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November 3, 1999

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RECORDS AND REPORTING

ORIGINAL

Ms. Blanca Bayo
2540 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

Re: Docket No. 981220-WS - Application for transfer of Certificates Nos. 592-W and 509-S from Cypress Lakes Associates, Ltd. to Cypress Lakes Utilities, Inc. in Polk County Florida.

Dear Ms. Bayo:

Pursuant to discussion with the Clerk's office today, enclosed for filing are the original and ten copies of the following documents:

1. Brief of Cypress Lakes Utilities, Inc.
2. Motion by Cypress Lakes Utilities, Inc. to file post-hearing documents in excess of the page limit set forth in Rule 28-106.215, F.A.C.

Thank you for your assistance. If there are any questions, please let me know.

Sincerely yours,



Ben E. Girtman

Encls.

AFA	_____
APP	_____
CAF	_____
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WAW	_____
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Brief
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Motion
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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

ORIGINAL

In re: Application for transfer)
of Certificate Nos. 592-W and)
509-S from Cypress Lakes)
Associates, Ltd., to Cypress Lakes)
Utilities, Inc., in Polk County.)
_____)

DOCKET NO. 971220-WS

Filed: November 3, 1999

BRIEF
of
CYPRESS LAKES UTILITIES, INC.

including
STATEMENT OF ISSUES AND POSITIONS,
COMMENTS ON PRIOR COMMISSION ORDERS,
and
PROPOSED FINDINGS OF FACT AND CONCLUSION OF LAW

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DOCUMENT NUMBER-DATE

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FPSC-RECORDS/REPORTING

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ATTACHMENT "A", Comments on Prior Commission Orders

ATTACHMENT "B", Proposed Findings of Fact and Conclusions of Law

I. BACKGROUND -

A. The Case

Utilities, Inc. (Buyer) entered into a contract on August 20, 1997, to purchase the assets of Cypress Lakes Associates, Ltd. (Seller) in Polk County. [Application for Transfer, Ex. B.] Through its newly formed subsidiary, Cypress Lakes Utilities, Inc., it subsequently filed an application with the Florida Public Service Commission seeking approval for the transfer.

After considering the application, the Commission entered its Order No. PSC-98-0993-FOF-WS, on July 20, 1998, approving, as a final action, the transfer of Certificates 592-W and 509-S from Cypress Lakes Associates, Ltd., to Cypress Lakes Utilities, Inc. It also granted, as final action, the continuation of rates and charges in effect at the time of transfer, with certain requested modifications relating to a cap on residential wastewater charges and a separate charge for irrigation meters. A portion of the order was issued as a Proposed Agency Action (PAA) order which set rate base for purposes of the transfer at \$617,609 for water and \$921,439 for wastewater. [Order No. PSC-98-0993-FOF-WS, at pages 4 and 13. See also, Wenz, Direct Testimony, page 2, line 22 to page 3, line 11, and page 4, lines 12 to 16.] These amounts were determined by the Commission Staff after an audit of the utility's books and records. [Wenz, Direct Testimony, page 4, lines 19 to 20.]

In its Order, the Commission discussed its exclusion of an acquisition adjustment:

An acquisition adjustment results when the purchase price differs from rate base. In the absence of extraordinary circumstances, it has been Commission policy that the purchase of a utility at a premium or discount shall not affect the rate base calculation. The circumstances in this exchange do not appear to be extraordinary. Further, an acquisition adjustment has not been requested by Cypress Lakes. Therefore, no negative

acquisition adjustment has been included in the rate base calculation. [Order No. PSC-98-0993-FOF-WS, at page 7, quoted in Wenz, Direct Testimony, page 3, line 16 to page 4, line 3.]

On or about August 10, 1998, the Office of Public Counsel (OPC) filed a protest of the PAA Order. After several motions were disposed of, a second revised order establishing procedure, Order No. PSC-99-0383-PCO-WS, was issued on February 23, 1999. In that order, the Commission set the final schedule for hearings to consider whether a negative acquisition adjustment should be included in rate base for purposes of the transfer.

The hearing was scheduled for October 20, 1999. At the suggestion of OPC made at the preliminary prehearing conference on September 23, 1999, and at the prehearing conference on October 4, 1999, it was discussed, and finally agreed by all parties and approved by the Prehearing Officer, that based upon the prefiled testimony and exhibits, there was no need for a hearing; the prefiled direct and rebuttal testimony and exhibits of the four witnesses would be accepted into evidence; Exhibit FS-1 of witness Seidman also was accepted into evidence; the list of prior Commission orders in Exhibit FS-1 was given official recognition, and those orders would be considered as evidence.

B. The Witnesses

There were four witnesses who presented prefiled direct or rebuttal testimony: Mr. Carl Wenz and Mr. Frank Seidman on behalf of Cypress Lakes Utilities, Inc. (Cypress Lakes, or the Utility); Mr. Hugh Larkin, Jr., on behalf of the Office of Public Counsel (OPC); and Mr. Jeffrey A. Small on behalf of the Commission Staff (Staff).

Mr. Wenz is Vice President of Regulatory Matters for Utilities, Inc. and of all its 67

subsidiaries, including Cypress Lakes Utilities, Inc. In that capacity, he is responsible for all aspects of utility commission regulation for all the subsidiaries. He is a certified public accountant, has been employed by Utilities, Inc. since 1984, and has testified before the regulatory commissions in several states. He is on the faculty of the Eastern Utility Rate School which is sponsored by the NARUC Water Committee and Florida State University.

[Wenz, Direct Testimony, page 1, line 13 to page 2 line 19.]

Mr. Seidman is President of Management and Regulatory Consultants and has 30 years experience in utility regulation, management and consulting. He has testified as an expert witness in Florida, California, Indiana, Michigan, Missouri, North Carolina ands Ohio with regard to water and wastewater utilities. He has also participated in, and appeared as a witness in, many of the Florida Public Service Commission's rulemaking proceedings with regard to water, wastewater, and electric rules, as well as proceedings before the Florida Division of Administrative Hearings. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 1, line 19 to page 2, line 20.]

C. References to the Record, Testimony, and Exhibits

Because no hearing was held, there is no transcript, per se. References to the record include references to the prefiled direct and rebuttal testimony, and the exhibits approved by the Prehearing Officer at the prehearing conference.

References to prefiled testimony include the witness's name, type of testimony, page, and line number(s). Examples: [Wenz, Direct Testimony, page 6, lines 15 to 22.] and [Wenz, Rebuttal to PSC Staff Witness Small, page 2, line 20 to page 3, line 7.]

References to Exhibits include the sponsoring witness's name, witness's exhibit number,

and title of exhibit. Reference to the Application for Transfer include the Part and Paragraph numbers or the letter of the Exhibit to the Application. Examples include:

[Wenz, Ex. CW-1, Comparison of Staff Audit and Staff Recommendation for Rate Base Components.]

[Small, Ex. JAS-1, Staff Audit Report.]

[Seidman, Ex. FS-1, List of Orders for Official Recognition, Including summary of Decisions and Summary and Chart of Purchase Price to Rate Base Ratios.]

[Larkin, Ex. HL-1, Hypothetical Example of Windfall to Company caused by Excessive Rates if a Negative Acquisition Adjustment is Not Adopted.]

[Application for Transfer, Ex. C.]

[Application, , Part I, Para. E., Part II, Para. A., and Ex. H, Articles of Incorporation.]

References to prior Commission orders include the Order number, date issued, and the Docket number.

D. Cypress Lakes Utilities, Inc. (Buyer)

Cypress Lakes Utilities, Inc., was incorporated in Florida on September 23, 1997, and is a wholly owned subsidiary of Utilities, Inc., which was incorporated in Illinois in 1965.

[Application, , Part I, Para. E., Part II, Para. A., and Ex. H, Articles of Incorporation.]

With recent additions, Utilities, Inc. now has 67 subsidiaries in fifteen states, including fourteen systems in Florida. The subsidiaries own and operate water and/or wastewater utilities serving approximately 200,000 customers, of which 63,000 are in Florida. [Wenz, Direct Testimony, page 2, lines 2 to 10, and Application,, Part II, Para. A.] For a listing of all except the most recently added systems, see Application, Ex. A, Wholly Owned Subsidiaries.

E. Cypress Lakes Associates, Ltd. (Seller)

The Seller has been providing water and wastewater services to its customers in Polk County pursuant to Commission Certificates 592-W and 509-S.

Mr. Wenz testified that the prior owner of the utility also is the developer the mobile

home community being served by the utility. When the utility was first established, it was under the rate jurisdiction of Polk County, but initially was exempt from Polk County regulation because there were no separately identified utility costs. That exemption was lost, and the utility filed for a Polk County franchise in 1995, which was granted in 1996. The prior owner is continuing as an active developer, but is not interested in operating the utility. [Wenz, Direct Testimony, page 7, lines 6 to 16.]

The PSC Staff witness, Mr. Jeffrey Small, testified about the Seller's rate case history:

On May 14, 1996, the Board of Commissioners of Polk County adopted a resolution pursuant to Section 367.171, Florida Statutes, declaring that privately owned water and wastewater utilities in that county were subject to the provisions of Chapter 367, Florida Statutes. However, Polk County retained jurisdiction over Cypress Lakes Associates, Ltd. whose initial rate request was under its consideration at that time. On August 6, 1996, Polk County established initial rates, miscellaneous fees, and service availability charges for Cypress Lakes Associates, Ltd.

By Order No. PSC-97-0569-FOF-WS, issued May 20, 1997, in Docket No. 961334-WS, the Commission granted a Grandfather Certificate and adopted the initial rates and charges established by Polk County for Cypress Lakes Associates, Ltd. The utility was able to provide sufficient historical records and supporting source documentation for the audit staff to compile CIAC and associated accumulated amortization of CIAC for the water and wastewater utilities as of December 31, 1997. . . . [Small, Direct Testimony, page 7, lines 5 to 19.]

Environmental standards for the utility are set by the Florida Department of Environmental Protection (DEP). [See, Application, Ex. C.]

F. Purpose of the Commission Policy

A major purpose for the current Commission policy on acquisition adjustments is to provide an incentive for larger utilities to acquire small, troubled utilities. [Order No. 25729,

Order Concluding Investigation and Confirmation Acquisition Adjustment Policy, issued on February 17, 1992, in Docket No. 891309-WS, at page 3.]

G. Purchaser's Reliance on Existing Commission Policy

When making its decision to purchase Cypress Lakes Associates, Ltd., Utilities Inc. was aware of, and relied on, the established Commission policy on acquisition adjustments. Utilities, Inc. has purchased several utilities in Florida, and the Commission's policy on acquisition adjustments has entered into the decision to purchase each of them. [Wenz, Direct Testimony, page 6, line 16 to page 7, line 2.]

Mr. Wenz testified that he was familiar with the Commission's policy on acquisition adjustments for water and wastewater utilities.

. . . My understanding of this Commission's policy is that, in the absence of extraordinary circumstances, the purchase of a utility at a premium or a discount shall not effect the rate base calculation. That is, the purchaser stands in the shoes of the seller. My understanding is based on my experience purchasing and operating utilities in Florida under this Commission's jurisdiction and on reading the Commission's orders establishing, investigating and reconfirming its policy on acquisition adjustments. [Wenz, Direct Testimony, page 6, lines 4 to 14.]

The Commission has already found that the transfer in this case is in the public interest in its order approving transfer. [Order No. PSC-98-0993-FOF-WS, issued July 20, 1999, at page 3.] To change the policy on acquisition adjustments now, during pendency of this case and after the fact of entering into a contract to purchase Seller, not only would be a denial of due process but it also would defeat the purposes of the policy as originally developed and implemented by the Commission.

H. Benefits to Customers

As discussed in Order No. 25729 issued in the investigation docket, Docket No. 891309-WS, the Commission's existing policy on acquisition adjustments translates into several benefits for the customers which result from the new ownership of utilities purchased under that policy. Conversely, in that investigation docket, OPC had proposed changes in the negative acquisition policy that it is trying to implement in this docket, and the Commission rejected those proposals. Order No. 23376 stated that: "Not only might OPC's proposed change not benefit the customers of troubled utilities, it might actually be detrimental, by removing any incentive for larger utility companies to acquire distressed systems." [Order No. 23376, issued August 21, 1990, in Docket No. 891309-WS, at page 3.]

Utilities, Inc. is not a developer, and its only business is to own and operate water and wastewater utilities. [Wenz, Direct Testimony, page 7, lines 18 to 21.] It has the financial ability, and, assuming fair ratemaking treatment by the Commission, it is willing to commit funds to the operation of Cypress Lakes Utilities. [Wenz, Direct Testimony, page 8, lines 14 to 23.] Utilities, Inc. can attract capital at reasonable costs. [Wenz, Direct Testimony, page 9, lines 1 and 2.] Utilities, Inc. also has the necessary professional and experienced utility management, in that it operates 67 water and wastewater utilities in fifteen states, and it has an established management team and access to professional operators in Florida. [Wenz, Testimony, page 9, lines 4 to 9.]

Utilities, Inc. can benefit from economies of scale in its operation because: 1) it already has experienced management in place in Florida, so it will not be necessary to obtain management just for Cypress Lakes; 2) Cypress Lakes will be allocated a portion of the overall

management expense; and 3) equipment and supply purchases for Cypress Lakes will benefit from the established vendor resources already being used for sister systems in Florida. [Wenz, Direct Testimony, page 9, lines 11 to 20.]

There is no credible evidence to suggest that any benefit that comes to the purchaser (as a result of the Commission's policy on acquisition adjustments) is at the expense of the customers. If a benefit results from the purchase price being lower than book value, it is at the expense of the seller, not at the expense of the customer. It comes out of the seller's pocket, not the customers. Similarly, if the buyer paid more than book value, it is at the buyer's expense, not at the expense of the customers. The customers' position remains neutral when ownership of the utility changes, regardless of whether the buyer pays book value, less than book value or more than book value. [See the discussion in Issue 5.]

