State of Florida

Public Service Commission

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DATE: March 15, 2012

TO: Office of Commission Clerk (Cole)

FROM: Division of Economic Regulation (Springer, Daniel, Fletcher, McRoy, Stallcup, Thompson)
Office of the General Counsel (Brown)

RE: Docket No. 110264-WS – Application for increase in water and wastewater rates in Pasco County by Labrador Utilities, Inc.

AGENDA: 03/27/12 – Regular Agenda – Proposed Agency Action – Except for Issue Nos. 19 & 20 - Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Graham

CRITICAL DATES: 03/30/12 (5-Month Effective Date (PAA Rate Case))

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\110264.RCM.DOC

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Case Background

Labrador Utilities, Inc. (Labrador or Utility) is a Class B utility providing water and wastewater service to approximately 767 water and 754 wastewater customers in Pasco County. Water and wastewater rates were last established for this Utility in its 2008 rate case.[1]

On September 27, 2011, Labrador filed its application for a rate increase at issue in the instant docket. The Utility's application did not meet the minimum filing requirements (MFRs). On October 31, 2011, the Utility provided corrections to its MFRs. Upon review of the MFRs, staff determined that the MFRs were complete. Therefore, the official filing date was established as October 31, 2011. The Utility requested that the application be processed using the Proposed Agency Action (PAA) procedure and requested interim rates.

By Order No. PSC-11-0573-PCO-WS, issued December 12, 2011 (Interim Order), the Commission authorized the collection of interim water and wastewater rates, subject to refund, pursuant to Section 367.082, Florida Statutes (F.S.). The approved interim revenue requirement for water is $285,793, which represents an increase of $39,180 or 15.89 percent. The approved interim revenue requirement for wastewater is $495,882, which represents an increase of $53,416 or 12.07 percent.

The test year established for final rates is the simple-average period ended December 31, 2010. The Utility requested final revenue increases of $106,066 (42.5 percent) for water and $103,778 (23.3 percent) for wastewater.

On October 6, 2011, the Office of Public Counsel (OPC) filed a Notice of Intervention in this docket, and an order acknowledging intervention was issued on October 7, 2011.[2]

On January 18, 2012, Forest Lake Estates Co-op, Inc. (Forest Lake or Co-op) filed a Motion of Intervention in this docket, which is pending at this time.

On March 6, 2012, Forest Lake filed a Motion to Dismiss or Abate (Motion) the instant case. On March 9, 2012, OPC and the Utility filed their respective responses to the Motion. No party requested oral argument on the motion, pursuant to Rule 25-22.0022, Florida Administrative Code (F.A.C.), but staff notes that the Commission has the discretion to hear oral argument on all matters over which it presides.

This recommendation addresses Labrador's request for final rates and Forest Lake's Motion to Dismiss Labrador's rate case. The Commission has jurisdiction pursuant to Section 367.081, F.S.

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[1] See Order Nos. PSC-09-0462-PAA-WS, issued January 22, 2009, and PSC-09-0711-AS-WS, issued October 26, 2009, in Docket No. 080249-WS, In re: Application for increase in water and wastewater rates in Pasco County by Labrador Utilities, Inc.

[2] See Order PSC-11-0445-PCO-WS.

Discussion of Issues

Issue 1: Should the Commission grant Forest Lake Estates Co-op, Inc.'s Motion to Dismiss or Abate this case?

Recommendation: No, the Commission should deny the Motion to Dismiss or Abate this case. Labrador should provide the Commission quarterly status reports on the course of Circuit Court Case No. 51-08-CA-4033-ES/B. (M. Brown)

Staff Analysis: On June 10, 1999, Forest Lake and Labrador Services, Inc., the predecessor in interest to Labrador, executed a commercial lease of the property on which Labrador operates its water and wastewater plants and an irrigation spray field. On February 22, 2012, in the matter of Forest Lake Estates Coop, Inc. v. Labrador Utilities, Inc., Pasco Circuit Case No. 51-08-CA-4033-ES/B, the Co-op filed a Motion for Leave to Amend its Complaint against Labrador. The amended complaint included a count requesting judicial recognition of the Co-op's termination of the Commercial Lease and the entry of an eviction judgment against Labrador. To date, the Court has not issued an order addressing the merits of Forest Lake's complaint.

In its Motion to Dismiss or Abate, Forest Lake argues that the rate case should be dismissed because the Utility no longer has any legally enforceable rights to use of the land under the Commercial Lease since the Co-op has now terminated the lease. Alternatively, Forest Lake argues that the rate case should be abated until the issue of the Utility's rights under the Commercial Lease, if any, is resolved in the Pasco Circuit Court litigation. In support of its argument, the Co-op stated that the Commission has consistently ruled that utilities must provide proof of compliance with Section 367.1213, F.S. and Rule 25-30.433, F.A.C., prior to receiving a rate increase. Forest Lake cites four Commission decisions that it claims support that contention.[3]

On March 9, 2012, OPC filed its response to the Co-op's Motion. OPC asserts that if Labrador voluntarily elects to extend the five-month statutory deadline for this case, the Commission could issue an order abating all activities until the lease litigation is resolved. OPC further asserts that if the abatement is ordered by the Commission, Labrador would be authorized to continue to collect from ratepayers the interim rate increase authorized by the Commission until such time as the lease litigation is resolved. OPC also contends that if the litigation is resolved in favor of the Utility, the abatement would end and the case would resume at the point it was abated. If the litigation is resolved in favor of the Co-op, the case would be dismissed and the docket closed after the Utility refunded the interim rate increase to the customers with

[3] See Order Nos. PSC-00-2054-PAA-WS, issued October 27, 2000, in Docket No. 990939-WS, In re: Application for rate increase in Martin County by Indiantown Company, Inc. (utility received rate increase and was ordered to obtain a long-term lease for land); PSC-94-0075-FOF-WS, issued January 21, 1994, in Docket No. 921261-WS, In re: Application for rate increase in Lee County by Harbor Utilities Company, Inc. (utility received rate increase and was ordered to provide documentary support of land ownership); PSC-02-1168-PAA-WS, issued August 26, 2002, in Docket No. 01-0869-WS, In re: Application for staff-assisted rate case in Marion County by East Marion Sanitary Systems, Inc. (utility received rate increase and was ordered to purchase or lease land within six months); PSC-00-2117-PAA-SU, issued November 7, 2000, in Docket No. 000090-SU, In re: Application for limited proceeding rate increase in Lee County by Useppa Island Utility, Inc. (utility received rate increase and was ordered to provide deeds showing the correct land description within 90 days of the order)

interest. OPC asserts that, if Labrador refuses to extend the five-month statutory deadline until the lease litigation is resolved, the Commission should dismiss Labrador's rate increase filing as being fatally flawed, and refund to customers the interim rate increase with interest.

On March 9, 2012, Labrador filed its response to the Co-op's Motion. Labrador states that the Lease provides that rents increase every six (6) years based upon an increase in the Consumer Price Index. According to the Utility, neither it nor Forest Lake realized the increase in rent occurred in June 2011, until the Co-op realized it in August 2011, and advised Labrador accordingly. In January 2012, Labrador states that Forest Lake advised it in writing that it was in default for failure to pay the increased amount of the Lease payments. Labrador contends that, due to the manner in which the rent payments were broken down on the demand letter, the letter was misread and Labrador sent the Co-op a check for $3,744.00, which was actually only for Parcel 3. The Utility stated that Forest Lake subsequently returned that check because Labrador omitted the $1,497.60 due on Parcels 1 and 2, and then demanded that Labrador immediately quit, surrender, and return to Forest Lake all of the leased premises.

Labrador argues that the Co-op's assertion that the Utility has no legally enforceable rights under the Lease is incorrect. Until a court rules otherwise, Labrador asserts, it continues to enjoy all of its rights under the Lease. As such, Labrador contends that it is in complete compliance with Section 367.1213, F.S., and Rule 25-30.433(10), F.A.C. Furthermore, Labrador contends that if the Lease is terminated, the Utility would exercise its rights of eminent domain pursuant to Section 361.04 and 361.07, F.S., and thereby maintain its rights to the water and wastewater treatment plant lands and spray irrigation site.

Standard of Review

A motion to dismiss challenges the legal sufficiency of the facts alleged in a petition to state a cause of action. Meyers v. City of Jacksonville, 754 So. 2d 198, 202 (Fla. 1st DCA 2000). The standard to be applied in disposing of a motion to dismiss is whether, with all the allegations in the petition assumed to be true, the petition states a cause of action upon which relief can be granted. Id. When making this determination, only the petition and documents incorporated therein can be reviewed, and all reasonable inferences drawn from the petition must be made in favor of the petitioner. Varnes v. Dawkins, 624 So. 2d 349, 350 (Fla. 1st DCA 1993); Flye v. Jeffords, 106 So. 2d 229 (Fla. 1st DA 1958), overruled on other grounds, 153 So. 2d 759, 765 (Fla. 1st DCA 1963).

Analysis

Section 367.1213, F.S., states:

> A utility under the Water and Wastewater System Regulatory Law must own the land or possess the right to continued use of the land upon which treatment facilities are located. The commission shall adopt rules in accordance with this section.

Rule 25-30.433(10), F.A.C., states:

> A utility is required to own the land upon which the utility treatment facilities are located, or possess the right to the continued use of the land, such as a 99-year lease. The Commission may consider a written easement or other cost-effective alternative.

Since the Co-op's complaint is currently pending in Circuit Court, and no final judgment has been issued, it appears to staff that the Utility enjoys all of its rights under the Lease at this time, in compliance with Section 367.1213, F.S., and Rule 25-30.433(10), F.A.C. Further, staff disagrees with Forest Lake's interpretation of the four Commission decisions cited in its Motion. First, in those cases the Commission did not withhold a rate increase until the land was secured, but rather approved a rate increase and required the land be secured by a time certain. Second, this case is distinguishable in that Labrador presently appears to have the land secured until otherwise ruled on by the Court and ultimately enjoys the right of Eminent Domain should the Lease be terminated by the Court.

Conclusion

Based on the above, staff recommends that Forest Lake's Motion to Dismiss or Abate should be denied. Labrador's petition for a rate increase adequately states a cause of action upon which the Commission can grant relief. Since this rate proceeding is being addressed as a Proposed Agency Action (PAA), a substantially interested person would have the opportunity to protest the PAA and raise the question of land ownership in an evidentiary proceeding. Further, staff recommends that Labrador provide the Commission quarterly status reports on the course of the Circuit Court litigation.

QUALITY OF SERVICE

Issue 2: Is the quality of service provided by Labrador satisfactory?

Recommendation: Yes. The overall quality of service provided by Labrador is satisfactory. (McRoy)

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

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

In Pasco County, the water and wastewater programs are regulated by the Southwest Florida Water Management District (SFWMD) and the DEP. Labrador's General Water Use Permit was issued by the SFWMD on February 15, 2011, and will expire on February 15, 2021. On March 9, 2010, the DEP conducted a Sanitary Survey of the Labrador water treatment plant (WTP) with no deficiencies noted during the inspection.

Labrador's wastewater permit was issued on March 23, 2010, and will expire on March 22, 2015. On October 6, 2010, the DEP conducted a compliance inspection of the Labrador wastewater treatment plant (WWTP). The WWTP was found to be in compliance, although deficiencies related to reporting and excess vegetation covering the spray field were noted. In addition, DEP strongly recommended replacing the charcoal filter media before the seasonal residents arrived. Labrador indicated that the filter media is routinely changed out.

Labrador is currently in compliance with all of the required chemical analyses and has met all required standards for both water and wastewater operations. The Utility has no outstanding consent orders or warning letters. A staff field investigation of Labrador was conducted on January 18, 2012. Staff found no apparent problems with the operations of either the water or wastewater facilities. Based on a review of the maintenance records and a physical inspection, the general condition of the facilities appeared to be adequate. Therefore, staff recommends that the quality of drinking water delivered to the customers, the wastewater effluent quality, and the operating condition of the Utility's water and wastewater plants and facilities are satisfactory.

