Sunshine Water Services

200 Weathersfield Avenue
Altamonte Spring, Florida
United States 32714

T 866.842.8432

www.sunshinewater.com

FLORIDA PUBLIC SERVICE COMMISSION WORKSHOP

SUNSHINE WATER SERVICES POST-WORKSHOP REPLY COMMENTS

REGULATORY POLICIES IN THE WATER & WASTEWATER INDUSTRIES

I. Introduction

Sunshine Water Services ("SWS" or "Company") again appreciates the Florida Public Service Commission's ("Commission" or "PSC") creation of this workshop and the ability for key stakeholders on these topics to provide insight and feedback for the Commission's consideration. The Company has reviewed the initial comments of the parties to the workshop and has the following reply comments.

II. Response to Comments of Ni Florida, US Water Services Corporation, CSWR and NAWC

The Company generally agrees with the comments of Ni Florida, US Water Services Corporation, CSWR and NAWC ("Utility Commenters"). The Company adds the following comments and responses to those of the Utility Commenters:

A. Ni Florida correctly points out that several of the 24 states that allow an infrastructure mechanism for water and wastewater utilities have eligibility criteria for investments beyond distribution and collection system infrastructure. Allowing for a broader eligibility of infrastructure investment can incentivize replacement of aging assets across the system in a more holistic manner and further mitigate rate shock from capturing all investments in periodic base rate cases. As the eligibility of investment is broadened, any rate cap or threshold between rate cases should likewise be broadened.

B. While we agree with CSWR that acquisition adjustments can be authorized and recovered in a future rate case after transfer, the Commission should not preclude the possibility of an adjustment to current rates at the time of transfer. There are scenarios where incorporating the acquired system into an existing uniform tariff group's rates will provide administrative and operational benefits as well as provide a phase-in approach in rates. This flexibility can incentivize such large, established service providers to acquire small, troubled systems that would generate efficiencies not just for the benefit of acquired customers, but existing customers as well. In such scenarios, the Commission shall make clear to the acquiring utility that, while a change in rates may be applied at the time of transfer, the ultimate disposition of an acquisition adjustment will be completed in the following rate

case, and the rate adjustment at the time of transfer does not incorporate any recovery of the proposed acquisition adjustment.

III. Response to Comments of the Office of Public Counsel ("OPC")

A. Acquisition Adjustments (Rule 25-30.0371, Florida Administrative Code)

i. OPC is correct to say that rule changes for acquisition adjustments should focus on systems that are in need of improvement, but the Commission should not lose sight of the need to regulate in a way that supports continued supply of proper, reliable service, which entails identifying systems that do not have the managerial, technical, and financial resources to operate in this manner in the long term, but may not currently qualify as "troubled". It is just as important to be proactive in transferring potential troubled systems as it is to be reactive in facilitating transfers for systems that are already troubled.

ii. OPC's contention that, in approving an acquisition adjustment, "customers effectively pay twice for plant cost" is not in fact correct. First, if a utility were to acquire a system based on its original cost NBV, this would merely establish a rate base for the acquirer that mirrors the existing rate base of the seller - no added or duplicative cost is created. Second, the establishment of an acquisition adjustment does not duplicate the cost of the acquired plant, and the utility indeed bears the burden of establishing that the increase in asset value is reasonable and benefits are generated for customers from the acquisition.

iii. OPC's claim that customers pay for plant assets twice when the new owner makes capital improvements to replace fully depreciated or contributed infrastructure is also not well founded. If an asset is replaced when fully depreciated, the customers have received the benefit of that retired asset over its useful life, and a replacement asset is 1) warranted to continue provision of proper service, and 2) reasonable to include as an addition to rate base as it is now providing and will in the future provide benefit to customers.

