

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:** August 6, 2009

**TO:** Office of Commission Clerk (Cole)

**FROM:** Division of Regulatory Compliance (Mann, Casey) *PK*  
Division of Economic Regulation (Daniel, Lingo, Redemann) *FAH*  
Office of the General Counsel (Brown) *DM JSA*  
*JD* *W* *1908*  
*JSO* *EL* *MCB*

**RE:** Docket No. 080597-WS – Application for increase in water and wastewater rates in Lake County by Southlake Utilities, Inc.

**AGENDA:** 08/18/09 – Regular Agenda – Proposed Agency Action Except Issues Nos. 21 and 22 - Interested Persons May Participate

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** Argenziano

**CRITICAL DATES:** 5-Month Effective Date Waived Through 08/18/09

**SPECIAL INSTRUCTIONS:** None

**FILE NAME AND LOCATION:** S:\PSC\RCP\WP\080597.RCM.DOC

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### **Case Background**

Southlake Utilities, Inc. (Southlake or utility) is a Class B utility providing water and wastewater service to approximately 2,321 water and 2,161 wastewater customers in Lake County. Water and wastewater rates were last established for this utility in 1990<sup>1</sup> in its original certificate filing.

On October 15, 2008, Southlake filed an Application for Rate Increase at issue in the instant docket. The utility had a few deficiencies in the Minimum Filing Requirements (MFRs). The deficiencies were corrected, and December 15, 2008 was established as the official filing date. The utility requested that the application be processed using the Proposed Agency Action (PAA) procedure and requested interim rates. The test year established for interim rates is the historical twelve-month period ended December 31, 2007. The test year established for final rates is the 13-month average period ending December 31, 2008.

Southlake requested interim rates for both its water and wastewater systems. By Order No. PSC-09-0116-FOF-WS, issued February 25, 2009, the Commission approved interim rates designed to generate annual water revenues of \$1,038,940, an increase of \$47,301 or 4.77 percent, and wastewater revenues of \$1,034,391, an increase of \$238,093 or 29.90 percent.

Southlake requested final rates designed to generate annual water revenues of \$1,184,327 and wastewater revenues of \$1,293,211. This represents a revenue increase on an annual basis of \$183,853 (18 percent) for water and \$487,912 (61 percent) for wastewater.

Southlake was issued a Consumptive Use Permit (CUP) on July 11, 2006 with an expiration date of January 1, 2009. Southlake was issued a short-term duration permit because staff of the St. Johns River Water Management District (SJRWMD or District) were concerned that withdrawals exclusively from the Upper Floridan Aquifer (UFA) to meet projected future demands had the potential for contributing adverse impacts to water resources and related natural systems. The utility is out of compliance with a number of conditions of its CUP. Southlake and the SJRWMD have met on several occasions to discuss Southlake's noncompliance and possible remedies, but no agreements have been reached. The utility filed its application for permit renewal prior to the expiration date of January 1, 2009. Therefore, the existing permit remains in effect until final action is taken on Southlake's new permit request, which includes a request for an increase in water allocation. Southlake's noncompliance with the SJRWMD will be discussed in greater detail in Issue 9.

Southlake is located in the Central Florida Coordination Area, encompassing portions of the St. Johns River, Southwest and South Florida Water Management Districts. These water management districts jointly concluded in 2006 that the availability of sustainable quantities of groundwater in central Florida are insufficient to meet future public water supply demands in the region. In addition, these water management districts concluded that alternative water supply sources must be developed to meet increased demands in central Florida beyond 2013. The requirement to develop alternative water supplies was incorporated by rule amendment in February 2008.<sup>2</sup>

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<sup>1</sup> See Orders No.s 24564 and 23947, issued May 21, 1991, in Docket No. 900738-WS, In re: Application for water and sewer certificates in Lake County by Southlake Utilities, Inc.

<sup>2</sup> Rule 40C-2. Specifics are in the Applicant's Handbook (incorporated by rule), sections 3.1.7, 6.5.4, and 12.10.

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By letter dated June 25, 2009, the utility waived the five-month statutory deadline for the case through August 18, 2009. This recommendation addresses the revenue requirement and rates that should be approved on a prospective basis. The Commission has jurisdiction pursuant to Sections 367.081 and 367.082, Florida Statutes (F.S.).

**Discussion of Issues**

**QUALITY OF SERVICE**

**Issue 1:** Is the quality of service provided by Southlake satisfactory?

**Recommendation:** Yes. The overall quality of service provided by Southlake is satisfactory. (Redemann)

**Staff Analysis:** Pursuant to Rule 25-30.433(1), Florida Administrative Code (F.A.C.), the Commission determines the overall quality of service provided by a utility by evaluating three separate components of water operations, including the quality of the utility's product, the operating condition of the utility's plant and facilities, and the utility's attempt to address customer satisfaction. The utility's compliance with the Florida Department of Environmental Protection (DEP) is considered, as well as customer comments or complaints.

**Quality of Utility's Product and Operational Condition of Plants**

Southlake's water and wastewater plants are regulated by the DEP Central District office in Orlando. The utility is current in all of the required chemical analyses and the utility has met all required standards for both water and wastewater. DEP conducted inspections of the water and wastewater facilities in November 2006 and October 2008. The quality of drinking water delivered to the customers and the wastewater effluent quality are both considered to be satisfactory by the DEP.

The utility's Consumptive Use Permit issued by the St. Johns River Water Management District (St. Johns) expired on January 1, 2009. St. Johns is concerned about the impact of water draw down due to the utility's drinking water wells located in the Upper Floridan Aquifer. St. Johns wants the utility to shift production to the Lower Floridan aquifer. The utility has drilled one deep well into the Lower Floridan aquifer and expensive and extensive drinking water treatment is needed to use the water in the Lower Floridan aquifer. Negotiations are under way. Staff is addressing St. Johns concerns in Issue 9.

A field investigation of the utility's service area was conducted by staff on February 26, 2009, and no apparent problems with the operation of either the water or wastewater treatment facilities were found. The water plant was operating normally and appeared to be well maintained. There was no odor present at the aerators or in the finished water. The wastewater plant was also operating normally and appeared to be well maintained. Therefore, staff recommends that the quality of product and operational condition of the water and wastewater plants is satisfactory.

**Customer Satisfaction**

A customer meeting was held on March 30, 2009, in Clermont. Utility representatives, a representative from the Office of Public Counsel, and one customer attended. The customer was concerned about the usage on her bill, which is about 5,000 gallons per month, and whether the fire hydrants in the service area are routinely tested.

A representative of the utility met with the customer at her home on April 1 and determined that both bathroom toilets were leaking. The customer purchased toilet repair kits and no further leakage has been detected. In addition, with respect to the fire hydrants, the utility responded that all system fire hydrants and main line valves are currently tested quarterly by Southlake personnel for operational ability and, beginning in April 2009, will be tested bi-annually.

