BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for rate increase and increase in service availability charges by Southern States Utilities, Inc. for Orange-Osceola Utilities, Inc. in Osceola County, and in Bradford, Brevard, Charlotte, Citrus, Clay, Collier, Duval, Highlands, Lake, Lee, Marion, Martin, Nassau, Orange, Pasco, Putnam, Seminole, St. Johns, St. Lucie, Volusia, and Washington Counties.	DOCKET NO. 950495-WS ORDER NO. PSC-99-1794-FOF-WS ISSUED: September 14, 1999

FINAL ORDER ON REMAND RECONSIDERING ORDER NO. PSC-99-0093-FOF-WS, APPROVING MODIFIED OFFER OF SETTLEMENT, SETTING FINAL RATES, CANCELING ESCROW REQUIREMENT AND RELEASING ESCROWED FUNDS, DENYING MOTION FOR CONSOLIDATION, AND CLOSING DOCKET

BY THE COMMISSION:

BACKGROUND

On June 28, 1995, Southern States Utilities, Inc., now Florida Water Services Corporation (hereinafter referred to as Florida Water or utility), a Class A utility, filed an application for approval of uniform interim and final water and wastewater rate increases for 141 service areas in 22 counties, pursuant to Sections 367.081 and 367.082, Florida Statutes. The utility also requested a uniform increase in service availability charges, approval of an allowance for funds used during construction (AFUDC) and an allowance for funds prudently invested (AFPI).

On October 30, 1996, we issued Order No. PSC-96-1320-FOF-WS (Final Order) granting, among other things, a rate increase using a capband rate structure, and approving AFPI charges in this rate proceeding. Notices of appeal were subsequently filed with the First District Court of Appeal (First DCA or Court).

The First DCA abated the appeal to allow us to dispose of all motions or cross-motions which were filed for reconsideration of our decision. On December 3, 1996, Florida Water filed a motion

requesting a stay of the refund of interim rates and a portion of the AFPI charges pending appeal, and a release or modification of the bond securing interim refunds. By Order No. PSC-97-0099-FOF-WS (Stay Order), issued January 27, 1997, we granted the utility's request to stay the refund of interim rates, but denied its request to stay a portion of the AFPI charges approved by the Final Order. On February 11, 1997, Florida Water filed a motion for reconsideration of the Stay Order. By Order No. PSC-97-0613-FOF-WS, issued May 29, 1997, we ruled on the utility's motion for reconsideration of the Stay Order and the Office of Public Counsel's (OPC's) March 3, 1997 motion requesting the full Commission to reconsider the Prehearing Officer's denial of its request to establish a schedule for filing motions for reconsideration. By that Order, we reconsidered our previous decisions on stays of AFPI charges and allowed Florida Water to implement its alternate stay proposal, to continue charging, subject to refund, the higher of any AFPI charges. Through this mechanism, we recognized that AFPI charges were severable and the potential for backbilling was minimized.

With the issuance of Order No. PSC-97-0613-FOF-WS, we disposed of all motions for reconsideration and any requests for stays, and briefs were filed with the First DCA. Subsequently, on June 10, 1998, the First DCA issued its opinion on review of the Final Order in Southern States Utils., Inc. v. FPSC, 714 So. 2d 1046 (Fla. 1st DCA 1998). Sugarmill Woods Civic Association, Inc. (Sugarmill Woods), timely filed a motion for rehearing, clarification, and certification of this opinion. By opinion dated August 5, 1998, the Court denied the motion, and, on August 21, 1998, issued its mandate. A summary of the June 10, 1998, Court opinion follows.

First DCA's Opinion

In issuing its mandate, the Court, acting *en banc*, affirmed and approved the capband rate structure and our decision declining to make a downward adjustment in rate base to reflect the price the utility paid for Lehigh Acres. In approving the capband rate structure, the Court held that "whenever the PSC has jurisdiction to set water and sewer rates for multiple systems, inter-system functional relatedness is no prerequisite to the PSC's setting rates that are uniform across a group of systems." Southern States Utils., Inc. v. FPSC, 714 So. 2d at 1051. In so holding, the Court expressly overruled Citrus County v. Southern States Utils., Inc., 656 So. 2d 1307 (Fla. 1st DCA 1995).

The Court reversed our decisions to use annual average daily flows (AADF) in the numerator of the used and useful equation for eight wastewater treatment plants and the lot count method in determining used and useful percentages for the water distribution and wastewater collection systems serving mixed use areas. The Court remanded these issues for the taking of additional evidence, if it exists. That failing, the Court held that we must adhere to our prior practices in calculating used and useful percentages. The Court also reversed our decision to exclude a portion of the prudently incurred construction costs for reuse facilities from rate base.

Moreover, the Court acknowledged that we had confessed error in canceling the previously allowed AFPI charges, and in using AADF in the numerator of the used and useful equation for three wastewater treatment plants when the Department of Environmental Protection permit was not based on AADF. Further, because a refund on the rate structure question was no longer being required in Docket No. 920199-WS, the Court concluded that we should revisit our decision to reduce (by $4.8 million) the utility's investment in equity in light of the status of ongoing litigation on that issue. Regarding the interim rate refund issue, the Court stated that "[b]ecause issues pertaining to refunds may well be moot, once the PSC sets new permanent rates on remand, addressing these issues at this juncture would be premature." Southern States Utils., Inc. v. FPSC, 714 So. 2d at 1049.

Actions Following Mandate

After the Court's issuance of its mandate, we considered whether to reopen the record to take further evidence on the AADF and lot count methodology issues. After much discussion and questions about the dollar amounts associated with each issue on remand, we directed our staff to analyze the costs and benefits of reopening the record and to meet with the parties to explore the possibility of settlement.

Although settlement meetings were held, no agreement could be reached among the parties. Nevertheless, on October 2, 1998, Florida Water and the Marco Island Fair Water Rate Defense Committee filed a joint offer of settlement and proposal for disposition of mandate. On November 12, 1998, Florida Water filed a modification to the joint offer of settlement. At the November 13, 1998 Special Agenda Conference, Florida Water made an additional modification to its November 12, 1998 modified offer.

