

FLORIDA PUBLIC SERVICE COMMISSION
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SEPTEMBER 11, 1997

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TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING *SB* *Records/Reporting*

FROM: DIVISION OF WATER & WASTEWATER *SM* *RWH* *Moniz* *Galloway* *Lingo*
MUNRO *M*
DIVISION OF LEGAL SERVICES (GERVASI) *MS* *AS*

RE: DOCKET NO. ~~970164~~-WU - THE HOBE SOUND WATER COMPANY -
APPLICATION FOR RATE INCREASE
COUNTY: MARTIN

AGENDA: SEPTEMBER 23, 1997 - REGULAR AGENDA - PROPOSED AGENCY
ACTION - INTERESTED PARTIES MAY PARTICIPATE

CRITICAL DATES: 5 MONTH EFFECTIVE DATE: OCTOBER 2, 1997

SPECIAL INSTRUCTIONS: I:\PSC\WAW\WP\970164WU.RCM

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FPSC-RECORDS/REPORTING

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CASE BACKGROUND

Hobe Sound Water Company (Hobe Sound or utility) is a Class A utility located in Martin County that provides water service only to approximately 1,268 customers. The service area includes customers both in Hobe Sound and on Jupiter Island. The South Florida Water Management District (SFWMD) has determined this area to be a critical water usage area. The water company is a wholly-owned subsidiary of the Hobe Sound Water Company operating under the provisions of Certificate No. WU-43.

The utility's last full rate case proceeding was in Docket No. 940475-WU. By Order No. PSC-94-1452-FOF-WU, issued December 20, 1994, the Commission approved the utility's current rate structure. This current structure is unique in that it is a three-tiered increasing block rate, which was designed to encourage conservation in an area where usage per capita is extremely high.

After Hobe Sound's 1994 rate increase, salt water intruded into the well field east of Highway US-1. Despite the utility's monitor system, there was no advanced warning of this occurrence. The loss of supply wells resulted in a critical supply problem. Hobe Sound's response to this problem was to institute an emergency interconnect with Hydratech Utilities, Inc. (Hydratech), as well as an accelerated supply program on the west side of Highway US-1.

On June 19, 1995, the utility and SFWMD entered into a Consent Agreement whereby the utility agreed to accomplish the following: (1) improve ground water monitoring; (2) incorporate operation restraints when any salt water intrusion is detected; (3) investigate interconnect options; and (4) pay civil penalties. On September 11, 1995, Hobe Sound signed a Consent Agreement with the Florida Department of Environmental Protection (DEP) whereby Hobe Sound agreed to correct alleged violations of maximum contaminant levels established for iron and manganese in drinking water.

On February 16, 1996, in Docket No. 960192-WU, Hobe Sound filed for a limited proceeding as the most cost efficient method to recover expenses and increased costs as agreed to in the Consent Agreement. In addition to the supply wells and interconnect with Hydratech, the costs of developing and implementing the Consent Agreement with SFWMD, and an improved ground water program including new monitor wells were also included in that filing.

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Pursuant to Order No. PSC-96-0870-FOF-WU, issued July 2, 1996, the Commission allowed the utility to recover the above described costs.

On April 3, 1997, the utility filed this current application for increased water rates pursuant to Chapters 367.081 and 367.082, Florida Statutes, and Rule 25-30.436, Florida Administrative Code. The utility has indicated in its filing that the requested rate increase is driven by the costs of installing a new iron manganese removal filtration facility as required by DEP. The utility satisfied the Minimum Filing Requirements (MFRs) for a rate increase, on May 2, 1997, and that date was designated as the official filing date pursuant to Section 367.083, Florida Statutes. The utility has requested that this case be processed pursuant to the proposed agency action (PAA) procedure as provided for in Section 367.081(8), Florida Statutes.

In its application, the utility requested an interim test year ending June 30, 1997. In its MFRS, Hobe Sound provided interim schedules based upon the historical period ended June 30, 1996, which did not agree with the test year stated in the application. By Order No. PSC-97-0839-FOF-WU, issued July 5, 1997, the Commission suspended the utility's requested rate increase and approved an interim water rate increase based on the historical test year ended June 30, 1996. Annual revenues of \$1,417,647 were approved, resulting in an increase of \$286,680 or 25.35%. The annualized revenues based on the limited proceeding rates which went into effect after the interim test year, as approved by Order No. PSC-96-0870-FOF-WU, were then compared with the Commission approved interim revenues. This resulted in a revenue increase of less than 1% or \$5,870 over current rates approved in the limited proceeding. The utility decided not to implement the approved interim rate increase because of the nominal impact.

Hobe Sound's requested test period for final rates is the projected 13-month average test year ending June 30, 1998. The utility has requested final water revenues of \$2,099,115. This results in an annual increase of \$424,226 or 25.33%.

An informal customer meeting was held on June 25, 1997, in Hobe Sound, Florida. Approximately twenty customers were in attendance. The main customer concerns were the conditions caused by the high levels of iron in the water which the filtration system will alleviate when it comes on line in late August to early September of 1997.

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DISCUSSION OF ISSUES

QUALITY OF SERVICE

ISSUE 1: Is the quality of service satisfactory?

RECOMMENDATION: Yes, the quality of service is satisfactory.
(MUNROE)

STAFF ANALYSIS: In accordance with Rule 25-30.433(1), Florida Administrative Code, in order to determine the overall quality of service provided by a utility, the Commission is to evaluate three separate components of water and wastewater operations. These are (1) the quality of the utility's product, (2) the operating conditions of the utility's plant and facilities, and (3) customer satisfaction. The rule also states that sanitary surveys, outstanding citations, violations, and consent orders on file with the DEP and the County Health Department over the preceding three year period shall be considered. DEP and Health Department officials' input as well as customer comments shall also be considered.

Hobe Sound's facilities consist of a well field with eight wells, two storage tanks, and a treatment plant. Current treatments consist of aeration and chlorination to which an iron and manganese filtration system is currently being added.

Quality of the Product

A customer meeting was held on June 25, 1997 in the Parish Hall of St. Christopher's Church in Hobe Sound. Twenty customers were in attendance. As stated in the case background, the main customer concerns were the conditions caused by the high levels of iron in the water which the filtration system will alleviate when it comes on line in late August to early September of 1997.

Although the iron levels have exceeded those allowable by DEP, a Consent Agreement (OGC Case No. 95-1586) was signed. Under the terms of the Consent Agreement, the company initiated a project to install filters which will reduce the iron levels.

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Operating Conditions

The staff engineer conducted a field inspection of the Hobe Sound facilities including the iron filtration project site on July 24-25, 1997. The company facilities were found to be clean and in good working condition. Although slightly behind schedule due to a permitting delay, the iron filtration project was found to be well organized and proceeding according to the plans.

Customer Satisfaction

At the customer meeting the majority of concerns centered around problems resulting from the excessive iron levels in the water. When completed, the filtration system will alleviate these problems. Staff would add that the company was well represented at the meeting and made special efforts to address customer concerns and problems at the conclusion of the meeting.

As a result of these findings, staff recommends the quality of service is satisfactory.

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RATE BASE

ISSUE 2: Should an adjustment be made to increase plant in service for items that were expensed but should have been capitalized?

RECOMMENDATION: Yes, based on the 13-month average balances, adjustments should be made to increase plant in service and accumulated depreciation by \$10,549 and \$1,001, respectively. Adjustments should also be made to increase test year depreciation and operation and maintenance expenses by \$468 and \$9,929, respectively. (MONIZ)

STAFF ANALYSIS: In Audit Exception No. 1, the staff auditor stated that the utility booked several items to operation and maintenance (O&M) expenses that should have been capitalized. In its response, the utility recognized that the \$6,585 related to the preliminary engineering work for the new catalytic filtration facility and the \$2,071 in engineering fees related to a new well should have been capitalized. The utility also agreed that the \$795 saw should have been capitalized. The above amounts were included in the utility's June 30, 1996 test year expenses. However, the utility escalated these amounts by 1.0252% for its June 30, 1997 intermediate year and its June 30, 1998, projected test year. Consequently, the amounts included in the MFRs for the June 30, 1998, are greater than the June 30, 1996, amounts presented above. The amounts included for the projected test year are as follows: \$2,176 in engineering fees related to the well, \$6,921 in engineering costs related to the catalytic filtration facility and \$832 for the saw.

Staff agrees with the utility and the auditor that the above items should be capitalized. Further, staff has discussed the utility's capitalization policy with the utility manager. He agreed that the utility mistakenly expensed the items listed above, since it is the utility's policy to capitalize items with a service life longer than a year and a cost basis greater than \$500.

Based on the above, and the 13-month average plant balances adjustments should be made to increase plant in service and accumulated depreciation by \$7,684 and \$703, respectively. Test year depreciation should be increased by \$350 and O&M expenses should be decreased by \$6,921, for fees related to the filtration facility. The increase to plant in service is greater than the O&M expense reduction, because staff applied an Allowance for Funds Used During Construction (AFUDC) to the original amount. The costs

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were incurred in November and December of 1996 and the facility was not added to plant in service until June 1996. Therefore, the utility is entitled to accrue AFUDC on the costs during the construction period.

Staff is also recommending adjustments to increase plant in service by \$2,070, and \$795, to increase accumulated depreciation by \$178 and \$120, to increase depreciation expense by \$69 and \$50 and to decrease O&M expenses by \$2,176 and \$832 for costs related to constructing the well and for the costs related to the purchase of the saw, respectively.

Accordingly, staff recommends that based on the 13-month average balances, adjustments should be made to increase plant in service and accumulated depreciation by \$10,549 and \$1,001, respectively. Adjustments should also be made to increase test year depreciation and operation and maintenance expenses by \$468 and \$9,929, respectively.

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ISSUE 3: What are the appropriate used and useful percentages for the distribution system, water plant, and new filtration system?

RECOMMENDATION: The distribution system and plant are 100% used and useful, and the filtration system is also determined to be 100%. (MUNROE)

STAFF ANALYSIS: Both the distribution system and plant were found to be 100% used and useful in the utility's last rate case. See Order PSC-94-1452-FOF-WU. The utility's capacities have not changed since that time. Therefore, the percentages remain at 100% for both the distribution system and water plant.

The maximum flow capacity of the filtration system is 5.990 MGD, and the maximum daily demand is 5.601 MGD. A comparison of these flow rates yields a 93.51% used and useful.

$$5.601 \text{ MGD} / 5.99 \text{ MGD} \times 100\% = 93.51\%$$

Since this is a modular type system with three filter tanks, a smaller two-tank system would not have provided adequate flow capacity. Therefore, staff recommends 100% used and useful for the newly constructed filtration system along with the distribution system and water plant.

