

State of Florida



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Public Service Commission

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

DATE: January 21, 2016

TO: Office of Commission Clerk (Stauffer)

FROM: Division of Accounting and Finance (Vogel, T. Brown) *W*
Division of Economics (Bruce) *CS*
Office of the General Counsel (Corbari, Lherisson) *CS* *ALM* *BY* *CS* *BY* *CS*

RE: Docket No. 150257-WS – Application for a staff-assisted rate case in Marion County, by East Marion Utilities, LLC.

AGENDA: 02/02/16 – Regular Agenda – Decision on Interim Rates – Participation is at the Discretion of the Commission

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Edgar

CRITICAL DATES: 02/03/16 (60-Day Suspension Date)

SPECIAL INSTRUCTIONS: None

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Case Background

East Marion Utilities, LLC (East Marion or utility) is a Class C utility serving one general service and approximately 100 residential water and wastewater customers in Marion County. Rate base was last established by the Commission in Order No. PSC-02-1168-PAA-WS.¹ The net book value was established and current rates were adopted by the Commission in Order No. PSC-15-0576-PAA-WS.² According to East Marion's 2014 annual report, the utility had water and wastewater operating revenues of \$23,750 and \$35,522, respectively, and operating expenses of \$31,504 and \$37,071, respectively, resulting in net operating losses of \$7,754 and \$1,550, respectively.

On December 3, 2015, East Marion filed its application for a staff-assisted rate case. In its application, the utility requested a test year ended December 31, 2015, for final rate purposes.

This recommendation addresses the utility's interim rates. The Commission has jurisdiction pursuant to Sections 367.082 and 367.0814(4), Florida Statutes (F.S.).

¹Order No. PSC-02-1168-PSS-WS, issued August 26, 2002, in Docket No. 010869-WS, *In re: Application for staff-assisted rate case in Marion County by East Marion Sanitary Systems, Inc.*

²Order No. PSC-15-0576-PAA-WS, issued December 21, 2015, in Docket No. 150091-WS, *In re: Application for approval of transfer of Certificate Nos. 490-W and 425-S from East Marion Sanitary Systems, Inc. to East Marion Utilities, LLC, in Marion County.*

Discussion of Issues

Issue 1: Should an interim revenue increase be approved?

Recommendation: Yes- East Marion should be authorized to collect interim revenues as indicated below:

	Adjusted Test Year Revenues	\$ Increase	Revenue Requirement	% Increase
Water	\$23,750	\$4,316	\$28,066	18.17%
Wastewater	\$35,522	\$0	\$35,522	0%

Revenues are sufficient to cover staff-adjusted O&M expenses for the wastewater system, but not the water system. As such, an interim revenue increase is warranted for the water system but not the wastewater system. (Vogel)

Staff Analysis: On December 3, 2015, East Marion filed an application requesting an interim increase in water and wastewater rates. Section 367.0814(4), F.S., details interim rate increases for staff-assisted rate cases.

Section 367.0814(4), F.S., states:

(4) The commission may, upon its own motion, or upon petition from the regulated utility, authorize the collection of interim rates until the effective date of the final order. Such interim rates may be based upon a test period different from the test period used in the request for permanent rate relief. To establish interim relief, there must be a demonstration that the operation and maintenance expenses exceed the revenues of the regulated utility, and interim rates shall not exceed the level necessary to cover operation and maintenance expenses as defined by the Uniform System of Accounts for Class C Water and Wastewater Utilities (1996) of the National Association of Regulatory Utility Commissioners.

Staff has reviewed the utility's filed O&M expenses in relation to its revenues. Based on the utility's filing, staff recommends that East Marion has demonstrated a *prima facie* entitlement to an interim rate increase in accordance with Section 367.0814(4), F.S., for the water system but not for the wastewater system.

Revenue Increase

In order to establish interim rate relief as prescribed by Section 367.0814(4), F.S., staff utilized the utility's revenues reflected in its filing. The filed revenues exceeded O&M expenses for the wastewater system, but not for the water system. Thus, staff recommends an interim increase for the water system only. The difference between the utility's revenues and the O&M expenses for water is \$4,130.

In addition, the interim water increase should be grossed up to include regulatory assessment fees (RAFs). The Commission has previously determined that it would be inappropriate to approve an increase in a utility's rates to cover its operating expenses and deny that same utility the funds to pay RAFs.³ Furthermore, by approving an interim rate increase that allows for the payment of RAFs, the utility should be able to fully cover its O&M expenses. The RAFs associated with the interim increase is calculated to be \$186 (\$4,130 x 4.5%).

