State of Florida

# Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

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

**DATE:** 04/03/03

**TO:** DIRECTOR, DIVISION OF THE COMMISSION CLERK & ADMINISTRATIVE SERVICES (BAYÓ)

**FROM:** DIVISION OF ECONOMIC REGULATION (JOYCE, REVELL, EDWARDS, FITCH, MERCHANT)
OFFICE OF THE GENERAL COUNSEL (STERN) MKS

**RE:** DOCKET NO. 020409-SU - APPLICATION FOR RATE INCREASE IN CHARLOTTE COUNTY BY UTILITIES, INC. OF SANDALHAVEN.

**AGENDA:** 04/15/03 - REGULAR AGENDA - PROPOSED AGENCY ACTION EXCEPT ISSUES 21,22,23 - INTERESTED PERSONS MAY PARTICIPATE

**CRITICAL DATES:** 5-MONTH EFFECTIVE DATE: Extended to 04/29/03 (PAA RATE CASE)

**SPECIAL INSTRUCTIONS:** NONE

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**CASE BACKGROUND**

Utilities, Inc. of Sandalhaven (Sandalhaven or utility) is a Class B wastewater utility providing service to approximately 827 customers in Charlotte County. Sandalhaven is a wholly-owned subsidiary of Utilities, Inc. Water service is provided by Charlotte County Utilities.

In 1995, the PSC was given jurisdiction over privately-owned water and wastewater utilities in Charlotte County as a result of a resolution by the Board of County Commissioners of Charlotte County. Sandalhaven was granted a grandfather certificate by Order No. PSC-95-0478-FOF-SU, issued April 13, 1995, in Docket No. 941341-SU. In 1999, the Commission approved the certificate transfer of Sandalhaven Utility, Inc. to Utilities, Inc. of Sandalhaven by Order No. PSC-99-2114-PAA-SU (Transfer Order), issued October 25, 1999, in Docket No. 981221-SU.

This utility has never had a full rate case; however the utility's rate base was established for the transfer as of August 31, 1998, by the Transfer Order.

On August 16, 2002, the utility filed for approval of final and interim rate increases, pursuant to Sections 367.081 and 367.082, Florida Statutes. However, the information submitted did not satisfy the minimum filing requirements (MFRs) for a general rate increase. Subsequently, on October 1, 2002, the utility satisfied the MFRs and this date was designated as the official filing date, pursuant to Section 367.083, Florida Statutes. The utility requested that the Commission process this case under the proposed agency action (PAA) procedure. The 5-month statutory deadline for processing this case was March 1, 2003.

However, by letter dated January 31, 2003, Sandalhaven filed a 30-day waiver of the 5-month statutory deadline for processing this rate case. This extended the 5-month deadline for the Commission's consideration of the PAA decision to March 30, 2003. Subsequently, by letter dated February 25, 2003, Sandalhaven filed for an additional 30-day waiver of the 5-month statutory deadline for processing this rate case. This extended the 5-month deadline for the Commission's consideration of the PAA decision to April 29, 2003.

The test year for interim and final purposes is the historical test year ended December 31, 2001. In its MFRs, the utility reported operating revenues of $221,904 and a net operating loss of $16,329. By Order No. PSC-02-1703-PCO-SU, issued December 6, 2002, Sandalhaven was granted interim revenues of $276,505, which represents an increase of $54,601 or 24.61%. The utility's requested final revenues are $336,914, representing an increase of $115,009, or 51.83%.

Staff's recommendation addresses the revenue requirement and rates that should be approved on a prospective basis. The Commission has jurisdiction pursuant to Sections 367.081 and 367.082, Florida Statutes.

## DISCUSSION OF ISSUES

**ISSUE 1:** Is the quality of service provided by Sandalhaven satisfactory?

**RECOMMENDATION:** Yes. The quality of service should be considered satisfactory. (EDWARDS)

**STAFF ANALYSIS:** Pursuant to Rule 25-30.433(1), Florida Administrative Code (F.A.C.), in every water and wastewater rate case, the Commission shall determine the overall quality of service provided by a utility by evaluating three separate components of water any wastewater operations. These components are (1) the quality of the utility's product; (2) the operating conditions of the utility's plant and facilities; and, (3) the utility's attempt to address customers' satisfaction. The rule further states that sanitary surveys, outstanding citations, violations, and consent orders on file with the Department of Environmental Protection (DEP) and the County Health Department over the preceding three-year period shall be considered, along with input from the DEP and health department officials and consideration of customer comments or complaints. Staff's analysis addresses each of these three components.

Sandalhaven provides only wastewater service in Charlotte County and is located in Englewood, Florida. Charlotte County provides the water service to this area. Its customer base consists of multi-family residential, single-family residential, commercial, and general service customers.

The wastewater treatment plant is located adjacent to the Fiddler's Green Condominium II. The plant is a 150,000 gallons per day (gpd) extended aeration domestic wastewater treatment plant. This facility processes the inflowing waste and directs it to the reclaimed water processing system of the plant. The reclaimed system consists of a filtration system and a high-level chlorination system. The reclaimed water is then transported, via wastewater distribution line, to a reuse holding pond which is located at the Wildflower Country Club Golf Course. In addition, this facility has a collection system which consists of collection mains and 11 lift stations that are located throughout the service area.

Staff has reviewed, from the MFRs filed by the applicant, the following: system maps, chemicals used, chemical analyses, monthly operation reports (MORs), DEP permits, wastewater compliance inspection reports, notices, field employees' records, vehicle, and customer complaint logs maintained by the utility. Staff also researched whether any customer complaints were filed with the Commission related to this utility. Based on staff's review, everything appeared to be in satisfactory condition. DEP has jurisdictional authority regarding compliance with environmentally related wastewater rules and enforcement of those rules. According to DEP, Sandalhaven does not have any consent orders or notices of violations filed against it.

Quality of the Product

Staff has reviewed the plant MORs and chemical analyses which the utility submits to DEP monthly. The information contained in these records indicates that the quality of the plant's effluent meets DEP standards. In addition, DEP last reviewed this facility on April 4, 2002. The results of that inspection indicate that the plant's finished product met DEP's standards. Therefore, staff believes that the finished product is satisfactory.

Operating Condition of the Plant and Facilities

Staff conducted a field inspection of the utility's treatment plant, collection, and reclaimed water systems. The investigation revealed that Sandalhaven's plant appeared to be in compliance with Department of Health and DEP rules and regulations. In addition, the DEP inspector that evaluates this plant stated to staff that, currently, the operating conditions of the treatment plant, reclaimed water, and collection systems meet DEP's standards. Based on the above, staff recommends that the operating condition of the utility's facilities is satisfactory.

Customer Satisfaction

On December 10, 2002, PSC staff conducted a customer meeting in the utility's service territory in Englewood, Florida. There were approximately 19 customers in attendance. Six customers signed up to speak at the meeting. The customers' concerns were the rate increase, plant odor, the possibility of future plant expansion, and road degradation.

After the meeting, staff requested a written response from the utility regarding the concerns expressed by the customers at the customer meeting. The concerns of the customers, response from the utility, and staff's comments regarding those concerns are as follows:

Plant Odor

Customers at the Fiddler's Green Condominium II Association (Association) complained that sometimes the odor coming from the plant was unbearable and offensive. The odor is worse during the peak season when the majority of the residents are present.

In its response, the utility stated that the plant's previous owners did not operate or maintain the plant adequately. However, after the utility acquired the plant, it made numerous improvements to reduce odors emanating from the plant. The utility increased aeration and repaired and installed additional blowers. In 2001, the utility terminated the process of stabilizing sludge on-site prior to transport and disposal, which reduced ammonia off-gassing. Also, in 2001, Sandalhaven started adding histosol, an odor control product, to its equalization tank to reduce the smell of the raw wastewater at the front of the plant.

During staff's investigation, no excessive odors coming from the plant were apparent. However, staff's investigation was not conducted during the peak season. Staff has reviewed the actions the utility has taken to address excessive odors and it appears that those actions are reasonable and should resolve this issue.

Future Growth

The customers wanted to know if the utility had plans for future expansion of the plant and the effects that those plans would have on current treatment facilities.

In its response, the utility stated that there are no specific plans at the current time to expand or construct additional treatment plant. In addition, the utility indicated that during the peak three months, the average flow of the plant had only increased 10% since 1999. Therefore, the utility has no immediate need to expand the plant.

Staff's analysis of the utility's projected growth indicates that the service area will grow at a rate of 5 equivalent residential connections (ERCs) per year and staff's recommended used and useful adjustment reflects that growth allowance. DEP rules require that utilities prepare a plan for expansion when plant reaches 80% capacity. Further, because the need for plant expansion is based on development growth, it would be speculative for staff to predict any specifics regarding growth beyond the 5-year growth allowance.

Road Degradation

The president of the Association stated that several customers in the community had expressed concern regarding the sludge hauling trucks gradually degrading the quality of the entrance road. The treatment plant access road travels through both of the Fiddler's Green Condominium complexes (I and II). The customers stated that the two homeowners' associations incur the cost of maintaining the road and that the utility does not seem to be concerned about the wear and tear that the sludge hauling trucks place on the access road to the plant.

The utility indicated that they had sent a letter to a representative of the Association to discuss the issues of repairing the road. However, no response was received. In addition, the utility stated that they would be willing to meet and discuss the issue with the condos' respective boards.

Staff believes that the two parties should meet to discuss future reimbursement for road repair. Further, prudent costs paid by the utility can be recovered through rates in the future.

Summary

Based on staff's review of the wastewater treatment, collection, and the reclaimed water systems, it appears that all systems are operating properly and are in compliance with DEP standards. Further, staff believes that the utility is actively attempting to address the major customer areas of concern. Staff recommends that the quality of service provided by Sandalhaven should be considered satisfactory.