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ISSUE 4: What is the appropriate allowance for working capital?

RECOMMENDATION: Using the balance sheet approach in accordance with Rule 25-30.433(2), Florida Administrative Code, working capital in the amount of \$256,261 should be approved. (MON12)

STAFF ANALYSIS: As prescribed by Rule 25-30.433 (2), Florida Administrative Code, Class A Utilities must use the balance sheet method to compute working capital. Using this methodology and a 13-month average, Hobe Sound requested \$301,124 as a working capital allowance.

Staff has reviewed the utility's balance sheet and its calculation of working capital. We believe that several adjustments are necessary to the utility's requested amounts.

CASH

The utility included a 13-month average cash balance of \$150,281 in its working capital calculation. According to the utility, \$7,300 of this amount is being held in an interest-bearing account. Generally, interest-bearing funds are excluded from working capital. See, e.g., Order No. 11498, issued January 11, 1983, in Docket No. 820150, wherein the Commission excluded Gulf Power's temporary cash investments from working capital to prevent subsidization of the company by the ratepayers. Based on the above, staff has removed \$7,300 in interest bearing funds from the working capital calculation.

LOAN ISSUANCE COSTS

The utility included \$5,646 in unamortized loan issuance costs in its working capital calculation. The debt associated with the issuance costs has been refinanced and is no longer on the utility's books. Past Commission practice has been to amortize the issuance costs over the life of the loan and incorporate the amortization in the cost of long-term debt. However, this is impossible to do in this case, as the loan no longer exists. Therefore, staff recommends removing the \$5,646 from the working capital calculation.

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OTHER DEFERRED DEBITS

As explained in Issue 12, staff is recommending and the utility agrees that the costs to repair the utility's generator be amortized over five years and the deferred balance should be included in working capital. Therefore, the unamortized 13-month average balance of \$5,560 should be included in the working capital calculation.

DEFERRED RATE CASE EXPENSE

Consistent with Commission practice, the provision for deferred rate case costs should reflect the 13-month average unamortized balance for the test year. As discussed in Issue 12, staff is recommending approval of a \$94,328 provision for current rate case charges. Therefore, beginning with July 1, 1997, the average unamortized balance of current rate case expense, to be considered in the working capital calculation is \$84,727. The remaining unamortized balance for the most recent rate case and limited proceeding is \$39,719. This results in a \$29,295 reduction to the utility's requested amount of \$153,742.

MISC. CURRENT & ACCRUED LIABILITIES

In discussions with the utility's accounting consultant, staff discovered that the utility failed to include \$8,182 in accrued pension costs in its projected balance sheet. Consequently, this amount was left out of its working capital calculation. Staff has reviewed this amount and believes it to be reasonable. Based on the above, we recommend increasing accrued liabilities by \$8,182.

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SUMMARY

After applying the adjustments addressed above, staff's adjusted working capital is \$256,261. This reduces the utility's requested amount by \$44,863. Staff's adjustments are shown on the following schedule.

| | | |
|---|----------------|-------------------|
| Working Capital Balance - Per Utility | | \$301,124 |
| Staff Adjustments | | |
| (1) Cash | \$ (7,300) | |
| (2) Other Misc Deferred Debits | | |
| Issuance Costs | (5,646) | |
| Unamortized Generator Costs | 5,560 | |
| (3) Deferred Rate Case Exp. | (29,295) | |
| (4) Misc Current & Accrued Liab. | <u>(8,182)</u> | |
| Net Decrease Per Staff | | <u>(\$44,863)</u> |
| Staff's Recommended Working Capital Allowance | | <u>\$256,261</u> |

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ISSUE 5: What is the appropriate rate base amount?

RECOMMENDATION: The appropriate rate base for Hobe Sound is \$6,179,676. (MONIZ)

STAFF ANALYSIS: Based on the staff's recommended adjustments and the use of a thirteen-month average, rate base is \$6,179,676. The rate base schedule is attached as Schedule No. 1-A. The schedule of adjustments to rate base is attached as Schedule No. 1-B.

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COST OF CAPITAL

ISSUE 6: What is the appropriate rate of return on equity?

RECOMMENDATION: Using the current leverage formula, the rate of return on equity should be 10.46%, with a range of 9.46% to 11.46%. (MONIZ)

STAFF ANALYSIS: Based upon the components of staff's adjusted capital structure, as shown on Schedule No. 2, the equity ratio for Hobe Sound is 29.05%. Using the current leverage formula approved by Order No. PSC-97-0660-FOF-WS, issued June 10, 1997, in Docket No. 970006-WS, the appropriate return on equity should be 10.46%. The appropriate range for the return on equity should be 9.46% to 11.46%.

ISSUE 7: What is the appropriate overall cost of capital?

RECOMMENDATION: The appropriate overall cost of capital should be 8.74%, with a range of 8.46% to 9.02%. (MONIZ)

STAFF ANALYSIS: The staff's recommended overall rate of return is based on application of Commission practice and is derived as shown in Schedule No. 2. Based upon the recommended adjustments in previous issues, staff recommends an overall cost of capital of 8.74%, with a range of 8.46% to 9.02%.

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NET OPERATING INCOME

ISSUE 8: Should an adjustment be made to reduce test year salaries and employee benefits?

RECOMMENDATION: Yes, test year salaries should be reduced by \$10,441. Corresponding reductions should also be made to reduce employee benefits and payroll taxes in the amounts of \$1,928 and \$892, respectively. (MONIZ)

STAFF ANALYSIS: In its MFRs, for the 1998 projected test year, the utility included \$22,952 in salary expense for Ms. Janet Brown. According to the staff audit workpapers, Ms. Brown acts as secretary to Mr. Nathaniel A. Reed, president of Hobe Sound Water Company and Land Company. By Order No. PSC-94-1452-FOF-WU, issued in the utility's last rate case, the Commission disallowed the salary expense for the secretary. According to that order, the secretary performed only personal duties for the president, none of which were utility-related. Further, normal secretarial duties for the utility were performed by the utility bookkeeper and the utility did not provide an estimate of hours or even a percentage of how much of the secretary's time was spent on utility-related work. The Commission found that since Mr. Reed spent most of his time on non-utility matters, the same would be true for his secretary and all related expenses were removed. At the time, her total salary was \$17,472, of which the entire amount was disallowed as were the related payroll taxes and employee benefits.

The MFRs in this docket reflect \$22,952 in annual salary expense for Ms. Brown, \$4,235 in benefits and \$1,962 in payroll taxes, for the test year ending June 30, 1998. Ms. Brown works part-time for the utility and receives one half of her annual salary from the water company. Audit Exception No. 5, of the staff audit report, discloses that according to Order No. PSC-94-1452-FOF-WU, the salary for the utility's executive secretary was disallowed. The auditor suggests that the secretary's salary should be removed in this case, since it was disallowed in the utility's last rate case.

In its response to the audit, the utility contends that although the Commission has disallowed Janet Brown's salary in the past, her position has changed as a result of the corporate restructuring. Due to the utility operating as a stand-alone entity following corporate restructuring, there no longer exists an

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opportunity for the utility to share employees with its former parent company. Further, Ms. Brown now acts as a utility officer as well as a secretary to Mr. Reed. She provides the utility president with administrative assistance in performing his vast range of utility policy and management functions and also provides the only "coverage" the utility has for secretarial and clerical duties which cannot always be handled by the office manager. The other half of her annual compensation, which is not paid by the utility, is for the time devoted to the President's other, outside business activities.

Staff believes that the utility has justified a need for someone to act in the absence of the office manager and to perform secretarial duties. However, we do not believe the utility has justified the amount of salary it has included for the secretary. The office manager is a full time employee and only receives \$25,040 in annual compensation (or \$12.03 per hour) for 2080 hours per year, while the secretary is part-time and receives \$22,952 in annual compensation (or \$22.07 per hour) for 1040 hours per year. Staff believes that since the secretary is part-time, her salary should be representative of a part-time secretary's salary. Since time sheets are not kept for the utility's office personnel, the exact amount of time the secretary spends on utility related matters cannot be determined. However, we do believe that it is reasonable for a utility of this size to have a half-time secretary in addition to the office manager. Further, staff believes that since the secretary is essentially assisting the office manager, it would be inappropriate to allow an hourly wage for the secretary greater than the hourly wage allowed for the office manager. We believe it would be more appropriate to allow an hourly rate equal to the office manager's hourly rate.

Based on the above, we recommend allowing an annual salary of \$12,511 ($\12.03×1040 hours) for the secretary. Accordingly, salary expense should be reduced by \$10,441. Corresponding adjustments should also be made to reduce payroll taxes and employee benefits by \$1,928 and \$892, respectively.

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ISSUE 9: Should an adjustment be made to disallow the utility's projected maintenance expenses for the new catalytic filtration facility?

RECOMMENDATION: Yes. Materials and supplies should be reduced by \$4,100 for the disallowance of projected maintenance expenses. (MONIZ)

STAFF ANALYSIS: In its MFRs, the utility included projected maintenance expenses for its new catalytic filtration facilities for the test year ending June 30, 1998. Included in the estimate is \$2,050 for the replacement of the media which is contained inside the filter and \$2,050 for painting the filter.

In Audit Disclosure No. 1, of the staff audit report, the auditor notes that the media replacement and filter painting will not occur for ten years. It is the opinion of the auditor that these costs should be removed since the utility will likely experience another rate proceeding within this time frame and the expenses may be captured at that time.

The catalytic filtration facility's annual cost projection, prepared by the engineering firm of Bishop & Associates, contained \$13,000 for a system operator. The utility states that it took a conservative approach when it established its annual proforma expenses associated with the operation of the filtration facility, since it did not include the costs for the facility operator. Staff has since discovered that the utility does not intend to hire anyone to fill this position. The facility will be operated by Mr. Talley, who is already a full time employee of the utility and his salary is already included in test year expenses. Therefore, staff does not believe this cost should be considered since the utility will not hire anyone to fill this position.

Based on the above, staff does not believe the utility has justified the costs it included for the filter painting and media replacement or the additional operator. Therefore, we recommend reducing test year Materials and Supplies by \$4,100.

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ISSUE 10: Should purchased power be reduced for out-of-period charges?

