

State of Florida



Public Service Commission

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-M-E-M-O-R-A-N-D-U-M-

DATE: August 13, 2014

TO: Office of Commission Clerk (Stauffer)

FROM: Division of Engineering (M. Watts, Rieger)
Division of Accounting and Finance (Barrett)
Division of Economics (Roberts)
Office of the General Counsel (Murphy)

RE: Docket No. 130194-WS – Application for staff-assisted rate case in Lake County by Lakeside Waterworks, Inc.

--STAFF REPORT--

This Staff Report is preliminary in nature. The Commission staff's final recommendation will not be filed until after the customer meeting on September 11, 2014.

Table of Contents

Case Background (M. Watts, Rieger)	3
Issue 1 Quality of Service (M. Watts, Rieger).....	4
Issue 2 Used and Useful (M. Watts, Rieger)	5
Issue 3 Average Test Year Rate Base (Barrett)	8
Issue 4 Rate of Return (Barrett).....	12
Issue 5 Test Year Revenues (Roberts).....	13
Issue 6 Operating Expenses (Barrett)	14
Issue 7 Operating Ratio Method (Barrett)	24
Issue 8 Revenue Requirement (Barrett).....	27
Issue 9 Rate Structures and Rates (Roberts).....	29
Issue 10 Four-Year Rate Reduction (Barrett).....	32
Issue 11 Initial Customer Deposits (Roberts).....	33
Issue 12 Late Payment Charge (Roberts).....	34
Issue 13 Temporary Rates (Barrett).....	35
Issue 14 Proof of Adjustments (Barrett).....	38
Issue 15 Close Docket (Murphy)	39
Schedule No. 1-A - Water Rate Base.....	40
Schedule No. 1-B - Wastewater Rate Base.....	41
Schedule No. 1-C - Adjustments to Rate Base	42
Schedule No. 2 - Schedule of Capital Structure	43
Schedule No. 3-A - Schedule of Water Operating Income.....	44
Schedule No. 3-B - Schedule of Wastewater Operating Income.....	45
Schedule No. 3-C - Adjustments to Operating Income	46
Schedule No. 3-D - Analysis of Water Operation and Maintenance Expense	49
Schedule No. 3-E - Analysis of Wastewater Operation and Maintenance Expense.....	50
Schedule No. 4-A - Monthly Water Rates	51
Schedule No. 4-B - Monthly Wastewater Rates	52

Case Background

On December 20, 2012, an application was filed for the transfer of Shangri-La by the Lake Utilities, Inc.'s (Shangri-La) water and wastewater systems, and Certificate Nos. 567-W and 494-S, to Lakeside Waterworks, Inc. (Lakeside or Utility). The transfer was approved on September 18, 2013.¹

On July 19, 2013, Lakeside filed an application for a staff-assisted rate case (SARC). The official filing date of the SARC has been determined to be September 17, 2013. Lakeside is a Class C water and wastewater utility serving approximately 183 water and 175 wastewater residential customers in Lake County. The last SARC for the system occurred in Docket No. 110130-WS, which was withdrawn by Shangri-La. The system was originally certificated in Docket No. 940653-WS.² There have not been any other rate cases for this system, thus the Commission has not previously set used and useful percentages.

This staff report is a **preliminary** analysis of the Utility prepared by Commission staff to give utility customers and the Utility an advanced look at what staff may be proposing. The final recommendation to the Commission (currently scheduled to be filed November 13, 2014, for the November 25, 2014 Commission Conference) will be revised as necessary using updated information and results of customer quality of service or other relevant comments received at the customer meeting. The Commission has jurisdiction in this case pursuant to Sections 367.011, 367.0814, 367.101, and 367.121, Florida Statutes (F.S.)

¹ See Order No. PSC-13-0425-PAA-WS, issued September 18, 2013, in Docket No. 120317-WS: In re: Application for approval to transfer water and wastewater system Certificate Nos. 567-W and 494-S in Lake County from Shangri-La by the Lake Utilities, Inc. to Lakeside Waterworks, Inc.

² See Order No. PSC-96-0062-FOF-WS, issued January 12, 1996, in Docket No. 940653-WS: In re: Application for certificates to provide water and wastewater services in Lake County by Shangri-La By The Lake Utilities, Inc.

Discussion of Issues

Issue 1: Is the quality of service provided by Lakeside satisfactory?

Preliminary Recommendation: Staff's recommendation regarding quality of service will not be finalized until after the September 11, 2014 customer meeting. (M. Watts, Rieger)

Staff Analysis: Pursuant to Rule 25-30.433(1), Florida Administrative Code (F.A.C.), in water and wastewater rate cases, the Commission shall determine the overall quality of service provided by a utility. This is derived from an evaluation of three separate components of the utility operations. These components are the quality of the utility's product, the operational conditions of the utility's plant and facilities, and the utility's attempt to address customer satisfaction. Lakeside's compliance with the Department of Environmental Protection (DEP) and St. Johns River Water Management District (SJRWMD) regulations, and customer comments or complaints received by the Commission, are also reviewed.

Quality of Utility's Product and Operating Condition of the Utility's Plant and Facilities

Lakeside's service area is located next to Lake Eustis, near Leesburg, Florida, in Lake County. The raw water source is ground water, which is obtained from two wells in the service area and is treated. The water treatment processing sequence is to pump raw water from the aquifer, perform an aeration process, inject calcium hypochlorite, store the treated water in a tank, and distribute. Lakeside is current in all of its required chemical analyses. Laboratory tests show that Lakeside's finished water product is well below the maximum contaminant levels allowed by DEP for all primary and secondary contaminants, and there appears to be no water compliance issues with this facility.

The wastewater treatment plant is an extended aeration activated sludge facility with chlorinated effluent sent to a spray field with a backup percolation pond for wet weather conditions. Also, there appears to be no wastewater compliance issues with this facility.

The Utility's Attempt to Address Customer Satisfaction

As of July 18, 2014, the Commission has received correspondence from five customers concerning the rate case. Four customers requested the date of the customer meeting be postponed from July 24, 2014, to the fall, and one customer objected to a rate increase. There are no outstanding complaints in the Commission's Complaint Tracking System, and there were no complaints to DEP during the test year. A customer meeting is scheduled to be held on September 11, 2014, in Leesburg, Florida. A determination of the Utility's attempt to address customer satisfaction will be decided at a later date, pending review of customer comments made at the upcoming meeting.

Summary

Quality of service will be determined at a later date, pending review of comments made at the September 11, 2014 customer meeting.

Issue 2: What are the used and useful percentages (U&U) of Lakeside's water treatment plant (WTP), water storage facilities, wastewater treatment plant (WWTP) and distribution and collection systems? (M. Watts, Rieger)

Preliminary Recommendation: Lakeside's WTP should be considered 42.8 percent U&U, its water storage facilities should be considered 100 percent U&U, its WWTP should be considered 16.8 percent U&U, and its distribution and collection systems should be considered 100 percent U&U. Staff recommends that, in consideration of 10 percent excessive unaccounted for water (EUW), a corresponding adjustment be made to decrease purchased power and chemical expenses for water by \$266 and \$32, respectively. There is no indication of excessive inflow and infiltration (I&I). (M. Watts, Rieger)

Staff Analysis: Lakeside's water system has an 8-inch well rated at 850 gallons per minute (gpm) and a 6-inch well rated at 270 gpm, for a total capacity of 1,120 gpm. Storage consists of a 20,000-gallon concrete ground storage tank with aeration, and two steel hydropneumatic tanks with capacities of 3,000 gallons and 5,000 gallons. A hypochlorination system is used for disinfection and water from the tanks is pumped into the water distribution system.

The distribution system is a composite network of approximately 2,820 linear feet of 10 inch PVC pipe, 2,828 linear feet of 8 inch PVC pipe, 3,450 linear feet of 6 inch PVC pipe, 1,700 linear feet of 4 inch PVC pipe, and 2,800 linear feet of 1.5 inch PVC pipe. According to the Utility, there are 11 fire hydrants in its service area.

The WWTP is a 50,000 gallon per day (gpd) extended aeration activated sludge facility. The chlorinated effluent is sent to a 3.2 acre restricted public access spray field with a backup percolation pond for wet weather conditions.

The collection system is a composite network of force mains, collecting mains, and four lift stations. The force mains consist of approximately 3,211 linear feet of 4 inch PVC pipe and 2,324 linear feet of 3 inch PVC pipe. The collecting mains consist of approximately 9,768 linear feet of 4 inch PVC pipe and 4,277 linear feet of 3 inch PVC pipe. According to the Utility, there are 15 manholes.

Excessive Unaccounted for Water

Rule 25-30.4325, F.A.C., describes EUW as unaccounted for water in excess of 10 percent of the amount produced. When establishing the Rule, the Commission recognized that some uses of water are readily measurable and others are not. Unaccounted for water is all water that is produced that is not sold, metered, or accounted for in the records of the utility. The Rule provides that to determine whether adjustments to plant and operating expenses, such as purchased electrical power and chemicals cost, are necessary, the Commission will consider all relevant factors as to the reason for EUW, solutions implemented to correct the problem, or whether a proposed solution is economically feasible. The unaccounted for water is calculated by subtracting both the gallons used for other purposes, such as flushing, and the gallons sold to customers from the total gallons pumped for the test year. The Utility's records indicated 9,526,500 gallons of water were produced during the test year, 7,659,000 gallons of water were sold to customers, and no gallons were used for other purposes. Thus, unaccounted for water is

20 percent of the amount produced, resulting in an EUW of 10 percent, or 952,650 gallons for the test year (which is equivalent to 2,610 gallons per day). An explanation justifying EUW has not been provided. Therefore, staff recommends that a corresponding adjustment should be made to decrease purchased power and chemical expenses for water by \$266 ($\$2,655 \times 10$ percent), and \$32 ($\318×10 percent), respectively.

Water Treatment Plant Used & Useful

Pursuant to Rule 25-30.4325, F.A.C., the U&U percentage of a WTP with storage is calculated by dividing the peak system demand by the firm reliable capacity (FRC). The system demand is based on the single maximum day in the test year less EUW, plus a fire flow and a growth allowance.

Because the Utility has storage capacity, the FRC is based on 16 hours of pumping excluding the largest well. The Utility has two wells rated at 850 gpm and 270 gpm. Thus, using the capacity of the smaller well, the Utility's FRC is 259,200 gpd ($270 \text{ gpm} \times 60 \text{ min/hr} \times 16 \text{ hrs}$).

The peak day of 50,400 gallons, which occurred on March 7, 2013, appears to be appropriate since it is not associated with unusual occurrences. Fire flow for the Utility's service area is 500 gpm for 2 hours, or 60,000 gpd. As discussed above, the Utility's EUW is 2,610 gpd. Pursuant to Rule 25-30.431, F.A.C., a linear regression analysis of the Utility's historical growth pattern results in 12 equivalent residential connections (ERCs) for the five-year statutory growth period. The Utility had an average of 186 ERCs for the test year, resulting in 257 gpd/ERC [$(50,400 \text{ gpd} - 2,610)/186$]. Thus, a growth allowance of 3,084 gpd is also considered. Therefore, pursuant to Rule 25-30.4325, F.A.C., staff recommends that the WTP be considered 42.8 percent U&U. [$(50,400 \text{ gpd} - 2,610 \text{ gpd} + 60,000 \text{ gpd} + 3,084 \text{ gpd})/259,200 \text{ gpd}$]

Storage Used & Useful

Pursuant to Rule 25-30.4325(8), F.A.C., for water systems with storage, if the storage capacity is less than the peak demand, the storage system should be considered 100 percent U&U. For Lakeside, since the storage capacity (20,000 gallons) is less than the peak demand (50,400 gallons), the storage system should be considered 100 percent U&U.