The Utility's Attempt to Address Customer Satisfaction

A customer meeting was held on January 18, 2012, inside Labrador's service territory at the Forest Lake Estates Community Clubhouse near Zephyrhills, Florida. Over 300 customers attended the evening meeting, and 22 customers spoke. Citing affordability concerns, the attendees were generally against the proposed rate increases for water and wastewater. Water quality in particular was cited as a reason for not justifying the rate increases. Although it was acknowledged that the water provided by the Utility met DEP health and safety standards, general consensus among the attendees was that the water was considered unfit to consume and not worth the rate increases because of the frequent taste, odor, and discoloration problems. One rust-colored, used filter from a home filtering device and one water sample was provided by customers as physical evidence to prove the questionable quality of the water. Several customers indicated that quality had not improved since the last rate case, while one customer made comments about public noticing concerning Precautionary Boil Water Notices (PBWNs).

The Utility's compliant log for the test year (2010) indicated that approximately 40 customer complaints were received. The majority of the water complaints during this time dealt with laundered clothing being discolored, sediment and discoloration in the water, taste, odor, and low or no water pressure. For wastewater, the main complaints received by the Utility during the test year were about odor emanating from the wastewater treatment plant.

Since 2010, there have been 4 complaints filed with the Commission. Two of the complaints related to improper bills, one complaint related to outages, and the other related to quality of service. There are currently no active complaints on file at the Commission.

The Commission also received a petition on December 15, 2011, signed by 114 customers as well as approximately 25 letters that reflected concern over the effect of the proposed rate increases and the quality of the water and wastewater service provided by Labrador.

According to the Utility, a polyphosphate sequestrate is added to the water supply at the treatment plant in order to keep the iron in the source water from precipitating out of the water. The Utility believes this has proven to be an effective means of addressing the color in the water when coupled with a periodic flushing program. The Utility flushes the remote locations in the distribution system on a monthly basis. In order to verify that adequate polyphosphate is being added, Utility staff monitor the concentration of phosphate in the water at least weekly. In addition, Labrador believes it is responsive to individual customer complaints by visiting the customer, identifying the issue, and then taking appropriate action to remedy the situation. In some cases, the Utility provides the customer with an iron removal product, at no cost to the customer, to assist in removing iron deposits from clothing.

Currently, the Utility has no plans to make additional capital improvements to the water treatment process, primarily because all of the parameters indicate compliance with DEP's rules and regulations. The Utility stated it would certainly entertain discussions with the customers regarding potential enhancements to the current treatment methodology provided there was a willingness on the part of the customer base to support such expenditures with full understanding of the impact to their water rates.

In reference to PBWNs, the Utility's records indicate that the last system-wide water outage occurred on December 3, 2010, and was due to a water main leak in the community. When PBWNs are required, the Utility indicates that the customers are notified by multiple methods of communications. For all PBWNs, no matter how many customers are affected, an outbound telephone message is made to all affected customers who have an active phone number posted on their account. The message format includes identifying that the caller is Labrador Utilities with important information. This is followed by specific information regarding the PBWN and concludes with the toll-free customer service number to call if the customer has any questions. Once the PBWN is rescinded, another reverse 911 call is issued to the same customers notifying them that the PBWN is no longer in effect.

Depending on what time the disruption of service or water outage occurs, Labrador's field staff notifies the Forest Lake Estates office. The Forest Lakes Estates general manager has agreed to post PBWNs issued by Labrador on the community's Closed-Circuit Television (CCTV) channel, which is available to those who subscribe to Brighthouse Networks for cable service. This method is most commonly used when a PBWN is issued during normal business hours when the Forest Lake Estates office is staffed. Once the PBWN is rescinded, Labrador notifies the office that the PBWN is no longer in effect.

In the case of a PBWN that requires notifying the whole community, signs are placed at both entrances to Forest Lake Estates. Once the PBWN is rescinded, the signs are updated to reflect the rescission date. If the PBWN affects a small number of customer connections, the PBWN is attached to door hangers and left on the door of the affected customers' homes. Historically, water outages are typically limited to specific streets or portions of the distribution system in order to make repairs. Once the PBWN is rescinded, notices are hung on the same doors with the news that the PBWN is no longer in effect.

In the Utility's last rate case,[4] the Commission approved a settlement agreement between Labrador and Office of Public Counsel in which the Utility agreed to work with customer representatives to study the WWTP odor problem and if necessary, propose cost effective measures to address the odor problem. In April 2011, Utility staff met on site with Forest Lake Estates Co-op's ("FLEC") attorney and engineering consultant, who toured the plant and lift station in order to observe the operation of the facilities and identify if plant operations was contributing to the production of malodors. If the consultant observed the presence of malodors, the consultant was to offer recommendations in his report that addressed the situation. The Utility and FLEC are currently in litigation regarding odor from the WWTP.

According to the Utility, several steps have been taken to try to control odors resonating from the WWTP. The carbon media in the filtration units are routinely changed out to maintain the functionality of the carbon media. Historically, the filer media lasts about 12 months before the granular carbon becomes saturated and no longer performs satisfactorily.

Chemical feed equipment was installed at the master lift station to reduce the production of hydrogen sulfide gas at the WWTP headworks. The Utility indicated that it has been using Bioxide for over two years with great success. The chemical feed pump is interconnected with the sewage pump controls so that the chemical is injected into the force main header pipe at the optimum concentration to maximize the effectiveness of the product.

[4] See Order No. PSC-09-0711-AS-WS, issued October 26, 2009, in Docket No. 080249-WS, In re: Application for rate increase in Pasco County by Labrador Utilities, Inc., pp. 5-10

A cover was installed over the rotating screen at the headworks and the grit chute was modified so that the chute drops into a hole in the lid of the dumpster in order to minimize odors. The dumpster is emptied on a frequent basis in order to avoid the material removed by the rotating screen from becoming malodorous.

In order to improve visibility and ease of maintenance, the Utility installed clear plastic covers on both equalization tanks at the plant headworks. The lighter panels allow a single person to perform necessary maintenance that previously required two people. In addition, the Utility installed forced air ventilation and charcoal filtration at the equalization tanks.

Modifications were made to the operation of a clarifier to improve the sludge return process and prevent sludge from accumulating on the bottom of the clarifier tank for lengthy periods. Process blowers are maintained so that the treatment plant will work properly and prevent septic conditions from developing.

Labrador directed its chemical supplier to take monthly measurements of sulfide concentrations in the air along the perimeter of the WWTP fence line in order to quantify the amount of sulfides present. The vendor has consistently done so with essentially zero sulfides occurring. The entire development is constructed in close proximity to the WWTP. Furthermore, several of the homes' rear lot lines are adjacent to the WWTP property line placing them extremely close to the plant. The Utility also investigated other sources of odors near the treatment plant site. It was determined that the WWTP is situated adjacent to a swampy area and there are chicken farms located near Forest Lake Estates.

According to DEP, two odor complaints were received in 2010 and no complaints were received for 2011 and 2012. DEP indicated to staff that it has not found any significant problems to warrant additional investigations.

Staff believes that the Utility's efforts to respond to customer concerns show its willingness to address customer satisfaction. While many customers either use bottled water or have some form of point-of-use treatment in order to obtain a product that meets their expectations, it appears that Labrador is making reasonable efforts to maintain good quality water. Although there have been situations that have inconvenienced customers, staff believes that treating the water used for all purposes by all customers to the highest customer expectation can come at significant cost to customers. For systems with challenging water quality aesthetics, point-of-use treatment systems are often the most cost effective mechanism to achieve customer aesthetic quality objectives. Further, the Utility has made changes to the operation and maintenance of the WWTP to address customer concerns regarding odor. Therefore, staff recommends that Labrador's attempt to address customer satisfaction is satisfactory.

Conclusion

Staff recommends that, pursuant to Rule 25-30.433(1), F.A.C., Labrador's quality of product, operating condition of its plants and facilities, and its attempt to address customer satisfaction are satisfactory. Therefore, staff recommends that the overall quality of service provided by the Utility be found to be satisfactory.

RATE BASE

Issue 3: Should the audit adjustments to rate base and operating expense to which the Utility and staff agree be made?

Recommendation: Yes. Based on the audit adjustments agreed to by the Utility and staff, the following adjustments should be made to rate base and net operating expense as set forth in staff's analysis below. (Springer)

Staff Analysis: In its response to the staff's audit report and other correspondence, Labrador agreed to the audit adjustments as set forth in the tables below.

Table 3-1

Labrador Audit Adjustments	Description of Adjustments
Finding No. 1	Reflect appropriate plant retirements that were not recorded by the Utility.
Finding No. 2	Correct error in the Utility's depreciation restatement.
Finding No. 3	Reflect the appropriate accumulated depreciation.
Finding No. 4	Correct allocations from headquarters – rate base.
Finding No. 5	Reflect appropriate amount for permit expenses.
Finding No. 9	Reflect appropriate non-recurring expense.
Finding No. 10	Correct error in Utility's recording of sludge hauling expense.
Finding No. 11	Reflect the appropriate rate case expense.
Finding No. 12	Reflect the appropriate purchased power expense.
Finding No. 13	Correct error in Utility's expense included in plant
Finding No. 14	Correct allocations from headquarters – net operating income.
Finding No. 15	Correct allocations for pro forma for pay increase.
Finding No. 16	Correct removal of operations & maintenance (O&M) expenses.
Finding No. 17	Correct prepaid – other expenses.

Based on the audit adjustments agreed to by the Utility, staff recommends that the adjustments set forth in Table 3-2 and Table 3-3 should be made to rate base and net operating expense.

Table 3-2

Water							
Labrador Audit Adjustments	Plant	Accum. Depreciation	Depreciation Expense	Ammort. Expense	Working Capital	O&M Expense	TOTI
Finding No. 1	($3,049)	($3,530)	($105)				
Finding No. 3		($1,190)					
Finding No. 4	($1,721)	($582)					
Finding No. 5						($8,784)	
Finding No. 9						($1,400)	
Finding No. 11						($7,461)	
Finding No. 12						($338)	
Finding No. 13	($517)						
Finding No. 14			($182)			($884)	($37)
Finding No. 16						($106)	($48)
Finding No. 17				($71)			
Adjustment Totals	($5,287)	($5,302)	($287)	($71)	$0	($18,973)	($85)

Table 3-3

Wastewater							
Labrador Audit Adjustments	Plant	Accum. Depreciation	Depreciation Expense	Ammort. Expense	Working Capital	O&M Expense	TOTI
Finding No. 1	($12,903)	($17,773)	($766)				
Finding No. 4	($1,693)	($573)					
Finding No. 5						($1,085)	
Finding No. 10						($11,441)	
Finding No. 11						($7,344)	
Finding No. 12						($1,454)	
Finding No. 13	($29)						
Finding No. 14			($180)			($873)	($37)
Finding No. 16						($105)	($47)
Finding No. 17				($70)			
Adjustment Totals	($14,625)	($18,346)	($946)	($70)	$0	($14,958)	($84)

Issue 4: Should any adjustment be made to the Utility's Project Phoenix Financial / Customer Care Billing System (Phoenix Project)?

Recommendation: Yes. Plant should be reduced by $6,578 for water and $6,473 for wastewater. In addition, accumulated depreciation should be reduced by $4,077 for water and $4,011 for wastewater. Depreciation expense should be decreased by $2,320 for water and $2,285 for wastewater. (Springer)

Staff Analysis: The purpose of the Phoenix Project is to improve accounting, customer service, customer billing, and financial and regulatory reporting functions of UI and its subsidiaries. The Phoenix Project became operational in December 2008. Since 2009, the Commission approved recovery of the cost of the Phoenix Project in 11 UI rate cases.[5] In those cases, UI allocated the Phoenix Project costs based on each subsidiary's equivalent residential connections (ERCs) to UI's total ERCs.

