

FLORIDA PUBLIC SERVICE COMMISSION
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Tallahassee, Florida 32399-0850

MEMORANDUM

OCTOBER 22, 1998

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYO)
FROM: DIVISION OF WATER & WASTEWATER (GALLOWAY, MUNROE, GOLDEN)
DIVISION OF LEGAL SERVICES (FLEMING) *S. E. ...*
RE: DOCKET NO. 980445-WU - APPLICATION FOR A STAFF-ASSISTED
RATE CASE BY MORNINGSIDE UTILITY, INC.

COUNTY: OSCEOLA

AGENDA: NOVEMBER 3, 1998 - REGULAR AGENDA - PROPOSED AGENCY
ACTION, EXCEPT ISSUES 12, 13 and 15 - INTERESTED PERSONS
MAY PARTICIPATE

CRITICAL DATES: 15 MONTHS EFFECTIVE DATE - JUNE 30, 1999

SPECIAL INSTRUCTIONS: S:\PSC\WAW\WP\980445WU.RCM

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CASE BACKGROUND

Morningside Utility, Inc., (utility or Morningside) is a Class C water utility located in Osceola County. The utility provides water service to approximately 181 residential customers who utilize septic tanks for waste disposal. The Commission acquired jurisdiction over Osceola County on October 12, 1959. However, the Commission was unaware of the utility's existence until 1997.

On May 28, 1997, the utility filed its application for an original certificate pursuant to Section 367.045, Florida Statutes. The utility was granted operating Certificate No. 595-W, pursuant to Order No. PSC 97-1211-FOF-WU, issued October 7, 1997. Morningside was established in 1983 by Schoolfield Properties. The present owner, Mr. George Devillers, purchased the utility in 1988 from Schoolfield Properties.

On March 30, 1998, Morningside applied for this staff assisted rate case (SARC) pursuant to Section 367.0814, Florida Statutes. Staff determined eligibility for the utility's request by letter dated April 27, 1998. The utility paid its filing fee on May 26, 1998.

In its application, the utility requested an increase in water rates. Staff has audited the utility's records for compliance with Commission rules and orders and examined all components necessary for rate setting. The staff engineer has also conducted a field investigation, which included a visual inspection of the water plant and distribution system along with the service area. The utility's operating expenses, maps, files, and rate application were also reviewed to determine reasonableness of maintenance expenses, regulatory compliance, utility plant in service and quality of service.

On September 3, 1998, a customer meeting was held at the Elks Lodge (BPOE #1873) in Kissimmee, Florida. Even though the utility customers were properly noticed, none attended the meeting.

Staff selected a historical test year ended December 31, 1997, for this case. Staff's adjusted test year revenues are \$53,040 and adjusted expenses are \$64,743. This results in an adjusted net loss of \$11,703.

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QUALITY OF SERVICE

ISSUE 1: Is the quality of service provided by Morningside satisfactory?

RECOMMENDATION: Yes, the quality of service provided by Morningside to its customers is satisfactory. (MUNROE)

STAFF ANALYSIS: Staff's recommendation on the overall quality of service provided by the utility is derived from the evaluation of three separate components of water utility operations:

- (1) Quality of the utility's product (water and/or wastewater),
- (2) Operational condition of the utility's plant or facilities and
- (3) Customer satisfaction

Quality of Utility's Product

In order to assess the overall quality of service provided by the utility, the quality of the product (water and/or wastewater) must be evaluated. This evaluation consists of a review of the utility's current compliance with Department of Environmental Protection (DEP) and Health Department (water and wastewater) standards.

The ultimate concern of a water utility is the quality of piped water consumed by customers. The degree to which a utility is able to maintain satisfactory water quality may be reflected by its ability to meet DEP primary and secondary drinking water standards, as well as several unregulated standards set by the Environmental Protection Agency (EPA).

The primary drinking water standards include maximum contaminant levels (MCLs) for harmful contaminants. These MCLs are not to be exceeded, unless specified otherwise by a DEP variance or exemption. Some examples of primary contaminants are arsenic, lead, trihalomethanes, coliform bacteria and radium. Secondary drinking water standards generally contain MCLs which regulate the aesthetic qualities of the water, such as color, corrosivity, odor and hardness. Additionally, each utility must periodically test for several unregulated contaminants, which the EPA considers potentially harmful. These contaminants are still under investigation.

Morningside has no current DEP, Health Department or EPA violations with its water facilities.

Operational Condition of the Utility's Plant or Facilities

The operational conditions of the utility's treatment and distribution systems must also be evaluated to determine the overall quality of service provided by the utility. Evaluation of these systems includes a review of the utility's compliance with Department of Environmental Protection standards of operation as well as an analysis of proper system design. For example, among other standards of evaluation, water treatment plants and distribution systems are reviewed for compliance with permit standards and minimum operator requirements as well as standards regarding the location of wells with regard to potential sources of pollution. Wastewater treatment plants and collection systems are reviewed for compliance with permit standards, minimum operator requirements and lift station location and reliability among other standards. The utility is in compliance with all operational regulations. During a site inspection performed by a staff engineer the week of May 18, 1998, all facilities were found to be in proper maintenance and operational condition.

Customer Satisfaction

The final component of the overall quality of service which must be assessed is the level of customer satisfaction which results from the utility's relations with its customers. A qualitative evaluation of these relations includes a review of proper notification requirements between the utility and its customers as well as a review of action taken by the utility regarding customer complaints. For example, utility policies are reviewed in order to insure that customers have been properly notified of scheduled service interruptions.

A customer meeting was held at 6:30 P.M. on September 3, 1998. The location of the meeting was the Elks Lodge (BPOE #1873) in Kissimmee, Florida. Although all utility customers were properly noticed, none attended the meeting.

The utility has made a concerted effort to prevent quality of service problems and to promptly correct any complaints that arise. Staff recommends the Commission find the quality of service provided to its customers by Morningside to be satisfactory.

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RATE BASE

ISSUE 2: What are the appropriate used and useful percentages for the water treatment plant and distribution system?

RECOMMENDATION: The water treatment plant should be considered 80% used and useful. The distribution system should be considered 100% used and useful. Staff recommends no margin reserve be allowed.
(MUNROE)

STAFF ANALYSIS:

Water Treatment Plant - A strict used and useful calculation based on actual flow data and rated capacity would result in the water treatment plant being considered 17% used and useful. However, because of the small size of this utility and limits to potential growth, staff recommends an alternate method of calculating used and useful based on current customers versus customers in the service area at buildout. Using this method results in the water treatment plant being considered 80% used and useful, which is recommended.

Distribution System - The distribution system is built out, and is therefore considered 100% used and useful.

Staff's calculations of the appropriate used and useful percentages are shown on Attachment A.

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ISSUE 3: What is the utility's appropriate average amount of rate base for ratesetting purposes?

RECOMMENDATION: The appropriate average amount of test year rate base should be \$49,957. (GALLOWAY, MUNROE)

STAFF ANALYSIS: The appropriate components of the utility's rate base include utility plant in service (UPIS), land, non-used and useful plant, contributions-in-aid-of-construction (CIAC), accumulated depreciation, accumulated amortization of CIAC and working capital allowance.

In September of 1988, Mr. Devillers purchased Morningside Utility, Inc. from Schoolfield Properties. As part of the purchase agreement, Mr. Devillers paid \$100,000 for utility stock in addition to a land swap. Based on information from staff's audit, the purchase price of the stock exceeded the net book value of the acquired property. Staff analyzed whether an acquisition adjustment for this utility should be considered as an additional component of rate base. However, staff determined that an acquisition adjustment is not appropriate for this utility given that the 1988 purchase was accomplished through a stock transfer and not through purchase of assets.

Staff selected a test year ended December 31, 1997 for this rate case. Adjustments have been made to reflect the appropriate balances. A summary of each component and the adjustments follows:

Utility Plant in Service (UPIS) - The utility's books reflected a plant balance of \$0 at the beginning of the test year. Staff performed an original cost study to determine the appropriate balance for each of the various plant accounts. Staff's resulting adjustment is an increase to UPIS in the amount of \$140,220 to reflect the appropriate amount of depreciable plant in service. Of this amount, based on the original cost study, \$91,530 was associated with plant put into service in 1983, when the utility was established. Also, according to the original cost study, additions to utility plant were made in 1996 in the amount of \$44,776. Further, adjustments were made to reflect the misclassification of plant in various expense accounts during the test year in the amount of \$7,829. Therefore, UPIS has been increased by \$144,135 to reflect total plant. However, staff has reduced this balance by \$3,915 to reflect an averaging adjustment. The resulting UPIS is \$140,220.