In its Order No. 25729 the Commission found that the customers of utilities acquired under its acquisition adjustment policy are not harmed, and indeed they benefit from a better quality of service at a reasonable cost. [Order No. 25729, at page 3.]

I. Detrimental Consequences of Imposing NAA

If a negative acquisition adjustment is imposed, for whatever reason, several detrimental consequences would result. If the Commission's policy were changed now, it would make unlikely any future changes in ownership of "troubled" water and wastewater systems. With no change in ownership, many of the benefits which the Commission identified in its Order No. 25729 would not be available to the customers of a "troubled" utility.

Imposing a negative acquisition adjustment would discourage utilities such as the purchaser in this case from buying troubled utility systems. That would thwart Commission

policy and would be a detrimental consequence of a change in policy. [See, Order No. 25729, at page 3.]

And there is another matter to consider. If Seller had not been purchased, Seller would still be entitled to apply for rates based on the net original cost of assets serving the public. That is the same asset base that the Commission would deny to a purchaser if the Commission were to impose a negative acquisition adjustment.

J. The Generic Proceedings Before the Commission

In 1990, at the urging of OPC, the Commission opened a docket to inquire into its acquisition adjustment policy. [Docket No. 891309-WS.] By its PAA Order No. 23376 issued on August 21, 1990, the Commission reaffirmed its policy on acquisition adjustments. OPC protested the PAA order and requested formal hearings. The PSC opened a full investigation and held hearings at which OPC and other interested persons, including utility companies, presented their views on July 29, 1991.

In the Investigation proceeding, OPC unsuccessfully tried to make "prior maintenance" a basis for granting acquisition adjustments. It also tried to shift the burden of proof from the proponent of the acquisition adjustment so it would always be on the utility company. [See, Order No. 23376, issued August 21, 1990, and Order No. 25729, issued February 17, 1992, in Docket No. 891309-WS.]

On February 17, 1992, the Commission issued its Order No. 25729 reaffirming its acquisition adjustment policy which had been developed, and which had been in place and followed, at least since 1983. One case was found in 1982. [See Attachment "A" to this Brief.]

Those two Orders in Docket No. 891309-WS discussed the pros and cons of negative

acquisition adjustments, and set forth arguments by OPC and by participating utility companies regarding acquisition adjustments, particularly relating to negative acquisition adjustments. The Commission specifically considered the arguments made by OPC and rejected OPC's effort to change the acquisition adjustment policy.

See also, the discussion in Issue 8 for the origin of the 107 cases cited in Exhibit FS-1.

K. Net Original Cost

Since 1971, when the Florida Legislature removed from the statutes any reference to the "fair value" ratemaking concept, the Commission has set rates based not on so-called "worth" or "value," but on the cost of utility property when first dedicated to public service. [See, Section 367.081(2)(a)1., Fla. Stat.]

For ratemaking, the Commission has interpreted "cost basis" to mean the original cost of property when first dedicated to public service. That interpretation applies not only in the context of acquisition adjustments, but elsewhere as well. [Order No. 25729]

L. Earnings and Depreciation Expense

In the past, the Commission has considered the question of whether the acquiring utility should recover depreciation expense on the original cost of the assets. The Commission found that it is appropriate to do so. From the customer's point of view, nothing changes as a result of a change in ownership. In its Order No. 25729, the Commission stated:

We still believe that our current policy provides a much needed incentive for acquisitions. The buyer earns a return on not just the purchase price but the entire rate base of the acquired utility. The buyer also receives the benefit of depreciation on the full rate base. Without these benefits, large utilities would have no incentive to look for and acquire small, troubled systems. The customers of the acquired utility are not harmed by this policy

because, generally upon acquisition, rate base has not changed, so rates have not changed. Indeed, we think the customers receive benefits which amount to a better quality of service at a reasonable rate. [Emphasis added. Commission Order No. 25729.]

If the current Commission policy is followed in the case and there is no negative acquisition adjustment to rate base, the utility will not earn an excessive return. It will continue to be afforded the opportunity to earn a fair return on the net original cost of the assets, used and useful in serving the public.

M. Purchase Price

Mr. Larkin's argues that a negative acquisition adjustment must be included in rate base merely because the assets were purchased for less than net book value. This is simply a statement of his prior argument against current, established Commission policy. Mr. Larkin doesn't agree with that policy, but the matter was settled by the Commission in its investigation, Docket No. 891309-WS, and it has been adhered to since at least 1983.

N. Lack of Authority to Change Current Policy On a Case-by-Case Basis

Chapter 120, Fla. Stat., prohibits a state agency from changing its policy statements without full notice to all affected entities and a right to a formal hearing in which all affected entities can participate. Such a change cannot occur on a case-by-case basis, and incipient rulemaking is no longer available. See also the discussions in Issue 5 and in Issue 8.

O. Uncontroverted Evidence in the Record

Except for the ultimate issue of whether there should be a negative acquisition adjustment, all of the testimony of the Utility's witnesses, Mr. Wenz and Mr. Seidman, is uncontroverted. Except for the specific audit adjustments testified to by Mr. Wenz, the

testimony of the Staff witness, Mr. Small, is uncontroverted. OPC's witness testified about matters applicable only to a rate case and which are not applicable to setting rate base for purposes of transfer. For a summary of Mr. Larkin's testimony, see Issue 5.

II. STATEMENT OF ISSUES AND POSITIONS -

The following are the issues in this case, followed by the position of Cypress Lakes on each issue and a discussion of evidence as to each issue.

SUMMARY OF THE OVERALL POSITION OF CYPRESS LAKES:

Rate base for transfer purposes is \$617,609 for water and \$921,439 for wastewater. In accordance with established Commission policy, no acquisition adjustment should be included in the rate base calculation. The purchaser has not requested any such adjustment, and there are no extraordinary circumstances to warrant it.

ISSUE 1: **What was the condition of the assets sold to Cypress Lakes Utilities, Inc.?**

Position: *Both the water and wastewater systems appeared to be in satisfactory condition, with no outstanding operating violations.*****

OPC took no position on this issue.

A. Inspection of the Plant

Prior to purchase, Utilities, Inc. had the utility system inspected by its representatives. During the inspection, they found that both the water and wastewater systems appeared to be in satisfactory condition, with no outstanding operating violations. [Wenz, Direct Testimony, page 10, lines 1 to 10.] More specifically,

... The water plant appears to be in satisfactory condition and meets applicable standards set forth by the Department of Environmental Protection. The wastewater plant has problems with capacity during the peak flow periods and requires expansion to meet future and existing flow demands. The need for expansion is addressed in the internal memorandum from FDEP . . . which indicates that the plant capacity is already exceeded. Expansion will be required to serve additional units. Operational problems with the facility are evident during peak flow periods as evidenced by the warning letter presented by FDEP These problems are partly due to inadequately sized facilities.

In order to resolve these problems, meetings were held with the seller and his engineer to determine the required improvements. A preliminary list of plant improvements was developed by their engineer to meet future capacity requirements This list was discussed at a meeting with the engineer and several changes were suggested by Utilities, Inc. due to the close proximity to residences when the plant reaches buildout. . . .

Preliminary cost estimates for the plant expansion were developed [Application, Exhibit C.]

Mr. Larkin's testimony does not mention that he ever inspected the utility system prior to preparing his testimony, and therefore, upon information and belief, it appears that he never even visited the plant. In addition, Mr. Larkin is not an engineer and was not in a position to judge the condition of the facilities.

Therefore, any interpretation of Mr. Larkin's testimony or the conclusions he reached, requiring an inspection of the utility system, would be invalid.

B. Plant Condition as a Basis for Purchase Price

Just because a utility is purchased at less than net book value, it does not mean that there is anything wrong with the plant and facilities. In this case, there was an arm's length, negotiated purchase. The seller's motivation for selling could have been based upon the losses being sustained by the utility and by the developer. [See, Issue 2.] Investment is required to bring the system up to proper standards. [See, the discussion of discrepancies above in this Issue 1.]

ISSUE 2: Was Cypress Lakes Associates, Ltd. a “troubled” system?

Position: *Yes. Agree with Staff.*****

The utility's annual reports filed with the Commission during the two years the utility was under PSC jurisdiction show that the utility sustained cumulative losses of over \$138,000 and had a negative equity position equal to that amount. These reports also show that, for the same period, the mobile home park had sustained cumulative losses of \$2.3 million which translated to a negative equity position of the same magnitude. [Wenz, Direct Testimony, page 8, lines 1 to 12.]

OPC has taken no position on this issue.

ISSUE 3: Are there any extraordinary circumstances which warrant an acquisition adjustment to rate base, and if so, what are they?

Position: *No. Agree with Staff.*****

With regard to whether there was anything extraordinary about this utility or the circumstances leading up to its purchase, Mr. Wenz testified that, although the purchase price paid by Utilities, Inc. was lower than the rate base reflected on the books of the utility [Wenz, Direct Testimony, page 5, lines 18 to 21], there were nothing extraordinary about the utility or the circumstances leading up to its purchase. The purchase price and the circumstances of sale “. . . were pretty much like those of the other utilities we have purchased in Florida.” [Wenz, Direct Testimony, page 11, lines 5 to 9.]

Furthermore, the Commission has recently addressed the issue of negative acquisition adjustment with regard to the acquisition of the assets of Econ Utilities Corporation by Wedgefield Utilities, Inc., another subsidiary of Utilities, Inc. In that case, after thorough hearings, the Commission found that “. . . extraordinary circumstances did not exist, that price differential alone did not constitute an extraordinary circumstance, and that in accordance with past practice, a negative acquisition adjustment would not be imposed.” [Wenz, Direct Testimony, page 12, lines 1 to 9; see also, Order No. PSC-98-1092-FOF-WS, at pages 20 and 21.]

The ratio of purchase price to rate base paid for Cypress Lakes (53.28%) is above the middle of the range of the ratios of purchase price to rate base paid in the other cases decided by the Commission. [Seidman, Ex. FS-1, table at page 11 and chart at page 12.] The ratio of purchase price to rate base was much lower in the Wedgefield transfer than in the Cypress Lakes transfer, and there were no circumstances in the purchase of Cypress Lakes that were

not previously addressed by the Commission in the Wedgefield case. [Wenz, Direct Testimony, page 12, lines 11 to 19.]

Mr. Larkin's testimony does not even claim that any extraordinary circumstances exist in this case. [See the entire Larkin, Direct Testimony; Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 7 to 9.] No evidence of any kind was presented to show that any extraordinary circumstances existed in regard to this transfer.

A negative acquisition adjustment is considered at the time of transfer and requires that extraordinary circumstances be found for taking the extreme step of permanently reducing the net original cost as rate base. A used and useful adjustment is sometimes made in a rate case for temporarily removing from rate base certain assets which are not currently used and useful in providing utility service to the customers. The two regulatory concepts perform different functions at different times. [See, discussion in Issue 5.]

OPC took no position on this issue.

ISSUE 4: What is the net book value for the water and wastewater system?

Position: *Agree with Staff. Net book value is \$617,609 for water and \$921,439 for wastewater.*****

The net book value of the assets is not in dispute. The CIAC is properly accounted for, the depreciation is properly accounted for, and the net book value is \$617,609 for water and \$921,439 for wastewater. This agrees with the amounts in the Staff audit, as adjusted in the Staff Recommendation and in the PAA Order.

OPC took no position on this issue. However, the OPC witness did assert that, “Cypress Lakes Associates, Ltd. did not maintain books and records that showed the actual investment in the water and wastewater facilities.” [Larkin, Direct Testimony, page 2, lines 19 to 20.] To the contrary, what the Staff auditor stated was that it was his opinion that the utility had not maintained its records in accordance with the NARUC Uniform System of Accounts. [Small, Direct Testimony, page 3, lines 9 to 22.] Mr. Small summarized his audit process [Small, Direct Testimony, page 2, line 15 to page 3, line 2], and he did not express any concern about being unable to complete his audit work in a satisfactory manner, for lack of books and records or for any other reason.

ISSUE 5: Should a negative acquisition adjustment be included in the rate base determination?

Position: *****No. Agree with Staff.*****

Mr. Larkin's testimony does not claim that any extraordinary circumstances exist in this case. [See the entire Larkin, Direct Testimony; Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 7 to 9.] Mr. Larkin did claim that there were reasons other than extraordinary circumstances for his recommendation to include a negative acquisition adjustment in rate base. However, as pointed out by Mr. Wenz,

 . . . none of [those concerns] have anything to do with an acquisition adjustment. All of the concerns he has voiced are proper matters for consideration in setting rate base in a rate case. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 11 to 19.]

And as pointed out by Mr. Seidman,

 . . . Whatever concerns Mr. Larkin has raised are appropriately examined in the context of a rate proceeding and have nothing to do with evaluating the appropriateness of an acquisition adjustment. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 3, line 24 to page 4, line 2.]

Mr. Larkin asserted that “. . . it is always appropriate to record a negative acquisition adjustment.” [Larkin, Direct Testimony, page 2, lines 8 to 14.] That is true (assuming the purchase price is below the previously established rate base). Mr. Wenz testified that:

 . . . It is not only appropriate, but the recording of an acquisition adjustment, positive or negative, is required by the NARUC Uniform System of Accounts (USOA) to which this Commission adheres. [Emphasis added. Wenz, Rebuttal Testimony to OPC Witness Larkin, page 2, lines 1 to 7.]

However, recording an acquisition adjustment for USOA purposes is significantly

different than recognizing it for ratemaking purposes.