Allocation of Phoenix Project Costs

In the instant case, UI allocated 0.56 percent of its costs to Labrador based on the ratio of Labrador's total ERCs to UI's total ERCs. Based on total Phoenix Project costs of $21,545,555, Labrador calculated its allocated share to be 0.56 percent, or $120,655.

2009 Divestitures of UI Subsidiaries

In 2009, UI divested several Florida subsidiaries including Miles Grant Water and Sewer Company, Utilities, Inc. of Hutchinson Island, and Wedgefield Utilities, Inc., as well as other subsidiaries in other states. In Order No. PSC-10-0585-PAA-WS, the Commission found that allocating costs according to ERCs is an appropriate methodology to spread the cost of the Phoenix Project, but it did not believe the Phoenix Project costs previously allocated to the divested subsidiaries should be reallocated to the surviving utilities.[6] Because no added benefit was realized by the remaining subsidiaries, the Commission found that it was not fair, just, or reasonable for ratepayers to bear any additional allocated Phoenix Project costs. Thus, the Commission ruled that the divested subsidiaries' allocation amounts shall be deducted from the total cost of the Phoenix Project before any such costs are allocated to the remaining UI subsidiaries.

Staff Affiliate Audit Finding No. 7

In Order No. PSC-10-0407-PAA-SU, the Commission established the total cost of the Phoenix Project as of December 31, 2008, at $21,617,487 and required UI to deduct $1,724,166 from the total cost of the Phoenix Project to account for the divestiture of several subsidiaries

[5] See Docket Nos. 090531-WS, 090462-WS, 090402-WS, 090392-WS, 080250-SU, 080249-WS, 080248-SU, 080247-SU, 070695-WS, 070694-WS, and 070693-WS.

[6] See Order No. PSC-10-0585-PAA-WS, issued September 22, 2010, in Docket No. 090462-WS, In re: Application for increase in water and wastewater rates in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida, p. 10.

resulting in a remaining balance of $19,893,321.[7] In this case, staff auditors determined that the Utility did not make the adjustment for the Phoenix Project that the Commission ordered. According to Affiliate Audit Finding No. 7, Labrador showed the Phoenix Project balance at December 31, 2008, to be $21,545,555. The difference between the Utility's balance and the Commission recognized balance is $1,652,234 ($21,545,555 - $19,893,321). Therefore, the UI balance for the Phoenix Project should be reduced by $1,652,234 to account for the divestiture of subsidiary utilities through 2009. The effect on the filing is a decrease to water and wastewater plant by $4,664 and $4,589, respectively. Corresponding adjustments should also be made to decrease accumulated depreciation by $700 for water and $688 for wastewater. Depreciation expense should also be decreased by $466 for water and $459 for wastewater. The depreciation calculation is based on a depreciation life of ten years for the Phoenix Project.

In its response to Affiliate Audit Finding No. 7, Labrador disagreed with the finding and argued that the full balance of the Phoenix Project should be included at the UI level, with 0.56 percent allocated to Labrador. The Utility argued that it is incorrect to reduce the Phoenix Project balance for sold companies as none of the Phoenix system was sold in conjunction with the divested companies. Labrador contended that reducing the Phoenix Project balance for the remaining subsidiaries creates an improper gain on sale situation in the amount of $1,652,234 because it effectively includes the allocated amount of the Phoenix Project costs with the sale of the divested utilities. The Utility contends such an adjustment is contrary to Section 367.0813, F.S. Labrador maintains that the total Phoenix Project balance is currently in-service and benefiting current ratepayers and it is arbitrary and inappropriate to reduce the balance.

In response to Labrador's objection to this adjustment, staff points out that the Commission has already determined in prior UI rate cases that the Phoenix Project balance should be reduced to account for the divestitures of subsidiary UI systems.[8] Moreover, the Utility's response to the audit adjustment mischaracterizes staff's recommended adjustment related to the Phoenix Project. Staff's recommended adjustment is not related to gain on sale. The adjustment is being made to prevent UI from allocating additional cost to Florida utility systems. The additional cost UI has proposed to allocate to Labrador is the result of UI's unilateral decision to sell assets unrelated to the provision of regulated water and wastewater service by Labrador. UI's proposed incremental increase in the Phoenix Project allocation is not related to additional investment in its computer system to improve its functionality or extend its useful life. Instead, this proposed increase in allocation is designed to offset an unrelated business decision. Without any added benefit or an extension of its useful life, it is inappropriate for UI to attempt to raise water and wastewater rates in Florida simply because it sold systems in other states.

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[7] See Order No. PSC-10-0407-PAA-SU, issued on September 22, 2010, in Docket No. 090381-WS, In re: Application for increase in water and wastewater rates in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida, p.6.

[8] Staff notes, however, that the Phoenix Project cost is a protested issue in a docket concerning another UI subsidiary. See Order No. PSC-11-0587-PAA-SU, issued December 21, 2011, in Docket No. 110153-SU, In re: Application for increase in wastewater rates in Lee County by Utilities, Inc. of Eagle Ridge.

2010 Divestitures of UI Subsidiaries

In 2010, UI divested four additional systems and subsidiaries as listed below.

Table 4-1

Date	Subsidiary	ERCs
March 15, 2010	Emerald Point Subdivision (North Carolina)	327
July 19, 2010	River Forest (South Carolina)	74
July 19, 2010	Stone Creek (South Carolina)	172
September 19, 2010	Alafaya Utilities, Inc. (Florida)	8,945

The four divested systems collectively represent 9,518 ERCs. UI planned to divest a fifth subsidiary, Montague in New Jersey, which was under contract to be sold. However, the sale of the Montague subsidiary did not close, and as such, the 1,019 ERCs related to Montague should not be included in the ERC percentage calculation. For purpose of this adjustment, the net number of ERCs related to the divested systems is 8,499, or 3.14 percent of the total number of ERCs for UI.

Consistent with prior Commission decisions, the adjustment to deduct the proportional amount of the divested companies from the total cost of the Phoenix Project should also be made for the subsequent divestitures. As such, staff calculated that the total cost of the Phoenix Project for UI should be reduced by an additional 3.14 percent, or $678,237 ($21,617,487 x 3.14 percent), to account for the divestiture of subsidiaries through 2010. The effect on the filing is a decrease to water and wastewater plant of $1,914 and $1,884, respectively. Corresponding adjustments should also be made to decrease both accumulated depreciation and depreciation expense by $287 for water and $283 for wastewater.

Amortization / Depreciation Period

In Staff Affiliate Audit Finding No. 8, staff auditors discovered that the Utility did not change the depreciation life for the Phoenix Project from eight to ten years as directed in Order No. PSC-10-0407-PAA-SU. In its response to Affiliate Audit Finding No. 8, Labrador disagreed with staff's finding and argued that the Commission has no basis for changing the amortization period for the Phoenix Project to ten years. The Utility contended that an eight year life has already been established in previous dockets and is the life used for all other computer software booked to the same account as the Phoenix Project.

In previous UI cases, the Commission approved a six-year amortization period for the Phoenix Project.[9] In subsequent UI cases, the Commission found that an eight-year amortization period was more appropriate for a software project of this magnitude.[10] In 2010, the Commission set the amortization period for the Phoenix Project to ten years in five separate rate cases involving Labrador sister companies.[11] There were three factors the Commission

[9] See Docket Nos. 070695-WS, 070694-WS, and 070693-WS.
[10] See Docket Nos. 080250-SU, 080249-WS, 080248-SU, and 080247-SU.
[11] See Order Nos. PSC-10-0407-PAA-SU, issued June 21, 2010, in Docket No. 090381-SU, In re: Application for Increase in wastewater rates in Seminole County by Utilities Inc. of Longwood; and PSC-10-0400-PAA-WS, issued

considered in its decision to increase the amortization period. First, the Phoenix Project was specifically tailor-made to meet all of UI's needs. This project is not "off the shelf" software, but software designed to fulfill long-term accounting, billing, and customer service needs specific to UI and its affiliates and subsidiaries. Second, the Commission concluded that Phoenix Project software will be used for at least ten years. UI's former Legacy accounting system had been used for 21 years. Third, in a 2008 docket involving a UI subsidiary in Nevada,[12] UI responded that any amortization period between four and ten years would be in compliance with Generally Accepted Accounting Principles (GAAP). Similarly, UI stated to this Commission that its own research revealed that computer software could be amortized over a period of anywhere from four to ten years.[13] As such, staff believes ten years is the appropriate amortization period for the instant case.

Based on the aforementioned, staff recommends that the appropriate depreciation period for Labrador is ten years which results in a necessary reduction to accumulated depreciation of $3,098 and $3,040 for water and wastewater, respectively. Accordingly, depreciation expense should be reduced by $1,567 for water and $1,543 for wastewater.

Conclusion

Based on the Phoenix Project balance for Labrador and the adjustment for the divestitures, staff believes the total cost of the Phoenix Project for UI should be reduced by $2,330,471. The resulting UI Phoenix Project balance for ratemaking purposes is $19,215,083. The appropriate amount of Labrador's allocated share of the Phoenix Project is $107,605 ($19,215,083 x 0.56 percent). Staff's recommended adjustments to Labrador's Phoenix Project balances are summarized in the following table.

June 18, 2010, in Docket No. 090392-WS, In re: Application for increase in water and wastewater rates in Lake County by Utilities Inc. of Pennbrooke; and PSC-10-0423-PAA-WS, issued July 1, 2010, in Docket No. 090402-WS, In re: Application for increase in water and wastewater rates in Seminole County by Sanlando Utilities Corporation; and PSC-10-0585-PAA-WS, issued September 22, 2010, In re: Application for increase in water and wastewater rates in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida; and PSC-1-0514-PAA-WS, issued November 3, 2011, in Docket No. 100426-WS, In re: Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc.

[12] Modified Final Order, issued January 15, 2009, in Docket No. 08-06036.

[13] See December 2, 2008, Commission Conference Transcript, Page 26, Line 3, through Page 27, Line 19.

Table 4-2

Staff Adjustment	Simple Average Plant		Simple Average Accumulated Depreciation		Depreciation Expense	
	Water	Wastewater	Water	Wastewater	Water	Wastewater
Affiliate Audit Finding No. 7	($4,664)	($4,589)	$700	$688	($466)	($459)
2010 Divestitures Adjustment	(1,914)	(1,884)	287	283	(287)	(283)
Affiliate Audit Finding No. 8	0	0	3,090	3,040	(1,567)	(1,543)
Total	($6,578)	($6,473)	$4,077	$4,011	($2,320)	($2,285)

Accordingly, staff recommends that plant be reduced by $6,578 for water and $6,473 for wastewater. In addition, accumulated depreciation should be reduced by $4,077 for water and $4,011 for wastewater. Depreciation expense should be decreased by $2,320 for water and $2,285 for wastewater.

Issue 5: Should any adjustments be made to the Utility's requested adjustments to accumulated depreciation?

Recommendation: Yes. Accumulated depreciation should be decreased by $179 for water and $1,826 for wastewater. Corresponding adjustments should be made to decrease depreciation expense by $179 and $1,826 for water and wastewater, respectively. (Springer)

Staff Analysis: In its MFRs, the Utility recorded adjustments of $179 for water and $1,826 for wastewater to annualize accumulated depreciation for assets placed in service during the test year. Labrador also made corresponding adjustments to increase depreciation expense by $179 for water and $1,826 for wastewater. Accumulated depreciation is based on when an asset is placed into service. It is not appropriate to annualize accumulated depreciation on a pro forma basis because the annualized amount includes a period of time when the asset was not in service during the test year. Further, Labrador failed to make matching adjustments to annualize any other rate base items such as amortization of CIAC. Consistent with the Commission's decision in Order No. PSC-02-1657-PAA-WU, the proposed adjustments to accumulated depreciation and depreciation expense should be removed from the Utility's filing.[14] Accordingly, accumulated depreciation should be decreased by $179 for water and $1,826 for wastewater. Corresponding adjustments should be made to decrease depreciation expense by $179 and $1,826 for water and wastewater, respectively.