**RATE BASE**

**ISSUE 2:** Should adjustments be made to organization and franchise costs?

**RECOMMENDATION:** Yes. Sandalhaven's organization and franchise costs should be reduced by $76,921 and $23,241, respectively, to reclassify them as below the line acquisition costs, prior owner and undocumented costs. Corresponding adjustments are also necessary to decrease accumulated depreciation and depreciation expense as follows: (JOYCE)

| | Accumulated Depreciation | Depreciation Expense |
|---|---|---|
| Organization Costs | $20,866 | $1,920 |
| Franchise Costs | 13,258 | 580 |

**STAFF ANALYSIS:** Pursuant to the Transfer Order, the Commission approved the transfer of the facilities of Sandalhaven Utility, Inc., to Utilities Inc. of Sandalhaven. The purchase price of the utility was $500,000 and the Commission established rate base was $30,378 as of August 31, 1998. This resulted in a positive acquisition adjustment which the Commission did not recognize in rate base. There were numerous transfers of the utility system that occurred prior to this, as discussed in more detail in Issue 4, regarding the value of land.

Organization Costs

In staff's review of the prior transfer audit, as of the date of the transfer to Utilities, Inc. of Sandalhaven, the utility reflected a balance in organization costs of $17,021. It also had a reported balance in accumulated depreciation equal to the plant account and, thus, the account was fully depreciated. Upon our discussion with the staff auditors, those balances were not addressed in the transfer audit report as they had no impact on rate base. In reviewing the transfer audit work papers, the pre-transfer organization costs related to earlier acquisition costs. Staff does not believe that these amounts are prudent to be included in plant and, thus, the continued depreciation of these intangible assets is inappropriate. As such, staff recommends that the $17,021 balance should be removed from rate base.

Subsequent to the Commission's approval of the transfer, Utilities, Inc. of Sandalhaven recorded additional organization costs of $59,900. Pursuant to Audit Exception No. 3, these costs included $9,900 for capitalized labor for Water Services Corp. (WSC) employees. WSC is a service company for the parent company, Utilities, Inc. The remaining $50,000 was a commission paid to Kace, Inc. (Kace) for the sale of the utility.

In its response to Audit Exception No. 3, the utility states that Kace was a company hired by Utilities, Inc. to perform acquisition services, such as finding assistance and due diligence work. The utility said that Kace was hired to perform these services for three acquisitions in Florida, including Sandalhaven and that the $50,000 commission paid to Kace on March 3, 1999, was for the acquisition of Sandalhaven and was not paid until the closing of the acquisition.

Further, the utility states that the remaining costs charged to organization costs consist of capitalized time for two executives and the regional manager of Sandalhaven. The utility states that this time was used to "secure easements on property, defend legalities of the acquisition, etc."

Per the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts (USOA), the organization account shall include all fees paid to federal or state governments for the privilege of incorporation and expenditures incident to organizing the corporation and putting it into readiness to do business.

In addition, the USOA states that the Utility Plant Acquisition Adjustment account includes the difference between the cost of the purchasing utility of plant acquired and the original cost of the property acquired less accumulated depreciation, accumulated amortization, and contributions in aid of construction (CIAC) at the time of purchase. Staff interprets the term "cost of acquisition" to include any consideration paid, plus any other costs incurred related to or given for the purchase of the assets.

Staff believes the expenses discussed above should not be recorded as organization costs. First, the expenses are acquisition costs and inappropriately treated as organization costs. Second, the expenses should be borne by the stockholders of Sandalhaven's parent company because the purchase of Sandalhaven was not the ratepayers' decision, nor has Sandalhaven demonstrated how the customers have benefitted from this transaction. Because these expenses are directly associated with the change of ownership, staff believes that they should be recorded as acquisition costs.

The Commission has previously disallowed acquisition costs recorded on a utility's books as organization costs. See Order No. PSC-93-1713-FOF-SU, issued November 30, 1993, in Docket No. 921293. See also Order No. PSC-98-0524-PAA-SU, issued April 16, 1998, in Docket No. 971065. Thus, staff recommends removing the additional balance of $59,900 for organization costs from rate base. Adding the adjustment for the pre-transfer balance of $17,021 to the $59,900 results in a decrease to organization costs of $76,921. Corresponding adjustments should also be made to decrease accumulated depreciation by $20,866 and depreciation expense by $1,920.

Franchise Costs

In addition to organization costs, the utility had a pre-transfer balance of franchise fees of $12,478, with an equal amount of accumulated depreciation. Based on staff's review of the transfer audit, this balance of franchise fees was also related to acquisition costs. Consistent with staff's recommendation regarding the pre-transfer organization costs, staff believes that the prior franchise costs should also be removed from rate base.

Further, subsequent to the Commission's approval of the transfer, the utility recorded additional franchise fees of $12,591. According to Audit Exception No. 3, supporting documentation was requested but never received for $10,763 recorded for adjusting journal entries to the franchise account. Staff has reviewed the remaining $1,828 in franchise costs which related to establishing the territory of the utility and those amounts appear reasonable. Thus, staff recommends removing $10,763 in franchise fees due to lack of supporting documentation.

Based on the above, the total adjustment to franchise fees should be $23,241. Corresponding adjustments should also be made to decrease accumulated depreciation and depreciation expense by $13,258 and $580, respectively.

Conclusion

Based on the above, Sandalhaven's organization and franchise costs should be reduced by $76,921 and $23,241, respectively, to reclassify them as below the line acquisition costs, prior owner, and undocumented costs. Corresponding adjustments are also necessary to accumulated depreciation and depreciation expense as follows:

| | Accumulated Depreciation | Depreciation Expense |
|---|---|---|
| Organization Costs | $20,866 | $1,920 |
| Franchise Costs | 13,258 | 580 |

**ISSUE 3:** Should plant additions related to capitalized Allowance for Funds Used During Construction (AFUDC) accruals be allowed?

**RECOMMENDATION:** No. The utility did not have an approved AFUDC rate. The utility should remove $8,628 and $432 of average capitalized AFUDC and accumulated depreciation, respectively. The utility should also remove $452 of depreciation expense. The utility should also be required to adjust its books to remove year-end plant of $9,881 and $657 of year-end plant and accumulated depreciation, respectively. (REVELL)

**STAFF ANALYSIS:** AFUDC is an accounting entry designed to permit a utility recovery over the life of an asset the cost associated with financing eligible construction activities. AFUDC is capitalized in lieu of interest, and capitalized AFUDC recognizes that the overall capital structure provides funding for construction projects, not just debt financing. Rule 25-30.116, F.A.C., specifies the requirements necessary to capitalize AFUDC and also the methodology used to determine the AFUDC rate. Subsection 5 of that rule states that "[n]o utility may charge or change its AFUDC rate without Commission approval."

According to the staff auditors, Sandalhaven capitalized $9,881 of AFUDC for the calender years of 1999-2001. However, the utility does not have Commission approval to capitalize AFUDC. While the Commission has been granted permission to accrue AFUDC for other Florida subsidiaries of Utilities, Inc., Sandalhaven has not requested, nor received, an approved AFUDC rate.

In 2000, the utility accrued $7,374 in Account 380, Treatment and Disposal Equipment, and an additional $2,255 in Account 354, Structures and Improvements, and $252 in Account 380 in 2001. Staff believes that these amounts, totaling $9,881 in year-end plant, and $35 and $622 of year-end accumulated depreciation for water and wastewater, respectively, should be removed from the utility's books.

Since the Commission is setting rates using an average rate base, 1/2 of the amount for 2001, or $1,254, should be removed from average test year plant. Including the $7,374 of average plant discussed above, a total of $8,628 in capitalized AFUDC should be removed from average test year plant. For accumulated depreciation, the utility accrued $205 and $417, a total of $622, in Account 380 for 2000 and 2001, respectively. It also accrued an additional $35 in Account 354 for 2001. Using the same averaging methodology as discussed above, $18 and $414, a total of $432, in average accumulated depreciation, for Accounts 354 and 380, respectively, should be removed. Depreciation expense for 2001 of $35 in Account 354 and $417 in Account 380, a total of $452, should also be removed.

**ISSUE 4**: Should an adjustment be made to the value of utility land?

**RECOMMENDATION:** Yes, the value of utility land is overstated and should be reduced by $190,000. (REVELL)

**STAFF ANALYSIS:** In its MFRs, the utility reflects a $225,000 value for the land on which the wastewater treatment plant is located. This land is made up of two parcels totaling 2.15 acres.

In approving the transfer from Sandalhaven Utilities, Inc. to Utilities, Inc. of Sandalhaven, the Commission reviewed the reasonableness of the requested land value of $225,000. (See the Transfer Order.) The Commission found that while the $225,000 appraisal might be overstated due to dissimilar characteristics of the compared lots, the appraisal had been conducted by an unrelated party. Further, the order stated:

> Because we were unable to determine the original cost of the land and the disparity between the properties, we find it appropriate to use the present appraisal in this case. However, the issue of the value of the land shall be revisited in a future rate proceeding.

As such, staff has analyzed what the original cost of land was when the treatment plant was first placed into service. In order to do this, staff has attempted to research the history of these land parcels to the dates prior to the in-service date of the plant.

The utility plant is contiguous to the Fiddler's Green condominiums in Englewood. The land was originally part of a larger parcel transferred from Gasparilla Pines Association, Inc. to Eugene and Helene Schwartz, and Melvin and Vilma Steinbaum in 1979. SFSC, a Florida Partnership, bought the land in 1985. Fiddler's Green purchased the property from SFSC, a related party, in September 1987. Three corporations, Fiddler's Green Condominiums, Inc., Fiddler's Green Condominium Association, Inc., and Fiddler's Green Condominium Association II, Inc., each deeded ownership to Sandalhaven Utility, Inc. in September 1987. This was also a related party transaction, as the owner of Fiddler's Green was a major stockholder in Sandalhaven Utility, Inc.