Staff also met with three customers prior to the customer meeting who were concerned about hydrogen sulfide (rotten egg smell) in the water, particularly in rental homes. Staff explained that DEP recommends that, if the house is vacant for a period of time, the water should be flushed out of the water lines to remove the odor. The utility agreed to investigate to see if automatic flushers or piping of dead ends is needed. In addition, the utility contacted each customer to offer training on the proper method for flushing the water lines in the home.

According to the DEP, the finished water test results at the point of entry into the distribution system indicate there is no odor in the finished water. The amount of sulfate is 19 mg/l and is well below the maximum contaminant level for sulfate of 250 mg/l. DEP also indicated that monthly distribution tests show the water system is maintaining a chlorine residual. Further, DEP received no complaints regarding the Southlake water system in 2008 or 2009.

There are no outstanding complaints on the Commission's Complaint Tracking System and the utility indicated that they did not receive any customer complaints during the test year. Therefore, staff recommends that the utility's attempts to address customer concerns are satisfactory.

### **Quality of Service Summary**

The quality of the product and the condition of the utility's water and wastewater plants are in compliance with regulatory standards. In addition, the utility addresses customer concerns on a timely basis and there are no outstanding complaints at this time. Therefore, staff recommends that the utility's overall quality of service be considered satisfactory.

### **Conclusion**

Staff recommends that Southlake's quality of product, operating condition of its plants and facilities, and its attempt to address customer concerns are satisfactory. Therefore, staff recommends that the overall quality of service provided by Southlake Utilities, Inc., be found to be satisfactory.

**Issue 2:** What are the used and useful percentages of Southlake's water treatment plant, ground storage tanks, and water distribution lines?

**Recommendation:** The Southlake water treatment plant, ground storage tanks, and water distribution system are 100 percent used and useful. (Redemann)

**Staff Analysis:** The utility has not had a previous rate case before the Commission. In its application, the utility asserts that the Southlake water treatment plant, ground storage facilities, and water distribution system are 100 percent used and useful.

The utility has three wells, which are rated at 701, 1,040, and 2,600 gallons per minute (gpm). The 1,040 gpm well is not interconnected with the other two wells; the water from this well is not chlorinated and is used strictly for landscape irrigation. The St. Johns River Water Management District limits the amount of water that this well can produce. Pursuant to Rule 25-30.431(4), F.A.C., staff recommends that because this well is not interconnected with the other wells in the system, it should be considered 100 percent used and useful.

The 701 and 2,600 gpm wells pump water to aerators located on top of the ground storage tanks, and liquid chlorine is then pumped into the ground storage tanks. The two ground storage tanks have a usable capacity of 2,500,000 gallons. The single maximum day in the test year of 2,759,000 gallons occurred on October 14, 2007. It does not appear that there was a fire, line break, or other unusual occurrence on that day. The utility's records indicate there is no excessive unaccounted for water. The utility's fire flow requirement is 1,500 gpm for 4 hours or 360,000 gallons.

The utility included a growth allowance of 780,260 gallons based on a growth rate of 27.63 percent. Pursuant to Rule 25-30.431(2)(a), F.A.C., growth is limited to 5 percent a year or 25 percent. Staff recommends that a growth allowance of 689,750 gallons should be added to the used and useful calculation based on a growth rate of 25 percent.

The utility calculated the firm reliable capacity of the water system to be 1,673,333 gallons per day (gpd) based on the capacity of the irrigation well and the smaller of the two wells that are interconnected. However, staff recommends that the firm reliable capacity is 672,960 gpd based on the capacity of the smaller of the two wells operating at 16 hour a day, pursuant to Rule 25-30.4325(6)(b), F.A.C.

Staff recommends that, pursuant to Rule 25-30.4325, F.A.C., the water treatment plant is 100 percent used and useful based on a peak day of 2,759,000 gallons, a fire flow allowance of 360,000 gallons, growth of 689,750 gallons, and firm reliable capacity of 672,960 gpd. In addition, because the usable storage capacity is less than the peak day demand, the storage tanks should be considered 100 percent used and useful, pursuant to Rule 25-30.4325(8), F.A.C. According to the utility, all single family lots are completely built out with no remaining lots available for construction. Future growth will require newly installed main extensions. Therefore, staff recommends that the treatment plant, ground storage tanks, and water distribution system be considered 100 percent used and useful.

**Issue 3:** What are the used and useful percentages of the utility's wastewater treatment plant and wastewater collection system?

**Recommendation:** The Southlake wastewater treatment plant is 76 percent used and useful. The used and useful adjustment should be made to Account No. 354.4, Structures and Improvements, and Account No. 380.4, Treatment and Disposal Equipment. The wastewater collection system should be considered 100 percent used and useful. (Redemann)

**Staff Analysis:** In its application, the utility asserts that the Southlake wastewater treatment plant and collection system are 100 percent used and useful because (1) the system is virtually built out, (2) the treatment plant design criteria builds in a level of excess capacity, (3) the construction was in compliance with a DEP requirement, pursuant to Section 367.081(2)a2C, F.S., and (4) there is an insignificant cost difference between a 1.15 mgd wastewater treatment plant (the permitted capacity) and a .904 million gallons per day (mgd) wastewater treatment plant (the current demand plus a growth allowance). In support of its position, the utility provided information showing the cost of several other wastewater treatment plants which cost significantly more per gallon of treatment than the Southlake facility, as well as a statement that the cost to construct smaller incremental units would have been considerably more than the actual construction cost.

The utility's 1994 Annual Report shows that the utility built its first wastewater treatment plant that year with a capacity of .3 mgd annual average daily flow (AADF). In 2002, the utility expanded the wastewater treatment plant to treat .6 mgd (AADF). According to the utility, the service area was growing rapidly in 2002 and 2003 and the projected flow for 2008 was .93 mgd. The existing plant was struggling to consistently meet the DEP treatment requirements and faced potential violations and enforcement action because the plant did not have the DEP redundancy requirement of two units each capable of meeting average annual flow. While the utility could have considered building smaller increments of .3 mgd, the cost for these smaller units would have been considerably more than the cost of the actual construction. Furthermore, smaller plants have operational problems, and the smaller plants would not fit on the 10 acre site without reducing the disposal area. In 2005, an additional .9 mgd expansion to the wastewater treatment plant was built. According to the current DEP permit, that expires on April 15, 2012, the Southlake wastewater treatment plant has a 1.5 mgd AADF design capacity using extended aeration, activated sludge; however, the permitted capacity is limited to 1.15 mgd AADF, the capacity of the rapid infiltrations basins (RIBS).