Land - Staff included land value in the amount of \$38,000 in rate base. This amount is based on and supported by the Osceola County Property Appraiser's records along with the land value reported on the utility's 1997 tax return.

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Non-Used and Useful Plant - As discussed in Issue 2, the staff engineer has determined the used and useful percentage for all plant accounts. The non-used and useful percentages times the appropriate accounts reflect average non-used and useful plant of \$15,464. The average accumulated non-used and useful depreciation on this plant is \$5,732. The net non-used and useful plant is \$9,732. Net non-used and useful plant has a negative impact on rate base. Therefore, rate base has been decreased by \$9,732.

Contribution-in-Aid-of-Construction (CIAC) - By Order No. PSC-97-1211-FOF-WU, issued October 7, 1997, a system capacity charge of \$600 per connection was approved. Both the original owners and the present owners have charged this amount since the utility was established in 1983. While the utility recorded no CIAC on its books, detailed records exist which enabled staff to determine the appropriate amount of cash CIAC. Prior to purchase in 1988, system capacity charges in the amount of \$57,000 were collected. Since the 1988 purchase, system capacity charges in the amount of \$52,800 were collected. The resulting total CIAC balance is \$109,800. Staff decreased the total amount of CIAC to reflect an averaging adjustment of \$600. Therefore, the calculated average CIAC is \$109,200.

Accumulated Depreciation - The utility recorded no accumulated depreciation on its books. Staff has calculated the appropriate balances based on depreciation rates in conformity with Rule 25-30.140, Florida Administrative Code. The appropriate balance including the effect of an averaging adjustment is \$57,374.

Amortization of CIAC - Amortization of CIAC has been calculated consistent with staff's calculation of accumulated depreciation. The resulting accumulated amortization is \$40,697. An adjustment of this amount was made to reflect the appropriate average balance of amortization of CIAC through December 31, 1997.

Working Capital Allowance - Consistent with Rule 25-30.443, Florida Administrative Code, staff recommends that the one-eighth of operation and maintenance expense (O&M) formula approach be used for calculating working capital allowance. Applying that formula, staff recommends a working capital allowance of \$7,345 (based on O&M expense of \$58,757). Working capital has been increased by \$7,345 to reflect one-eighth of staff's recommended O&M expense.

Rate Base Summary - Applying all of the above adjustments results in a year end rate base of \$49,957.

Rate base is shown on Schedule No. 1 and adjustments are shown on Schedule No. 1-A.

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COST OF CAPITAL

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

RECOMMENDATION: The appropriate rate of return on equity is 8.89% with a range of 7.89% - 9.89% and the overall rate of return is 9.21% with a range of 8.48% - 9.94%. (GALLOWAY)

STAFF ANALYSIS: The utility's capital structure includes common equity of \$79,423 and long term debt in the amount of \$29,549, resulting in total capital of \$108,972. The utility's long term debt consists of two separate notes payable. The utility's books reflected a total notes payable balance of \$14,646 for the test year. Staff reduced the \$14,646 balance by \$1,466 to reflect a current loan balance of \$13,180. To reflect a second note which was not recorded on the utility's books, staff increased long term debt by \$16,369.

Using the current leverage formula approved by Order No. PSC-98-0903-FOF-WS, in Docket No. 980006-WS, the rate of return on equity is 8.89% with a range of 7.89% - 9.89%.

The utility's cost of debt is 10.25% for the \$13,180 loan and 10.00% for the \$16,369 loan. The utility's capital structure has been reconciled with staff's recommended rate base. Applying the cost times the pro rata share of each capital component results in an overall rate of return of 9.21% with a range of 8.48%-9.94%.

The return on equity and overall rate of return are shown on Schedule No. 2.

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NET OPERATING INCOME

ISSUE 5: What is the appropriate test year revenue?

RECOMMENDATION: The appropriate test year revenue is \$53,040.
(GALLOWAY)

STAFF ANALYSIS: During the test year the utility provided water service to approximately 181 residential customers. The utility recorded revenue of \$75,409. Per the audit, the utility recorded as revenue, CIAC in the amount of \$1,200; two loans in the amount of \$6,000 and \$15,000; and redeposits in the amount of \$540. These amounts which total \$22,740, have been removed from the utility's recorded revenue resulting in a balance of \$52,669.

As will be discussed further in Issue 12, the utility collected late payment charges in the amount of \$1,110. The utility's tariff does not authorize Morningside to charge late payment charges. However, staff believes that a late payment charge should be implemented for this utility in the amount of \$5.00. Staff believes the \$1,110 is miscellaneous revenue and has not made any adjustment to remove this amount from the utility's recorded revenue.

The selected test year for this rate case includes the 12 month period from January 1997 through December 1997. Annualized revenues have been calculated using test year number of bills and gallons of water billed times the existing rates. Annualized revenue is \$51,930. Staff has increased the annualized revenue amount by \$1,110 to reflect the late payment charges collected during the test year (miscellaneous revenues). The resulting test year revenue balance is \$53,040. Therefore, the total net adjustment for revenue is (\$22,369).

Test year revenues are shown on Schedule No. 3 and adjustments are shown on Schedule No. 3-A.

ISSUE 6: What is the appropriate amount of operating expenses?

RECOMMENDATION: The appropriate amount of operating expenses is \$65,512. (GALLOWAY, MUNROE)

STAFF ANALYSIS: The utility's recorded operating expense includes operation and maintenance expense, depreciation expense, amortization of CIAC, and taxes other than income. Adjustments have been made to reflect annual operating costs on a going forward basis. A summary of adjustments follows:

Operation and Maintenance Expenses

- 1) Salaries and Wages - Employees (601) - The utility recorded employee salaries and wages of \$10,900 during the test year. This amount represents a salary for the bookkeeping, billing, receptionist and clerical duties associated with the utility. Staff believes this amount is reasonable for the duties described.

No salary was recorded for the owner/operator. Staff is recommending an additional allowance to salaries and wages expense of \$19,760 for the duties associated with operating the utility. These duties include meter reading, grounds keeping, and general management along with labor for various repairs. The total adjustment for this expense is an increase in the amount of \$19,760.

- 2) Salaries and Wages - Officers (603) - The utility recorded a \$0 balance in this account. Staff has increased this account by \$3,640 to reflect salaries associated with the two officers of this utility.

As stated above, the owner/operator of this utility performs a variety of tasks necessary for the day-to-day operations of the utility. While a salary allowance has been recommended for the day-to-day utility operating tasks, no compensation has been allowed for the responsibilities associated with making broad overview of operation decisions, short and long-term financial decisions for the utility, as well as signing checks and other time-consuming tasks associated with an officer for a utility of this size. Therefore, staff is recommending a total allowance of \$3,640 for the President and the Vice President/Treasurer.

- 3) Purchased Power (615) - The utility recorded purchased power expense in the amount of \$2,274. Staff has reduced

this balance by \$91 to reflect the repression adjustment. The resulting balance for this expense is \$2,183.

- 4) Chemicals (618) - The utility recorded chemicals expense of \$2,400. An automatic chlorinator was misclassified to this expense account. Staff has removed \$660 which represents the cost of the automatic chlorinator and has included this cost as part of the utility's plant. Staff also adjusted this account to reflect a repression adjustment in the amount of \$70. The appropriate chemicals expense is \$1,670.
- 5) Materials and Supplies (620) - During the test year, the utility recorded \$9,475 for materials and supplies. Of this balance, \$5,499 was misclassified by the utility. Staff has reduced this account by \$115 which represents costs associated with Well #2; \$877 which represents costs associated with the generator; \$3,950 which represents costs associated with the electric panel; and \$557 which represents costs associated with the alarm. All of the misclassified items have been included in the appropriate plant accounts. The resulting balance for materials and supplies is \$3,976.
- 6) Contractual Services - Accounting (631) - As addressed in Issue 15, staff is recommending that the utility be required to maintain its books and records in conformity with the National Association of Regulatory Commission's (NARUC) Uniform System of Accounts (USOA) and reconcile its books with the Commission's order. The utility recorded a \$0 balance in this account. The utility provided an estimate in the amount of \$1,300 to convert the utility's accounting system to the NARUC's USOA. Staff believes this amount is reasonable and has included it in this account. Staff has increased this expense by \$260 ($\$1,300/5$) to reflect the accounting allowance of \$1,300 amortized over five years.
- 7) Contractual Services - Testing (635) - The utility recorded \$3,952 for testing expense. This expense has been decreased by \$1,670 to reflect a reclassification to plant, and by \$600 to reflect a reclassification to contractual services - repairs and maintenance (636). A schedule of the required water tests, frequency and costs follows:

cont.