The utility plant was placed in service in 1987, and construction began in at least 1985. In July 1990, the owners at that time had an appraisal performed that valued the land at $225,000. The appraisers used, as a comparable site, waterfront property in Venice, Florida, which is 12 miles north of the plant location in Englewood. This appraisal was reaffirmed in August 1991. According to audit work papers developed in the 1998 transfer docket, the land was not recorded on the utility books until 1991.

Additional documentation obtained from the Charlotte County Clerk of the Court, and contained in the work papers for the audit performed in this docket, indicated that the land was sold by Fiddler's Green Condominium, Inc. on December 27, 1996, to Sandalhaven Utility, Inc. for $70,000. Other county appraiser records indicate that the property was then resold on the same date, December 27, 1996, by Sandalhaven Utility, Inc. to CHP Utility, Inc., for $70,000.

In an attempt to determine the reasonableness of the 1990 appraisal of $225,000, the auditors in the 1998 transfer audit obtained a deed for comparable property sold in the Cape Haze subdivision in 1986. The Cape Haze subdivision is in the Sandalhaven service territory and is not waterfront property. The particular property was sold for $40,000. The auditors noted that the utility property was 3.67 times as large, so the $40,000 for the smaller property was grossed up to $146,826, to represent a price 3.67 times greater.

In the 1998 transfer docket, the auditors concluded that the appraisal of $225,000 was overstated because the land in Venice represented as comparable was, in fact, not comparable. The conclusion was that a value of $146,966 was more reasonable because the comparison was with a piece of land in the service area and it was usually less expensive to purchase a larger tract as opposed to a lot.

Unaudited financial records of CHP Utility, Inc. as of October 31, 1998, indicate that the land was being carried on its books at $70,000. Ten days later, on November 10, 1998, Charlotte County Property Appraiser records indicate that CHP Utility, Inc. gave a quit claim deed and a warranty deed for $35,000 to Sandalhaven Utility, Inc. According to additional Charlotte County Property

Appraiser records, the land was sold March 26, 1999, by Sandalhaven Utility, Inc. to Utilities, Inc. of Sandalhaven for $100,000.

In the current rate case audit, the auditors conducted an extensive review of mortgage records and tax appraisal documents. The auditors stated in Audit Exception No. 1 that the land value should be no higher than $35,000, which was the value based on the November 10, 1998 transfer from CHP Utility, Inc. to Sandalhaven Utility, Inc. The audit opinion also stated that the $35,000 valuation is also close to the current tax appraisal. The utility initially responded to the audit exception by stating that they believed the value should be no less than the $146,966 value placed on the land determined in the 1998 transfer docket.

In a rate proceeding for Poinciana Utilities, Inc., the utility purchased several tracts of land from a related developer party. The Commission specifically stated that:

> [i]t is the utility's burden to prove that it has recorded its investment at the original cost when first devoted to public service and we do not believe that the Utility has met this burden for its recorded cost.

<u>See</u> Order No. 22166, issued November 9, 1989, in Docket No. 881503-WS.

Further, in a rate proceeding involving Orange/Osceola Utilities, Inc., the Commission found that several related-party transactions had inflated the cost of the land. The land was transferred several times between 1974 and when it was first dedicated to public service in 1981. The Commission found that since the record was silent as to what an arms-length price would have been in 1981, the land's value should be based on the last available arms-length price per acre in 1974, adjusted for inflation. <u>See</u> Order No. 17366, issued April 6, 1987, in Docket No. 850031-WS.

The Sandalhaven property was sold by CHP Utility, Inc. to Sandalhaven Utility, Inc. for $35,000 in November 1998. As indicated previously, it appears to have been purchased for $70,000 from Sandalhaven Utility, Inc. in December 1996. CHP Utility, Inc. was a not-for-profit entity comprised of existing service area ratepayers, and the 1998 purchase from the existing for-profit utility would qualify as an arms-length transaction. This date is more than 10 years after the date that the property was dedicated to public use.

To establish the value of land in an arms-length transaction, the Commission has used appraisals valued as of the date the plant was dedicated to public service. Depending on the circumstances, the Commission has accepted or rejected appraisals depending on whether the appraisals were based on equivalent land sales.

In a rate proceeding involving Rolling Oaks Utilities, Inc., the Commission addressed the utility's purchase of 24 acres from a related development corporation. The land had previously been undeveloped, but the utility planned to place percolation ponds on the site in order to comply with a DEP requirement. Because the sale was not an arm's-length transaction and the Commission could not rely on the utility's appraisal assumptions, the Commission looked at the original cost of the land paid by the related party, adjusted for inflation, to determine the land's value. The Commission adjusted the land account to reflect the appropriate land value. See Order No. 17532, issued May 8, 1987, in Docket No. 850941-WS.

Staff believes that the value of the land on Sandalhaven's books should be reduced. The utility has not provided any information in two separate dockets to show that the $225,000 value of the land is representative of the value when the plant was first devoted to public service. Regardless of the appraisal values in 1990-1991, this value was determined more than five years after construction began. Thus, staff does not believe the utility has met its burden to prove the value of the land.

The November 1998 sale from CHP Utility, Inc. to Sandalhaven Utility, Inc. appears to be the most reasonable valuation and is the closest arms-length sales price to the date the plant was placed in service. Staff does not believe that the fact that this property had been sold for a higher price in earlier years is important; in some cases these were not arms-length transactions.

Staff requested that if the utility intended to seek another valuation for the land, that a more accurate appraisal would be required. By letter dated February 25, 2003, Sandalhaven filed for an additional 30-day waiver of the 5-month statutory deadline for processing this rate case to obtain an appraisal. By letter dated March 17, 2003, the utility stated that the appraiser's value was not substantially in excess of the $35,000 value and agreed with staff's recommendation. Based on the above, staff recommends that the Commission set the value of the utility land at $35,000, which is a reduction to utility land of $190,000.

**ISSUE 5:** Should adjustments be made to the accumulated depreciation and accumulated amortization of contributions in aid of construction (CIAC) accounts?

**RECOMMENDATION:** Yes. The utility failed to record depreciation and amortization of CIAC and used incorrect rates. Accordingly, accumulated depreciation should be increased by $84,433; depreciation expense should be increased by $15,949; accumulated amortization of CIAC should be increased by $35,128; and CIAC amortization expense should be increased by $11,461. (REVELL)

**STAFF ANALYSIS:** Rate base was established for Sandalhaven as of August 31, 1998, in Docket No. 981221-SU. According to the staff auditors in Audit Exception No. 7, the utility did not record any depreciation or amortization of CIAC for September 1998, through December 1998. Utility schedules show only an increase of $3,268 for accumulated depreciation for 1999. In addition, the depreciation rates used do not agree with the guideline lives pursuant to Rule 25-30.140, F.A.C. This rule requires water and wastewater utilities to maintain depreciation rates as prescribed by the Commission, unless specifically modified by the Commission. Staff believes that restatement of the reserve account is necessary to properly state rate base for rate-setting purposes, and to do otherwise would overstate rate base.

This restatement results in a net decrease to rate base of $21,672. Staff believes that because Sandalhaven failed to depreciate its plant and amortize its CIAC, the ratepayers will be harmed if the reserve accounts are not corrected. Sandalhaven's last rate base was established by using Commission prescribed rates, so the utility was on notice that those depreciation rates were in effect. Further, staff believes that the utility in this case made an adjustment to increase its rate base to reflect the amortization of CIAC it failed to record, but made no corresponding adjustment to correct the depreciation reserve account.

Field audit staff recalculated accumulated depreciation and accumulated amortization of CIAC for the period of September 1998 through December 2001 to reflect the correct amounts that were not reflected in the utility's calculations. The average accumulated depreciation listed in the utility's MFRs is $565,289. The audit found that accumulated depreciation should be $649,722, a difference of $84,433. Staff recommends that the accumulated depreciation account be increased by $84,433. As a result of the incorrect depreciation rates used by the utility, depreciation expense should also be increased by $15,949.

Further, staff recalculated accumulated amortization of CIAC for the same period. The average of accumulated amortization of CIAC in the utility's MFRs was $591,754. Staff auditors found that the actual average balance should be $626,882, a difference of $35,128. As such, staff also recommends that the accumulated amortization of CIAC account be increased by $35,128. Amortization expense of CIAC should also be increased by $11,461.

**ISSUE 6:** Should an adjustment be made to the Water Services Corp. (WSC) rate base allocation?

**RECOMMENDATION:** Yes, an adjustment in the amount of $12,208 should be made to increase rate base. (JOYCE)

**STAFF ANALYSIS:** Utilities, Inc., the parent company, through its subsidiary Water Service Corporation (WSC), allocates common costs, including billing costs to all of its subsidiary utilities, including Sandalhaven.

Per Audit Exception No. 2, the company included an allocation for Utilities Inc. of Florida's rate base in the general ledger to Sandalhaven but did not include an allocation of WSC's rate base. According to the staff audit of Utilities, Inc.'s affiliate transactions, the amount allocated to Sandalhaven is $12,208. Based on the above, staff recommends that rate base should be increased by $12,208.

**ISSUE 7:** What are the used and useful percentages of the utility's wastewater treatment plant, wastewater collection system, and reclaimed water system?

**RECOMMENDATION:** Based on staff's analysis, the wastewater treatment plant should be considered 57.54% used and useful (49.89% on a composite basis), and the collection system and reclaimed water system should be considered 100% used and useful. However, since the net plant subject to used and useful consideration is 100% contributed, staff believes that it would be inappropriate to make any rate base adjustment for used and useful. (EDWARDS, REVELL, MERCHANT)

**STAFF ANALYSIS:** The utility, in its filing, calculated the used and useful percentage for the wastewater treatment plant to be 66.22%. The utility requested that the used and useful percentages for land and the collection and reclaimed water systems all be considered 100%. Staff has analyzed the utility's request and our analysis of used and useful is discussed below.