Upon consideration and rejection of the above-noted offers of settlement, a hearing on remand was scheduled for June 16-18, 1999. However, that hearing was canceled pending further appellate action of Florida Water. Order No. PSC-99-0093-FOF-WS, issued January 15, 1999, memorialized our decisions made at the November 13, 1998 Special Agenda Conference and the December 15, 1998 Agenda Conference. By that Order, we authorized Florida Water to implement increased rates for the used and useful adjustment for reuse facilities, the equity adjustment, and admitted errors (non-discretionary or Category I issues) and ordered that the record in this proceeding be reopened to take additional evidence on the use of the lot count methodology in mixed use areas and the use of AADF in the numerator of the used and useful equation (discretionary or Category II issues).

Moreover, we proposed to authorize Florida Water to implement a surcharge for the nondiscretionary issues and ordered that if protested, the issue of what action should be taken with regard to the collection of surcharges would be made an issue in the scheduled hearing on remand. Sugarmill Woods timely protested this proposed action. By Order No. PSC-99-0664-PCO-WS, issued April 5, 1999, we granted Sugarmill Woods' petition for formal hearing concerning the proposed surcharges and approved a list of issues for consideration on remand.

Upon disagreement with that Order, and with Order No. PSC-99-0612-PCO-WS, issued April 2, 1999, (an order on discovery), Florida Water filed a Motion for Abatement and Continuance and Request for Expedited Ruling (Motion for Abatement) on April 12, 1999. Moreover, Florida Water disagreed with a second order on discovery, Order No. PSC-99-0708-PCO-WS, issued April 13, 1999, and filed a Motion to Enforce Mandate in the First DCA on May 3, 1999, in which it argued that all three of the above-noted orders were in error. On May 6, 1999, Florida Water filed a Motion to Toll Time for Service of Responses to OPC's Second Set of Interrogatories and Third and Fourth Requests for Production of Documents on Remand (Motion to Toll Time).

By Order No. PSC-99-0800-PCO-WS, issued April 21, 1999, the Prehearing Officer granted Florida Water's Motion for Abatement, abating the remand proceeding pending disposition of the appellate action on the utility's Motion to Enforce Mandate, and the Chairman's Office canceled the prehearing and hearing dates. Moreover, by Order No. PSC-99-1199-PCO-WS, issued June 14, 1999,

the Prehearing Officer granted in part and denied in part the utility's Motion to Toll Time.

On that same date, June 14, 1999, the utility filed a Motion for Approval of New Offer of Settlement and Proposal for Disposition of Mandate on Remand (New Offer of Settlement). In the New Offer of Settlement, Florida Water states that the offer is supported by the City Of Marco Island and the Amelia Island Community Association, Inc., et al. (Amelia Island).

On June 24, 1999, the utility filed a Motion for Reconsideration of Order No. PSC-99-1199-PCO-WS (Motion for Reconsideration), whereby it requested that we reconsider our decision to require the utility to respond to OPC's discovery propounded before the abatement of the remand proceeding and to which the utility had no objection. However, one week prior to the filing of this Motion for Reconsideration, by Opinion dated June 17, 1999, the First District denied Florida Water's Motion to Enforce Mandate, disposing of the appellate action.

On June 28, 1999, OPC and Sugarmill Woods filed responses to the New Offer of Settlement. With its response, OPC also moved to consolidate this docket with the Florida Water gain-on-sale docket, Docket No. 980744-WS. On July 2, 1999, OPC filed a response to the utility's Motion for Reconsideration and on July 12, 1999, Florida Water filed its Response to OPC's Motion to Consolidate.

We have received numerous letters from individuals from the Zephyr Shores Estate Property Owners in opposition to the 1.7 percent rate increase proposed in the New Offer of Settlement. We also received a letter dated July 8, 1999, signed by eight individuals purporting to be members of the Board of Directors of the Citrus Springs Civic Association, in Citrus County, in support of the New Offer of Settlement. In addition, by letter dated June 28, 1999, the utility forwarded a letter from the Marco Island Fair Water Defense Fund Committee, stating that it was in support of the utility's New Offer of Settlement. Also, by cover letter dated July 21, 1999, Kenneth W. Bolster forwarded a petition signed by eight customers of Florida Water's Deltona plant. In their petition, the customers request the Commission to accept the settlement offer, and specifically state, among other things, that "surcharges create a severe hardship for our customers, and further litigation expenses are only included in future customer rates."

This Order addresses the utility's New Offer of Settlement and Motion for Reconsideration and OPC's Motion to Consolidate.

NEW OFFER OF SETTLEMENT

As noted above, on June 14, 1999, Florida Water filed its New Offer of Settlement, the purpose of which is to resolve the outstanding issues on remand in the instant case. Pursuant to the appellate decision rendered in this case, we have the prerogative to reopen the record and conduct further proceedings on remand on the two discretionary issues. Although by Order No. PSC-99-0093-FOF-WS we opted to reopen the record for the taking of further evidence on those issues, we believe that we may reconsider that decision on our own motion if we find it to be in the public interest to do so.

We have analyzed whether it is in the public interest to accept the utility's New Offer of Settlement. In so doing, we have examined possible outcomes of the two discretionary issues and what the utility is willing to accept in its offer. The premise is that we could decline to conduct further proceedings and the utility would thereby be entitled to the revenues associated with the two discretionary issues. The additional revenues required for these two issues can be calculated from the evidence in the record. To the extent that the utility has agreed to accept less than the revenues associated with these two issues, at some point the public interest may not be served by conducting further hearings. Moreover, because the utility is willing to take less than what it is entitled to under the Court's decision and it is the only party adversely affected by so doing, due process has been met and we may issue our decision as final agency action.

In addition to determining whether the New Offer of Settlement is in the public interest, we must also determine whether any of the provisions contained therein are in contravention of the law, due process, or the law of the case as set forth in the First DCA's opinion.