RECOMMENDATION: Yes. Purchased Power should be reduced by \$3,294.
(MONIZ)

STAFF ANALYSIS: Audit Exception No. 7 reported that the utility's historical test year included thirteen months of purchased power payments (June 1, 1995 through June 30, 1996). The auditor asserts that the June 1, 1995 payment of \$3,294 should be removed since it is not part of the test period.

In its response to the audit, the utility had no objection to removing the \$3,294 from its test year expenses. Based on the above and the fact that out-of-period charges should not be included in test year expenses, staff recommends reducing purchased power by \$3,294.

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ISSUE 11: Should an adjustment be made to reduce equipment rental for computer related expenses?

RECOMMENDATION: Yes. Equipment rental should be reduced by \$2,400. (MONIZ)

STAFF ANALYSIS: During the audit investigation, the staff auditors discovered that the utility failed to remove \$2,400 in computer rental charges that were previously allocated from the parent company. The auditor also reported the utility did not provide support for this amount.

In its response, the utility reported that the \$2,400 was an equipment sharing charge from its parent company prior to the reorganization. The utility contends that this amount was not removed because its new office arrangement, following the corporate restructuring, might require the rental of non-computer related equipment.

Staff does not agree with the utility's rationalization on why the \$2,400 should remain in test year expenses. We believe that since the utility no longer has a parent and the costs are no longer being incurred, they should be removed. Accordingly, staff recommends reducing equipment rental expenses by \$2,400.

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ISSUE 12: What is the appropriate amount of rate case expense?

RECOMMENDATION: The appropriate amount of current rate case expense should be \$98,327, amortized over four years for an annual amortization amount of \$24,582. The appropriate amount of prior rate case expense to include in test year expenses is \$29,263. Total current and prior rate case expense amount of \$53,845 should be included in test year expenses. This is a net increase of \$7,038 to the utility's total amortization. (MONIZ)

STAFF ANALYSIS: In its original filing, Hobe Sound estimated rate case expense to be \$131,084 for this proceeding. The breakdown is shown below.

| | |
|--|------------------|
| Guastella & Associates (Engineering & Accounting Fees) | \$95,000 |
| Holland & Knight (Legal Fees) | 30,000 |
| Mark Veil (Tax Schedules) | 2,000 |
| Printing & Postage (MFRs & Customer Notification) | 2,084 |
| Florida Public Service Commission (Filing fee) | <u>2,000</u> |
| TOTAL | <u>\$131,084</u> |

In addition to the rate case expense for this proceeding, Hobe Sound included unamortized expenses in the amount of \$56,145 associated with two prior rate proceedings: Dockets Nos. 940475-WU and 940475-WU. In total, Hobe Sound requested rate case expense of \$187,229 to be amortized over four years for an annual expense of \$46,807.

On August 19, 1997, the utility submitted its update of current rate case expense, with supporting documentation and an estimate to complete the PAA proceeding. The utility's current rate case expense and estimate to complete the PAA proceeding produced a revised rate case expense of \$103,405. In our review, staff found several areas where adjustments are necessary.

LEGAL

Staff has reviewed the requested amount of legal fees incurred in connection with this rate case. According to the utility, only \$19,739 was actually incurred and remaining to process the case through PAA. Staff's analysis determined that the revised request for legal fees appear to be prudent and reasonable; therefore, we recommend that \$19,739 be approved for legal fees. This is a \$10,264 reduction to the utility's original request.

ENGINEERING & ACCOUNTING

In the utility's rate case analysis in its MFRs, the engineering and accounting fees were combined. In its revised request, the utility separated these charges. The breakdown is shown below.

| GUASTELLA ASSOCIATES, INC. | | | | |
|----------------------------|-----------------|-----------------|----------------------|-------------------|
| Description | Avg Hourly Rate | Amount Billed | Estimate to Complete | Total By Category |
| Engineering | \$197 | \$28,158 | \$4,800 | 32,958 |
| Accounting | \$107 | 38,237 | 2,640 | 40,877 |
| Travel | | 2,549 | 1,450 | 3,999 |
| Support Staff | | 3,216 | 152 | 3,368 |
| Fed Ex. & Other | | <u>278</u> | <u>50</u> | <u>328</u> |
| Total | | <u>\$72,438</u> | <u>\$9,092</u> | <u>\$81,530</u> |

Engineering: Mr. Guastella, the principal engineer hired by the utility to work on the rate case, billed the utility \$28,158 for his services through July 31, 1997. He estimated his additional charges to be \$4,800 to complete the rate case, through the PAA process. Mr. Guastella charged the utility for 167 hours at an average hourly rate of \$197 an hour. Staff reviewed several past rate proceedings in an attempt to determine what hourly rates have been allowed by the Commission. From our review, staff found that the Commission in water and wastewater cases, generally has accepted hourly rates for engineers ranging from \$75 to \$140 an hour. Based on this review, we believe that Mr. Guastella's hourly rate is excessive.

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While staff believes that Hobe Sound's decision to retain Mr. Guastella for his expertise is reasonable, it does not automatically follow that the customers should have to bear the full costs for his services. The Commission enjoys a broad discretion with respect to allowance of rate case expense. Florida Crown Util. Servs., Inc. v. Utility Regulatory Bd. of Jacksonville, 274 So. 2d 597, 598 (Fla. 1st DCA 1973). Nevertheless, it would constitute an abuse of discretion for the Commission to automatically award rate case expense without reference to the prudence of the costs incurred in the rate case proceedings. Meadowbrook Util. Sys., Inc. v. FPSC, 518 So. 2d 326, 327 (Fla. 1st DCA 1987), rehearing denied, 529 So. 2d 694 (Fla. 1988). Based on the foregoing Court decisions and past Commission decisions, staff believes it is appropriate to adjust rate case expense to an hourly rate which we believe to be more reasonable for the rate payers of Hobe Sound.

Staff believes a more appropriate hourly rate for Mr. Guastella would be the rate approved in the Palm Coast Utility Corporation rate case proceeding. Pursuant to Order No. PSC-96-1338-FOF-WS, issued November 7, 1996, the Commission found that an hourly rate of \$140 was a more appropriate rate for Mr. Guastella's expertise. Accordingly, staff recommends that Mr. Guastella's hourly rate should be reduced to \$140. We recommend the utility be allowed to recover \$23,380 in rate case expense for Mr. Guastella (\$140 x 167 hours). This is a \$9,578 reduction to the amount requested for Mr. Guastella.

Accounting: Guastella Associates billed the utility \$38,238 for 328 hours of accounting work related to this rate case. In its update, the utility included the support for the above and also its estimate to complete for \$2,640. Staff has reviewed the supporting documentation and believe these charges to be reasonable. We also compared the accounting hourly rate to the rates allowed in previous rate cases and found that it fell within the Commission allowed hourly rate for accounting fees. Therefore, we recommend the \$40,877 in accounting fees included in the utility's revised requests be allowed.

Support Staff, Travel & Miscellaneous Charges: Staff has reviewed the amounts included in the utility's rate case expense revision for Guastella Associates' administrative charges. We believe these amounts to be reasonable. Therefore we are not recommending any adjustments be made to the utility's requests.

Summary: Based on the above adjustments, staff recommends that the utility be allowed to recover \$71,952 in rate case expense for

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Guastella Associates. Accordingly, rate case expense reported in the MFRs should be reduced by \$23,048.

TAX PREPARATION

The utility initially estimated that the costs to prepare the MFR tax schedules would be \$2,000. The utility's update revealed that the actual charges were only \$935. After our review of the supporting invoices, staff believes that these charges appear to be reasonable. Accordingly, we recommend that the utility should be allowed to recover the \$935 in tax preparation charges included in the utility's revised request. Consequently, this reduces the amount included in the MFRs by \$1,065.

MISCELLANEOUS

In its filing, the utility requested recovery of \$2,084 for printing and customer noticing. In its update, the utility revised its requests to include \$415 for printing and \$786 for mailing customer notices. Staff has reviewed the update and the supporting documentation and believe the utility has justified its revised request. Therefore, we recommend that the utility should be allowed \$1,201 in miscellaneous rate case expense. This reduces the utility's original request by \$883.

FPSC FILING FEE

The utility included \$2,000 for the PSC filing fee in its original request. In its update, it failed to include any amount for filing its rate case. Regardless, on June 12, 1997, the Commission received a \$4,500 check, which was the amount required by Rule 25-30.020(e)(4), Florida Administrative Code, for filing a rate case for this size utility. Accordingly, staff recommends that the utility be allowed to recover the full \$4,500 filing fee.

PRIOR RATE CASE EXPENSE

As mentioned previously, Hobe Sound added \$56,145 to its current rate case expense for prior unamortized rate case expense. In the utility's two prior rate proceedings, the Commission approved annual expenses of \$21,526, by Order No. PSC-94-0870-FOF-WU, issued November 28, 1994, in Docket No. 940475-WU, and \$7,737, by Order No. PSC-96-0870-FOF-WU, issued July 2, 1996, in Docket No. 960192-WU.

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According to Section 367.0815, Florida Statutes, and the orders stated above, the resulting rates will be reduced on December 20, 1998, for Docket No. 940475-WU and on August 1, 2000, for Docket No. 960192-WU. If the unamortized balance of prior rate case expense was added to the current balance and re-amortized over the next four years, the utility would be penalized when the four-year rate reductions take place. Therefore, staff recommends removing the \$56,145 in unamortized rate case expense and including the amount of annual rate case expense amortization for each prior docket. Accordingly, staff recommends that \$29,263 in prior rate case expense be included in test year expenses.

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SUMMARY

Based on staff's adjustments, \$98,327 should be allowed as reasonable rate case expense. Staff's adjustments are shown below.

| | | |
|---------------------------------------|---------------|-----------------|
| Current Rate Case Expense (Per MFRs) | | \$131,084 |
| Adjustment per Utility | | <u>(27,679)</u> |
| Total Revised RC Expense Per Utility | | 103,405 |
| Adjustments per staff: | | |
| Guastella Associates | (9,578) | |
| FPSC Filing Fee | <u>4,500</u> | 5,078 |
| Staff Recommended RC Expense | | <u>98,327</u> |
| Current Rate Case Expense Per MFRs | 131,084 | |
| Prior Unamortized RC Expense Per MFRs | <u>56,145</u> | |
| Total Amount Requested Per MFRs | | <u>187,229</u> |
| Utility's Annualized MFR Request | | 46,807 |
| Staff Recommended Current RC Expense | <u>98,327</u> | |
| Divide by four | 4 | |
| Staff Recom. Current Annual Amort. | 24,582 | |
| Prior Rate Case Expense Amortization | <u>29,263</u> | |
| Staff's Recommended RC Exp. | | <u>53,845</u> |
| Staff Recommended Net Adjustment | | <u>7,038</u> |

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ISSUE 13: Should an adjustment be made to amortize the costs to repair the utility's generator?