| <u>Description</u> | <u>Frequency</u> | <u>Annual Cost</u> |
|----------------------|---------------------|--------------------|
| Microbiological | Monthly | \$ 215 |
| Primary Inorganics | 36 Months | 62 |
| Secondary Inorganics | 36 Months | 45 |
| Asbestos | 1/ 9 Years | 20 |
| Nitrate & Nitrite | 12 Months | 25 |
| Volatile Organics | 36 Months | 210 |
| Pesticides & PCB | 36 Months | 253 |
| Radionuclides | | |
| Group I | 36 Months | 100 |
| Group II | 36 Months | 220 |
| Unregulated Organics | 36 Months | 67 |
| Lead & Copper | Biannually | <u>465</u> |
| | Total Amount | \$1,682 |

- 8) Contractual Services - Repairs and Maintenance (636) - The utility recorded a \$0 balance in this account. Staff has increased this account by \$120 to reflect a reclassification from contractual services - testing. The utility misclassified a generator repair expense in the amount of \$600. Staff has amortized this amount over 5 years resulting in an adjustment of \$120.
- 9) Rents (640) - The utility recorded a \$0 balance in this account. To reflect an allowance for rental of office space, this account has been increased by \$1,200 (\$100.00/month).
- 10) Regulatory Commission Expense (665) - The utility paid a \$1,000 filing fee for this rate case. Pursuant to Section 367.0816, Florida Statute, this expense has been amortized over 4 years, which allows an annual expense of \$250. The utility did not record a regulatory commission expense. Therefore, this expense has been increased by \$250.

Rule 25-30.455(1), Florida Administrative Code, states that if a utility chooses to utilize the staff assisted rate case option, and employs outside experts to assist in developing information for staff or evaluating staff's schedules and conclusions, the prudent expense can be recovered through the rates developed by staff. The utility employed professional accounting services for rate case purposes. Staff believes that the expense is prudent and an additional allowance of \$197 (\$788/4) is recommended for this account. Therefore, the total adjustment for regulatory commission expense is \$447.

- 11) Miscellaneous Expense (675) - The utility recorded \$4,642 in this expense. Staff reduced this balance by \$750 to reflect a misclassified and incorrectly calculated regulatory assessment fee. Staff reclassified the appropriate regulatory assessment fee for 1997 as taxes other than income, shown on Schedule 3. The resulting balance for miscellaneous expenses is \$3,892.

Depreciation Expense - Test year depreciation expense has been calculated using the rates prescribed by Rule 25-30.140, Florida Administrative Code. Test year depreciation is \$6,645. Test year non-used and useful depreciation is \$897. Net depreciation is \$5,748. The utility recorded depreciation expense in the amount of \$12,845. This expense has been decreased by \$7,097 to reflect staff's calculated depreciation expense.

Amortization of CIAC - Amortization of CIAC has a negative impact on depreciation expense. The utility did not record an amortization expense. This expense has been adjusted by a negative \$5,034 to reflect staff's calculated test year amortization of CIAC expense.

Taxes Other Than Income - The utility recorded \$2,886 in this expense. This total includes \$278 for real estate tax, \$1,177 for tangible tax, \$1,080 for FICA and \$351 for other state sales and payroll taxes. The total does not include the appropriate regulatory assessment fee. The utility misclassified regulatory assessment fees in the amount of \$750 as miscellaneous expense. Staff has adjusted the total taxes other than income by \$750 to reclassify the misclassified amount. In addition, staff has increased this amount by \$1,637 to reflect the appropriate regulatory assessment fee on test year revenue. Therefore, the total adjustment to taxes other than income is an increase of \$2,387.

Increase in Operating Revenues and Expenses:

Operating Revenue - Revenue has been increased by \$17,073 to reflect the increase required to allow the utility to recover its expenses and earn the authorized return on its investment.

Taxes Other Than Income - This expense has been increased by \$768 to reflect regulatory assessment fees at 4.5% on the required increase in revenue.

The application of staff's recommended adjustments to the utility's recorded operating expenses results in staff's recommended operating expenses of \$65,512.

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Operating expenses are shown on Schedule No. 3 and adjustments are shown on Schedule No. 3-A.

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REVENUE REQUIREMENT

ISSUE 7: What is the appropriate revenue requirement for this utility?

RECOMMENDATION: The appropriate revenue requirement is \$70,113.
(GALLOWAY)

STAFF ANALYSIS: The utility should be allowed an annual increase in revenue of \$17,073 (32.19%). This increase will allow the utility the opportunity to recover its expenses and earn a 9.21% return on its investment. The calculations are as follows:

| | |
|-------------------------|----------------------------|
| Adjusted rate base | \$ 49,957 |
| Rate of return | <u>X .0921</u> |
| Return on investment | \$ 4,601 |
| plus | |
| Adjusted O&M expense | 58,757 |
| Depreciation expense | 5,748 |
| Amortization expense | (5,034) |
| Taxes other than income | <u>6,041</u> |
| Revenue requirement | \$ 70,113 |
| Test year revenue | <u>(53,040)</u> |
| Increase in revenue | \$ 17,073 |
| Percentage increase | 32.19% (\$17,073/\$53,040) |

The revenue requirement is shown on Schedule No. 3.

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RATES AND TARIFF CHARGES

ISSUE 8: What is the appropriate conservation rate structure for this utility?

RECOMMENDATION: The appropriate conservation rate structure for this utility is a continuation of the current base facility and gallonage charge rate structure.

STAFF ANALYSIS: The South Florida Water Management District (SFWMD) advised staff that this utility is not located in a water use caution area (WUCA). As a result, the SFWMD informed us that this utility is not required to have a conservation program.

The utility's current rate structure consists of a base facility and gallonage charge rate structure. Under the current rate structure, the total average consumption per bill is 6,840 gallons which is below the 10,000 gallon threshold that determines whether a more aggressive conservation-oriented rate structure is appropriate. Although this utility has not implemented a conservation program, it appears that its customers are voluntarily making efforts to conserve water because the water consumption for this utility is low. Based on the information above, staff is recommending that the base facility and gallonage charge rate structure be continued for this utility.

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ISSUE 9: Is repression of consumption likely to occur in this instance, and, if so, what is the appropriate consumption adjustment?

RECOMMENDATION: Yes, repression of consumption is likely to occur in this instance. The appropriate consumption adjustment is a reduction of 525,280 gallons for the water system. (GOLDEN)

STAFF ANALYSIS: This case represents only the fourth instance in which staff has contemplated making a repression adjustment to billed consumption. Therefore, in order to present a thorough analysis, a discussion of the merits of repression adjustments in general is warranted, as well as a discussion of staff's recommended adjustment.

General Discussion Regarding Repression and Price Elasticity

The term "price elasticity" refers to the relationship between water use and water price. Price elasticity measures the percentage change in the quantity demanded resulting from a one percent change in price, all other factors held constant. For example, if a water price increase of one percent leads to a 0.2 percent reduction in water use, price elasticity would be -0.2. (In other words, there is an inverse relationship between price and the quantity demanded -- this is the first law of demand). The term "repression" refers to the expected reduction in quantity demanded resulting from an increase in price.

Consider the following example:

Assume: A 10% increase in price
Price elasticity = -0.3
Then: Resulting price = 110%
Reduction in demand = 3% (10% x -0.3)
Resulting demand = 97%
Resulting revenue increase = 6.7%
(110% price x 97% demand)

The above example illustrates that ignoring price elasticity in rate design analysis creates the potential for both revenue instability and revenue shortfalls. Furthermore, if rate structure is substantially modified or if a large rate increase is implemented, revenue shortfalls can be especially problematic.

The preliminary increase in average customer bills in this case, before any adjustments for repression, is approximately 34%. Staff believes this increase is significant enough to warrant consideration of a repression adjustment in this proceeding.

Staff's Recommended Repression Adjustment

In an attempt to quantify the relationship between revenue increases and consumption impacts, staff has created a database of all water utilities that were granted rate increases or decreases (excluding indexes and pass-throughs) between January 1, 1990 and December 31, 1995 (including those that were granted concomitant wastewater rate increases). This database contains utility-specific information from the applicable orders, tariff pages and the utilities' annual reports for the years 1989 - 1995. A summary of the contents of the database is listed below:

Data Obtained from:

Orders

1. The dollar amount of the revenue requirement increase for the water system (and for the wastewater system, if applicable).
2. The utility's rate structure(s) and rates before and after the rate proceeding.