. . . The USOA requires an acquisition adjustment to be recorded, but it leaves it to each Commission's discretion how to treat it for ratemaking purposes. The policy of this Commission is quite clear: In the absence of extraordinary circumstances, the purchase of a utility at a premium or discount shall not affect the rate base calculation. See, PAA Order No. PSC 98-0993-FOF-WS issued July 20, 1998, in this case. Also see, Order No. 20707, issued February 6, 1989, in Docket No. 880907-WU; Order No. 23970, issued January 1, 1991, in Docket No. 900408-WS; Order No. 25584, issued January 8, 1992, in Docket No. 910672-WS; Order No. PSC-95-0268-FOF-WS, issued February 28, 1995, in Docket No. 940091-WS; Order No. PSC-96-1320-FOF-WS, issued October 30, 1996, in Docket No. 950495-WS. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 2, line 15 to page 3, line 5.]

As pointed out by Mr. Wenz, the concerns expressed by Mr. Larkin are his general concerns in any purchase and transfer, but they are not specific to this case. He never presented any evidence that they occurred for this utility, and he never even alleged that they exist in this case, only that they might exist. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, line 22 to page 4, line 1, and page 6, lines 1 to 5.]

So, what were Mr. Larkin's concerns? [See, Larkin, Direct Testimony, page 3, line 3 to page 4, line 17; and page 6 line 15 to page 7, line 1.] Mr. Wenz responded to all of Mr. Larkin's concerns.

Mr. Larkin is concerned that the original owner, a developer, might have overbuilt the system. That is clearly an issue of used and useful to be addressed in a rate case, not in determining whether a negative acquisition adjustment should be included in rate base. Mr. Larkin expressed concern that assets may have deteriorated at a rate greater than reflected in the book depreciation rate. Of course, they also may have deteriorated at a lesser rate. Regardless, this is a normal consideration in a rate case and can be addressed, if appropriate, by adjusting

depreciation expense. Mr. Larkin expressed concern that the prior owner may not have properly installed or maintained the system in order to keep rates down. If so, then the lower rates over that period of time reflect the fact that customers were not being improperly charged for something they didn't receive. If the issue is whether deferred maintenance or improper installation may have resulted in higher long run costs, that again is properly addressed in a rate case.

Mr. Larkin has expressed concern that the method of allocating overhead costs, which is at issue in a pending rate case of another subsidiary of Utilities, Inc.[,] may result in an increase in the rates of the customers of Cypress Lakes. That is speculative, irrelevant, a proper concern in a rate proceeding and is not a basis for a negative acquisition adjustment to rate base. There is no rate case pending for Cypress Lakes. When and if there is one, the legitimacy of expenses, including overhead expenses, is properly scrutinized in that arena. And it is certainly speculative to conclude that even if overhead expenses are allocated to Cypress Lakes, that they would not be offset by a decrease in other expenses.

Again, none of these concerns are properly addressed in determining whether an acquisition adjustment should be recognized in rate base. [Emphasis added. Wenz, Rebuttal Testimony to OPC Witness Larkin, page 4, line 5 to page 5, line 22.]

Mr. Larkin testified that he believed that the purchase price paid is the market value of the utility, that market value reflects true economic value, and that the ratepayer should be charged based on that "true" economic value. [Larkin, Direct Testimony, page 4, line 19 to page 5, line 1.] In his rebuttal testimony, when asked if that position is consistent with regulatory requirements in Florida, Mr. Wenz responded:

No. That is consistent with the fair value ratemaking concept. Florida is an original cost state. Further, based on Mr. Larkin's statement, the Commission would also be required to accept positive acquisition adjustments to rate base as well as negative adjustments, since he believes customers should pay

based on his definition of “true” value. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 6, lines 7 to 20.]

Mr. Larkin’s testimony erroneously suggests that if the Commission does not recognize a negative acquisition adjustment, the purchasing utility will earn an unreasonable rate of return. [Larkin, Direct Testimony, page 5, line 3 to page 6, line 12, and Larkin, Ex. HL-1, Hypothetical Example of Windfall to company caused by Excessive.]

The Commission has determined otherwise. Under the ratemaking authority granted this Commission in Section 367.081, Fla. Stat., it must set rates based on cost, specifically the original cost of the utility property when first dedicated to public service. This has been the law since 1971. The Commission recognized this interpretation of the law in its investigation Order No. 25729. Mr. Seidman testified that it is Commission policy to allow a rate of return on the full original cost rate base and include the depreciation expense on that amount in its rate recovery. Quoting the Commission’s order, Mr. Seidman stated:

‘ . . . [T]he buyer earns a return on not just the purchase price but the entire rate base of the acquired utility. The buyer also receives the benefit of depreciation on the full rate base. . . . The customers of the acquired utility are not harmed by this policy because, generally, upon acquisition, rate base has not changed so rates have not changed.’ [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 5, lines 6 to 14, quoting PSC Order No. 25729, issued February 17, 1992, in Docket No. 891309-WS.]

Mr. Wenz also responded to Mr. Larkin’s suggestion of excessive earnings by stating:

. . . without a negative acquisition adjustment to rate base, the utility will be allowed to earn a fair return and recover depreciation expense on the net original cost of the assets actually invested on behalf of the customers, when those assets were first committed to public service. No more, no less. A change of ownership does not change that fact. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 4, line 23 to page 5, line 11.]

Mr. Seidman testified that, based on the Commission policy of allowing no acquisition adjustment to rate base, the net effect is zero because:

. . . the buyer is essentially stepping into the shoes of the seller, the assets serving the customers remain unchanged, the cost of those assets remain unchanged, rate base remains unchanged and the basis for rates remains unchanged. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 5, lines 16 to 24.]

But what if the Commission did allow a negative acquisition adjustment. What would be the consequences? Mr. Seidman responded:

Since all of the concerns discussed by Mr. Larson are rate case issues, a negative acquisition adjustment would have the effect of making permanent, irreversible used and useful and expense adjustments. In addition, when used and useful adjustments are to be made in a future rate proceeding, the utility would be penalized again because the used and useful adjustment would be applied to a rate base that is already less than the cost incurred in making the assets available to the customer. Finally, and ironically, it would thwart conservation of scarce resources by sending a signal to customers that the cost to treat and dispose of wastewater is less than is actually incurred. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 6, lines 1 to 18.]

Mr. Larkin also testified on the subject of negative acquisition adjustments in the Wedgefield Utilities case, Docket No. 960235-WS, involving the purchase of assets of Econ Utilities. Mr. Wenz and Mr. Seidman also testified in that case, on behalf of Wedgefield Utilities, which also is a subsidiary of Utilities, Inc. In regard to that case, Mr. Seidman testified that,

. . . In that case I did extensive research into the historical development of the policy of this Commission on acquisition adjustments. Nothing in that research and nothing in the Commission's policy development supports Mr. Larkin's suggestion of a negative acquisition adjustment to rate base for Cypress Lakes. [Seidman, Rebuttal Testimony to OPC Witness

Larkin, page 4, lines 4 to 21.]

So, should there be a negative acquisition adjustment? According to Mr. Seidman:

No. The policy of this Commission is that absent extraordinary circumstances, the purchase of a utility at a premium or discount shall not effect the rate base calculation. Mr. Larkin has made no showing of extraordinary circumstances and therefore there is no basis for an adjustment to rate base. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 12 to 18.]

Rule 25-30.037(2)(m), F.A.C., Application for Authority to Transfer, sets forth what a utility must file with the Commission when it seeks authority for a utility transfer. The rule requires that an application for transfer must include:

(m) a statement setting out the reasons for the inclusion of an acquisition adjustment, if one is requested; . . . [Emphasis added.]

Cypress Lakes did not request an acquisition adjustment. [Wenz, Direct Testimony, page 5, lines 23 to 25.] The only proponent of an adjustment in this case is OPC. No evidence has been presented to show extraordinary circumstances warranting an acquisition adjustment. OPC has shown only a general dissatisfaction with existing Commission policy.

No acquisition adjustment should be made to rate base.

ISSUE 6: What is the rate base for the water and wastewater systems, for the purposes of this transfer?

Position: *Agree with Staff. Rate base is \$617,609 for water and \$921,439 for wastewater.*****

Mr. Wenz reviewed the Commission Staff audit and the subsequent Staff adjustments. For purposes of the transfer, Utilities, Inc. agrees with the Staff audit, as adjusted - by Staff in the Staff Recommendation - and in the PAA Order. [Wenz, Direct Testimony, page 5, lines 5 to 16.] Based on those adjustments, Mr. Wenz found that the rate base of the utility at the time of transfer was \$617,609 for the water system and \$921,439 for the wastewater system, for a combined rate base of \$1,539,048 [Wenz, Direct Testimony, page 4, lines 12 to 16] and that these Staff audit amounts correctly reflect the original cost of plant in service, net of accumulated depreciation and unamortized CIAC, at the time of transfer. [Wenz, Direct Testimony, page 5, lines 10 to 16.]

OPC takes the position that rate base should include a negative acquisition adjustment.

However,

[The proper amounts] were established by the Commission Staff after an audit of the utility's books in this docket and represent the original cost of plant in service net of accumulated depreciation and unamortized CIAC. These amounts reflect adjustments by Commission Staff that exclude some capitalized franchise costs and unaudited costs associated with phase V-1 development. They do not reflect any used and useful or other ratemaking adjustments such as an allowance for working capital. [Wenz Direct Testimony, page 4, line 18 to page 5, line 3.]

The Staff audit was prepared and sponsored by Mr. Jeffrey A. Small, a CPA and Regulatory Analyst IV in the Commission's Division of Auditing and Financial Analysis. He

has been employed by the Commission for over five years and works out of the Commission's Orlando office. He sponsored the Staff audit report. [Small, Direct Testimony, page 1, lines 6 to 10 and page 2, lines 3 to 5.]

Mr. Small's rate base analysis did not include any consideration of used-and-useful calculations or other ratemaking adjustments such as working capital allowance. [Small, Direct Testimony, page 3, lines 1 and 2, and Wenz, Direct Testimony, page 5, lines 1 to 3.]

Based on the audit and on his knowledge of the system and its records, Mr. Small initially concluded that, for purposes of the transfer, water rate base is \$582,805 for water and \$891,277 for wastewater. [Small, Direct Testimony, page 2, lines 23 to 25.] In his rebuttal testimony, Mr. Wenz addressed the differences in the audit rate base and the corrected rate base which was included in the PAA Order. Mr. Wenz confirmed that, based on the Staff Recommendation of June 18, 1998 and the PAA Order No. 98-0993-FOF-WS, the values to be approved for rate base in the final order were \$617,609 for water and \$921,439 for wastewater. [Wenz, Rebuttal Testimony to Staff Witness Small, page 2, line 8 to page 3, line 7.]

The Staff audit was filed April 6, 1998. On May 18, 1998, the utility filed a response to the audit, including corrections to certain findings. On July 18, 1998, the Staff filed its Recommendation for consideration at the agenda conference. The reason for the discrepancy was explained in the rebuttal testimony of Mr. Wenz:

. . . That [Staff] Recommendation differed in two ways from the audit report, with regard to the determination of rate base at the time of transfer. First, it included in Plant in Service, \$10,991 in water mains and \$6,868 in sewer mains that had been left out of the audit report. These were amounts for which

invoices had been provided to the auditor but were apparently overlooked. Second, in accordance with Commission policy, the Staff Recommendation determined the balances for accumulated depreciation and accumulated amortization of CIAC based on the service lives in effect at time of transfer as opposed to recalculating those balances, as the audit report did, based on the service lives stated in the Commission Rules. Commission Order PSC-98-0993-FOF-WS adopted both these adjustments. [Wenz Rebuttal Testimony to Staff Witness Small, page 3, line 16 to page 4, line 7.]

* * *

The net effect is an increase in water rate base of \$34,804 and wastewater rate base of \$30,162, as compared to the amounts testified to by Mr. Small, which did not take these proper and necessary adjustments into account. . . . Exhibit CW-1 summarizes the differences between the June 18 Staff Recommendation and the audit report for each rate component. [Wenz Rebuttal Testimony to Staff Witness Small, page 4, lines 12 to 19.]

Thus the slight discrepancies in the Staff audit on the amount of water and wastewater rate base for purposes of the transfer were updated in the Staff Recommendation, the PAA Order, and the Staff's position on Issue 6 in its Prehearing Statement.

Therefore, for purposes of the transfer, the rate base amounts should be \$617,609 for the water system and \$921,439 for the wastewater system. [Wenz Rebuttal Testimony to Staff Witness Small, page 4, lines 21 to 24. See also, Wenz, Ex. CW-1, Comparison of Staff Audit and Staff Recommendation for Rate Base Components.]

ISSUE 7: Who bears the burden of proving whether an acquisition adjustment should be included in the rate base?

Position: *The burden of proof is discussed in Order No. PSC-98-1092-FOF-WS, Docket No. 960235-WS, Wedgefield Utilities, Inc. The Utility has met its burden, but OPC has not.*****

The burden of proof was discussed in the recent Wedgefield decision, Order No. PSC-98-1092-FOF-WS. At page 8 of the Order, it stated:

We find that in the instant case, as in rate proceedings, the ultimate burden of proof rests upon the utility. . . . [W]e find that the utility must carry the ultimate burden of proof as to why an acquisition adjustment should or should not be included in the rate base calculation . . . [and] that a showing of extraordinary circumstances must be made to warrant a rate base inclusion of an acquisition adjustment. Once the utility makes an initial showing that there are no extraordinary circumstances, the burden of persuasion shifts to the opposing party to demonstrate that extraordinary circumstances are present. If the opposing party meets the burden of persuasion, the ultimate burden of rebutting the opposing party's allegations rests upon the utility. [Order No. PSC-98-1092-FOF-WS, issued August 12, 1998, in Docket No. 96-0235-WS, at page 8.]