[14] See Order No. PSC-02-1657-PAA-WU, issued November 26, 2002, in Docket No. 011621-WU, In re: Petition for a limited proceeding to implement an increase in water rates in Highlands County, by Placid Lakes Utilities, Inc.

Issue 6: What are the used and useful percentages of the Utility's water and wastewater system?

Recommendation: The Utility's WTP, storage, WWTP, and distribution and collection systems should be considered 100 percent used and useful. (McRoy)

Staff Analysis: In its application, the Utility asserts that the WTP and WWTP, as well as the water distribution and wastewater collection systems, are all 100 percent used and useful (U&U). Labrador maintains that the service territory the treatment plants are designed to serve is built out and there is no apparent potential for expansion. The service area consists of the 894-lot Forest Lakes Estates Mobile Home Park and the 274-lot Forest Lakes RV Resort. Within the service area of the Utility, there are four vacant lots in the mobile home park and a vacant 11.6 acre parcel of land which is owned by Forest Lakes Estates Cooperative. A 90-unit RV park was being considered but, the project has been placed on indefinite hold.

Water Treatment Plant

Pursuant to Rule 25-30.4325, F.A.C., the U&U calculation for a WTP is determined by dividing the peak demand by the firm reliable capacity of the WTP. Because the system has storage facilities, the calculation is in gallons per day (gpd). Consideration of growth, fire flow requirements, unaccounted for water, and other factors may also be included.

Labrador's WTP has two wells. One is rated at 950 gallons per minute (gpm) and the other is rated at 200 gpm. Before being pumped into the distribution system, raw water is treated with liquid chlorine for disinfection and a sequestration chemical for iron control. Pursuant to Rule 25-30.4325(6)(b), F.A.C., staff calculated the firm reliable capacity of the water system to be 192,000 gpd.

The single maximum day in the test year occurred on November 8, 2010; however, according to the Utility, significant tri-lateral flushing occurred on that day. The second maximum day in the test year of 168,000 gallons occurred on January 4, 2010. It does not appear that there was a fire, line break, or other unusual occurrence on that day. Fire hydrants are located throughout the service area; therefore, a fire flow allowance of 500 gpm for 2 hours should be included in the U&U analysis pursuant to Rule 25-30.4325(1)(c), F.A.C. According to the Utility, the system is built out, and thus a growth allowance was not included in the U&U calculation.

The Utility's F-1 schedule in the MFRs indicates excessive unaccounted for water (EUW) of 1.70 percent. Pursuant to Rule 25-30.4325, F.A.C., EUW is unaccounted for water in excess of 10 percent of the amount pumped. However, according to staff's review of the Utility's Monthly Operation Reports (MORs) submitted to DEP showing gallons pumped compared with the Utility's reported gallons sold and other uses, the EUW is 2.10 percent or 1,442 gpd.

Pursuant to Rule 25-30.4325, F.A.C., staff recommends that the WTP is 100 percent U&U based on a peak day of 168,000 gpd, a fire flow allowance of 120,000 gpd, EUW of 1,442 gpd, and firm reliable capacity of 192,000 gpd.

Ground Storage Tank

Rules 25-30.4325(8) and (9), F.A.C., provide that the U&U percentage for a storage tank is determined by dividing the peak demand by the usable capacity of the tank. A ground storage tank is considered 90 percent usable if the bottom of the tank is below the centerline of the pumping unit. The Utility has a 34,000-gallon ground storage tank. Pursuant to Rule 25-30.4325(9)(b), F.A.C., the usable capacity of the tank is 30,900 gpd. Because the usable storage capacity is less than the peak day demand, the storage tank should be considered 100 percent used and useful, pursuant to Rule 25-30.4325(8), F.A.C.

Wastewater Treatment Plant

The current DEP permitted capacity for the WWTP is based on three-month average daily flows (TMADF). The WWTP, which uses extended aeration for treatment, has a rated capacity of 216,000 gpd based on TMADF. The treated effluent is disposed of on a 34.7 acre slow-rate restricted public access spray field. The TMADF during the test year was 79,216 gpd. It appears that there is no excessive infiltration and inflow (I&I) in the collection system. According to the Utility, an allowance for growth was not included because the area served by the existing plant is built out. Based on the TMADF flow during the test year, the wastewater treatment plant is 37 percent U&U. However, the Utility believes that this facility should be considered 100 percent used and useful because the plant was designed to serve full occupancy at design flows of 280 gpd/equivalent residential connection (ERC) which would require 250,000 gpd capacity. The actual flows are closer to 69 gpd/ERC in the peak month assuming 95 percent occupancy.

Staff agrees with the Utility that the plant was appropriately sized to meet the projected needs of the community that it was intended to serve, including the 90-unit RV park that is proposed for the vacant property discussed earlier. There appears to be no timetable for the construction of the proposed RV park addition. Owner representatives of the property have indicated that further development is dependant on the economy. Given the speculative nature of the additional development, staff recommends that pursuant to Rule 25-30.432, F.A.C., the service area be considered built out and the WWTP be considered 100 percent U&U.

Water Distribution and Wastewater Collection Systems

The U&U calculations for the water distribution and wastewater collection systems are determined by dividing the number of customers connected to the systems by the number of lots available for service. Consideration is given for growth; however, in this case, growth is not considered a factor since the systems are built out. The distribution and collection systems were designed to serve the existing customers. Therefore, staff recommends the water distribution and wastewater collection systems be considered 100 percent U&U.

Conclusion

Based on the above discussion, staff recommends that the Utility's WTP, storage tank, WWTP, and distribution and collection systems be considered 100 percent used and useful.

Issue 7: What is the appropriate working capital allowance?

Recommendation: The appropriate working capital allowance is $19,653 for water and $26,245 for wastewater. As such, the working capital allowance should be decreased by $6,021 for water and $6,278 for wastewater. (Springer)

Staff Analysis: Rule 25-30.433(2), F.A.C., requires that Class B utilities use the formula method, or one-eighth of O&M expense, to calculate the working capital allowance. The Utility has properly filed its allowance for working capital using the formula method. Staff has recommended adjustments to Labrador's O&M expense. As a result, staff recommends working capital of $19,653 for water and $26,245 for wastewater. This reflects a decrease of $6,021 for water and $6,278 for wastewater to the Utility's requested working capital allowance of $25,674, and $32,523 for water and wastewater, respectively.

Issue 8: What is the appropriate rate base for the test year ended December 31, 2010?

Recommendation: The appropriate simple average rate base for the test year ended December 31, 2010, is $695,645 for water and $1,351,693 for wastewater. (Springer)

Staff Analysis: In its MFRs, the Utility recorded rate base of $703,973 for water and $1,354,886 for wastewater. Staff has calculated Labrador's water and wastewater rate bases using the Utility's MFRs with adjustments as recommended in the preceding issues. Accordingly, staff recommends that the appropriate simple average rate base for the test year ended December 31, 2010, is $695,645 for water and $1,351,693 for wastewater. Staff's recommended water and wastewater rate bases are shown on Schedule Nos. 1-A and 1-B, respectively. The adjustments are shown on Schedule No. 1-C.

COST OF CAPITAL

Issue 9: What is the appropriate return on equity?

Recommendation: Based on the Commission leverage formula currently in effect, the appropriate return on equity (ROE) is 10.51 percent with an allowed range of plus or minus 100 basis points. (Springer)

Staff Analysis: The ROE included in the Utility's filing is 10.51 percent. Based on the current leverage formula in effect and an equity ratio of 47.6 percent, the appropriate ROE is 10.51 percent.[15] Staff recommends an allowed range of plus or minus 100 basis points be recognized for ratemaking purposes.

[15] See Order No. PSC-11-0287-PAA-WS, issued July 5, 2011, in Docket No. 110006-WS, In re: Water and wastewater industry annual reestablishment of authorized range of return on common equity for water and wastewater utilities pursuant to Section 367.081(4)(f), F.S.

Issue 10: What is the appropriate weighted average cost of capital including the proper components, amounts, and cost rates associated with the capital structure for the test year ended December 31, 2010?

Recommendation: The appropriate weighted average cost of capital for the test year ended December 31, 2010 is 8.26 percent. (Springer)

Staff Analysis: In its filing, the Utility requested an overall cost of capital of 8.26 percent. Based upon the proper components, amounts, and cost rates associated with the capital structure for the test year ended December 31, 2010, staff agrees with the Utility and recommends a weighted average cost of capital of 8.26 percent. Schedule No. 2 details staff's recommended overall cost of capital.

NET OPERATING INCOME

Issue 11: Should any adjustments be made to the Utility's requested water O&M expense related to tank maintenance and repair?

Recommendation: Yes. Water O&M expense should be decreased by $3,213 to reflect the appropriate amount of water tank maintenance and repair expense. (Springer)

Staff Analysis: On MFR Schedule B-11, Labrador provided an analysis of all maintenance projects greater than 2 percent of test year revenue during the test year, 2 years prior to the test year, and 1 year subsequent to the test year. In its analysis, the Utility requested a budgeted amount of $46,204 for the cost to maintain and repair the water tank. The budgeted amount was amortized over 5 years and $9,241 was included in water O&M expense. The basis for Labrador's budgeted amount was the cost incurred in April 2004 to repair and maintain the tank. The cost in 2004 included work to sandblast and recoat the tank inside and out, cut off the old roof, and install a new pre-fabricated roof with handrails.

A tank inspection report from Liquid Engineering, dated January 27, 2010, indicated that the condition of the interior of the tank was in fair condition, but was in need of repairs to continue functioning as designed. Liquid Engineering recommended that the tank be sandblasted and recoated in addition to making other minor repairs. Staff estimates that the appropriate cost to maintain and repair the water tank is $30,138. Staff based its estimate on the actual cost of $23,500 to sandblast and recoat the tank in April 2004. Staff used an inflation factor of 1.156093 to inflate the cost in 2004 to the cost in 2011. The estimated cost in 2011 was calculated to be $27,168 (1.156093 x $23,500). Staff added the cost of the tank inspection ($2,970) to the cost of sandblasting and recoating for a total estimated cost of $30,138. In accordance with Rule 25-30.433(8), F.A.C., this cost should be amortized over 5 years. Accordingly, the appropriate estimated annual cost is $6,028 ($30,138 ÷ 5). Therefore, the annual cost of water tank maintenance and repair should be decreased by $3,213 ($9,241 - $6,028) to reflect the appropriate estimated amount of water tank maintenance and repair expense.

Issue 12: Should any adjustment be made to the Utility's salaries and wages expense?

Recommendation: Yes. Salaries and wages expense should be decreased by $1,704 for water and $1,677 for wastewater. (Springer)

Staff Analysis: In its MFRs, Labrador included a pro forma adjustment to water and wastewater salaries and wages expense to reflect a 3 percent salary increase in April 2011. Given the tumultuous state of the economy, and the fact the Utility received a rate increase in 2009, staff believes that any pay increase at this time should not be borne by the ratepayers. As such, staff recommends the Utility's pro forma pay increase be disallowed. This treatment is consistent with the Commission's recent decisions in the Aqua Utilities Florida, Inc. (AUF) and the Lake Utility Services, Inc. (LUSI) rate cases.[16] Therefore, staff believes an adjustment to reduce Labrador's requested salaries and wages expense by the amount of the pro forma adjustment is appropriate. Accordingly, staff recommends that salaries and wages expense be decreased by $1,704 for water and $1,677 for wastewater.

[16]See Order Nos. PSC-11-02-0102-PAA-WS, issued March 5, 2012, in Docket No. 100330-WS, In re: Application for increase in water/wastewater rates in Alachua, Brevard, DeSoto, Hardee, Highlands, Lake, Lee, Marion, Orange, Palm Beach, Pasco, Polk, Putnam, Seminole, Sumter, Volusia, and Washington Counties by Aqua Utilities Florida, Inc.; and PSC-10-0514-PAA-WS, issued November 3, 2011, in Docket No. 100426-WS, In re: Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc.