Annual Reports

1. The number of water gallons sold for the years 1989 - 1995.
2. The number of year-end water system meter equivalents for the years 1989 - 1995.

Tariff Pages

1. The effective date of the revised rates.

Resulting Calculations:

1. The revenue requirement percentage increase (decrease) for the water system (and for the wastewater system, if applicable).
2. The annual dollar amount of the water system revenue requirement increase (decrease) per meter equivalent (and for the wastewater system, if applicable).
3. The average monthly water consumption per meter equivalent for the years 1989 - 1995.
4. The percentage change in the average monthly water consumption per meter equivalent from the prior year for the years 1990 - 1995.
5. The average monthly water bill for both the year prior to and the year subsequent to the rate change. The average monthly bills are based on the average monthly consumption per meter equivalent in the year prior to the rate change.

Several utilities were excluded from the analysis, typically due to the lack (or unreliability) of consumption data. Data from the

remaining 67 utilities forms the basis for our analysis.

Our analysis in this case was performed using two different bases of comparison. The first basis of comparison used Morningside's preliminary rate increase to the water system (before a regression adjustment) of 34%. This preliminary rate increase was compared to other utilities in the database which, as in Morningside's case, underwent no change in the BFC/gallage water system rate structure. Staff then isolated seven utilities in the database which had experienced similar percentage increases in the average monthly bills. The change in average monthly consumption per meter equivalent (ME) for these seven isolated utilities was (13%), (13%), (7%), (4%), (1%), 1% and 5%. The utilities with the 1% and 5% increases in average consumption appear to be anomalous, as the other utilities all exhibited consumption reductions ranging from 1% to 13% following rate increases. Next, staff compared Morningside's average consumption per ME to the remaining five utilities. The utilities which most closely matched Morningside's average consumption exhibited 1% and 4% consumption reductions. Based on this analysis, a consumption reduction between 1% and 4% would appear to be a conservative prediction of Morningside's anticipated consumption reduction.

The second basis of comparison used Morningside's annual revenue requirement increase, which was \$110/ME. The remaining steps using this basis of comparison follow those described in the preceding paragraph. The \$110/ME increase was compared to similar increases in annual revenue requirement per ME of other utilities in the database which underwent no change in the BFC/gallage water rate structure. This comparison produced five utilities which experienced similar increases. The changes in average monthly consumption per ME for these five utilities were (7%), (5%), (1%), (1%) and 5%. Staff believes the utility with the 5% increase in average consumption is anomalous also, as the other four utilities all exhibited consumption reductions. Staff then compared Morningside's average consumption per meter equivalent to the remaining four utilities. The two utilities that exhibited 1% reductions in consumption most closely matched Morningside's average consumption. Using this basis of analysis, a 1% consumption reduction would appear to be the most conservative prediction of Morningside's anticipated consumption reduction.

As discussed above, this case represents only the fourth instance in which staff recommends that a regression adjustment be made, and, as such, staff has no established, previously-approved methodology to calculate an appropriate adjustment. Until approved methodologies are in place, staff believes it is appropriate to err on the side of caution when considering the

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magnitude of our recommended adjustments. As discussed above, our analysis indicates that in this case a consumption reduction between 1% and 4% is more likely to occur than a reduction in the 5% to 13% range seen at the high end of the sample. Although staff's analysis leans more heavily toward a 1% repression adjustment, staff is concerned that given the wide range of decreases that appeared in both samples a 1% reduction may be too conservative. In consideration of these factors, staff believes a 4% repression adjustment is appropriate in this case. Therefore, staff recommends a repression adjustment of 525,280 gallons for the water system.

ISSUE 10: What are the appropriate rates and rate structure?

RECOMMENDATION: The recommended rates are designed to produce revenue of \$69,003 which excludes miscellaneous service charges. The utility should retain its base facility and gallonage charge rate structure. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code, provided the customers have received notice. The rates may not be implemented until proper notice has been received by the customers. The utility should provide proof of the date notice was given within 10 days after the date of the notice. (GALLOWAY)

STAFF ANALYSIS: The utility currently employs the base facility and gallonage charge rate structure. Staff recommends that the utility retain its current rate structure. The current rate structure promotes conservation and is designed to provide equitable sharing by the rate payers of both the fixed and variable costs for providing service. The base facility charge is based on the concept of readiness to serve all customers connected to the system. This ensures that ratepayers pay their share of the fixed costs for providing service (through the base facility charge) and also pay their share of the variable costs of providing service (through the consumption or gallonage charge).

During the test year the utility provided water service to approximately 181 residential customers. As discussed earlier, staff is implementing a repression adjustment to the number of gallons sold to customers. Therefore, rates have been calculated using the number of bills and the adjusted number of gallons of water billed during the test year. A schedule of the utility's existing rates and staff's recommended rates follows:

WATER
Monthly Rates

| BASE FACILITY CHARGE | <u>Existing Rates</u> | <u>Staff's Recommended Rates</u> |
|-----------------------------|------------------------------|---|
| <u>Meter Size</u> | | |
| 5/8 x 3/4" | \$ 12.00 | \$ 15.47 |
| 1" | N/A | 38.68 |
| 1 1/2" | N/A | 77.37 |
| 2" | N/A | 123.79 |
| 3" | N/A | 247.58 |
| 4" | N/A | 386.84 |
| 6" | N/A | 773.69 |
| GALLONAGE CHARGE | \$ 2.20 | \$ 3.12 |

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The average number of gallons of water billed for the test year is approximately 6,840 gallons per month/customer. A schedule of an average bill based on existing rates and recommended rates follows:

| | |
|--------------------------------------|--------------------------|
| Average bill using recommended rates | \$ 36.81 |
| Average bill using existing rates | <u>(27.05)</u> |
| Increase in bill | \$ 9.76 |
| Percentage increase in bill | 36.10% (\$ 9.76/\$27.05) |

The recommended rates are designed to produce revenue in the amount of \$69,003, which excludes miscellaneous service revenues. The utility should retain the base facility and gallonage charge rate structure. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code, provided the customers have received notice. The rates may not be implemented until proper notice has been received by the customers. The utility should provide proof of the date notice was given within 10 days after the date of the notice.

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ISSUE 11: 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 as required by Section 367.0816, Florida Statutes?

RECOMMENDATION: The water rates should be reduced as shown on Schedule No. 4, to remove rate case expense grossed-up for regulatory assessment fees and amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the recovery period, pursuant to Section 367.0816, Florida Statutes. 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. (GALLOWAY)

STAFF ANALYSIS: Section 367.0816, Florida Statutes requires that the rates be reduced immediately following the expiration of the four year period by the amount of the rate case expense previously included in the rates. The reduction will reflect the removal of the revenues associated with the amortization of rate expense and the gross-up for regulatory assessment fees, which is \$468. The reduction in revenues will result in the rates recommended by staff on Schedule No. 4.

The utility should be required to file revised tariffs no later than one month prior to the actual date of the required rate reduction. The utility also should be required to file a proposed customer notice setting forth the lower rates and the reason for the reduction.

If the utility files this reduction in conjunction with a price index or pass-through rate adjustment, separate data shall 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.

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ISSUE 12: Should the recommended rates be approved for the utility on a temporary basis in the event of a timely protest filed by a party other than the utility?

RECOMMENDATION: Yes, the recommended rates should be approved for the utility on a temporary basis in the event of a timely protest filed by a party other than the utility. The utility should be authorized to collect the temporary rates after staff's approval of the security for potential refund, the proposed customer notice, and the revised tariff sheets. In addition, after the increased rates are in effect, pursuant to Rule 25-30.360(6), Florida Administrative Code, the utility should file reports with the Division of Water and Wastewater no later than 20 days after each monthly billing. These reports should indicate the amount of revenue collected under the increased rates. (GALLOWAY, FLEMING)

STAFF ANALYSIS: This recommendation proposes an increase in water rates. A timely protest might delay what may be a justified rate increase resulting in an unrecoverable loss of revenue to the utility. Therefore, in the event of a timely protest filed by a party other than the utility, staff recommends that the recommended rates be approved as temporary rates. The recommended rates collected by the utility shall be subject to the refund provisions discussed below.

The utility should be authorized to collect the temporary rates upon the staff's approval of the security for potential refund and the proposed customer notice. The security should be in the form of a bond or letter of credit in the amount of \$11,802. Alternatively, the utility could establish an escrow agreement with an independent financial institution.