Pursuant to Rule 25-30.432, F.A.C., the wastewater treatment plant is 76 percent used and useful based on the AADF of 697,482 gpd, a growth allowance of 174,020 gpd, and the permitted capacity of the system of 1,150,000 gpd. Staff agrees that Southlake was able to build the wastewater treatment systems at a lower cost than comparable plants and the cost of the existing facilities are less than the cost might have been if smaller incremental units had been built as needed. However, staff believes that allowing the plant to be considered 100 percent used and useful, instead of 76 percent used and useful, based on the utility's economies of scale argument, would be excessive. The service area is not built out and the remaining capacity will be needed as development in the existing service area continues. It should be noted that, alternatively, used and useful could have been calculated using the 1.5 mgd capacity of the treatment plant by including the additional cost that would be needed to expand the effluent



disposal capacity, which would have resulted in a lower used and useful percentage than is currently being recommended.

Therefore, staff recommends that, pursuant to Rule 25-30.432, F.A.C, the wastewater treatment plant should be considered 76 percent used and useful. The used and useful adjustment should be made to Account No. 354.4, Structures and Improvements, and Account No. 380.4, Treatment and Disposal Equipment. The wastewater collection system should be considered 100 percent used and useful. According to the utility, all single family lots in the development are built out with no remaining lots available for construction and future development will require newly installed main extensions.

**RATE BASE**

**Issue 4:** Should the audit adjustments to rate base to which the utility agrees be made?

**Recommendation:** Yes. Based on audit adjustments agreed to by the utility and staff, plant in service should be increased \$114,555 for water and decreased \$307,196 for wastewater, Land and Land Rights should be decreased by \$57,386 for water and \$207,861 for wastewater, Construction Work in Progress should be reduced by \$58,895 for water, and Accumulated Depreciation should be decreased \$31,105 for water and decreased \$65,867 for wastewater. (Mann, Casey)

**Staff Analysis:** In its response to the staff's audit report,<sup>3</sup> Southlake agreed to the audit findings and audit adjustments listed below. Staff recommends the following adjustments to rate base.

<b>Audit Findings</b>	<b>Water</b>	<b>Wastewater</b>
AF No. 1 – Decrease PIS for Unsupported Plant	(\$142,789)	(\$176,812)
AF No. 3 – Transfer PIS from Water to Wastewater	\$0	\$50,048
AF No. 3 – Transfer PIS from Wastewater to Water	\$222,868	(\$222,868)
AF No. 3 – To Eliminate Duplicate Amount	\$0	(\$15,000)
AF No. 6 – Reclassify Expensed Costs to Capital Costs	<u>\$34,476</u>	<u>\$57,436</u>
Plant in Service Adjustments	<u>\$114,555</u>	<u>(\$307,196)</u>
<b>Land and Land Rights</b>		
AF No. 2 – Decrease Land	<u>(\$57,386)</u>	<u>(\$207,861)</u>
<b>Construction Work in Progress</b>		
AF No. 3 – Transfer Wastewater CWIP to Water PIS	(\$50,048)	\$0
AF No. 3 – Adjust CWIP item to Expense	<u>(\$8,847)</u>	<u>\$0</u>
Construction Work in Progress Adjustments	<u>(\$58,895)</u>	<u>\$0</u>
<b>Accumulated Depreciation</b>		
AF No. 3 – Adjust A/D for CWIP / PIS Reclassification	\$2,486	\$30,794
AF No. 6 – Increase A/D for Reclassified Capital Costs	(\$431)	(\$899)
AF No. 1 – Adjust A/D for Undocumented Plant	<u>\$29,050</u>	<u>\$35,972</u>
Accumulated Depreciation Adjustments	<u>\$31,105</u>	<u>\$65,867</u>

The company could not provide supporting documentation for \$142,789 in water plant and \$176,812 in wastewater plant. Staff made adjustments to remove these amounts and related Accumulated Depreciation of \$29,050 for water and \$35,972 for wastewater.

<sup>3</sup> Audit Control No. 09-021-2-1, Issued April 2009.

Because the majority of plant additions posted in the general ledger Plant in Service accounts are transferred from Construction Work In Progress (CWIP), staff also performed an analysis of CWIP. Staff made adjustments of \$50,048 to reclassify plant from water CWIP to wastewater Plant in Service, \$222,868 to reclassify plant from wastewater to water, \$15,000 to remove a duplicate payment made to a vendor for wastewater plant, \$2,486 to water and \$30,794 to wastewater Accumulated Depreciation to reduce Accumulated Depreciation related to the reclassifications, and \$8,847 to remove two water CWIP items which should have been expensed in prior years.

In 2004, the utility sold land with a book value of \$20,000. In 2005, the utility had an addition to wastewater land in the amount of \$50,585. As shown below, Land should be decreased by \$57,386 for water and \$207,861 for wastewater to reflect land value as determined by Commission Order No. PSC-00-0917-SC-WS.

	<b>Water</b>	<b>Wastewater</b>
Per Order – 12/31/98	\$95,500	\$300,000
Land sale - 2004	( <u>\$20,000</u> )	<u>0</u>
Land Value after sale	<u>\$75,900</u>	<u>\$300,000</u>
Additions - 2005	0	\$50,585
Per utility books	(\$133,286)	(\$558,446)
Staff Adjustment	<u>(\$57,386)</u>	<u>(\$207,861)</u>

Staff also determined that the utility expensed costs that should have been recorded as capital expenditures and charged to water and wastewater treatment systems. Staff made adjustments of \$34,476 to water Plant in Service and \$57,436 to wastewater Plant in Service to reclassify expensed plant to Plant in Service, and increased Accumulated Depreciation by \$431 for water and \$899 for wastewater accordingly.

Based on audit adjustments agreed to by the utility and staff, staff recommends that Plant in Service should be increased \$114,555 for water and decreased \$307,196 for wastewater, Land and Land Rights should be decreased by \$57,386 for water and \$207,861 for wastewater, Construction Work in Progress should be reduced by \$58,895 for water, and Accumulated Depreciation should be decreased \$31,105 for water and decreased \$65,867 for wastewater.

**Issue 5:** Should any additional adjustments be made to the utility's test year rate base?

**Recommendation:** Yes. Staff recommends that Plant in Service be reduced by an additional \$26,869 for water and increased by \$263,228 for wastewater, Construction Work in Progress should be reduced by an additional \$134,895 for water, Non-Used and Useful Plant in Service should be \$1,052,860, Accumulated Depreciation should be increased by an additional \$346,922 for water and \$348,671 for wastewater, and Average Unamortized Project Costs should be reduced by \$117,088 for water and \$67,088 for wastewater. (Mann, Casey)

**Staff Analysis:** Staff made adjustments of (\$21,224) to water and (\$17,106) to wastewater Plant in Service to reconcile the audited test year figures to the utility's filing. Staff also made adjustments of (\$5,645) to water and \$382,800 to wastewater Plant in Service to reflect averaging adjustments.

Staff performed an analysis of construction work in progress (CWIP) which consisted of: compiling all activity in each CWIP account for water subsequent to December 31, 1997, and wastewater subsequent to December 31, 1995; selecting line items that exceeded a certain threshold; requesting documentation which supports the selected line items; and determining that the documentation received is adequate and supports the sample items. Staff found insufficient or no documentation for \$145,941 in water CWIP and \$102,466 in wastewater CWIP. Staff decreased water CWIP by \$145,941, and wastewater Plant in Service by \$102,466. The wastewater CWIP entries were made prior to 2005 and had been moved to wastewater Plant in Service. Staff also made an adjustment of \$11,046 to include test year additions to CWIP.