In total, East Marion should be allowed an interim water revenue increase of \$4,316 (\$4,130 + \$186) in order to produce revenues sufficient to cover water O&M expenses and RAFs. Thus, staff recommends the appropriate interim revenue requirement should be \$28,066 for water. This is an 18.17 percent increase above the utility's 2014 water revenues of \$23,750. Table 1 illustrates staff's interim increase calculation.

Table 1
Determination of Interim Increase

	Water	Wastewater
1. Utility Adjusted Test Year O&M Expenses	\$27,880	\$33,083
2. Less: Staff's Adjustments	<u>\$0</u>	<u>\$0</u>
3. Staff Adjusted Test Year O&M Expenses	\$27,880	\$33,083
4. Less: Utility Test Year Revenues	<u>\$23,750</u>	<u>\$35,522</u>
5. Revenues to Cover O&M Expenses	\$4,130	(\$2,439)
6. Interim Revenue Increase	\$4,130	\$0
7. RAFs on Interim Rate Increase	\$186	\$0
8. Total Interim Revenue Increase (\$)	<u>\$4,316</u>	<u>\$0</u>
9. Total Interim Revenue Increase (%)	<u>18.17%</u>	<u>0%</u>

³Order No. PSC-01-1654-FOF-WS, issued August 13, 2001, in Docket No. 010396-WS, *In re: Application for staff-assisted rate case in Brevard County by Burkim Enterprises, Inc.*

Issue 2: What are the appropriate interim water rates?

Recommendation: The interim rate increase of 18.71 percent for water should be applied as an across-the-board increase to the service rates in effect as of December 31, 2014. The rates, as shown on Schedule No. 1, should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), Florida Administrative Code (F.A.C.). The utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. In addition, the approved rates should not be implemented until the required security has been filed, 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. (Bruce)

Staff Analysis: Staff recommends that interim service rates for East Marion be designed to allow the utility the opportunity to generate annual operating revenues of \$27,880 for water. Before removal of miscellaneous revenues, this would result in an increase of \$4,130 (17.39 percent) for water. To determine the appropriate increase to apply to the service rates, miscellaneous revenues should be removed from the test year revenues. The calculation is as follows:

Table 2
Percentage Increase Less Miscellaneous Revenues

	<u>Water</u>
1 Total Test Year Revenues	\$23,750
2 Less: Miscellaneous Revenues	<u>\$1,675</u>
3 Test Year Revenues from Service Rates	\$22,075
4 Revenue Increase	<u>\$4,130</u>
5 % Service Rate Increase (Line 4/Line 3)	18.71%

Source: Staff's Recommended Revenue Requirement and MFRs

Staff recommends that the interim rate increase of 18.71 percent for water should be applied as an across-the-board increase to the service rates in effect as of December 31, 2014.⁴ The rates, as shown on Schedule No. 1, should be effective for service rendered on or after the stamped approval date on the tariff sheets pursuant to Rule 25-30.475(1), F.A.C. The utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. In addition, the approved rates should not be implemented until the required security has been filed, 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.

⁴The revenue increase is based on 2014 water revenues. Therefore, the percentage increase should be applied to the rates in effect at year end 2014.

Issue 3: What is the appropriate security to guarantee the interim increase?

Recommendation: The utility should be required to open an escrow account or secure a surety bond or letter of credit to guarantee any potential refund of revenues collected under interim conditions. If the security provided is an escrow account, the utility should deposit \$360 into the escrow account each month. Otherwise, the surety bond or letter of credit should be in the amount of \$2,880. Pursuant to Rule 25-30.360(6), F.A.C., the utility should provide a report by the 20th of each month indicating the monthly and total revenue collected subject to refund. Should a refund be required, the refund should be with interest and in accordance with Rule 25-30.360, F.A.C. (Vogel)

Staff Analysis: Pursuant to Section 367.082, F.S., revenues collected under interim rates shall be placed under bond, escrow, letter of credit, or corporate undertaking subject to refund with interest at a rate ordered by the Commission. As recommended in Issue 1, the interim increase for water is \$4,316. In accordance with Rule 25-30.360, F.A.C., staff calculated the potential refund of revenues and interest collected under interim conditions to be \$2,880. This amount is based on an estimated eight months of revenue being collected under the recommended interim rates shown on Schedule No. 1.

