

State of Florida



Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

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

DATE: SEPTEMBER 1, 2000

TO: DR. MARY BANE, DEPUTY EXECUTIVE DIRECTOR, TECHNICAL

FROM: TRICIA MERCHANT, DIVISION OF ECONOMIC REGULATION
DIVISION OF LEGAL SERVICES (CHRISTENSEN)

Handwritten initials and signatures: PM, MAB, 9/1/00

RE: ITEM 25

DOCKET NO. 990939-WS - APPLICATION FOR RATE INCREASE IN
MARTIN COUNTY BY INDIANTOWN COMPANY, INC.
COUNTY: MARTIN

AGENDA: 09/05/2000 - REGULAR AGENDA - PROPOSED AGENCY ACTION -
INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: 5-MONTH EFFECTIVE DATE: 9/28/2000 (PAA RATE CASE)

Staff became aware today that 2 changes were necessary to staff's recommendation, Item No. 25. Neither of these changes affect the revenue requirement or service rate calculation. The first change is a wording change that corrects staff's interpretation of Order No. 23541 on the regulatory treatment of gross-up. The second change adds language stating the Commission's practice regarding the removal of public fire protection rates. We have also attached a corrected water rate schedule which includes the prior and staff recommended public fire protection rates.

I have attached a type and strike version of the two issues that are affected, in addition to the revised rate water rate schedule. Since this is a PAA rate case with a 5-month statutory deadline, the item cannot be deferred.

Vertical stamp: P, P, M, R, P, C, C, H

CC: Division of Records & Reporting

OK
MAB
9/1/00

DOCUMENT NUMBER-DATE

10072 SEP-18

FPSC-RECORDS/REPORTING

ISSUE 10: What is the appropriate amount of deferred income taxes to be included in the capital structure?

RECOMMENDATION: The appropriate amount of deferred taxes for the test year is \$388,955. This amount should be specifically identified in the capital structure and not be subject to pro rata adjustment. (MERCHANT, B. DAVIS)

STAFF ANALYSIS: The amount of credit deferred taxes for the test year listed in the MFRs on Schedules A-19 and D-2 is \$713,164. In calculating its cost of capital, the utility adjusted this amount by \$285,089 to remove deferred taxes specifically identified as relating to non-utility operations and to include pro forma plant additions. The utility further reduced deferred taxes by \$299,291 as part of the pro rata adjustment to reconcile capital with rate base. Using this calculation, deferred taxes make up 7.93% of total capital.

The balance of debit deferred taxes on the utility's books relate to CIAC and the utility has been allowed to collect gross-up (contributed taxes) to offset its investment in debit deferred taxes. Order No. 23541, issued October 1, 1990, established the Commission's practice on the regulatory treatment of gross-up on CIAC. According to that order, any deferred taxes associated with gross-up should be removed for rate setting purposes. As such, the utility appropriately excluded the balance of debit deferred taxes from the rate setting equation. Consistent with that order, any deferred taxes associated with gross-up should offset the unamortized balance of contributed taxes. In this case, staff agrees that the utility appropriately excluded the balance of debit deferred taxes from the rate setting equation.

Staff has reviewed the utility's deferred income tax balance requested in this proceeding. We believe that several adjustments are appropriate.

First, staff agrees with the utility's specific removal of the deferred taxes relating to non-utility operations. This was done in Order No. 11891, issued April 27, 1983, in Docket No. 810037-WS, the utility's last full rate proceeding, as well as Order No. PSC-96-0657-FOF-WS, issued May 10, 1996, in Docket No. 960011-WS, Indiantown's last earnings investigation. However, based on Indiantown's trial balance, staff believes that the MFRs understate the deferred taxes associated with the non-utility operations and pro forma plant additions by \$12,633. After making this adjustment, the correct balance of deferred taxes for utility assets is \$415,442.

Secondly, other than a pro rata adjustment, the utility did not make any specific adjustments to deferred taxes associated with non-used and useful plant. In accordance with Rule 25-30.433(3), Florida Administrative Code, states that used and useful credit deferred taxes should be included in the capital structure. In order to estimate these amounts, staff has taken the amount of credit deferred taxes to depreciable plant (per books) and applied this ratio to the amount of non-used and useful plant. We also applied this percentage to the non-used and useful portion of pro forma plant. This resulted in a specific reduction to credit deferred taxes of \$58,665.

To determine the amount of deferred taxes related to the pro forma plant additions, staff used the ratio of test year incremental current deferred tax expense to plant additions to estimate the deferred taxes that would have been booked for the pro forma additions. This adjustment results in an increase to credit deferred taxes of \$32,178.

Based on the above adjustment, staff believes that the appropriate balance of deferred taxes to be included in the capital structure is \$388,955, which results in a ratio of 24.58% to total capital.

Staff does not believe that the utility's pro rata adjustment to deferred taxes is proper. Just as the utility plant, which gave rise to the deferred taxes, is specifically identified and adjusted, the related deferred taxes should also be specifically adjusted. In Order No. PSC-96-1338-FOF-WS, issued on November 7, 1996, in Docket No. 951056-WS (Palm Coast Utility Corporation), the Commission found that the investment tax credit (ITCs) adjustment should be a specific adjustment and that a pro rata adjustment should not be applied to ITCs. The order stated that the capital structure should include customer deposits, ITCs and deferred taxes that are specifically related to the requested rate base and reconcile any remaining difference pro rata over the investor sources of capital only. This issue was appealed by Palm Coast to the First District Court of Appeal and the Commission's treatment was upheld by the Court without discussion. Palm Coast Utility Corporation v. State, 742 So.2d 482 (1st DCA 1999)

ISSUE 32: What are the appropriate water and wastewater rates?