iv. OPC's concern of rate base churn or swapping assets is straightforwardly mitigated by the PSC's authority to determine and carry out the process for authorizing acquisition adjustments, and the PSC can take all relevant evidence into consideration in each case. Note that the Utility Commenters consistently support the Commission having the final say on what is reasonable and in the public interest with regard to acquisition adjustments. In other words, if the PSC believes the acquiring utility is engaged in "swapping assets", the PSC has full authority to deny the acquisition adjustment.

v. None of the articulated considerations for positive acquisition adjustments in 25-30.0371(2) F.A.C. would be “extraordinary circumstances” when it comes to acquisition of a small, struggling utility by a more capable utility. This highlights the issue with the existing extraordinary circumstances language - it doesn't appear to reflect the fact that, by a capable utility acquiring a non-viable utility, the ability of the owner of the system to fulfill “a utility's fundamental obligation as a responsible utility manager" is enhanced immediately. Therefore, it meets the first two considerations posed by the Rule. Simply put, a sufficiently stable and experienced acquiring utility can be expected to improve a struggling system, even if the acquirer is merely "engaging in activities that a reasonable utility manager would be doing anyway", by improving compliance, quality and other key service requirements due to its available resources. It is also important to note a positive acquisition adjustment under the “extraordinary circumstances” provision has not been approved in approximately 35 years, which palpably represents the lack of incentive inherent in the policy.

vi. The OPC’s references to Section 367.071(5) and Rule 25-30.037(2)(o) are not sufficient to support OPC's conclusion that the acquisition adjustment "should be made at the time of transfer". The Statute says the "commission by order **may** establish" (emphasis added) rate base when a sale is approved, which allows for the flexibility to defer the decision until a later date when more information is known about the impact of the transfer to customers. The Rule requires the utility put forth a proposed rate base in its transfer application, but this does not require the Commission to rule on the final rate base for ratemaking in its order on the application. Instead, as noted above, the Commission **may** consider the facts brought by and presented in the application for transfer, provisionally approve the acquisition adjustment, and determine that the resolution of recovery of the acquisition adjustment should be made at a later date. This process is also supported by subsection (5) of the Rule. As NAWC noted in their comments, the Commission has later found the acquiring utility did not conform to the terms of the original approval of an acquisition adjustment and removed the amount from rate base in a subsequent case[1].

vii. OPC's expectation that "benefits should exist at the time of transfer" and "extraordinary circumstances will not magically appear six months, or a year, after the fact" undersells and mischaracterizes the practical considerations of acquiring a small, troubled system. While an acquiring utility will perform a level of due diligence before the agreement is signed and approval is sought, certain benefits may not be immediately realized and certain costs to remediate issues may not be known and measurable. For example, the acquiring utility may need to perform water quality or

[1] See page 5 of NAWC comments, filed March 1, 2023, concerning Central Florida Gas Co.

environmental testing, engineering analysis, leak detection or I&I investigation to establish the source and scope of an identified problem. This kind of work may not be able to be performed by the seller - due to cost or complexity - nor pre-acquisition by the acquiring utility - due to lack of ownership of the system and level of cost - and therefore remediation costs and benefits may not be fully estimable at the time of approval request. In addition, the criteria for consideration by the PSC in 25-30.071(2) implies that "anticipated" improvements can be cited in the application for transfer, but the satisfaction of those criteria will only and can only occur post-closing.

viii. Contrary to OPC's concern, customers will still know their rates at the time of transfer - there is not a ratemaking analysis performed in transfer proceedings, and the resolution of the acquisition adjustment would be done in a future rate case, if not in the transfer proceeding. Even if the acquiring utility requests the PSC adjust rates at the time of transfer due to the applicable circumstances, customers will have transparency and an ability to be heard in the transfer application proceeding.

ix. In OPC's comments, they do not address or provide practical solutions for the very real concern that struggling utilities are not incented to transfer their systems before or while experiencing service or financial issues. Allowing greater flexibility in the setting of acquisition adjustments will incentivize owners of non-viable systems to pursue a transfer, and for a reasonable transfer price to be attained. This is not only in the best interest of owners of the non-viable system, but it's also in the best interest of the customers of the non-viable system to be taken over by a capable utility operator for the long-term.