Wastewater Treatment Plant

In its filing, the utility calculated its used and useful percentage for the wastewater treatment plant by taking the sum of the annual average daily flows (AADF) of 70,792 gpd and a growth allowance of 19,615 gpd (14 ERCs x 5 years x 280 gpd). It then divided that total by the plant's DEP permitted capacity of 150,000 gpd AADF. The utility did not make any adjustments for inflow and infiltration (I&I) in its calculations. This resulted in a 60.27% used and useful percentage for wastewater treatment plant. Since the utility included its reclaimed water facilities in the subaccount with other wastewater treatment equipment, it used a composite rate to recognize the reclaimed water plant as 100% used and useful. The utility calculated a composite used and useful of 66.22% and applied it to plant, accumulated depreciation, and depreciation expense accounts.

In calculating its growth allowance, the utility used historical total company flows instead of ERC growth, which is not consistent with the Commission's practice in projecting future growth. As a result of the prior owner's improper record keeping, while it had wastewater flow data, the utility had only the most recent 3 years of customer growth data. The utility's consulting engineer stated that to use linear regression on 3 years of growth data would produce an illogical conclusion. Therefore, Sandalhaven used linear regression on 10 years of historical wastewater treatment flows to project the next 5 years of flows. The utility then took the 5-year total projected flows and subtracted that from the test year flows resulting in a growth allowance of (90,407 gpd less 70,792 gpd = 19,615 gpd). To back into the annual growth of 14 ERCs, the utility used 280 gpd for consumption per ERC (which is a design criterion), and a 5-year growth period per statute.

Staff used the same methodology as the utility to calculate used and useful but we recommend that several adjustments are appropriate. The first relates to a difference in the amount of test year AADF flows. The utility used 70,792 gpd and staff calculated a different amount. Staff reviewed the utility's monthly operating reports, and performed a day-by-day count of the operator's daily logs. Staff recalculated the sum of the flows for the test year to be 72,740 gpd. Staff discussed this issue with the utility's engineering consultant, and Sandalhaven agreed with staff's calculation.

The second difference deals with determining the average historical customer growth rate. Pursuant to Commission practice, staff would normally use 5 years of historical customer growth data and apply linear regression; however, 5 years of data was not available. Therefore, staff used the 3 years of available customer growth data which was contained in the MFRs. The data was averaged and the growth allowance was determined to be 5 ERCs per year.

Staff believes that the utility's methodology in estimating the ERC growth rate has several flaws. The first is that the utility's result of 14 ERCs per year is clearly excessive based on the most recent 3-year average. Second, using total flows improperly blends the impact of customer growth with weather fluctuations, consumption changes, as well as infiltration levels. The utility's method actually measures growth in flows as opposed to ERC growth and could easily skew customer growth rates. For these reasons, staff believes that the 3-year simple average reflects a more accurate method to measure customer growth. The method staff used to determine the average ERC growth was also discussed with the utility's engineering consultant, and Sandalhaven agreed with staff.

Staff also followed Commission practice to determine the wastewater usage per customer by taking the 72,740 gpd AADF and divided that by the test year number of ERCs (861 ERCs). The result is 84 gpd per ERC. Staff calculated the 861 test year ERCs based on meter equivalents, pursuant to Rule 25-30.055, F.A.C. Staff believes that using actual consumption per ERC is more accurate than a design criteria consumption factor, as it reflects what occurred during the test year. It also matches the AADF method used to determine the test year flows and permitted capacity of the plant. Based on our calculations, the growth allowance that should be included in the used and useful calculation should be 2,100 gpd.

Staff believes that our method of calculating used and useful is consistent with Rules 25-30.431 and 25-30.432, F.A.C. Applying the above adjustments to the used and useful formula, staff believes that the wastewater treatment plant should be considered 57.54% used and useful. After removing the reclaimed water facilities, the composite used and useful percentage would be 49.89%.

Staff has also reviewed the utility's wastewater treatment plant land. This land is made up of two parcels totaling 2.15 acres, on which the treatment facilities are located. Based on our review, the utility is fully utilizing the total amount of land and we agree with the utility that it should be considered 100% used and useful.

Contribution Level of Plant

Both the utility and staff analyzed used and useful on an engineering basis and calculated adjustments to rate base consistent with each of our methodologies. However, if you look at the engineering aspect of the test year equation in a vacuum, staff believes that applying the used and useful adjustment to the utility's rate base presents an illogical result. There are two reasons for this. The first reason is that neither the utility's nor staff's used and useful equations include an estimate of consumption for the 148 ERCs that pay monthly guaranteed revenues. In its filing, the utility reflected those revenues above the line in calculating its requested revenues. Including the revenues but not incorporating the usage in used and useful clearly creates a mismatch between the rate calculation and the used and useful revenue requirement. In order to reflect the proper amount of used and useful, staff believes that this estimate should be included in the test year flows included in the numerator of the equation, thus increasing the total used and useful percentage. However, staff does not believe that this adjustment is necessary as discussed below.

The second and most crucial aspect that was left out of the used and useful analysis is the amount of CIAC included in the utility's rate base. The purpose of making a used and useful calculation is to remove from rate base any investment that the utility has in non-used and useful plant held for future customers. If non-used and useful plant is fully contributed, making a used and useful reduction to rate base would reduce rate base more than the book value originally included. Thus, a negative rate base impact would result.

An analysis of the utility's rate base components without land and working capital are shown below. Working capital is not subject to used and useful adjustments, and staff has recommended that land be considered 100% used and useful.

| **Contribution Level** | **Per Utility** | **Per Staff** |
|---|---|---|
| Plant (w/o land) | $1,685,206 | $1,588,023 |
| Accumulated Depreciation | (565,289) | (617,210) |
| Net Plant | $1,119,917 | $971,413 |
| CIAC | ($1,607,051) | ($1,607,051) |
| Accum. Amort. of CIAC | 591,754 | 626,882 |
| Net CIAC | ($1,015,297) | ($980,169) |
| Rate Base | $104,620 | ($8,756) |
| Original Non-used & Useful Adjustment | (120,350) | (147,701) |
| Rate Base Before Land & Working Capital | ($15,730) | ($156,457) |

As the above table reflects, making any used and useful adjustment will penalize the utility, given the contribution level of the utility's plant. Based on the above, staff does not believe that a used and useful adjustment should be made in this case.

Inflow and Infiltration (I&I)

In the MFRs, the utility stated that I&I was not a factor; therefore, no adjustments were required. Staff has used the customer billing analysis, which was part of the utility's filing, to determine the level of I&I. By using the data regarding the amount of water sold to customers and comparing it with the amount of wastewater treated, staff determined that I&I is not an issue. Therefore, staff agrees with the utility that no adjustments are necessary.

Reclaimed Water System

Chapter 367.0817(3), Florida Statutes, states that all prudent costs of a reuse project shall be recovered in rates. The utility, in its filing, requested 100% used and useful percentage for the reclaimed water system. As such, staff agrees with the utility that the reclaimed water system should be considered 100% used and useful.

Wastewater Collection System

The utility's customer base is primarily residential and multifamily units. A calculation for used and useful percentage of the collection system was not required because virtually all of the wastewater mains and lift stations were contributed by the developers. As such, staff believes that the wastewater collection system should be considered 100% used and useful.

Summary

Based on the above, making any used and useful adjustment will penalize the utility, given the contribution level of the utility's plant. As such, staff does not believe that a used and useful adjustment should be made in this case.

**ISSUE 8:** What is the appropriate working capital allowance?

**RECOMMENDATION:** The appropriate amount of working capital is $26,623, based on the formula method. (REVELL)

**STAFF ANALYSIS:** Rule 25-30.433(2), F.A.C., requires that Class B utilities use the formula method, or one-eighth of operation and maintenance (O&M) expenses, to calculate the working capital allowance. The utility has properly filed its allowance for working capital using the formula method. Staff has recommended several adjustments to the utility's balance of O&M expenses. Due to the adjustments recommended by staff, a decrease of $2,908 to the utility's requested working capital allowance of $29,531 is appropriate.

**ISSUE 9:** What is the appropriate rate base?

**RECOMMENDATION:** The appropriate wastewater rate base for the test year ending December 31, 2001 is $54,048. (REVELL)

**STAFF ANALYSIS:** Staff has calculated Sandalhaven's wastewater rate base using the utility's MFRs with adjustments as recommended in the preceding issues, as $54,048.

**COST OF CAPITAL**

**ISSUE 10:** What is the appropriate weighted cost of capital including the proper components, amounts and cost rates associated with the capital structure for the test year ending December 31, 2001?

**RECOMMENDATION:** Adjustments should be made to include Sandalhaven's balance of average accumulated deferred income taxes at a zero-cost rate and to correct the interest costs for long and short-term debt. The resulting overall cost of capital should be 5.72%, with a range of 5.49% to 5.96%. The return on equity (ROE) should be 10.93%, with a range of 9.93% to 11.93%. (REVELL)

**STAFF ANALYSIS:** In its MFRs, the utility used the debt and equity ratios of its parent, Utilities, Inc., to prorate Sandalhaven's share of the parent's capital. The utility then included the actual balance of Sandalhaven's customer deposits. Sandalhaven did not include any amounts for deferred income taxes in its cost of capital calculation.

In the staff audit of Utilities, Inc.'s affiliate transactions for the year ending December 31, 2001, the staff auditors recommended that the debt rates used by the utility in its MFRs were incorrect. Staff has reflected the correct debt rates in our recommended cost of capital. The auditors also stated that several components, including accumulated deferred income taxes were omitted from the various capital structures of the subsidiaries. Based on staff's review of supporting documentation provided by the utility, the only missing component for Sandalhaven was the balance of deferred income taxes. The appropriate average balance of accumulated deferred income taxes related to Sandalhaven agrees with those amounts included in the income tax section of the MFRs. Thus, staff recommends that deferred income taxes should be increased by $17,937.

Staff used the current leverage formula approved by Order No. PSC-02-0898-PAA-WS, issued July 5, 2002, in Docket No. 020006-WS to calculate the ROE. The 2002 leverage formula decision from that order was consummated by Order No. PSC-02-1252-CO-WS, issued September, 11, 2002. Using an equity ratio of 45.48%, the utility's ROE is 10.93%, with a range of 9.93% to 11.93%.