If the utility chooses a bond as security, the bond should contain wording to the effect that it will be terminated only under the following conditions:

- 1) The Commission approves the rate increase; or
- 2) If the Commission denies the increase, the utility shall refund the amount collected that is attributable to the increase.

If the utility chooses a letter of credit as security, it should contain the following conditions:

- 1) The letter of credit is irrevocable for the period it is in effect.

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- 2) The letter of credit will be in effect until final Commission order is rendered, either approving or denying the rate increase.

If security is provided through an escrow agreement, the following conditions should be part of the agreement:

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

In no instance should the maintenance and administrative costs associated with the refund be borne by the customers. These costs are the responsibility of, and should be borne by, the utility. Irrespective of the form of security chosen by the utility, an account of all monies received as result of the rate increase should be maintained by the utility. This account must specify by whom and on whose behalf such monies were paid. If a refund is ultimately required, it should be paid with interest calculated pursuant to Rule 25-30.360(4), Florida Administrative Code.

The utility should maintain a record of the amount of the bond, and the amount of revenues that are subject to refund. In addition, after the increased rates are in effect, pursuant to Rule

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25-30.360(6), Florida Administrative Code, the utility should file reports with the Division of Water and Wastewater no later than 20 days after each monthly billing. These reports should indicate the amount of revenue collected under the increased rates.

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ISSUE 13: Should the Commission order Morningside to show cause, in writing within twenty-one days, why it should not be fined an amount up to \$5,000 for violations of Sections 367.081(1) and 367.091(3), Florida Statutes.

RECOMMENDATION: No, a show cause proceedings should not be initiated. Further, the \$1,110 collection of late payments should not be refunded. However, the utility should be placed on notice that pursuant to Sections 367.081(1) and 367.091(3), Florida Statutes, it may in the future only collect rates and charges approved by the Commission.

STAFF ANALYSIS: Morningside is presently charging a \$5.00 late payment fee that is not contained in its tariff. The utility collected late payment charges in the amount of \$1,110. Morningside is in apparent violation of Sections 367.081(1) and 367.091(3), Florida Statutes, which provide that a utility may only collect rates and charges approved by the Commission and contained in the tariff.

Section 367.161(1), Florida Statutes, authorizes the Commission to assess a penalty of not more than \$5,000 for each offense, if a utility is found to have knowingly refused to comply with, or have willfully violated, any provision of Chapter 367, Florida Statutes. Utilities are charged with the knowledge of the Commission's rules and statutes. Additionally, "[i]t is a common maxim, familiar to all minds that 'ignorance of the law' will not excuse any person, either civilly or criminally." Barlow v. United States, 32 U.S. 404, 411 (1833). Thus, any intentional act, such as the utility's failure to obtain Commission approval prior to collecting a late payment charge not contained in its tariff, would meet the standard for a "willful violation." In Order No. 24306, issued April 1, 1991, in Docket No. 890216-TL titled In Re: Investigation Into The Proper Application of Rule 25-14.003, F.A.C., Relating To Tax Savings Refund for 1988 and 1989 For GTE Florida, Inc., the Commission, having found that the company had not intended to violate the rule, nevertheless found it appropriate to order it to show cause why it should not be fined, stating that "'willful' implies an intent to do an act, and this is distinct from an intent to violate a statute or rule." Id. at 6.

Although the utility collected unauthorized charges, staff believes that a show cause proceeding should not be initiated. During the test period, the utility collected late payment charges in the amount of \$1,110. This amount represents 220 late payments or approximately 11.4% of the utility's customer base making late payments each month. Applying the percentage of late payments to the utility's average monthly revenue results in a significant

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portion of this utility's revenue not being realized each month which in turn places the utility at risk of inability to pay monthly utility expense. Further, as stated in Issue 14, the cost causer (customers who are late on payment) should pay the costs incurred to the utility by late payments. Therefore, staff has recommended approval for the \$5.00 late payment charge. Accordingly, staff recommends that Morningside not be required to show cause for violation of Sections 367.081 and 367.091, Florida Statutes. However, the utility should be placed on notice that pursuant to Sections 367.081(1) and 367.091(3), Florida Statutes, it may in the future only collect rates and charges approved by the Commission. Further, the Commission should not require a refund of the \$1,110.

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ISSUE 14: Should the utility's tariff have a provision for a late payment charge along with a customer deposit, and if so, what are the appropriate charges?

RECOMMENDATION: Yes. A late payment charge in the amount of \$5.00 and a customer deposit in the amount of \$73.62 should be included as part of this utility's tariff. The utility should file revised tariff sheets which are consistent with the Commission's vote. Staff should be given administrative authority to approve the revised tariff sheets upon staff's verification that the tariffs are consistent with the Commission's decision. If the revised tariff sheets are filed and approved, the late payment charges and customer deposits should become effective after the stamped approval date of the revised tariff sheets, if no protest is filed.
(GALLOWAY)

STAFF ANALYSIS: The utility's tariff presently does not have a provision for late payment charges or for customer deposits. Staff believes that both provisions are necessary for this utility.

While the utility's tariff does not have a provision for a late payment charge, the utility collected late payment charges in the amount of \$1,110 during the test period. This amount represents 220 late payments or approximately 11.4% of the utility's customer base making late payments each month. Applying the percentage of late payments to the utility's average monthly revenue results in a significant portion of this utility's revenue not being realized each month which in turn places the utility at risk of inability to pay monthly utility expenses.

In the past, late payment fee requests have been handled on a case-by-case basis. Recommendations have been made based upon the conditions presented by each individual utility. The Commission has authorized late payment charges for water and wastewater companies based on demonstration by the company of a service delinquency. Presently, Commission rules provide that late paying customers may be required by the utility to provide an additional deposit. However, there is no further incentive for late paying customers to pay their bills on time. Staff believes that the cost causer should pay the additional costs incurred to the utility by late payments, rather than the general body of the utility's rate payers. Therefore, staff recommends that the utility implement a late payment charge of \$5.00.

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Additionally, staff is recommending that a provision be included in the utility's tariff for a customer deposit. Rule 25-30.311(1), Florida Administrative Code, states:

"A utility may require, upon reasonable written notice of not less than 30 days, such request or notice being separate and apart from any bill for service, a new deposit, where previously waived or returned, or an additional deposit, in order to secure payment of current bills; provided, however, that the total amount of the required deposit shall not exceed an amount equal to the average actual charge for water and/or wastewater service for two billing periods for the 12 month period immediately prior to the date of notice. In the event the customer has had service less than 12 months, then the utility shall base its new or additional deposit upon the average monthly billing available."

The utility has experienced a high number of late paying during the test year. Staff believes that in an effort to discourage these payment practices, a customer deposit should be included in the utility's tariff. Staff has calculated a customer deposit of \$73.62. Therefore, our preliminary recommendation is to approve a late payment charge in the amount of \$5.00 and a customer deposit in the amount of \$73.62 for the residential customers.

Staff is also recommending that the utility file revised tariff sheets which are consistent with the Commission's vote. Staff should be given administrative authority to approve the revised tariff sheets upon staff's verification that the tariffs are consistent with the Commission's decision. If the revised tariff sheets are filed and approved, the late payment charges and customer deposits should become effective after the stamped approval date of the revised tariff sheets, if no protest is filed.

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ISSUE 15: Should the Commission order Morningside to show cause, in writing within twenty-one days, why it should not be fined an amount up to \$5,000 for violation of Rule 25-30.115, Florida Administrative Code?

RECOMMENDATION: No. A show cause proceeding should not be initiated. However, the utility should be ordered to maintain its books and records in conformity with the 1996 NARUC Uniform System of Accounts (USOA) and should be required to submit a statement from its accountant by March 31, 1999, along with its 1998 annual report, stating that its books are in conformity with NARUC USOA and have been reconciled with the Commission's order. (FLEMING)

STAFF ANALYSIS: During the test year, the utility's books were not maintained in conformity with the USOA. Paragraph (1) of Rule 25-30.115, Florida Administrative Code, entitled "Uniform System of Accounts for Water and Sewer Utilities," states:

- 1) Water and Sewer Utilities shall, effective January 1, 1998, maintain its [sic] accounts and records in conformity with the 1996 NARUC Uniform System of Accounts Adopted by the National Association of Regulatory Utility Commissioners.