In accordance with the engineering determination that 24 percent of the wastewater treatment plant should be considered nonused and useful (see Issue No. 3), wastewater Plant in Service should be decreased by \$1,052,860, and related Accumulated Depreciation should be decreased by \$266,100.

Staff made adjustments of (\$493,910) to water and (\$810,595) to wastewater Accumulated Depreciation to reconcile the audited test year figures to the utility's filing. Staff also made adjustments of \$146,988 to water and \$195,824 to wastewater Accumulated Depreciation to reflect averaging adjustments.

Southlake's MFRs included unamortized project costs of \$117,088 (\$50,000 for consumptive use permit and \$67,088 for rate case expense) for water and \$67,088 (rate case expense) for wastewater. Since these unamortized balances are non-annual project costs, staff made adjustments to remove them from rate base. Based on the above, staff recommends the following adjustments:

<b><u>Staff Adjustments</u></b>	<b><u>Water</u></b>	<b><u>Wastewater</u></b>
<b>Plant in Service (PIS)</b>		
To adjust PIS to year-end General Ledger Amount	(\$21,224)	(\$17,106)
To reflect PIS averaging adjustment	(\$5,645)	\$382,800
Adjust PIS for Lack of Documentation (AF No. 3)	\$0	(\$102,466)
Additional PIS Adjustments	<u>(\$26,869)</u>	<u>\$263,228</u>
<b>Construction Work In Progress</b>		
Adjust CWIP for Lack of Documentation (AF No. 3)	(\$145,941)	\$0
To include test year additions to CWIP	\$11,046	\$0
Additional CWIP Adjustments	<u>(\$134,895)</u>	<u>\$0</u>
<b>Non-Used and Useful PIS</b>		
Adjust PIS for Net Nonused and Useful	\$0	(\$1,052,860)
<b>Accumulated Depreciation</b>		
To adjust A/D to staff calculated General Ledger Amount	(\$493,910)	(\$810,595)
Adjust A/D on Nonused and Useful PIS	\$0	\$266,100
To reflect A/D averaging adjustment	\$146,988	\$195,824
Additional A/D Adjustments	<u>(\$346,922)</u>	<u>(\$348,671)</u>
<b>Average Unamortized (non-annual) Project Cost</b>		
Remove Unamortized Project Costs included in MFR's	<u>(\$117,088)</u>	<u>(\$67,088)</u>

Based on the above analysis, staff recommends that Plant in Service be reduced by an additional \$26,869 for water and increased by \$263,228 for wastewater, Construction Work in Progress should be reduced by an additional \$134,895 for water, Non-Used and Useful Plant in Service should be \$1,052,860, Accumulated Depreciation should be increased by an additional \$346,922 for water and \$348,671 for wastewater, and Average Unamortized Project Costs should be reduced by \$117,088 for water and \$67,088 for wastewater.

**Issue 6:** What is the appropriate working capital allowance?

**Recommendation:** The appropriate amount of working capital should be \$60,965 for water and \$93,214 for wastewater. (Mann, Casey)

**Staff Analysis:** Rule 25-30.433(2), F.A.C., requires that Class B utilities use the formula method, or one-eighth of operating and maintenance (O&M) expenses, to calculate the working capital allowance. The utility has properly filed its allowance for working capital using the formula method. Staff has recommended adjustments to Southlake's O&M expenses. As a result, staff recommends that working capital of \$60,965 and \$93,214 be approved for water and wastewater, respectively. This reflects a decrease of \$8,796 to the utility's requested working capital allowance of \$69,761 for water and a decrease of \$18,470 to Southlake's requested allowance of \$111,684 for wastewater. Details of the formula method for working capital are as follows:

<b><u>Working Capital</u></b>	<b><u>Water</u></b>	<b><u>Wastewater</u></b>
O&M	\$487,721	\$745,712
Working Capital Factor	<u>/8</u>	<u>/8</u>
Working Capital Allowance	\$60,965	\$93,214
Working Capital Allowance Per Filing	<u>\$69,761</u>	<u>\$111,684</u>
Adjustment	<u>(\$8,796)</u>	<u>(\$18,470)</u>

The appropriate amount of working capital for Southlake Utility should be \$60,965 for water and \$93,214 for wastewater.

**Issue 7:** Should any adjustments be made to the Contributions in Aid of Construction balances ending December 31, 2008?

**Recommendation:** Yes. Contributions in Aid of Construction (CIAC) should be increased by \$8,958 for water and \$7,525 for wastewater and the associated Accumulated Amortization of CIAC should be decreased by \$66,597 for water and \$162,935 for wastewater. (Mann, Casey)

**Staff Analysis:** Staff performed an analysis of CIAC for the years 1999 through 2008. Adjustments of (\$22,786) to water and (\$27,191) to wastewater were made to increase CIAC to the adjusted general ledger amount. Staff also calculated averaging adjustments of \$13,828 for water and \$19,666 for wastewater to reflect average balances. Staff recommends test year CIAC of \$3,955,193 for water and \$5,360,474 for wastewater

For Accumulated Amortization of CIAC, staff made adjustments of (\$18,403) to water and (\$99,460) to wastewater to decrease Accumulated Amortization of CIAC to the adjusted general ledger amount. Staff also calculated averaging adjustments of (\$48,194) for water and (\$63,475) for wastewater to reflect average balances. Staff recommends test year Accumulated Amortization of CIAC of \$824,009 for water and \$1,401,350 for wastewater.

**Issue 8:** What is the appropriate rate base for the December 31, 2008, test year?

**Recommendation:** Based on staff's recommended adjustments, addressed in previous issues, the appropriate average rate base for the test year ending December 31, 2008, is \$3,312,594 for water and \$534,143 for wastewater. (Mann, Casey)

**Staff Analysis:** Based on staff's recommended adjustments addressed in previous issues, the appropriate average rate base for the December 31, 2008 test year is \$3,312,594 for water and \$534,143 for wastewater. Staff's recommended water and wastewater rate bases are shown on Schedules Nos. 1-A and 1-B, respectively. The adjustments to rate base are shown on Schedule No. 1-C.