Inflow & Infiltration

Typically, infiltration results from groundwater entering a wastewater collection system through broken or defective pipes and joints; whereas, inflow results from water entering a wastewater collection system through manholes or lift stations. The allowance for infiltration is 500 gallons per day per inch diameter pipe per mile, and an additional 10 percent of water sold is allowed for inflow. The Utility's records indicated that there was no excessive I&I for the test year.

Wastewater Treatment Plant Used & Useful

Pursuant to Rule 25-30.432, F.A.C., the U&U analysis of the Utility's WWTP is based on the customer demand compared with the permitted plant capacity, with customer demand measured on the same basis as permitted capacity. Consideration is given for growth and I&I. Based on the annual average daily flow during the test year of 8,000 gpd and the DEP permitted plant capacity of 50,000 gpd, with 405 gpd considered for growth, staff recommends that the WWTP be considered 16.8 percent U&U.

Water Distribution and Wastewater Collection Systems Used & Useful

The U&U analysis for the water distribution and wastewater collection systems are determined by dividing the number of lots connected to the systems by the number of lots fronting mains in the service area. Consideration is given for growth, if applicable. However, staff believes that the lines that are currently recognized in the Utility's rate base serve an area in the service territory that appears to be built out. Therefore, staff recommends that the water distribution and wastewater collection systems be considered 100 percent U&U.

Summary

Lakeside's WTP should be considered 42.8 percent U&U, and the water storage facilities should be considered 100 percent U&U. Lakeside's WWTP should be considered 16.8 percent U&U, and the distribution and collection systems should be considered 100 percent U&U. Staff recommends that, in consideration of 10 percent EUW, a corresponding adjustment should be made to decrease purchased power expense by \$266 and chemical expenses by \$31.80 for water. No adjustment is recommended for excessive I&I.

Issue 3: What is the appropriate average test year rate base for Lakeside?

Preliminary Recommendation: The appropriate average test year rate base for Lakeside is \$22,021 for water and \$8,127 for wastewater. (Barrett)

Staff Analysis: The appropriate components of the Utility’s rate base include utility plant in service, accumulated depreciation, contribution-in-aid-of-construction (CIAC), amortization of CIAC, and working capital. The last proceeding that established balances for rate base was Docket No. 940653-WS.³ Staff selected the test year ended June 30, 2013, for the instant rate case. A summary of each component and the recommended adjustments follows:

Utility Plant in Service (UPIS): The Utility recorded \$138,299 for water and \$147,414 for UPIS. Staff’s adjustments to UPIS are identified in Table 3-1 below.

Description		Water	Wastewater
1.	To reflect plant balance (301) per Order No. PSC-13-0425-PAA-WS	(\$3,160)	\$0
2.	To reflect plant balance (310) per Order No. PSC-13-0425-PAA-WS	(603)	0
3.	To reflect plant balance (351) per Order No. PSC-13-0425-PAA-WS	0	(1,125)
4.	To reflect plant balance (371) per Order No. PSC-13-0425-PAA-WS	0	(1,057)
5.	To reflect plant balance (393) per Order No. PSC-13-0425-PAA-WS	0	(245)
6.	To reflect an averaging adjustment	0	(93)
7.	To reflect net pro forma plant	<u>1,632</u>	<u>923</u>
Total		<u>(\$2,131)</u>	<u>(\$1,598)</u>

The adjustments identified in lines 1-5 of Table 3-1 above are necessary to reconcile certain items to the Utility’s general ledger. Order No. PSC-13-0425-PAA-WS⁴ approved the transfer of ownership of the Utility to Lakeside. The adjustment identified on line 6 is an averaging adjustment for the wastewater plant balance, and the adjustments included in line 7 reflect the net increase of pro forma plant balances for additions that have been completed, less their associated retirement values. The pro forma plant items are discussed below.

³See Order No. PSC-96-0062-FOF-WS, issued January 12, 1996, in Docket No. 940653-WS, In re: Application for certificate to provide water and wastewater services in Lake County by Shangri-La by the lake Utilities, Inc.

⁴See Order No. PSC-13-0425-PAA-WS, issued September 18, 2013, in Docket No. 120317-WS, In re: Application for approval to transfer water and wastewater system Certificate Nos. 567-W and 494-S in Lake County from Shangri-La by the Lake Utilities, Inc. to Lakeside Waterworks, Inc.

Pro forma Plant

Lakeside is requesting cost recovery for \$6,529 in water and \$3,690 in wastewater pro forma plant, as shown in Table 3-2 below. The Utility has completed the work described for each pro forma plant item and provided invoices which staff has reviewed.

Table 3-2 Pro forma Plant			
Description		Water	Wastewater
1.	Installed Mercoid switch on Hydro Tank #2, 4 new chlorine pumps, chlorine injection system & saddle taps, installed new conduit, cleaned up electrical panel and other minor repairs	\$5,296	\$0
2.	Replaced 10 inch of 6 inch distribution pipe	1,233	0
3.	Installed new stenner pumps (2). Repaired diffusers (4) and manifold at the Wastewater Treatment Plant. Repaired and reinforced steel walkways and handrails. Repaired air header, and other minor repairs.	0	3,690
Total Plant Pro forma		<u>\$6,529</u>	<u>\$3,690</u>

Lakeside provided an invoice for \$5,296 in repairs, asserting the replacements and repairs were necessary to comply with a DEP regulatory mandate.⁵ In a data response dated May 30, 2014, the Utility stated that no specific cost savings resulted from completing this project. Staff reviewed the invoice and description of the work performed, and believes this pro forma item is justified and prudent.

The Utility provided an invoice for \$1,233 for an emergency repair of a 6 inch water main. Staff reviewed the invoice and description of the work performed, and believes this pro forma item is justified and prudent. Therefore, staff recommends a total of \$6,529 (\$5,296 + \$1,233) in pro forma water plant.

Lakeside provided an invoice for \$3,690 for replacements and repairs at the wastewater plant to comply with a DEP regulatory mandate.⁶ In a data response dated May 30, 2014, the Utility stated that no specific cost savings resulted from completing this project. Staff reviewed the invoice and description of the work performed, and believes this pro forma item is justified and prudent. Therefore, staff recommends a total of \$3,690 in pro forma wastewater plant.

Lakeside has requested cost recovery of the pro forma plant as shown in Table 3-2. Staff notes that the \$6,529 of pro forma water plant and the associated retirement results is a net increase to UPIS of \$1,632. Also, the \$3,690 of pro forma wastewater plant and the associated retirement results in a net increase to UPIS of \$923. As noted previously, the Utility has

⁵ Pursuant to Rule 62-555.320(12)(d), F.A.C.

⁶ Pursuant to Rules 62-600.410(1), 62-600.410(6), and 62-600.410(8), F.A.C.

completed the work on these projects and provided invoices which staff has reviewed. Staff recommends approval of \$1,632 in net water and \$923 in net wastewater pro forma plant.

UPIS Summary

Staff's adjustments to UPIS result in net decreases of \$2,131 and \$1,598 for water and wastewater, respectively. Staff's recommended UPIS balance is \$136,168 for water and \$145,817 for wastewater.

Land & Land Rights: The Utility recorded no test year land value for water and wastewater. As the Utility's plants are located on leased land, no adjustments are necessary. Therefore, staff recommends land balances of \$0 for water and wastewater.

Non-Used and Useful Plant: Non-Used and Useful Plant is discussed in Issue 2. Staff's adjustments to these accounts are identified in Table 3-3 below.

Description		Water	Wastewater
1.	To reflect non used and useful plant	(\$28,455)	(\$78,864)
2.	To reflect non used and useful accumulated depreciation	22,656	33,936
3.	To reflect non used and useful CIAC	0	0
4.	To reflect non used and useful accumulated amortization	(7,274)	0
Total		(\$13,073)	(\$44,928)

Contributions-In-Aid-of-Construction (CIAC): Lakeside recorded CIAC balances of \$13,776 for water and \$18,257 for wastewater. Staff made no adjustments to CIAC, and recommends a CIAC balance of \$13,776 and \$18,257 for water and wastewater, respectively.

Accumulated Depreciation: Lakeside recorded balances for accumulated depreciation of \$106,153 and \$95,725 for water and wastewater, respectively. Staff's adjustments to accumulated depreciation are identified in Table 3-4 below.

Description		Water	Wastewater
1.	To reflect the appropriate test year accumulated depreciation (AF2)	(\$464)	\$5,534
2.	To reflect an averaging adjustment	2,396	266
3.	To reflect pro forma plant repairs	4,513	2,522
Total		\$6,445	\$8,322

Staff has calculated accumulated depreciation using the prescribed rates set forth in Rule 25-30.140, F.A.C., and determined that net accumulated depreciation should be decreased by \$6,445 for water and \$8,322 for wastewater. Staff recommends an accumulated depreciation balance of \$99,708 for water and \$87,404 for wastewater.

Accumulated Amortization of CIAC: Lakeside recorded balances for amortization of CIAC of \$5,830 for water and \$11,929 for wastewater. Staff's adjustments to amortization of CIAC are identified in Table 3-5 below.

Description		Water	Wastewater
1.	To reflect the appropriate test year amortization of CIAC (AF3)	\$245	(\$5,691)
2.	To reflect an averaging adjustment	(245)	(139)
Total		<u>\$0</u>	<u>(\$5,830)</u>

Staff's net adjustments for water were off-setting amounts. The amortization of CIAC for wastewater was decreased by \$5,830. Staff recommends amortization of CIAC balances of \$5,830 for water and \$6,099 for wastewater.

Working Capital Allowance: Lakeside did not record a working capital balance for water or wastewater. Working capital is defined as the investor-supplied funds that are necessary to meet operating expenses or going-concern requirements of the Utility. Consistent with Rule 25-30.433(2), F.A.C., staff used one-eighth of the operation and maintenance (O&M) expense formula approach for calculating the working capital allowance. Applying this formula, staff recommends a working capital allowances of \$6,639 for water (based on O&M expense of \$53,113/8), and \$6,800 for wastewater (based on O&M expense of \$54,402/8). Staff recommends increasing the working capital allowances by \$6,639 for water and \$6,800 for wastewater.

Rate Base Summary: Based on the foregoing, staff recommends that the appropriate average test year rate base is \$22,080 for water and \$8,127 for wastewater. Rate base for water is shown on Schedule No. 1-A and on Schedule No. 1-B for wastewater. The related adjustments for water and wastewater are shown on Schedule No. 1-C.

Issue 4: What is the appropriate rate of return on equity and overall rate of return for Lakeside?

Preliminary Recommendation: The appropriate return on equity (ROE) is 8.74 percent with a range of 7.74 percent to 9.74 percent. The appropriate overall rate of return is 8.74 percent. (Barrett)

Staff Analysis: The Utility's capital structure consists of \$181,898 of common stock. The Utility has no long-term debt or customer deposits. The appropriate ROE is 8.74 percent using the Commission-approved leverage formula currently in effect.⁷ The Utility's capital structure has been reconciled with staff's recommended rate base. Staff recommends an ROE of 8.74 percent, with a range of 7.74 percent to 9.74 percent, and an overall rate of return of 8.74 percent. The ROE and overall rate of return are shown on Schedule No. 2.