Schedule 2 shows the components, amounts and cost rates associated with the capital structure for the test year. As addressed above, staff recommends that adjustments should be made to include an allocated portion of the parent company's accumulated deferred ITCs and deferred income taxes, both at a zero-cost rate. Staff recommends approval of an overall cost of capital of 5.72%, with a range of 5.49% to 5.96%, and that the ROE be set at 10.93%, with a range of 9.93% to 11.93%.

**ISSUE 11:** Should an Allowance for Funds Used During Construction (AFUDC) rate be approved, and if so, what is the appropriate annual rate, monthly discounted rate, and the effective date for Sandalhaven?

**RECOMMENDATION:** Yes, since the utility does not currently have an authorized AFUDC rate, the Commission, on its own motion, should establish such a rate. The utility should be authorized to implement an AFUDC rate of 5.72%, on an annual basis, with a monthly discounted rate of 0.476756%. These charges should be effective for projects as of January 1, 2002. (REVELL)

**STAFF ANALYSIS:** As indicated in Issue 3, Sandalhaven does not currently have an approved AFUDC rate; nor did it request approval of such a rate in this proceeding. As previously noted, Rule 25-30.116(5), F.A.C., states that no utility may charge or change its AFUDC rate without prior Commission approval. However, Rule 25-30.116(7) states that the Commission on its own motion may initiate a proceeding to revise a utility's AFUDC. In the event that the utility will need to charge AFUDC in the future, staff believes that one should be authorized, since we are recommending that the cost of capital be updated for current costs in this proceeding. The incremental costs of approving an AFUDC rate in this docket are very minimal compared to the cost of a separate future filing for approval of an AFUDC rate.

As discussed in Issue 10, staff has recommended that the cost of capital be established as 5.72%. Consistent with Rules 25-30.116(2) and (3), the annual AFUDC rate would also be 5.72%, with a monthly discounted rate of 0.476756%. Further, Rule 25-30.116(5) states that the AFUDC rate should be effective the month following the end of the period used to establish the rate. Since the test year ended December 31, 2001 was used to determine the cost of capital, the AFUDC rate should be effective January 1, 2002. Schedule 2 reflects staff's recommended cost of capital and resulting annual AFUDC rate.

**NET OPERATING INCOME**

**ISSUE 12:** Should adjustments be made to salaries, other O&M expenses, and taxes other than income?

**RECOMMENDATION:** Yes, salaries should be reduced by $24,946 with a corresponding reduction to payroll taxes of $1,909. In addition, due to allocation errors, allocated expenses O&M and payroll taxes should be reduced by $2,032 and $971, respectively. (REVELL)

**STAFF ANALYSIS:** In Audit Exception No. 9, staff auditors noted that the utility had made a pro forma adjustment in its MFRs to increase salary expense by $15,751 to reflect 2002 salary levels. The MFRs reflect test year salaries of $54,441. After adding the $15,751 pro forma increase, the utility's total requested salary expense is $70,192.

In its pro forma adjustment, the utility included annualized full-time salary levels for two employees that were actually part-time employees in 2001 and 2002. As a result of this error, the utility's salary expense was overstated. The staff auditors also found that Sandalhaven's salaries for 2002 were lower than those in 2001, since some employees that had left the company were not replaced. In order to test this, the auditors calculated the actual salary expense for 2002 through December 9, 2002. They then projected the amount to be expensed for the remaining three weeks of the calender year. The revised 2002 salary expense calculated by the auditors totaled $45,246, rather than the company-projected amount of 70,192, a difference of $24,946. The associated payroll tax expense overstatement on the $24,946 salary expense was $1,909.

The utility responded to the auditor's salary reduction by stating that staff was correct that the two employees were part time and that the original pro forma increase was overstated. The utility prepared a revised schedule for the projected salaries of the two employees stating that the employees worked approximately 25 hours per week and were paid $12.40 an hour. This resulted in annual salaries of $32,240 for both employees, rather than the original company estimate of $51,854. Based on its corrected analysis, the utility believes that the appropriate decrease to salaries should be $19,614, ($51,854-$32,240), rather than the $24,946 recommended by the auditors.

Staff discussed the utility's response with the staff auditors. The auditors stated that their adjustment was based on 2002 actual salaries earned with an estimate for the last three weeks of 2002. The utility's projection only considered the two part-time employees and did not consider the overall salary reduction for employees no longer with the company.

Staff believes that the auditor's adjustment is appropriate because it reflects the most current level of salaries. To only consider increased salary levels without reviewing those that have been reduced is improper. As such, staff recommends that salary expense be reduced by $24,946 and that a corresponding reduction of $1,909 to the related payroll taxes also be removed.

Also in this audit exception, the auditors found that several adjustments originally proposed in the Utilities, Inc. affiliated transactions audit should be made. In that audit, there were a number of recommended adjustments to WSC's O&M expense accounts. The affiliate transactions' audit report detailed the resulting allocation adjustments for each of the Utilities, Inc. systems, including Sandalhaven. The auditors in the present docket referenced those adjustments by stating that the allocated O&M expenses from WSC were $2,032 higher than the properly allocated amount. This amount reflects the cumulative effects of the Affiliate Audit Exceptions 3,4,5,7,8, and 9. Further, the auditors recommended that payroll taxes for WSC expenses be reduced by $971. Because of the immaterial impact to Sandalhaven in this rate case, the utility has not disputed any of the exceptions in the affiliate transaction audit.

Based on the above, staff recommends that salary expense be reduced by $24,946 and associated payroll expense be reduced by $1,909. In addition, due to allocation errors, staff recommends that allocated O&M expenses and payroll taxes should be reduced by $2,032 and $971, respectively.

**ISSUE 13:** Are any miscellaneous adjustments necessary to O&M expenses?

**RECOMMENDATION:** Yes, O&M expenses should be decreased by $8,730 to remove prior period, unsupported, and non-recurring items from several accounts. (JOYCE, MERCHANT)

**STAFF ANALYSIS:** In Audit Exception No. 10, the auditors address four miscellaneous adjustments related to O&M expenses. Staff has analyzed each of the issues and our analysis is discussed below. Staff notes that the utility did not provide a response to the audit report regarding this exception.

First, the utility included 13 months of water bills in the 2001 test year purchased water account. The auditors recommended that the $115 that relates to December 2000 should be removed.

The second adjustment deals with prior period miscellaneous expenses. The company accrued bills from Waste Management that included past due bills. The actual 2001 test year expense totaled $797 for the year, instead of the $1,295 that was recorded. Thus the auditors recommended that a $498 reduction to miscellaneous expenses was appropriate.

The third adjustment addressed non-recurring and unsupported miscellaneous costs. The utility included $83 for six months of prepaid costs that are fully amortized and will not be recurring. The amount in the test year totaled $502. Also, the utility expensed $167 monthly related to a prepaid invoice of $2,000. According to the staff auditors, this invoice was requested, but never received. The auditors recommended that this unsupported amount be disallowed. Thus, the auditors recommended that $2,502 be disallowed for these miscellaneous expenses.

The last adjustment in Audit Exception No. 10 deals with legal fees associated with the ownership of lines. The total invoice was $7,019 and the auditors believe that this cost is non-recurring and may need to be deferred. Pursuant to Rule 25-30.433(8), F.A.C., non-recurring expenses shall be amortized over a 5-year period unless a shorter or longer period can be justified. Accordingly, staff believes that $1,404 should be allowed as a test year expense, and the remaining unamortized portion of $5,615 should be removed.

Based on the above, staff recommends the following adjustments to the utility's test year expenses:

| | |
|---|---|
| Purchased Water - Prior Period | ($115) |
| Miscellaneous - Prior Period | (498) |
| Miscellaneous - Non-recurring & Unsupported | (2,502) |
| Contractual Services Legal - Non-recurring | (5,615) |
| Total | ($8,730) |

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

**RECOMMENDATION:** The appropriate rate case expense for this docket is $49,750. This expense is to be recovered over four years for an annual expense of $12,438. This results in a decrease to the rate case expense requested in the MFRs of $17,563. (JOYCE)

**STAFF ANALYSIS:** The utility included a $120,000 estimate in the MFRs for current rate case expense. As part of our analysis, staff requested an update of the actual rate case expense incurred, with supporting documentation, as well as the estimated amount to complete the case. The utility submitted a revised estimated rate case expense through completion of the PAA process of $62,056, including an increase of $1,800 to consultant's fees for appraisal costs related to the determination of the proper value of utility land discussed in Issue 4. The components of the estimated rate case expense are as follows:

| | MFR Estimate | Actual | Additional Estimated | Revised Estimate to Complete |
|---|---|---|---|---|
| Filing Fee | $2,000 | $2,000 | $0 | $2,000 |
| Legal Fees | 50,000 | 6,419 | 4,050 | 10,469 |
| Consultant Fees | 45,000 | 28,874 | 2,630 | 31,504 |
| WSC In-house Fees | 11,000 | 2,884 | 3,849 | 6,733 |
| Miscellaneous Expense | 12,000 | 680 | 10,670 | 11,350 |
| **Total Rate Case Expense** | $120,000 | $40,857 | $21,199 | $62,056 |

Pursuant to Section 367.081(7), Florida Statutes, the Commission shall determine the reasonableness of rate case expenses and shall disallow all rate case expenses determined to be unreasonable. Staff has examined the requested actual expenses, supporting documentation, and estimated expenses as listed above for the current rate case. Staff believes that the revised estimate to complete the case is reasonable with two exceptions, as discussed below.

The first adjustment relates to cost incurred to correct deficiencies in the MFR filing. As reflected in its response to staff's data request, the utility's consultant incurred $2,496 related to correcting the MFRs. The Commission has previously disallowed rate case expense associated with correcting MFR deficiencies because of duplicate filing costs. See Order No. PSC-01-0326-FOF-SU, issued February 6, 2001, in Docket No. 991643-SU. Accordingly, staff recommends that $2,496 be removed as duplicative and unreasonable rate case expense.