**Issue 9:** What is the appropriate return on equity?

**Recommendation:** Based on the Commission's approved 2009 leverage formula and an equity ratio of 100 percent, the appropriate return on equity (ROE) is 9.67 percent for the wastewater rate base. However, due to the utility's noncompliance with the SJRWMD, the ROE for the water rate base should be reduced 100 basis points to 8.67 percent. At such time as the utility is in compliance with all conditions listed in its current CUP, the utility may petition the Commission for removal of the 100 basis points reduction to ROE. (Mann, Casey, Lingo)

**Staff Analysis:** The ROE requested in the utility's filing is 9.56 percent for the test year ending December 31, 2008. It appears that the utility used the 2008 leverage formula and incorrectly included deposits when calculating the equity ratio. Based on the Commission's 2009 leverage formula<sup>4</sup> and an equity ratio of 100 percent, staff calculated an ROE of 9.67 percent. However, based on the utility's noncompliance with the St. Johns River Water Management District, staff believes a reduction in ROE for the water system is appropriate.

Southlake is located in the Central Florida Coordination Area (CFCA), encompassing portions of the St. Johns River, Southwest and South Florida Water Management Districts. These water management districts jointly concluded in 2006 that the availability of sustainable quantities of groundwater in central Florida are insufficient to meet future public water supply demands in the region. In addition, these water management districts concluded that alternative water supply sources must be developed to meet increased demands in central Florida beyond 2013. The requirement to develop alternative water supplies was incorporated by rule amendment in February 2008.<sup>5</sup>

Southlake's noncompliance with the St. Johns River Water Management District (SJRWMD or District) has been ongoing since 2004. In March of 2005, the District issued the utility a Notice of Violation because the utility exceeded its allocated withdrawal in 2004 by 66.5 million gallons (66.5 mgals), or approximately 16 percent. Subsequently, the utility exceeded its allocated withdrawal in 2005 by 239.8 mgals, or approximately 57 percent. These violations resulted in an executed Consent Order between the District and the utility in July 2006. The primary condition of the Consent Order was that the utility not undertake any further withdrawals of water except as authorized by District permit or the Consent Order. Additionally, the Consent Order required the utility to retain a half-time position for a Water Conservation Compliance Coordinator and a full-time position for a Water Conservation field officer.<sup>6</sup>

On July 11, 2006, the District issued Southlake a CUP renewal, with an expiration date of January 1, 2009. District staff had concerns that withdrawals exclusively from the Upper Floridan Aquifer (UFA) to meet projected future demands had the potential for contributing adverse impacts to water resources and related natural systems. Based on the utility's past noncompliance, and the need to reduce or eliminate withdrawals from the Upper Floridan Aquifer as soon as possible, the permit was issued for a short duration (two and one-half years),

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<sup>4</sup> See Order No. PSC-09-0430-PAA-WS, issued June 19, 2009, in Docket No. 090006-WS, In re: Water and Wastewater Industry Annual Reestablishment of Authorized Range of Return on Common Equity for Water and Wastewater Utilities Pursuant to Section 367.081(4)(f), F.S.

<sup>5</sup> Rule 40C-2. Specifics are incorporated by rule in the Applicant's Handbook (sections 3.1.7, 6.5.4, and 12.10.)

<sup>6</sup> See F.O.R. 2006-57, issued July 12, 2006, In re: Southlake Utilities, 16654 Crossing Blvd., Suite 2, Clermont, FL, 34711, CUP No. 2392.

with an expiration date of January 1, 2009. The District placed 37 conditions in the permit.<sup>7</sup> Substantive conditions in the permit include:

- 1) timely submission of periodic reports regarding water level data from UFA well C;
- 2) implementation of the utility's water conservation plan on file with the District;
- 3) a requirement of alternative distribution lines in new developments to enable reuse;
- 4) initiation of a PSC rate case for a water conserving rate structure, and keeping the District apprised of increased operating costs and construction programs, and how these will contribute to favorable conditions of the rate case;
- 5) initiation of upgrades to the wastewater treatment plant and distribution lines by January 1, 2008, unless otherwise agreed to by the District;
- 6) submission, upon completion, of a report summarizing the testing plan for Lower Floridan Aquifer (LFA) well F, and if blending UFA and LFA water is proposed, a demonstration that UFA withdrawals will not cause environmental harm;
- 7) a requirement that the three wetlands identified in the permit be monitored;
- 8) if significant unanticipated impacts to wetlands occurs, the District shall revoke the permit, in whole or in part, until adverse impacts are mitigated;
- 9) within 18 months of permit issuance, the utility shall identify viable, potential water supply partners regarding development of water supply; and
- 10) total withdrawals are not to exceed 715.4 mgals in 2006, 919.8 mgals in 2007 and 1,040.25 mgals in 2008.

In April 2007, less than one year after the issuance of its CUP renewal, the District issued the utility a Notice of Violation regarding noncompliance with several of the conditions contained in the CUP.<sup>8</sup> In addition, in January 2009, the District received a report from CH2M Hill, which concluded that there appeared to be a drawdown of two feet in the surficial aquifer and three feet in the UFA.

Currently, the utility is in substantial noncompliance with its CUP. Based on information obtained from the District,<sup>9</sup> the utility has committed 22 violations and received 7 citations from July 11, 2006 through January 1, 2009. Issues of noncompliance include or have included:

- 1) failure to keep the SJRWMD apprised of the status of construction programs and increased operating costs, and how these activities contribute to favorable conditions for initiating a rate case with the Commission to develop a water-conserving rate structure;

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<sup>7</sup> SJRWMD Consumptive Use Permit no. 2392 (District document no. Permit wC 2392 6.tif).

<sup>8</sup> SJRWMD violation notice letter (District document no. VioNtcLtr 2392 6 1247545.tif).

<sup>9</sup> SJRWMD, Comprehensive Compliance Review, August 3, 2009.

- 2) failure to maintain flow meter accuracy thresholds;
- 3) failure to submit periodic reports of weekly water level data taken from UFA Well C;
- 4) failure to conduct hydrologic and photo monitoring of specified wetland areas;
- 5) adversely impacting wetlands, lakes or spring flows; and
- 6) failure to identify viable, potential water supply partners by January 2008.

Southlake and the SJRWMD have met on several occasions to discuss Southlake's noncompliance and possible remedies, but no agreements have been reached.

Staff believes that the ultimate responsibility of the prior and current noncompliance rests with the utility. The Commission has the authority to reduce a utility's ROE, and in certain situations has done so. Section 367.111(2), Florida Statutes, provides that:

If the commission finds that a utility has failed to provide its customers with water or wastewater service that meets the standards promulgated by the Department of Environmental Protection or the water management districts, the commission may reduce the utility's return on equity until the standards are met.

Therefore, based on the utility's history of severe and continued noncompliance with the conditions of its consumptive permit with the SJRWMD, staff recommends that a reduction to the ROE for the utility's water system is appropriate.