In paragraph 20 its New Offer of Settlement, Florida Water proposes the following:

> A. Reduction in prospective Category II rate increase - Florida Water proposes to settle the Category II prospective rate increase for $966,167, or approximately one-half of the amount remaining at issue. This results

in approximately a 1.7% average increase in rates. The increase in rates would be implemented within sixty days after the Commission vote approving this Settlement Offer.

B. No Surcharges - Florida Water proposes that both Category I and II surcharges be booked as a regulatory asset in the amount of $8.5 million (including interest) as of August 1, 1999 and the Commission shall authorize recovery of such regulatory asset (to be amortized over 30 years or a shorter period if the Commission deems appropriate) in the Company's next rate case based on the same surcharge methodology previously ordered for Category I surcharges in Order No. PSC-99-0093-FOF-WS. No amortization of the asset would occur until it is included in rates.[1]

C. Three Year Stayout - Florida Water proposes a 3 year stayout for both rate filings by the Company and earnings investigations by the Commission for all service areas involved in this docket. Indexing and pass-throughs would be allowed. Under this proposal, Florida Water would forego the filing of an application for increased rates, either pursuant to Section 367.081(6) or 367.0822, Florida Statutes, for a period running to Friday, June 28, 2002. For the same period, Florida Water would not be subject to an earnings investigation by the Commission or a petition or complaint to decrease Florida Water's water or wastewater rates or charges. If Florida Water experiences earnings in excess of the top of the range of its authorized return on equity for the calendar years 1999, 2000, 2001 or 2002[2] such excess earnings would be

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[1]According to Florida Water, the total estimated surcharge through August 1, 1999 assuming approval of its New Offer of Settlement is $8.5 million (including interest). The regulatory asset to be booked is proposed to be calculated based upon the effective date of the Category II rate increase. If remand hearings go forward and an appeal is filed, a virtual certainty, the utility estimates the surcharge to grow to $13.5 million through August 1, 2001.

[2]According to Florida Water, the prospect of the utility earning in excess of its authorized return on equity is extremely

shared between Florida Water and its customers on a one-third/two-thirds basis, one-third to be retained by Florida Water and two-thirds to be refunded to Florida Water's customers.[3]

D. Close Orange County Docket No. 980744-WS - Florida Water's shareholders would retain in full the gain on sale of Florida Water's Orange County land and facilities. In sufficient time prior to Commission consideration of this settlement proposal, the Commission would provide notice in the Florida Administrative Weekly of its intent to close Docket No. 980744-WS in recognition of this settlement. Any and all issues concerning Florida Water's gain on sale of its Orange County land and facilities shall not be revisited or reconsidered by the Commission.

E. Rate Case Expense - Accrued rate case expense relating to reconsideration, appeals and the remand would be deferred and considered in Florida Water's next rate case. The total actual appeal and remand expense to date is approximately $450,000 and the total estimated through hearings and appeals is $1.1 million.

F. Interim Rate Refunds - There would be no interim rate refunds. This issue applied only to Lehigh and Marco Island wastewater customers. While Florida Water continues to believe the refund requirement was unlawful, these refunds are eliminated as a result of the Category I rate increase and surcharges approved by the Commission and the Category II rates and surcharges reflected in this Settlement Offer.

G. No Change in AFPI Rates - The Company proposes no change in Allowance for Funds Prudently Invested (AFPI) rates and termination of the existing escrow.

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unlikely given the fact that it earned approximately a 5% return on water and wastewater operations per its 1998 annual report.

[3]Florida Water points out that we recently approved a similar sharing proposal for Florida Power & Light Company pursuant to Order No. PSC-99-0519-AS-EI, issued March 17, 1999, in Docket No. 990067-EI.

H. The resolution of the revenue requirements and rate issues as proposed herein shall not be construed to reflect Commission precedent or policy and shall not be revisited or reconsidered by the Commission.

I. This Settlement Offer is not severable, divisible or subject to modification and shall be deemed withdrawn in the event the Commission does not vote to approve this Offer of Settlement and Proposal for Disposition of Mandate on Remand in its entirety.

In reviewing this New Offer of Settlement, our staff recommended that in order to approve the offer, several provisions contained in subparagraphs C. and D. of paragraph 20 should be deleted. These provisions were as follows:

1. [For a period running to June 28, 2002,] Florida Water would not be subject to an earnings investigation by the Commission or a petition or complaint to decrease Florida Water's water or wastewater rates or charges;

2. If Florida Water experiences earnings in excess of the top of the range of its authorized return on equity for the calendar years 1999, 2000, 2001 or 2002 such excess earnings would be shared between Florida Water and its customers on a one-third/two-thirds basis, one-third to be retained by Florida Water and two-thirds to be refunded to Florida Water's customers; and

3. Florida Water's shareholders would retain in full the gain on sale of Florida Water's Orange County land and facilities. In sufficient time prior to Commission consideration of this settlement proposal, the Commission would provide notice in the Florida Administrative Weekly of its intent to close Docket No. 980744-WS in recognition of this settlement. Any and all issues concerning Florida Water's gain on sale of its Orange County land and facilities shall not be revisited or reconsidered by the Commission.

MODIFIED OFFER OF SETTLEMENT

At the August 23, 1999, Special Agenda Conference, which we held in order to consider Florida Water's New Offer of Settlement, Florida Water submitted a Modified Offer of Settlement and Proposal

for Disposition of Mandate on Remand (Modified Offer of Settlement). In this Modified Offer of Settlement, the utility agreed to delete the three above-noted provisions of the New Offer of Settlement which our staff had recommended were objectionable.

According to Florida Water, the additional benefits of the Modified Offer of Settlement when compared to prior settlement offers include:

1) The overall water and wastewater revenue requirement increase (Categories I and II combined) would be reduced from $2.8 million to $2.0 million.

2) Out-of-pocket, cash payments of surcharges are eliminated. Category I surcharges currently total approximately $2.4 million to date, with interest continuing to accrue. Total potential Category I and II surcharges, assuming an appellate process through August 1, 2001 (a conservative estimate), with interest, are estimated to be $13.5 million. Cash payments of approximately $13.5 million of surcharges are eliminated, replaced by approximately $8.5 million of surcharges (as of August 1, 1999) booked as a regulatory asset as described above.