RECOMMENDATION: Staff has recommended monthly rates using the base facility and gallonage charge rate structure. The recommended water rates should be designed to produce annual operating revenues of \$560,099, which is the \$580,011 revenue requirement less \$19,212 in miscellaneous revenue. The recommended wastewater rates should be designed to produce annual operating revenues of \$830,770 which is the \$831,026 revenue requirement less \$256 in miscellaneous revenue. The residential wastewater gallonage charge should continue to be capped at 6,000 gallons per month. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets, pursuant to Rule 25-30.475, Florida Administrative Code, provided customers have received notice. The revised tariff sheets should be approved upon staff's verification that the tariff is consistent with the Commission's decision, that the protest period has expired, and that the proposed customer notice is adequate. (B. DAVIS, C. WILLIAMS)

STAFF ANALYSIS: The permanent water rates requested by the utility are designed to produce annual operating revenues of \$697,224. The requested revenues represent an increase of \$107,540 (21.52%) for water based on the historic test year ending June 30, 1999. The permanent wastewater rates requested by the utility are designed to produce annual operating revenues of \$1,023,257. The requested revenues represent an increase of \$463,360 (82.75%) for wastewater based on the historic test year ending June 30, 1999.

The utility's current rate structure consists of a base facility and gallonage charge rate structure. Under the current rate structure, the total average consumption per bill is 9,595 gallons which is below the 10,000 gallon threshold used by staff to determine whether a more aggressive conservation-oriented rate structure is appropriate. Based on the information above, staff recommends that the base facility and gallonage charge rate structure be continued for this utility.

Staff recommends that the final water rates approved for the utility should be designed to produce annual operating revenues of \$560,099. This represents the \$580,011 revenue requirement less \$19,912 in miscellaneous revenue. Staff recommends that the final wastewater rates approved for the utility should be designed to produce annual operating revenues of \$830,770, which is the \$831,026 recommended revenue requirement less \$256 in miscellaneous revenue. For wastewater service, the utility currently has a monthly cap of 6,000 gallons for residential customers. There is

no cap for general service customers. Staff recommends that this cap is reasonable and should be continued.

There is also a differential in the gallonage charge for residential and general service wastewater customers that is designed to recognize that a portion of a residential customer's water usage will not be returned to the wastewater system. The last case also recognized a 1.2 differential in the gallonage charge between general service and residential wastewater customers. Staff has applied this differential to staff's recalculated billing and consumption to produce the recommended rates as shown on Schedule Nos. 4-A and 4-B.

In the MFRs, the utility also requested discontinuance of its public fire protection charge. The charge of \$76.93 per fire hydrant was paid annually by Martin County to cover maintenance of the hydrants. The Commission's practice has been to discontinue public fire protection charges and include the cost of maintenance in service rates rather than a separate charge. (See Order No. PSC-95-1417-FOF-WS, issued on November 21, 1995, in Docket No. 941234-WS.) Staff, therefore, recommends that Indiantown be allowed to eliminate the separate charge for public fire protection.

The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets, pursuant to Rule 25-30.475, Florida Administrative Code, provided that the customers have received noticed. The revised tariff sheets should be approved upon staff's verification that the tariff is consistent with the Commission's decision, that the protest period has expired, and that the proposed customer notice is adequate.

The comparison of the utility's original rates and requested rates, expressed as monthly rates, and staff's recommended rates is shown on Schedule Nos. 4-A and 4-B.

**INDIANTOWN COMPANY,
 WATER MONTHLY SERVICE RATES
 TEST YEAR ENDED 06/30/99**

**SCHEDULE NO. 4-A
 DOCKET 990939-WS
 PAGE 1 OF 1**

	Utility Rates As of 6/30/99	Commission Approved Interim	Utility Requested Final	Staff Recomm. Final
<u>Residential, General Service and Multi-Family</u>				
Base Facility Charge:				
Meter Size				
5/8" x 3/4"	\$7.54	\$8.48	\$12.70	\$9.75
1"	\$18.86	\$21.21	\$31.75	\$24.37
1-1/2"	\$37.73	\$42.43	\$63.50	\$48.74
2"	\$60.36	\$67.87	\$101.60	\$77.98
3"	\$113.16	\$127.25	\$190.50	\$146.21
4"	\$188.60	\$212.08	\$317.50	\$243.69
6"	\$377.22	\$424.18	\$635.00	\$487.37
8"	\$603.54	\$678.68	\$1,016.00	\$779.80
8" Turbine	\$679.00	\$763.54	\$1,143.00	\$877.27
Gallonge Charge, Per 1000 gallons	\$1.08	\$1.21	\$1.43	\$1.33
<u>Private Fire Protection</u>				
Base Facility Charge:				
Meter Size				
2"	\$20.53	\$23.09	\$8.47	\$6.50
3"	\$38.49	\$43.28	\$15.88	\$12.18
4"	\$64.15	\$72.14	\$26.46	\$20.31
6"	\$128.31	\$144.28	\$52.92	\$40.61
8"	\$205.30	\$230.86	\$84.67	\$64.98
<u>Public Fire Protection</u> (Annual Charge)	\$76.93	None	None	None
<u>Typical Residential Bills</u>				
5/8" x 3/4" Meter Size				
3,000 Gallons	\$10.78	\$12.11	\$16.99	\$13.74
5,000 Gallons	\$12.94	\$14.53	\$19.85	\$16.40
10,000 Gallons	\$18.34	\$20.58	\$27.00	\$23.05