



Public Service Commission

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RECORDS AND REPORTING

DATE: FEBRUARY 12, 1999

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYO)

FROM: DIVISION OF LEGAL SERVICES (VACCARO) *[Signature]*
DIVISION OF WATER AND WASTEWATER (WELLIS) *[Signature]*

RE: DOCKET NO. 960444-WU - APPLICATION FOR RATE INCREASE AND FOR INCREASE IN SERVICE AVAILABILITY CHARGES IN LAKE COUNTY BY LAKE UTILITY SERVICES, INC.
COUNTY: LAKE

AGENDA: FEBRUARY 16, 1999 - REGULAR AGENDA - DECISION ON MOTION TO DISMISS PRIOR TO HEARING - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: 8-MONTH EFFECTIVE DATE: February 8, 1999 - UTILITY HAS NOT PLACED REQUESTED RATES INTO EFFECT.

SPECIAL INSTRUCTIONS: THIS RECOMMENDATION WAS FILED ON AN EMERGENCY BASIS FOR CONSIDERATION PRIOR TO THE MARCH 10, 1999, HEARING.

FILE NAME AND LOCATION: S:\PSC\LEG\WP\960444.RCM

CASE BACKGROUND

Lake Utility Services, Inc., (LUSI or utility) is a Class B utility located in Lake County. LUSI is a wholly-owned subsidiary of Utilities, Inc. and provides no wastewater service. The service area is composed of eighteen subdivisions, which are served by twelve water plants. All of the plants are basically pump and chlorinate with hydro pneumatic tanks. There are ten plants in the South Clermont Region. In this region there are groups of two (Oranges-Vistas), three (Clermont I-Amber Hill-Lake Ridge Club) and four (Highland Point-Crescent Bay-Crescent West-Lake Crescent Hills) interconnected plants with one stand alone plant (Clermont II). The other two plants (Lake Saunders & Four Lakes) are outside

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this area. The minimum filing requirements (MFRs) filed in this docket indicate that the service area contained a total of 915 customers at the end of 1995. The utility reported adjusted test year operating revenues of \$313,946 for its water operations for 1995. According to the St. Johns River Water Management District, LUSI is in a water conservation area.

The utility filed this application for a rate increase on June 3, 1996. The utility was notified of several deficiencies in the filing by staff. Those deficiencies were corrected, and the official filing date was established as July 9, 1996. The utility's requested test year for both interim and final rates is the historical period ended December 31, 1995. Also, the utility requested that this case be processed using the Proposed Agency Action (PAA) procedure pursuant to Section 367.081(8), Florida Statutes.

During the course of this PAA rate case, staff identified a large number of errors in both the MFRs and the utility books. The attempts to correct these errors resulted in several staff information requests and three five-month statutory time extensions. The responses from the utility contained more errors. The first numbers resulted in a negative rate base. Although the second set of numbers indicated a relatively small rate base, it was staff's opinion that this rate case should proceed without further delays.

The Commission issued PAA Order No. PSC-97-0531-FOF-WU on May 9, 1997. In that order, rates were set and an overall rate of return of 9.26% was approved. On May 30, 1997, LUSI filed a Petition on Proposed Agency Action, protesting certain portions of the PAA Order No. PSC-97-0531-FOF-WU. Pursuant to Section 120.80 (13)(b), Florida Statutes, those portions of the PAA Order which were not protested are deemed stipulated. On July 21, 1997, the Office of Public Counsel (OPC) filed a notice of intervention in this docket. By Order No. PSC-97-0899-PCO-WU, issued July 30, 1997, the Commission acknowledged OPC's intervention.

On September 17, 1997, LUSI filed an offer of settlement to avoid the time and expense of further litigation in this docket. LUSI also filed a motion for continuance, requesting that further activity in this docket cease, pending final negotiation with the OPC. By Order No. PSC-97-1092-PCO-WU, issued September 19, 1997, LUSI's motion was granted. Pending the Commission's review of the utility's offer of settlement, LUSI filed three eight-month statutory time extensions. By PAA Order No. PSC-98-0683-AS-WU, issued May 18, 1998, the Commission accepted LUSI's settlement

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offer. OPC opposed the settlement at the time of the Commission's consideration of that matter. On June 8, 1998, OPC filed a petition on PAA, protesting Settlement Order No. PSC-98-0683-AS-WU and requesting a hearing on its protest. As a result of OPC's protest of Order No. PSC-98-0683-AS-WU, this matter was scheduled to proceed to hearing on September 15-16, 1998.