3) The Company stays out of rate cases affecting the service areas in this docket until at least June 28, 2002.

4) This Settlement Offer has a net present value benefit of approximately $1.9 million to Florida Water's customers compared to Florida Water's prior offers.

5) Rate case expense of approximately $650,000 is eliminated and all rate case expense related to reconsideration of the final order, the appeals and the remand process is deferred until Florida Water's next rate case.

6) The potential for higher rates and additional rate case expense of approximately $1.7 million associated with another rate case is deferred until at least June 28, 2002 due to the 3 year stayout.

ANALYSIS OF EACH PROVISION OF MODIFIED OFFER OF SETTLEMENT

A. Category II Rate Increase

In its Modified Offer of Settlement, Florida Water proposes to settle for an increase of $966,167 in its annual water and wastewater revenue for the discretionary (Category II) issues, or approximately one-half of the amount remaining at issue. This represents an increase of 1.7 percent. In its response to Florida Water's New Offer of Settlement, OPC argued that instead of accepting the utility's revenue requirement proposals, the Commission should decide the amount Florida Water is entitled to receive in the remand proceeding. In its written response, Sugarmill Woods stated that it opposed the offer and that it thought the hearing process should be completed. However, at the August 23, 1999, Special Agenda Conference, Sugarmill Woods represented that it is now in favor of, and OPC represented that it is neither for nor against, our approval of the Modified Offer of Settlement of this case.

In evaluating this Modified Offer of Settlement, we have attempted to quantify the possible outcome of the AADF and lot count methodology issues which are the only issues on remand upon which we were permitted by the Court a choice as to how to proceed. For the lot count issue, approximately $466,971 in additional annual revenue is at stake. For the AADF issue, approximately $1,464,644 in additional annual revenue is at stake. If we do not support a departure from our prior policy concerning the AADF and the lot count methodologies, the utility wold be entitled to the total amount of approximately $1,931,615 in additional annual revenue.

Further, these amounts do not include any allowance for additional rate case expense. Therefore, another factor which must be considered is the time and cost of continuing litigation. Florida Water has estimated that additional rate case expense to date is approximately $400,000, with an estimated $1.1 million in estimated rate case expense through the hearing and appeal process.

Another factor not present when we considered the prior settlement offers in this case is the First DCA's decision in Palm Coast Utility Corp. v. FPSC, Case No. 97-1720 (Fla. 1st DCA May 10, 1999)[Palm Coast -- Docket No. 951056-WS]. In the Palm Coast case, the same Category II issues at issue in the instant case (AADF and lot count) were in dispute and considered by the Court. In Palm

Coast, the Commission staff sponsored a staff witness to present evidence to support the methods used. Notwithstanding this evidence, the Court again overturned our decision to use the AADF and lot count methodologies, finding that the record lacked an adequate basis for the change in methodology. As a result, our confidence that we will be able to support a departure from our prior policy on appeal of these two issues is somewhat diminished.

Based on the above considerations, we find that Florida Water's offer to accept approximately one-half of the amount remaining at issue constitutes a fair, just, and reasonable resolution to this case.

Discussion of Rate Structure

While the rate increase proposed by Florida Water in its Modified Offer of Settlement represents an increase of 1.7 percent, the utility did not indicate how the rates should be calculated. In setting rates for the Category I issues, we strictly adhered to the capband rate structure. In Order No. PSC-99-0093-FOF-WS, we stated that

> [b]ecause this capband rate structure was upheld by the Court on appeal, in calculating rates based on the new revenue requirement, we have strictly adhered to the capband methodology described above. In our opinion, to do otherwise would be a change in rate structure and could be subject to a subsequent appeal.

However, after further extensive analysis of the capband rate structure, we now believe that our previous statement does not apply when calculating rates based upon a settlement offer. The premise behind the calculation of the capband rate structure is that it starts with system stand-alone rates, modifies the stand-alone rates based on a cap of customers' bills at 10,000 gallons, and then groups the remaining systems below the cap based on similar cost as determined by an average bill. In other words, the basis of the capband rate structure, and the starting point for calculating rates using this rate structure, is the system-specific revenue requirement.

Under Florida Water's Modified Offer of Settlement, there is no system specific revenue requirement. The amount of the increase contained therein is simply a revenue amount offered by the utility that it is willing to accept. Nowhere is there any calculation of

how this amount is spread among the issues on remand or even between the water and wastewater systems. Therefore, there is no means of spreading this increase between the water and wastewater services and then among the various systems based on any accurate measure of cost.

Since there is no cost-based method of allocating the revenue increase by system under the Modified Offer of Settlement, we would be left with allocating the increase in the same proportion as the non-discretionary revenue requirement in order to estimate system-specific revenue increases. In other words, the method we would use would be to spread the total settlement offer revenue increase between the water and wastewater services in the same proportion as the non-discretionary revenue requirement. Then these amounts would be spread to the various service areas in the same manner. This method would result in, at best, a rough estimate of the revenue requirement by system since each system is not equally affected by the issues on remand and neither issue affects all systems.

In our opinion, given our inability to calculate a system-specific revenue requirement from an amount which is not cost-based, but which the utility is nevertheless willing to settle for, it makes no sense to fine tune the rate calculations by insisting on a strict adherence to the capband rate structure. Without accurate system stand-alone rates, there would be no way of ensuring that the systems contained in the resulting bands are truly grouped according to similar costs.

For the above noted reasons, we find it appropriate to allocate the proposed settlement amount across the board, without regard to the existing caps. The caps were originally established well over six years ago in Docket No. 920199-WS, on the basis of an affordability determination. The caps have been raised at least twice since the final rates went into effect as a result of the instant docket. Thus, the affordability concern has not been addressed for several years. We find that it would be fair, just, and reasonable to increase all water and wastewater rates by 1.7 percent across the board. This increase will maintain the current level of subsidizations in the capband rates calculated as a result of the non-discretionary items. This across the board increase will also minimize any inequities which could have occurred if the increase had been calculated through the capband rate structure by artificially banding service areas. Thus, we find that this across

the board methodology will not lead to unfairly discriminatory rates.