Staff's second adjustment relates to $10,670 in estimated travel expenses for WSC employees. When reviewing the submitted invoices and estimates to complete, staff realized that the utility did not submit any documentation for the $11,350 in miscellaneous rate case expense. When requested by staff, the utility provided documentation supporting $430 in preparation and mailing costs for one customer notice and an additional $250 for other miscellaneous mailing costs. The utility responded that the remaining $10,670 related to estimated travel costs for a utility representative to travel to Florida at least once before the resolution of the case.

Staff does not believe the estimated travel expenses are reasonable for several reasons. One, the travel cost appears excessive for one trip to Tallahassee and there are no breakdowns of the estimated travel costs to allow staff to test for reasonableness. In addition, staff does not believe that travel costs are required since estimated costs are already included for the utility's consultant to prepare for and attend the agenda conference.

However, staff notes that the utility's estimate does not include the costs for additional customer notices that are required. Staff is aware that one notice recently went out for the implementation of interim rates and a second notice will be required for the PAA rates. Using the actual cost for one notice of $430, staff recommends that $860 in additional costs should be added back to the utility's estimated rate case expense. Based on the above, staff believes that the miscellaneous expenses should be reduced by $9,810. This allows a total of $1,540 for miscellaneous notice and mailing costs.

Staff recommends that the appropriate total rate case expense is $49,750. A breakdown of the allowance of rate case expenses is as follows:

| | MFR Estimate | Utility Revised Actual & Estimated | Staff Adjustments | Total |
|---|---|---|---|---|
| Filing Fee | $2,000 | $2,000 | $0 | $2,000 |
| Legal Fees | 50,000 | 10,469 | 0 | 10,469 |
| Consultant Fees | 45,000 | 31,504 | (2,496) | 29,008 |
| WSC In-house Fees | 11,000 | 6,733 | 0 | 6,733 |
| Miscellaneous Expense | 12,000 | 11,350 | (9,810) | 1,540 |
| **Total Rate Case Expense** | $120,000 | $62,056 | ($12,306) | $49,750 |
| **Annual Amortization** | $30,000 | | ($17,563) | $12,438 |

The recommended allowable rate case expense is to be amortized over four years, pursuant to Chapter 367.0816, Florida Statutes, at $12,438 per year. Based on the data provided by the utility and the staff recommended adjustments mentioned above, staff recommends that the rate case expense should be reduced by $17,563. This is the difference between the $12,438 recommended by staff and the $30,000 included as expenses on MFR Schedule B-10.

**ISSUE 15:** What adjustments, if any, should be made to the utility's property taxes?

**RECOMMENDATION:** Property taxes should be decreased by $6,893 to remove a prior year past due amount. (JOYCE)

**STAFF ANALYSIS:** Per Audit Exception No. 11, a $6,893 payment of past due property tax was made in October 2001, and was included in the $22,147 of real and personal property taxes shown in the MFRs. Staff believes these taxes should be removed because they overstate the proper amount of test year taxes other than income.

Staff notes that the utility did not provide a response to this audit exception.

**ISSUE 16:** What is the test year operating income before any revenue increase?

**RECOMMENDATION:** Based on the adjustments discussed in previous issues, staff recommends that the test year operating income before any provision for increased revenues should be ($14,405). (JOYCE)

**STAFF ANALYSIS:** As shown on attached Schedule 3-A, after applying staff's adjustments, net operating income for the test year is ($14,405). Staff's adjustments to operating income are listed on attached Schedule 3-B.

**REVENUE REQUIREMENT**

**ISSUE 17:** What is the appropriate revenue requirement?

**RECOMMENDATION:** The following revenue requirement should be approved. (JOYCE)

| | Test Year Revenues | $ Increase | Revenue Requirement | % Increase |
|---|---|---|---|---|
| Wastewater | 221,904 | $29,378 | $251,282 | 13.24% |

**STAFF ANALYSIS:** Sandalhaven requested final rates designed to generate annual revenues of $336,913. These revenues exceed test year revenues of $221,904 by $115,009 (or 51.83%).

Based upon staff's recommendations concerning the underlying rate base, cost of capital, and operating income issues, we recommend approval of rates that are designed to generate a revenue requirement of $251,282. These revenues exceed staff's adjusted test year revenues by $29,378 (or 13.24%) as shown on attached Schedule 3-A. This increase will allow the utility the opportunity to recover its expenses and earn an 5.72% return on its investment in rate base.

**RATES AND RATE STRUCTURE**

**ISSUE 18:** Should the utility's general service tariff be revised to remove a 1½ inch meter (15 ERC Restaurant) class of service?

**RECOMMENDATION:** Yes. That class of service should be discontinued and the customer should be charged a tariff rate based on its water meter size. (MERCHANT, JOYCE)

**STAFF ANALYSIS:** The utility's tariff currently has a general service class labeled "1½ inch (15 ERC Restaurant)" and the utility collects this tariff from a restaurant in Sandalhaven's territory. The customer currently has a 1½ inch meter, as issued by Charlotte County who provides water service to the area. As stated on its tariff, this is equivalent to 15 ERCs instead of the normal three ERCs that all other 1½ inch meter customers are charged. Thus, this customer is charged 5 times what all other 1½ inch metered customers are charged. Staff questioned the utility about the history of this rate classification and why it is not discriminatory.

The utility's response to this issue was that the account was set up under prior ownership and while under the rate jurisdiction of Charlotte County. The rate for this account was approved by Charlotte County and grandfathered in by the Florida Public Service Commission. The utility has no specific knowledge of why the 3-inch tariff rate was used for this account. One explanation offered by the utility was that a 3-inch base facility charge was used because that meter is equivalent to 15 ERCs and the restaurant was estimated to have a demand of 15 ERCs.

It is the utility's burden to show that this rate class is appropriate and not discriminatory. The answer that "it has always been that way" is insufficient. The utility has provided no information whatsoever to show that this customer produces more wastewater than any other 1½ inch-metered customer. As such, staff recommends that this class of service be discontinued, and the customer be charged a tariff rate based on its 1½ inch meter size.

**ISSUE 19:** What are the appropriate monthly rates for wastewater services for this utility?

**RECOMMENDATION:** The appropriate monthly rates are shown on Schedule 4. Staff's recommended rates are designed to produce revenues of $245,872, excluding miscellaneous service charge revenues. The utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. In addition, the rates should not be implemented until after staff has approved the proposed customer notice, and after the notice is expected to have been received by the customers. The utility should provide proof of the date the notice was given no less than 10 days after the date of the notice. (JOYCE)

**STAFF ANALYSIS:** As discussed in Issue 17, the appropriate revenue requirement is $251,282. After excluding miscellaneous service charges of $5,410, the revenue to be recovered through rates is $245,872. Sandalhaven's current rate structure is the base facility charge and gallonage charge with an 8,000 gallon cap on residential customers. The utility's current rate structure does not contain a differential in the gallonage charge between residential and general service. The differential is designed to recognize that approximately 80% of the residential customer's water usage will not return to the wastewater system. For multi-family and general service customers, approximately 96% of water usage is returned. This wastewater gallonage rate differential is employed by the Commission in wastewater rate settings and is widely recognized as an industry standard. Based on the above, staff believes that the gallonage rate differential should be used in this case.

The utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice, and the notice has been received by the customers. The utility should provide proof of the date notice was given no less than 10 days after the date of the notice.

A comparison of the utility's original rates, requested rates and staff's recommended rates is shown on Schedule 4, which is attached.

**ISSUE 20:** Should the utility's proposed tariff to implement a reuse service rate be approved?

**RECOMMENDATION:** Yes, the utility's proposed tariff to implement a reuse service rate should be approved. First Revised Tariff Sheet No. 16.0 and Original Tariff Sheet No. 17.5 should be approved as filed. The approved tariffs 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. (FITCH)

**STAFF ANALYSIS:** The utility entered into a contract with the Wildflower Golf & Country Club (Club) on March 13, 1995, to provide reuse to the Club at a rate of zero for 60 months from the date that reuse would be available (September 30, 1995). On November 7, 1997, the utility and Club entered into a contract for reuse modifying the March 13, 1995, contract. The November 7, 1997, contract included an annual fee of $4,000 (to be paid in $1,000 increments quarterly) which was intended to cover an unanticipated cost increase for testing and operating the reuse system. Staff discovered this charge while reviewing the utility's rate filing for this case. Staff notified the utility that this charge was not included in the utility's tariffs. Subsequently, the utility requested approval of the quarterly reuse rate for the Club and provided staff with First Revised Tariff No. 16.0 and Original Tariff No. 17.5 reflecting the quarterly reuse rate for the Club of $1,000.

Section 367.091(3), Florida Statutes, specifies that each utility's rates, charges, and customer service policies must be contained in a tariff approved by and on file with the Commission. Section 367.091(4), Florida Statutes, specifies that a utility may only impose and collect those rates and charges approved by the Commission for the particular class of service involved. Currently, the utility is charging the Club $1,000 per quarter for reuse service. The utility does not have a tariffed reuse rate on file with the Commission.

The Club is currently the utility's only reuse customer. According to responses to staff's data request, the Club is able to meet the utility's effluent disposal needs, and the utility has no plans to expand its reuse service to residential customers in the near future. The current rate that the utility is charging was agreed to by the Club. The Club is not a related party to the utility.

Generally, reuse rates cannot be determined in the same fashion as other water and wastewater rates set by the Commission. Reuse rates based on rate base and revenue requirements would typically be so high that it would be impractical to use reuse at all, based on the revenue needed to supply the service. When staff considers recommending reuse rates, staff must consider the type of customer being served and balance the disposal needs of the utility with the consumption needs of the customer. In this case, the only reuse customer is the Club, and the utility does not plan on expanding its reuse service to residential customers in the near future.