Cypress Lakes has met its burden, and OPC has not shown, or even alleged that extraordinary circumstances exist in this case. As stated in the Wedgefield decision quoted above,

. . . Because OPC did not carry its burden of persuasion and there was no subsequent shift in the burden of proof, it was not required . . . that the utility rebut OPC's allegations and carry the ultimate burden of proof. [Order No. PSC-98-1092-FOF-WS, issued August 12, 1998, in Docket No. 96-0235-WS, at page 7.]

OPC took no position on this issue.

ISSUE 8: Must extraordinary circumstances be shown in order to warrant rate base inclusion of acquisition adjustment?

Position: *Yes. Agree with Staff. The Commission must remain consistent with its own Order Nos. 23376 (8/21/90) and 25729 (2/17/92), which confirmed the requirements for acquisition adjustments. Generic proceedings confirmed prior case-by-case development of the requirement that extraordinary circumstances must be shown before an acquisition adjustment is warranted.*****

The Commission has stated that its policy regarding acquisition adjustments has been in effect at least since 1983, and that its policy is ". . . absent extraordinary circumstances, the purchase of a utility system at a premium or discount shall not affect rate base." [Emphasis added. Order No. 25729 issued February 17, 1992, at page 1. See also, cases discussed in Attachment "A" to this Brief.]

Exhibit FS-1 contains a list of 107 cases decided by the Commission relating to both positive and negative acquisition adjustments. Generic proceedings were held in 1989 to 1992 in Docket No. 891309-WS. For the Wedgefield case (Docket No. 96-0235-WS), 99 cases were found starting as far back as January 1988, almost two years before the generic docket began. In addition, a 1982 case was found which stated that, for purposes of acquisition adjustments, "the purchaser shall stand in the shoes of the seller in the determination of the rate base". [Order No. 11266, issued October 25, 1982, and identified as Case No. 0 in Exhibit FS-1.] Since the hearing in the Wedgefield case, 7 more cases have been decided, making a total of 107 cases listed in and considered in Exhibit FS-1.

So, the Commission policy was developed on a case-by-case basis, actually beginning at least as far back as 1982. [See Attachment "A", page 1, case #0, Order No. 11266, issued October 25, 1982]. That case-by-case development was later followed by a generic proceeding

(with notice to all potentially affected persons) in 1989 to 1992 which was initiated by OPC's petition for rulemaking on acquisition adjustments. The Commission opened an investigation on the subject, and an OPC witness, now a member of the Public Service Commission, participated in that proceeding as a witness. [See, Docket No. 890309-WS. That docket and investigation resulted in Order No. 23376, issued August 21, 1990, and Order No. 25729, issued February 17, 1992.]

In the case decided in 1982, and in the 106 acquisition adjustment cases which the Commission has considered since January, 1988, the Commission has consistently followed that same policy. [See Attachment "A" to this Brief, containing a discussion and analysis of those cases dealing with acquisition adjustments.] The Commission's policy is clear and unequivocal that there will be no acquisition adjustment for ratemaking purposes, absent extraordinary circumstances.

The arguments set forth by Mr. Larkin have been made before and have been rejected by this Commission in the generic proceedings. [See, Order No. 23376 issued August 21, 1990, and Order No. 25729 issued February 17, 1992.] Even so, despite OPC's participation in the generic proceedings and hearings in 1989 - 1992, and despite OPC's participation in the Wedgefield case, and despite OPC's participation in many other cases where a negative acquisition adjustment was considered, OPC takes the position in this case that extraordinary circumstances need not be shown in order to warrant rate base inclusion of a negative acquisition adjustment. *Go figure.*

In this Cypress Lakes case, there was nothing extraordinary about the utility or the circumstances leading up to its purchase. The purchase price and circumstances surrounding

the sale “. . . were pretty much like those of the other utilities we have purchased in Florida.” [Wenz, Direct Testimony, page 11, lines 5 to 9.] The OPC witness did not even allege that extraordinary circumstances exist in this case. [See all of Larkin, Direct Testimony.]

Mr. Larkin's testimony does not make a case for extraordinary circumstances. He has only shown a general dissatisfaction with Commission policy and the outcome of applying that policy to cases before the Commission. [Larkin, Direct Testimony.] In a circuitous way, OPC is merely trying to re-argue the OPC position rejected by the Commission in Order No. 25729.

In prehearing proceedings in this docket, OPC has argued that rate base for the purposes of transfer must be set at the purchase price, if the purchase price is lower than the previously established rate base (net book value). This is the same argument OPC made in the generic investigation docket almost a decade ago. The Commission did not accept the argument.

OPC seems to view positive and negative acquisition adjustments somewhat differently. For positive acquisition adjustments, OPC believes that appropriate standards must be established for the buyer to show, and for the Commission to evaluate, the prudence of the acquisition at a premium so the sale of a utility does not increase customer rates without any new assets being devoted to utility service. But for negative acquisition adjustments OPC believes that the commission has no alternative except to automatically impose an adjustment. [Emphasis added. Order No. 25729 issued February 17, 1992 in Docket No. 890309-WS.]

OPC also has argued that the Commission does not have a rule allowing it either to deny a negative acquisition adjustment or to require a showing of extraordinary circumstances before it can grant a negative acquisition adjustment.

Rule 25-30.037(2)(m), F.A.C., Application for Authority to Transfer, sets forth what a utility must file with the Commission when it seeks authority for a utility transfer. The rule requires that an application for transfer must include:

(m) a statement setting out the reasons for the inclusion of an acquisition adjustment, if one is requested; . . . [Emphasis added.]

OPC seems to think that this rule, plus the generic proceedings which were initiated in 1989 by OPC filing a petition to initiate rulemaking, plus the PAA order and the final order in that proceeding, plus all 106 cases consistently ruling on acquisition adjustments, do not allow the Commission to apply the policy which it has followed since at least 1983 and which it reaffirmed in the generic proceeding. OPC argues that the Commission must grant a negative acquisition adjustment and set the rate base for purposes of transfer at the amount of the purchase price.

If OPC is right that there is no authority to follow the existing Commission policy on acquisition adjustments, then there is no authority to even consider, must less require, a negative acquisition adjustment, for any reason. Either the existing policy is valid or there is no policy at all and no authority for the Commission to inquire into acquisition adjustments. There have been no hearings, no notice to affected persons, and no testimony or exhibits accepted by the Commission, either deviating from the existing Commission policy or supporting such a new policy, which has been proposed repeatedly by OPC, in case after case, and rejected every time by the Commission.

The Commission cannot act “. . . inconsistently with its published regulatory philosophy.” The Commission cannot now deviate from its established policy on negative

acquisition adjustments because, “No newly promulgated rule necessitated, authorized, or justified such a policy change.” Florida Cities Water Co. v. State, 705 So.2d 620, at 625 (Fla. 1st DCA 1998). [It should be noted that several legal and procedural issues raised by amendments to the Florida Administrative Procedure Act (Ch. 120, Fla. Stat.) were not raised by the parties to the Florida Cities case, and therefore, were not decided by the Court.]

The issue of whether the current Commission policy constitutes an invalid rule has not been tested in proceedings before the Division of Administrative Hearings (DOAH), which has exclusive jurisdiction to decide that issue. OPC has repeatedly, for at least the past 11 ½ years, failed to file a petition with DOAH for that determination. In that time period, 106 cases have been decided by the Commission, consistent with the policy that “. . . absent extraordinary circumstances, the purchase of a utility system at a premium or discount shall not affect rate base.” [Emphasis added. Order No. 25729, issued February 17, 1992, at page 1.]

III. CONCLUSION -

Rate base for purposes of the transfer is \$617,609 for water and \$921,439 for wastewater. Cypress Lakes Utilities, Inc. has met its burden of proof. OPC, the only proponent of the acquisition adjustment in this case, has not met its burden of persuasion of its burden of proof. Extraordinary circumstances must be shown to warrant an acquisition adjustment, and none were shown to exist. None were even claimed to exist in this case. Therefore, no acquisition adjustment should be included in the rate base calculation.

Filed simultaneously herewith is a motion to file post-hearing pages in excess of the number provided by Rule 28-106.215, F.A.C.



ATTACHMENT "A"

COMMENTS ON PRIOR COMMISSION ORDERS

In 1989, the Public Service Commission opened Docket No. 891309-WS, a generic docket resulting from the petition of the Office of Public Counsel to initiate rulemaking to amend Rule 25-30.04(3)(o), F.A.C.¹ or in the alternative to examine its policy on *acquisition adjustments and determine if modifications were warranted*. The Commission declined to initiate rulemaking but granted OPC's request to investigate the Commission's policy on acquisition adjustments (90 FPSC 1:11). As a result of that generic investigation, the Commission confirmed its existing policy (90 FPSC 8:306; 92 FPSC 2:409). The policy, since approximately 1983, has been that absent extraordinary circumstances, the purchase of a utility system at a premium or discount shall not effect rate base (92 FPSC 2:409).

Applicant Exhibit (FS-1), identifies 107 prior orders of the Commission involving acquisition adjustments. Order No. 11266, identified as Case No. 0, issued October 25, 1982, establishes that "the purchaser shall stand in the shoes of the seller in the determination of the rate base" and sets the precedent for the Commission acquisition policy since 1983. The orders identified as Case Nos. 1 through 106 represent all of the orders issued on acquisition adjustments from January, 1988 through June, 1999. Each of these 106 orders were reviewed to determine whether the Commission has consistently applied its acquisition adjustment policy. These orders make up the statistics for the various categories of orders discussed below. These

¹ This is still a valid rule, but it has been renumbered Rule 25-30.036(2)(m), F.A.C.

Commission orders have been officially recognized, are evidence, and are part of the record.

Every order reviewed (with the exception of Case No. 53) specifically identifies the existing Commission policy as the basis for evaluating whether an acquisition adjustment to rate base would be appropriate. In addition, several of the orders include a discussions of the reasons for deciding a case on acquisition adjustments. Those orders are set forth below under these headings.

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Current Commission policy was formally established in generic proceedings by two orders, PAA Order No. 23376, issued 8/21/90 and Final Order No. 25729, issued 2/17/92. This review of orders begins with January, 1988 to provide an indication of how the policy was being established on a case-by-case basis in the two year period 1988-1989 leading up to the formal generic statement of Commission policy in 1990. The rest of the orders indicate how the Commission addressed the acquisition adjustment issue after it had formally established its policy on a generic basis.

During the 11 ½ year period for which Commission orders were reviewed there were 106 orders, excluding the PAA in this case, which addressed acquisition adjustments. Of those, 34 specifically addressed negative acquisition adjustments, 36 specifically addressed positive acquisition adjustments, and 36 others appear from the discussion to address positive acquisition adjustments, but that fact was not specifically stated in the orders.

A. NEGATIVE ACQUISITION ADJUSTMENTS (NAA)

Of the 34 orders which addressed negative acquisition adjustments, only three orders [Case Nos. 36, 62 and 69] included an adjustment in rate base. Of the remaining 31 orders in which a negative acquisition adjustment was not included in rate base, thirteen of them relied solely on a re-statement of the Commission's acquisition adjustment policy as the reason for not including an acquisition adjustment in rate base. The policy statement in each of those orders was the same as or similar to the language in other orders addressing either positive or negative acquisition adjustments. For example, Order No. 19163 (identified as Case No. 3) reads:

In the absence of extraordinary circumstances, Commission policy is that the purchase of a utility at a premium or discount shall not effect the rate base calculation. The circumstances in this transfer are not unusual or extraordinary; therefore, no positive acquisition adjustment is included in rate base. Further, the Applicants did not request that an acquisition adjustment be included in rate base. [Emphasis added.]

The remaining 18 orders which did not include a negative acquisition adjustment in rate base did contain some additional discussion (either in the majority opinion or the dissent) that gave some insight into the Commission or Commissioner's reasoning for their decisions in those cases. See Ex. (FS-1), Case Nos. 16, 19, 43, 47, 50, 53, 55, 59, 63, 65, 76, 77, 78, 83, 89, 91, 102 and 103.

B. ORDERS EXPLAINING WHY NO NAA

The following paragraphs summarize each of the 18 orders discussing why a negative acquisition adjustment was not included, and then relate those comments to Cypress Lakes's situation. Each order is identified by its case number (from No. 1 to No. 106).

Case No. 16 was a transfer case between Utility Systems, Inc. and Sunshine Utilities. The purchase price was less than rate base, but the Commission did not include a negative acquisition adjustment in rate base. The Commission stated its policy regarding extraordinary circumstances and indicated that in other orders related to a negative acquisition adjustment, it had considered whether the system was in such poor condition that it needed replacing and whether the purchase was prudent in light of such factors as jurisdictional status, growth potential and per-customer operating costs.

In Cypress Lakes's case, the system does not require replacing, the

jurisdictional status is known, there is growth potential, and the company has indicated that the system will benefit from certain economies under new ownership. The Cypress Lakes transfer meets the conditions considered in the Utility Systems, Inc. order. Therefore, there is no basis in these factors for including a negative acquisition adjustment in Cypress Lakes's rate base.

Case No. 19 was a rate case for the Marion County division of Southern States Utilities. In a previous docket for transfer of this utility, the Commission had investigated the circumstances in light of its acquisition adjustment policy and did not find them extraordinary enough to include a negative acquisition adjustment. At issue in this case was whether to reverse that ruling based on the testimony in the current record. The Commission reiterated its policy, that the buyer acquires the seller's rate base balance unless there are extraordinary conditions to justify an acquisition adjustment. It then went on to consider the testimony.

The OPC witness testified that the Commission should change its policy and shift to the utility the burden of proving that an adjustment not be included, and why, without an adjustment, customers would pay a return on the previous owner's rate base plus a return on SSU's improvements.