Issue 13: Should further adjustments be made to the Utility's O&M expense?

Recommendation: Yes. O&M expense should be reduced by $640 for water and $3,330 for wastewater to reflect the appropriate level of miscellaneous and sludge removal expenses. (Springer)

Staff Analysis: In its filing, Labrador recorded miscellaneous expenses of $29,056 for water and $22,423 for wastewater. Also, the Utility recorded $21,441 for sludge removal expense. Staff believes adjustments are necessary as discussed below.

Miscellaneous Expense

Labrador's miscellaneous expense includes allocated computer maintenance expenses from UI. In the test year, the computer maintenance expenses were $5,280 for water and $5,196 for wastewater. Based on responses to OPC's discovery, UI has experienced volatility in the amount of computer maintenance expense over the last five years from 2007-2011 as shown in the Table below:

Table 13-1

Year	2007	2008	2009	2010	2011
Misc. Expense Amount	$1,022,146	$1,208,569	$1,778,919	$1,914,523	$1,389,050

Recognizing the volatility of computer maintenance expense, staff believes that a three-year average is an appropriate basis for ratemaking purposes. Based on the three-year average (2009-2011) and Labrador's .56 ERC allocation percentage, staff calculated computer maintenance expense of $4,640 and $4,566 for water and wastewater, respectively. Therefore, staff recommends miscellaneous expense be reduced by $640 for water and $630 for wastewater.

Sludge Removal Expense

In Labrador's 2009 Annual Report, the sludge removal expense listed in Account 711 was $32,860. In Labrador's filing for the 2010 test year, the Utility recorded sludge removal expense of $21,441. As discussed in Issue 2, Labrador's estimated sludge removal expense would be approximately $10,000 for 2011, and agreed with a reduction of $11,441. However, Labrador's response to OPC's First Set of Interrogatories No. 16 states that the Utility incurred an actual amount of $7,300 for sludge removal expense in 2011. As a result, staff recommends that the Utility's requested level of sludge removal expense be further reduced by an additional amount of $2,700 to reflect the 2011 sludge removal expense incurred by the Utility. Staff notes this adjustment is consistent with the adjustment made in a limited proceeding with Labrador's sister Utility, Cypress Lakes Utilities, Inc., in Order No. PSC-10-0682-PAA-WS. [17]

[17] See Order No. PSC-10-0682-PAA-WS, page 17, issued November 15, 2010, in Docket No. 090349-WS, In re: Application for limited proceeding rate increase in Polk County by Cypress Lakes Utilities, Inc.

Summary

Based on the above, staff recommends that O&M expense be reduced by $640 for water and $3,330 ($630 + $2,700) for wastewater to reflect the appropriate level of miscellaneous and sludge removal expenses.

Issue 14: What is the appropriate amount of rate case expense?

Recommendation: The appropriate amount of rate case expense is $83,374. This expense should be recovered over four years for an annual expense of $20,844, or $10,505 for water and $10,338 for wastewater. Therefore, annual rate case expense should be reduced by $23,213 for water and $22,844 for wastewater from the amounts requested in the Utility's MFRs. (Springer)

Staff Analysis: In its MFRs, Labrador requested $267,603 for current rate case expense. Staff requested an update of the actual rate case expense incurred, with supporting documentation, as well as the estimated amount to complete the case. On November 17, 2011, the Utility submitted a revised estimated rate case expense as of October 31, 2011, through completion of the PAA process of $204,452.

Table 14-1

	MFR B-10 Estimated	Actual as of 10/31/11	Additional Estimated	Revised Total
Legal Fees	$82,325	$4,046	$31,249	35,295
Accounting Consultant Fees	67,250	$13,225	36,588	49,813
Engineering Consultant Fees	3,900	338	2,900	3,238
WSC in-house Fees	87,928	21,715	68,191	89,906
Filing Fee	4,000	0	4000	4,000
WSC Travel	3,200	273	2,927	3,200
WSC Temp Employee Fees	2000	31	1969	2,000
WSC FedEx/Misc.	12,000	89	11,911	12,000
Notices	5,000	499	4,501	5,000
Total Rate Case Expense	$267,603	$40,216	$164,236	$204,452

Pursuant to Section 367.081(7), F.S., the Commission shall determine the reasonableness of rate case expense and shall disallow all rate case expense determined to be unreasonable. Staff has examined the requested actual expenses, supporting documentation, and estimated expenses as listed above for the current rate case. In addition, staff reviewed the Commission Orders in the Utility's 2003 and 2008 rate cases. Based on its review, staff believes the following adjustments to Labrador's rate case expense estimate are appropriate.

Legal Consultant Fees

Staff recommends three adjustments related to the Utility's legal consultant fees, resulting in a total reduction of $9,836. The first adjustment relates to unbilled fees and costs in the amount of $4,588. The Utility submitted an estimate to complete the rate case through the PAA process from the legal consultant that included $3,000 for unbilled legal fees, but did not include any description documenting the legal consultant's time. In addition, the legal consultant provided a cost report totaling $1,588 for unbilled outside photocopies and Federal Express, but did not provide any documentation demonstrating the costs were associated with the instant rate case or any invoices for the costs. Accordingly, staff recommends that legal fees be reduced by $4,588 ($3,000 + $1,588).

The second adjustment relates to travel expenses. The legal consultant included an estimate of $400 to attend the customer meeting and $1,000 to attend the Commission Conference, for a total of $1,400 related to travel, meals, and hotel. The customer meeting was held in Zephyr Hills, Florida, which is approximately a 90-minute drive from the legal consultant's law offices in Lake Mary, Florida. Therefore, staff believes $400 for travel to the customer meeting is excessive. Staff believes an expense of $1,000 for travel to attend the Commission Conference is also excessive. In July 2011, the legal consultant requested, and the Commission approved, $500 for travel to attend the Commission Conference in the LUSI rate case. It is unreasonable to assume the cost for travel from Lake Mary, Florida to Tallahassee has doubled since July 2011. Therefore, staff believes the requested travel expenses for the legal consultant should be reduced by $700. This adjustment provides $500 for travel to the Commission Conference consistent with the amount allowed in a recent case for a sister utility and $200 for travel to the customer meeting.

The third adjustment relates to the hourly rate billed by the legal consultant. In the AUF rate case, the Commission voted to decrease the hourly rate of the consultants to the rate authorized in the Utility's previous rate case. Staff believes the conditions in this case are similar to those in the Aqua case, and as such, the hourly billing rate for the legal consultant should be set at the rate authorized in Labrador's 2008 rate case. The hourly billing rate in the instant case is $340 for the partner and $315 for the associate. In Labrador's 2008 rate case, the hourly billing rate for the partner was $315 and $290 for the associate. Applying the hourly billing rate from the last rate case to the total hours in the instant case equates to a difference of $4,548. Accordingly, staff recommends that legal fees be reduced by $4,548.

Accounting Consultant Fees

The Utility is requesting accounting consultant expenses of $49,813 for 324 hours of work. In a data request, staff asked the following:

> (a) For each individual person, in each firm providing consulting services to the applicant pertaining to this docket, provide the billing rate, and an itemized description of work performed. Please provide detail of hours worked associated with each activity. Also provide a description and associated cost for all expenses incurred to date.
>
> (b) For each firm or consultant providing services for the applicant in this docket, please provide copies of all invoices for services provided to date.
>
> (c) If rate consultant invoices are not broken down by hour, please provide reports that detail by hour, a description of actual duties performed, and amount incurred to date.

Although staff requested a detailed description of the actual duties performed, the reports submitted by the Utility for the accounting consultant's time reflect a very broad description of the work performed. The description of duties performed in the report simply states, "MFRs Preparation." In addition, the duties listed in the accounting consultants estimate to complete appear duplicative of the duties that were reportedly performed by WSC in-house employees. For example, the duties listed include: respond to staff data requests; review interim order; review audit, discuss issues with client; review, research and prepare a response to OPC interrogatories; review staff recommendation, test revenue requirement including suppression calculations; review PAA Order, test revenue requirement including suppression calculations.

Staff believes the Utility has not demonstrated that the accounting consultant fees, along with the significant increase in WSC in-house employee costs, are necessary to file the rate case. Further, staff believes the rate case expense has increased to an amount that is unreasonable and excessive as compared to the rate case expense from the Utility's last two rate cases.

In Labrador's 2003 rate case, the Utility requested a total rate case expense of $100,554, and the Commission approved an amount of $68,988. In the 2003 case, Labrador did not include any expenses for an accounting consultant. The supporting documentation showed that 4 WSC in-house employees prepared the MFRs, responded to data and audit requests, and performed all other necessary non-legal duties related to the rate case. The Commission approved expenses of $16,664 for WSC in-house employees that reflected 335 hours worked to process the PAA rate case.

In Labrador's 2008 rate case, the Utility initially requested total rate case expense of $207,715 that included accounting consultant expense of $45,000. The revised amount for accounting consultant expense increased to $64,435. The Commission disallowed all of the accounting consultant fees of $64,435 in that case.[18] At the Commission Conference, the Commission agreed with OPC's proposed adjustment to remove all accounting consultant fees.[19] In the 2008 case, OPC argued that the Utility added a substantial number of WSC in-house employees since the last rate case.[20] In fact, the revised rate case schedule showed that 15 WSC in-house employees worked on the 2008 rate case compared to only 4 employees who worked on the 2003 rate case. OPC also argued that the addition of the $20 million Project Phoenix, the cost of which is allocated to all UI subsidiaries, was intended to result in improved accounting and computer efficiencies.[21] OPC argued that the expenses for an accounting consultant to help Labrador prepare MFRs and respond to data requests, in addition to the increase in WSC in-house employees and the Project Phoenix costs, was unreasonable and duplicative, and as such, should not be borne by the ratepayers.[22] OPC argued that if the Commission were to disallow the accounting consultant rate case expenses from a policy standpoint, it would bring the rate

[18]See Order No. PSC-09-0462-PAA-WS, issued June 22, 2009, in Docket No. 080249-WS, In re: Application for increase in water and wastewater rates in Pasco County by Labrador Utilities, Inc.
[19]See Transcript of June 2, 2009, Agenda Conference, pp. 134-135, in Docket No. 080249-WS, In re: Application for increase in water and wastewater rates in Pasco County by Labrador Utilities, Inc.
[20] Id., pp.16-17.
[21] Id., pp. 21-22.
[22] Id.

case expense back into line with the 2003 rate case.[23] The Commission agreed and voted to approve staff's recommendation for rate case expense with OPC's adjustments.[24]

Staff believes the same scenario that OPC was concerned with in the 2008 rate case exists in the instant rate case. The number of WSC in-house employees working on the rate case and the related expense has increased since the prior rate case. In the 2008 rate case, Labrador requested WSC in-house expenses of $37,470 for 853 hours worked. The Commission approved WSC in-house expenses of $24,644, and total rate case expense of $69,241. In the instant case, the Utility is requesting WSC in-house expenses of $89,906 for 1,921 hours worked. In its rate case expense schedule, Labrador indicated that 18 WSC in-house employees worked on the rate case. In addition, the Utility is requesting accounting consultant expenses of $49,813 for 324 hours of work.

Based on the aforementioned, staff believes the Utility has not demonstrated that both the accounting consultant time and the significant increase in WSC in-house accounting work are necessary to file and process its rate case. In addition, it appears that the accounting consultant services are duplicative of the duties performed by WSC in-house employees. Staff is concerned that the Utility has not sufficiently documented the accounting-related work preformed by the outside consultant and the in-house employees. While an argument can be made that the Utility has failed to carry its burden of proof with respect to these costs, staff recognizes that the MFRs were prepared, document and audit requests were responded to, and the rate case was processed by someone on behalf and the Utility. Staff's recommendation regarding WSC in-house employees is discussed later in this issue. Because staff is recommending the incremental time of WSC in-house employees be disallowed, staff recommends that the accounting consultant fees in the amount of $49,813 be allowed.