The next factor looked at was the disposal needs of the utility and customer. In cases where a utility has excess reuse capacity, rates typically would be set lower to promote reuse at a level sufficient to meet the utility's disposal needs. In cases where a utility's reuse capacity is unable to meet demand, rates would be set higher or rate structure would be changed in order to promote conservation. In this case, the Club is able to meet the needs of the utility's disposal and has agreed to a rate for accepting the reuse.

Based on the above, staff believes that a quarterly flat rate of $1,000 is an appropriate rate for reuse service to the Club. The utility's proposed tariff to implement a reuse service rate should be approved. First Revised Tariff Sheet No. 16.0 and Original Tariff Sheet No. 17.5 should be approved as filed. The approved tariffs 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.

**ISSUE 21**: In determining whether any portion of the interim increase granted should be refunded, how should the refund be calculated, and what is the amount of the refund, if any?

**RECOMMENDATION**: The proper refund amount should be calculated by using the same data used to establish final rates, excluding rate case expense. This revised revenue requirement for the interim collection period should be compared to the amount of interim revenues granted. Based on this calculation, the utility should be required to refund 14.11% of wastewater revenues collected under interim rates. The refund should be made with interest in accordance with Rule 25-30.360(4), F.A.C. The utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C. (JOYCE)

**STAFF ANALYSIS**: By Order No. PSC-02-1703-PCO-SU, issued on December 6, 2002, in this docket, the Commission authorized the collection of interim wastewater rates, subject to refund, pursuant to Section 367.082, Florida Statutes. The approved interim revenue requirement is shown below:

| Revenue Requirement | Revenue Increase | Percentage Increase |
|---|---|---|
| $ 276,505 | $54,601 | 24.61% |

According to Section 367.082, Florida Statutes, any refund should be calculated to reduce the rate of return of the utility during the pendency of the proceeding to the same level within the range of the newly authorized rate of return. Adjustments made in the rate case test period that do not relate to the period interim rates are in effect should be removed. The inclusion of a prospective attrition allowance or rate case expense is an example of adjustments which are recovered only after final rates are established.

In this proceeding, the test period for establishment of interim and final rates is the twelve-month period ended December 31, 2001. Sandalhaven's approved interim rates did not include any provisions for pro forma, or projected, operating expenses or plant. The interim increase was designed to allow recovery of actual interest costs, and the floor of the last authorized range for equity earnings.

To establish the proper refund amount, staff has calculated a revised interim revenue requirement utilizing the same data used to establish final rates. Rate case expense was excluded because it was not an actual expense during the interim collection period.

Using the principles discussed above, staff has calculated the interim revenue requirement for the interim collection period to be $238,258 for wastewater. This revenue level is less than the interim revenue which was granted in Order No. PSC-02-1703-PCO-SU. Therefore, staff recommends a refund of 14.11% of interim rates.

Thus, the utility should be required to refund 14.11% of wastewater revenues collected under interim rates. The refund should be made with interest in accordance with Rule 25-30.360(4), F.A.C. The utility should be required to submit proper refund reports pursuant to Rule 25-30.360(7), F.A.C. The utility should treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C.

**ISSUE 22:** What is the appropriate amount by which rates should be reduced four years after the established effective date to reflect the removal of the amortized rate case expense as required by Section 367.0816, Florida Statutes?

**RECOMMENDATION:** The wastewater rates should be reduced as shown on Schedule 4 to remove $13,024 in rate case expense, grossed-up for regulatory assessment fees, which is being amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the four-year rate case expense recovery period, pursuant to Section 367.0816, Florida Statutes. The utility should be required to file revised tariffs and a proposed customer notice setting forth the lower rates and the reason for the reduction no later than one month prior to the actual date of the required rate reduction. (JOYCE)

**STAFF ANALYSIS:** Section 367.0816, Florida Statutes, 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 the rates. The reduction will reflect the removal of revenues associated with the amortization of rate case expense and the gross-up for regulatory assessment fees which is $13,024. The decreased revenues will result in the rate reduction recommended by staff on Schedule 4.

The utility should be required to file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), F.A.C. The 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 no less than 10 days after the date of the notice.

If the utility files this reduction in conjunction with a price index or pass-through rate adjustment, separate data shall be filed for the price index and/or pass-through increase or decrease, and for the reduction in the rates due to the amortized rate case expense.

**OTHER ISSUES**

**ISSUE 23:** Should Sandalhaven be ordered to show cause, in writing, within 21 days, why it should not be fined for collecting charges not approved by the Commission, in apparent violation of Sections 367.081(1), and 367.091(3), Florida Statutes?

**RECOMMENDATION:** No, a show cause proceeding should not be initiated at this time for this issue. The utility should be put on notice that pursuant to Sections 367.081(1) and 367.091(3), Florida Statutes, it may only charge rates and charges approved by the Commission. (STERN, FITCH)

**STAFF ANALYSIS:** The utility entered into a contract with the Wildflower Golf & Country Club (Club) on March 13, 1995, to provide reuse to the Club at a rate of zero for 60 months from the date that reuse would be available (September 30, 1995). On November 7, 1997, the utility and Club entered into a contract for reuse modifying the March 13, 1995, contract. The November 7, 1997, contract included an annual fee of $4,000 (to be paid in $1,000 increments quarterly) which was intended to cover the increase in cost for testing and operating the reuse system, which was not anticipated in the original contract. Staff discovered this charge while reviewing the utility's rate filing for this case. Staff notified the utility that this charge was not included in the utility's tariffs. Subsequently, the utility requested approval of the quarterly reuse rate for the Club and provided staff with First Revised Tariff No. 17.0 and Original Tariff No. 20.5 reflecting the quarterly reuse rate for the Club of $1,000.

Section 367.081(1), Florida Statutes, provides that a utility may only charge rates and charges that have been approved by the Commission. Section 367.091(3), Florida Statutes, provides that "each utility's rates, charges, and customer service policies must be contained in a tariff approved by and on file with the Commission." It appears that the utility violated these statutes.

Schedule E-5 of the utility's rate case filing lists revenues for reuse contract charges of $4,000. The Commission did not approve a reuse rate for this utility and the utility does not have an approved reuse rate tariff on file with the Commission. This collection of reuse charges was unauthorized, and thus was an apparent violation of Sections 367.081(1) and 367.091(3), Florida Statutes.

Section 367.161(1), Florida Statutes, authorizes the Commission to assess a penalty of not more than $5,000 per day for each offense, if a utility is found to have knowingly refused to comply with, or to have willfully violated any Commission rule, order, or provision of Chapter 367, Florida Statutes.

Staff recommends that a show cause proceeding not be initiated at this time for several reasons. First, the revenue was properly recorded. Second, once staff informed the utility of the situation, they submitted a proposed tariff in a timely fashion. Finally, it has been the Commission's practice to encourage reuse. However, the utility should be put on notice that, pursuant to Sections 367.081(1) and 367.091(3), Florida Statutes, it may only charge rates and charges approved by the Commission.

**ISSUE 24:** Should this docket be closed?

**RECOMMENDATION:** If no person whose substantial interests are affected by the proposed agency action files a protest within twenty-one days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the utility and approved by staff, and the refund has been completed and verified by staff. Once these actions are complete, this docket may be closed administratively, and the escrow account may be released. (STERN, JOYCE)

**STAFF ANALYSIS:** If no person whose substantial interests are affected by the proposed agency action files a protest within twenty-one days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the utility and approved by staff, and the refund has been completed and verified by staff. Once these actions are complete, this docket may be closed administratively, and the escrow account may be released.

**UTILITIES, INC. OF SANDALHAVEN**
**SCHEDULE OF WASTEWATER RATE BASE**
**TEST YEAR ENDED 12/31/01**

**SCHEDULE 1-A**
**DOCKET 020409-SU**

| | DESCRIPTION | TEST YEAR PER UTILITY | UTILITY ADJUST-MENTS | ADJUSTED TEST YEAR PER UTILITY | STAFF ADJUST-MENTS | STAFF ADJUSTED TEST YEAR |
|---|---|---|---|---|---|---|
| 1 | UTILITY PLANT IN SERVICE | $1,685,206 | $0 | $1,685,206 | ($96,582) | $1,588,624 |
| 2 | LAND | 225,000 | 0 | 225,000 | (190,000) | 35,000 |
| 3 | NON-USED & USEFUL COMPONENTS | 0 | (120,350) | (120,350) | 120,350 | 0 |
| 4 | CONSTRUCTION WORK IN PROGRESS | 8,546 | (8,546) | 0 | 0 | 0 |
| 5 | ACCUMULATED DEPRECIATION | (565,289) | 0 | (565,289) | (50,741) | (616,030) |
| 6 | CIAC | (1,607,051) | 0 | (1,607,051) | 0 | (1,607,051) |
| 7 | AMORTIZATION OF CIAC | 544,039 | 47,715 | 591,754 | 35,128 | 626,882 |
| 8 | ACQUISITION ADJUSTMENTS - NET | 448,387 | (448,387) | 0 | 0 | 0 |
| 9 | WORKING CAPITAL ALLOWANCE | 0 | 29,531 | 29,531 | (2,908) | 26,623 |
| | **RATE BASE** | $738,838 | ($500,037) | $238,801 | ($184,753) | $54,048 |

| | UTILITIES, INC. OF SANDALHAVEN<br>ADJUSTMENTS TO RATE BASE<br>TEST YEAR ENDED 12/31/01 | SCHEDULE 1-B<br>DOCKET 020409-SU |
|---|---|---|
| | **EXPLANATION** | **WASTEWATER** |
| | **PLANT IN SERVICE** | |
| 1 | Removal of Organization Costs | ($76,921) |
| 2 | Removal of Franchise Costs | (23,241) |
| 3 | Add allocated WSC Plant | 12,208 |
| 4 | Remove capitalized AFUDC | (8,628) |
| 5 | Total | ($96,582) |
| | **LAND** | |
| | Reduction for adjusted value | ($190,000) |
| | **NON-USED AND USEFUL** | |
| | Reflect net non-used and useful adjustment | $120,350 |
| | **ACCUMULATED DEPRECIATION** | |
| 1 | Correction for incorrect rates | ($84,433) |
| 2 | Remove AFUDC accumulated depreciation | (432) |
| 3 | Remove for Organization | 20,866 |
| 4 | Remove for Franchise | 13,258 |
| 5 | Total | ($50,741) |
| | **ACCUM. AMORT. OF CIAC** | |
| | Increase for error | $35,128 |
| | **WORKING CAPITAL** | |
| | To reduce to 1/8 O&M Expense | ($2,908) |