The SSU witness testified that a negative adjustment should not be included because the customers would benefit by SSU's ability to attract capital at a lower cost and by economies of scale and managerial and operational expertise. He also testified that the revenue requirement associated with the net original cost of the system would be no more than under the previous ownership.

The Commission noted that any improvements that had to be made were in the public interest and that there was no new evidence presented on which to alter its previous decision.

In the case of Cypress Lakes, no extraordinary circumstances were alleged, nor did OPC argue that they exist.

Case No. 43 involved a transfer from Grand Terrace to SSU. The purchase price was approximately 40% of rate base. The Order indicates that OPC outlined four points that they believe show extraordinary circumstances. OPC argued that no incentive to purchase the system was necessary because the utility was not having any problems. But the Commission responded that its policy on acquisition adjustments did not require the seller to prove hardship. OPC also argued that the seller would show the below-cost sale as a loss on its tax return. The Commission ruled the tax treatment of the seller was irrelevant. In addition, OPC argued that rate base should equal the original cost at the time the assets were dedicated to public service. The Commission agreed with the principle of rate base equal to original cost, but not with OPC's interpretation of the statute and when the assets were dedicated to public service. The Commission found that the circumstances in this transaction did not appear extraordinary, and in accordance with Commission policy, a negative acquisition adjustment was not included in rate base.

No allegations have been made by an party that extraordinary circumstances exist in the purchase of Cypress Lakes. However, the Grand Terrace case provides some guidance for the Cypress Lakes case with regard to the Commission's conclusion that rate base recognize the original cost of assets at the time they are first dedicated to public service.

This is consistent with the Commission's ruling in Order No. 25729 (the final order in the generic investigation docket, issued some 16 months following the order in the Grand Terrace case) concluding its investigation and confirming its acquisition adjustment policy.

In the Cypress Lakes case, the Applicant and the PSC Staff have presented testimony establishing net original cost as rate base.

The Grand Terrace case also provides guidance as to what Cypress Lakes does not have to prove - hardship on the part of the seller. The Grand Terrace case is consistent with the Commission's policies that 1) absent extraordinary circumstances, not to include a negative acquisition adjustment in rate base, and 2) once the utility makes an initial showing that there are *no extraordinary circumstances*, the burden of persuasion shifts to the opposing party to demonstrate that extraordinary circumstances are present.

Case No. 47 was a transfer from Springside, Inc. to Springside at Manatee. The purchase price was at 12% of rate base. In accordance with its policy, the Commission did not include a negative acquisition adjustment in rate base. The Commission stated that, although a large negative acquisition adjustment resulted, the circumstances did not appear to be extraordinary.

In the Cypress Lakes case, OPC has not alleged that the differential between purchase price and rate base is an extraordinary circumstance. Nevertheless, the Springside order, which does not find a purchase at 12% of rate base to be extraordinary, provides some guidance. The Cypress Lakes differential (53% of rate base) is not nearly as great as in Springside. Therefore, consistent with the Springside order, the Cypress Lakes price/rate base differential is not extraordinary. The Commission decision in the Springside Manatee

case relied upon and evaluated the propriety of an acquisition adjustment in accordance with its consistent policy, which is, absent extraordinary circumstances, not to include a negative acquisition adjustment in rate base.

Case No. 50 was a transfer from Pine Harbour to Pine Harbour Water Utilities at a price less than rate base. In accordance with its policy, the Commission did not include a negative acquisition adjustment. No additional explanation was given. One Commissioner dissented, asserting that there was no evidence to support the Commission's decision, and asserting that the utility should bear the burden of proving why an adjustment should not be included. He also stated that a negative acquisition adjustment may not be proper in all cases, but the dissenting opinion provided no indications of what situations may be proper.

The guidance provided to Cypress Lakes by this case is that, consistent with Commission policy, where no evidence is shown that extraordinary circumstances exist, an acquisition adjustment to rate base should not be included. No allegations of extraordinary circumstances have been made and no evidence of extraordinary circumstances has been presented in the Cypress Lakes case.

Case No. 53 was a Staff Assisted Rate Case (SARC) for The Woods, a division of Homosassa Utilities. In that case, due to a lack of original cost documentation, the original cost was determined by a Staff-prepared original cost study. The capital structure was composed solely of negative retained earnings. To balance the books, the Commission increased common equity to equal rate base "to reflect the unrecognized negative acquisition adjustment resulting from the purchase of this utility at a discount." This is a case in which the issue of an acquisition adjustment and acquisition policy was not directly

raised. However, the end result is consistent with Commission policy in that rate base was set at original cost.

One Commissioner dissented, stating that because the case involved an initial determination of rate base, the purchase price was superior to an engineering estimate. He also stated that the Commission's acquisition adjustment policy was incentive-based, and that since the original cost study was performed after the purchase, there is no evidence that an incentive was needed in the acquisition.

There are no similarities between Homosassa Utilities and Cypress Lakes. However, some guidance can be gleaned from both the majority opinion and the dissent. The determination of rate base in the Cypress Lakes transfer is not an initial determination, in that rate base had been determined earlier in another (Polk County) jurisdiction. The purchase by Cypress Lakes was made with knowledge of the rate base and of the Commission's acquisition adjustment policy, and Cypress Lakes took those factors into consideration in making the purchase. The stated concerns of the dissent in the Homosassa case are not applicable to the Cypress Lakes application.

The end result of the Homosassa case is a consistent application of Commission acquisition adjustment policy in that with no indication of extraordinary circumstances, a negative acquisition adjustment was not included in rate base.

Case No. 55 was a transfer from Hideaway Services to FIMC Hideaway resulting from a foreclosure. The purchase price was less than rate base. The Commission policy was stated. The Commission specifically noted that, even though the previous owner had failed to maintain the system properly and the new owner had to make considerable

expenditures to bring the system into compliance, these events did not appear to be extraordinary. In accordance with Commission policy a negative acquisition adjustment was not included in rate base.

One Commissioner dissented. The dissent noted that the previous owner had failed to maintain the system, that the new owner would have to spend considerable amounts to bring the system into compliance and the customer would "pay twice" and this was an extraordinary circumstance. The dissent also stated that there was no indication an incentive (i.e., no negative acquisition adjustment included in rate base) was needed or that the buyer was even aware of the Commission's policy on acquisition adjustments. Cypress Lakes was aware of Commission policy.

Inferences, not allegations, have been made by OPC in the Cypress Lakes case that facilities "may" have deteriorated due to lack of maintenance, but provides no evidence that they have. The Applicant has indicated that the systems appear to be in satisfactory condition. Nevertheless, relying on the FIMC Hideaway decision, even if such inferences relating to maintenance were correct in the Cypress Lakes case, they do not constitute extraordinary circumstances and are not a basis to include a negative acquisition adjustment in rate base.

Contrary to the dissent's statement, the customers would not have to "pay twice". As long as accounting and rate making treatment is consistent, regardless of ownership, the customers pay only for the legitimate cost of assets and expenses incurred and actually paid in their behalf. By not including a negative acquisition adjustment in rate base, neither the rate base nor the rates to customers are affected by the transfer.

Customers will not pay for anything under the new ownership that they would not have been required to pay for under prior ownership. The transfer is customer-neutral, except for the forthcoming benefits to the customers summarized in testimony by Mr. Wenz.

The FIMC Hideaway case provides continuity for the application of Commission policy, which is, absent extraordinary circumstances, not to include a negative acquisition adjustment in rate base.

Case No. 59 was a transfer of assets from San Pablo to Jacksonville Suburban (Jax). The Commission stated its acquisition policy and indicated that in this exchange, circumstances do not appear extraordinary, and therefore, did not include an acquisition adjustment to rate base. In this case, Jax, had requested that a negative acquisition adjustment not be included in rate base. The Commission noted that Jax had made improvements in the system and in its management. This was not an issue with Cypress Lakes.

The Jacksonville Suburban case continued the consistent application of the Commission's policy that, absent extraordinary circumstances, a negative acquisition adjustment not be included in rate base.

Case No. 63 was a transfer of assets from Countryside to Pennbrooke Utilities. The sale was a result of a bankruptcy and foreclosure. The Commission stated that the circumstances in this instance did not appear to be extraordinary, and in accordance with its policy, the PSC did not include a negative acquisition in rate base. One Commissioner dissented, but gave no reasons in his dissent that would provide guidance. The Pennbrooke

case continued the consistent application of the Commission's policy that, absent extraordinary circumstances, a negative acquisition adjustment not be included in rate base.

Case No. 65 was the SSU/Deltona rate case, concluded in 1993. In its post-hearing brief, OPC had argued that a negative acquisition adjustment be included in rate base. However, it did not specify the adjustments nor did it sponsor or solicit any evidence at hearing supporting its position. The SSU/Deltona case continued the application of the Commission's policies that, absent extraordinary circumstances, a negative acquisition adjustment not be included in rate base and that once the utility makes an initial showing that there are no extraordinary circumstances, the burden of persuasion shifts to the opposing party to demonstrate that extraordinary circumstances are present.

Case No. 76 was a case establishing rate base in the transfer from Lake Placid to Lake Placid Utilities, Inc (LPUI). That system was purchased out of bankruptcy by a subsidiary of Utilities, Inc. at a price less than rate base. LPUI argued that a negative acquisition adjustment was not appropriate because it would be inconsistent with the Commission's policy of encouraging the purchase of small, poorly run utilities, that the parent had made other purchases at a premium without acquisition adjustments and that purchasing at less than book value did not constitute extraordinary circumstances. Upon consideration, the Commission found that circumstances did appear to be extraordinary. Consistent with its policy, the Commission did not recognize a negative acquisition adjustment to rate base. One Commissioner dissented, but gave no guidance.

The LPUI case consistently continued the application of Commission policy that, absent extraordinary circumstances, not to include a negative acquisition adjustment in rate

base.

Case No. 77 was the transfer of Lakeside Golf to SSU at a price of approximately 40% of rate base. In accordance with its policy, the PSC did not include a negative acquisition in rate base.

The Commission noted there were no major service problems, no extraordinary circumstances, and that SSU uniform rates would be lower than the stand-alone rates would have been under the prior owner, had the prior owner been charging for service. SSU, in support of its position that a negative acquisition adjustment was inappropriate, stated that, as a starting point in its purchase negotiations with the seller, it had calculated rate base as if used and useful adjustments had been made. *It argued that to reduce rate base by a negative acquisition and then apply used and useful adjustments in the future would be double counting.*

There is no indication in the SSU order that SSU's argument was a factor in the Commission's decision. Although no estimate of used and useful adjustments has been made for Cypress Lakes, in the SSU case the utility was correct that to include both a negative acquisition adjustment and used and useful adjustments on the same plant would be double counting. Under Commission policy correlation between used and useful rate base and purchase price. The Commission, in an earlier order (see Case No. 47) indicated that price/rate base differential is not an extraordinary circumstance. Although estimated used and useful may be a factor considered by a potential purchaser in its negotiations, used and useful adjustments are never a factor in calculating rate base for purposes of a transfer. They will be a factor in a future rate case, but the calculation of used and useful is

not dependent on who owns the system.

The SSU/Lakeside Golf case continued a consistent application of the Commission policy that, absent extraordinary circumstances, not to include a negative acquisition adjustment in rate base.

Case No. 78 involved a transfer of assets from Lake Utilities, LTD to SSU. That case is similar to Lakeside Golf in Case No. 77. As a starting point in its negotiations, SSU had calculated rate base as if used and useful adjustments had been made and argued that to reduce rate base by a negative acquisition adjustment and then apply used and useful adjustments in the future would be double counting.

SSU argued that no extraordinary circumstances existed, and the Commission found that the exchange did not appear to be extraordinary. In accordance with its policy, and without further explanation, the Commission did not include a negative acquisition adjustment in rate base. One Commissioner dissented, without opinion.

This case continued a consistent application of the Commission policy that, absent extraordinary circumstances, not to include a negative acquisition adjustment in rate base.

Case No. 83 involved a transfer of assets from Tamiami Village Utility to Tamiami Village Water. The purchase price was approximately 41% of rate base. The Applicant misunderstood Commission policy and believed the Commission required an acquisition adjustment to balance the books for reporting purposes. The Commission stated that it did not view a desire to balance the books as extraordinary. In accordance with its policy, the Commission did not include a negative acquisition adjustment in rate base.

One Commissioner dissented on the basis that the Commission policy was supposed

to be an incentive, but this buyer was unaware of the policy and misunderstood the purpose of an acquisition adjustment.

This case continued a consistent application of the Commission policy that, absent *extraordinary circumstances*, not to include a negative acquisition adjustment in rate base.

Case No. 89 was a full rate case for SSU's PSC regulated systems. In that case, OPC revisited the issue of acquisition adjustment specifically with regard to the purchase of the Lehigh and Deltona systems and with regard to policy in general. It was pointed out by the Commission that both purchases were stock transfers, and acquisition adjustments were not applicable. Nevertheless, the Commission discussed the Lehigh and Deltona purchases and noted that even a showing that Lehigh was purchased at 45% of book value did not demonstrate that extraordinary circumstances exist.

The Commission went on to reaffirm its generic acquisition adjustment policy. The Commission also reiterated its observation that not including a negative acquisition adjustment does no harm to customers, because, generally, rate base and rates do not change and customers often receive a better quality of service.

The guidance this case provides is that the PSC's policy has not changed and that the differential between rate base and purchase price does not demonstrate that extraordinary circumstances exist. One Commissioner dissented, restating his basic position but also seeking to distinguish the SSU case because of the issue of uniform rates and the allegation that uniform rates result in a cross subsidy of the effect of no negative acquisition adjustment.

Uniform rates is not a factor in the Cypress Lakes case, so there are no special issues

in the SSU dissent to which to respond.