Following OPC's protest, the parties attempted to settle this case in lieu of proceeding to a hearing. During settlement negotiations, review of data presented in LUSI's 1997 annual report suggested that LUSI may be overearning under the interim rates set in this docket, due to increased customer growth. Settlement negotiations reached a stalemate, and, as a result, on August 27, 1998, LUSI filed a Notice of Withdrawal of Offer of Settlement and Notice of Withdrawal of Protest of PAA. By its notice, LUSI indicated its intent to withdraw its September 17, 1997 settlement offer and to withdraw its May 30, 1997 petition on PAA, by which it protested Order No. PSC-97-0531-FOF-WU. Following LUSI's notice of withdrawal, a Prehearing Conference was held on August 31, 1998.

At the Prehearing Conference, the Prehearing Officer continued that proceeding, pending Commission review of LUSI's notice of withdrawal. The Chairman's office postponed further action in this docket, and by Order No. PSC-98-1582-PCO-WU, issued November 25, 1998, the Commission rejected LUSI's notice of withdrawal based on OPC's protest of Order No. PSC-98-0683-AS-WU. By Order No. PSC-98-1622-PCO-WU (Order Revising Order Establishing Procedure), issued December 4, 1998, new procedural dates were scheduled, including dates for filing testimony and prehearing statements. The prehearing conference and hearing dates were rescheduled for March 1, 1999 and March 10-11, 1999, respectively.

On February 2, 1999, OPC filed a Motion to Dismiss LUSI's application for increased rates and increased service availability charges. On February 3, 1999, OPC filed a Motion for Expedited Hearing on Motion to Dismiss. On February 10, 1999, LUSI responded to OPC's motion to dismiss. This recommendation addresses OPC's motion to dismiss. The Chairman's office approved the inclusion of this recommendation on the February 16, 1999, agenda conference. Therefore, as discussed in Issue 1, staff believes that OPC's motion for expedited hearing is moot.

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DISCUSSION OF ISSUES

ISSUE 1: Should the Commission grant OPC's Motion for Expedited Hearing on its Motion to Dismiss?

RECOMMENDATION: There is no need to rule on OPC's motion for expedited hearing because it is moot. (VACCARO)

STAFF ANALYSIS: The Chairman's office approved the inclusion of OPC's motion to dismiss on the February 16, 1999, agenda conference. Therefore, OPC's motion for expedited hearing is moot and need not be ruled upon.

ISSUE 2: Should OPC's motion to dismiss LUSI's application for a rate increase and for an increase in service availability charges be granted?

RECOMMENDATION: No, OPC's motion to dismiss LUSI's application for a rate increase and for an increase in service availability charges should be denied because the grounds alleged do not support a motion to dismiss. Furthermore, OPC's motion should be denied because it was not filed on a timely basis pursuant to Rule 28-106.204(2), Florida Administrative Code. (VACCARO, WILLIS)

STAFF ANALYSIS: OPC argues that the 1995 test year used in this case can no longer set rates which are just, reasonable and compensatory, as required by Section 367.081(2)(a), Florida Statutes. In support of its argument, OPC raises two points: 1) LUSI's 1995 test year does not reflect typical conditions in the immediate future; and 2) the information filed by LUSI in this docket is not sufficiently reliable for setting rates.

With regard to its first point, OPC states that the test year is a tool used to reach rates which are just, reasonable and compensatory. The propriety or impropriety of the test year depends on how well it accomplishes the objective of determining a fair rate of return in the future. To that end, OPC asserts that "the test period should be based on the utility's most recent actual experience with such adjustments as will make the test period reflect typical conditions in the immediate future." Gulf Power Company v. Bevis, 289 So.2d 401, 404 (Fla. 1974). See also In Re: Petition for a Rate Increase by Florida Power Corporation, 92 F.P.S.C. 10:408, 415 ("The purpose of a test year is to represent the financial operations of a company during the period in which the new rates will be in effect."). OPC states that the 1995 test year cannot be used to set rates for the future, because the test year does not properly match investment with customer usage. In fact, OPC asserts that the mismatch between investment and customer growth between 1995 and 1997 led to the utility overearning during 1997. OPC further asserts that the mismatch between the test year and the effective date for permanent rates will be even more aggravated if the 1995 test year is used to set rates that will take effect in 1999.

With regard to its second point, OPC states that under the test set forth in South Florida Natural Gas Company v. Public Service Commission, 534 So.2d 695 (Fla. 1988), the utility must demonstrate that its present rates are unreasonable and show by a

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preponderance of the evidence that the rates fail to compensate the utility for its prudently incurred expenses. The utility must also demonstrate that the rates fail to produce a reasonable return on investment. OPC states that the utility has failed to meet its burden based upon incorrect information filed in this docket.