⁷ See Order Nos. PSC-14-0272-PAA-WS, issued May 29, 2014, and PSC-14-0323-CO-WS, issued June 24, 2014, in Docket No. 140006-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 5: What are the appropriate test year revenues?

Preliminary Recommendation: The appropriate test year revenues for the Utility are \$38,806 for water and \$32,176 for wastewater. (Roberts)

Staff Analysis: Lakeside recorded total revenues for water of \$38,080 and for wastewater of \$31,949, including service revenues of \$38,050 and \$31,949 and miscellaneous revenues of \$30 and \$0, for water and wastewater, respectively. Based on staff's review of the Utility's billing determinants and the rates that were in effect during the test year, staff recommends the Utility increase service revenues by \$726 and \$227 for water and wastewater, respectively, to reflect the appropriate test year revenues. Based on the above, staff recommends that the appropriate test year revenues for water and wastewater are \$38,806 ($\$38,050 + \$726 + \30) and \$32,176 ($\$31,949 + \227), respectively. Test year revenues are shown on Schedule Nos. 3-A and 3-B and adjustments are shown on Schedule No. 3-C.

Issue 6: What is the appropriate amount of operating expense?

Preliminary Recommendation: The appropriate amount of operating expense for water is \$61,705. The appropriate amount of operating expense for wastewater is \$60,077. (Barrett)

Staff Analysis: Lakeside recorded operating expense of \$44,358 for water and \$42,164 for wastewater for the test year ended June 30, 2013. The test year O&M expenses have been reviewed, and invoices, canceled checks, and other supporting documentation have been examined. Staff has made several adjustments to the Utility’s operating expenses as summarized below:

Salaries and Wages - Employees (601/701) - Lakeside recorded \$1,799 for water and \$1,799 for wastewater employee salaries expense in these accounts. Staff has made adjustments to remove these amounts because the expense associated with labor is captured in the Contractual Services – Other accounts (636/736). Staff recommends \$0 for these accounts for water and wastewater.

Salaries and Wages - Officers (603/703) – The Utility recorded \$1,727 for water and \$849 for wastewater officer salaries expense. Staff has made adjustments to increase water by \$773 and wastewater by \$1,651 because the officer administers and oversees the Utilities’ management services agreement, which is addressed in the discussion of Contractual Services – Other (636/736). Staff recommends salaries and wages for officers of \$2,500 for water and \$2,500 for wastewater.

Purchased Power (615/715) - Lakeside recorded \$1,916 for purchased power expense for water and \$3,519 for wastewater in these accounts. Staff’s adjustments to these accounts are identified in Table 6-1 below.

Description		Water	Wastewater
1.	To reflect the appropriate test year purchased power (AF5)	\$739	\$1,336
2.	To reflect a rate increase from Duke Power Company	83	731
3.	To reflect an adjustment for excessive unaccounted water	(266)	0
Total		<u>\$556</u>	<u>\$2,067</u>

Staff increased these balances by \$739 for water and \$1,336 for wastewater based on invoices for purchased power. Staff made an additional adjustment to reflect a rate increase implemented by Duke Power Company, effective January 1, 2014. The final adjustment removes \$266 for excessive unaccounted for water, which was previously discussed in Issue 2. The net of these adjustments increases the expense for water by \$556, and increases the expense for wastewater by \$2,067. Staff recommends purchased power expense of \$2,472 for water and \$5,586 for wastewater.

Fuel For Power Production (616) - The Utility recorded \$437 for this expense. Based on a lack of documentation, staff has made an adjustment to remove \$108 from this account. Staff recommends a balance of \$329 for this account.

Chemicals (618/718) - The Utility recorded \$269 for water and \$404 for wastewater for chemicals expense. Staff's adjustments to these accounts are identified in Table 6-2 below.

Table 6-2 Adjustments to Chemicals			
Description		Water	Wastewater
1.	To reflect the appropriate test year chemicals expense	\$201	\$116
2.	To reflect an adjustment for excessive unaccounted water	(32)	0
Total		<u>\$169</u>	<u>\$116</u>

Staff increased the water balance by \$201 and the wastewater balance by \$116 based on invoices for chemicals. Staff also made an adjustment to remove \$32 of water expense for excessive unaccounted for water, which was previously discussed in Issue 2. The net of the adjustments is an increase of \$169 for water, and an increase of \$116 for wastewater. Staff recommends chemical expense of \$438 for water and \$520 for wastewater.

Materials and Supplies (620/720) - The Utility recorded \$1,767 for materials and supplies expense for water and \$77 for wastewater. Staff has made adjustments to remove \$926 from the water balance, and increased the balance for wastewater by \$63, based on invoices for materials and supplies. Staff recommends balances of \$841 for water and \$140 for wastewater.

Contractual Services - Billing (630/730) - Lakeside recorded \$2,030 for water and \$18,230 for wastewater. Staff has made adjustments to remove these amounts because billing service costs are captured in the Contractual Services – Other accounts (636/736). Staff recommends \$0 for these accounts for water and wastewater.

Contractual Services - Professional (631/731) - Lakeside recorded \$6,318 for water and \$1,334 for wastewater. Staff made adjustments to the water balance to remove \$3,698 due to a lack of documentation. Staff made an adjustment to increase wastewater by \$1,286 to correct an allocation between water and wastewater balances. Staff recommends balances of \$2,620 for water and \$2,620 for wastewater for this account.

Contractual Services – Other (636/736) – Lakeside recorded \$18,259 for water and \$4,824 for wastewater for Contractual Services - Other. Staff has increased these amounts by \$19,938 for water and \$30,906 for wastewater to account for the Utilities' management services agreement, as discussed below.

Discussion

Staff notes that the prior owner of this Utility paid outside sources for operating and billing services for the water and wastewater systems. On November 16, 2012, the Utility signed

a five year management services agreement with U.S. Water Services Corporation (U.S. Water contract). Table 4 of the U.S. Water contract provides a summary of the scope of the agreement, setting forth the respective cost responsibilities for the Utility's owner and U.S. Water Services Corporation.⁸ The U.S. Water contract:

- Puts in place certified utility operators with a focus on preventative and prescriptive maintenance services.
- States that all Customer Service/Billing/Collection functions are provided by the same entity (U.S. Water Services Corporation).
- Covers the costs of minor repairs (up to a \$400 threshold).
- States that testing services and permitting expenses are covered by U.S. Water.
- States that meter/hydrant testing is provided by U.S. Water.
- Record keeping & governmental relations are addressed by U.S. Water.

Section 4 of the U.S. Water contract addresses the monthly fees for service. Per the contract, Lakeside is obligated to pay U.S. Water Services Corporation \$3,183 monthly for the water operation and \$2,978 monthly for the wastewater operation (for a monthly total of \$6,161).

Bids for Management Service and Pricing

In a data request response dated March 25, 2014, the Utility states that it sought other bidders for the management services provided in the U.S. Water contract. Bids were solicited from two local companies and these contractors stated they were "not capable or interested in providing the required services." As a result, the Utility entered into the management services agreement with U.S. Water Services Corporation.

In a data request response dated April 30, 2014, the Utility provided information on how the cost of its contract measures up to a comparative study conducted by Wetzel Consulting, LLC (WetCon) for the Florida Governmental Utility Authority (FGUA). In early 2013, the FGUA Board hired WetCon, an independent consultant, to evaluate FGUA systems against others in the South, using American Water Works Association (AWWA) Performance Indicators. Eleven indicators were captured in the WetCon study. Lakeside used the average values from three of the indicators for benchmarking purposes: the annual cost per account indicator for Customer Service and the combined metrics for water and wastewater O&M.

In its April 30, 2014 response, the Utility states that the WetCon study values were calculated to reflect average costs per service, and claims that Lakeside's average cost per service of \$206.51 compares favorably with the results from the WetCon study. Staff developed Table 6-3 to present how the \$206.51 was calculated:

⁸ The complete U.S. Water contract is in the audit staff's work papers. Table 4 is on Audit work paper 43-3.21.

Table 6-3 Calculation of Average contract cost per service for Lakeside Waterworks (\$ per Account)					
Contracted Service for Lakeside Waterworks	Annual Contracted Amounts (a)	Mathematical Average of Column (a) (\$73,932/2) (b)	Number of Customers (c)	Mathematical Average of Column (c) (358/2) (d) = (c)/2	Annual Cost per Customer for each Contracted Service (e) = (b)/(d)
Water	\$38,196	\$36,966	183	179	\$206.51
Wastewater	<u>35,736</u>		<u>175</u>		
Total	<u>\$73,932</u>		<u>358</u>		

Three steps are involved in calculating the average annual cost per service. First, the Utility determined the mathematical average of the annual contracted amounts, as shown in columns (a) and (b) of Table 6-3. Second, the Utility determined the mathematical average number of water and wastewater customers, as shown in columns (c) and (d) of Table 6-3. Finally, the mathematical average of the annual contracted amounts (\$36,966) is divided by the mathematical average number of customers (179), to reflect the \$206.51 annual cost per customer for each contracted service.

Staff developed Table 6-4 to present the WetCon study results⁹ with the average contract cost per service for Lakeside (\$206.51) inserted for comparative purposes. As shown below, the Utility claims its \$206.51 average cost per customer compares favorably with the FGUA figures captured in the WetCon study and also with the benchmarked groupings.

⁹ Staff notes that the data responses from the Utility provided summary data of certain findings from a 2011 report. Staff obtained and reviewed the entire report.

Table 6-4 Summary of WetCon study results showing Average Annual Cost per account of utilities in the South (\$/account) Compared to Lakeside Waterworks				
Utilities sampled	Customer Service Costs in Study (a)	O&M Costs Water & Wastewater in Study (b)	Total Costs as Reflected in Study (c) = (a) + (b)	Comparison of Average Cost
Lakeside Waterworks (Utility's calculation)	Not separately identified	N/A	N/A	\$206.51
FGUA West	\$38.51	\$225.00	\$263.51	\$263.51
FGUA South	\$50.58	\$213.00	\$263.58	\$263.58
Top Grouping (Lowest Cost of Benchmark)	\$36.43	\$246.00	\$282.43	\$282.43
Median Grouping (Median Cost of Benchmark)	\$41.16	\$301.00	\$342.16	\$342.16
Bottom Grouping (Highest Cost of Benchmark)	\$52.38	\$379.00	\$431.38	\$431.38

Analysis

Staff evaluated the Utility's data request responses and developed Tables 6-3 and 6-4 to facilitate a comparison of the Lakeside contract to the data in the WetCon study. Because the Utility was unable to attract any other bids for services at the time it entered into its contract with U.S. Water, staff does not have directly comparable bids for service or alternative contracts to review, and therefore, evaluated the results of the WetCon study for comparative purposes. As noted previously, the WetCon study benchmarked the pricing of services in FGUA systems against a sampling of other utilities. Staff notes, however, that comparing Lakeside to any of the FGUA systems in the WetCon study is difficult for the following reasons:

1. All of the FGUA systems have a much larger customer base than Lakeside (under 200 water customers for Lakeside versus over 12,000 for the largest of the FGUA systems identified).
2. A similar disparity exists for the respective wastewater customer bases.
3. The level of repair, renewal, and replacement of utility plant is much different for the FGUA (the U.S. Water contract with Lakeside Waterworks contains a \$400 threshold, and the FGUA threshold is \$7,500).