Case No. 91 was a Staff assisted rate case (SARC) for J&J Water and Sewer. The \$32,000 system was purchased for one dollar, or .003% of rate base. The Commission noted that circumstances were extraordinary due to the combination of the \$1.00 price and the sale of 91 lots to the new owner at a price of \$17,500. However, the Commission did not include a negative acquisition adjustment because of other mitigating circumstances.

The seller had filed for abandonment of the utility system, but the abandonment was put off due to the sale of the system. Furthermore, including a negative acquisition adjustment would have resulted in inadequate operating funds and might possibly have triggered another abandonment proceeding.

One Commissioner dissented, asserting that the transfer did not meet the goals of the Commission's policy because there was no incentive involved and because the sale of the utility was a by-product of the sale of the lots; the purchase was not by a large utility; and the purchaser had no previous experience.

CASE NO. 102 was a transfer of utility assets from Radnor/Plantation to IHC Realty. The utility continues to operate under the name of Plantation Utilities. The purchase price was equal to rate base at December 31, 1996 as shown in the utility's 1996 annual report. Based upon the PSC Staff audit, the Commission adjusted rate base downward by an amount that is the equivalent of approximately 4.5% of net book value. The Commission found that the intent of the buyer and seller was to transfer at a price equal to rate base. The Commission found that the circumstances in the exchange did not appear extraordinary, and nothing was found in the audit that would require an acquisition

adjustment. The Commission stated that, in the past they have determined that in the absence of extraordinary circumstances, a purchase at a premium or discount shall not effect rate base.

CASE NO. 103 was a transfer from Econ Utilities to Wedgefield Utilities, a subsidiary of Utilities, Inc. The Commission made a finding in this case that the utility must carry the ultimate burden of proof as to why an acquisition adjustment should or should not be included in rate base. But the Commission also found that 1) a showing of extraordinary circumstances must be made to warrant rate base inclusion of an acquisition adjustment and 2) once the utility makes an initial showing that there are no extraordinary circumstances, the burden of persuasion shifts to the opposing party to demonstrate that extraordinary circumstances are present. In Cypress Lakes, the Applicant made an initial showing that extraordinary circumstances did not exist and the opposing party made no allegation of extraordinary circumstances and did not carry the burden of persuasion that extraordinary circumstances were present. Thus, the burden of persuasion never shifted back to the utility.

In the Wedgefield case, the purchase price was approximately 19% of rate base. The Commission found that the purchased assets were in fair condition and not extraordinary in nature, that the purchased utility was economically troubled, that price differential alone does not constitute an extraordinary circumstance, and that there were no extraordinary circumstances that warrant a rate base inclusion of an acquisition adjustment.

One Commissioner dissented, asserting that the Commission's standard (regarding extraordinary circumstances) had been met and a negative acquisition adjustment should

have been recognized.

The Wedgefield case confirms that extraordinary circumstances must be shown to warrant an acquisition adjustment to rate base, and it continued a consistent application of the Commission policy that, absent extraordinary circumstances, not to include a negative acquisition adjustment in rate base.

C. SUMMARY OF 18 ORDERS EXPLAINING WHY NO NAA

As a summary of these 18 cases, the following are factors which the Commission considered when ruling not to include a negative acquisition adjustment in rate base:

1. Is the system in such poor condition that it needs replacing? (Case No. 16)
2. Was the purchase prudent in light of jurisdictional status, growth potential and per customer operating costs? (Case No. 16)
3. Are there benefits due to the purchaser's ability to attract capital at lower costs, economies of scale and managerial and operational expertise? (Case No. 19)
4. Is the purchaser making improvements in the public interest? (Case Nos. 19, 59)

The Commission also identified these factors as being important in considering whether to include an acquisition adjustment:

1. A showing of extraordinary circumstances must be made to warrant rate base inclusion of an acquisition adjustment. (Case No. 103)
2. Price differential alone does not constitute an extraordinary circumstance. (Case No. 47, 89, 103)

In addition to the list of factors set forth above, the Commission also has found that it was not necessary to show hardship on the part of the seller (Case No. 43) and that the failure of the previous owner to maintain the system (and considerable expenditures made by the new owners) were not extraordinary circumstances and were not reasons to include a negative acquisition adjustment in rate base. (Case No. 55).

Additional concerns raised in dissenting opinions were that the purchaser be aware of, and have considered, the "incentive" purpose of the Commission policy (Case Nos. 53, 55, 83); that uniform rates not result in cross subsidies (Case No. 89); that the purchaser be a large utility with expertise in utility operations (Case No. 91); and that customers not pay for anything twice (Case No. 55).

D. NEGATIVE ACQUISITION ADJUSTMENT APPROVED IN JUST 3 CASES

An acquisition adjustment has very rarely ever been approved. Of the 31 cases which specifically addressed the subject, a negative acquisition adjustment was approved in only 3.

Case No. 36 occurred in 1990 and addressed the purchase of the Beacon 21 water and wastewater utility by Laniger Enterprises. In that case, the Commission had, in a PAA, not included a negative acquisition adjustment in rate base. The PAA was protested by OPC. Eventually, the Applicant and OPC entered into a settlement in which they agreed that rate base be set at the purchase price. In the order accepting the settlement, the Commission noted that the OPC had alleged extraordinary circumstances. The

Commission also noted that recognition of acquisition adjustments for rate making purposes goes against its established practice. The Commission did not rule on the allegations, but in the absence of any evidence to the contrary (and with the acquiescence of the utility) it approved the settlement.

Because this was a settlement, no issues of fact were addressed. The only guidance is that, even with the stipulation of the parties, the Commission is reluctant to include a negative acquisition adjustment in rate base, and to do so goes against the Commission's established practice.

Case No. 62 was the second of the three cases in which a negative acquisition adjustment was approved. It was a Staff assisted rate case for CGD Corp. which occurred in 1993. In that case, the Commission explained that the transfer involved an extraordinary circumstance and set rate base equal to the purchase price. The Commission identified the following as extraordinary circumstances: 1) it involved a three-party, nontaxable exchange in which two of the parties, the initial developer and the final utility owner (developer family trust) were considered virtually the same; 2) the developer fully recovered its investment in the utility through the exchange, and 3) without the adjustment, the developer (i.e., the developer family trust) would allegedly double recover its investment.

None of the circumstances in the CGD Corp. case are applicable to Cypress Lakes. The Cypress Lakes transfer involved an arms length transaction between unrelated parties. There are no trusts involved.

Case No. 69 was the third and final case in which a negative acquisition adjustment was approved. It was decided in 1993, and involved a rate application for Jasmine Lakes in

which the Commission reversed its prior decision in a 1990 transfer case. In the transfer docket (Case No. 44), the Commission, based on its policy, did not include a negative acquisition adjustment. The rate case order stated that OPC had argued that: 1) the utility was in "bad shape" at the time of purchase; 2) the prior owner did not adequately maintain the utility; 3) the prior management was neglectful; and 4) a negative acquisition adjustment would insulate the customers from the failures of prior management. A majority of the Commission agreed with OPC's position that a negative acquisition adjustment was appropriate. The Commission stated that it based its decision on customer testimony, the need for repairs and improvements at the time of transfer, and the lack of responsibility of (prior) management. Also, the Commission noted that, at the time of transfer, the utility was already purchasing 80% of its water from the county, yet the utility had earned a return on the water plant components for two years.

A different Commissioner dissented from this decision, and stated three reasons: 1) the Commission had already rendered its decision on this issue in a previous order; 2) the OPC witness had testified that the purchase was not extraordinary; and 3) in the absence of extraordinary circumstances, the prior decision should remain undisturbed. That dissent is consistent with the policy and prior decisions of the Commission.

If the Commission's decision in Jasmine Lakes (Case No. 69, 11/18/93) were to be construed to include the prior owner's failure to maintain the system as a reason to include a negative acquisition adjustment, then such an interpretation would be inconsistent with its decision in the earlier FIMC Hideaway case discussed above (Case No. 55, 1/18/92, and subsequent decisions). Such an inconsistency would leave affected parties with little

guidance as to what the policy of the Commission actually is.

The Jasmine Lakes decision (Case No. 69) is more properly construed to prevent full recovery of the costs associated with water plant components in a system for which 80% of the water was being purchased from another utility system while the utility was still receiving revenues as though based on use of its entire system.

There is no similarity at Cypress Lakes to the Jasmine Lakes situation wherein allegations were made of earning on unused treatment plant while purchasing most of the water from the county. That situation does not exist in this case.

Even if the circumstances in the Cypress Lakes case were the same as in Jasmine Lakes with regard to alleged failures of the prior owners, the majority's solution in the Jasmine Lakes case cannot be interpreted to mean that prior poor maintenance is an extraordinary circumstance warranting a negative acquisition adjustment.

If the Jasmine Lakes case were to be interpreted to mean that prior poor maintenance by the previous owner were the basis for the Commission's decision, then it would raise the question as to how a utility under the jurisdiction and surveillance of this Commission for many years would be allowed by the Commission to provide allegedly inadequate maintenance and be negligent in its management, without being subject to a show cause order or subject to investigation and penalty. If that situation were true, the question also would arise as to why the solution to the Commission's own failure to act would be to penalize a new owner (committed to correcting the situation) by assessing a permanent reduction to the new owner's rate base through a negative acquisition adjustment, especially when the asset transfer had already been found to be in the public

interest.

The Commission's regulatory and monitoring programs should prevent that level of poor maintenance from happening. The Commission has issued many orders to show cause to utilities for poor maintenance and poor service, but there is no evidence that the Commission issued a show cause order against Jasmine Lakes. Therefore, the Jasmine Lakes case cannot be interpreted as simply standing for the proposition that prior poor maintenance is an extraordinary circumstance warranting a negative acquisition adjustment. Furthermore, such an interpretation of the Jasmine Lakes case would be totally contrary to decisions made in prior (and subsequent) case-by-case and generic proceedings before this Commission.

An asset transfer, without an acquisition adjustment, puts the buyer in the shoes of the seller. Therefore, only solutions to problems that would have been applicable to the seller should be applicable to the buyer. If maintenance were inadequate, could the Commission have permanently reduced the rate base of the seller? No, of course not. What it could do, at the time of a rate case, would be to make used and useful adjustments for plant that is not properly functioning or reduce expenses for rate making purposes, if expenses are found to be inappropriate.

If prior owners were found to be negligent, could the Commission permanently reduce the rate base of those owners as a solution? No, definitely not. But it could reduce its allowed rate of return, or adjust allowed management salaries, or even impose a penalty on that management, if the negligence was willful. Even the condition wherein the utility is purchasing most of its water from another utility while still owning and earning on a water

plant is usually addressed by applying used and useful adjustments or by retiring the plant.

The point is, the Commission cannot do to the buyer what it could not do to the seller. The acquisition adjustment recognizes extraordinary circumstances in a sale, if they exist. A negative acquisition adjustment is not, and cannot be, an arbitrary punishment to get back at the seller because of perceived misdeeds against which the Commission itself failed to act in the past. That procedure would result in an arbitrary and capricious punishment against the purchaser.

E. SUMMARY OF THE 3 ORDERS EXPLAINING WHY NAA APPROVED

In summary, there is little similarity between the circumstances in the purchase of Cypress Lakes and the circumstances considered in these three cases. One of the three cases (Lanier) involved a stipulated settlement between the utility and OPC which resolved none of the facts in that case and involved none of the facts in the Cypress Lakes case. Another case (CGD) involved a three-party nontaxable exchange with unique circumstances that are not generally applicable and are specifically not applicable to the Cypress Lakes case. The third case (Jasmine Lakes) involved a reversal of a prior decision, having circumstances unique to that one case among the 106 cases which have dealt with acquisition adjustments. An interpretation of facts (regarding a prior owner's alleged failure to maintain) as supporting a negative acquisition adjustment would be inconsistent with prior and subsequent decisions. But as was discussed, there were other factors involved, so the case provides no guidance.