Specifically, OPC cites to a staff recommendation filed in this docket on September 11, 1998, in which staff recommended that the utility's application be dismissed. OPC includes a passage from that recommendation which lists a number of instances where incorrect information was filed including, but not limited to, the following: the utility's 1997 annual report overstated income tax expenses; staff attempted to estimate utility revenues collected prior to interim but could not reconcile reported revenues with the number of reported customer bills. This made it appear that the utility understated 1997 revenues; the utility's 1997 annual report was not adjusted for numerous adjustments found during the PSC staff audit and discovery during this docket; and staff auditors had to perform a 100 percent review of all plant and rate base from the date of inception or purchase of the individual facilities, due to the lack of supporting documentation retained by the utility. OPC also states that the utility has failed to meet the aforementioned burden, because LUSI's rates prior to interim provide a reasonable return. OPC states that this is the result of LUSI's extraordinary growth. Therefore, OPC moves that LUSI's application be dismissed.

LUSI'S RESPONSE

LUSI argues that OPC's motion to dismiss must be denied based on three arguments: 1) the motion is untimely; 2) the motion does not demonstrate a legal basis for relief; and 3) the motion seeks to inject an issue regarding test year which is no longer an issue in this case.

With regard to its first argument, LUSI cites Rule 28-106.204(6), Florida Administrative Code (new uniform rule), which states:

Unless otherwise provided by law, motions to dismiss the petition shall be filed no later than 20 days after service of the petition on the party.

LUSI further states that there is no provision of law extending the time in which a motion to dismiss can be filed, and OPC has failed to make a showing of mistake, inadvertence, or excusable neglect. See Hamilton Board of County Commissioners v. FDER, 587 So.2d 1378,

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1389-90 (Fla. 1st DCA 1991). Thus, LUSI states that the motion must be denied as untimely. See In re: Petition of Florida Cities Water Company, Order No. PSC-98-1160-PCO-WS (August 25, 1998).

With regard to its second argument, LUSI states that OPC's motion fails under the standard set forth in Varnes v. Dawkins, 624 So.2d 349, 350 (Fla. 1st DCA 1993), in that OPC's motion involves factual issues and evidence. LUSI states that pursuant to Varnes, OPC has failed to challenge the sufficiency of LUSI's application to state a cause of action upon which relief can be granted. Further, LUSI states that its application and MFRs do state a proper request for rate relief pursuant to Section 367.081, Florida Statutes.

With regard to its final argument, LUSI states that the 1995 test year is no longer an issue in this case. LUSI states that it did not protest this issue in PAA Order No. PSC-97-0531-FOF-WU (First PAA Order), and pursuant to Section 120.80(13)(b), Florida Statutes, that issue was stipulated. LUSI states that OPC did not raise this issue in its protest of the Second PAA Order, and in Order No. PSC-98-1582-PCO-WU (Order Rejecting LUSI's Withdrawal), the Commission again acknowledged that this issue was stipulated. LUSI states that the absence of this issue in the Order Rejecting Withdrawal, and OPC's failure to seek reconsideration of the Order with regard to the issue of test year means that the issue is not properly before the Commission at this time.

STAFF ANALYSIS

A motion to dismiss raises as a question of law the sufficiency of the facts alleged in a petition to state a cause of action. Varnes v. Dawkins, 624 So.2d 349, 350 (Fla. 1st DCA 1993). The standard to be applied in disposing of a motion to dismiss is whether, with all allegations in the petition assumed to be true, the petition states a cause of action upon which relief may be granted. Id. When making this determination, only the petition can be reviewed, and all reasonable inferences drawn from the petition must be made in favor of the petitioner. Id.

In order to determine whether the petition states a cause of action upon which relief may be granted, it is necessary to examine the elements which must be alleged under the substantive law on the matter. All of the elements of a cause of action must be properly alleged in a pleading that seeks affirmative relief. If they are not, the pleading should be dismissed. Kislak v. Kreedian, 95 So. 2d 510 (Fla. 1957).

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The substantive law upon which the Commission derives its authority to grant rate relief is Section 367.081(2)(a), Florida Statutes, which provides, in relevant part, that

[t]he commission shall, either upon request or upon its own motion, fix rates which are just, reasonable, compensatory, and not unfairly discriminatory.