We note that we have long held that spreading rate increases across the board for interim purposes does not change rate structure. (See Orders Nos. PSC-96-1388-FOF-WS, issued November 19, 1996, in Docket No. 960451-WS and PSC-96-0170-FOF-WS, issued February 6, 1996, in Docket No. 951027-WS.) Similarly, we find that spreading the proposed settlement amount across the board to the existing rates is not a change in rate structure. For these reasons, we recede from our finding in Order No. PSC-99-0093-FOF-WS that to do other than strictly adhere to the capband methodology in calculating rates based on the new revenue requirement would be a change in rate structure.

Rate Increase

Based on the above, and our decision to accept the utility's Modified Offer of Settlement, Florida Water shall be allowed to increase its rates across the board by 1.7 percent. Florida Water shall file revised tariff sheets consistent with our decisions herein. The approved rates shall be effective for service rendered on or after the stamped approval dates on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code, provided the customers have received notice. Florida Water shall provide proof of the date customer notice was given within ten days after the date of the notice.

B. No Surcharges But Creation of Regulatory Asset

Florida Water proposes that both Category I and Category II surcharges be booked as a regulatory asset in the amount of $8.5 million, including interest, as of August 1, 1999, with an appropriate increase for the continuing accrual of the Category II surcharges through the effective date of the Category II rate increase. The utility requests that we authorize recovery of such regulatory asset, to be amortized over 30 years or a shorter period if we deem appropriate, in the utility's next rate case based on the same surcharge methodology previously ordered for Category I surcharges by Order No. PSC-99-0093-FOF-WS. Because Florida Water is not requesting recovery through its rates at this time, it is foregoing any return on this regulatory asset for at least the next three years. We find that this return could amount to approximately $2.59 million of additional revenue over these three

years. Further, no amortization of the asset would occur until it is included in rates.

In its response to this portion of the Modified Offer of Settlement, OPC agreed that we should approve a regulatory asset in lieu of surcharges. However, OPC stated that the proposal was far too heavily weighed in Florida Water's favor on the two discretionary issues. OPC proposed that we determine in this remand proceeding the amount of surcharges Florida Water is entitled to receive book that amount as a regulatory asset.

In its written response, Sugarmill Woods objected to the creation of a regulatory asset, arguing that the booking of "Category I and II surcharges as a regulatory asset would ultimately charge the wrong customers for the surcharges," and that such allocation "on a uniform basis would be a departure from the Commission's policy favoring capband rates." However, at the August 23, 1999 Special Agenda Conference, Sugarmill Woods supported the Modified Offer of Settlement.

We note that there exists some inconsistency in the wording contained in this portion of the Modified Offer of Settlement. First, the offer indicates that there are to be no surcharges and continues with recovery through a regulatory asset to be amortized over 30 years. However, the Modified Offer of Settlement also provides that the recovery of the asset would be based on the same surcharge methodology contained in Order No. PSC-99-0093-FOF-WS.[4] At the August 23, 1999 Special Agenda Conference, after discussions with the utility, the other parties, and our staff, we concluded that the allocation of the regulatory asset among the systems shall be based on the proportion of equivalent residential connections

[4]By Order No. PSC-99-0093-FOF-WS, issued January 15, 1999, we approved a surcharge methodology for Florida Water based upon a base facility surcharge (BFS) to be applied across the board to all systems. This BFS would have been applied, by meter size, to all affected customers for the period of time they were utility customers. For water-only customers who were customers during this time, the utility was to collect these surcharges as a one-time charge. For the wastewater-only customers and the water and wastewater customers, the utility was to collect the surcharges over a six-month time frame. The utility would have had an opportunity to petition for a mechanism to recover any remaining uncollectible amount.

(ERCs) for each system in the test year in this rate case to the total number of ERCs in the test year ending December 31, 1996. The amortization of the regulatory asset shall be amortized over 30 years. Further, we determined that the charge would be collected through the base facility charge (BFC) based on the size of the meter. If a system is sold or if a county rescinds Commission jurisdiction subsequent to the test year, then the portion of the regulatory asset associated with the system sold or those systems in the non-jurisdictional county or counties shall remain with that system or systems. That is, each portion of the regulatory asset shall remain with each individual system in the proportion of its ERCs found in this rate case to the total number of ERCs found for all systems in this rate case for the projected test year ending December 31, 1996.

Regulatory assets are created from rate actions taken by regulatory agencies. Regulatory assets arise from specific expenses or losses that would have been included in determining operating income in one period under the general requirements of the Uniform System of Accounts, but for it being probable that such items will be included in a different period or periods for purposes of developing the rates the utility is authorized to charge. Regulatory assets can also be created in reconciling differences between the requirements of generally accepted accounting principles, regulatory practice and tax laws. A regulatory asset can be used to recover both historic and future costs.

Regulatory assets are commonly used in all of the regulated industries. Rate case expense is an example of a regulatory asset that is created for water and wastewater utilities in every rate case. Rate case expense is an historic cost that is amortized or recovered over a four-year period on a prospective basis. In the instant rate case, we created regulatory assets to recover historic costs from current and future customers. By Order No. PSC-96-1320-FOF-WS, issued October 30, 1996, in this docket, we created a regulatory asset to recover the utility's costs associated with Docket No. 930880-WS (the rate structure investigation). This asset was required to be recovered over a five-year period from all customers during the five-year period, regardless of whether they were customers during the time those costs were incurred. Another regulatory asset was created to recover the historic costs for three Marco Island water supply projects that were abandoned. These costs were amortized over ten years and recovered from both current and future customers.

By creating a regulatory asset, we avoid surcharging customers for past usage. As mentioned above, the amount of the asset as of August 1, 1999, is $8.5 million, including interest. However, the actual amount of the asset would be calculated based upon the effective date of the rate increase for Category II issues. Florida Water estimates that if remand hearings go forward and a subsequent appeal is filed, the surcharge would grow to approximately $13.5 million through August 1, 2001.