POSITIVE ACQUISITION ADJUSTMENTS

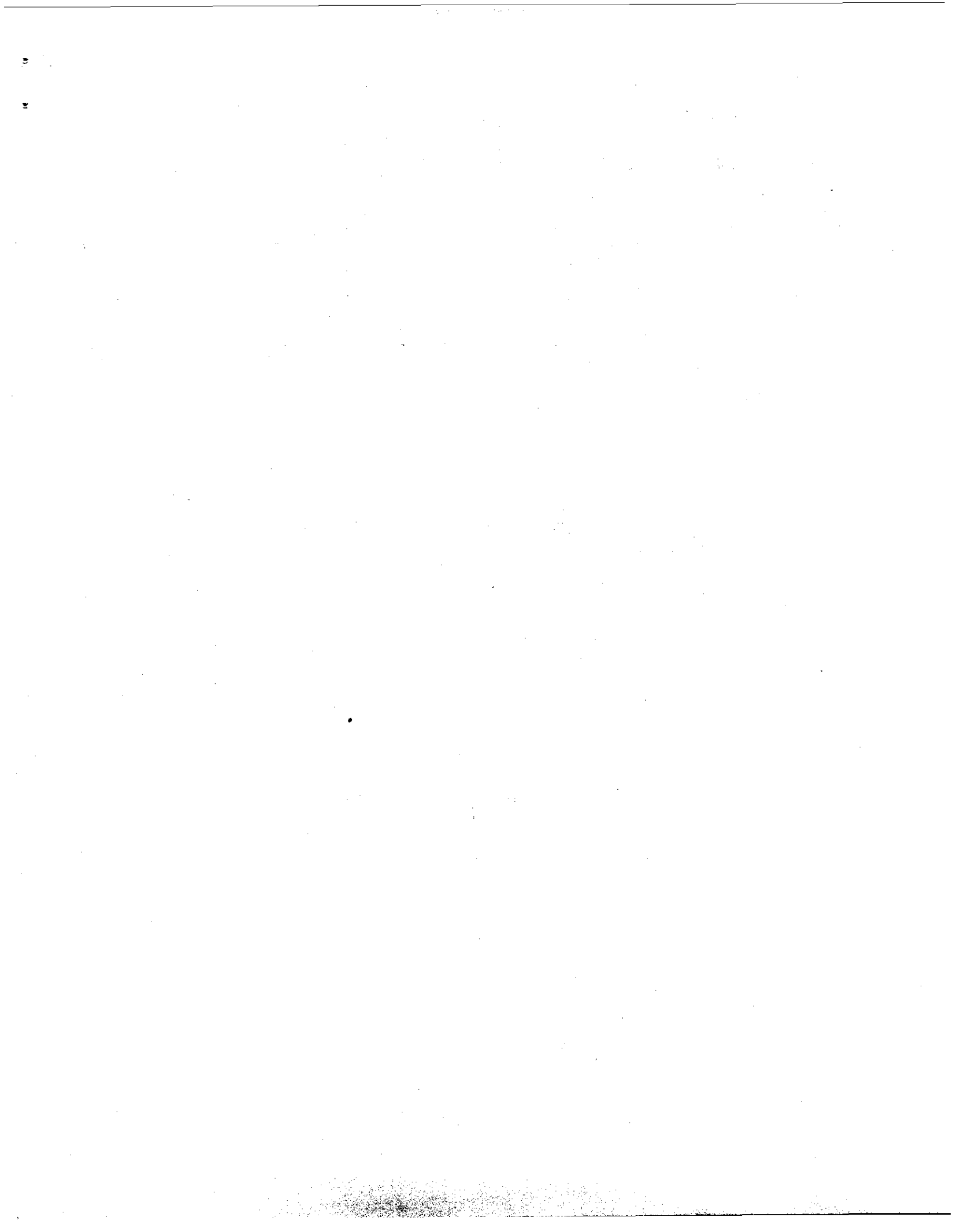
There were 72 orders which deal with, or appear to deal with, purchase prices above rate base (positive acquisition adjustment). Of these, only three [Case Nos. 38, 61 and 70] had positive acquisition adjustments included in rate base. All but ten of the orders relied solely on a statement of the Commission's acquisition adjustment policy as the reason for not including an acquisition adjustment in rate base.

In general, the ten orders that included some additional support for the decisions, identified the benefits which customers should be expected to receive if a positive acquisition adjustment were included. For the most part, these are the same benefits identified in the two generic orders arising from the investigation of the acquisition adjustment policy. Cypress Lakes provided testimony describing those benefits, which are anticipated to enure to Cypress Lakes's customers as a result of the change in ownership. Although those benefits are usually considered the justification for increasing rate base through a positive adjustment, Cypress Lakes's customers will enjoy those benefits without an increase in rate base.

G. CONCLUSION

Exhibit (FS-1) lists 106 cases which provide a concise history of the Commission consideration of acquisition adjustment issues for the last 11 ½ years. In addition, case #0 in Exhibit FS-1 was decided in 1982, which is 17 years ago, and set the precedent that "... the purchaser shall stand in the shoes of the seller in the determination of the rate base." [Order No. 11266, issued October 25, 1982] The Commission has rarely ever included an acquisition adjustment, either positive or negative, in rate base. The 3 cases that included a negative acquisition adjustment involve circumstances that were quite unique. The purchase by Cypress Lakes is not unique and is consistent with Commission prior findings and policy.

The Commission's orders regarding acquisition adjustments over the last 11 ½ years shows a remarkably consistent application, on a case by case basis, of an officially stated agency policy adopted in a generic investigation. The officially stated agency policy is: Absent extraordinary circumstances, the purchase of a utility system at a premium or discount shall not effect rate base. The review of Commission orders shows that agency practice for the two years prior to that official statement and for the 9 ½ years subsequent to that official statement have been consistently applied to each case. Every party entering a proceeding involving a possible acquisition adjustment knows what the policy is and that the policy has not shifted in nearly a dozen years and in over 100 cases.



ATTACHMENT "B"

PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW

Cypress Lakes Utilities, Inc. submits the following proposed findings of fact and conclusions of law. The citations to authority are not intended to be interpreted as the exclusive authority for the finding of fact.

Findings of Fact 1
Conclusions of Law 6

FINDINGS OF FACT

1. An acquisition adjustment results when the purchase price differs from rate base.
2. In the absence of extraordinary circumstances, it has been Commission policy since at least 1983 that the purchase of a utility at a premium or discount shall not affect the rate base calculation. [Order No. PSC-98-0993-FOF-WS, at page 7, quoted in Wenz, Direct Testimony at page 3, line 16 to page 4, line 3.]
3. Cypress Lakes did not request an acquisition adjustment. [Wenz, Direct Testimony, page 5, lines 23 to 25.]
4. The Office of Public Counsel is the only entity requesting an acquisition adjustment in this case. [Wenz, Direct Testimony, page 7, lines 6 to 16.]
5. No evidence has been presented that any extraordinary circumstances exist in this case. [See the entire Larkin, Direct Testimony; Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 7 to 9.]
6. As for the condition of the assets sold to Cypress Lakes Utilities, Inc., both the water

and wastewater systems appeared to be in satisfactory condition, with no outstanding operating violations. [Wenz, Direct Testimony, page 10, lines 1 to 10.]

The water plant appears to be in satisfactory condition and meets applicable standards set forth by the Department of Environmental Protection. The wastewater plant has problems with capacity during the peak flow periods and requires expansion to meet future and existing flow demands. [Application, Exhibit C.]

7. Cypress Lakes Utilities, Inc., was incorporated in Florida on September 23, 1997, and is a wholly owned subsidiary of Utilities, Inc., which was incorporated in Illinois in 1965. [Application, , Part I, Para. E., Part II, Para. A., and Ex. H, Articles of Incorporation.]
8. With recent additions, Utilities, Inc. now has 67 subsidiaries in fifteen states, including fourteen systems in Florida. The subsidiaries own and operate water and/or wastewater utilities serving approximately 200,000 customers, of which 63,000 are in Florida. [Wenz, Direct Testimony, page 2, lines 2 to 10, and Application, , Part II, Para. A.]
9. The prior owner of the utility also developed the mobile home community being served by the utility. [Wenz, Direct Testimony, page 7, lines 6 to 16.]
10. The prior owner is continuing as an active developer, but is not interested in operating the utility. [Wenz, Direct Testimony, page 7, lines 6 to 16.]
11. Cypress Lakes Associates, Ltd. became subject to the jurisdiction of Polk County in

1996, and on August 6, 1996, Polk County established initial rates, miscellaneous fees, and service availability charges for the utility. [Small, Direct Testimony, page 7, lines 5 to 19.]

12. By Order No. PSC-97-0569-FOF-WS, issued May 20, 1997, in Docket No. 961334-WS, the Commission granted a Grandfather Certificate and adopted the initial rates and charges established by Polk County for Cypress Lakes Associates, Ltd. The utility was able to provide sufficient historical records and supporting source documentation for the audit staff to compile CIAC and associated accumulated amortization of CIAC for the water and wastewater utilities as of December 31, 1997. [Small, Direct Testimony, page 7, lines 5 to 19.]
13. When making its decision to purchase Cypress Lakes Associates, Ltd., Utilities Inc. was aware of, and relied on, the established Commission policy on acquisition adjustments. [Wenz, Direct Testimony, page 6, line 16 to page 7, line 2.]
14. Utilities, Inc. has purchased several utilities in Florida, and the Commission's policy on acquisition adjustments has entered into the decision to purchase each of them. [Wenz, Direct Testimony, page 6, line 16 to page 7, line 2.]
15. According to Order No. 25729 issued in the investigation docket, Docket No. 891309-WS, the Commission's existing policy on acquisition adjustments translates into several benefits for the customers which result from the new ownership of utilities purchased under that policy. Order No. 23376 stated that: "Not only might OPC's proposed change not benefit the customers of troubled utilities, it might

actually be detrimental, by removing any incentive for larger utility companies to acquire distressed systems." [Order No. 23376, issued August 21, 1990, in Docket No. 891309-WS, at page 3.]

16. Utilities, Inc. is not a developer, and its only business is to own and operate water and wastewater utilities. [Wenz, Direct Testimony, page 7, lines 18 to 21.]
17. In its Order No. 25729 the Commission found that the customers of utilities acquired under its acquisition adjustment policy are not harmed, and indeed benefit from a better quality of service at a reasonable cost. [Order No. 25729, at page 3.]
18. In 1990, at the urging of OPC, the Commission opened a docket to inquire into its acquisition adjustment policy. By its PAA Order No. 23376 issued on August 21, 1990, the Commission reaffirmed its policy on acquisition adjustments. OPC protested the PAA order and requested formal hearings. The PSC opened a full investigation and held hearings at which OPC and other interested persons, including utility companies, presented their views on July 29, 1991. [Docket No. 891309-WS.]
19. Mr. Larkin's testimony does not mention that he ever inspected the utility system prior to preparing his testimony. In addition, Mr. Larkin does not claim to be an engineer. [See the entire Larkin, Direct Testimony; Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 7 to 9.]
20. The utility's annual reports filed with the Commission during the two years the utility was under PSC jurisdiction show that the utility sustained cumulative losses of

over \$138,000 and had a negative equity position equal to that amount. These reports also show that, for the same period, the mobile home park had sustained cumulative losses of \$2.3 million which translated to a negative equity position of the same magnitude. [Wenz, Direct Testimony, page 8, lines 1 to 12.]

21. The Staff audit did not include any consideration of used-and-useful calculations or other ratemaking adjustments such as working capital allowance. [Small, Direct Testimony, page 3, lines 1 and 2, and Wenz, Direct Testimony, page 5, lines 1 to 3.]
22. Sometimes there is a difference of opinion whether a statement is a finding of fact or a conclusion of law. Therefore, to avoid denial of a proposed “finding of fact” on the basis that it has been “mischaracterized” as a “conclusion of law”, Cypress Lakes Utilities, Inc. adopts and incorproates herein each and every request characterized as a “conclusion of law” and requests that each be ruled on as a “finding of fact”.

CONCLUSIONS OF LAW

The citations to authority are not intended to be interpreted as the exclusive authority for the conclusion of law.

1. An acquisition adjustment should not be included in the rate base calculation in this case. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 12 to 18. Wenz, Direct Testimony, page 6, lines 4 to 14. Wenz, Rebuttal Testimony to OPC Witness Larkin, page 2, line 15 to page 3, line 5.]
2. The appropriate rate base is net book value as determined by the Staff audit, and adjusted by Staff in the Staff Recommendation and in the PAA Order. [Wenz, Direct Testimony, page 5, lines 5 to 16.]
3. The net book value is \$617,609 for water and \$921,439 for wastewater. This agrees with the amounts in the Staff audit, as adjusted in the Staff Recommendation and in the PAA Order. [Wenz, Direct Testimony, page 4, lines 12 to 16 and page 5, lines 5 to 16. See also, discussion of Issue 4 and Issue 6.]
4. Rate base for transfer purposes \$617,609 for water and \$921,439 for wastewater. [See, Wenz, Direct Testimony, page 4, lines 12 to 16 and page 5, lines 5 to 16.]
5. The CIAC is properly accounted for, and the depreciation is properly accounted for.
6. The current Commission policy regarding acquisition adjustments, which has been in effect at least since 1983, is that ". . . absent extraordinary circumstances, the purchase of a utility system at a premium or discount shall not affect rate base." [Emphasis added. Order No. 25729 issued February 17, 1992, at page 1. See also,

Attachment “A” to this Brief.]

7. Extraordinary circumstances must be shown in this case in order to warrant rate base inclusion of a negative acquisition adjustment. [Order No. PSC-98-1092-FOF-WS, issued August 12, 1998, in Docket No. 96-0235-WS, at page 8. See also, discussion at Issue 8. See also, discussion at Issue 5.]
8. Not including a negative acquisition adjustment in the rate base calculation is in accordance with established Commission policy. [Wenz, Direct Testimony, page 12, lines 1 to 9; see also, Order No. PSC-98-1092-FOF-WS, at pages 20 and 21. See also, discussion at Issue 5 and comments on prior Commission cases in Attachment “A”.]
9. Including a negative acquisition adjustment in the rate base calculation would be contrary to established Commission policy. [Order No. PSC-98-1092-FOF-WS, issued August 12, 1998, in Docket No. 96-0235-WS, at page 8. See also, discussion at Issue 8. See also, discussion at Issue 5 and comments on prior Commission cases in Attachment “A”.]
10. In this Cypress Lakes case, there was nothing extraordinary about the utility or the circumstances leading up to its purchase. The purchase price and the circumstances of sale “. . . were pretty much like those of the other utilities we have purchased in Florida.” [Wenz, Direct Testimony, page 11, lines 5 to 9.]
11. Current Commission policy on acquisition adjustments was developed on a case-by-case basis beginning at least as far back as 1982. [see Attachment “A”, page 1, case

- #0, Order No. 11266, issued October 25, 1982, and other cases discussed therein.]
12. That case-by-case development was later followed by a generic proceeding (with notice to all potentially affected persons) in 1989 to 1992 which was initiated by OPC's petition for rulemaking on acquisition adjustments. [See, Docket No. 890309-WS.]
 13. The Commission opened an investigation on the subject, and an OPC witness, now a member of the Public Service Commission, participated in that proceeding as a witness. [See, Docket No. 890309-WS.]
 14. Docket No. 890309-WS resulted in Order No. 23376, issued August 21, 1990, and Order No. 25729, issued February 17, 1992. [See, Docket No. 890309-WS.]
 15. In the 106 acquisition adjustment cases which the Commission has considered since January, 1988, the Commission has consistently followed the same policy. The Commission's policy is clear and unequivocal that there will be no acquisition adjustment for ratemaking purposes, absent extraordinary circumstances.
 16. OPC has made no showing of extraordinary circumstances, and therefore there is no basis for an adjustment to rate base. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 12 to 18.]
 17. Mr. Larkin's testimony does not even claim that any extraordinary circumstances exist in this case. [See the entire Larkin, Direct Testimony; Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 7 to 9.]
 18. No evidence of any kind has been presented to show that any extraordinary