By its application, the utility seeks increased rates and service availability charges. LUSI's application states the following:

LUSI's water operations in Lake County are not receiving rates which are just, reasonable, and compensatory. These operations are earning below a reasonable rate of return. The requested rate increase is necessary to provide LUSI with the opportunity to earn a fair rate of return on its investment in property used and useful in the public service.

Pursuant to the requirements of Varnes v. Dawkins, LUSI sufficiently states a cause of action upon which relief can be granted. Therefore, OPC's motion to dismiss should be denied on this regard.

OPC's arguments regarding LUSI's test year involve ultimate issues of fact which go beyond the four corners of the petition. Matters which go beyond the four corners of the petition may not be considered in deciding a motion to dismiss. See Pizzi v. Central Bank and Trust Co., 250 So.2d 895 (Fla. 1971). See also Lewis v. Barnett Bank of South Florida, 604 So.2d 937, 938 (Fla. 3d DCA 1992). Therefore, looking only at the four corners of the application, if the application is viewed in the light most favorable to LUSI and all allegations in the application are considered to be true, OPC's motion to dismiss should fail on this ground. See Varnes at 350. Again, OPC's motion to dismiss should be denied in this regard.

Staff notes that LUSI's argument regarding the applicability of the test year issue to this proceeding are no more appropriate for consideration at this point than OPC's arguments on the subject contained in the motion to dismiss. In any case, staff notes that the Commission has the inherent power to consider all pertinent information, whether contained in a stipulated issue or not, when setting just, reasonable and compensatory rates for the future. At the November 3, 1998, agenda conference, the Commission considered LUSI's notice of withdrawal. The Commission decided to reject LUSI's notice of withdrawal and go forward with the hearing in this

matter. With regard to the concern regarding the ability to set just, reasonable and compensatory rates in light of the 1995 test year and subsequent customer growth of the utility, the Commission stated that it would

move forward with the case and make whatever adjustments we have to do in that case to come up with an appropriate rate structure, and rates, and refunds, and if the utility is still not forthcoming with the necessary information . . . [staff] could come back with a recommendation that we dismiss it on our own motion.

Section 367.081(2)(a), Florida Statutes, requires that the Commission fix rates which are just, reasonable, compensatory, and not unfairly discriminatory. Pursuant to Section 367.121(1)(g), Florida Statutes, the Commission has the power to do all things necessary to the full and complete exercise of its jurisdiction. Further, Section 367.121(1)(b), Florida Statutes, grants the Commission the power to prescribe fair and reasonable rates. Therefore, the Commission may consider the effect of the 1995 test year in setting LUSI's rates.

Further, LUSI argues that Rule 28-106.204(2), Florida Administrative Code, requires that motions to dismiss a petition shall be filed no later than 20 days after service of the petition unless otherwise provided by law, and the law does not provide otherwise. OPC filed its motion on February 2, 1999. Staff is cognizant of the fact that the uniform rules became effective on July 1, 1998, and LUSI's application was filed back in June of 1996. However, there is no provision in the uniform rule indicating that it does not apply to cases begun prior to the effective date of the rule.

Staff notes, however, that the Commission on its own motion, can dismiss the utility's application. In fact, on September 11, 1998, staff recommended that the Commission dismiss LUSI's application on its own motion, based on inaccurate information filed by the utility and because of the staleness of the 1995 test year. Staff also recommended that the Commission deny LUSI's notice of withdrawal of settlement offer and PAA. By Order No. PSC-98-1582-PCO-WU, issued November 25, 1998, the Commission rejected LUSI's notice of withdrawal. However, at the November 3, 1998, agenda conference, the Commission did not approve staff's recommendation to dismiss LUSI's application. As discussed earlier, the Commission decided to proceed with a hearing and indicated that it would make whatever adjustments were necessary to come up with appropriate rate structure, rates and refunds. Since

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that time, there have been no changes in circumstances which warrant deviation from the Commission's prior decision in this matter. Based on the foregoing analysis, staff recommends that OPC's motion to dismiss should be denied. Staff notes that its recommendation is consistent with past Commission action. See In re: Petition of Florida Cities Water Company, Order No. PSC-98-1160-PCO-WS (August 25, 1998). By that Order, the Commission denied OPC's motion to dismiss a petition for limited proceeding filed by Florida Water Services Company, because the motion was filed beyond 20 days of the petition and involved ultimate issues of fact.

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ISSUE 3: Should this docket be closed?

RECOMMENDATION: No, this docket should remain open in order to proceed to hearing on OPC's petition. (VACCARO)

STAFF ANALYSIS: If the Commission approves staff's recommendation in Issue 1 of this recommendation, this docket should remain open in order to proceed to hearing on the OPC's petition.