**Staff is unaware of a case in which the Commission has used its authority to reduce a utility's ROE due to noncompliance issues with a Water Management District (WMD). However, DEP is a supervising agency of the WMDs. For example, DEP is involved in managing the quality and quantity of water through its relationship with the state's five WMDs.<sup>10</sup> Furthermore, the Commission has used the above-referenced statute to reduce a utility's ROE due to noncompliance with DEP. In a recent case involving Aqua Utilities Florida, Inc., the Commission found that the overall quality of service for the Chuluota and The Woods water systems was unsatisfactory, and that the ROE for each system should be reduced by 100 basis points. The ROE reductions remain in effect until DEP closes the Consent Orders and satisfactory standards are met for those systems.<sup>11</sup>**

Courts have affirmed reductions to ROE for poor quality of service or mismanagement, as long as the reductions kept the utility's rate of return within the fair range. In a case involving Gulf Power, the Florida Supreme Court held that so long as the final number remains within the authorized range, the Commission could adjust the rate of return for mismanagement. The Court

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<sup>10</sup> <http://www.dep.state.fl.us/secretary/watman/>.

<sup>11</sup> See Order No. PSC-09-0385-FOF-WS, issued May 29, 2009, in Docket No. 080121-WS, In re: Application for increase in water and wastewater rates in Alachua, Brevard, Desoto, Highlands, Lake, Lee, Marion, Orange, Palm Beach, Pasco, Polk, Putnam, Seminole, Sumter, Volusia, and Washington Counties by Aqua Utilities Florida, Inc. For The Woods water system, the Commission was subsequently provided with a letter from DEP that showed the water standards for that system were being met and that the Consent Order had been closed. Therefore, the ROE for The Woods was then increased by 100 basis points.

held that the adjustment of Gulf Power's rate of return within the fair rate of return range falls within those powers expressly granted by statute or by necessary implication, and that inherent in the authority to adjust for management efficiency is the authority to reduce the rate of return for mismanagement, as long as the resulting rate of return falls within the reasonable range.<sup>12</sup>

For the foregoing reasons, and based upon the utility's history and continued noncompliance with the SJRWMD, the Gulf Power and Aloha cases, Commission precedent, and statutory authority, staff recommends that the allowed ROE for the water system be reduced by 100 basis points. The recommended adjustment to the utility's ROE will still permit the utility the opportunity to earn a reasonable rate of return. At such time as the utility is in compliance with all conditions listed in its current CUP, the utility may petition the Commission for removal of the 100 basis points reduction to ROE. This is consistent with other cases in which the commission approved a reduction to ROE.<sup>13</sup>

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<sup>12</sup> See Gulf Power Company v. Wilson, 597 So. 2d 270 (Fla. 1992), where the Commission's reduction of the utility's ROE by 50 basis points for corrupt practices was approved by the Supreme Court of Florida. See also Order No. PSC-02-0593-FOF-WS, issued April 30, 2002, in Docket No. 010503-WU, In re: Application for increase in water rates for Seven Springs System in Pasco County by Aloha Utilities, Inc. The Order was "Per Curiam, Affirmed" on appeal (See Aloha Utilities, Inc. v. Fla. PSC, 848 So. 2d 307 (Fla. 1<sup>st</sup> DCA 2003)). In the Aloha Order, the Commission reduced the ROE by 100 basis points, upon finding that the quality of the utility's product and operational conditions was satisfactory, but customer satisfaction and overall quality of service was unsatisfactory.

<sup>13</sup> See Docket No. 950495-WS, Order No. PSC-96-1320-FOF-WS, issued October 30, 1996, In re: Application for rate increase and increase in service availability charges by Southern States Utilities, Inc. for Orange-Osceola Utilities, Inc. in Osceola County, and in Bradford, Brevard, Charlotte, Citrus, Clay, Collier, Duval, Highlands, Lake, Lee, Marion, Martin, Nassau, Orange, Osceola, Pasco, Putnam, Seminole, St. Johns, St. Lucie, Volusia, and Washington Counties.

**Issue 10:** What is the appropriate overall weighted average cost of capital including the proper components, amounts, and cost rates associated with the capital structure for the test year ending December 31, 2008?

**Recommendation:** The appropriate overall weighted average cost of capital for the test year ending December 31, 2008, is 8.52 percent for water and 9.47 percent for wastewater. (Mann, Casey)

**Staff Analysis:** As required by Rule 25-30.033(1)(w), F.A.C., a schedule of the utility's capital structure was included in the application. The test year amounts for cost of capital were taken directly from Southlake's MFR filing Schedule D-1. Based on the proper components, amounts, and cost rates associated with the capital structure for the test year ending December 31, 2008, and the different water and wastewater ROEs explained in Issue 9, staff recommends that the overall weighted average cost of capital for water is 8.52 percent and the overall weighted average cost of capital for wastewater is 9.47 percent. Schedule No. 2 details staff's recommendation. As shown on Schedule No. 2, the utility's capital structure consists of common equity and customer deposits. These rates are the result of using the Commission's 2009 water and wastewater return on equity leverage graph formula.

## **NET OPERATING INCOME**

**Issue 11:** Should any adjustments be made to operation and maintenance expenses?

**Recommendation:** Yes, adjustments should be made to reduce water O&M by \$137,243 and reduce wastewater O&M by \$181,305. (Mann, Casey)

**Staff Analysis:** O&M Expense - Staff performed an analysis of O&M expenses for water and wastewater to determine if the amounts recorded in the general ledger were accurately stated and to determine if a difference exists between O&M expenses reported in the general ledger and O&M expenses reported in the filing. The company filing includes O&M expenses based upon projections for the calendar year 2008. Total O&M expenses per the utility filing are \$624,964 for water and \$927,017 for wastewater. Test year general ledger balances for O&M water and wastewater expenses are \$589,016 and \$929,931, respectively, a difference of (\$35,948) for water and \$2,914 for wastewater. An adjustment of (\$35,948) for water and \$2,914 for wastewater should be made to the filing to reconcile the utility's filing and the test year general ledger amounts.

Rate Case Expense - Staff's calculated rate case expense should be recovered over four years for an annual expense of \$62,283 with \$31,141 allocated to water and \$31,141 allocated to wastewater. As recommended in audit finding No. 6, staff removed utility rate case expense of \$68,307 for water and \$67,307 for wastewater included in the test year. See Issue No. 12.

Consumptive Use Permit - In 2008, the company began preparation of a consumptive use permit (CUP) required by the St. John's River Water Management District (SJRWMD). Anticipated costs, as calculated by the company, total \$103,950. Based on the last CUP issued, it appears that Southlake's CUP will be issued by the SJRWMD for a period of three years. Because of Southlake's non-compliance with SJRWMD requirements, it may be a period of time before the actual CUP is issued. Staff believes an appropriate amortization period for the CUP should be five years based on Rule 25-30.433(8), Florida Administrative Code, which states "Non-recurring expenses shall be amortized over a 5-year period unless a shorter or longer period of time can be justified." It is unknown at this time if or when Southlake will be issued its CUP. Staff used a five year period for amortization of this permit with annual amortization of \$20,790. Costs incurred and expensed during the test period for the CUP are \$11,389. Therefore, staff recommends inclusion of an additional \$9,401 in CUP permit costs for the test year.