Section 367.161, Florida Statutes, authorizes the Commission to assess a penalty of not more than \$5,000 per day for each offense, if a utility is found to have knowingly refused to comply with, or have willfully violated any Commission rule, order, or provision of Chapter 367, Florida Statutes. Utilities are charged with the knowledge of the Commission's rules and statutes. Additionally, "[i]t is a common maxim, familiar to all minds that 'ignorance of the law' will not excuse any person, either civilly or criminally." Barlow v. United States, 32 U.S. 404, 411 (1833). Thus, any intentional act, such as the utility's failure to maintain its books and records in conformity with the 1996 NARUC Uniform System of Accounts, would meet the standard for a "willful violation." In Order No. 24306, issued April 1, 1991, in Docket No. 890216-TL, entitled In Re: Investigation Into The Proper Application of Rule 25-14.003, F.A.C., Relating To Tax Savings Refund for 1988 and 1989 For GTE Florida, Inc., the Commission, having found that the company had not intended to violate the rule, nevertheless found it appropriate to order it to show cause why it should not be fined, stating that "'willful' implies an intent to do an act, and this is distinct from an intent to violate a statute or rule." Id. at 6.

Although staff recognizes that the utility is in apparent violation of Rule 25-30.115, Florida Administrative Code, staff

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believes that a show cause proceeding is unwarranted for the following reasons. The test year for this rate case ended December 31, 1997, and the utility was not aware of the Commission's rules and regulations until mid-way through the test year. As stated in the background, this utility was granted operating Certificate No. 595-W, pursuant to Order No. PSC-97-1211-FOF-WU, issued October 7, 1997. This current proceeding is the utility's first rate case before the Commission. Therefore, given the relatively short time under Commission jurisdiction, staff believes the utility should be given time and an accounting allowance to set up its books in conformity with NARUC USOA and to reconcile its books with the Commission's order.

In Issue 6, staff has recommended an additional \$1,300 accounting allowance for the purpose of setting up the utility's books in conformity with the USOA. The accounting allowance is amortized over 5 years, resulting in an annual accounting allowance of \$350 for this purpose. These funds will also be used to reconcile the utility's books with the Commission's order.

Therefore, staff recommends that the Commission not order Morningside to show cause for violation of Rule 25-30.115, Florida Administrative Code. However, the utility should be ordered to maintain its books and records in conformity with the 1996 NARUC USOA and should be required to submit a statement from its accountant by March 31, 1999, along with its 1998 annual report, stating that its books are in conformity with NARUC USOA and have been reconciled with the Commission's order.

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ISSUE 16: Should this docket be closed?

RECOMMENDATION: This docket should be closed if no person, whose interests are substantially affected by the proposed action, files a protest within the 21 day protest period. (GALLOWAY, FLEMING)

STAFF ANALYSIS: Staff believes that, upon expiration of the protest period, this docket should be closed if no person, whose interests are substantially affected by the proposed action, files a protest within the 21 day protest period.

MORNINGSIDE UTILITY, INC.
 SCHEDULE OF WATER RATE BASE
 TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 1
 DOCKET NO. 980445-WU

| | <u>BALANCE PER UTILITY</u> | <u>STAFF ADJ. TO UTIL. BAL.</u> | <u>BALANCE PER STAFF</u> |
|--|------------------------------------|-------------------------------------|---|
| UTILITY PLANT IN SERVICE | \$ 0 | \$ 140,220 A | \$ 140,220 |
| LAND/NON-DEPRECIABLE ASSETS | 0 | 38,000 B | 38,000 |
| NON-USED AND USEFUL PLANT | 0 | (9,732) C | (9,732) |
| ACQUISITION ADJUSTMENT | 0 | 0 | 0 |
| CWIP | 0 | 0 | 0 |
| CIAC | 0 | (109,200) D | (109,200) |
| ACCUMULATED DEPRECIATION | 0 | (57,374) E | (57,374) |
| AMORTIZATION OF ACQUISITION ADJUSTMENT | 0 | 0 | 0 |
| AMORTIZATION OF CIAC | 0 | 40,697 F | 40,697 |
| WORKING CAPITAL ALLOWANCE | 0 | 7,345 G | 7,345 |
| WATER RATE BASE | \$ 0 | \$ 49,957 | \$ 49,957 |

MORNINGSIDE UTILITY, INC.
ADJUSTMENTS TO RATE BASE
TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 1A
DOCKET NO. 980445-WU

| | <u>WATER</u> |
|--|---------------------|
| A. <u>UTILITY PLANT IN SERVICE</u> | |
| 1. To record plant per original cost study at establishment (198 | \$ 91,530 |
| 2. To record 1996 additions to plant | 44,776 |
| 3. To record test year additions to plant | 7,829 |
| 4. To reduce plant by averaging adjustment | <u>(3,915)</u> |
| | <u>\$ 140,220</u> |
| B. <u>LAND</u> | |
| 1. To record land | <u>\$ 38,000</u> |
| C. <u>NON-USED AND USEFUL PLANT</u> | |
| 1. To reflect non-used and useful average plant | \$ (15,464) |
| 2. To reflect non-used and useful average accumulated depreciation | <u>5,732</u> |
| | <u>\$ (9,732)</u> |
| D. <u>CONTRIBUTIONS IN AID OF CONSTRUCTION(CIAC)</u> | |
| 1. To reflect CIAC at 12/31/97 | \$ (109,800) |
| 2. To reflect averaging adjustment | <u>600</u> |
| | <u>\$ (109,200)</u> |
| E. <u>ACCUMULATED DEPRECIATION</u> | |
| 1. To reflect accumulated depreciation at 12/31/97 | \$ (60,696) |
| 2. To reflect averaging adjustment | <u>3,322</u> |
| | <u>\$ (57,374)</u> |
| F. <u>AMORTIZATION OF CIAC</u> | |
| 1. Amortization of CIAC at 12/31/97 | \$ 43,214 |
| 2. To reflect averaging adjustment | <u>(2,517)</u> |
| | <u>\$ 40,697</u> |
| G. <u>WORKING CAPITAL ALLOWANCE</u> | |
| 1. To reflect 1/8 of operation and maintenance expense | <u>\$ 7,345</u> |

MORNINGSIDE UTILITY, INC.
 SCHEDULE OF CAPITAL STRUCTURE
 TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 2
 DOCKET NO. 980445-WU

| | <u>PER UTILITY</u> | <u>STAFF ADJUST. TO UTIL. BAL.</u> | <u>ADJUSTED BALANCE PER STAFF</u> | <u>PRO RATA ADJUST. PER STAFF</u> | <u>RECONCIL- IATION TO RATE BASE</u> | <u>PERCENT OF TOTAL</u> | <u>COST</u> | <u>WEIGHTED COST</u> |
|-------------------|--------------------|--|---|---|--|-----------------------------|-------------|--------------------------|
| COMMON EQUITY | \$ 79,423 | \$ 0 | \$ 79,423 | \$ (43,012) | 36,411 | 72.88% | 8.89% | 6.48% |
| LONG-TERM DEBT | 14,646 | (1,466) | 13,180 | (7,138) | 6,042 | 12.09% | 10.25% | 1.24% |
| LONG-TERM DEBT | 0 | 16,369 | 16,369 | (8,865) | 7,504 | 15.02% | 10.00% | 1.50% |
| PREFERRED EQUITY | 0 | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% |
| CUSTOMER DEPOSITS | 0 | 0 | 0 | 0 | 0 | 0.00% | 6.00% | 0.00% |
| OTHER | 0 | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% |
| TOTAL | \$ 94,069 | \$ 14,903 | 108,972 | \$ (59,015) | 49,957 | 100.00% | | 9.21% |

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| <u>RANGE OF REASONABLENESS</u> | <u>LOW</u> | <u>HIGH</u> |
|--------------------------------|------------|-------------|
| RETURN ON EQUITY | 7.89% | 9.89% |
| OVERALL RATE OF RETURN | 8.48% | 9.94% |