4. Staffing needs are much greater for the FGUA systems compared to the Lakeside systems.
5. The FGUA contracts with U.S. Water include the costs for chemicals, whereas chemicals are not included in Lakeside's contract with U.S. Water.
6. Reporting requirements and regulatory oversight. The FGUA is not an entity regulated by the FPSC.

Additionally, staff notes that the WetCon report reached a similar conclusion in stating:

It is virtually impossible to find any two water utilities that are comparable, given their unique treatment systems, customer bases, permit requirements, operational procedures, capital needs and rate structures. This is particularly true when comparing other systems to FGUA, with its' geographic spread, diverse customer base and broad range of treatment technologies.

In its April 30, 2014, data request response, the Utility emphasized that the results of the WetCon study show that Lakeside's average contract costs are below the costs for FGUA systems. Staff performed the same mathematical calculations illustrated in Table 6-3, and by operation of math, these steps yield an average cost per service of \$206.51, the exact figure the Utility calculated. Staff notes, however, three important considerations when evaluating the results using the averaging method:

- 1) The \$206.51 amount shown in Table 6-4 reflects an average cost per service (water and wastewater), not a total cost.
- 2) The number of water customers, while not the same, is not significantly different from the number of wastewater customers for this utility. These calculations are based on June 2013 billing data reflecting 183 water customers and 175 wastewater customers. Staff believes the averaging method effectively levels the allocation of costs between water and wastewater customers.
- 3) The monthly contractual charges for water-related and wastewater-related services are not equal for this utility. By mathematically averaging these contractual charges, staff believes the utility is presenting its cost information in a manner that is comparable with how the cost data is presented in the WetCon study.

Even though the averaging method levels the variables noted above, staff believes a cost comparison is needed since the Utility's customers are getting an array of services under this contract that were not provided by the Utility's prior owners. As noted previously, the Utility sought competitive bids for these services, and received none. Based on this limitation, staff does not have an "apples-to-apples" comparison available, but notes that the WetCon study

results provide comparative information to review. As shown in Table 6-4, staff observes that the average cost per customer of \$206.51 per service puts Lakeside well under the much-larger FGUA amounts shown in the WetCon study results, and lower than the benchmarked groupings. Noting the difficulty of making direct comparisons between water and wastewater utilities, staff believes the average cost per customer of \$206.51 per service for Lakeside compared to the findings in the WetCon study demonstrates reasonableness.

Affiliate Relationship

Because there is a nexus¹⁰ between the utility's owners and U.S. Water Services Corporation, staff considered how the Commission addressed affiliate transactions in other cases. In Order No. PSC-12-0102-FOF-WS,¹¹ the Commission evaluated relevant statutes and rules related to affiliate transactions. Section 367.081(2)(a)1, F.S., sets forth the Commission's responsibility in rate setting as follows:

The commission shall, either upon request or upon its own motion, fix rates which are just, reasonable, compensatory, and not unfairly discriminatory. In every such proceeding, the commission shall consider the value and quality of the service and the cost of providing the service, which shall include, but not be limited to, debt interest; the requirements of the utility for working capital; maintenance, depreciation, tax, and operating expenses incurred in the operation of all property used and useful in the public service; and a fair return on the investment of the utility in property used and useful in the public service

In Order No. PSC-12-0102-FOF-WS, at 99-100, the Commission interpreted Section 367.081(2)(a)1, F.S., and applicable case law as follows:

As reflected in the statute cited above [Section 367.081(2)(a)1., F.S.], we are required to set reasonable rates, but we must also set rates that are compensatory. The provisions in the statute require that we consider the cost of providing service, which includes operating expenses incurred in the operation of all property used and useful in the public service, as well as a fair return on the investment of the Utility in property used and useful in the public service. In conducting our analysis of the appropriate operating expenses to be included, we are mindful of two Florida Supreme as

¹⁰ In its SARC application, the Utility states that four shareholders own Lakeside Waterworks. In a March 27, 2014 response to a Data Request, the Utility states that three of the four Utility shareholders are Corporate Officers of U.S. Water Services Corporation.

¹¹ See pp. 99-100 of Order No. PSC-12-0102-FOF-WS, Order Approving in Part Requested Increase in Water and Wastewater Rates and Requiring Refunds With Interest, 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.

Court cases. In the case of Keystone Water Co v. Bevis, 278 So. 2d 606 (Fla. 1973), the Court held that a utility is entitled to a fair rate of return on property used or useful in public service. In Keystone, the Court further found that rates which do not yield a fair rate of return are unjust, unreasonable, and confiscatory and their enforcement deprives a utility of due process.¹² Additionally, in GTE v. Deason, 642 So. 2d 545 (Fla. 1994), the Florida Supreme Court laid out the standard of review for affiliate transactions, stating:

The mere fact that a utility is doing business with an affiliate does not mean that unfair or excess profits are being generated, without more. Charles F. Phillips, Jr., *The Regulation of Public Utilities* 254-55 (1988). We believe the standard must be whether the transactions exceed the going market rate or are otherwise inherently unfair If the answer is “no,” then the PSC may not reject the utility’s position.

GTE v. Deason, 645 So. 2d at 547-548.

Although a related party relationship exists between the Utility’s owners and U.S. Water Services Corporation, staff believes the holdings in Keystone v. Bevis and GTE v. Deason indicate that an affiliate relationship is not “unfair” on its face. As noted previously, no other service companies provided bids for the services included in the U.S. Water contract, and staff believes this is relevant. In a data request response dated May 30, 2014, the Utility states “there is zero amount (no portion) of the monthly contractual services charge that includes compensation for any owner of the utility.” Because the Utility’s customers will be getting an array of services that no other management services company was willing to provide, staff is recommending that the expense for the U.S Water contract is appropriate.

Staff acknowledges that the U.S Water contract is a significant operating expense. However, staff notes that the U.S Water contract is comprehensive in nature, and provides the Utility’s customers with services that prior owners/operators did not provide. Staff notes that providing such services is the primary reason that the water and wastewater expenses have increased.

Summary

Staff recommends Contractual Services – Other expenses of \$38,197 for water and \$35,730 for wastewater.

¹² See Keystone Water Co. v. Bevis, 278 So. 2d 606, 609 (Fla. 1973).

Rents (640/740) – Lakeside recorded rent expense of \$2,996 for water and \$0 for wastewater. Staff has made adjustments to remove \$428 from water, and to increase the wastewater balance by \$2,568. The land lease is \$5,136 annually, and is allocated equally between water and wastewater. Staff recommends rent expense of \$2,568 for water and \$2,568 for wastewater.

Insurance Expense (655/755) – Lakeside recorded insurance expense of \$576 for water and \$424 for wastewater. Staff has made adjustments to remove \$54 from water, and increased this account by \$97 for wastewater. Staff notes that the insurance expense is allocated equally between water and wastewater, and recommends insurance expense of \$522 for water and \$521 for wastewater.

Regulatory Commission Expense (665/765) - Lakeside recorded \$0 for regulatory commission expense in these accounts. Regarding the current rate case, pursuant to Rule 25-22.0407, F.A.C., the Utility is required to mail notices of the customer meeting and notices of final rates to its customers. For these notices, staff has estimated \$91 for postage expense, \$93 for printing expense, and \$9 for envelopes, for a total cost of \$193. For the notification of a rate change, staff has estimated \$91 for postage expense, \$37 for printing expense, and \$9 for envelopes, for a total of \$137. The Utility paid a \$1,000 rate case filing fee for the water utility, and a \$1,000 rate case filing fee for the wastewater utility. The total rate case expense including postage, notices, envelopes, and filing fee is \$2,330. Pursuant to Section 367.0816, F.S., rate case expense is amortized over a four-year period, which is \$583 per year ($\$2,330/4$). Staff's net adjustment to this account is an increase of \$292 for water, and \$292 for wastewater. Staff recommends regulatory commission expense of \$292 for water and \$292 for wastewater.

Bad Debt Expense (670/770) – Lakeside recorded bad debt expense of \$865 for water and \$638 for wastewater. In addition, the Utility requested that its bad debt expense be 2 percent of revenue. Staff believes bad debt expense of 2 percent of revenues is reasonable, and has increased these accounts by \$423 for water and \$602 for wastewater. Staff recommends bad debt expense of \$1,288 for water and \$1,240 for wastewater.

Miscellaneous Expense (675/775) – Lakeside recorded \$1,480 for water and \$2,273 for wastewater for miscellaneous expense. Staff has made adjustments to remove \$433 for water and \$2,088 for wastewater due to a lack of documentation. Staff recommends miscellaneous expense of \$1,047 for water and \$185 for wastewater.

Sludge Removal Expense (711) – The Utility recorded \$0 for wastewater sludge removal. Based on invoices, staff made an adjustment to increase this account by \$2,500. Staff recommends a sludge removal expense of \$2,500 for wastewater.

Transportation Expense (750) – Lakeside recorded \$19 for transportation expense. Staff has made an adjustment to remove this amount due to a lack of documentation. Staff recommends a transportation expense of \$0 for wastewater.

Operation and Maintenance Expenses (O&M) Summary – Total adjustments to O&M expense result in increases of \$12,674 for water and \$20,012 for wastewater. Staff's recommended O&M expense is \$53,113 for water and \$54,402 for wastewater. O&M expenses are shown on Schedule Nos. 3-A and 3-B for water and wastewater, respectively.

Depreciation Expense (Net of Related Amortization of CIAC) – The Utility recorded depreciation expense of \$1,932 for water and \$6,068 for wastewater during the test year. Staff has calculated depreciation expense using the prescribed rates set forth in Rule 25-30.140, F.A.C., and recommends adjustments to increase the water balance by \$2,956 and decrease the wastewater balance by \$3,817. Staff recommends depreciation expense balances of \$4,888 for water, and \$2,252 for wastewater. The Utility recorded no Amortization of CIAC for water and wastewater during the test year. Staff has made adjustments to increase this account by \$490 for water and \$278 for wastewater. Therefore, staff recommends net depreciation expense of \$4,398 for water and \$1,974 for wastewater.

Taxes Other Than Income (TOTI) – The Utility recorded \$1,987 for water and \$1,706 for wastewater for TOTI. Staff has reduced these amounts by a net of \$43 for water and \$61 for wastewater to reflect the appropriate Regulatory Assessment Fees, less payroll taxes. Additionally, adjustments increase TOTI by \$1,269 for water and \$1,500 for wastewater due to staff's recommended increase. Therefore, staff recommends TOTI balances for the test year of \$3,213 for water and \$3,146 for wastewater.

Income Tax – The Utility is a limited liability company and did not record income tax for the test year. As a limited liability company, the Utility pays no income tax. Therefore, staff has not made any adjustments to this account.

Operating Expenses Summary – The application of staff's recommended adjustments to Lakeside's recorded test year operating expenses results in staff's recommended operating expenses of \$61,705 for water and \$60,077 for wastewater. Operating expenses are shown on Schedule No. 3-A for water and Schedule 3-B for wastewater. The related adjustments for water and wastewater are shown on Schedule No. 3-C.

