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100104-WS

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Sent: Friday, June 17, 2011 2:43 PM
To: Filings@psc.state.fl.us
Cc: Gene Brown; Maggie McCall Moody; Ralph Jaeger; Rosanne Gervasi
Subject: e-filing (Dkt. No. 100104-WS)
Attachments: 100104.response.sversion.doc

Electronic Filing

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b. Docket No. 100104-WS

In re: Application for increase in water rates in Franklin County by Water Management Services, Inc.

c. Document being filed on behalf of Office of Public Counsel

d. There are a total of 7 pages.

e. The document attached for electronic filing is OPC's Response to WMSI's Motion to Allow Installment Payment of Regulatory Assessment Fee.
(See attached file: 100104.response.sversion.doc)

Thank you for your attention and cooperation to this request.

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DOCUMENT NUMBER-DATE

04182 JUN 17 =

FPSC-COMMISSION CLERK

6/17/2011

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for increase in water)
rates in Franklin County by Water)
Management Services, Inc.)

Docket No. 100104-WU
Filed: June 17, 2011

**OPC'S RESPONSE TO WMSI'S MOTION TO ALLOW INSTALLMENT
PAYMENT OF REGULATORY ASSESSMENT FEE**

Pursuant to Rule 28-106.204, F.A.C., the Citizens of the State of Florida, through the Office of Public Counsel, hereby respond to Water Management Services, Inc's (WMSI) Motion To Allow Installment Payment of Regulatory Assessment Fee.

On June 8, 2011, WMSI filed its Motion To Allow Installment Payment of Regulatory Assessment Fee ("Motion"). WMSI filed the Motion in the docket that was opened to process and consider WMSI's most recent revenue requirements proceeding. In its final order in this docket, the Commission directed its Staff to conduct a cash flow audit to determine whether the levels of balances in Account 123, "Investments in Associated Companies," are appropriate or whether, as OPC contended at the evidentiary hearing, WMSI has been and is subsidizing the President of WMSI and his unregulated businesses. See Order No. PSC-11-0010-SC-WU, at page 51.¹

Under normal circumstances, OPC likely would not respond to a request for leave to extend the deadline for payment of regulatory assessment fees. However, in this instance WMSI is attempting to support its Motion with schedules that are related directly to the cash flow audit that the Commission ordered in the rate case, which in turn stems from an issue in which OPC

¹ The evidence proved that WMSI's Account 123 showed a net outflow of advancements to unregulated entities of \$1.2 million during time frames in which WMSI has claimed financial hardship and difficulty in borrowing funds for operations. WMSI has not received interest or a return on these advances. OPC's position in the case was that the Commission should place WMSI on notice that the Commission would impute earnings on advances remaining in WMSI's next revenue requirements case and offset any calculated revenue deficiency by the amount of imputed earnings. WMSI countered by claiming that, notwithstanding the balance of Account 123, its President and an unregulated affiliate have been subsidizing the utility over time. The Commission declined to adopt OPC's position. Instead, it directed its Staff to perform a cash flow audit that would establish definitively, in a way that would inform the Commission as to appropriate next steps, the nature and extent of cash transfers between WMSI, on the one hand, and its President and/or the President's unregulated businesses, on the other.

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was heavily engaged during the proceeding. Moreover, even a preliminary review of the schedules reveals that they support neither WMSI's contention regarding its financial position nor its claim that the nonutility entities to which WMSI has advanced more than \$1.2 million (net outstanding balance calculated during the rate case hearing) have been subsidizing the utility. If anything, the attachments to WMSI's motion contain red flags signaling that they need to be scrutinized and investigated carefully during the course of the Commission Staff's cash flow audit. Examples of issues and concerns that become apparent after an initial review include the following:

Assertion that the Utility Lost Over \$500,000 in 2010 is Misleading

The Motion asserts, under item 2, that "...the utility lost over \$500,000 in 2010, as shown by its 2010 annual report." WMSI then refers to an Exhibit "A", which provides a single page from its 2010 Annual Report filed with the Commission. While the single page that was provided shows Net Income for 2010 of (\$504,038), when entries on other pages are reviewed it becomes clear that the net income shown on this single page is misleading. The \$504,038 loss shown on the page provided is not a cash flow statement. The purported loss includes several non-cash items, such as \$199,395 of net depreciation expense (shown on the prior page of the full Annual Report) and \$58,436 for the amortization of debt discount and expense.