- circumstances existed in regard to this transfer. [See the entire Larkin, Direct Testimony; Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 7 to 9.]
19. There are no extraordinary circumstances which warrant an acquisition adjustment to rate base. [Wenz, Direct Testimony, page 12, lines 1 to 9.]
 20. The Commission has already found that the transfer is in the public interest in its order approving transfer. [Order No. PSC-98-0993-FOF-WS, issued July 20, 1999, at page 3.]
 21. A major purpose for the current Commission policy on acquisition adjustments is to create an incentive for larger utilities to acquire small, troubled utilities. [Order No. 25729, Order Concluding Investigation and Confirmation Acquisition Adjustment Policy, at page 3, issued on February 17, 1992, in Docket No. 891309-WS.]
 22. Utilities, Inc. has the financial ability, and is willing to commit funds to the operation of Cypress Lakes Utilities. [Wenz, Direct Testimony, page 8, lines 14 to 23.]
 23. Utilities, Inc. can attract capital at reasonable costs. [Wenz, Direct Testimony, page 9, lines 1 and 2.]
 24. Utilities, Inc. also has the necessary professional and experienced utility management, in that it operates 67 water and wastewater utilities in fifteen states, and it has an established management team and access to professional operators in Florida. [Wenz, Testimony, page 9, lines 4 to 9.]
 25. Utilities, Inc. can benefit from economies of scale in its operation because: 1) it already has experienced management in place in Florida, so it will not be necessary

to obtain management just for Cypress Lakes; 2) Cypress Lakes will be allocated a portion of the overall management expense; and 3) equipment and supply purchases for Cypress Lakes will benefit from the established vendor resources already being used for sister systems in Florida. [Wenz, Direct Testimony, page 9, lines 11 to 20.]

26. If Seller had not been purchased, Seller would still be entitled to apply for rates based on the net original cost of assets serving the public. That is the same asset base that the Commission would deny to a purchaser if the Commission were to impose a negative acquisition adjustment. [See discussion in Brief, Background, Part I.]
27. Since 1971, when the Florida Legislature removed from the statutes any reference to the "fair value" ratemaking concept, the Commission has set rates based not on so-called "worth" or "value," but on the cost of utility property when first dedicated to public service. [See, Section 367.081(2)(a)1., Fla. Stat.]
28. For ratemaking, the Commission has interpreted "cost basis" to mean the original cost of property when first dedicated to public service. That interpretation applies not only in the context of acquisition adjustments, but elsewhere as well. [Order No. 25729.]
29. The Commission has considered the question of whether the acquiring utility should recover depreciation expense on the original cost of the assets and found that it is appropriate to do so. From the customer's point of view, nothing changes as a result of change in ownership. [Order No. 25729.]

30. Commission policy is to allow a rate of return on the full original cost rate base and include the depreciation expense on that amount in its rate recovery. “. . . [T]he buyer earns a return on not just the purchase price but the entire rate base of the acquired utility. The buyer also receives the benefit of depreciation on the full rate base. . . . The customers of the acquired utility are not harmed by this policy because, generally, upon acquisition, rate base has not changed so rates have not changed.” [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 5, lines 6 to 14, quoting PSC Order No. 25729, issued February 17, 1992, in Docket No. 891309-WS.]
31. If the OPC request for a negative acquisition adjustment is denied in this case, the utility will not earn an excessive return. It will continue to be afforded the opportunity to earn a fair return on the net original cost of the assets, used and useful in serving the public.
32. Investment is required to bring the system up to proper standards. [See, the discussion of discrepancies above in this Issue 1.]
33. Cypress Lakes Associates, Ltd. was a “troubled” system. [See, the discussion of the financial condition of the utility and its developer-owner, above in this Issue 2.]
34. “. . . [P]rice differential alone did not constitute an extraordinary circumstance, and that in accordance with past practice, a negative acquisition adjustment would not be imposed.” [Wenz, Direct Testimony, page 12, lines 1 to 9; see also, Wedgefield Utilities, Inc., Order No. PSC-98-1092-FOF-WS, at pages 20 and 21.]

35. The differential between purchase price and rate base is much less in the Cypress Lakes transfer than in the Wedgefield transfer. [Wenz, Direct Testimony, page 12, lines 11 to 19.]
36. A negative acquisition adjustment is considered at the time of transfer and requires that extraordinary circumstances be found for taking the extreme step of permanently reducing the net original cost as rate base. A used and useful adjustment is used in a rate case for temporarily removing from rate base certain assets which are not currently used and useful in providing utility service to the customers. The two regulatory concepts perform different functions at different times. [See, discussion in Issue 5.]
37. Although Cypress Lakes Associates, Ltd. did not maintain its records in accordance with the NARUC Uniform System of Accounts, it did maintain its books and records in a manner that showed the actual investment in the water and wastewater facilities. [Small, Direct Testimony, page 2, line 15 to page 3, line 2 and page 3, lines 9 to 22.]
38. Mr. Larkin claimed that there were reasons other than extraordinary circumstances for his recommendation to include a negative acquisition adjustment in rate base. Whatever concerns Mr. Larkin has raised are appropriately examined in the context of a rate proceeding and have nothing to do with evaluating the appropriateness of an acquisition adjustment. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, lines 11 to 19, and page 5, lines 20 to 22. Seidman, Rebuttal Testimony to OPC

Witness Larkin, page 3, line 24 to page 4, line 2.]

39. The concerns expressed by Mr. Larkin are his general concerns in any purchase and transfer, but they are not specific to this case. He never presented any evidence that they occurred for this utility, and he never even alleged that they exist in this case, only that they might exist. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 3, line 22 to page 4, line 1, and page 6, lines 1 to 5.]
40. Mr. Larkin expressed concern that the original owner, a developer, might have overbuilt the system. That is clearly an issue of used and useful to be addressed in a rate case, not in determining whether a negative acquisition adjustment should be included in rate base. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 4, lines 5 to 10.]
41. Mr. Larkin expressed concern that assets may have deteriorated at a rate greater than reflected in the book depreciation rate. Of course, they also may have deteriorated at a lesser rate. Regardless, this is a normal consideration in a rate case and can be addressed, if appropriate, by adjusting depreciation expense. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 4, lines to 16.]
42. Mr. Larkin expressed concern that the prior owner may not have properly installed or maintained the system in order to keep rates down. If so, then the lower rates over that period of time reflect the fact that customers were not being improperly charged for something they didn't receive. If the issue is whether deferred maintenance or improper installation may have resulted in higher long run costs,

that again is properly addressed in a rate case. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 4, line 17 to page 5, line 2.]

43. Mr. Larkin has expressed concern that the method of allocating overhead costs, which is at issue in a pending rate case of another subsidiary of Utilities, Inc. may result in an increase in the rates of the customers of Cypress Lakes. That is speculative, irrelevant, a proper concern in a rate proceeding an is not a basis for a negative acquisition adjustment to rate base. Because there is no rate case pending for Cypress Lakes, when and if there is one, the legitimacy of expenses, including overhead expenses, is properly scrutinized in that arena. And it is certainly speculative to conclude that even if overhead expenses are allocated to Cypress Lakes, that they would not be offset by a decrease in other expenses. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 5, lines 4 to 18.]
44. Recording an acquisition adjustment for USOA purposes is significantly different than recognizing it for ratemaking purposes. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 2, line 15 to page 3, line 5]
45. Florida is an “original cost” state. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 6, lines 7 to 20.]
46. Mr. Larkin testified in support of negative acquisition adjustments when purchase price is below net book value because he believes customers should pay based on his definition of “true” value (purchase price in relation to net book value). However, if the Commission were to accept that policy, then when the purchase price is above

net book value, the Commission also would be required to accept positive acquisition adjustments to rate base, again based on Mr. Larkin's definition of "true" value (purchase price in relation to net book value). [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 6, lines 7 to 20.]

47. Without a negative acquisition adjustment to rate base, the utility will be allowed to earn a fair return and recover depreciation expense on the net original cost of the assets actually invested on behalf of the customers, when those assets were first committed to public service. No more, no less. A change of ownership does not change that fact. [Wenz, Rebuttal Testimony to OPC Witness Larkin, page 4, line 23 to page 5, line 11.]
48. The net effect of not allowing a negative acquisition adjustment is zero because the buyer is essentially stepping into the shoes of the seller, the assets serving the customers remain unchanged, the cost of those assets remain unchanged, rate base remains unchanged and the basis for rates remains unchanged. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 5, lines 16 to 24.]
49. If the Commission did allow a negative acquisition adjustment, it would have the effect of making permanent, irreversible used and useful and expense adjustments. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 6, lines 1 to 18.]
50. If the Commission did allow a negative acquisition adjustment, when used and useful adjustments are to be made in a future rate proceeding, the utility would be penalized again because the used and useful adjustment would be applied to a rate

base that is already less than the cost incurred in making the assets available to the customer. [Seidman, Rebuttal Testimony to OPC Witness Larkin, page 6, lines 1 to 18.]

51. If the Commission did allow a negative acquisition adjustment, ironically it would thwart conservation of scarce resources by sending a signal to customers that the cost to provide water and wastewater services is less than is actually incurred.

[Seidman, Rebuttal Testimony to OPC Witness Larkin, page 6, lines 1 to 18.]

52. The Commission is bound by its own Order Nos. 23376 (8/21/90) and 25729 (2/17/92), which confirmed the requirements for acquisition adjustments. Generic proceedings confirmed prior case-by-case development of the requirement that extraordinary circumstances must be shown before an acquisition adjustment is warranted. [Docket No. 891309-WS.]

53. Rule 25-30.037(2)(m), F.A.C., Application for Authority to Transfer, sets forth what a utility must file with the Commission when it seeks authority for a utility transfer.

The rule requires that an application for transfer must include:

(m) a statement setting out the reasons for the inclusion of an acquisition adjustment, if one is requested; . . . [Emphasis added.]

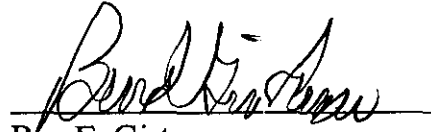
54. The Utility has met its burden of proof, but OPC has not. [See discussion in Issue 7. See also, Order No. PSC-98-1092-FOF-WS, issued August 12, 1998, in Docket No. 960235-WS, PSC-98-1092-FOF-WS at page 8, in the case of Wedgefield Utilities, Inc.]

55. Because OPC did not carry its burden of persuasion and there was no subsequent shift in the burden of proof, it was not required that the utility rebut OPC's allegations and carry the ultimate burden of proof. [[See discussion in Issue 7. See also, Order No. PSC-98-1092-FOF-WS, issued August 12, 1998, in Docket No. 96-0235-WS, at page 7.]
56. If OPC is right that there is no authority to follow the existing Commission policy on acquisition adjustments, then there is no authority to even consider, must less require, a negative acquisition adjustment, for any reason. [See, Ch. 120, Fla. Stat. See also, discussion in Issue 8.]
57. Either the existing policy is valid or there is no policy at all and no authority for the Commission to inquire into acquisition adjustments. [See, Ch. 120, Fla. Stat. See also, discussion in Issue 8.]
58. There have been no hearings, no notice to affected persons, and no testimony or exhibits accepted by the Commission, either deviating from the existing Commission policy or supporting such a new policy, which has been proposed repeatedly by OPC, in case after case, and rejected every time by the Commission. [See Attachment "A", Comments on Prior Commission Orders. See also, Florida Cities Water Co. v. State, 705 So.2d 620, at 625 (Fla. 1st DCA 1998).]
59. The Commission cannot act "... inconsistently with its published regulatory philosophy." The Commission cannot now deviate from its established policy on negative acquisition adjustments because, "No newly promulgated rule necessitated,

authorized, or justified such a policy change.” [Florida Cities Water Co. v. State, 705 So.2d 620, at 625 (Fla. 1st DCA 1998).]

60. The issue of whether the current Commission policy constitutes invalid rule has not been tested in the Division of Administrative Hearings (DOAH) which has exclusive jurisdiction to decide that issue.. [See, Ch. 120, Fla. Stat. See also, discussion in Issue 8.]
61. OPC has repeatedly, for at least the past 11 ½ years, failed to file a petition with DOAH for that determination of alleged rule invalidity or non-rule policy. In that time period, 106 cases have been decided by the Commission, consistent with the policy that “. . . absent extraordinary circumstances, the purchase of a utility system at a premium or discount shall not affect rate base.” [Order No. 25729 issued February 17, 1992, at page 1.]
62. Sometimes there is a difference of opinion whether a statement is a conclusion of law or a finding of fact. Therefore, to avoid denial of a proposed “conclusion of law” on the basis that it has been “mischaracterized” as a “finding of fact”, Cypress Lakes Utilities, Inc. adopts and incorproates herein each and every request characterized as a “finding of fact” and requests that each be ruled on as a “conclusion of law”.

RESPECTFULLY SUBMITTED, this 3rd day of November, 1999.



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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been sent to Harold McLean, Esq., Office of Public Counsel, 111 W. Madison St., Tallahassee, FL 32399-1400; and to Jennifer Brubaker, Esq.*, Division of Legal Services, Florida Public Service Commission, 2540 Shumard Oak Blvd., Tallahassee FL 32399-0850, by U.S. mail (* or by hand delivery) this 3rd day of November, 1999.



Ben E. Girtman