RECOMMENDATION: Yes, expenses should be reduced by \$7,414.
(MONIZ)

STAFF ANALYSIS: According to Audit Exception No. 8, the utility's generator was struck by lightning and subsequently cost \$22,994 to repair. The company had insurance to cover the cost except for a \$10,000 deductible. This \$10,000 amount was charged to Regulatory Commission Expenses - Other, in December 1995. An offsetting entry for \$733 was credited to Materials and Supplies, leaving a balance of \$9,267 in Operation and Maintenance Expenses. This amount was included as an expense in the MFRs for each of the test years, June 30, 1996, June 30, 1997, and June 30, 1998.

In accordance with Rule 25-30.433(8), Florida Administrative Code, non-recurring expenses shall be amortized over a 5-year period unless a shorter or longer period of time can be justified. In its response to the audit, the utility does not object to amortizing the costs over five years. However, it does suggest that the unamortized portion should be included in rate base.

Based on the above, staff recommends that the generator repair costs of \$9,267 should be amortized over five years, beginning in December 1995. This results in a net reduction to test year expenses of \$7,414 (\$9,267-\$1,853). In addition, an adjustment should be made to increase the working capital allowance to include the 13-month average unamortized balance of \$5,560. This adjustment is discussed in Issue No. 4.

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ISSUE 14: What is the appropriate level of test year operating income before any revenue increase?

RECOMMENDATION: The appropriate level of test year operating income should be \$334,796. (MONIZ)

STAFF ANALYSIS: Based on the adjustments discussed in previous issues, staff recommends that the test year operating income before any provision for increased revenues should be \$334,796. The schedule for operating income is attached as Schedule No. 3-A and the adjustments are shown on Schedule No. 3-B.

REVENUE REQUIREMENT

ISSUE 15: What is the appropriate revenue requirement?

RECOMMENDATION: The following revenue requirement should be approved: (MONIZ)

| | <u>TOTAL</u> | <u>\$ INCREASE</u> | <u>% INCREASE</u> |
|-------|--------------|--------------------|-------------------|
| Water | \$2,019,226 | \$344,337 | 20.56% |

STAFF ANALYSIS: The revenues required as a result of staff's analysis are \$2,019,226. This will allow the utility the opportunity to recover its allowed level of expenses and to earn a 8.74% rate of return on its investment in rate base.

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RATES & RATE STRUCTURE

ISSUE 16: What is the appropriate projected number of ERCs and gallons that should be used to set rates for monthly service for the projected test period ending June 30, 1998?

RECOMMENDATION: The appropriate projections that should be used to set rates for monthly service for the projected test period ending June 30, 1998 are those proposed by the utility of 38,221 ERCs and 587,717 thousand gallons. (LINGO)

STAFF ANALYSIS: As discussed in the case background, the utility's projected test year ends June 30, 1998, based on a historical test year ended June 30, 1996. In order to arrive at its total projected number of bills, ERCs and gallons (billing determinants), the utility projected the increases or decreases to these respective billing determinants it anticipated during the July 1, 1996 - June 30, 1998 period, and added these changes to the corresponding historical test year figures. Staff's calculations of projected bills and ERCs, average consumption reductions and projected total consumption are shown on pages 1-3 of Attachment A; a summary comparison of the utility's projections of customer bills, ERCs and consumption along with staff's corresponding projections is shown on page 4 of Attachment A. A discussion of the utility's projections follows.

Projected ERCs

The utility projected that a total of 54 additional connections would be added between the period of July 1, 1996 and June 30, 1998. In response to a staff Data Request, the utility explained the anticipated growth in terms of the general subdivisions or areas served:

| | Projected Additional <u>Connections</u> |
|------------------------|--|
| Jupiter Island - North | 10 |
| Jupiter Island - South | 4 |
| Olympia #1 | 38 |
| Olympia #4 | <u>2</u> |
| | 54 |

It is projected that neither Hobe Sound nor the Eaglewood subdivision would experience any additional connections. (Response to staff Data Request dated May 20, 1997, No. 3) As an independent check of these projections, staff discussed Hobe Sound's projected customer growth in the various subdivisions with an official of the Martin County Property Appraiser's office. As a result of this discussion, staff believes the utility's customer growth projections are reasonable.

As shown on the utility's customer growth workpaper (MFR vol. IV, p. 16), the utility projected that 446 additional bills would result from the addition of the 54 projected additional connections. However, there appears to be an error on the workpaper, as staff's recalculation of the workpaper (as shown on p. 1 of Attachment A) yields 497 additional bills, rather than 446 bills. The additional 51 bills (497 bills - 446 bills) as calculated by staff results in a projection of 72 ERCs greater than that proposed by the utility (see p. 1 of Attachment A). However, as shown on p. 4 of Attachment A, the utility's total projected ERCs are within 0.2% of staff's corresponding calculation; therefore, we recommend no adjustment to the utility's projection.

Projected Consumption

Anticipated Reduction in Average Consumption per ERC

As discussed in the case background, the test period approved for the utility is the projected test year ending June 30, 1998, based on a historical test year ended June 30, 1996. The utility's projected total consumption assumes an annual average reduction in consumption of 2.54% per ERC. The utility states: "This decrease assumes future usage will react similarly to the impacts of weather, conservation measures, and rate increases." (MFR volume IV, p. 1) The utility requested and was granted a similar adjustment in its last full rate case. In that proceeding, consumption figures used to calculate rates reflected an average annual decline in consumption of 5.46% over the 1989 - 1993 period.

The utility's support for its request in the instant proceeding is included on page 18 (meter and ERC analysis workpaper) of volume IV of the utility's MFRs, and, based on our review of the utility's analysis, we agree that the data indicates

an average annual decline in average consumption per ERC of at least 2.54%. In order to further analyze the utility's request in this regard, staff performed an independent analysis of the change in average consumption per ERC from December 31, 1993 to the end of the historical test period ended June 30, 1996. This analysis was performed in part based on data provided by the utility in its monthly reports that have been filed with the Commission. (The utility was ordered to file these reports as a result of its rate case in Docket No. 940475-WU (Order No. PSC-94-1452-FOF-WU)).

The results of this analysis are included on page 2 of Attachment A. As shown on the attachment, the overall average consumption per meter equivalent for the 12-month period ended December 31, 1993 was 17,159 gallons per day (gpd), and had declined to 16,022 gpd at the end of the 12-month period ended June 30, 1996 -- representing an average annual reduction of approximately 2.7%. Therefore, based on this analysis in conjunction with the support provided by the utility, we believe that the utility's requested reduction of 2.54% is reasonable.

Calculation of Projected Consumption

The utility applied the 2.54% anticipated annual consumption reduction per ERC to its historical test year consumption to arrive at total projected test year consumption of 587,717 thousand gallons. Staff reviewed this calculation, and we believe the utility appropriately applied the anticipated reduction to arrive at its projected total consumption.

A comparison of the utility's projections of bills, ERCs and consumption versus staff's corresponding calculations is presented on p. 4 of Attachment A. Although the utility's consumption projection is less than staff's, its total projected gallons are within 0.2% of staff's corresponding calculation. Therefore, we recommend no adjustment to the utility's projection.

Conclusion

As shown on p. 4 of Attachment A, the utility's total projections of customer bills, ERCs and consumption are all within 0.3% of staff's corresponding projections. Therefore, staff recommends that the utility's projections of 15,662 bills, 38,221

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ERCs and 587,717 thousand gallons for the projected test year ending June 30, 1998 are reasonable and should be approved.

STAFF'S CALCULATION OF PROJECTED CUSTOMER BILLS AND ERCs

| | (a) | (b) | (c) = (a) x (b) | (d) | (e) = (a) x (d) |
|-------------------------------------|--------------------------------|---|--|---|--|
| | RESIDENTIAL 5/8" METERS | | | RESIDENTIAL 1" METERS | |
| | | Util Proj Growth in Custs 7/01/96 Thru 6/30/98 | Resulting Additional Bills 7/01/96 Thru 6/30/98 | Util Proj Growth in Custs 7/01/96 Thru 6/30/98 | Resulting Additional Bills 7/01/96 Thru 6/30/98 |
| | Mos. | | | | |
| Jul-96 | 24 | | | | |
| Aug-96 | 23 | | | | |
| Sep-96 | 22 | | | | |
| Oct-96 | 21 | | | | |
| Nov-96 | 20 | 1 | 20 | | |
| Dec-96 | 19 | 1 | 19 | 1 | 19 |
| Jan-97 | 18 | 1 | 18 | | |
| Feb-97 | 17 | 1 | 17 | | |
| Mar-97 | 16 | 1 | 16 | 1 | 16 |
| Apr-97 | 15 | 1 | 15 | 1 | 15 |
| May-97 | 14 | 1 | 14 | | |
| Jun-97 | 13 | 2 | 26 | | |
| Jul-97 | 12 | 4 | 48 | 2 | 24 |
| Aug-97 | 11 | 3 | 33 | 2 | 22 |
| Sep-97 | 10 | 3 | 30 | 2 | 20 |
| Oct-97 | 9 | 3 | 27 | | |
| Nov-97 | 8 | 2 | 16 | | |
| Dec-97 | 7 | 2 | 14 | 1 | 7 |
| Jan-98 | 6 | 2 | 12 | | |
| Feb-98 | 5 | 2 | 10 | 1 | 5 |
| Mar-98 | 4 | 2 | 8 | 2 | 8 |
| Apr-98 | 3 | 3 | 9 | | |
| May-98 | 2 | 3 | 6 | | |
| Jun-98 | 1 | 2 | 2 | 1 | 1 |
| TOTALS: | | | | | |
| ADDL CONNECTS | | 40 | | 14 | = 54 Addl Connections |
| ADDL BILLS | | | 360 | | 137 = 497 Addl Bills |
| TOTAL ADDL ERCs | | | 360 | | 343 = 703 Total ERCs |
| GRAND TOTAL ADDL 5/8" BILLS: | | | 360 | GRAND TOTAL ADDL 1" BILLS: | |
| Staff | | | 360 | Staff | 137 |
| Utility | | | 323 | Utility | 123 |
| Diff to increase | | | 37 | Diff to increase | 14 = 51 Bills Staff > Utility |
| GRAND TOTAL ADDL 5/8" ERCs: | | | 360 | GRAND TOTAL ADDL 1" ERCs: | |
| Staff | | | 360 | Staff | 343 |
| Utility | | | 323 | Utility | 308 |
| Diff to increase | | | 37 | Diff to increase | 35 = 72 ERCs Staff > Utility |