**UTILITIES, INC. OF SANDALHAVEN**
**CAPITAL STRUCTURE-SIMPLE AVERAGE**
**TEST YEAR ENDED 12/31/01**

**SCHEDULE 2**
**DOCKET 020409-SU**

| | DESCRIPTION | TOTAL CAPITAL | SPECIFIC ADJUST-MENTS (EXPLAIN) | PRO RATA ADJUST-MENTS | CAPITAL RECONCILED TO RATE BASE | RATIO | COST RATE | WEIGHTED COST |
|---|---|---|---|---|---|---|---|---|
| **PER UTILITY** | | | | | | | | |
| 1 | LONG TERM DEBT | $72,051,803 | $0 | ($71,948,438) | $103,365 | 43.28% | 8.82% | 3.82% |
| 2 | SHORT-TERM DEBT | 15,659,000 | 0 | (15,636,545) | 22,455 | 9.40% | 2.54% | 0.24% |
| 3 | PREFERRED STOCK | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% |
| 4 | COMMON EQUITY | 73,169,033 | 0 | (73,064,076) | 104,957 | 43.95% | 11.14% | 4.90% |
| 5 | CUSTOMER DEPOSITS | 8,025 | 0 | 0 | 8,025 | 3.36% | 6.00% | 0.20% |
| 6 | DEFERRED INCOME TAXES | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% |
| 7 | **TOTAL CAPITAL** | $160,887,861 | $0 | ($160,649,059) | $238,802 | 100.00% | | 9.15% |
| **PER STAFF** | | | | | | | | |
| 8 | LONG TERM DEBT | $72,051,803 | $0 | ($72,039,225) | $12,578 | 23.27% | 8.71% | 2.03% |
| 9 | SHORT-TERM DEBT | 15,659,000 | 0 | ($15,656,266) | 2,734 | 5.06% | 4.38% | 0.22% |
| 10 | PREFERRED STOCK | 0 | 0 | $-0 | 0 | 0.00% | 0.00% | 0.00% |
| 11 | COMMON EQUITY | 73,169,033 | 0 | ($73,156,260) | 12,773 | 23.63% | 10.93% | 2.58% |
| 12 | CUSTOMER DEPOSITS | 8,025 | 0 | 0 | 8,025 | 14.85% | 6.00% | 0.89% |
| 13 | DEFERRED INCOME TAXES | 0 | 17,937 | 0 | 17,937 | 33.19% | 0.00% | 0.00% |
| 15 | **TOTAL CAPITAL** | $160,887,861 | $17,937 | ($160,851,750) | $54,048 | 100.00% | | 5.72% |

| | LOW | HIGH |
|---|---|---|
| **RETURN ON EQUITY** | 9.93% | 11.93% |
| **OVERALL RATE OF RETURN** | 5.49% | 5.96% |

**UTILITIES, INC. OF SANDALHAVEN**
**STATEMENT OF WASTEWATER OPERATIONS**
**TEST YEAR ENDED 12/31/01**

**SCHEDULE 3-A**
**DOCKET 020409-SU**

| | DESCRIPTION | TEST YEAR PER UTILITY | UTILITY ADJUST-MENTS | ADJUSTED TEST YEAR PER UTILITY | STAFF ADJUST-MENTS | STAFF ADJUSTED TEST YEAR | REVENUE INCREASE | REVENUE REQUIREMENT |
|---|---|---|---|---|---|---|---|---|
| 1 | OPERATING REVENUES | $221,904 | $115,009 | $336,913 | ($115,009) | $221,904 | $29,378<br>13.24% | $251,282 |
| | OPERATING EXPENSES | | | | | | | |
| 2 | OPERATION & MAINTENANCE | $228,069 | $38,182 | $266,251 | ($53,271) | $212,981 | | $212,981 |
| 3 | DEPRECIATION | 4,507 | (4,990) | (483) | 6,526 | 6,043 | | 6,043 |
| 4 | AMORTIZATION | 0 | 0 | 0 | 0 | 0 | | 0 |
| 5 | TAXES OTHER THAN INCOME | 37,964 | 4,537 | 42,501 | (14,948) | 27,553 | 1,322 | 28,875 |
| 6 | INCOME TAXES | (32,307) | 39,078 | 6,771 | (17,038) | (10,267) | 10,557 | 291 |
| 7 | TOTAL OPERATING EXPENSES | $238,233 | $76,807 | $315,040 | ($78,731) | $236,309 | $11,879 | $248,189 |
| 8 | OPERATING INCOME | ($16,329) | $38,202 | $21,873 | ($36,278) | ($14,405) | $17,498 | $3,093 |
| 9 | RATE BASE | $738,838 | | $238,801 | | $54,048 | | $54,048 |
| 10 | RATE OF RETURN | (2.21%) | | 9.16% | | (26.65%) | | 5.72% |

| UTILITIES, INC. OF SANDALHAVEN<br>ADJUSTMENTS TO OPERATING INCOME<br>TEST YEAR ENDED 12/31/01 | | SCHEDULE 3-B<br>DOCKET 020409-SU |
|---|---|---|
| | **EXPLANATION** | **WASTEWATER** |
| | **OPERATING REVENUES** | |
| | Remove requested final revenue increase | ($115,009) |
| | **OPERATION & MAINTENANCE EXPENSE** | |
| 1 | Remove out of eriod water expense | ($115) |
| 2 | Correction of error of waste management expense | (498) |
| 3 | Reduction of amortized prepaid expenses | (2,502) |
| 4 | Amortize non-recurring legal fees | (5,615) |
| 5 | Overstated pro forma salary | (24,946) |
| 6 | Reduce WSC allocated operating expenses | (2,032) |
| 7 | Reduction to rate case expense amortization | (17,563) |
| | Total | ($53,271) |
| | **DEPRECIATION EXPENSE-NET** | |
| 1 | Remove organization depreciation expense | ($1,920) |
| 2 | Remove franchise depreciation expense | (580) |
| 3 | Remove AFUDC depreciation expense | (452) |
| 4 | Correction of depreciation rates | 15,949 |
| 5 | Correction of amortization of CIAC rates | (11,461) |
| 6 | Remove non-used and useful adjustment | 4,990 |
| | Total | $6,526 |
| | **TAXES OTHER THAN INCOME** | |
| 1 | RAFs on revenue adjustments above | ($5,175) |
| 2 | Payroll tax reduction for overstated pro forma | (1,909) |
| 3 | Reduce WSC allocated payroll taxes | (971) |
| 4 | Remove prior year payment of property tax | (6,893) |
| | Total | ($14,948) |
| | **INCOME TAXES** | |
| | To adjust to test year income tax expense | ($17,038) |

**UTILITIES, INC. OF SANDALHAVEN**
**WASTEWATER MONTHLY SERVICE RATES**
**TEST YEAR ENDED 12/31/01**

**SCHEDULE 4**
**DOCKET 020409-SU**

| | Rates Prior to Filing | Commission Approved Interim | Utility Requested Final | Staff Recomm. Final | 4-YEAR Rate Reduction |
|---|---|---|---|---|---|
| **Residential** | | | | | |
| Base Facility Charge: | | | | | |
| All meter sizes | $12.00 | $15.03 | $18.40 | $12.24 | $0.63 |
| Gallonage Charge (per 1,000 gallons) | | | | | |
| 8,000 gallon cap | $2.59 | $3.24 | $3.97 | $3.44 | $0.18 |
| **Multi-Family** | | | | | |
| Base Facility Charge: | | | | | |
| All meter sizes | $12.00 | $15.03 | $18.40 | $12.24 | $0.63 |
| Gallonage Charge (per 1,000 gallons) | $2.59 | $3.24 | $3.97 | $4.13 | $0.21 |
| **General Service** | | | | | |
| Base Facility Charge: | | | | | |
| Meter Size: | | | | | |
| 5/8" x 3/4" | $12.00 | $15.03 | $18.40 | $12.24 | $0.63 |
| 1" | $30.00 | $37.57 | $46.01 | $18.36 | $0.95 |
| 1-1/2" | $60.00 | $75.13 | $92.02 | $30.61 | $1.59 |
| 1-1/2" (15 ERC Restaurant) | $180.00 | $225.39 | $276.07 | $61.21 | $3.17 |
| 2" | $96.00 | $120.21 | $147.24 | $97.94 | $5.08 |
| 3" | $180.00 | $225.39 | $276.07 | $0.00 | $0.00 |
| 4" | $300.00 | $375.66 | $460.12 | $0.00 | $0.00 |
| 6" | $600.00 | $751.31 | $920.24 | $0.00 | $0.00 |
| Gallonage Charge, per 1,000 Gallons | $2.59 | $3.24 | $3.97 | $4.13 | $0.21 |
| | | **Typical Residential Bills** | | | |
| 5/8" x 3/4" meter | | | | | |
| 3,000 Gallons | $19.77 | $24.75 | $30.31 | $22.57 | $1.17 |
| 5,000 Gallons | $24.95 | $31.23 | $38.25 | $29.45 | $1.53 |
| 8,000 Gallons | $32.72 | $40.95 | $50.16 | $39.78 | $2.06 |
| (Gallonage Cap - 8,000 Gallons) | | | | | |