B. Allowed Return on Equity (ROE)

i. While tacitly acknowledging the issues water and wastewater utilities have in investing continually in their systems, the OPC position that avoiding ROE adders will avoid their import into other industries is readily addressable: the Commission can simply adopt a rule that is only applicable to water and wastewater. This would be consistent with the logic cited by OPC regarding application of *inclusio unis est exclusio alterius*.

ii. It should be noted that, in practice, the 24-month period beyond the test year ends for which capital may be recovered in a historic test year rate case is almost entirely completed before the utility is able to change its rates to recover the investment. In other words, the timing of the 24-month pro-forma period coincides with the time it takes to prepare and process a rate case, and thus a utility is not earning a return on investment 24 months in the future, as OPC' claims.

C. Used and Useful Adjustments (Rules 25-30.431, 25-30.432, and 25-30.4325, Florida Administrative Code)

i. OPC's comments do not consider the downstream implications of this policy as the utility system ages and is replaced prudently over time. The issue is not with existing small systems, it's with legacy developments that have had such an adjustment applied in the past, and the new owner is effectively punished for prudently investing in the system that it operates. In the workshop Mr. Rendell of US Water Services Corporation cited a particularly acute and egregious example of this scenario with regards to the Sunny Hills development. Therefore, the PSC should ensure that used and useful adjustments should be removed when the applicable assets are replaced over time to properly serve the customers who exist on the system, which would incentivize aging asset replacement by the current owner. Used and useful adjustments can also hinder the transfer of the system to a new, more capable owner. The resulting lower rate base value may create an unnecessary gap in negotiations between the seller and a willing buyer, limiting the ability or incentive of the owner to sell the system and increasing the risk of service issues overtime.

D. System Consolidation

i. OPC makes the misleading claim that the PSC has jurisdiction over a relatively small number of water and wastewater systems. In fact, the PSC has jurisdiction over 38 of Florida's 67 counties including many of the most populous counties in Florida such as Brevard, Palm Beach, Pinellas, Orange, Seminole, Marion, Duval, Leon and Escambia. Additionally, OPC seems to not consider that the unregulated water and wastewater systems in Florida are also potential sellers of their systems, and thus can be expected to be acquired over time to some degree by regulated utilities. See, for example, Order Nos. PSC-2001-1792-PAA-SU, PSC-2019-0071-PAA-SU, and PSC-.2022-0272-PAA-SU. In these cases, although the Commission does not <u>currently</u> regulate these systems, they must account for the potential to include them within their jurisdiction, and that doing so may bring with it the aforementioned economies of scale, efficiencies in operations, as well as consolidation considerations.

E. Cost Recovery Mechanisms

i. OPC makes the bold claim that, not only does the PSC not have statutory power to establish a water or wastewater infrastructure mechanism, but "(n)o reviewing court would be able to conclude that the Commission possessed a lawful basis or a factual basis in the record that would support

any explanation for changing Commission policy and Florida law by authorizing an ICRM." The OPC does not, however, adequately substantiate this claim, and we detail our disagreement below. In short, authorization of a capital recovery mechanism does not constitute "changing Commission policy or Florida law."

ii. As detailed in the rebuttal testimony of Jared Deason in Docket No. 20200139-WS, the PSC has broad ratemaking authority under 367.011(2) & (3), while 367.081 and 367.121(1)(a) Florida Statutes (F.S.) provides the necessary legal authority. In addition, 367.121(1)(d) F.S. specifically grants the FPSC the authority to require repairs and improvements if reasonably necessary to provide adequate and proper service (similar to 366.05(1)(a) F.S.) Therefore, the Company believes its proposed mechanism rule, included with its initial comments, is fully compliant with the relevant statutes and rules, and requires a hearing and commission approval for a mechanism to be utilized up to a revenue threshold. Indeed, 367.121(1)(d) F.S. is a specific grant of authority endowed by the legislature to the PSC, and therefore no override of this authority would transpire should a capital recovery mechanism be authorized. Therefore, the Commission does not require a proposal from a utility or a settlement in a proceeding to implement such a mechanism, as its statutory authority is sufficient to enact a Rule that authorizes an infrastructure mechanism.