Engineering Consultant Fees

At the time the Utility submitted it revised rate case expense schedule, Labrador requested total engineering fees of $3,238, which was comprised of $338 in actual costs and $2,900 in estimated fees to complete the rate case. The estimate to complete the rate case included $900 for 6 hours worked in the week of May 23, 2011, to prepare MFRs. The remaining expense related to 8 hours for assisting with and responding to data requests, 4 hours to prepare for and attend the Commission Conference, and $50 for expenses.

The only support provided for the work to be performed was the following statement on the revised MFR Schedule B-10: "U&U Analysis, Assist w/ MFRs, data requests, audit facilitation." Staff notes that there would be no work remaining for engineering U&U Analysis, assisting with MFRs, responding to data requests, and audit facilitation. Also, staff believes any remaining data requests would be more appropriately addressed by WSC in-house employees. Based on the documentation provided by the Utility, staff believes the appropriate amount of engineering consultant fees is $1,238 ($900 + $338).

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[23] Id.

[24] See Vote Sheet from June 2, 2009, Agenda Conference, Issue 11, in Docket No. 080249-WS, In re: Application for increase in water and wastewater rates in Pasco County by Labrador Utilities, Inc.

WSC in-house Employee Fees

In its revised rate case expense estimate, the Utility requested $89,906 for expenses related to WSC in-house employees to process the instant case. Labrador reported that the total number of actual hours incurred by WSC in-house employees as of October 31, 2011, was 507, and estimated an additional 1,414 hours remaining to complete the rate case, for a total of 1,921 hours. Based on the Utility's requested number of hours and expenses for WSC in-house employees in Labrador's 2003 and 2008 rate cases, staff believes the number of hours proposed by the Utility for WSC in-house employee fees is excessive, unreasonable, and unsupported.

The only support provided for the estimated hours remaining for WSC in-house employees was a notation in Revised MFR Schedule B-10 that listed the type of service rendered as "Assist w/MFRs, data requests, audit facilitation" for most employees. One WSC employee was designated as "Billing Analyst, Implementation of Rates." Regardless, the Utility failed to provide any detailed documentation of what tasks were involved in its estimate to complete the case for each employee. The hours needed to complete data requests and audit facilitation were not broken down to estimate the hours needed to complete each item. In addition, there were no timesheets provided to show actual hours worked for each task in this case. Therefore, staff had no basis to determine whether the individual hours estimated were reasonable. Staff reviewed these requested expenses and believes the estimates are overstated. In those cases where rate case expense has not been supported by detailed documentation, the Commission's practice has been to disallow some portion or remove all unsupported amounts.[25]

Based on a review of the confidential salary information filed in the instant case, staff believes that 100 percent of the compensation for the positions listed in Table 14-2 has been allocated to Labrador and its sister companies as salaries and wages for WSC employees and officers. The Utility included total salaries and wages for WSC employees and officers of $95,883, or $48,325 for water and $47,558 for wastewater, in its O&M expense for the test year ended December 31, 2010. In addition, staff notes that the positions that paid by the hour did not incur overtime for time spent on this rate case.

Table 14-2

WSC Job Title (No. of positions)	Rate Case Related Essential Functions, Duties, or Responsibilities
Administrative Assistant (2)	-Under direct supervision of the Regional Director. -Performs complex and confidential administrative functions, including written correspondence, reports, spreadsheets and other documents. -Prepares or assists with the preparation of scheduled and/or ad hoc statistical and narrative reports; performs basic information gathering and analysis and/or forecasting, as specifically directed. -May assist other operational staff depending on work load.

[25] See Order No. PSC-94-0075-FOF-WS, issued January 21, 1994, in Docket No. 921261-WS, In re: Application for a Rate Increase in Lee County by Harbor Utilities Company, Inc.; Order No. PSC-96-0629-FOF-WS, issued May 10, 1996, in Docket No. 950515-WS, In re: Application for staff-assisted rate case in Martin County by Laniger Enterprises of America, Inc.; and Order No. PSC-96-0860-FOF-SU, issued July 2, 1996, in Docket No. 950967-SU, In re: Application for staff-assisted rate case in Highlands County by Fairmount Utilities, the 2nd, Inc. Staff notes that, in all of these cases, the Commission removed the entire unsupported amounts.

Customer Care Manager (1)	-Provides training to all customer service employees in the areas of billing, tariff compliance, rate cases and quality customer service. -Performs other related duties as assigned.
Director, Customer Care (1)	A Job Summary for this position was not provided in Volume III of the MFRs.
Director of Governmental Affairs (1)	-Provides leadership and guidance to newer regulatory staff not familiar with the rate case process. -Performs other related duties as assigned.
Regional Director (1)	-Manages the preparation of all rate cases, pass-through and indexing activity, changes to service territory, and any other PSC related activities in coordination with the company's regulatory department.
Regional Vice President (1)	-Oversees all operations of the regional offices. -Serves as the regional ambassador and local company contact for customers, community organizations, state commissions, and representatives. -Performs other related duties as assigned.
Regulatory Accounting Manager (1)	-Manages regulatory team responsibilities such as, rate cases, limited proceedings, indicies/pass-throughs, etc. -Files large-dollar rate cases or upon request, supplies required regulatory information to consultants. -Supplies audit trail and documentation to easily support work product. -Performs all follow-up compliance issues in accordance with Commission order.
Regulatory Staff Accountant I (3)	-Assists and supports Regulatory Accountant II, Senior Regulatory Accountant and Manager on rate case filings and other proceedings. -Provides audit trail and documentation to easily support work product.
Regulatory Staff Accountant II (1)	-Prepares commission-ordered adjustments. -Files rate cases or, upon request, supplies regulatory information to consultants. -Follows all required steps to close rate cases. -Provides financial support documentation. -Assists with commission staff performed audits and discovery. -Provides audit trail and documentation to easily support work product.
Senior Regulatory Accountant (1)	-Directly assists manager with regulatory responsibilities such as rate cases, limited proceedings, indicies/pass-throughs, etc. -Prepares commission-ordered adjustments. -Files large-dollar rate cases or upon request, supplies required regulatory information to consultants. -Performs all follow-up compliance issues in accordance with Commission order. -Provides audit trail and documentation to easily support work product.
Billing Manager (1)	-Responsible for management of the Billing Department, including directing, planning, managing, staffing and organizing the billing and collection aspect of all Utilities, Inc. subsidiaries. -Validates and rate changes required by state tariffs. -Informs management by reviewing and analyzing special reports, summarizing information and identifying trends. -Performs other related duties as assigned.
Regulatory Assistant (1)	-Performs general administrative duties -Maintains various regulatory spreadsheets and reports. -Assists in organizing documentation requirements. -Compiles and creates library of resource materials for regulatory staff. -Assists regulatory staff with the timely completion of assignments and projects in accordance with established deadlines.
Chief Operating Officer (1)	A Job Summary for this position was not provided in Volume III of the MFRs.
Regional Manager (1)	-Oversees plant operations and maintenance, customer contact and capital planning. -Assists Regional Director in the development and implementation of operational and regional strategies.

	-Serves as contact for inquiries regarding operational issues; answers routine and ad hoc information requests that are regional or unit-specific in nature. -Acts as point of contact with developers, engineers, consultants, regulators, and customers. -Performs other related duties as assigned.

In consideration of the aforementioned, staff believes that by requesting rate case expense for the hours WSC in-house employees incurred to process the rate case in addition to the expense for salaries and wages of these same WSC employees, the Utility is seeking double recovery of the allocated compensation for the positions listed in Table 14-2. Therefore, staff recommends that all of the hours associated with WSC in-house fees of $89,906 related to the instant rate case be disallowed.

WSC Travel Expenses

In its MFRs, Labrador estimated $3,200 for travel. However, the documentation the Utility provided to support this expense did not demonstrate that this expense was related to this rate case. The time of travel on the receipts and invoices did not correlate to the time during which the customer meeting took place. Furthermore, based on several previous UI rates cases, it is staff's experience that for PAA rate cases, UI does not send a representative from its Illinois office to attend the Commission Conference. Therefore, staff recommends that rate case expense be decreased by $3,200.

WSC Temp Employee Fees

In its initial rate case expense estimate, Labrador requested WSC temporary employee costs of $2,000. In its revised rate case expense schedule, the Utility reported it incurred $31 in actual costs and estimated an additional expense of $1,969 to complete the rate case. Labrador provided an invoice supporting $31 of actual costs, but did not provide any support documentation for the $1,969 of additional estimated costs. Accordingly, staff recommends that $1,969 be removed as unsupported rate case expense.

WSC FedEx Expenses

The next adjustment relates to WSC expenses for FedEx Corporation (FedEx) and other miscellaneous costs. In its MFRs, the Utility estimated $12,000 for these items. In support of these expenses, the Utility provided only $81 in costs from FedEx invoices for services. There was no breakdown or support for the remaining $11,911. Accordingly, staff recommends that rate case expense be decreased by $11,911.

Customer Notices and Postage

The Utility included expenses of $5,000 for customer notices and postage. In its revised rate case expense schedule, Labrador reflected actual charges incurred of $499. In 2009 UI rate cases, the Commission allowed expenses of $0.05 per envelope, $0.34 for postage,[26] and $0.10

[26] UI has a presorted postage rate of $0.341.

per copy. Staff recommends using the 2009 costs in order to remain consistent with the Commission's recent decision for Labrador's sister company, Lake Utility Services, Inc.[27]

Labrador is responsible for sending 4 notices: the interim notice, the initial notice, customer meeting notice, and notice of the final rate increase. The initial notice and customer meeting notice were combined in this docket. As such, staff estimated the postage cost for the notices to be approximately $1,555 (1520 customers x $0.34 pre-sorted rate x 3 notices). Staff estimates envelope costs to be $228 (1520 customers x $0.05 per envelope x 3 notices) and copying costs to be $912 (1520 customers x $0.10 per copy x 6 pages).[28] Based on these components, the total cost for customer notices and postage is $2,695 ($1,555 + $228 + $912). Accordingly, staff recommends rate case expense be decreased by $2,035 ($5,000 - $2,695).

Conclusion

It is the Utility's burden to justify its requested costs.[29] Further, the Commission has broad discretion with respect to the allowance of rate case expense. It would constitute an abuse of discretion to automatically award rate case expense without reference to the prudence of the costs incurred in the rate case proceedings.[30] In summary, staff recommends that Labrador's revised rate case expense of $204,452 be decreased by $121,078 for excessive, unsupported and unreasonable rate case expense. The appropriate total rate case expense is $83,374. A breakdown of rate case expense is as follows:

[27] See Order No. PSC-11-0514-PAA-WS, Issued November 03, 2011, in Docket No. 100426-WS, In re: Application for increase in water and wastewater rates in Lake County by Lake Utility Services, Inc. at p. 31.
[28] Staff anticipates that both the interim notice and final notice would be one page each while the combined initial and customer meeting notice would be four pages.
[29] See Florida Power Corp. v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982)
[30] See Meadowbrook Util. Sys., Inc. v. FPSC, 518 So. 2d 326, 327 (Fla. 1st DCA 1987), rev. den., 529 So. 2d 694 (Fla. 1988)

Table 14-3

Description	MFR Estimated	Utility Revised Actual & Estimated	Staff Adjustments	Total
Legal Fees	$82,325	$35,295	($9,836)	$25,459
Accounting Consultant Fees	67,250	49,813	0	49,813
Engineering Consultant Fees	3,900	3,238	(2,000)	1,238
WSC In-house Fees	87,928	89,906	(89,906)	0
Filing Fee	4,000	4,000	0	4,000
Travel - WSC	3,200	3,200	(3,200)	0
Temp Employee Fess - WSC	2000	2,000	(1,969)	31
Miscellaneous	12,000	12,000	(11,862)	138
Notices, Postage	5,000	5,000	(2,305)	2,695
Total Rate Case Expense	$267,603	$204,452	($121,078)	$83,374
Annual Amortization	$66,901	$51,113	($30,269)	$20,844

In its MFRs, Labrador requested total rate case expense of $267,603, which amortized over four years is $66,901, or $33,718 for water and $33,183 for wastewater. Based on the adjustments recommended above, total rate case expense should be decreased by $184,229 ($267,603 - $83,374), and the annual amortization amounts by $23,213 for water and $22,844 for wastewater.