Purchased Power - The company's general ledger showed purchased power expense of \$66,977 for water and \$115,841 for wastewater for the test year. Per the audit, purchased power expense for the test year of 2008 was \$68,692 for water and \$117,814 for wastewater. Staff made adjustments of \$1,715 for water and \$1,973 for wastewater purchased power expense. This was done to include purchased power expense that was incurred during the test period, but billed after the test period.

Land Lease - According to the audit report, for the test year, the utility had a capital lease agreement with Southlake Development, Ltd. A capital lease requires a company to record the plant asset on its books and records, with payments made to the lessor used to reduce the cost of land lease obligation. Instead, the utility recorded the payments to expense accounts 641 and 741 (Rental of Building - Real Property) in the amounts of \$11,778 and \$45,299, respectively.

As this property is now owned by the utility, staff recommends that these costs be removed from O&M expenses.

Contractual Services – Other - The company included Contractual Services-Other costs of \$8,250 in water and \$8,250 in wastewater for the test year which were out-of-period non-recurring expenses. The costs were incurred in connection with an examination by the Internal Revenue Service for the 2005 tax year. Staff removed these costs as out-of-period expenses.

Communication Expense - Staff reviewed postage costs included in the utility's communications expense account. Auditors found support for \$1,324 of water and \$1,324 of wastewater postage expense. The utility recorded \$1,750 of water and \$1,750 of wastewater postage expense. Staff made adjustments of (\$426) to water and (\$426) to wastewater communication expense to reflect the unsupported postage cost.

Reclassification of Capital Costs - Staff determined that the utility expensed certain costs that should have been recorded as capital expenditures. Staff reclassified the following costs from O&M expenses to rate base:

	<u>Water</u>	<u>Wastewater</u>
Mapping	\$34,476	\$34,477
Sanitary Lateral Connection	0	\$5,700
Lift Station Construction	0	\$17,259
Total	<u>\$34,476</u>	<u>\$57,436</u>

Unsupported Expense - The utility bears the responsibility of maintaining documentation which supports its general ledger amounts. During the audit analysis of O&M expense, the utility could not provide supporting documentation for certain expense items recorded in the general ledger. Unsupported water expense totaled \$20,315 and wastewater expense totaled \$38,615. Staff recommends that these amounts be removed from O&M for the test year.

### **Conclusion**

In conclusion, based on the above adjustments, along with rate case expense (See Issue No. 12), staff recommends that O&M expenses be reduced by \$137,243 for water and \$181,305 for wastewater. The following table reflects staff's O&M expense adjustments for the test year ending December 31, 2008.

<b>Description of O&amp;M Expense</b>	<b>Staff Adjustments to 2008 O&amp;M</b>	
	<b>Water</b>	<b>Wastewater</b>
To adjust filing to 12/31/2008 General Ledger (AF No. 6)	(\$35,948)	\$2,914
To reflect staff calculated Rate Case expense	31,141	31,141
To reflect CUP cost amortized over 3 year period.	9,401	0
To adjust purchased power to test year amount	1,715	1,973
To remove land lease expense (AF No. 6)	(11,778)	(45,299)
To remove out of test year contractual services	(8,250)	(8,250)
To reflect actual test year postage cost	(426)	(426)
To reflect audit finding regarding reclassification of capital costs (AF No. 6)	(34,476)	(57,436)
To reflect audit finding regarding Undocumented Costs (AF No. 6)	(20,315)	(38,615)
To remove test year rate case expense (AF No. 6)	(68,307)	(67,307)
Total	(\$137,243)	(\$181,305)



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

**Recommendation:** The appropriate amount of rate case expense for this docket is \$249,131. This expense should be recovered over four years for an annual expense of \$62,283 allocated \$31,141 for water and \$31,141 for wastewater. (Mann, Casey)

**Staff Analysis:** Southlake initially submitted in its MFRs \$268,350 in rate case expense, with an annual amortization expense of \$67,088. The utility subsequently updated its estimated rate case expenses to \$360,353. The breakdown of fees is shown below as reflected in the Utility's MFRs.

	<u>MFR</u> <u>Estimated</u>	<u>Utility Revised</u> <u>Actual</u>
Acctg/Eng- Guastella & Assoc./Printing/Noticing	\$158,350	\$243,777
Legal- James Ade	77,000	87,851
In house/Administrative - Cagan & Kitchens	10,000	10,000
Accounting – DeNagy/Corbin	15,000	10,725
Filing Fee	<u>8,000</u>	<u>8,000</u>
Total	<u>\$268,350</u>	<u>\$360,353</u>

Pursuant to Section 367.081(7), F.S., the Commission shall determine the reasonableness of rate case expenses and shall disallow all rate case expenses determined to be unreasonable. Staff has examined the requested actual expenses, supporting documentation, and estimated expenses as listed above for the current rate case. Based on its review, staff believes several adjustments are necessary to the revised rate case expense estimate.

The first adjustment is in regards to the hourly rate charged by Guastella Associates which includes services by Mr. Guastella and Mr. White. In this proceeding, Mr. Guastella and Mr. White charged between \$195 - \$275 per hour for rate case expense. According to the invoices submitted, 1,142.5 total hours were billed for services provided by Mr. Guastella and Mr. White. Staff believes the hourly rates of \$195 - \$275 per hour are high compared to other accounting and rate consultants that practice before the Commission. While Southlake's decision to retain Guastella Associates for their expertise is reasonable, it does not automatically follow that the customers should have to bear the full costs for their services. The Commission has previously reduced Mr. Guastella's hourly rate and found that an hourly rate of \$140 was appropriate.<sup>14</sup> Applying a similar rate reduction in this docket results in a decrease to consulting and accounting fees of \$79,380.

The second adjustment involves costs incurred to correct deficiencies in the MFR filing. Based on information obtained from Guastella Associates and Southlake's Counsel, Southlake was billed \$7,695 by Guastella Associates and \$3,835 by Jim Ade for correcting the MFR deficiencies and revising the utility's filing. The Commission has previously disallowed rate

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<sup>14</sup> See Order Nos. PSC-09-0385-FOF-WS, issued May 29, 2009, in Docket No. 080121-WS, In Re: Application for increase in water and wastewater rates in Alachua, Brevard, DeSoto, Highlands, Lake, Lee, Marion, Orange, Palm Beach, Pasco, Polk, Putnam, Seminole, Sumter, Volusia, and Washington Counties by Aqua Utilities Florida, Inc. and PSC-01-0327-PAA-WU, issued February 6, 2001, in Docket No. 000295-WU, In Re: Application for increase in water rates in Highlands County by Placid Lakes Utilities, Inc.

case expense associated with correcting MFR deficiencies because of duplicate filing costs.<sup>15</sup> Accordingly, staff recommends that \$11,530 (\$7,695 + \$3,835) be removed as duplicative and unreasonable rate case expense.