We have previously been faced with a similarly complicated and extremely difficult decision regarding the imposition of surcharges to customers of this utility. In Docket No. 920199-WS, we were faced with the task of determining whether surcharges and refunds should be required as a result of a change in rate structure, and, if so, how they should be recovered. Ultimately, by Order No. PSC-98-0143-FOF-WS, issued January 26, 1998, we determined that no refunds and no surcharges should be made.

In making the determination that no refunds or surcharges were appropriate in that case, we struggled with reconciling several court decisions. First, in GTE Florida Inc. v. Clark, 668 So. 2d 971 (Fla. 1996), the Florida Supreme Court mandated that GTE be allowed to recover its erroneously disallowed expenses from the date the erroneous order was issued through a surcharge that could be applied only to customers that received GTE services during the disputed period of time. In so holding, the Court viewed "utility ratemaking as a matter of fairness. Equity required that both ratepayers and utilities be treated in a similar manner." Id. at 972. Subsequently, the First DCA issued its decision in Southern States Utils., Inc. v. FPSC, 704 So. 2d 555 (Fla. 1st DCA 1997). In Southern States, the Court found that the Commission violated the directive of treating the ratepayers and the utility in a similar manner when it ordered a refund to customers who paid more under a uniform rate structure without allowing a surcharge to customers who paid less under the uniform rate structure. Thus, consistent with the GTE and the Southern States decisions, we must establish a method of collecting the surcharge amount that: 1) ensures that neither the utility nor ratepayers receive a windfall as a result of the erroneous Commission order; 2) treats the utility and ratepayers in a similar manner; and 3) allows the utility the opportunity to earn a fair rate of return. In Order No. PSC-98-0143-FOF-WS, we recognized that these objectives are extremely difficult to reconcile in a fashion that is entirely equitable for all involved.

In attempting to fulfill these objectives, we have considered the principles of fairness and equity espoused by both the GTE and Southern States Courts. There are several problems that exist when determining an equitable solution to surcharges. The first is that the affected customers were not given notice of the possibility of retroactive surcharges, and these customers are unable to go back over the past three years and adjust their consumption in order to lower their bills. This is the main policy reason why ratemaking has historically been prospective in nature and retroactive ratemaking has been prohibited. It was also our overriding concern in Docket No. 920199-WS when we were faced with requiring surcharges to customers who paid too little under the uniform rate structure if a refund to those who paid too much were to be allowed. At page 24 of Order No. PSC-98-0143-FOF-WS, issued January 26, 1998, in Docket No. 920199-WS, we determined that, in that instance, it was more inequitable to surcharge customers who had no ability to change consumption or choose to remain a utility customer.

If a surcharge were to be implemented, the dollar impact on the customers in this case would be much greater than the dollar impact on the customers in the GTE case. In GTE, the Court did not address the establishment of a regulatory asset. In this docket, we estimate that establishment of a regulatory asset as proposed by the utility will only increase the bill of a residential customer by seven cents per month. This amount will decrease over time as the regulatory asset is amortized and the customer base increases. Therefore, we find that the impact on customers will be diminished.

Moreover, the ability of the utility to collect from former customers must be considered. Nearly three years have passed since the final rates were first placed into effect. Florida Water has indicated that it experiences customer attrition of up to seven percent per year. This could result in up to 21 percent of the affected customers having moved from the utility's service area. One must consider the ability of the utility to collect surcharges from these customers given the reality that customers that have left the system have little incentive to pay the surcharges. In the likely event that these customers do not pay, Florida Water's only recourse would be through the court system, which may be impractical and costly. We recognized this concern in Order No. PSC-99-0093-FOF-WS, issued in this docket. Consistent with the GTE decision, to keep the utility whole, the remaining customers that were on line during the surcharge period would be responsible for

the surcharge amounts that the utility was unable to collect from the customers that have left the system.

Further, the ability of the remaining customers to pay the surcharge amounts must be considered, especially if they will be responsible for the uncollectible amount related to those customers who have left the system. If the surcharges are too high and customers are not able to pay, the utility may be faced with the decision of disconnecting service. However, this may not be a practical or effective means of collection, especially if there is a large number of customers that do not pay. Pursuant to GTE and Southern States, these uncollectible amounts would also have to be addressed.

We have had extreme difficulty in attempting to reconcile the First DCA's decisions, the Supreme Court's decision, and the various interpretations of those decisions, with the practical aspects of implementation. At page 13 of Order No. PSC-98-0143-FOF-WS, issued in Docket No. 920199-WS, we determined that if the utility cannot, from a practical standpoint, collect the entire surcharge amount, the fairness and equity principles espoused in the Southern States and GTE decisions will not have been fulfilled. Further, in Order No. PSC-99-0093-FOF-WS, we determined that we must approve a surcharge method which is as fair as is practicable and permitted by the facts and complexity of this case. At page 22 of that Order, we found that we had the flexibility in this case to administer surcharges in any equitable manner that the facts will permit.

Considering all of the above arguments, we believe that we must look at the broader ramifications of this Modified Offer of Settlement. We note that the utility is proposing to take only approximately one half of the revenues on the Category II issues to which it would be entitled if we choose not to reopen the record. Further, the utility has agreed not to file for a rate increase prior to June 28, 2002. These two provisions alone appear to be of great benefit to all customers. Therefore, we find that Florida Water's offer to book the surcharges as a regulatory asset is fair, just, reasonable, and not unduly discriminatory and it is hereby approved.

C. Three-Year One-Sided Stay-Out Provision for the Utility

Under this provision of the Modified Offer of Settlement, Florida Water agrees not to file for a rate increase prior to June

28, 2002; provided, however, that if a petition or complaint is filed seeking a decrease in Florida Water's rates and/or the Commission pursues an earnings investigation or decrease in Florida Water's rates, then the three-year stay-out terminates as of the date that such docket is opened and Florida Water may pursue appropriate rate relief. This stay-out provision is not applicable to price indexes and pass throughs, and such rate adjustments shall be allowed. We find that this provision is of direct benefit to all customers and it is hereby approved.