Issue 7: Should the Commission utilize the operating ratio methodology as an alternative means to calculate the revenue requirement for Lakeside and, if so, what is the appropriate margin?

Preliminary Recommendation: Yes, the Commission, on its own motion, should utilize the operating ratio methodology for calculating the revenue requirement for Lakeside. The margin should be 10.00 percent of O&M expense for water and wastewater. (Barrett)

Staff Analysis: Section 367.0814(9), F.S., provides that the Commission may, by rule, establish standards and procedures for setting rates and charges of small utilities using criteria other than those set forth in Sections 367.081(1), (2)(a), and (3), F.S. Rule 25-30.456, F.A.C., provides an alternative to a staff-assisted rate case as described in Rule 25-30.455, F.A.C. As an alternative, utilities with total gross annual operating revenue of less than \$250,000¹³ per system may petition the Commission for staff assistance in alternative rate setting.

Although Lakeside did not petition the Commission for alternative rate setting under the aforementioned rule, staff believes that the Commission should exercise its discretion to employ the operating ratio methodology to set rates in this case. The operating ratio methodology is an alternative to the traditional calculation of revenue requirements. Under this methodology, instead of applying a return on the Utility's rate base, the revenue requirement is based on the margin of Lakeside's O&M expenses. This methodology has been applied in cases in which the traditional calculation of revenue requirements would not provide sufficient revenue to protect against potential variances in revenues and expenses.

By Order No. PSC-96-0357-FOF-WU,¹⁴ issued March 13, 1996, the Commission, for the first time, utilized the operating ratio methodology as an alternative means for setting rates. This order also established criteria to determine the use of the operating ratio methodology and a guideline margin of 10.00 percent of O&M expense. This criteria was applied again in Order No. PSC-97-0130-FOF-SU,¹⁵ issued February 10, 1997. Most recently, the Commission approved the operating ratio methodology for setting rates in Order No. PSC-13-0327-PAA-SU,¹⁶ issued July 16, 2013.

By Order No. PSC-96-0357-FOF-WU, the Commission established criteria to determine whether to utilize the operating ratio methodology for those utilities with low or non-existent rate base. The qualifying criteria established by Order No. PSC-96-0357-FOF-WU, and how they apply to the Utility are discussed below:

- 1) Whether the Utility's O&M expense exceeds rate base. The operating ratio method substitutes O&M expense for rate base in calculating the amount of return. A Utility generally would not benefit from the operating ratio method if rate base exceeds O&M expense. The decision to use the operating ratio method depends on the determination of whether the primary risk resides in capital costs or operating expenses. In the instant

¹³ Effective August 10, 2014, the gross annual revenue level to qualify for alternative rate setting is \$275,000.

¹⁴ Docket No. 950641-WU, In re: Application for staff-assisted rate case in Palm Beach County by Lake Osborne Utilities Company, Inc.

¹⁵ Docket No. 960561-SU, In re: Application for staff-assisted rate case in Citrus County by Indian Springs Utilities, Inc.

¹⁶ Docket No. 120270-SU, In re: Application for staff-assisted rate case in Polk County by West Lakeland Wastewater, LLC.

case, the rate base is less than the level of O&M expense. Staff believes the Utility's primary risk resides with covering its operating expenses. Based on staff's recommendation, the rate base for the test year is \$22,080 for water and \$8,127 for wastewater, while adjusted O&M expenses are \$53,113 for water and \$54,402 for wastewater.

2) Whether the Utility is expected to become a Class B utility in the foreseeable future. Pursuant to Section 367.0814(9), F.S., the alternative form of regulation being considered in this case only applies to Class C utilities, small utilities with gross annual revenue of \$250,000 or less. Lakeside is a Class C utility and the recommended revenue requirements of \$67,016 for water and \$65,517 for wastewater are substantially below the threshold level for Class B status (\$200,000 per system). The Utility's service area has not had any significant growth in the last five years. Therefore, staff believes the Utility will not become a Class B utility in the foreseeable future.

3) Quality of service and condition of plant. While staff will not make a final determination on quality of service until after the September 11, 2014 customer meeting, staff's initial review of Commission and DEP records did not reveal any quality of service issues.

4) Whether the Utility is developer-owned. The current owner of this Utility is not a developer.

5) Whether the Utility operates treatment facilities or is simply a distribution and/or collection system. The consideration at issue is whether the Utility purchases water and/or wastewater services and whether such costs should be excluded in the computation of the operating margin. Staff notes that the Utility does not purchase water and also operates its wastewater treatment plant and collection system.

Based on staff's review of the Utility's situation relative to the above criteria, staff recommends that Lakeside is a viable candidate for the operating ratio methodology.

By Order Nos. PSC-96-0357-FOF-WS and PSC-97-0130-FOF-WU, the Commission determined that a margin of 10 percent shall be used unless unique circumstances justify the use of a greater or lesser margin. The important question is not what the return percentage should be, but what level of operating margin will allow the utility to provide safe and reliable service and remain a viable entity. The answer to this question requires a great deal of judgment based upon the particular circumstances of the utility.

Several factors must be considered in determining the reasonableness of a margin. First, the margin must provide sufficient revenue for the Utility to cover its interest expense. However, in this case, the Utility is not paying interest expense.

Second, use of the operating ratio methodology rests on the contention that the principal risk to the utility resides in operating cost rather than in capital cost of the plant. The fair return on a small rate base may not adequately compensate the utility owner for incurring the risk associated with covering the much larger operating cost. Under the rate base method, the return on rate base would be \$1,930 for water and \$710 for wastewater, compared to \$5,311 for water

and \$5,440 for wastewater, using the operating ratio method. Staff believes the margins under the rate base method do not provide a sufficient financial cushion, and do not adequately compensate the utility owner for that risk.

Third, if the return on rate base method was applied, Lakeside could be left with insufficient funds to cover operating expenses. Therefore, the margin should provide adequate revenue to protect against potential variability in revenue and expenses. If the Utility's operating expenses increase and revenue decreases, the Utility would not have the funds required for day-to-day operations.

In conclusion, staff believes the above factors show that the Utility needs a higher margin of revenue over operating expenses than the traditional return on rate base method would allow. Therefore, in order to provide Lakeside with adequate cash flow to meet environmental requirements and to provide some assurance of safe and reliable service, staff recommends application of the operating ratio methodology at a margin of 10.00 percent of O&M expense for determining the water and wastewater revenue requirements.

Issue 8 What is the appropriate revenue requirement?

Preliminary Recommendation: The appropriate revenue requirement is \$67,016 for water and \$65,517 for wastewater, resulting in an annual increase of \$28,210 for water (72.69 percent), and an annual increase of \$33,341 for wastewater (103.62 percent). (Barrett)

Staff Analysis: Lakeside should be allowed an annual increase of \$28,210 for water (72.69 percent), and \$33,341 for wastewater (103.62 percent). This will allow the Utility the opportunity to recover its expenses and earn a 10.00 percent margin over its O&M expenses. The calculations are shown in Table 8-1 and Table 8-2 for water and wastewater, respectively:

Table 8-1 Water Revenue Requirement	
Adjusted O&M	\$53,113
Operating Ratio	10.00%
Operating Margin	\$5,311
Adjusted O&M expense	53,113
Depreciation expense	4,888
Amortization	490
Taxes Other Than Income	3,213
Income Taxes	0
Revenue Requirement	\$67,016
Less Test Year Revenues	38,806
Annual Increase	\$28,210
Percent Increase/(Decrease)	72.69%

Table 8-2 Wastewater Revenue Requirement	
Adjusted O&M	\$54,402
Operating Ratio	10.00%
Operating Margin	\$5,440
Adjusted O&M expense	54,402
Depreciation expense	2,252
Amortization	278
Taxes Other Than Income	3,146
Income Taxes	0
Revenue Requirement	\$65,517
Less Test Year Revenues	32,176
Annual Increase	\$33,341
Percent Increase/(Decrease)	103.62%

Issue 9: What are the appropriate rate structures and rates for Lakeside's water and wastewater systems?

Preliminary Recommendation: The preliminary recommended rate structures and monthly water and wastewater rates are shown on Schedule Nos. 4-A and 4-B, respectively. 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 services rendered on or after the stamped approval date on the tariff sheets, pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved rates should not be implemented until staff has approved the proposed customer notice and the notice has been received by the customers. The Utility should provide proof of the date notice was given within 10 days of the date of the notice. (Roberts)

Staff Analysis:

Water Rates

Lakeside is located in Lake County within the SJRWMD. The Utility provides service to approximately 183 residential water customers. Approximately 22 percent of the residential bills during the test year had zero gallons indicating a somewhat seasonal customer base. The average residential water demand is 3,450 gallons per month. The average residential water demand, excluding zero gallon bills, is 4,438 gallons per month. Currently, Lakeside's water system rate structure consists of a base facility charge (BFC) and gallonage charge for both residential and general service customers, and only a gallonage charge for irrigation customers.

Staff performed an analysis of the Utility's billing data in order to evaluate various BFC cost recovery percentages, usage blocks, and usage block rate factors for the residential rate class. The goal of the evaluation was to select the rate design parameters that: (1) produce the recommended revenue requirement; (2) equitably distribute cost recovery among the Utility's customers; (3) establish the appropriate non-discretionary usage threshold for restricting repression; and (4) implement, where appropriate, water conserving rate structures consistent with Commission practice.

Due to the customers' low average monthly consumption and the seasonal nature of the customers, staff recommends that 54 percent of the water revenues should be generated from the BFC in order to ensure that the Utility will have sufficient cash flow to cover fixed costs. The average people per household served by the water system is 2.18; therefore, based on the number of persons per household, 50 gallons per day per person, and the number of days per month the non-discretionary usage threshold should be 4,000 gallons per month. Staff recommends a traditional BFC and gallonage charge rate structure with an additional gallonage charge for non-discretionary usage for residential water customers. Irrigation customers should continue being billed only the approved gallonage charge. The Commission previously found that the separate irrigation meter would not place any additional demand on the Utility's water system and irrigation customers should only be assessed the gallonage charge for the water usage registered

by the separate irrigation meter.¹⁷ Staff believes that this is still appropriate. General service customers should be billed a BFC and uniform gallonage charge.

Based on billing data provided by the Utility and an assumption of 4,000 gallons per month of non-discretionary usage, approximately 43 percent of total residential consumption is discretionary and, therefore, subject to the effects of repression. A repression adjustment quantifies changes in consumption patterns in response to an increase in price. Customers will typically reduce their discretionary consumption in response to price changes, while non-discretionary consumption remains relatively unresponsive to price changes. Based on a recommended revenue increase of approximately 73 percent, the residential discretionary consumption can be expected to decline by 1,813,000 gallons resulting in anticipated average residential demand of 3,356 gallons per month, excluding zero gallon bills. Staff recommends a 24.4 percent reduction in total residential consumption and corresponding reductions of \$585 for purchased power, \$104 for chemicals, and \$32 for RAFs to reflect the anticipated repression, which results in a post repression revenue requirement of \$66,264.

Based on the foregoing, staff recommends that 54 percent of the water revenues should be generated from the BFC. Staff also recommends a traditional BFC and gallonage charge rate structure with an additional gallonage charge for non-discretionary usage threshold of 4,000 gallons should be approved for residential customers. Irrigation customers should be billed only the approved gallonage charge. A 24.4 percent reduction in total residential consumption and corresponding reductions of \$585 for purchased power, \$104 for chemicals, and \$32 for RAFs should be made to reflect the anticipated repression. General service customers should continue to be billed a BFC and gallonage charge. Staff's recommended rate structure and resulting water rates are shown on Schedule No. 4-A.