The criteria for a corporate undertaking include sufficient liquidity, ownership equity, profitability, and interest coverage to guarantee any potential refund. Because East Marion was purchased from East Marion Sanitary Systems, Inc. in 2015,⁵ the utility does not have a full year of financial statements. Commission practice is to evaluate three years of financial statements for determining if the utility has the financial capability to support a corporate undertaking. Staff recommends East Marion be required to secure a surety bond, letter of credit, or escrow agreement to guarantee any potential refund of water revenues.

If the security provided is an escrow account, said account should be established between the utility and an independent financial institution or the Division of Treasury for the Florida Department of Financial Services pursuant to a written escrow agreement. The Commission should be a party to the written escrow agreement and a signatory to the escrow account. The written escrow agreement should state the following: the account is established at the direction of the Commission for the purpose set forth above; no withdrawals of funds shall occur without the prior approval of the Commission through the Commission Clerk, Office of Commission Clerk; the account shall be interest bearing; information concerning that escrow account shall be available from the institution to the Commission or its representative at all times; the amount of revenue subject to refund shall be deposited in the escrow account within seven days of receipt; and, pursuant to *Cosentino v. Elson*, 263 So. 2d 253 (Fla 3d DCA 1972), escrow accounts are not subject to garnishments.

If the security provided is an escrow account, the utility should deposit \$360 into the escrow account each month. The escrow agreement should also state that “if a refund to the customers is

⁵Order No. PSC-15-0576-PAA-WS, issued December 21, 2015, in Docket No. 150091-WS, *In re: Application for approval of transfer of Certificate Nos. 490-W and 425-S from East Marion Sanitary Systems, Inc. to East Marion Utility, LLC, in Marion County.*

required, all interest earned on the escrow account shall be distributed to the customers, and if a refund to the customers is not required, the interest earned on the escrow account shall revert to the utility.”

If the security provided is a surety bond or a letter of credit, said instrument should be in the amount of \$2,880. If the utility chooses a surety bond as security, the surety bond should state that it will be released or terminated only upon subsequent order of the Commission. If the utility chooses to provide a letter of credit as security, the letter of credit should state that it is irrevocable for the period it is in effect and that it will be in effect until a final Commission order is rendered releasing the funds to the utility or requiring a refund.

Regardless of the type of security provided, the utility should keep an accurate and detailed account of all monies it receives. Pursuant to Rule 25-30.360(6), F.A.C., the utility should provide a report by the 20th day of each month indicating the monthly and total revenue collected subject to refund. Should a refund be required, the refund should be with interest and undertaken in accordance with Rule 25-30.360, F.A.C.

In no instance should maintenance and administrative costs associated with any refund be borne by the customers. Such costs are the responsibility of, and should be borne by, the utility.

Issue 4: Should this docket be closed?

Recommendation: No. The docket should remain open pending the Commission's final action on the utility's requested rate increase. (Corbari, Lherisson)

Staff Analysis: The docket should remain open pending the Commission's final action on the utility's requested rate increase.

EAST MARION SANITARY SYSTEMS, INC.			SCHEDULE NO. 1
TEST YEAR ENDED DECEMBER 31, 2014			DOCKET NO. 150257-WS
MONTHLY WATER RATES			
	RATES AT 12/31/2014 (1)	CURRENT RATES (2)	STAFF RECOMMENDED INTERIM
<u>Residential and General Service</u>			
Base Facility Charge by Meter Size			
5/8" x 3/4"	\$9.88	\$10.05	\$11.73
3/4"	\$14.84	\$15.10	\$17.60
1"	\$24.72	\$25.15	\$29.33
1-1/2"	\$49.44	\$50.29	\$58.65
2"	\$79.11	\$80.47	\$93.84
3"	\$158.22	\$160.94	\$187.68
4"	\$247.22	\$251.47	\$293.25
6"	\$494.43	\$502.93	\$586.50
Charge per 1,000 Gallons - Residential			
0-10,000 gallons	\$2.07	\$2.11	\$2.46
Over 10,000 gallons	\$3.10	\$3.15	\$3.68
Charge per 1,000 gallons - General Service			
	\$2.42	\$2.46	\$2.87
<u>Typical Residential 5/8" x 3/4" Meter Bill Comparison</u>			
3,000 Gallons	\$16.09	\$16.38	\$19.11
6,000 Gallons	\$22.30	\$22.71	\$26.49
10,000 Gallons	\$30.58	\$31.15	\$36.33
(1) The interim rate increase was applied to the rates at 12/31/2014.			
(2) The current rates became effective October 1, 2015 as a result of a price index.			