MORNINGSIDE UTILITY, INC.
 SCHEDULE OF WATER OPERATING INCOME
 TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 3
 DOCKET NO. 980445-WU

| | <u>TEST YEAR PER UTILITY</u> | <u>COMM. ADJ. TO UTILITY</u> | <u>COMM. ADJUSTED TEST YEAR</u> | <u>ADJUST. FOR INCREASE</u> | <u>TOTAL PER COMM.</u> |
|---------------------------|----------------------------------|----------------------------------|---|-------------------------------------|----------------------------|
| OPERATING REVENUES | \$ <u>75,409</u> | \$ <u>(22,369) A</u> | \$ <u>53,040</u> | \$ <u>17,073 F</u> | \$ <u>70,113</u> |
| | | | | 32.19% | |
| OPERATING EXPENSES: | | | | | |
| OPERATION AND MAINTENANCE | \$ <u>42,670</u> | \$ <u>16,087 B</u> | \$ <u>58,757</u> | \$ <u>0</u> | \$ <u>58,757</u> |
| DEPRECIATION (NET) | <u>12,845</u> | <u>(7,097) C</u> | <u>5,748</u> | <u>0</u> | <u>5,748</u> |
| AMORTIZATION (CIAC) | <u>0</u> | <u>(5,034) D</u> | <u>(5,034)</u> | <u>0</u> | <u>(5,034)</u> |
| TAXES OTHER THAN INCOME | <u>2,886</u> | <u>2,387 E</u> | <u>5,273</u> | <u>768 G</u> | <u>6,041</u> |
| INCOME TAXES | <u>0</u> | <u>0</u> | <u>0</u> | <u>0</u> | <u>0</u> |
| TOTAL OPERATING EXPENSES | \$ <u>58,401</u> | \$ <u>6,343</u> | \$ <u>64,743</u> | \$ <u>768</u> | \$ <u>65,512</u> |
| OPERATING INCOME/(LOSS) | \$ <u>17,008</u> | | \$ <u>(11,703)</u> | | \$ <u>4,601</u> |
| WASTEWATER RATE BASE | | | \$ <u>49,957</u> | | \$ <u>49,957</u> |
| RATE OF RETURN | | | <u>-23.43%</u> | | <u>9.21%</u> |

MORNINGSIDE UTILITY, INC.
 ADJUSTMENTS TO OPERATING INCOME
 TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 3A
 PAGE 1 OF 2
 DOCKET NO. 980445-WU

| <u>A. OPERATING REVENUES</u> | <u>WATER</u> |
|--|-------------------------|
| 1. To reflect misclassified CIAC | \$ (1,200) |
| 2. To reflect misclassified loans | (21,000) |
| 3. To reflect redeposits | (540) |
| 4. To reflect annualized revenue based on existing rates | 371 |
| | <u>\$ (22,369)</u> |
| | |
| <u>B. OPERATION AND MAINTENANCE EXPENSES</u> | |
| 1. <u>Salaries and Wages - Employees</u> | |
| a. To reflect salaries and wages associated with owner/operator (groundskeeping, meter reading, general management and labor) | \$ <u>19,760</u> |
| 2. <u>Salaries and Wages - Officers</u> | |
| a. To reflect salaries and wages for President & Vice President/Treasurer | \$ <u>3,640</u> |
| 3. <u>Purchased Power</u> | |
| a. To reflect repression adjustment | \$ <u>(91)</u> |
| 4. <u>Chemicals</u> | |
| a. To reflect misclassified automatic chlorinator | \$ (660) |
| b. To reflect repression adjustment | (70) |
| | <u>(730)</u> |
| 5. <u>Material and Supplies</u> | |
| a. To reflect misclassified costs associated with Well #2 | \$ (115) |
| b. To reflect misclassified costs associated with generator | (877) |
| c. To reflect misclassified costs associated with electric panel | (3,950) |
| d. To reflect misclassified costs associated with alarm | (557) |
| | <u>(5,499)</u> |
| 6. <u>Contractual Services (Accounting)</u> | |
| a. To reflect accounting allowance | \$ <u>260</u> |
| 7. <u>Contractual Services (Testing)</u> | |
| a. Reclassification to plant | \$ (1,670) |
| b. To reflect misclassified costs associated with repair to generator | (600) |
| | <u>(2,270)</u> |
| 8. <u>Contractual Services (Other)</u> | |
| a. To reflect repair to generator amortized over 5 years (\$600/5) | \$ <u>120</u> |
| 9. <u>Rents</u> | |
| a. To reflect office space rental | \$ <u>1,200</u> |
| 10. <u>Regulatory Commission Expense</u> | |
| a. To reflect rate case expense amortized over 4 years | \$ <u>447</u> |
| 11. <u>Miscellaneous Expense</u> | |
| a. To remove misclassified regulatory assessment fee | \$ <u>(750)</u> |
| TOTAL O & M ADJUSTMENTS | \$ <u>16,087</u> |

MORNINGSIDE UTILITY, INC.
ADJUSTMENTS TO OPERATING INCOME
TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 3A
PAGE 2 OF 2
DOCKET NO. 980445-WU

C. DEPRECIATION EXPENSE

| | |
|--|-------------------|
| 1. To remove recorded test year depreciation expense | \$ (12,845) |
| 2. To reflect appropriate used & useful test year depreciation expense | 6,645 |
| 3. To reflect non-used and useful depreciation expense | (897) |
| | <u>\$ (7,097)</u> |

D. AMORTIZATION EXPENSE (CIAC)

| | |
|--|-------------------|
| 1. To reflect test year amortization of CIAC | <u>\$ (5,034)</u> |
|--|-------------------|

E. TAXES OTHER THAN INCOME

| | |
|--|-----------------|
| 1. To reflect reclassification of regulatory assessment fees from miscellaneous expense | \$ 750 |
| 2. To adjust for appropriate amount of regulatory assessment fees @ 4.5% of test year revenues | 1,637 |
| | <u>\$ 2,387</u> |

F. OPERATING REVENUES

| | |
|---|------------------|
| 1. To reflect increase in revenue required to cover expenses and allow recommended rate of return | <u>\$ 17,073</u> |
|---|------------------|

G. TAXES OTHER THAN INCOME

| | |
|--|---------------|
| 1. To reflect regulatory assessment fee at 4.5% on increase in revenue | <u>\$ 768</u> |
|--|---------------|

MORNINGSIDE UTILITY, INC.
 ANALYSIS OF WATER OPERATION AND
 MAINTENANCE EXPENSE
 TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 3B
 DOCKET NO. 980445-WU

| | <u>TOTAL PER UTIL.</u> | <u>STAFF RECOM- MENDED ADJUST.</u> | <u>TOTAL PER STAFF</u> |
|--|----------------------------|--|----------------------------|
| #801 SALARIES AND WAGES - EMPLOYEES | \$ 10,900 | \$ 19,760 [1] | \$ 30,860 |
| #803 SALARIES AND WAGES - OFFICERS | 0 | 3,640 [2] | 3,640 |
| #804 PENSIONS AND BENEFITS | 2,495 | 0 | 2,495 |
| #810 PURCHASED WATER | 0 | 0 | 0 |
| #815 PURCHASED POWER | 2,274 | (91)[3] | 2,183 |
| #816 FUEL FOR POWER PRODUCTION | 75 | 0 | 75 |
| #818 CHEMICALS | 2,400 | (730)[4] | 1,670 |
| #820 MATERIALS AND SUPPLIES | 9,475 | (5,499)[5] | 3,976 |
| #830 CONTRACTUAL SERVICES (MGMT) | 0 | 0 | 0 |
| #831 CONTRACTUAL SERVICES (ACCOUNTING) | 0 | 260 [6] | 260 |
| #835 CONTRACTUAL SERVICES (TESTING) | 3,952 | (2,270)[7] | 1,682 |
| #835 CONTRACTUAL SERVICES (OPERATOR) | 2,395 | 0 | 2,395 |
| #836 CONTRACTUAL SERVICES (REPAIRS & MAINT.) | 0 | 120 [8] | 120 |
| #840 RENTS | 0 | 1,200 [9] | 1,200 |
| #850 TRANSPORTATION EXPENSE | 2,122 | 0 | 2,122 |
| #855 INSURANCE EXPENSE | 1,940 | 0 | 1,940 |
| #865 REGULATORY COMMISSION EXPENSE | 0 | 447 [10] | 447 |
| #870 BAD DEBT EXPENSE | 0 | 0 | 0 |
| #875 MISCELLANEOUS EXPENSES | 4,642 | (750)[11] | 3,892 |
| | <u>\$ 42,670</u> | <u>\$ 16,087</u> | <u>\$ 58,757</u> |

MORNINGSIDE UTILITY, INC.
 SCHEDULE OF RATE CASE EXPENSE RATE
 REDUCTION AFTER FOUR YEARS
 TEST YEAR ENDED DECEMBER 31, 1997