Also included would be several expense items that were disallowed in the rate case decision in Docket No. 100104-WU. For example, the amount includes \$115,192 for the compensation of Gene Brown and \$69,745 for the compensation of Sandra Chase. The recent order disallowed part of Ms. Chase's salary and allocated part of Mr. Brown and Ms. Chase's salaries to affiliates. The purported loss amount would also include depreciation expense and interest expense on vehicles that were fully or partially disallowed by the Commission.

Also included in the \$504,038 net loss on the income statement is \$294,845 of interest expense. The 2010 Annual Report filed with the Commission, at page F-17, shows total long term debt of \$5,236,908 and outstanding Notes Payable of \$2,859,129 resulting in combined debt outstanding of \$8,096,037. As was pointed out in the recent WMSI rate case, the amount of debt on the utility's books far exceeds the amount of rate base. Schedule No. 1-A in Docket No. 100104-WU shows the Commission-allowed rate base was \$3.74 million. The same exhibit shows total allowed plant in service of \$8.8 million and Contribution in Aid of Construction of \$3.2 million. This would result in net plant not funded through contributions of \$5.6 million (\$8.8M - \$3.2M). Clearly, the amount of debt on WMSI's books far exceeds the rate base and the amount it has invested in plant assets, and results in inordinately high levels of interest expense. One objective of the cash flow audit ordered by the Commission should be to gauge whether WMSI advanced funds to unregulated businesses that could and should have been used to pay down debt, thereby lowering interest expense and increasing net income.

The Contention that WMSI Management and Affiliates have been Subsidizing the Operations of the Utility for Many Years is not Supported by the Information Provided in the Motion

The Motion contends, under item 3, that "The management and affiliates of the utility have been subsidizing the operations of the utility for the benefit of its ratepayers for many years, as shown by the general ledgers filed with the Commission's audit staff in this docket...and by the annual reports on file with this Commission." Attached to the Motion is Exhibit "B", which WMSI asserts shows the "extent of this subsidy." WMSI claims that the exhibit consists of "summaries of the financial facts." OPC disagrees that the information provided by WMSI in Exhibit B demonstrates that "management and affiliates" have been subsidizing the operations of the utility. While OPC has not conducted an audit of the financial information and accounting records used by WMSI in preparing the various items in Exhibit B, OPC does have many

concerns with the limited information that was provided in the exhibit. Here are a few examples of problems, questions or concerns with the information provided in Exhibit B:

WMSI Financial Sources and Uses 2010

- This document is not a cash flow statement and should not be interpreted as being a cash flow statement.
- This document shows “Utility Plant Additions” purportedly funded by ratepayers of \$218,294 and “Remainder of Utility Plant Additions” of \$267,209, resulting in combined utility plant additions in 2010 of \$485,503. The 2010 Annual Report filed with the Commission, at pages W-4(a) and W-4(b), shows a net decrease in plant between 2009 and 2010, and page W-4(a) identifies utility plant additions of only \$98,094. The Balance Sheet, at page F-1(a) of the Annual Report does show that Nonutility Property increased by \$278,645 between 2009 and 2010; however, this is *Nonutility Property*, not utility assets. Page F-9 of the annual report shows the addition of \$325,800 of Non-Utility Land. One must question why the purchase of non-utility property or non-utility assets is included in the “Financial Sources and Uses” analysis presented in Exhibit B of the Motion.
- There is no indication of how the \$150,701 adjustment to “convert from accrual to cash basis” was determined by WMSI. It is clear that non-cash items are included in prior lines of the analysis, but no explanation of this conversion adjustment is provided.
- Included is \$330,080.70 identified as “Utility Expenses not included on W-10(a) above.” The Utility Expenses shown for page W-10(a) are \$1,115,100 and tie exactly into the Utility Operating Expenses on page F-3(a) and page W-10(a) of the annual report. WMSI does not identify, much less support, the specific expenses it wishes to add to Utility Expenses already reported as utility operating expenses in the Annual Report to the Commission. The interest payments and tax expenses are already separately included in the analysis, and expenses such as depreciation are non-cash items.
- The analysis identifies cash received from third parties, with no indication of what that cash is for, how it was determined, or from whom it was received.