Wastewater Rates

The Utility provides wastewater service to approximately 175 residential customers. Approximately 23 percent of the residential wastewater bills during the test year had zero gallons. The average water demand for wastewater customers is 3,243 gallons per month. Currently, the residential rate structure for the wastewater system consists of a uniform BFC for all meter sizes and a gallonage charge with a 6,000 gallon cap. General service customers are billed a BFC by meter size and a gallonage charge that is 1.2 times higher than the residential gallonage charge.

Staff performed an analysis of the Utility's billing data to evaluate various BFC cost recovery percentages and gallonage caps for the residential customers. The goal of the evaluation was to select the rate design parameters that: (1) produce the recommended revenue requirement; (2) equitably distribute cost recovery among the Utility's customers; and (3) implement a gallonage cap that considers the amount of water that may return to the wastewater system.

¹⁷ See Order No. PSC-00-0259-PAA-WS, issued February 8, 2000, in Docket No. 990080-WS, In re: Complaint and request for hearing by Linda J. McKenna and 54 petitioners regarding unfair rates and charges of Shangri-La by the Lake Utilities, Inc. in Lake County.

Typically, Commission practice is to set the BFC allocation to at least 50 percent due to the capital intensive nature of wastewater plants. Based on the seasonality of Lakeside's wastewater customers and the significant increase in the revenue requirement, staff recommends that 50 percent of the revenue requirement be generated from the BFC in order to mitigate the rate increase. In addition, based on the expected reduction in water demand described above, staff recommends that a repression adjustment also be made for wastewater. Because wastewater rates are calculated based on customers' water demand, if those customers' water demand is expected to decline, then the billing determinants used to calculate wastewater rates should also be adjusted. Therefore, staff recommends that a repression adjustment for the discretionary water usage also be made to calculate wastewater rates. Based on the billing analysis for the wastewater system, staff recommends that discretionary usage be reduced by 328,230 gallons to reflect the anticipated reduction in water demand used to calculate wastewater rates. Staff recommends a 7.21 percent reduction in total residential consumption and corresponding reductions of \$403 for purchased power, \$38 for chemicals, \$180 for sludge removal, and \$28 for RAFs to reflect the anticipated repression, which results in a post repression revenue requirement of \$64,868. Further, staff recommends no change to the Utility's existing residential cap of 6,000 gallons because a reduction to the cap would result in fewer gallons to spread the revenue requirement across and an additional increase in the wastewater gallonage charge. General service customers should continue to be billed a BFC by meter size and a gallonage charge that is 1.2 times higher than the residential gallonage charge.

Based on the foregoing, staff recommends that 50 percent of the wastewater revenues be generated from the BFC. The residential wastewater customers' rate structure should consist of a BFC for all meter sizes, with a cap of 6,000 gallons. A 7.21 percent reduction in residential consumption and corresponding reductions of \$403 for purchased power, \$38 for chemicals, \$180 for sludge removal, and \$28 for RAFs should be made to reflect the anticipated repression. General service wastewater customers should be billed a BFC and gallonage charge that is 1.2 times higher than the residential gallonage charge. Staff's recommended rate structure and the resulting wastewater rates are shown on Schedule No. 4-B.

The preliminary recommended rate structures and monthly water and wastewater rates are shown on Schedule Nos. 4-A and 4-B, respectively. 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 on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved rates should not be implemented until staff has approved the proposed customer notice and the notice has been received by the customers. The Utility should provide proof of the date notice was given within 10 days of the date of the notice

Issue 10: What is the appropriate amount by which rates should be reduced in four years after the published effective date to reflect the removal of the amortized rate case expense as required by Section 367.0816, F.S.?

Preliminary Recommendation: The water and wastewater rates should be reduced as shown on Schedule Nos. 4-A and 4-B, respectively, to remove rate case expense grossed-up for regulatory assessment fees and amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the four-year rate case expense recovery period, pursuant to Section 367.0816, F.S. Lakeside 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. 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 the reduction in the rates due to the amortized rate case expense. (Barrett)

Staff Analysis: Section 367.0816, F.S., requires that the rates be reduced immediately following the expiration of the four-year period by the amount of the rate case expense previously included in rates. The reduction will reflect the removal of revenue associated with the amortization of rate case expense, the associated return in working capital, and the gross-up for RAFs. The total reduction is \$590 (\$295 for water and \$295 for wastewater). Using Lakeside's current revenue, expenses, capital structure and customer base, the reduction in revenue will result in the rate decreases as shown on Schedule Nos. 4-A and 4-B.

The Utility should be required to file revised tariff sheets no later than one month prior to the actual date of the required rate reduction. Lakeside should also be required to file a proposed customer notice setting forth the lower rates and the reason for the reduction. If the Utility files this reduction in conjunction with a price index or pass-through rate adjustment, separate data should be filed for the price index and/or pass-through increase or decrease and the reduction in the rates due to the amortized rate case expense.

Issue 11: What are the appropriate initial customer deposits for Lakeside?

Preliminary Recommendation: The appropriate initial customer deposits should be \$60 and \$80 for the residential 5/8 inch by 3/4 inch meter size for water and wastewater, respectively. The initial customer deposits for all other residential meter sizes and all general service meter sizes should be two times the average estimated bill for water and wastewater. The approved customer deposits should be effective for services rendered or connections made on or after the stamped approval date on the tariff sheets, pursuant to Rule 25-30.475, F.A.C. The Utility should be required to charge the approved charges until authorized to change them by the Commission in a subsequent proceeding. (Roberts)

Staff Analysis: Rule 25-30.311, F.A.C., contains the criteria for collecting, administering, and refunding customer deposits. Customer deposits are designed to minimize the exposure of bad debt expense for the Utility and, ultimately, the general body of ratepayers. Historically, the Commission has set initial customer deposits equal to two times the average estimated bill.¹⁸ Currently, the Utility's existing initial deposits are \$45 for water and \$55 for wastewater. Based on staff's recommended rates, the existing initial customer deposits are not sufficient to cover two months' bills for water and wastewater, respectively. Staff recommends the existing initial customer deposit be increased to reflect two times the average estimated bill for both water and wastewater to ensure that the cost of providing service is recovered from those that incurred cost.

Staff recommends the appropriate initial customer deposits should be \$60 and \$80 for the residential 5/8 inch by 3/4 inch meter size for water and wastewater, respectively. The initial customer deposits for all other residential meter sizes and all general service meter sizes should be two times the average estimated bill for water and wastewater. The approved customer deposits should be effective for services rendered or connections made on or after the stamped approval date on the tariff sheets, pursuant to Rule 25-30.475, F.A.C. The Utility should be required to charge the approved charges until authorized to change them by the Commission in a subsequent proceeding.

¹⁸ See Order No. PSC-03-1342-PAA-WS, issued November 24, 2003, in Docket No. 021228-WS, In re: Application for staff-assisted rate case in Brevard County by Service Management Systems, Inc.; and PSC-03-0845-PAA-WS, issued July 21, 2003, in Docket No. 021192-WS, In re: Application for staff-assisted rate case in Highlands County by Damon Utilities, Inc.

Issue 12: Should Lakeside's request to implement a \$5.25 late payment charge be approved?

Preliminary Recommendation: Yes. Lakeside's request to implement a \$5.25 late payment charge should be approved. Lakeside should be required to file a proposed customer notice to reflect the Commission-approved charge. The approved charge should be effective for services rendered on or after the stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved charge should not be implemented until staff has approved the proposed customer notice. The Utility should provide proof of the date notice was given no less than ten days after the date of the notice. (Roberts)

Staff Analysis: Section 367.091, F.S., authorizes the Commission to establish, increase, or change a rate or charge other than monthly rates or services availability charges. The Utility is requesting a \$5.25 late payment charge to recover the cost of supplies and labor associated with processing late payment notices. The Utility's request for a late payment charge was accompanied by its reason for requesting the charge, as well as the cost justification required by Section 367.091, F.S.

Based on staff's research, since the late 1990s, the Commission has approved late payment charges ranging from \$2.00 to \$7.00.¹⁹ The purpose of this charge is not only to provide an incentive for customers to make timely payment, thereby reducing the number of delinquent accounts, but also to place the cost burden of processing delinquent accounts solely upon those who are cost causers.

Based on the above, staff recommends that Lakeside's request to implement a \$5.25 late payment charge should be approved. Lakeside should be required to file a proposed customer notice to reflect the Commission-approved charge. The approved charge should be effective for services rendered on or after the stamped approval date on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. In addition, the approved charge should not be implemented until staff has approved the proposed customer notice. The Utility should provide proof of the date notice was given no less than ten days after the date of the notice.

¹⁹ See Order Nos. PSC-01-2101-TRF-WS, in Docket No. 011122-WS, issued October 22, 2001, In re: Tariff filing to establish a late payment charge in Highlands County by Damon Utilities, Inc.; PSC-08-0255-PAA-WS, in Docket No. 070391-WS, issued April 24, 2008, In re: Application for certificates to provide water and wastewater service in Sumter County by Orange Blossom Utilities, Inc.; PSC-09-0752-PAA-WU, in Docket No. 090185-WU, issued November 16, 2009, In re: Application for grandfather certificate to operate water utility in St. Johns County by Camachee Island Company, Inc. d/b/a Camachee Cove Yacht Harbor Utility.; PSC-10-0257-TRF-WU, in Docket No. 090429-WU, issued April 26, 2010, In re: Request for approval of imposition of miscellaneous service charges, delinquent payment charge and meter tampering charge in Lake County, by Pine Harbour Water Utilities, LLC.; and PSC-11-0204-TRF-SU, in Docket No. 100413-SU, issued April 25, 2011, In re: Request for approval of tariff amendment to include a late fee of \$14.00 in Polk County by West Lakeland Wastewater.

Issue 13: Should the recommended rates be approved for the Utility on a temporary basis, subject to refund with interest, in the event of a protest filed by a party other than the Utility?

Preliminary Recommendation: Yes. Pursuant to Section 367.0814(7), F.S., the recommended rates should be approved for the Utility on a temporary basis, subject to refund with interest, in the event of a protest filed by a party other than the Utility. Lakeside 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 on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. In addition, the temporary rates should not be implemented until staff has approved the proposed notice, and the notice has been received by the customers. Prior to implementation of any temporary rates, the Utility should provide appropriate security. If the recommended rates are approved on a temporary basis, the rates collected by the Utility should be subject to the refund provisions discussed below in the staff analysis. In addition, after the increased rates are in effect, pursuant to Rule 25-30.360(6), F.A.C., the Utility should file reports with the Commission's Office of Commission Clerk no later than the 20th of each month indicating the monthly and total amount of money subject to refund at the end of the preceding month. The report filed should also indicate the status of the security being used to guarantee repayment of any potential refund. (Barrett)

Staff Analysis: This recommendation proposes an increase in water and wastewater rates. A timely protest might delay what may be a justified rate increase resulting in an unrecoverable loss of revenue to the Utility. Therefore, pursuant to Section 367.0814(7), F.S., in the event of a protest filed by a party other than the Utility, staff recommends that the recommended rates be approved as temporary rates. Lakeside 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 on the tariff sheet, pursuant to Rule 25-30.475(1), F.A.C. In addition, the temporary rates should not be implemented until staff has approved the proposed notice, and the notice has been received by the customers. The recommended rates collected by the Utility should be subject to the refund provisions discussed below.