Source:
 (b), (d) Hobe Sound Water Company, Docket No. 970164-WU, MFR vol. IV, p. 16 (customer growth worksheet)

ANNUAL PERCENTAGE CHANGE IN MONTHLY CONSUMPTION PER ERC

| | (a) | (b) | (c) = [(b) - (a)] / (a) / 30 mos x 12 mos |
|--|---|--|---|
| | Per Monthly Reports Filed with PSC | | |
| | Average Monthly Consumption per ERC @ 1231.83 | Average Monthly Consumption per ERC @ 930.06 | Annual Percentage Change in Monthly Cons per ERC |
| RESIDENTIAL | | | |
| Mainland | 12,164 | 11,938 | -0.7% |
| Jupiter Island | 16,374 | 16,046 | -0.8% |
| Subtotal | 15,270 | 14,975 | -0.8% |
| GENERAL SERVICE | | | |
| Mainland | 13,782 | 10,272 | -10.2% |
| Jupiter Island | 37,498 | 31,878 | -6.0% |
| Subtotal | 26,791 | 21,250 | -8.3% |
| TOTAL RESIDENTIAL AND GENERAL SERVICE | 17,159 | 16,022 | -2.7% |

Sources:

- (a) Hobe Sound Water Company, Docket No. 940475-WU, response to Staff's informal data request received from Guestalla Associates on 10/07/94.
- (b) Hobe Sound Water Company, monthly reports filed in compliance with Order No. PSC-94-1452-FOF-WU.

STAFF'S CALCULATION OF PROJECTED CONSUMPTION

| | (a) | (b) | (c) | (d) = (c) / (b) | (e) | (f) = (d) x (e) | (g) = (c) + (f) |
|---|---------------|---------------|------------------|--------------------|---------------------------------------|---|---|
| PER UTILITY: PROJECTED TEST PERIOD ENDING 6/30/98 STAFF'S CALCULATED PROJECTED CONSUMPTION | | | | | | | |
| | Bills | ERCs | (000) Gallons | (000) Gals/ERC | Staff Adjustment to Projected ERCs | Staff's Adjust to Proj Gals @ 6/30/98 | (000) Staff's Calculated Gals @ 6/30/98 |
| Residential | | | | | | | |
| 5/8" | 8,507 | 8,507 | 108,097 | 12.472 | 37 | 461 | 108,558 |
| 1" | 2,355 | 5,888 | 107,318 | 18.228 | 35 | 629 | 107,945 |
| 1 1/2" | 1,752 | 8,760 | 128,824 | 14.708 | | | 128,824 |
| 2" | 1,020 | 8,180 | 116,676 | 14.299 | | | 116,676 |
| Sub | 13,634 | 31,315 | 458,913 | 14.655 | 72 | 1,090 | 460,003 |
| General Service | | | | | | | |
| 5/8" | 732 | 732 | 8,251 | 11.272 | | | 8,251 |
| 1" | 812 | 1,530 | 21,656 | 14.154 | | | 21,656 |
| 1 1/2" | 504 | 2,520 | 36,174 | 14.355 | | | 36,174 |
| 2" | 108 | 784 | 6,581 | 7.617 | | | 6,581 |
| 3" | 80 | 960 | 5,368 | 5.590 | | | 5,368 |
| 4" | 12 | 300 | 50,777 | 169.257 | | | 50,777 |
| Sub | 2,028 | 6,908 | 128,805 | 18.651 | | 0 | 128,805 |
| TOTALS: | 15,662 | 38,221 | 587,718 | 15.377 | | 1,090 | 588,808 |

Sources:

- (a) - (c) Hobe Sound Water Company, Docket No. 970164-WU, MFR vol. IV, p. 15 (Rates III workpaper).
- (e) Staff's Memorandum dated September 11, 1997, Attachment A, p. 1.

**COMPARISON OF PROJECTED BILLS, ERCs AND CONSUMPTION:
 UTILITY V. STAFF**

| | (a) | (b) | (c) = (b) - (a) | (d) = (c) / (a) |
|-------------------|---|-----------|--|-----------------|
| | Projected Test Year Ending June 30, 199 | | Difference: Staff in Excess of Utility | |
| | Per Utility | Per Staff | Amount | Percent |
| Customer Bills | 15,662 | 15,713 | 51 | 0.3% |
| ERCs | 38,221 | 38,293 | 72 | 0.2% |
| Consumption (000) | 587,717 | 588,807 | 1,090 | 0.2% |

Sources:

- (a) Hobe Sound Water Company, Docket No. 970164-WU, MFR vol. IV, p. 15 (Rates III workpaper).
- (b) Staff Memorandum dated September 11, 1997, Attachment A, pp. 1, 3.

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ISSUE 17: What is the appropriate rate structure for this utility, and what are the appropriate monthly rates for service?

RECOMMENDATION: The appropriate rate structure for the residential customers is a continuation of the current base facility and gallonage charge rate structure consisting of three tiers (usage blocks) with an inclining rate for each subsequent tier. The appropriate rate structure for the general service customers is a continuation of the traditional base facility and uniform gallonage charge rate structure. The recommended rates, as shown on Schedule No. 4, should be designed to produce revenues of \$2,017,316, 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), Florida Administrative Code. 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. (LINGO, GALLOWAY)

STAFF ANALYSIS: The utility's current rate structure consists of a base facility and gallonage charge rate structure. Standard base facility charges apply to both the residential and general service customers. However, general service customers are charged a uniform gallonage charge rate, while the residential customers are charged based on a conservation-oriented three-tiered inclining block rate.

The utility was first granted an inclining-block (conservation) rate structure in Docket No. 900656-WU. In that case, the per capita consumption of Hobe Sound's customers was approximately 500 gpd. By Order No. 24485, issued May 7, 1991, the Commission recognized that the utility's proposed conservation rates would be considered as part of an overall conservation plan. Therefore, by the aforementioned order, the Commission granted the utility's request for inclining-block residential rates, with the second usage block set at consumption greater than 10,000 gallons per month (gpm). A factor of approximately 2.1 times the initial block rate was approved for consumption greater than 10,000 gpm.

The utility's current rate structure was granted in Docket No. 940475-WU. In that case, the Commission: 1) separated the

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second tier monthly usage block into two blocks, resulting in usage blocks of 0 - 10,000 gpm, 10,001 - 40,000 gpm, and usage in excess of 40,000 gpm; 2) approved a "conservation adjustment" of 25%, whereby 25% of the base facility charge (BFC) costs were shifted to the gallonage charge; and 3) approved a factor 2.25 times the initial block rate to be used for monthly consumption in the 10,001 - 40,000 gpm tier, and a factor of 3.0 times the initial block rate to be used for monthly consumption in excess of 40,000 gpm. In recognition of the need to evaluate the effects of this unique rate structure, the Commission also ordered Hobe Sound to compile monthly reports containing detailed billing data with regards to bills, consumption and revenues, separated by customer class, meter size, and by customers on the mainland versus those customers on Jupiter Island.

A summary of the utility's history with regard to conservation-oriented rates is presented in the table below:

| | COMMISSION-APPROVED | | |
|----------------------|------------------------------|--------------------------|-------------------------|
| | Usage Blocks (kgals) | Usage Block Rate Factors | Conservation Adjustment |
| Docket No. 900656-WU | 0 - 10 Over 10 | 1.0 2.1 | None |
| Docket No. 940475-WU | 0 - 10 10 - 40 Over 40 | 1.0 2.25 3.0 | 25% |

In the instant proceeding, the utility proposes to continue its current three-tiered rate structure. The utility used a multi-step process with regard to the calculation of its requested rates. First, based on the utility's requested revenue requirement, cost-based rates of \$23.24 for the BFC and \$2.06 for the gallonage charge were calculated. Next, the utility made a "conservation adjustment," whereby 20% of the BFC costs were shifted to the gallonage component for the residential class. This lowered the BFC to \$18.68.

The utility then separated the portion of the revenue attributable to general service gallonage charges from the total

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revenue requirement to determine the revenue that must be generated through the residential increasing-block gallonage charges. The utility proposed that a factor of 2.0 times the initial block rate be used for monthly consumption in the 10,001 - 40,000 gpm tier, and a factor of 2.5 times the initial block rate be used for monthly consumption in excess of 40,000 gpm. (These factors are referred to as "usage block rate factors" or "rate factors".) These rate factors were the basis for the calculation of the factored number of gallons. The utility's requested revenue requirement, the "conservation adjustment" of 20% and the calculation of factored gallons resulted in the utility's requested residential rates for the three tiers of \$1.20 for the first usage block, \$2.40 for the second block and \$3.00 for the third block.

The utility's rate design proposals in the instant proceeding are summarized below:

| UTILITY'S PROPOSALS | | | |
|----------------------------|---------------------------------|-------------------------------------|------------------------------------|
| | Usage Blocks (kgals) | Usage Block Rate Factors | Conservation Adjustment |
| Docket No. 970164-WU | 0 - 10 | 1.0 | 20% |
| | 10 - 40 | 2.0 | |
| | Over 40 | 2.5 | |

As discussed above, there are several steps involved in evaluating and calculating an inclining-block rate structure including (but not limited to) determining: 1) the appropriate usage blocks; 2) the appropriate "conservation adjustment," if any; and 3) the appropriate usage block rate factors. Staff agrees in part and disagrees in part with the utility's proposed rate structure and methodology of calculating its requested rates. There are several unique aspects of the utility's rate structure addressed below.

Usage Blocks

Staff examined the utility's historical residential consumption data for the period ended June 30, 1996 as part of our review of the utility's request to continue its current three-tiered rate structure. Our analysis reveals that approximately

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45% of total residential bills are accounted for in the first usage block. Approximately 79% of total residential bills are captured within the first two usage blocks, while the third usage block accounts for the remaining 21% of total residential bills. Staff believes the current first two usage blocks capture an appropriate and representative portion of the utility's residential population; therefore, we recommend no change to the utility's current usage blocks.

