

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation of rates of O&S Water Company, Inc. in Osceola County for possible overearnings. | DOCKET NO. 100400-WU  
ORDER NO. PSC-10-0656-FOF-WU  
ISSUED: November 1, 2010

The following Commissioners participated in the disposition of this matter:

NANCY ARGENZIANO, Chairman  
LISA POLAK EDGAR  
NATHAN A. SKOP  
ART GRAHAM  
RONALD A. BRISÉ

ORDER INITIATING OVERTURNING INVESTIGATION  
AND MAKING REVENUES SUBJECT TO REFUND

BY THE COMMISSION:

**Background**

O&S Water Company, Inc. (O&S or Utility) is a Class A water utility located in Osceola County. O&S serves approximately 2,186 residential customers, 29 commercial customers, and 858 irrigation customers. The Utility's service area is located in the South Florida Water Management District. According to the Utility's 2009 Annual Report, O&S reported annual operating revenues of \$1,205,487 and net operating income of \$56,008. The Utility's rate base was last established for the 12-month period ended June 30, 1991 by our approval of the transfer of majority organizational control of O&S.<sup>1</sup>

The Utility's 2009 Annual Report was received on April 26, 2010. Our preliminary analysis indicates that O&S's achieved return on equity (ROE) is 19.33 percent, which is in excess of the top of its authorized range of ROE.

This Order addresses opening a formal overearnings investigation of the Utility and holding revenues subject to refund under an appropriate security. We have jurisdiction pursuant to Sections 367.081 and 367.082, Florida Statutes (F.S).

Additionally, at the October 12, 2010, Agenda Conference, we voted to deny O&S's requested payment plan for delinquent regulatory assessment fees (RAFs) of \$127,789 in Docket No. 090322-WU.

<sup>1</sup> See Order No. PSC-92-0204-FOF-WU, issued April 14, 1992, in Docket No. 910895-WU, In re: Application for transfer of majority organizational control of C & S Water Company's Certificate No. 510-W in Osceola County from Doug Stewart and the Estate of Jack Chernau to Douglas B. Stewart.

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**Analysis and Decision**

The Utility's 2009 Annual Report was received on April 26, 2010. Our preliminary analysis indicates that O&S's achieved ROE is 19.33 percent, which is in excess of the top of its authorized range of ROE. The Utility's last authorized ROE was set at 11.51 percent in its last case.<sup>2</sup> However, as stated in the background, O&S was transferred in 1991.<sup>3</sup> Consistent with Commission practice, the approved ROE does not survive a transfer.<sup>4</sup> Pursuant to Sections 367.081(4)(f) and 367.082(5)(b)3, F.S., we used the current leverage formula to determine the appropriate ROE for purposes of deciding whether to initiate an investigation of possible overearnings. Based on our current leverage formula,<sup>5</sup> the calculated ROE is 10.85 percent with a range of plus or minus 100 basis points.

As stated above, we believe that O&S may be overearning. Pursuant to Section 367.082(5)(b)(1), F.S., the achieved rate of return for interim purposes shall be calculated by applying appropriate adjustments consistent with those used in the Utility's most recent rate proceeding. The last rate proceeding for O&S was a staff-assisted rate case as memorialized in Order No. 20583.<sup>6</sup> Based on our review of that Order, we find that no consistency adjustments are necessary for interim purposes. The attached accounting schedules illustrate our approved rate base, capital structure, and test year operating income as shown on Schedule Nos. 1, 2, and 3, respectively.

Pursuant to Rule 25-30.433, Florida Administrative Code (F.A.C.), the averaging method used to calculate rate base and the cost of capital for Class A utilities is the 13-month average. The Utility's 2009 Annual Report only reflects O&S's year-end financial data. As such, we used the simple average of 2008 and 2009. Rate base for interim purposes is \$645,223.

Consistent with Section 367.082(5)(b), F.S., the required rate of return shall be calculated using the last authorized rate of ROE and the test year cost rates of other sources of capital. As discussed above, O&S was transferred in 1991. Consistent with Commission practice, the ROE does not survive a transfer. Based on our current leverage formula and an equity ratio of 1.55 percent, the calculated ROE is 10.85 percent with a range of plus or minus 100 basis points in accordance with Sections 367.081(4)(f) and 367.082(5)(b)3, F.S.

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<sup>2</sup> See Order No. 20583, issued January 10, 1989, in Docket No. 870392-WU, In re: Application of C&S Water Company for an original water certificate in Osceola County, Florida.

<sup>3</sup> See Order No. PSC-92-0204-FOF-WU.

<sup>4</sup> See Order Nos. PSC-07-0325- FOF-WS, issued April 16, 2007, in Docket No. 060368-WS, In re: Application for increase in water and wastewater rates in Alachua, Brevard, Highlands, Lake, Lee, Marion, Orange, Palm Beach, Pasco, Polk, Putnam, Seminole, Sumter, Volusia, and Washington Counties by Aqua Utilities Florida, Inc., PSC-06-0925-PCO-WS, issued November 6, 2006, in Docket No. 060246-WS, In re: Application for increase in water and wastewater rates in Polk County by Gold Coast Utility Corp., and PSC-06-0675-PCO-SU, issued August 7, 2006, in Docket No. 060255-SU, In re: Application for increase in wastewater rates in Pinellas County by Tierra Verde Utilities, Inc.