iii. The Company's proposed rule was drafted with consideration of additional review time for the parties. In addition, multiple states with similar mechanisms function similarly, with a review focused on the details of the completed projects, and a window of review of approximately 30-60 days[2]. The Company's proposed rule allows for up to 120 days of review on a limited eligibility of capital investments. In addition, in these jurisdictions, the mechanism is initially approved in a rate case or separate filing, like a limited proceeding, which allows for hearings and customer comment, while establishing the cumulative revenue increase threshold, thereby streamlining the periodic rate update process.

iv. While the GRIP is a helpful corollary to a water/wastewater infrastructure mechanism, a key difference is that the Company would need to submit an initial application for the mechanism, including a three-year eligible capital plan, subject to hearing and eventual Commission-voted approval. The recovery of any capital investment that follows the initial application would be historic - that is, it would not be projected with a true up, as is GRIP, but based on actual investments, supported as being in-service and benefiting

[2] North Carolina Utility Commission Rule R7-39(f); 66 Pa.C.S.A. § 1357(a)(2); N.J. Admin. Code § 14:9-10.5(b); 170 IAC 6-1.1-7(a); 16 Tex. Admin. Code § 24.76(g)(4).

customers and signaled to the utility's stakeholders by a three-year capital plan (updated annually).

v. Contrary to OPC's contention, a benefit of post hoc support and rate implementation is to improve the quality of support, mitigate risk of imprudent investment and recovery, and therefore simplify the review process. OPC appears to agree that submitting invoices after the infrastructure is in-service and adjusting rates accordingly poses "little to no risk of disallowance".

vi. The mechanism would also incent utilities to invest in replacing aging infrastructure in a way that produces only incremental increases in rates, as opposed to the only other alternatives of lengthy and costly limited proceedings or periodic fully litigated rate cases where accumulated capital investment, large rate case expenses (and the associated regulatory recovery lag) is foisted on customer bills in a single increase.

vii. Also contrary to OPC's contention, there are safety and related analogues in the water and wastewater industry to those used to support implementing GRIP. In addition to those comments provided in Mr. Deason's rebuttal testimony cited above, the issues surrounding aging infrastructure are well documented. A 2011 Report from the American Society of Civil Engineers states that failures in drinking-water infrastructure can result in water disruptions, impediments to emergency response, and damage to other types of essential infrastructure. In extreme situations caused by failing infrastructure or drought, water shortages may result in unsanitary conditions, increasing the likelihood of public health issues. Additionally, the health effects associated with failing wastewater infrastructure can be severe as the instances of people getting infected from exposure to raw sewage is quite high. It is estimated that approximately 10 percent of those exposed to sewage get infected and frequently get hospitalized. Diseases caused by germs found in sewage spills include, but or not limited to, salmonellosis, shigellosis, diarrhea, trachoma, melioidosis, gastroenteritis, hepatitis A, giardiasis, dwarf tapeworm infection, threadworm infection, hookworm infection, and strongyloidiasis. All customers deserve a water and wastewater infrastructure system that meets modern safety standards, protects the environment, and enables continued prosperity. The costs of inaction are simply too high.

viii. Again, GRIP and other alternative mechanisms are helpful corollaries, but the Company's proposed rule is generally not reliant on the statutes, policies, or precedents upon which GRIP or the energy infrastructure clauses were implemented. Implementation of these energy utility mechanisms, however, highlights the service reliability and safety concerns regarding utility infrastructure and the need to facilitate investments to support long-term provision of proper service.

Sunshine Water Services appreciates the Commission's attention and consideration on these topics and looks forward to the next steps to this discussion on regulatory policies and frameworks in the State of Florida.