Conservation Adjustment

As mentioned previously, the utility proposes to shift 20% of the BFC costs to the gallonage charge. A conservation adjustment of 25% was requested and approved in the utility's last full rate case (Docket No. 940475-WU). In order to evaluate the need for such an adjustment in this case, staff (based on our recommended revenue requirement) calculated cost-based rates of \$21.16 for the BFC for a 5/8" x 3/4" meter and \$2.06 for the general service gallonage charge. The relatively low gallonage rate as compared to the BFC is due mainly to the unusually high consumption levels of Hobe Sound's residential customers. Therefore, in order to mitigate this disparity, as well as shift more of the burden of cost recovery to the gallonage charge in order to promote conservation, staff believes that some "conservation adjustment" is appropriate. However, the utility's proposal contemplates that all general service customers would pay \$2.02 per 1,000 gallons. Staff believes that the overall rate increase should be enough to promote some conservation by the general service customers.

The magnitude of the proposed 20% conservation adjustment is less than what was proposed and approved in the utility's last rate case, and the utility offered no explanation as to why it is proposing to reduce the magnitude of the adjustment. Staff questions the reasoning behind Hobe Sound's proposal to lower the magnitude of the conservation adjustment in this proceeding when, as will be discussed in greater detail below, the utility's customers' consumption patterns since the last rate case would indicate a need for more aggressive conservation measures. Therefore, we recommend that the utility's requested conservation adjustment of 20% be denied in favor of the higher, current conservation adjustment of 25%.

Usage Block Rate Factors

In the instant proceeding, the utility has requested a change in its usage block rate factors from the current factors of 1.0, 2.25 and 3.0 to lower factors of 1.0, 2.0 and 2.5. In one of its data requests, staff asked Hobe Sound how it had used the information contained in the monthly reports filed with the Commission when formulating its anticipated 2.54% consumption reduction and its proposed gallonage charge rate block factors of 1.0, 2.0 and 2.5. The utility responded:

This information was not used for the formulation of the consumption reduction or the block rate factors....The Company is not seeking to change the block rate structure from that proposed and accepted in the last rate order and therefore used the factors consistent with that filing. (Hobe Sound's response to staff's Data Request Dated May 20, 1997, No. 6)

Curiously, the utility's responses seem to indicate not only a disregard of the importance of monitoring its approved conservation-oriented rate structure, but a lack of analysis with regard to its rate design proposals.

Staff disagrees with the utility's request to lower its rate factors to 1.0, 2.0 and 2.5 for numerous reasons, several of which are interrelated. First, monthly usage below 10,000 gallons is not considered excessive, and is less discretionary than usage in subsequent blocks. For example, 56% of all bills rendered to the utility's "typical" residential customers on 5/8" x 3/4" meters are captured in the 0 - 10,000 gallon usage block. In fact, 34% of these customers' bills are captured in usage of 5,000 gallons or less. Since usage below 10,000 gpm is relatively nondiscretionary, staff believes the rate in this usage block should be kept as low as possible.

Second, as discussed previously, residential customers' usage in the monthly block of 10,001 - 40,000 gallons accounts for 27% of the utility's total residential consumption, and usage in the third block (monthly consumption in excess of 40,000 gallons) accounts for 51% of the utility's total residential consumption.

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Therefore, the combined usage of customers in the second and third tiers accounts for an unusually high 78% of total residential consumption. As a result, staff believes it is necessary to send the customers in the second and third tiers stronger price signals than those generated by the currently approved rate factors of 1.0, 2.25 and 3.0, and certainly stronger than those proposed by the utility.

Staff's belief in this regard is further supported by our analysis of the monthly reports filed by Hobe Sound as required by Order No. PSC-94-1452-FOF-WU. These monthly reports provide greater detail of the utility's customers' consumption patterns. For example, the utility's residential mainland customers (over 98% of whom have 5/8" meters) account for over 50% of the utility's total system bills -- residential and general service customers combined -- while accounting for only 16% of all gallons sold. Conversely, the utility's Jupiter Island customers account for approximately 35% of the utility's entire customer base, but these customers consume over 60% of all water sold by Hobe Sound. In fact, the number of gallons sold to those customers in the third usage block alone represents over 35% of total gallons sold. Staff believes this analysis supports our contention for the need of more stringent rate factors.

Third, an analysis of similar residential data from Docket No. 940475-WS reinforces this point. In that case: 1) residential customers' usage in the second tier accounted for 28% of total residential consumption; 2) usage in the third tier accounted for an additional 52% of total residential consumption; and 3) combined second and third tier consumption accounted for 80% of the utility's total residential consumption. The percentages of total residential consumption captured in the second and third tiers in the instant proceeding are virtually identical to those corresponding percentages in the utility's last rate case. This suggests that more aggressive, rather than less aggressive, rate factors are appropriate in this instance.

In order to further evaluate the utility's proposed usage block rate factors, and evaluate other rate factor options as well, staff used a combination of different rate factors, in conjunction with conservation adjustments of 20% and 25%, and calculated the resulting gallonage charge rates based on staff's recommended revenue requirement. Consumption charges (charges excluding the BFC) were then calculated at different usage levels,

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and the resulting increase in those bills over the current rates were also calculated. A representative sample of this analysis is shown on Attachment B.

Based on the analysis on Attachment B, our final area of disagreement with the utility's rate design proposal is that it shifts a portion of the revenue recovery burden from the high consumption customers to the low consumption customers. This is illustrated in column (b) of Attachment B, which presents the gallonage charge rates resulting from the utility's proposed: a) 20% conservation adjustment; and b) rate factors of 1.0, 2.0 and 2.5. As shown in column (b), the percentage increase in the consumption charges for a low-use customer using 5,000 gpm is 35.6%, while the corresponding percentage increase for a high-use customer using 100,000 gpm is only 15.5%, or less than one-half the percentage increase of the customer using 5,000 gpm. This indicates that the utility's proposal shifts a portion of the revenue recovery burden from the high use customers to the low use customers.

We believe the utility's rate design proposal sends weaker, and, therefore, inappropriate pricing signals to the customers in the second and third usage blocks. As discussed previously, staff believes that stronger price signals are appropriate for the second and third usage blocks. Therefore, based on the foregoing, we disagree with the utility's proposed usage block rate factors.

As mentioned previously, Attachment B also presents a representative sample of our analysis of other rate factor combinations. Consistent with our belief that stronger-than-current price signals are appropriate for the second and third usage blocks, columns (c) through (e) and (g) through (i) of Attachment B present our analysis, based on our recommended revenue requirement, of three rate factor combinations that are more stringent than the current rate factors of 1.0, 2.25 and 3.0. The analysis in columns (g) through (i) is based on staff's recommended conservation adjustment of 25%. (The analysis in columns (c) through (e) is based on the utility's proposed conservation adjustment of 20%, and because we are recommending a conservation adjustment different than what was proposed by Hobe Sound, the information in these columns is presented for comparative purposes only.)

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Column (g) presents our analysis of the price signals that would result from a rate factor combination of 1.0, 2.25 and 3.75. As shown in the lower portion of column (g), the percentage increase in consumption charges over current levels for customers at usage levels of 5,000 gallons, 10,000 gallons and 25,000 gallons is a uniform 4.6%. Therefore, this rate factor combination was eliminated from consideration because we believe that customers using 25,000 gallons should receive a greater percentage increase than those customers at the lower consumption levels. Column (h) presents our analysis of a rate factor combination of 1.0, 2.5 and 3.75. As shown in the lower portion of column (h), the consumption charges for customers at usage levels greater than 10,000 gallons are progressively higher than the 2.3% increase that would be experienced by the customers with usage of 10,000 gallons or less. Column (i) presents our corresponding analysis of a rate factor combination of 1.0, 2.75 and 4.0. This combination was also eliminated from consideration, as the customers in the first usage block (0 - 10,000 gallons) would experience a 4.6% decrease in their consumption charge.

Based on the analysis discussed above, staff recommends a rate for the second block that is 2.5 times that of the initial block rate, and a rate for the third block that is 3.75 times the initial block rate. Not only do these recommended factors send stronger price signals to high-use customers than the utility's proposed rate factors, but the factors send even stronger price signals to those high-use customers than the factors approved in Docket No. 940475-WU. Finally, staff's higher factors have the resulting effect of a lower rate in the first usage block than would be achieved using the utility's proposed factors. As we believe a goal is to keep the rate in the first tier as low as possible (without going below the current rate in that tier), staff's recommended factors better achieve this goal.

The permanent rates requested by the utility are designed to produce revenues of \$2,099,115 for water service. The requested revenues represent an increase of \$424,226, or 25.33%. Staff recommends that the final rates approved for the utility should be designed to produce revenues of \$2,017,316 (excluding miscellaneous service charge revenues), which is an increase of \$344,337, or 20.56%.

Approximately 30% (or \$606,563) of the revenue requirement is recovered through the recommended base facility charge. The

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fixed costs are recovered through the BFC based on the projected number of factored ERCs. The remaining 70% of the revenue requirement (or \$1,410,753) represents revenues collected through the gallonage charge based on the projected number of gallons consumed during the projected year ending June 30, 1998.

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), Florida Administrative Code. 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, interim rates, requested rates and staff's recommended rates is shown on Schedule No. 4.