<sup>5</sup> See Order Nos. PSC-10-0401-PAA-WS, issued June 18, 2010, and PSC-10-0446-CO-WS, issued July 13, 2010, in Docket No. 100006-WS, In re: Water and wastewater industry annual reestablishment of authorized range of return on common equity for water and wastewater utilities pursuant to Section 367.081(4)(f), F.S.

<sup>6</sup> Issued December 10, 1990, in Docket No. 900238-WU, In re: Application for staff-assisted rate case in Pasco County by C.S. Water Company, Inc.

Pursuant to Section 368.082(2)(b), F.S., in a proceeding for an interim decrease in rates, we shall authorize the continued collection of the previously authorized rates; however, revenues collected under those rates sufficient to reduce the achieved rate of return to the maximum of the rate of return calculated in accordance with subsection (5) shall be attached and held subject to refund. In accordance with Section 368.082(2)(b), F.S., the appropriate ROE for interim purposes is 11.85 percent. Based on our approved rate base, cost of capital, and net operating income, the following amount shall be held subject to refund:

	<u>Adjusted Test Year Revenues</u>	<u>\$ Decrease</u>	<u>Subject to Refund</u>
Water	\$1,205,487	(\$76,352)	6.33%

Pursuant to Section 367.082(2)(b), F.S., in the case of an interim decrease, the utility shall be authorized to continue collecting its previously authorized rates provided that the attached revenues held subject to refund are secured. The amount held subject to refund with interest shall be placed under bond, escrow, letter of credit or corporate undertaking pending our final action in this docket. As stated above, the amount of potential overearnings is \$76,352. Assuming an 8-month time frame, the potential refund amount is \$50,901. The interest component is \$60, bringing the total to \$50,961 that shall be held subject to refund with interest.

As stated in the background, at the October 12, 2010 Agenda Conference, we approved staff's recommendation in Docket No. 090322-WU to deny O&S' requested payment plan for delinquent RAFs of \$127,789. Normally, a utility may be provided an opportunity to use a corporate undertaking to secure funds held subject to refund. In this case, however, because the amount of delinquent RAFs is more than double the recommend security amount, the Utility shall be required to open an escrow account or file 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, said account shall be established between the Utility and an independent financial institution pursuant to a written escrow agreement. The Commission shall be a party to the written escrow agreement and a signatory to the escrow account. The written escrow agreement shall state the following: that the account is established at the direction of the Commission for the purpose set forth above; that 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.

The Utility shall deposit \$6,363 into the escrow account each month for possible refund. The escrow agreement shall also state that if a refund to the customers is 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 shall be in the amount of \$50,961. If the Utility chooses a surety bond as security, the surety bond shall 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 shall 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 shall keep an accurate and detailed account of all monies it receives. By no later than the twentieth (20th) day of each month, the Utility shall file a report showing the amount of revenues collected each month subject to refund. Should a refund be required, the refund shall be with interest and undertaken in accordance with Rule 25-30.360, F.A.C. In no instance shall maintenance and administrative costs associated with any refund be borne by the customers. These costs are the responsibility of, and shall be borne by, the Utility.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that an overearnings investigation of O&S Water Company, Inc. shall be initiated. It is further

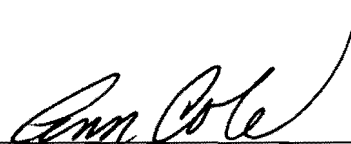
ORDERED that in the interim, O&S Water Company, Inc. shall be authorized to continue collecting its previously authorized rates; however, \$50,961 shall be attached and held subject to refund. It is further

ORDERED that O&S Water Company, Inc. shall be required to open an escrow account or file a surety bond or letter of credit as specified herein to guarantee any potential refund of revenues collected under interim conditions. It is further

ORDERED that this docket shall remain open pending our investigation of O&S Water Company, Inc.'s earnings for 2009.

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By ORDER of the Florida Public Service Commission this 1st day of November, 2010.



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ANN COLE  
Commission Clerk

(SEAL)

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

Any party adversely affected by the Commission's decision to initiate an investigation into overearnings in this matter, which is final action, may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Office of Commission Clerk, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water and/or wastewater utility by filing a notice of appeal with the Office of Commission Clerk, and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

For the decision making revenues subject to refund, which is preliminary, procedural or intermediate in nature, any party adversely affected by this order may do (1) and (2) in the paragraph above. However, judicial review of a preliminary, procedural or intermediate ruling or order is available only if review of the final action will not provide an adequate remedy. Such review may be requested from the appropriate court, as described above, pursuant to Rule 9.100, Florida Rules of Appellate Procedure.

