</u>	
<u>ACCUMULATED DEPRECIATION</u>	
1. To reflect accumulated depreciation per Rule 25-30.0140	\$81,377
2. To reflect an averaging adjustment	7,020
Total	<u>\$88,397</u>
<u>ACCUMULATED AMORTIZATION OF CIAC</u>	
1. To reflect the appropriate amort of CIAC per utility as of 12/31/2008	(\$53,539)
2. To reflect an averaging adjustment	(10,126)
Total	<u>(\$63,665)</u>
<u>WORKING CAPITAL ALLOWANCE</u>	
1. To reflect 1/8 of test year O & M expenses.	<u>\$18,114</u>

NEIGHBORHOOD UTILITIES, INC.
 TEST YEAR ENDING 12/31/08
 SCHEDULE OF CAPITAL STRUCTURE
 PHASE II

SCHEDULE NO. 6
 DOCKET NO. 090060-WU

CAPITAL COMPONENT	PER UTILITY	SPECIFIC ADJUSTMENTS	BALANCE BEFORE PRO RATA ADJUSTMENTS	PRO RATA ADJUSTMENTS	BALANCE PER STAFF	PERCENT OF TOTAL	COST	WEIGHTED COST
1. COMMON STOCK	\$0	\$0	\$0					
2. RETAINED EARNINGS	\$0	\$0	\$0					
3. PAID IN CAPITAL	\$0	\$0	\$0					
4. TREASURY STOCK	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>					
5. TOTAL COMMON EQUITY	\$0	\$0	\$0	\$0	\$0	0.00%	0.00%	0.00%
6. LONG TERM DEBT	\$94,761	\$0	\$94,761	\$0	\$94,761	91.21%	10.00%	9.12%
7. LONG TERM DEBT	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	\$0	\$0	<u>0.00%</u>	0.00%	0.00%
TOTAL LONG TERM DEBT	\$94,761	\$0	\$94,761	\$0	\$94,761	91.21%		
8. CUSTOMER DEPOSITS	<u>\$9,127</u>	<u>\$0</u>	<u>\$9,127</u>	<u>\$0</u>	<u>\$9,127</u>	<u>8.79%</u>	6.00%	<u>0.53%</u>
9. TOTAL	<u>\$103,888</u>	<u>\$0</u>	<u>\$103,888</u>	<u>\$0</u>	<u>\$103,888</u>	<u>100.00%</u>		<u>9.65%</u>
RANGE OF REASONABLENESS								
RETURN ON EQUITY							<u>LOW</u>	<u>HIGH</u>
OVERALL RATE OF RETURN							<u>10.30%</u>	<u>12.30%</u>
							<u>9.65%</u>	<u>9.65%</u>

NEIGHBORHOOD UTILITIES, INC.			SCHEDULE NO. 7-A		
TEST YEAR ENDING 12/31/08			DOCKET NO. 090060-WU		
SCHEDULE OF WATER OPERATING INCOME					
PHASE II					
	TEST YEAR PER UTILITY	STAFF ADJUSTMENTS	STAFF ADJUSTED TEST YEAR	ADJUST. FOR INCREASE	REVENUE REQUIREMENT
1. OPERATING REVENUES	<u>\$88,344</u>	<u>\$1,331</u>	<u>\$89,675</u>	<u>\$76,997</u> 85.86%	<u>\$166,672</u>
OPERATING EXPENSES:					
2. OPERATION & MAINTENANCE	123,516	21,393	144,909	0	144,909
3. DEPRECIATION	17,417	(2,839)	14,578	0	14,578
4. AMORTIZATION OF CIAC	(31,463)	11,563	(19,900)	0	(19,900)
5. TAXES OTHER THAN INCOME	18,373	(9,243)	9,130	3,465	12,595
6. INCOME TAXES	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>0</u>	\$0
7. TOTAL OPERATING EXPENSES	<u>\$127,843</u>	<u>\$20,874</u>	<u>\$148,717</u>	<u>\$3,465</u>	<u>\$152,181</u>
8. OPERATING MARGIN	<u>(\$39,499)</u>		<u>(\$59,042)</u>		<u>\$14,491</u>
9. WATER RATE BASE	<u>(\$86,523)</u>		<u>\$4,250</u>		<u>\$4,250</u>
10. OPERATING RATIO					<u>10.00%</u>