D. Treatment of Rate Case Expense for Reconsideration, Appeals and Remand

In paragraph E. of the Modified Offer of Settlement, Florida Water requests that accrued rate case expense incurred for reconsideration, appeals and remand be deferred and considered in its next rate case. The utility estimates that this amount to date is approximately $450,000. If the case continues to hearing, Florida Water projects that rate case expense will escalate to $1.1 million.

We find that this portion of the Modified Offer of Settlement is reasonable and it is hereby approved. This decision does not address the prudence of any amounts incurred; only that they will be considered in the next rate proceeding. Any issues regarding prudence of rate case expense incurred for reconsideration, appeals and remand will be litigated along with the projected rate case expense of the next rate case.

E. Interim Rate Refunds

By Order No. PSC-96-1320-FOF-WS, we required Florida Water to refund 5.69 percent of wastewater service revenues collected under interim rates for Lehigh, and refund 27.53 percent of wastewater revenues collected for Marco Island. However, in so doing, we ordered a higher interim refund to Marco Island than the amount of interim revenues held subject to refund. This was due to the fact that in Order No. PSC-96-0125-FOF-WS, we only ordered Florida Water to hold 18.19 percent of interim revenues subject to refund. We confessed this error to the Court on appeal.

Further, Florida Water appealed our decision on interim refunds arguing that such refunds should have been set on a company-wide basis. OPC cross-appealed, and took the opposite view that interim refunds should have been ordered on a system-specific

basis. The Court did not find it necessary to address either argument "[b]ecause issues pertaining to refunds may well be moot, once the PSC sets new permanent rates on remand." Southern States Utils., Inc. v. FPSC, 714 So. 2d at 1049. In the Modified Offer of Settlement, the utility proposes no interim refunds. The offer states that "[w]hile Florida Water continues to believe the refund requirement was unlawful, these refunds are eliminated as a result of the Category I rate increases and surcharges approved by the Commission and the Category II rates and surcharges reflected in this Settlement Offer."

In order to evaluate this aspect of the Modified Offer of Settlement, we determined whether interim refunds would be required if the issues of lot count methodology and AADF were decided in Florida Water's favor. Based on our analysis, there would be no wastewater interim refunds to Lehigh, but there would still be an insignificant wastewater interim refund of .01 percent to Marco Island. The approximate amount is $422 annually. Given the insignificant amount of the potential interim wastewater refund to Marco Island wastewater customers, this refund would be extremely difficult to calculate, and would likely only total a few cents to customers. Furthermore, both the City of Marco Island and the Marco Island Fair Water Defense Fund Committee, Inc., support the Modified Offer of Settlement. Therefore, because the affected parties agreed to forgo their potential right to an interim refund, and because of the insignificant amount of any interim rate refund, we find Florida Water's Modified Offer of Settlement proposing no interim rate refunds to be acceptable and it is hereby approved.[5]

F. No Change in AFPI Rates

In subparagraph G. of the Modified Offer of Settlement, Florida Water requests that we not make any changes to AFPI charges and that the escrow requirement be terminated. Most of the issues on remand relate to increases in used and useful plant and, as

[5]We note that, in its written response, Sugarmill Woods initially opposed this provision of the Modified Offer of Settlement, indicating that there may be interim rate refunds due to Sugarmill Woods. However, Sugarmill Woods now supports the Modified Offer of Settlement, and, further, it has been previously determined that there are no interim rate refunds due to Sugarmill Woods.

such, most likely would have a corresponding decrease to the AFPI charges approved for some systems in the Final Order.

In accepting the Modified Offer of Settlement regarding the revenue increase, we note that the amount is not based on any specific system and revenue requirements by system have not been determined. Accordingly, the appropriate amount of AFPI per system cannot be determined.

Next, as we admitted in our appellate brief, some AFPI charges were erroneously decreased in the Final Order. Those AFPI charges should have been capped at the amount approved in previous cases. The escrow requirement relates to those systems for which we admitted error and the escrowed amount relates to the difference between the AFPI charges approved in the Final Order and the previously approved capped amounts. Since we have admitted error on those amounts, we find that it is appropriate to release the funds in the escrow account and cancel the escrow requirement. For those systems where AFPI charges were capped, no changes would result even if a revenue requirement per system were identified.

Moreover, we note that the recent statutory change to lengthen the margin reserve period will increase the prospective amounts of used and useful plant allowed in future rate proceedings. We believe that the role of AFPI will therefore need to be revisited in future rate proceedings, and particularly in Florida Water's next rate case. Based on all the above, and to dispose of this proceeding on remand and ultimately reduce rate case expense charged to the ratepayers, we find it appropriate to approve Florida Water's request to not change AFPI charges. Further, the escrow requirement shall be discontinued and the escrowed funds shall be released to the utility.

G. Acceptance of Settlement Offer Not to Reflect Commission Precedent or Policy and Not Subject to Being Revisited or Reconsidered

Regarding the portion of this provision which proposes that acceptance of the Modified Offer of Settlement not reflect Commission precedent or policy, we find that this is a fairly standard provision for settlements, and is properly contained in any such offer of settlement. However, this Modified Offer of Settlement is not a stipulation, and all parties are entitled to file a motion for reconsideration pursuant to the provisions of Rule 25-22.060, Florida Administrative Code. Therefore, any final

order approving this Modified Offer of Settlement is subject to a motion for reconsideration. Regarding the provision proposing that the Modified Offer of Settlement would not be revisited, if an offer of settlement is approved as final agency action, then the principles of administrative finality are applicable. With these understandings, this portion of the Modified Offer of Settlement is acceptable and is hereby approved.

H. Settlement Offer Not Divisible or Subject to Modification

The utility has merely indicated that this is an all or nothing settlement offer. With the utility having modified its offer at the August 23, 1999 Special Agenda Conference, it has deleted the portions of the New Offer of Settlement that our staff found objectionable. We find that the Modified Offer of Settlement is acceptable in its entirety.