Lakeside should be authorized to collect the temporary rates upon staff's approval of an appropriate security for the potential refund and the proposed customer notice. Security should be in the form of a bond or letter of credit in the amount of \$41,050, based upon the non-financial commercial paper rate for July 2014. Alternatively, the Utility could establish an escrow agreement with an independent financial institution.

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

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

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

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

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

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

In no instance should the maintenance and administrative costs associated with the refund be borne by the customers. These costs are the responsibility of, and should be borne by, the Utility. Irrespective of the form of security chosen by Lakeside, an account of all monies received as a result of the rate increase should be maintained by the Utility. If a refund is ultimately required, it should be paid with interest calculated pursuant to Rule 25-30.360(4), F.A.C.

Lakeside should maintain a record of the amount of the bond, and the amount of revenues that are subject to refund. In addition, after the increased rates are in effect, pursuant to Rule 25-30.360(6), F.A.C., the Utility should file reports with the Commission's Office of Commission Clerk no later than the 20th of each month indicating the monthly and total amount of money subject to refund at the end of the preceding month. The report filed should also indicate the status of the security being used to guarantee repayment of any potential refund

Issue 14: 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 applicable National Association of Regulatory Commissioners Uniform System of Accounts (NARUC USOA) primary accounts associated with the Commission approved adjustments?

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

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

Issue 15: Should this docket be closed?

Preliminary 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 should 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 adjustments for all applicable NARUC USOA primary accounts have been made. Once these actions are complete, this docket should be closed administratively. (Murphy)

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 should 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 adjustments for all applicable NARUC USOA primary accounts have been made. Once these actions are complete, this docket should be closed administratively.

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 1-A	
TEST YEAR ENDED 6/30/2013		DOCKET NO. 130194-WS	
SCHEDULE OF WATER RATE BASE			
DESCRIPTION	BALANCE PER UTILITY	STAFF ADJUSTMENTS TO UTIL. BAL.	BALANCE PER STAFF
UTILITY PLANT IN SERVICE	\$138,299	(\$2,131)	\$136,168
LAND & LAND RIGHTS	0	0	0
NON-USED AND USEFUL COMPONENTS	0	(13,073)	(13,073)
CIAC	(13,776)	0	(13,776)
ACCUMULATED DEPRECIATION	(106,153)	6,445	(99,708)
AMORTIZATION OF CIAC	5,830	0	5,830
WORKING CAPITAL ALLOWANCE	<u>0</u>	<u>6,639</u>	<u>6,639</u>
WATER RATE BASE	<u>\$24,200</u>	<u>(\$2,120)</u>	<u>\$22,080</u>

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 1-B	
TEST YEAR ENDED 6/30/2013		DOCKET NO. 130194-WS	
SCHEDULE OF WASTEWATER RATE BASE			
DESCRIPTION	BALANCE PER UTILITY	STAFF ADJUST. TO UTIL. BAL.	BALANCE PER STAFF
1. UTILITY PLANT IN SERVICE	\$147,414	(\$1,598)	\$145,817
2. LAND & LAND RIGHTS	0	0	0
3. NON-USED AND USEFUL COMPONENTS	0	(44,928)	(44,928)
4. CIAC	(18,257)	0	(18,257)
5. ACCUMULATED DEPRECIATION	(95,725)	8,322	(87,404)
6. AMORTIZATION OF CIAC	11,929	(5,830)	6,099
7. WORKING CAPITAL ALLOWANCE	<u>0</u>	<u>6,800</u>	<u>6,800</u>
8. WASTEWATER RATE BASE	<u>\$45,361</u>	<u>(\$37,234)</u>	<u>\$8,127</u>

LAKESIDE WATERWORKS, INC.	SCHEDULE NO. 1-C	
TEST YEAR ENDED 6/30/2013	DOCKET NO. 130194-WS	
ADJUSTMENTS TO RATE BASE	<u>WATER</u>	<u>WASTEWATER</u>
<u>UTILITY PLANT IN SERVICE</u>		
1. To reflect plant balance (301) per Order No. PSC-13-0425-PAA-WS	(\$3,160)	\$0
2. To reflect plant balance (310) per Order No. PSC-13-0425-PAA-WS	(603)	0
3. To reflect plant balance (351) per Order No. PSC-13-0425-PAA-WS	0	(1,125)
4. To reflect plant balance (371) per Order No. PSC-13-0425-PAA-WS	0	(1,057)
5. To reflect plant balance (393) per Order No. PSC-13-0425-PAA-WS	0	(245)
6. To reflect an averaging adjustment	0	(93)
7. To reflect pro forma plant repairs	<u>1,632</u>	<u>923</u>
Total	<u>(\$2,131)</u>	<u>(\$1,598)</u>
<u>LAND</u>		
Not applicable	<u>\$0</u>	<u>\$0</u>
<u>NON-USED AND USEFUL PLANT</u>		
To reflect non used and useful plant	(\$28,455)	(\$78,864)
To reflect non used and useful accumulated depreciation	22,656	33,936
To reflect non used and useful CIAC	0	0
To reflect non used and useful accumulated amortization	<u>(\$7,274)</u>	<u>0</u>
Total	<u>(\$13,073)</u>	<u>(\$44,928)</u>
<u>CIAC</u>		
Not applicable	<u>\$0</u>	<u>\$0</u>
<u>ACCUMULATED DEPRECIATION</u>		
1. To reflect the appropriate test year accumulated depreciation (AF2)	(\$464)	\$5,534
2. To reflect an averaging adjustment	2,396	266
3. To reflect pro forma plant repairs	<u>4,513</u>	<u>2,522</u>
Total	<u>\$6,445</u>	<u>\$8,322</u>
<u>AMORTIZATION OF CIAC</u>		
1. To reflect the appropriate Amortization of CIAC (AF3)	\$245	(\$5,691)
2. To reflect an averaging adjustment	<u>(245)</u>	<u>(139)</u>
Total	<u>\$0</u>	<u>(\$5,830)</u>
<u>WORKING CAPITAL ALLOWANCE</u>		
To reflect 1/8 of test year O&M expenses.	<u>\$6,639</u>	<u>\$6,800</u>

LAKESIDE WATERWORDS, INC.	SCHEDULE NO. 2
TEST YEAR ENDED 6/30/2013	DOCKET NO. 130194-WS
SCHEDULE OF CAPITAL STRUCTURE	

CAPITAL COMPONENT	PER UTILITY	SPECIFIC ADJUSTMENTS	BALANCE BEFORE PRO RATA ADJUSTMENTS	PRO RATA ADJUSTMENTS	BALANCE PER STAFF	PERCENT OF TOTAL	COST	WEIGHTED COST
1. COMMON STOCK	\$181,898	\$0	\$181,898					
2. RETAINED EARNINGS	0	0	0					
3. PAID IN CAPITAL	0	0	0					
4. TREASURY STOCK	<u>0</u>	<u>0</u>	<u>0</u>					
5. TOTAL COMMON EQUITY	\$181,898	\$0	\$181,898	(\$103,489)	\$78,409	100.00%	8.74%	8.74%
6. LONG TERM DEBT	\$0	\$0	\$0	\$0	\$0	0.00%	7.00%	0.00%
7. LONG TERM DEBT	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0.00%</u>	6.00%	0.00%
TOTAL LONG TERM DEBT	\$0	\$0	\$0	\$0	\$0	0.00%		
8. CUSTOMER DEPOSITS	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0.00%</u>	2.00%	<u>0.00%</u>
9. TOTAL	<u>\$181,898</u>	<u>\$0</u>	<u>\$181,898</u>	<u>(\$103,489)</u>	<u>\$78,409</u>	<u>100.00%</u>		<u>8.74%</u>
RANGE OF REASONABLENESS						<u>LOW</u>	<u>HIGH</u>	
RETURN ON EQUITY						<u>7.74%</u>	<u>9.74%</u>	
OVERALL RATE OF RETURN						<u>7.74%</u>	<u>9.74%</u>	

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 3-A				
TEST YEAR ENDED 6/30/2013		DOCKET NO. 130194-WS				
SCHEDULE OF WATER OPERATING INCOME						
	TEST YEAR PER UTILITY	STAFF ADJUSTMENTS	STAFF ADJUSTED TEST YEAR	ADJUST. FOR INCREASE		REVENUE REQUIREMENT
1. OPERATING REVENUES	<u>\$38,080</u>	<u>\$726</u>	<u>\$38,806</u>	<u>\$28,210</u> 72.69%		<u>\$67,017</u>
OPERATING EXPENSES:						
2. OPERATION & MAINTENANCE	\$40,439	\$12,674	\$53,113	\$0		\$53,113
3. DEPRECIATION (NET)	1,932	2,956	4,888	0		4,888
4. AMORTIZATION	0	490	490	0		490
5. TAXES OTHER THAN INCOME	1,987	(43)	1,944	1,269		3,213
6. INCOME TAXES	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>		<u>0</u>
7. TOTAL OPERATING EXPENSES	<u>\$44,358</u>	<u>\$16,078</u>	<u>\$60,436</u>	<u>\$1,269</u>		<u>\$61,705</u>
8. OPERATING INCOME/(LOSS)	<u>(\$6,278)</u>		<u>(\$21,630)</u>			<u>\$5,311</u>
9. WATER RATE BASE	<u>\$24,200</u>		<u>\$22,080</u>			<u>\$22,080</u>
10. OPERATING RATIO						<u>10.00%</u>

LAKESIDE WATERWORKS, INC.					SCHEDULE NO. 3-B	
TEST YEAR ENDED 6/30/2013					DOCKET NO. 130194-WS	
SCHEDULE OF WASTEWATER OPERATING INCOME						
	TEST YEAR PER UTILITY	STAFF ADJUSTMENTS	STAFF ADJUSTED TEST YEAR	ADJUST. FOR INCREASE	REVENUE REQUIREMENT	
1. OPERATING REVENUES	<u>\$31,949</u>	<u>\$227</u>	<u>\$32,176</u>	<u>\$33,341</u> 103.62%	<u>\$65,517</u>	
OPERATING EXPENSES:						
2. OPERATION & MAINTENANCE	\$34,390	\$20,012	\$54,402	\$0	\$54,402	
3. DEPRECIATION (NET)	6,068	(3,817)	2,252	0	2,252	
4. AMORTIZATION	0	278	278	0	278	
5. TAXES OTHER THAN INCOME	1,706	(61)	1,645	1,500	3,146	
6. INCOME TAXES	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	
7. TOTAL OPERATING EXPENSES	<u>\$42,164</u>	<u>\$16,413</u>	<u>\$58,577</u>	<u>\$1,500</u>	<u>\$60,077</u>	
8. OPERATING INCOME/(LOSS)	<u>(\$10,215)</u>		<u>(\$26,401)</u>		<u>\$5,440</u>	
9. WASTEWATER RATE BASE	<u>\$45,361</u>		<u>\$8,127</u>		<u>\$8,127</u>	
10. OPERATING RATIO					<u>10.00%</u>	