Water Management Services, Inc. – Cash Flow Deficit (Composite Exhibit “B”)

- This is a high level comparison showing what is claimed to be all “Cash in from Ratepayers” and all “Cash Out per Checkbooks,” resulting in purported cash operating deficit amounts by year for the period 2000 through 2010. This is not representative of a complete or accurate cash flow analysis.
- It is clear from the record of the rate case that WMSI, Gene Brown and Brown Management Group have extensively intermingled funds with constant cash inflows and outflows between WMSI, Mr. Brown and Brown Management Group.

- The “Cash Flow Deficit” does not reflect other cash coming in, such as the net cash received as a result of the settlement relating to the failure of the paint coating on the water supply main attached to the bridge to St. George Island and the proceeds received as part of the loan for the bridge from the DEP.

Water Management Services – Cash Flow

- This appears to merely show the total deposits and total checks written from the various bank accounts. As previously noted, it would include the impact of the extensive intermingling of funds between WMSI, Gene Brown and Brown Management Group.

The above listed items are merely a few examples of the concerns or problems with the purported analysis presented by WMSI in its Exhibit B attached to the Motion. A complete and thorough evaluation of WMSI’s cash flow and intermingling of cash and investments between WMSI, Mr. Brown and Brown Management Group and potentially other affiliates should entail a detailed analysis of not only WMSI’s general ledgers, but also of WMSI’s bank statements and the bank statements, general ledger and finances of Mr. Brown, Brown Management Group and any other affiliates from which cash has flowed into or out of WMSI over a historic period. Only such a detailed analysis can assess Mr. Brown’s claim that the proceeds of personal loans have been used to pay the utility’s financial obligations in amounts that exceed the net advances to unregulated entities recorded in Account 123. Page 2 of the letter provided with Exhibit B, dated May 20, 2011, indicates that WMSI has not been able to document all of the personal loans of Mr. Brown and WMSI’s affiliates that were used to purportedly subsidize the utility operations.² Given the extensive intermingling of funds and assets, as well as the frequent transfers of funds and assets, coupled with Mr. Brown’s contention that he has been unable to document all of the personal loans, very little reliance should be placed on the information

² OPC notes that it is one thing to demonstrate that a personal loan was obtained; it is quite another to demonstrate, through appropriate documentation, that the proceeds of the personal loan were used to defray costs or expenses of the utility operation. That is one of the subjects of the cash flow audit.

provided by WMSI in Exhibit B in support of its Motion. Rather, a detailed and comprehensive analysis of the books of WMSI, Gene Brown, and Brown Management should be undertaken.

CONCLUSION

OPC takes no position on WMSI's request to pay regulatory assessment fees over five months, *per se*. However, OPC disputes WMSI's assertion that its request is supported by the attachments to its Motion. If in its discretion the Commission authorizes the installment payments requested by WMSI, it should make clear in its order granting the Motion that it does so without relying on the attached schedules. In addition, the Commission should not accept the schedules as satisfying the purposes of the cash flow audit that it ordered in Order No. PSC-11-0010-SC-WU, and should direct its Staff to perform all tests and conduct all analyses necessary to assess the schedules and independently determine the nature and extent of cash flows between WMSI and unregulated entities.

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CERTIFICATE OF SERVICE
DOCKET NO. 100104-WU

I HEREBY CERTIFY that a true and correct copy of the foregoing OPC's Response to WMSI's Motion to Allow Installment Payment of Regulatory Assessment Fee has been furnished by electronic mail and/or U.S. Mail to the following parties on this 17th day of June, 2011.

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