Conclusion

Based on the foregoing, we find that the utility's Modified Offer of Settlement is in the public interest and it is approved. The Category II rates as contained therein shall be calculated as an across the board increase. We hereby reconsider our decision menorialized by Order No. PSC-99-0093-FOF-WS to reopen the record and conduct further proceedings and find that no hearing on remand is necessary. Moreover, Sugarmill Woods' pending protest to the proposed agency action portion of Order No. PSC-99-0093-FOF-WS concerning surcharges is mooted by our decision to approve the Modified Offer of Settlement because there is no assessment of a surcharge and no surcharge methodology in dispute. For these reasons, the Chairman's Office has canceled the February 2-4, 2000, hearing.

OPC'S MOTION TO CONSOLIDATE

Along with its Response to Florida Water's Motion for Approval of New Offer of Settlement, OPC moved to consolidate this docket with the utility's gain-on-sale docket, Docket No. 980744-WS. In paragraph 6. of its response, OPC states that if the gain on the sale of Florida Water's systems in Orange County and the gain on the sale of a laboratory in Volusia County are decided in favor of the citizens, the amount of the gain on sale could be used to offset the surcharge (regulatory asset) decided upon in Docket No. 950495-WS, and perhaps even eliminate the need for any surcharge (regulatory asset). OPC argues that netting the impact of these

two proceedings would provide greater regulatory predictability to customers and provide a more even-handed approach to all parties.

Florida Water timely filed a Response in Opposition to OPC's Motion to Consolidate on Jule 12, 1999. In its argument, Florida Water cites to Rule 28-106.108, Florida Administrative Code, which states that "[i]f there are separate matters which involve similar issues of law or fact, or identical parties, the matters may be consolidated if it appears that consolidation would promote the just, speedy and inexpensive resolution of the proceedings, and would not unduly prejudice the rights of a party."

Based on this rule, Florida Water argues that the two used-and-useful issues left open by the First DCA are in no way similar to the gain-on-sale issues in Docket No. 980744-WS. Moreover, Florida Water argues that OPC wishes to consolidate post-test year revenue items into this rate case remand proceeding while ignoring Florida Water's post-test year increased investments and expenses. Florida Water states that such an approach would violate the basic tenets of ratemaking (i.e., would skew the ratemaking equation) and clearly prejudice the rights of Florida Water.

Also, Florida Water argues that consolidation would violate the mandate of the First DCA in this case. In making this argument, Florida Water cites to Basic Energy Corp. v. Hamilton Co., 667 So. 2d 249, 250 (Fla. 1st DCA 1995), and Doctors' Osteopathic Medical Center v. Department of Health & Rehabilitative Services, 459 So. 2d 1063 (Fla. 1st DCA 1984). In Basic Energy Corp., the First DCA stated that:

> [a] trial court's role upon the issuance of a mandate from an appellate court becomes purely ministerial and its function is limited to obeying the appellate court's order or decree. . . . A trial court does not have discretionary power to alter or modify the mandate of an appellate court in any way, shape or form.

Florida Water argues that the mandate issued by the First DCA in this case was a specific mandate, as opposed to a general mandate. Florida Water contends that a specific mandate limits the lower tribunal to proceedings on remand which conform to the specific language used by the court in reversing the lower tribunal. In Basic Energy Corp., the First DCA specifically stated that "[a] remand phrased in language which limits the issues for

determination will preclude consideration of new matters affecting the cause." Basic Energy Corp. v. Hamilton Co., 667 So. 2d at 250. Florida Water argues that the First DCA only gave the Commission discretion on two issues, lot count and AADF, and that to open up the proceeding to other issues would be in violation of the mandate.

We find that consolidation would not promote the just, speedy and inexpensive resolution of the remand proceedings. Further, based on our decision to accept the Modified Offer of Settlement, we find that there is no longer any need for consolidation. The outcome of the gain-on-sale docket, which is proceeding, is not contingent on our decision herein, and will have its own effect on the rate base of the utility. Therefore, OPC's Motion to Consolidate is denied.

MOTION FOR RECONSIDERATION OF ORDER NO. PSC-99-1199-PCO-WS

As noted in the background, the utility filed a Motion for Reconsideration of Order No. PSC-99-1199-PCO-WS. By that Order, issued June 14, 1999, the Prehearing Officer ordered the utility to respond to those portions of OPC's Second Set of Interrogatories and Third Request for Production of Documents to which the utility had raised no objection within 23 days of the effective date of the Order. These discovery requests were served on the utility on April 9, 1999.

Given our decision to accept the Modified Offer of Settlement and the cancellation of the scheduled hearing, discovery is no longer necessary. Therefore, we find that the Motion for Reconsideration is moot and it is unnecessary for us to rule upon it.

CLOSING OF DOCKET

Because we approve the utility's Modified Offer of Settlement, final rates and charges are set and no refunds are required. Because no further action is required, upon the filing of the appropriate tariff sheets and proof of notice to the utility's customers, this docket shall be closed administratively.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that Florida Water Services Corporation's Modified Offer of Settlement is hereby approved as set forth in the body of this Order. It is further

ORDERED that the regulatory asset approved as set forth in the body of this Order shall be allocated among the systems as set forth in the body of this Order. It is further

ORDERED that the allocated portion of the regulatory asset shall remain with each system as set forth in the body of this Order. It is further

ORDERED that the escrow requirement for the allowance for funds prudently invested charges shall be discontinued and the escrowed funds shall be released to the utility. It is further

ORDERED that Florida Water Services Corporation shall increase its rates as set forth in the body of this Order. It is further

ORDERED that Florida Water Services Corporation shall file revised tariff sheets consistent with our decision herein. It is further

ORDERED that the approved rates shall be effective for service rendered on or after the stamped approval dates on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code, provided the customers have received notice. It is further

ORDERED that Florida Water Services Corporation shall provide proof of the date customer notice was given within ten days after the date of the notice. It is further

ORDERED that the Office of the Public Counsel's Motion to Consolidate is denied. It is further

ORDERED that upon our staff's verification that the appropriate tariff sheets and customer notice have been provided consistent with our decision herein, this docket shall be closed administratively.

By ORDER of the Florida Public Service Commission this 14th day of September, 1999.

Blanca S. Bayó

BLANCA S. BAYÓ, Director
Division of Records and Reporting

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water and/or wastewater utility by filing a notice of appeal with the Director, Division of Records and reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.