SELECTION OF RECOMMENDED USAGE BLOCK RATE FACTORS

| (a) | (b) | (c) | (d) | (e) | (f) | (g) | (h) | (i) |
|-------------------|--|---------------|--------------|--------------|--|---------------|--------------|--------------|
| | CONSUMPTION CHARGES WITH CONSERVATION ADJUSTMENT @ 20% | | | | CONSUMPTION CHARGES WITH CONSERVATION ADJUSTMENT @ 25% | | | |
| Current Rates | | | | | | | | |
| 0-10 gpd | \$1.18 | \$0.86 | \$0.86 | \$0.80 | \$1.23 | \$0.91 | \$0.89 | \$0.83 |
| 10-40 gpd | 2.36 | 1.98 | 2.15 | 2.26 | 2.46 | 2.05 | 2.23 | 2.28 |
| 40+ gpd | 2.85 | 3.36 | 3.23 | 3.20 | 3.08 | 3.41 | 3.34 | 3.32 |
| Consumption (gpd) | 1.0/2.0/2.5 | 1.0/2.25/3.75 | 1.0/2.5/3.75 | 1.0/2.75/4.0 | 1.0/2.0/2.5 | 1.0/2.25/3.75 | 1.0/2.5/3.75 | 1.0/2.75/4.0 |
| 5 | \$5.90 | \$4.40 | \$4.30 | \$4.00 | \$5.15 | \$4.55 | \$4.45 | \$4.15 |
| 10 | 11.80 | 8.80 | 8.60 | 8.00 | 17.30 | 9.10 | 8.90 | 8.30 |
| 25 | 47.20 | 38.50 | 40.85 | 41.00 | 49.20 | 39.85 | 42.35 | 42.50 |
| 50 | 112.10 | 101.20 | 105.40 | 106.00 | 116.90 | 104.70 | 109.20 | 109.90 |
| 75 | 185.85 | 183.70 | 188.15 | 186.00 | 193.90 | 189.95 | 192.70 | 192.90 |
| 100 | 259.60 | 268.20 | 268.90 | 268.00 | 279.90 | 275.20 | 278.20 | 275.90 |

% CHG IN CONSUMPTION CHARGES WITH CONSERVATION ADJUSTMENT @ 20%

% CHG IN CONSUMPTION CHARGES WITH CONSERVATION ADJUSTMENT @ 25%

| Consumption (gpd) | 1.0/2.0/2.5 | 1.0/2.25/3.75 | 1.0/2.5/3.75 | 1.0/2.75/4.0 | 1.0/2.0/2.5 | 1.0/2.25/3.75 | 1.0/2.5/3.75 | 1.0/2.75/4.0 |
|-------------------|-------------|---------------|--------------|--------------|-------------|---------------|--------------|--------------|
| 5 | 35.6% | 1.1% | -1.1% | -4.0% | 41.4% | 4.6% | 2.3% | -4.6% |
| 10 | 35.6% | 1.1% | -1.1% | -4.0% | 41.4% | 4.6% | 2.3% | -4.6% |
| 25 | 23.9% | 1.0% | 7.2% | 7.6% | 28.1% | 4.6% | 11.2% | 11.5% |
| 50 | 19.6% | 8.0% | 12.5% | 13.1% | 24.8% | 11.7% | 16.5% | 17.3% |
| 75 | 16.7% | 15.4% | 16.9% | 16.8% | 21.8% | 19.3% | 21.0% | 21.2% |
| 100 | 15.5% | 18.5% | 18.8% | 18.4% | 20.6% | 22.5% | 22.9% | 22.9% |

LEGEND:

- 1.0/2.0/2.5 = new rate is less than the current rate in that usage block.
- 1.0/2.25/3.75 = usage block differentials of 1.0 for the first usage block, 2.0 times the initial block rate for the second usage block, and 2.5 times the initial block rate for the third usage block.
- 1.0/2.5/3.75 = usage block differentials of 1.0 for the first usage block, 2.25 times the initial block rate for the second usage block, and 3.75 times the initial block rate for the third usage block.
- 1.0/2.75/4.0 = usage block differentials of 1.0 for the first usage block, 2.5 times the initial block rate for the second usage block, and 3.75 times the initial block rate for the third usage block.
- 1.0/2.75/4.0 = usage block differentials of 1.0 for the first usage block, 2.75 times the initial block rate for the second usage block, and 4.0 times the initial block rate for the third usage block.

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ISSUE 18: What information should the utility continue to file to enable staff to monitor the effects of the recommended increasing-block rates, and how often should this information be filed?

RECOMMENDATION: The utility should continue preparing monthly reports containing the number of customer bills, gallons billed and revenues billed. This information should be provided for each customer class, meter size and approved usage block, separated between customers located on the mainland versus those customers located on Jupiter Island. The monthly reports requested in this issue should be filed with the Commission on a quarterly basis for a period of two years, commencing on the first billing cycle in which the revised rates go into effect. (LINGO)

STAFF ANALYSIS: In consideration of the need to evaluate the effects of the utility's increasing-block rate structure approved by Order No. PSC-94-1452-FOF-WU, the Commission ordered the utility to compile and submit monthly reports containing the number of customer bills, gallons billed and revenues billed. This information was ordered for each customer class, meter size and usage block, separated between customers located on the mainland versus those customers located on Jupiter Island.

As discussed in the previous issue, staff recommends that the utility's three-tiered increasing-block rate structure be continued. Staff believes there is a need to continue to monitor the effects of this utility's rate structure. To that end, we believe it is appropriate to require the utility to continue to prepare monthly reports containing the number of customer bills, gallons billed and revenues billed. This information should be provided for each customer class, meter size and usage block, separated between customers located on the mainland versus those customers located on Jupiter Island. The monthly reports requested in this issue should be filed with the Commission on a quarterly basis for a period of two years, commencing on the first billing cycle in which the revised rates go into effect.

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ISSUE 19: What is the appropriate amount by which rates should be reduced four years after the established effective date to reflect the removal of the amortized rate case expense as required by Section 367.0816, Florida Statutes?

RECOMMENDATION: The water rates should be reduced as shown on Schedule No. 5, to remove rate case expense in the amount of \$98,327, grossed-up for regulatory assessment fees and amortized over a four-year period. The decrease in rates should become effective immediately following the expiration of the four-year recovery period, pursuant to Section 367.0816, Florida Statutes. The utility should be required to file revised tariff sheets and a proposed customer notice setting forth the lower rates and the reason for the reduction not later than one month prior to the actual date of the required rate reduction. (GALLOWAY)

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 rate case expense previously authorized in the rates. The reduction will reflect the removal of water revenues associated with the amortization of rate case expense and the gross-up for regulatory assessment fees which is \$98,327. The removal of rate case expense will reduce rates as recommended by staff on Schedule No. 5.

The utility should be required to file revised tariffs no later than one month prior to the actual date of the required rate reduction. The utility also should be required to file a proposed customer notice setting forth the lower rates and reason for the reduction.

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

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ISSUE 20: Is a refund of interim rates required, and if so, what is the appropriate amount?

RECOMMENDATION: No. Interim rates were not implemented; therefore, no refund is required. (MONIZ, GALLOWAY)

STAFF ANALYSIS: Pursuant to Order No. PSC-97-0839-FOF-WU, issued July 14, 1997, the Commission suspended the utility's proposed rates. The annualized revenues based on the limited proceeding rates which went into effect after the interim test year, as approved by Order No. PSC-96-0870-FOF-WU, were compared with the Commission approved interim revenues. This comparison resulted in a revenue increase of less than 1% or \$5,870 over current limited proceeding rates. The utility decided not to implement the approved rates because of the nominal impact. Since the interim rate increase was not implemented, no refund is required.

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OTHER

ISSUE 21: What are the appropriate annual and monthly discounted rates, and the effective date for AFUDC?

RECOMMENDATION: The annual AFUDC rate should be 8.74% and the discounted monthly rate should be 0.728204%, consistent with Rule 25-30.116, Florida Administrative Code. The AFUDC effective date should be July 1, 1998. (MONI2)

STAFF ANALYSIS: As discussed in Issue No. 7, staff is recommending an 8.74% weighted cost of capital. Therefore, staff recommends an annual AFUDC rate of 8.74% and a discounted rate of 0.728204% consistent with Rule 25-30.116, Florida Administrative Code. Additionally, according to the above rule, the new AFUDC rate shall be effective the month following the end of the 12-month period used to establish that rate. Therefore, since the end of the utility's test year is June 30, 1998, the effective date should be July 1, 1998.

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ISSUE 22: Should the docket be closed?

RECOMMENDATION: Yes, In the event a timely protest is not filed, the docket may be closed upon the utility's filing of and staff's approval of revised tariff sheets. (GERVASI, MONIZ)

STAFF ANALYSIS: If a protest is not received within 21 days of issuance of the Proposed Agency Action order, the order will become final. The docket may be closed upon the utility's filing of and staff's approval of revised tariff sheets.

HOBE SOUND WATER COMPANY
 SCHEDULE OF WATER RATE BASE
 PROJECTED TEST YEAR ENDING 6/30/98

SCHEDULE NO. 1-A
 DOCKET NO. 970164-WU

| COMPONENT | PER BOOK BALANCE 06/30/98 | UTILITY ADJUSTMENTS | ADJUSTED TEST YEAR PER UTILITY | STAFF ADJUSTMENTS | STAFF ADJUSTED TEST YEAR |
|--------------------------------|---------------------------------|------------------------|--------------------------------------|----------------------|--------------------------------|
| 1 UTILITY PLANT IN SERVICE | \$8,558,650 | \$3,373 | \$8,562,023 | \$10,549 | \$8,572,572 |
| 2 LAND | \$3,983 | \$0 | \$3,983 | \$0 | \$3,983 |
| 3 NON-USED & USEFUL COMPONENTS | \$0 | \$0 | \$0 | \$0 | \$0 |
| 4 ACCUMULATED DEPRECIATION | (\$2,341,449) | (\$150,457) | (\$2,491,906) | (\$1,001) | (\$2,492,907) |
| 5 CIAC | (\$322,984) | (\$3,303) | (\$326,287) | \$0 | (\$326,287) |
| 6 AMORTIZATION OF CIAC | \$160,973 | \$5,081 | \$166,054 | \$0 | \$166,054 |
| 7 ACQUISITION ADJUSTMENTS -NET | \$0 | \$0 | \$0 | \$0 | \$0 |
| 8 ADVANCES FOR CONSTRUCTION | \$0 | \$0 | \$0 | \$0 | \$0 |
| 9 DEFERRED TAXES | \$0 | \$0 | \$0 | \$0 | \$0 |
| 10 WORKING CAPITAL ALLOWANCE | \$189,782 | \$111,342 | \$301,124 | (\$44,863) | \$256,261 |
| RATE BASE | \$6,248,955 | (\$37,337) | \$6,214,991 | (\$35,315) | \$6,179,676 |

**HOBE SOUND WATER COMPANY
ADJUSTMENTS TO RATE BASE
PROJECTED TEST YEAR ENDING 6/30/98**

**SCHEDULE NO. 1-B
DOCKET NO. 970164-WU**

| EXPLANATION | WATER |
|--|-------------------|
| (1) PLANT IN SERVICE To capitalize items expensed by the utility (Issue 2) | <u>\$10,549</u> |
| (2) ACCUMULATED DEPRECIATION To reflect above adjustment to capitalize items (Issue 2) | <u>(\$1,001)</u> |
| (3) Working Capital To reflect adjustments to working capital (Issue 4) | <u>(\$44,863)</u> |