NEIGHBORHOOD UTILITIES, INC.
 TEST YEAR ENDING 12/31/08
 ADJUSTMENTS TO OPERATING INCOME – PHASE II

		<u>WATER</u>
OPERATING REVENUES		
1.	To reflect the appropriate test year revenues	\$1,331
	Subtotal	<u>\$1,331</u>
OPERATION AND MAINTENANCE EXPENSES		
1.	Salaries and Wages - Employees (601)	
	a. To reflect pro-forma addition of employee to assist the billing project to go from quarterly to monthly	<u>20,000</u>
	Subtotal	<u>\$20,000</u>
2.	Salaries and Wages - Officers, Directors and Major Stockholders (603)	
	a. Not used	<u>\$0</u>
	Subtotal	<u>\$0</u>
3.	Purchased Power (615)	
	a. Not used	\$0
	Subtotal	<u>\$0</u>
4.	Chemicals (618)	
	a. Not used	\$0
	Subtotal	<u>\$0</u>
5.	Materials and Supplies (620)	
	a. To increase for mailing of bills to go from quarterly to monthly	<u>3,440</u>
	Subtotal	<u>\$3,440</u>
6.	Contractual Services - Professional (631)	
	a. Not used	\$0
	Subtotal	<u>\$0</u>
7.	Contractual Services - Testing (635)	
	a. To amortize tests required by DEP every three or more years	<u>785</u>
	Subtotal	<u>\$785</u>
8.	Contractual Services - Other (636)	
	a. To reflect proforma meter replacement program – US Water	<u>\$5,255</u>
	Subtotal	<u>\$5,255</u>
9.	Rents (640)	
	a. To remove parking fees associated with weekend parking	<u>(\$257)</u>
	Subtotal	<u>(\$257)</u>
10.	Transportation Expense (650)	
	b. Not used	0
	Subtotal	<u>\$0</u>
11.	Insurance Expense (655)	
	a. To remove non-utility life insurance coverage	<u>(\$3,346)</u>
	Subtotal	<u>(\$3,346)</u>
 (O & M EXPENSES CONTINUED ON NEXT PAGE)		

NEIGHBORHOOD UTILITIES, INC.

SCHEDULE NO. 7-B

TEST YEAR ENDING 12/31/08

DOCKET NO. 090060-WU

ADJUSTMENTS TO OPERATING INCOME – PHASE II

PAGE 2 OF 2

12	Regulatory Commission Expense (665)	
	a. To adjust amount of consulting fee that should be amortized over four years	<u>(900)</u>
	b. To adjust amount to include filing fee that will be amortized over four years	<u>250</u>
	c. To adjust amount to include noticing expenses that will be amortized over four years	<u>214</u>
	Subtotal	<u>(\$436)</u>
13	Miscellaneous Expense (675)	
	a. To remove utility's finance charges	(2,950)
	b. To remove utility's late payments	(489)
	c. To remove utility's charge backs due to payments declared NSF	(2,256)
	d. To remove utility's returned deposited items	(180)
	e. To remove non utility Comcast Service Bundle - removed cable	(669)
	f. To remove non utility newspaper - Florida Time	(200)
	g. To remove non utility newspaper - Morris Paper	(16)
	h. To remove non utility dental visits - Scott Watson	(95)
	i. To remove non utility vitamin purchase - Swanson Health	(35)
1	j. To remove non utility Sunbiz payment - for Colt Development	(150)
	k. To remove non utility - Swamp Holly Shop - retail store	(266)
	l. To remove non utility - S&K Internet	(205)
	m. To remove no utility - late fee – Verizon	(5)
	n. To increase 1/ of painting of facilities	3,467
	Subtotal	<u>(\$4,049)</u>
2	TOTAL OPERATION & MAINTENANCE ADJUSTMENTS	<u>\$21,393</u>
	DEPRECIATION EXPENSE	
3	To reflect the adjustment due to rate changes over the years.	(3,399)
	To reflect the adjustment due to changes in pre 2008 additions and retirements	<u>(383)</u>
	To reflect the depreciation expense applicable to post 2008 additions and retirements	<u>943</u>
	Subtotal	<u>(\$2,839)</u>
	AMORTIZATION of CIAC	
	To reflect the adjustment due to rate changes over the years.	<u>\$11,563</u>
	Subtotal	<u>\$11,563</u>
	TAXES OTHER THAN INCOME	
	To reflect the appropriate RAFs for the test year revenues per utility	\$3,975
	To reflect the appropriate RAFs for the test year revenues per audit	\$60
	To reflect the appropriate property taxes - Not used	0
	To reflect the appropriate payroll taxes	1,530
	To remove right of way and public service utility tax	<u>(14,808)</u>
		<u>(\$9,243)</u>
	INCOME TAX	
	Income Tax Per Staff	<u>\$0</u>