In conclusion, staff recommends that Labrador has failed to demonstrate that the requested level of expenses to prepare and process the instant case has more than tripled over the amount approved to process the 2008 rate case. To improve the efficiency of the Commission's evaluation of rate case expense, staff recommends the Utility compile and present detailed records regarding the costs incurred by both in-house staff and outside consultants in all future cases.

REVENUE REQUIREMENT

Issue 15: What is the appropriate revenue requirement for the test year ended December 31, 2010?

Recommendation: The following revenue requirement should be approved.

	Test Year Revenue	$ Increase	Revenue Requirement	% Increase
Water	$249,568	$51,655	$301,223	20.70%
Wastewater	$445,644	45,449	$491,093	10.20%

(Springer)

Staff Analysis: In its filing Labrador requested revenue requirements to generate annual revenue of $355,634 and $549,422 for water and wastewater, respectively. These requested revenue requirements represent revenue increases of $110,904, or approximately 45 percent, for water and $110,312, or approximately 25 percent, for wastewater.

Consistent with staff's recommendations concerning the underlying rate base, cost of capital, and operating income issues, staff recommends approval of rates designed to generate a water revenue requirement of $301,223 and a wastewater revenue requirement of $491,093. The recommended water revenue requirement exceeds staff's adjusted test year revenue by $51,655, or 20.70 percent, for water. The recommended wastewater revenue requirement exceeds staff's adjusted test year revenue by $45,449 or 10.20 percent. These recommended pre-repression revenue requirements will allow the Utility the opportunity to recover its expenses and earn an 8.26 percent return on its investment in water and wastewater rate base.

RATE STRUCTURE AND RATES

Issue 16: What are the appropriate rate structures for the Utility's water and wastewater systems?

Recommendation: The appropriate rate structure for the Utility's water system is the base facility charge (BFC)/uniform gallonage charge rate structure. The BFC cost recovery allocations should be set at 40 percent. The appropriate rate structure for the utility's wastewater system is the BFC/gallonage charge rate structure. The BFC cost recovery allocation should be set at 50 percent. Residential wastewater consumption should remain capped for billing purposes at 6 kgal per month. The general service wastewater gallonage charge should be 1.2 times the corresponding residential gallonage charge. (Thompson)

Staff Analysis: The current rate structure for the Utility's water system is the BFC/uniform gallonage charge rate structure, with a monthly BFC of $9.16. Customers are also charged $6.78 for each 1,000 gallons (kgal) used. This rate structure is considered usage-sensitive, because customers are charged for all gallons consumed. Staff takes several things into consideration when designing rates, including the current rate structure, characteristics of the Utility's customer base, various conditions of the Utility's Consumptive Use Permit, and current and anticipated climatic conditions in the Utility's service area. Staff performed detailed analyses of Labrador's billing data in order to evaluate various BFC cost recovery percentages. The goals of the evaluation were to select the rate design parameters that: 1) allow the utility to recover its revenue requirement; and 2) equitably distribute cost recovery among the utility's customers. Based on a detailed billing analysis of the residential class, approximately 70 percent of all of the water bills have been accounted for at a monthly consumption of 2 kgal or less. This review indicates that the residential customer base is seasonal, with an average consumption per customer of 1.56 kgal per month. Staff recommends a continuation of the current rate structure with the BFC cost recovery allocation set at 40 percent.

Staff's recommended rate structure, plus two alternative rate structures, is shown on Table 16-1 on the following page.

The current rate structure for the Utility's wastewater system is a BFC/uniform gallonage charge rate structure, with a monthly BFC of $22.38. Customers are also charged $9.98 for each 1,000 gallons (kgal) used with a maximum of 6,000 gallons for residential customers. General service wastewater gallonage charge is set at 1.2 times the corresponding residential gallonage charge. Staff recommends a continuation of this current rate structure and an across-the-board increase.

Based on the foregoing, staff recommends that the appropriate rate structure for the Utility's water system is the BFC/uniform gallonage charge rate structure. The BFC cost recovery allocation should be set at 40 percent. The appropriate rate structure for the Utility's wastewater system is the BFC/gallonage charge rate structure. The BFC cost recovery allocation should be set at 50 percent. Residential wastewater consumption should remain capped for billing purposes at 6 kgal per month. The general service gallonage charge should be 1.2 times greater than the corresponding residential gallonage charge.

Table 16-1

LABRADOR UTILITIES, INC. STAFF'S RECOMMENDED AND ALTERNATIVE RATE STRUCTURES FOR THE WATER SYSTEM			
Current Rate Structure and Rates		**Recommended Rate Structure and Rates**	
BFC/uniform kgal		BFC/uniform kgal BFC = 40%	
BFC	$9.16	BFC	$10.58
All kgals	$6.78	All kgals	$8.44
Typical Monthly Bills		Typical Monthly Bills	
Cons (kgal)		Cons (kgal)	
0	$9.16	0	$10.58
2	$22.72	2	$27.46
3	$29.50	3	$35.90
5	$43.06	5	$52.78
7	$56.62	7	$69.66
10	$76.96	10	$94.98
Alternative 1		**Alternative 2**	
BFC/uniform kgal BFC = 45%		BFC/uniform kgal BFC = 50%	
BFC	$11.90	BFC	$13.23
All kgal	$7.74	All kgal	$7.04
Typical Monthly Bills		Typical Monthly Bills	
Cons (kgal)		Cons (kgal)	
0	$11.90	0	$13.23
2	$27.38	2	$27.31
3	$35.12	3	$34.35
5	$50.60	5	$48.43
7	$66.08	7	$62.51
10	$89.30	10	$83.63

Issue 17: What are the appropriate rates for this utility?

Recommendation: The appropriate monthly water rates are shown on Schedule No. 4-A, and the corresponding appropriate monthly wastewater rates are shown on Schedule No. 4-B. Excluding miscellaneous service revenue, the recommended water rates are designed to produce revenue of $300,268 while the recommended wastewater rates are designed to produce revenue of $490,515. The Utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. In addition, the rates should not be implemented until staff has approved the proposed customer notice. The Utility should provide proof of the date the notice was given within 10 days of the date of the notice. (Thompson, Springer)

Staff Analysis: Excluding miscellaneous service revenue, the recommended water rates shown on Schedule No. 4-A are designed to produce revenue of $300,268. Approximately 40 percent (or $120,107) of the water monthly service revenue is recovered through the base facility charge, while approximately 60 percent (or $180,161) represents revenue recovered through the consumption charge. Excluding miscellaneous service revenue, the recommended wastewater rates shown on Schedule No. 4-B are designed to produce revenue of $490,515. Approximately 50 percent (or $245,258) of the wastewater monthly service revenue is recovered through the base facility charge, while approximately 50 percent (or $245,258) represents revenue recovered through the consumption charge.

The Utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice. The Utility should provide proof of the date notice was given within 10 days of the date of the notice.

OTHER ISSUES

Issue 18: In determining whether any portion of the interim water and wastewater revenue increase granted should be refunded, how should the refund be calculated, and what is the amount of the refund, if any?

Recommendation: The proper refund amount should be calculated by using the same data used to establish final rates, excluding rate case expense and other items not in effect during the interim period. This revised revenue requirement for the interim collection period should be compared to the amount of interim revenue requirement granted. Based on this calculation the Utility should be required to refund 3.08 percent, or $8,838, of water annual revenue and 5.71 percent, or $28,358, of wastewater annual revenue granted under interim rates. The refund should be made with interest in accordance with Rule 25-30.360(4), F.A.C. The Utility should be required to submit proper refund reports pursuant to Rule 25-30.360(7), F.A.C. The Utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C. Further, the corporate undertaking should be released upon staff's verification that the required refunds have been made. (Springer)

Staff Analysis: In the Interim Order, the Commission authorized the collection of interim water and wastewater rates, subject to refund, pursuant to Section 367.082, F.S. The approved interim revenue requirement for water is $285,793, which represents an increase of $39,180 or 15.89 percent. The approved interim revenue requirement for wastewater is $495,882, which represents an increase of $53,416 or 12.07 percent.

According to Section 367.082, F.S., any refund should be calculated to reduce the rate of return of the Utility during the pendency of the proceeding to the same level within the range of the newly authorized rate of return. Adjustments made in the rate case test period that do not relate to the period interim rates are in effect should be removed. Rate case expense is an example of a cost which is recovered only after final rates are established.

In this proceeding, the test period for establishment of interim and final rates is the simple average test year ended December 31, 2010. Labrador's approved interim rates did not include any provisions for pro forma or projected operating expenses or plant. The interim increase was designed to allow recovery of actual interest costs and the floor of the last authorized range of return on equity.

Using the principles discussed above, staff calculated a revised interim revenue requirement of $277,910 for water and $468,102 for wastewater utilizing the same data used to establish final rates. Rate case expense was excluded because this item is prospective in nature and did not occur during the interim collection period. The revised water interim revenue requirement of $277,910 is less than the interim revenue requirement of $285,793 granted in the Interim Order, plus miscellaneous service revenue of $955, for a total of $286,748. This results in a difference of $8,838 or 3.08 percent. The revised wastewater interim revenue requirement of $468,102 is less than the interim revenue requirement of $495,882 granted in the Interim Order, plus other wastewater revenue of $578, for a total of $496,460. This results in a difference of $28,358 or 5.71 percent.

The Utility should be required to refund 3.08 percent of water revenue and 5.71 percent of wastewater revenue collected under interim rates. The refund should be made with interest in accordance with Rule 25-30.360(4), F.A.C. The Utility should be required to submit proper refund reports pursuant to Rule 25-30.360(7), F.A.C. The Utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C.

Issue 19: 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 rates should be reduced as shown on Schedule Nos. 4-A and 4-B to remove $11,114 for water and $10,937 for wastewater related the annual rate case expense, grossed-up for RAFs, which is being amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the four-year rate case expense recovery period, pursuant to Section 367.0816, F.S. 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. (Springer)

Staff Analysis: Section 367.0816, F.S., requires rates to be reduced immediately following the expiration of the four-year amortization period by the amount of the rate case expense previously included in the rates. The reduction will reflect the removal of revenue associated with the amortization of rate case expense, the associated return included in working capital, and the gross-up for RAFs, which is $11,114 for water and $10,937 for wastewater. The decreased revenue will result in the rate reduction recommended by staff on Schedule Nos. 4-A and 4-B.

The Utility should be required to file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice. Labrador should provide proof of the date notice was given within 10 days of the date of the notice.

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

Issue 20: Should the Utility be required to provide proof, within 90 days of an effective order finalizing this docket, that it has adjusted its books for all the applicable National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts (USOA) primary accounts associated with the Commission approved adjustments

Recommendation: Yes. To ensure that the Utility adjusts its books in accordance with the Commission's decision, Labrador should provide proof, within 90 days of the final order in this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made. (Springer)

Staff Analysis: To ensure that the Utility adjusts its books in accordance with the Commission's decision, Labrador should provide proof, within 90 days of the final order in this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made.

Issue 21: Should this docket be closed?

Recommendation: No. If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the Utility and approved by staff, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively. (M. Brown, Springer)

Staff Analysis: If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the Utility and approved by staff, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively.