HOBE SOUND WATER COMPANY
 CAPITAL STRUCTURE
 PROJECTED TEST YEAR ENDING 6/30/98

SCHEDULE NO. 2
 DOCKET NO. 970164-WU

| DESCRIPTION | TOTAL CAPITAL | SPECIFIC ADJUSTMENTS (EXPLAIN) | PRO RATA ADJUSTMENTS | CAPITAL RECONCILED TO RATE BASE | RATIO | COST RATE | WEIGHTED COST | |
|--------------------------------|-----------------|--------------------------------|----------------------|---------------------------------|------------|-------------|---------------|--|
| PER UTILITY | | | | | | | | |
| 1 LONG TERM DEBT | \$ 4,331,250 \$ | 0 \$ | (84,447) \$ | 4,246,803 | 68.33% | 8.51% | 5.82% | |
| 2 SHORT-TERM DEBT | 0 | 0 | 0 | 0 | 0.00% | 10.00% | 0.00% | |
| 3 PREFERRED STOCK | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 4 COMMON EQUITY | 1,773,626 | 0 | (34,581) | 1,739,045 | 27.98% | 11.88% | 3.32% | |
| 5 CUSTOMER DEPOSITS | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 6 DEFERRED ITC'S-ZERO COST | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 7 DEFERRED ITC'S-WTD COST | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 8 DEFERRED INCOME TAXES | 233,700 | 0 | (4,557) | 229,143 | 3.69% | 0.00% | 0.00% | |
| 9 TOTAL CAPITAL | \$ 6,338,576 \$ | 0 \$ | (123,585) \$ | 6,214,991 | 100.00% | | 9.14% | |
| PER STAFF | | | | | | | | |
| 10 LONG TERM DEBT | \$ 4,331,250 \$ | 0 \$ | (108,579) \$ | 4,222,671 | 68.33% | 8.51% | 5.82% | |
| 11 SHORT-TERM DEBT | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 12 PREFERRED STOCK | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 13 COMMON EQUITY | 1,773,626 | 0 | (44,462) | 1,729,164 | 27.98% | 10.46% | 2.93% | |
| 14 CUSTOMER DEPOSITS | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 15 DEFERRED ITC'S-ZERO COST | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 16 DEFERRED ITC'S-WTD COST | 0 | 0 | 0 | 0 | 0.00% | 0.00% | 0.00% | |
| 17 DEFERRED INCOME TAXES | 233,700 | 0 | (5,858) | 227,841 | 3.69% | 0.00% | 0.00% | |
| 18 TOTAL CAPITAL | \$ 6,338,576 \$ | 0 \$ | (158,900) \$ | 6,179,676 | 100.00% | | 8.74% | |
| RANGE OF REASONABLENESS | | | | | LOW | HIGH | | |
| RETURN ON EQUITY (ROE) | | | | | 9.46% | 11.46% | | |
| OVERALL RATE OF RETURN | | | | | 8.46% | 9.02% | | |

HOBE SOUND WATER COMPANY
 STATEMENT OF WATER OPERATIONS
 PROJECTED TEST YEAR ENDING 6/30/98

SCHEDULE NO. J-A
 DOCKET NO. 970164-WU

| DESCRIPTION | AMOUNT PER BOOKS 06/30/98 | UTILITY ADJUSTMENTS | UTILITY ADJUSTED TEST YEAR | STAFF ADJUSTMENTS | STAFF ADJUSTED TEST YEAR | REVENUE INCREASE | REVENUE REQUIREMENT |
|-----------------------------|---------------------------|---------------------|----------------------------|-------------------|--------------------------|------------------|---------------------|
| 1 OPERATING REVENUES | \$1,674,493 | \$424,672 | \$2,099,115 | (\$424,276) | \$1,674,839 | \$344,337 | \$2,019,226 |
| OPERATING EXPENSES: | | | | | | 20.56% | |
| 2 OPERATION AND MAINTENANCE | \$823,755 | \$9,836 | \$833,591 | (\$31,432) | \$802,159 | | \$802,159 |
| 3 DEPRECIATION | \$290,742 | \$0 | \$290,742 | \$468 | \$291,210 | | \$291,210 |
| 4 AMORTIZATION | \$44,208 | \$0 | \$44,208 | \$0 | \$44,208 | | \$44,208 |
| 5 TAXES OTHER THAN INCOME | \$218,276 | \$20,010 | \$238,286 | (\$21,018) | \$217,268 | \$15,495 | \$232,763 |
| 6 INCOME TAXES | (\$33,578) | \$157,909 | \$124,331 | (\$109,580) | (\$14,751) | \$123,743 | \$108,993 |
| 7 OPERATING EXPENSES | \$1,343,401 | \$187,755 | \$1,531,156 | (\$181,562) | \$1,349,593 | \$139,238 | \$1,479,331 |
| 8 OPERATING INCOME | \$331,092 | \$424,672 | \$755,764 | (\$282,664) | \$473,100 | \$205,099 | \$539,895 |
| 9 RATE BASE | \$6,249,955 | | \$6,214,991 | | \$6,179,876 | | \$6,179,876 |
| 10 RATE OF RETURN | 5.30% | | 9.14% | | 5.52% | | 8.74% |

**HOBE SOUND WATER COMPANY
ADJUSTMENTS TO OPERATING STATEMENTS
PROJECTED TEST YEAR ENDING 6/30/98**

**SCHEDULE NO. 3-B
DOCKET NO. 970164-WU**

| EXPLANATION | WATER |
|--|-------------|
| (1) OPERATING REVENUES To reverse the utility's proposed revenue increase | (\$424,226) |
| (2) O & M Expenses | |
| a) To reduce secretary's salary (Issue 8) | (\$10,441) |
| b) To reduce employee benefits (Issue 8) | (\$892) |
| c) To disallow projected maintenance expenses for new catalytic filtration facility (Issue 9) | (\$4,100) |
| d) To reduce purchased power for out of period charges (Issue 10) | (\$3,294) |
| e) Net adjustment to reduce materials & supplies & amortize generator repair costs for 5 years (Issue 13) | (\$7,414) |
| f) To reduce equipment rental for computer related expenses (Issue 11) | (\$2,400) |
| g) Net rate case expense adjustment (Issue 12) | \$7,038 |
| h) To reduce O&M per capitalized expense adjustment (Issue 2) | (\$9,929) |
| | (\$31,432) |
| (3) DEPRECIATION EXPENSE To reflect adjustment to capitalized expenses (Issue 2) | \$468 |
| (4) TAXES OTHER THAN INCOME | |
| a) To reduce payroll taxes associated with reduction to salaries (Issue 8) | (\$1,928) |
| b) Adjustment to remove RAF's related to revenue increase | (\$19,090) |
| | (\$21,018) |
| (5) INCOME TAXES Adjustment to show income taxes consistent with adjusted test year year income | (\$109,580) |

RATE SCHEDULE

WATER

Monthly Rates

| | Rates As of 08/20/95 | Rates as of 1/01/96 | Utility Requested Interim | Commission Approved Interim | Utility Requested Final | Staff Recommended Final |
|---|----------------------------|------------------------|---------------------------------|-----------------------------------|-------------------------------|-------------------------------|
| Residential and General Service | | | | | | |
| <i>Base Facility Charge.</i> | | | | | | |
| Meter Size: | | | | | | |
| 5/8"x3/4" | \$12.14 | \$13.59 | \$14.25 | \$13.62 | \$18.68 | \$15.87 |
| 3/4" | \$18.21 | \$20.38 | \$21.37 | \$20.43 | \$28.02 | \$23.81 |
| 1" | \$30.35 | \$33.96 | \$35.61 | \$34.05 | \$46.70 | \$39.68 |
| 1-1/2" | \$60.59 | \$67.92 | \$71.22 | \$68.09 | \$93.40 | \$79.35 |
| 2" | \$97.11 | \$108.68 | \$113.97 | \$108.95 | \$149.44 | \$126.96 |
| 3" | \$194.22 | \$217.35 | \$227.93 | \$217.90 | \$298.88 | \$253.92 |
| 4" | \$303.46 | \$339.60 | \$356.12 | \$340.45 | \$467.00 | \$396.75 |
| <i>Residential Gallonage Charge</i> | | | | | | |
| (per 1,000 gallons) | | | | | | |
| 0 to 10,000 gal | \$0.78 | \$0.87 | \$0.91 | \$0.88 | \$1.20 | \$0.89 |
| 10,001 to 40,000 gal | \$1.76 | \$1.96 | \$2.06 | \$1.97 | \$2.40 | \$2.23 |
| Over 40,000 gal. | \$2.34 | \$2.62 | \$2.75 | \$2.63 | \$3.00 | \$3.34 |
| <i>General Service Gallonage Charge</i> | | | | | | |
| (per 1,000 gallons) | | | | | | |
| All gallons | \$1.46 | \$1.63 | \$1.71 | \$1.64 | \$2.06 | \$2.06 |
| Typical Residential Bills | | | | | | |
| <i>5/8" x 3/4" meter</i> | | | | | | |
| 5,000 Gallons | \$16.04 | \$17.94 | \$18.80 | \$18.02 | \$24.68 | \$20.32 |
| 10,000 Gallons | \$19.94 | \$22.29 | \$23.35 | \$22.42 | \$30.68 | \$24.77 |
| 25,000 Gallons | \$46.34 | \$51.69 | \$54.25 | \$51.97 | \$68.68 | \$58.22 |
| 60,000 Gallons | \$96.14 | \$107.29 | \$112.65 | \$107.62 | \$132.68 | \$125.07 |
| 75,000 Gallons | \$154.64 | \$172.79 | \$181.40 | \$173.57 | \$207.68 | \$208.57 |

UTILITY: HOBE SOUND WATER COMPANY
COUNTY: MARTIN COUNTY
DOCKET NO. 970164-WU

Schedule 5

Schedule of Rate Decrease After Expiration of
Amortization Period for Rate Case Expense

| RESIDENTIAL & GENERAL SERVICE | Staff Recommended Final Rates | Staff Recommended Decrease |
|--|--|---|
| Base Facility Charge | | |
| 5/8"x3/4" | \$15.87 | \$0.53 |
| 3/4" | \$23.81 | \$0.80 |
| 1" | \$39.68 | \$1.33 |
| 1-1/2" | \$79.35 | \$2.65 |
| 2" | \$126.96 | \$4.24 |
| 3" | \$253.92 | \$8.48 |
| 4" | \$396.75 | \$13.25 |
| Residential Gallonage Charge (per 1,000 gallons) | | |
| 0 to 10,000 gal | \$0.89 | \$0.02 |
| 10,001 to 40,000 gal | \$2.23 | \$0.05 |
| Over 40,000 gal | \$3.34 | \$0.08 |
| General Service Gallonage Charge (per 1,000 gallons) | | |
| All gallons | \$2.06 | \$0.05 |