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 3-C	
TEST YEAR ENDED 6/30/2013		DOCKET NO. 130194-WS	
ADJUSTMENTS TO OPERATING INCOME		PAGE 1 OF 3	
	<u>WATER</u>	<u>WASTEWATER</u>	
OPERATING REVENUES			
. To adjust utility revenues to audited test year amount.	<u>\$726</u>	<u>\$227</u>	
OPERATION AND MAINTENANCE EXPENSES			
1. Salaries and Wages - Employees (601/ 701)			
To reflect the appropriate Salaries & Wages exp. for Employees	<u>(\$1,799)</u>	<u>(\$1,799)</u>	
2. Salaries and Wages - Officers (603/ 703)			
To reflect the appropriate Salaries & Wages exp. for Officers	<u>\$773</u>	<u>\$1,651</u>	
3. Purchased Power (615/715)			
a. To reflect the appropriate Purchased Power expense	\$739	\$1,336	
b. To reflect a rate increase from Duke Power Company	83	731	
c. To reflect an adjustment for excessive unaccounted water	<u>(\$266)</u>	<u>0</u>	
Subtotal	<u>\$556</u>	<u>\$2,067</u>	
4. Fuel For Power Production (616)			
To reflect the appropriate Purchased Power expense (AF5)	<u>(\$108)</u>	<u>\$0</u>	
5. Chemicals (618/718)			
a. To reflect the appropriate Chemicals expense	\$201	\$116	
b. To reflect an adjustment for excessive unaccounted water	<u>(32)</u>	<u>0</u>	
Subtotal	<u>\$169</u>	<u>\$116</u>	
6. Materials & Supplies (620)			
To reflect the appropriate Materials & Supplies expense (AF5)	<u>(\$926)</u>	<u>\$63</u>	
7. Contractual Services - Billing (630/730)			
To reclassify these expenses to 636/736	<u>(\$2,030)</u>	<u>(\$18,230)</u>	
(O & M EXPENSES CONTINUED ON NEXT PAGE)			

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 3-C	
TEST YEAR ENDED 5/31/2013		DOCKET NO. 130194-WS	
<u>ADJUSTMENTS TO OPERATING INCOME</u>		<u>PAGE 2 OF 3</u>	
(O & M EXPENSES CONTINUED)	<u>WATER</u>	<u>WASTEWATER</u>	
8. Contractual Services – Professional (631/731)			
a. To reflect reclassified expense from 632/732 (AF5)	(\$1,250)		\$0
b. To reflect reclassified expense from 633/733 (AF5)	0		1,286
c. To reflect the appropriate expense (AF5)	<u>(2,448)</u>		<u>0</u>
Subtotal	<u>(\$3,698)</u>		<u>\$1,286</u>
9. Contractual Services - Other (636/736)			
a. To reflect the reclassified expenses from 630/730	\$2,030		\$18,230
b. To reflect the appropriate Contractual Services expense	(2,030)		(18,230)
c. To reflect the US Water management services agreement	<u>19,938</u>		<u>30,906</u>
Subtotal	<u>\$19,938</u>		<u>\$30,906</u>
10. Rents (640/ 740)			
To reflect the appropriate rental expense (AF6)	<u>(\$428)</u>		<u>\$2,568</u>
11. Insurance Expense (655/755)			
To reflect the appropriate insurance expense	<u>(\$54)</u>		<u>\$97</u>
12. Regulatory Commission Expense (765/765)			
To reflect 4-year amortization of rate case expense (\$2,336/4)	<u>\$292</u>		<u>\$292</u>
13. Bad Debt Expense (670/770)			
To reflect the appropriate bad debt expense	<u>\$423</u>		<u>\$602</u>
14. Miscellaneous Expense (675/775)			
To reflect the appropriate miscellaneous expenses (AF5)	<u>(\$433)</u>		<u>(\$2,088)</u>
15. Sludge Removal Expense (711)			
To reflect the appropriate sludge removal expense (AF5)	<u>\$0</u>		<u>\$2,500</u>
16. Transportation Expense (750)			
To reflect the appropriate transportation expense (AF5)	<u>\$0</u>		<u>(\$19)</u>
TOTAL O & M EXPENSE ADJUSTMENTS	<u>\$12,674</u>		<u>\$20,012</u>

LAKESIDE WATERWORKS INC.		SCHEDULE NO. 3-C	
TEST YEAR ENDED 5/31/2013		DOCKET NO. 130194-WS	
<u>ADJUSTMENTS TO OPERATING INCOME</u>		<u>PAGE 3 OF 3</u>	
	<u>WATER</u>	<u>WASTEWATER</u>	
DEPRECIATION EXPENSE			
1. To reflect test year depreciation calculated per 25-30.140, FAC (AF2)	\$2,860	(\$3,878)	
2. To reflect the depreciation expense of pro forma plant	<u>96</u>	<u>62</u>	
Total	<u>\$2,956</u>	<u>(\$3,817)</u>	
AMORTIZATION OF CIAC			
1. To reflect the appropriate amount of amortization expense (AF3)	<u>\$490</u>	<u>\$278</u>	
TAXES OTHER THAN INCOME			
1. To reflect the appropriate RAFs	\$186	\$287	
2. To reflect the appropriate payroll taxes	<u>(230)</u>	<u>(348)</u>	
Total	<u>(\$43)</u>	<u>(\$61)</u>	
INCOME TAX			
To reflect the appropriate income tax	<u>\$0</u>	<u>\$0</u>	

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 3-D	
TTEST YEAR ENDED 5/31/2013		DOCKET NO. 130194-WS	
ANALYSIS OF WATER OPERATION AND MAINTENANCE EXPENSE			
	TOTAL PER UTILITY	STAFF ADJUST- MENT	TOTAL PER STAFF
(601) SALARIES AND WAGES - EMPLOYEES	\$1,799	(\$1,799)	\$0
(603) SALARIES AND WAGES - OFFICERS	1,727	773	2,500
(610) PURCHASED WATER	0	0	0
(615) PURCHASED POWER	1,916	557	2,473
(616) FUEL FOR POWER PRODUCTION	437	(108)	329
(618) CHEMICALS	269	169	438
(620) MATERIALS AND SUPPLIES	1,767	(926)	841
(630) CONTRACTUAL SERVICES - BILLING	2,030	(2,030)	0
(631) CONTRACTUAL SERVICES - PROFESSIONAL	6,318	(3,698)	2,620
(635) CONTRACTUAL SERVICES - TESTING	0	0	0
(636) CONTRACTUAL SERVICES - OTHER	18,259	19,938	38,197
(640) RENTS	2,996	(428)	2,568
(655) INSURANCE EXPENSE	576	(54)	522
(665) REGULATORY COMMISSION EXPENSE	0	292	292
(670) BAD DEBT EXPENSE	865	423	1,288
(675) MISCELLANEOUS EXPENSES	<u>1,480</u>	<u>(433)</u>	<u>1,047</u>
	<u>\$40,439</u>	<u>\$12,674</u>	<u>\$53,114</u>

LAKESIDE WATERWORKS, INC.	SCHEDULE NO. 3-E		
TEST YEAR ENDED 5/31/2013	DOCKET NO. 130194-WS		
ANALYSIS OF WASTEWATER OPERATION AND MAINTENANCE EXPENSE			
	TOTAL PER UTILITY	STAFF ADJUST- MENT	TOTAL PER STAFF
(701) SALARIES AND WAGES - EMPLOYEES	\$1,799	(\$1,799)	\$0
(703) SALARIES AND WAGES - OFFICERS	849	1,651	2,500
(710) PURCHASED SEWAGE TREATMENT	0	0	0
(711) SLUDGE REMOVAL EXPENSE	0	2,500	2,500
(715) PURCHASED POWER	3,519	2,067	5,586
(718) CHEMICALS	404	116	520
(720) MATERIALS AND SUPPLIES	77	63	140
(730) CONTRACTUAL SERVICES - BILLING	18,230	(18,230)	0
(731) CONTRACTUAL SERVICES - PROFESSIONAL	1,334	1,286	2,620
(735) CONTRACTUAL SERVICES - TESTING	0	0	0
(736) CONTRACTUAL SERVICES - OTHER	4,824	30,906	35,730
(740) RENTS	0	2,568	2,568
(750) TRANSPORTATION EXPENSE	19	(19)	0
(755) INSURANCE EXPENSE	424	97	521
(765) REGULATORY COMMISSION EXPENSES	0	292	292
(770) BAD DEBT EXPENSE	638	602	1,240
(775) MISCELLANEOUS EXPENSES	<u>2,273</u>	<u>(2,088)</u>	<u>185</u>
	<u>\$34,390</u>	<u>\$20,012</u>	<u>\$54,402</u>

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 4-A	
TEST YEAR ENDED 6/30/13		DOCKET NO. 130194-WS	
MONTHLY WATER RATES			
	UTILITY EXISTING RATES*	STAFF PRELIMINARY RATES*	4 YEAR RATE REDUCTION
<u>Residential, General Service, and Irrigation</u>			
Base Facility Charge by Meter Size			
5/8"X3/4"	\$12.96	\$15.80	\$0.08
3/4"	\$19.45	\$23.70	\$0.12
1"	\$32.42	\$39.50	\$0.20
1-1/2"	\$64.83	\$79.00	\$0.40
2"	\$103.73	\$126.40	\$0.64
3"	\$207.45	\$252.80	\$1.29
4"	\$324.16	\$395.00	\$2.01
6"	\$648.30	\$790.00	\$4.03
*Irrigation customers do not pay a base facility charge.			
Charge per 1,000 Gallons - Residential and Irrigation			
All Gallons	\$1.23		
0 - 4,000 Gallons		\$4.02	\$0.02
Over 4,000 Gallons		\$10.28	\$0.05
Charge per 1,000 Gallons – General Service	\$1.23	\$5.21	\$0.03
<u>Typical Residential 5/8" x 3/4" Meter Bill Comparison</u>			
4,000 Gallons	\$17.88	\$31.88	
6,000 Gallons	\$20.34	\$52.44	
10,000 Gallons	\$25.26	\$93.56	

LAKESIDE WATERWORKS, INC.		SCHEDULE NO. 4-B	
TEST YEAR ENDED 06/30/13		DOCKET NO. 130194-WS	
MONTHLY WASTEWATER RATES			
	UTILITY EXISTING RATES	STAFF PRELIMINARY RATES	4 YEAR RATE REDUCTION
<u>Residential</u>			
Base Facility Charge - All Meter Sizes	\$10.01	\$15.47	\$0.08
Charge per 1,000 Gallons- Residential*			
*6,000 gallon cap	\$2.46	\$7.68	\$0.04
<u>General Service</u>			
Base Facility Charge by Meter Size			
5/8"X3/4"	\$10.01	\$15.47	\$0.08
3/4"	\$15.02	\$23.21	\$0.12
1"	\$25.05	\$38.68	\$0.20
1-1/2"	\$50.08	\$77.35	\$0.40
2"	\$80.14	\$123.76	\$0.64
3"	\$160.26	\$247.52	\$1.29
4"	\$250.41	\$386.75	\$2.01
6"	\$500.84	\$773.50	\$4.02
Charge per 1,000 Gallons - General Service	\$2.95	\$9.22	\$0.05
<u>Typical Residential 5/8" x 3/4" Meter Bill Comparison</u>			
4,000 Gallons	\$19.85	\$46.19	
6,000 Gallons	\$24.77	\$61.55	
10,000 Gallons	\$24.77	\$61.55	