SCHEDULE NO. 4
 DOCKET NO. 980445-WU

MONTHLY RATES

| <u>RESIDENTIAL WATER SERVICE</u> | <u>STAFF REC. RATES</u> | <u>STAFF REC. DECREASE</u> |
|---|-----------------------------|--------------------------------|
| BASE FACILITY CHARGE: | | |
| Meter Size: | | |
| 5/8" x 3/4" | \$ 15.47 | \$ 0.18 |
| 1" | 38.88 | 0.44 |
| 1 1/2" | 77.37 | 0.89 |
| 2" | 123.79 | 1.42 |
| 3" | 247.58 | 2.85 |
| 4" | 386.84 | 4.45 |
| 6" | 773.69 | 8.90 |
| | | |
| RESIDENTIAL GALLONAGE CHARGE PER 1,000 GALLONS | \$ 3.12 | \$ 0.04 |

PLANT USED & USEFUL

Used & Useful = (Av. Daily Flow + Margin Reserve + Fire Flow - Excessive

$$\begin{aligned} & \text{Unaccounted for Water) } \div \text{ Rated Plant Capacity} \times 100\% \\ & = (35,979 \text{ GPD} + 0 + 0 - 0) \div 216,000 \text{ GPd} \times 100\% \\ & = 17\% \end{aligned}$$

Used & Useful (Alt. Method) = (current customers ÷ no. of customers at build-out) × 100%

$$= 167 \div 210 \times 100\% = 80\%$$

DISTRIBUTION SYSTEM USED & USEFUL

Used & Useful = (Number of Lots Currently Connected to the Distribution System ÷ Lots Accessible to the Distribution System) × 100%

$$\begin{aligned} & = (167 \div 167) \times 100\% \\ & = 100\% \end{aligned}$$

DOCKET NO. 980445-WU
OCTOBER 22, 1998

ISSUE AND RECOMMENDATION SUMMARY

ISSUE 1: Is the quality of service provided by Morningside satisfactory?

RECOMMENDATION: Yes, the quality of service provided by Morningside to its customers is satisfactory. (MUNROE)

ISSUE 2: What are the appropriate used and useful percentages for the water treatment plant and distribution system?

RECOMMENDATION: The water treatment plant should be considered 80% used and useful. The distribution system should be considered 100% used and useful. Staff recommends no margin reserve be allowed. (MUNROE)

ISSUE 3: What is the utility's appropriate average amount of rate base for ratesetting purposes?

RECOMMENDATION: The appropriate average amount of test year rate base should be \$49,957. (GALLOWAY, MUNROE)

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

RECOMMENDATION: The appropriate rate of return on equity is 8.89% with a range of 7.89% - 9.89% and the overall rate of return is 9.21% with a range of 8.48% - 9.94%. (GALLOWAY)

ISSUE 5: What is the appropriate test year revenue?

RECOMMENDATION: The appropriate test year revenue is \$53,040. (GALLOWAY)

ISSUE 6: What is the appropriate amount of operating expenses?

RECOMMENDATION: The appropriate amount of operating expenses is \$65,512. (GALLOWAY, MUNROE)

ISSUE 7: What is the appropriate revenue requirement for this utility?

RECOMMENDATION: The appropriate revenue requirement is \$70,113. (GALLOWAY)

DOCKET NO. 980445-WU
OCTOBER 22, 1998

ISSUE 8: What is the appropriate conservation rate structure for this utility?

RECOMMENDATION: The appropriate conservation rate structure for this utility is a continuation of the current base facility and gallonage charge rate structure.

ISSUE 9: Is repression of consumption likely to occur in this instance, and, if so, what is the appropriate consumption adjustment?

RECOMMENDATION: Yes, repression of consumption is likely to occur in this instance. The appropriate consumption adjustment is a reduction of 525,280 gallons for the water system. (GOLDEN)

ISSUE 10: What are the appropriate rates and rate structure?

RECOMMENDATION: The recommended rates are designed to produce revenue of \$69,003 which excludes miscellaneous service charges. The utility should retain its base facility and gallonage charge rate structure. The approved rates should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code, provided the customers have received notice. The rates may not be implemented until proper notice has been received by the customers. The utility should provide proof of the date notice was given within 10 days after the date of the notice. (GALLOWAY)

ISSUE 11: 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 as required by Section 367.0816, Florida Statutes?

RECOMMENDATION: The water rates should be reduced as shown on Schedule No. 4, to remove rate case expense grossed-up for regulatory assessment fees and amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the recovery period, pursuant to Section 367.0816, Florida Statutes. 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. (GALLOWAY)

DOCKET NO. 980445-WU
OCTOBER 22, 1998

ISSUE 12: Should the recommended rates be approved for the utility on a temporary basis in the event of a timely protest filed by a party other than the utility?

RECOMMENDATION: Yes, the recommended rates should be approved for the utility on a temporary basis in the event of a timely protest filed by a party other than the utility. The utility should be authorized to collect the temporary rates after staff's approval of the security for potential refund, the proposed customer notice, and the revised tariff sheets. In addition, after the increased rates are in effect, pursuant to Rule 25-30.360(6), Florida Administrative Code, the utility should file reports with the Division of Water and Wastewater no later than 20 days after each monthly billing. These reports should indicate the amount of revenue collected under the increased rates. (GALLOWAY, FLEMING)

ISSUE 13: Should the Commission order Morningside to show cause, in writing within twenty-one days, why it should not be fined an amount up to \$5,000 for violations of Sections 367.081(1) and 367.091(3), Florida Statutes.

RECOMMENDATION: No, a show cause proceedings should not be initiated. Further, the \$1,110 collection of late payments should not be refunded. However, the utility should be placed on notice that pursuant to Sections 367.081(1) and 367.091(3), Florida Statutes, it may in the future only collect rates and charges approved by the Commission. (FLEMING)

ISSUE 14: Should the utility's tariff have a provision for a late payment charge along with a customer deposit, and if so, what are the appropriate charges?

RECOMMENDATION: Yes. A late payment charge in the amount of \$5.00 and a customer deposit in the amount of \$73.62 should be included as part of this utility's tariff. The utility should file revised tariff sheets which are consistent with the Commission's vote. Staff should be given administrative authority to approve the revised tariff sheets upon staff's verification that the tariffs are consistent with the Commission's decision. If the revised tariff sheets are filed and approved, the late payment charges and customer deposits should become effective after the stamped approval date of the revised tariff sheets, if no protest is filed. (GALLOWAY)

DOCKET NO. 980445-WU
OCTOBER 22, 1998

ISSUE 15: Should the Commission order Morningside to show cause, in writing within twenty-one days, why it should not be fined an amount up to \$5,000 for violation of Rule 25-30.115, Florida Administrative Code?

RECOMMENDATION: No. A show cause proceeding should not be initiated. However, the utility should be ordered to maintain its books and records in conformity with the 1996 NARUC Uniform System of Accounts (USOA) and should be required to submit a statement from its accountant by March 31, 1999, along with its 1998 annual report, stating that its books are in conformity with NARUC USOA and have been reconciled with the Commission's order. (FLEMING)

ISSUE 16: Should this docket be closed?

RECOMMENDATION: This docket should be closed if no person, whose interests are substantially affected by the proposed action, files a protest within the 21 day protest period. (GALLOWAY, FLEMING)

STATE OF FLORIDA

Commissioners:
JULIA L. JOHNSON, CHAIRMAN
J. TERRY DEASON
SUSAN F. CLARK
JOE GARCIA
E. LEON JACOBS, JR.



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

Public Service Commission

October 29, 1998

RECEIVED-FPSC
98 OCT 29 AM 10:32
RECORDS AND
REPORTING

Morningside Utility, Inc.
1106 Monroe Avenue
St. Cloud, Florida 34769-6713

Re: Docket No. 980445-WU - Application for a staff-assisted rate case by
Morningside Utility, Inc.

To Whom it May Concern:

Enclosed is a copy of the Staff Recommendation filed in this matter on October 22, 1998. The Commission is expected to consider this Recommendation at its November 3, 1998, Agenda Conference which will be held in Room 148, Betty Easley Conference Center, 4075 Esplanade Way, in Tallahassee beginning at 9:30 a.m. Due to the number of items to be covered at this conference, we cannot state the exact time at which this item will be heard. You are welcome to come to this Agenda Conference and observe and/or participate in the discussion of this item. If you have any questions, please feel free to call me at (850) 413-6199.

Sincerely,

A handwritten signature in cursive script that reads "Shannon R. Fleming".

Shannon R. Fleming
Staff Counsel

SRF/lw

cc: Division of Water and Wastewater (Galloway, Gilchrist, Golden, Munroe, Rendell,
Willis)
✓ Division of Records and Reporting