	Labrador Utilities, Inc. Schedule of Water Rate Base Test Year Ended 12/31/2010					Schedule No. 1-A Docket No. 110264-WS
	Description	**Test Year Per Utility**	**Utility Adjust-ments**	**Adjusted Test Year Per Utility**	**Staff Adjust-ments**	**Staff Adjusted Test Year**
1	Plant in Service	$962,062	($86,079)	$875,983	($11,865)	$864,118
2	Land and Land Rights	529	(253)	276	0	276
3	Accumulated Depreciation	(344,659)	147,003	(197,656)	9,558	(188,098)
4	CIAC	(342)	0	(342)	0	(342)
5	Amortization of CIAC	38	0	38	0	38
6	Acquisition Adjustments	(351,387)	351,387	0	0	0
7	Accum. Amort. o Acq. Adjust.	66,690	(66,690)	0	0	0
8	Working Capital Allowance	0	25,674	25,674	(6,021)	19,653
9	Rate Base	$332,931	$371,042	$703,973	($8,328)	$695,645

	Labrador Utilities, Inc. Schedule of Wastewater Rate Base Test Year Ended 12/31/2010					Schedule No. 1-B Docket No. 110264-WS
	Description	**Test Year Per Utility**	**Utility Adjust-ments**	**Adjusted Test Year Per Utility**	**Staff Adjust-ments**	**Staff Adjusted Test Year**
1	Plant in Service	1,865,420	145,067	2,010,487	(21,098)	1,989,389
2	Land and Land Rights	0	271	271	0	271
3	Accumulated Depreciation	(609,112)	(79,283)	(688,395)	24,183	(664,212)
4	Working Capital Allowance	0	32,523	32,523	(6,278)	26,245
5	Rate Base	$1,256,308	$98,578	$1,354,886	($3,193)	$1,351,693

	Labrador Utilities, Inc. Adjustments to Rate Base Test Year Ended 12/31/2010	Schedule No. 1-C Docket No. 110264-WS	
	Explanation	**Water**	**Wastewater**
	Plant In Service		
1	Adjustments from Staff Audit Findings to which the Utility agrees. (Issue 3)	($5,287)	($14,625)
2	Reflect appropriate amount for Project Phoenix Divestitures. (Issue 4)	(6,578)	(6,473)
	Total	($11,865)	($21,098)
	Accumulated Depreciation		
1	Adjustments from Staff Audit Findings to which the Utility agrees. (Issue 3)	$5,302	$18,346
2	Reflect appropriate amount for Project Phoenix Divestitures. (Issue 4)	4,077	4,011
3	Reverse pro forma adjustment to annualize accum. Depreciation. (Issue 5)	179	1,826
	Total	$9,558	$24,183
	Working Capital		
	Reflect appropriate working capital. (Issue 7)	($6,021)	($6,278)

Labrador Utilities, Inc.
Capital Structure-Simple Average
Test Year Ended 12/31/2010

Schedule No. 2
Docket No. 110264-WS

	Description	Total Capital	Specific Adjust-ments	Subtotal Adjusted Capital	Pro rata Adjust-ments	Capital Reconciled to Rate Base	Ratio	Cost Rate	Weighted Cost
Per Utility									
1	Long-term Debt	$180,000,000	$0	$180,000,000	($178,998,935)	$1,001,065	48.62%	6.65%	3.23%
2	Short-term Debt	8,500,000	0	8,500,000	(8,452,816)	47,184	2.29%	7.36%	0.17%
3	Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%
4	Common Equity	171,000,439	0	171,000,439	(170,049,358)	951,081	46.19%	10.51%	4.86%
5	Customer Deposits	800	0	800	0	800	0.04%	6.00%	0.00%
6	Deferred Income Taxes	58,729	0	58,729	0	58,729	2.85%	0.00%	0.00%
7	**Total Capital**	$359,559,968	$0	$359,559,968	($357,501,109)	$2,058,859	100.00%		8.26%
Per Staff									
8	Long-term Debt	$180,000,000	$0	$180,000,000	($179,004,715)	$995,285	48.61%	6.65%	3.23%
9	Short-term Debt	8,500,000	0	8,500,000	(8,453,000)	47,000	2.30%	7.36%	0.17%
10	Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%
11	Common Equity	171,000,439	0	171,000,439	(170,054,915)	945,524	46.18%	10.51%	4.86%
12	Customer Deposits	800	0	800	0	800	0.04%	6.00%	0.00%
13	Deferred Income Taxes	58,729	0	$58,729	$0	$58,729	2.87%	0.00%	0.00%
14	**Total Capital**	$359,559,968	$0	$359,559,968	($357,512,631)	$2,047,337	100.00%		8.26%

	LOW	HIGH
RETURN ON EQUITY	9.51%	11.51%
OVERALL RATE OF RETURN	7.80%	8.72%

Labrador Utilities, Inc.
Statement of Water Operations
Test Year Ended 12/31/2010

Schedule No. 3-A
Docket No. 110264-WS

	Description	Test Year Per Utility	Utility Adjust-ments	Adjusted Test Year Per Utility	Staff Adjust-ments	Staff Adjusted Test Year	Revenue Increase	Revenue Requirement
1	**Operating Revenues:**	$244,730	$110,904	$355,634	($106,066)	$249,568	$51,655	$301,223
							20.70%	
	Operating Expenses							
2	Operation & Maintenance	$350,514	($145,121)	$205,393	($48,170)	$157,223		$157,223
3	Depreciation	49,180	(11,407)	37,773	(2,786)	34,987		34,987
4	Amortization	0	0	0	0	0		0
5	Taxes Other Than Income	73,988	(40,284)	33,704	(4,858)	28,846	2,324	31,171
6	Income Taxes	12,639	7,982	20,621	(18,803)	1,818	18,563	20,381
7	**Total Operating Expense**	$486,321	($188,830)	$297,491	($74,617)	$222,874	$20,888	$243,762
8	**Operating Income**	($241,591)	$299,734	$58,143	($31,449)	$26,694	$30,768	$57,461
9	**Rate Base**	$332,931		$703,973		$695,645		$695,645
10	**Rate of Return**	-72.56%		8.26%		3.84%		8.26%

Labrador Utilities, Inc. — **Schedule No. 3-B**
Statement of Wastewater Operations — **Docket No. 110264-WS**
Test Year Ended 12/31/2010

	Description	Test Year Per Utility	Utility Adjust-ments	Adjusted Test Year Per Utility	Staff Adjust-ments	Staff Adjusted Test Year	Revenue Decrease	Revenue Requirement
1	**Operating Revenues:**	$439,110	$110,312	$549,422	($103,778)	$445,644	$45,449	$491,093
							10.20%	
	Operating Expenses							
2	Operation & Maintenance	$68,925	$191,258	$260,183	($50,224)	$209,959		$209,959
3	Depreciation	68,100	18,040	86,140	(5,057)	81,083		81,083
4	Amortization	0	0	0	0	0		0
5	Taxes Other Than Income	0	51,505	51,505	(4,754)	46,751	2,045	48,796
6	Income Taxes	12,437	27,250	39,687	(16,418)	23,269	16,333	39,602
7	**Total Operating Expense**	$149,462	$288,053	$437,515	($76,452)	$361,063	$18,378	$379,441
8	**Operating Income**	$289,648	($177,741)	$111,907	($27,326)	$84,581	$27,071	$111,652
9	**Rate Base**	$1,256,308		$1,354,886		$1,351,693		$1,351,693
10	**Rate of Return**	23.06%		8.26%		6.26%		8.26%

	Labrador Utilities, Inc. **Adjustment to Operating Income** **Test Year Ended 12/31/2010**	**Schedule No. 3-C** **Docket No. 110264-WS**	
	Explanation	**Water**	**Wastewater**
	Operating Revenues		
	Remove requested final revenue increase.	($106,066)	($103,778)
	Operation and Maintenance Expense		
1	Adjustments from Staff Audit Findings to which the Utility agrees. (Issue 3)	($19,224)	($22,372)
2	Reflect appropriate O&M expense for EUW adjustment. (Issue 6)	(175)	
3	Reflect appropriate amount of tank maint. & repair expense. (Issue 11)	(3,213)	
4	Audit Finding No. 15 - Remove 3% Salary Increase in April 2011. (Issue 12)	(1,704)	(1,677)
5	Reflect appropriate amount of miscellaneous and sludge removal expense.(Issue 14)	($640)	($3,330)
6	Reflect appropriate amount of rate case expense. (Issue 15)	(23,213)	(22,844)
	Total	($48,170)	($50,224)
	Depreciation Expense - Net		
1	Adjustments from Staff Audit Findings to which the Utility agrees. (Issue 3)	($287)	($946)
2	Reflect appropriate amount for Project Phoenix Divestitures. (Issue 4)	(2,320)	(2,285)
3	Reverse pro forma adjustment to annualize depreciation expense. (Issue 5)	(179)	(1,826)
	Total	($2,786)	($5,057)
	Taxes Other Than Income		
1	RAFs on revenue adjustments above.	($4,773)	($4,670)
2	Adjustments from Staff Audit Findings to which the Utility agrees. (Issue 3)	(85)	(84)
	Total	($4,858)	($4,754)

Labrador Utilities, Inc. **Schedule No. 4-A**
Water Monthly Service Rates **Docket No. 110264-WS**
Test Year Ended 12/31/2010

	Rates Prior to Filing	Commission Approved Interim	Utility Requested Final	Staff Recomm. Final	4-Year Rate Reduction
Residential					
Base Facility Charge, 5/8 Meter Size:	$9.16	$10.49	$13.07	$10.58	$0.39
Gallonage Charge (per 1,000 gallons)	$6.78	$7.77	$9.67	$8.44	$0.31
General Service					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	$9.16	$10.49	$13.07	$10.58	$0.39
3/4"	$13.58	$15.75	$19.62	$26.45	$0.98
1"	$22.63	$26.24	$32.68	$52.90	$1.95
1-1/2"	$45.26	$52.48	$65.35	$84.64	$3.12
2"	$72.42	$83.97	$104.57	$169.28	$6.25
3"	$144.84	$167.94	$209.15	$264.50	$9.76
4"	$226.30	$262.39	$326.78	$529.00	$19.52
6"	$452.62	$524.81	$653.58	$846.40	$31.23
Gallonage Charge (per 1,000)	$6.70	$7.77	$9.67	$8.44	$0.31
Irrigation Service					
Base Facility Charge, 2":	$72.42	$83.97	$104.57	$84.64	$3.12
Gallonage Charge (per 1,000 gallons)	$6.70	$7.77	$9.67	$8.44	$0.31
	Typical Residential Bills 5/8" x 3/4" Meter				
3,000 Gallons	$29.50	$33.80	$42.08	$35.90	
5,000 Gallons	$43.06	$49.34	$61.42	$52.78	
10,000 Gallons	$76.96	$88.18	$109.77	$94.98	

Labrador Utilities, Inc. **Schedule No. 4-B**
Wastewater Monthly Service Rates **Docket No. 110264-WS**
Test Year Ended 12/31/2010

	Rates Prior to Filing	Commission Approved Interim	Utility Requested Final	Staff Recomm. Final	4-Year Rate Reduction
Residential					
Base Facility Charge, 5/8 Meter Size:	$22.38	$24.91	$27.59	$24.66	$0.54
Gallonage Charge - Per kgal (10 kgal cap)	$9.98	$11.11	$12.31	$11.00	$0.24
General Service					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	$22.38	$24.91	$27.59	$24.66	$0.54
1"	$33.58	$37.36	$41.40	$61.65	$1.36
1-1/2"	$55.96	$62.27	$69.00	$123.30	$2.72
2"	$111.91	$124.52	$137.99	$197.28	$4.35
3"	$179.07	$199.24	$220.79	$394.56	$8.70
4"	$358.14	$398.47	$441.59	$616.50	$13.59
6"	$559.59	$622.62	$689.97	$1,233.00	$27.18
8"	$1,119.18	$1,245.23	$1,379.95	$1,972.80	$43.49
Gallonage Charge - Per 1,000 Gallons	$11.98	$13.33	$14.77	$13.20	$0.29
	Typical Residential Bills 5/8" x 3/4" Meter				
3,000 Gallons	$52.32	$58.23	$64.52	$57.66	
5,000 Gallons	$72.28	$80.45	$89.14	$79.66	
10,000 Gallons	$122.18	$135.99	$150.69	$134.66	
(Wastewater Gallonage Cap - 10,000 Gallons)					