<b>O&amp;S Water Company, Inc</b>						<b>Schedule No. 1</b>
<b>Schedule of Water Rate Base</b>						
<b>Year Ended 12/31/09</b>						
<b>Description</b>	<b>Test Year Per Utility</b>	<b>Utility Adjust- ments</b>	<b>Adjusted Test Year Per Utility</b>	<b>Commission Adjust- ments</b>	<b>Commission Adjusted Test Year</b>	
1 Plant in Service	\$6,211,597	\$0	\$6,211,597	\$0	\$6,211,597	
2 Land and Land Rights	2,100	0	2,100	0	2,100	
3 Non-used and Useful Components	0	0	0	0	0	
4 Accumulated Depreciation	(926,670)	0	(926,670)	0	(926,670)	
5 CIAC	(5,446,330)	0	(5,446,330)	0	(5,446,330)	
6 Amortization of CIAC	684,214	0	684,214	0	684,214	
7 Working Capital Allowance	<u>120,312</u>	<u>0</u>	<u>120,312</u>	<u>0</u>	<u>120,312</u>	
8 <b>Rate Base</b>	<u>\$645,223</u>	<u>\$0</u>	<u>\$645,223</u>	<u>\$0</u>	<u>\$645,223</u>	

O&S Water Company, Inc							Schedule No. 2		
Capital Structure-Simple Average									
Year Ended 12/31/09									
Description	Total Capital	Specific Adjustments	Subtotal Adjusted Capital	Prorata Adjustments	Capital Reconciled to Rate Base	Ratio	Cost Rate	Weighted Cost	
<b>Per Utility</b>									
1 Long-term Debt	\$493,874	\$0	\$493,874	(\$346,408)	\$147,465	22.85%	7.63%	1.74%	
2 Short-term Debt	1,667,033	0	1,667,033	(1,169,275)	497,758	77.15%	8.14%	6.28%	
3 Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%	
4 Common Equity	(2,222,857)	2,222,857	0	0	0	0.00%	11.85%	0.00%	
5 Customer Deposits	0	0	0	0	0	0.00%	6.00%	0.00%	
6 Deferred Income Taxes	0	0	0	0	0	0.00%	0.00%	0.00%	
7 <b>Total Capital</b>	<u>(\$61,951)</u>	<u>\$2,222,857</u>	<u>\$2,160,907</u>	<u>(\$1,515,683)</u>	<u>\$645,224</u>	<u>100.00%</u>		<u>8.03%</u>	
<b>Per Commission</b>									
8 Long-term Debt	\$493,874	\$0	\$493,874	(\$346,408)	\$147,465	22.85%	7.63%	1.74%	
9 Short-term Debt	1,667,033	0	1,667,033	(1,169,275)	497,758	77.15%	8.14%	6.28%	
10 Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%	
11 Common Equity	(2,222,857)	2,222,857	0	0	0	0.00%	11.85%	0.00%	
12 Customer Deposits	0	0	0	0	0	0.00%	6.00%	0.00%	
13 Deferred Income Taxes	0	0	0	0	0	0.00%	0.00%	0.00%	
14 <b>Total Capital</b>	<u>(\$61,951)</u>	<u>\$2,222,857</u>	<u>\$2,160,907</u>	<u>(\$1,515,683)</u>	<u>\$645,224</u>	<u>100.00%</u>		<u>8.03%</u>	
						<b>LOW</b>	<b>HIGH</b>		
RETURN ON EQUITY						<u>9.85%</u>	<u>11.85%</u>		
OVERALL RATE OF RETURN						<u>8.03%</u>	<u>8.03%</u>		



O&S Water Company, Inc. Statement of Water Operations Year Ended 12/31/09							Schedule No. 3	
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Commission Adjust- ments	Commission Adjusted Test Year	Revenue Increase	Revenue Requirement	
1 <b>Operating Revenues:</b>	<u>\$1,205,487</u>	<u>\$0</u>	<u>\$1,205,487</u>	<u>\$0</u>	<u>\$1,205,487</u>	<u>(\$76,352)</u> -6.33%	<u>\$1,129,135</u>	
<b>Operating Expenses</b>								
2 Operation & Maintenance	\$908,087	\$0	\$908,087	\$0	\$908,087		\$908,087	
3 Depreciation	175,165	0	175,165	0	175,165		16,284	
4 Amortization	(158,881)	0	(158,881)	0	(158,881)		0	
5 Taxes Other Than Income	156,419	0	156,419	0	156,419	(3,436)	152,983	
6 Income Taxes	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	
7 <b>Total Operating Expense</b>	<u>\$1,080,790</u>	<u>\$0</u>	<u>\$1,080,790</u>	<u>\$0</u>	<u>\$1,080,790</u>	<u>(\$3,436)</u>	<u>\$1,077,354</u>	
8 <b>Operating Income</b>	<u>\$124,697</u>	<u>\$0</u>	<u>\$124,697</u>	<u>\$0</u>	<u>\$124,697</u>	<u>(\$72,917)</u>	<u>\$51,780</u>	
9 <b>Rate Base</b>	<u>\$645,223</u>		<u>\$645,223</u>		<u>\$645,223</u>		<u>\$645,223</u>	
10 <b>Rate of Return</b>	<u>19.33%</u>		<u>19.33%</u>		<u>19.33%</u>		<u>8.03%</u>	