The third adjustment relates to costs incurred meeting with the St. Johns River Water Management District to discuss Southlake's non-compliance with SJRWMD. Staff believes these costs would not have been necessary if Southlake had fulfilled the requirements agreed to in its consumptive use permit issued three years ago. Staff believes customers should not have to pay for Southlake's non-compliance with SJRWMD requirements. Staff removed \$3,221 of Guastella Associates costs and \$7,092 of Jim Ade's costs related to meeting with the SJRWMD regarding the non-compliance of Southlake.

Lastly, staff recommends that the estimated cost of \$10,000 for in-house rate case expense be eliminated. There is no supporting documentation that certain utility staff, who are already paid a salary, worked any overtime. Staff believes that this cost component is duplicative and should not be allowed.

It is the utility's burden to justify its requested costs. *Florida Power Corp. v. Cresse*, 413 So. 2d 1187, 1191 (Fla. 1982). Further, the Commission has broad discretion with respect to the allowance of rate case expense. It would constitute an abuse of discretion to automatically award rate case expense without reference to the prudence of the costs incurred in the rate case proceedings. *Meadowbrook Util. Sys., Inc. v. FPSC*, 518 So. 2d 326, 327 (Fla. 1st DCA 1987), rev. den. 529 So. 2d 694 (Fla. 1988).

In summary, staff recommends that Southlakes' revised rate case expense be decreased by \$111,222 for MFR deficiencies and for unsupported, unreasonable rate case expense. The appropriate total rate case expense should be \$249,131. A breakdown of rate case expense is as follows:

<u>Description</u>	<u>MFR</u>	<u>Utility</u> <u>Revised</u> <u>Actual</u>	<u>Staff</u> <u>Adjustments</u>	<u>Total</u>
Legal Fees	\$77,000	\$87,851	(\$10,927)	\$76,924
Consultant Fees-G&W/Noticing	158,350	243,777	(90,295)	153,482
Consultant Fees- DeNagy/Corbin	15,000	10,725	0	10,725
In-House Fees-Cagan/Kitchens	10,000	10,000	(10,000)	0
Filing Fee	8,000	8,000	0	8,000
<b>Total Rate Case Expense</b>	<b>\$268,350</b>	<b>\$360,353</b>	<b>(\$111,222)</b>	<b>\$249,131</b>
<b>Annual Amortization</b>	<b>\$67,088</b>	<b>\$90,088</b>	<b>(\$27,806)</b>	<b>\$62,283</b>

<sup>15</sup> See Order Nos. PSC-05-0624-PAA-WS, issued June 7, 2005, in Docket No. 040450-WS, *In Re: Application for rate increase in Martin County by Indiantown Company, Inc.*; and PSC-01-0326-FOF-SU, issued February 6, 2001, in Docket No. 991643-SU, *In Re: Application for increase in wastewater rates in Seven Springs System in Pasco County by Aloha Utilities, Inc.*

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Southlake's revised estimate of total rate case expense is \$360,353, which amortized over four years, would be \$90,088. The recommended total rate case expense should be amortized over four years, pursuant to Section 367.0816, F.S. Based on the data provided by Southlake and the recommended adjustments discussed above, staff recommends annual rate case amortization of \$62,283 allocated \$31,141 for water and \$31,141 for wastewater.

**Issue 13:** Should any adjustments be made to the 2008 test year taxes other than income for water and wastewater?

**Recommendation:** Yes. Taxes other than income for the 2008 test year should be decreased by \$351 for water and decreased by \$15,268 for wastewater. (Mann, Casey)

**Staff Analysis:** Audit Finding No. 7 shows that taxes other than income should be increased by \$12,884 for water and \$17,114 for wastewater. Staff determined that the payroll tax was overstated by \$134 and \$104, respectively, for water and wastewater. The utility filing understated the taxes other than income general ledger balance by \$17,979 for water and \$22,137 for wastewater. In addition, the filing overstated regulatory assessment fees recorded in the general ledger by \$4,961 for water and \$4,919 for wastewater. Details of these adjustments are as follows:

<b>Taxes Other Than Income</b>			
<b>Description</b>	<b>Water</b>	<b>Wastewater</b>	<b>Total</b>
Payroll Taxes – AF No. 7	(\$134)	(\$104)	(\$238)
Property Tax – AF No. 7	\$17,979	\$22,137	\$40,116
RAF – AF No. 7	(\$4,961)	(\$4,919)	(\$9,880)
Total Adjustment	<u>\$12,884</u>	<u>\$17,114</u>	<u>\$29,998</u>

Due to the nonused and useful adjustment for the wastewater plant (See Issue No. 4), staff believes it is appropriate to decrease property tax expense for the wastewater system by \$5,506. Details of this adjustment are as follows:

<b>Non-Used and Useful Adjustment to Property Taxes</b>		
<b>Description</b>	<b>Water</b>	<b>Wastewater</b>
Non-used and Useful PIS Adjustment	\$0	(\$1,052,860)
Property Tax Rate 0.523%	0.523%	0.523%
Property Tax Adjustment	\$0	(\$5,506)

The utility included regulatory assessment fees of \$8,273 for water and \$21,956 for the adjusted test year, based on the utility calculated revenue increase. Staff reduced regulatory assessment fees by \$8,273 for water and \$21,956 for wastewater for calculation of staff recommended test year revenue. Staff also reduced regulatory assessment fees by \$4,962 for water and \$4,920 for wastewater to reflect RAFs on actual test year revenues. Combining these adjustments, along with the adjustment for regulatory assessment fees for the adjustment to revenue, taxes other than income for the 2008 test year should be decreased by \$351 for water and decreased by \$15,268 for wastewater, as shown below.

<b>Staff Adjustments To Taxes Other Than Income</b>	<b>Water</b>	<b>Wastewater</b>
Taxes Other than Income	\$12,884	\$17,114
Non-Used and Useful Adjustment to Property Taxes	\$0	(\$5,506)
Test year RAFs	(\$13,235)	(\$26,876)
	<u>(\$351)</u>	<u>(\$15,268)</u>

**Issue 14:** Should any adjustments be made to net depreciation expense for 2008 for water and wastewater?

**Recommendation:** Yes. Net depreciation expense for water should be increased by \$101,340 and net depreciation expense for wastewater should be increased by \$158,456. (Mann, Casey)

**Staff Analysis:** Southlake's filing included test year depreciation expense of \$201,627 for water and \$391,647 for wastewater. Staff calculated test year depreciation is \$293,976 for water and \$263,580 for wastewater. Staff made adjustments of \$92,349 to water and \$128,067 to wastewater to reflect test year depreciation.

Audit finding No. 1 found that \$142,789 of water and \$176,812 of wastewater plant in service did not have supporting documentation and should be removed from rate base. Related depreciation for these amounts are \$4,469 for water and \$5,534 for wastewater which should be removed from test year depreciation expense.

Audit finding No. 6 reclassified \$34,476 of water and \$57,436 of wastewater costs which were expensed by the utility to capital expenditures. The related depreciation expense is \$431 for water and \$899 for wastewater. Test year depreciation should be increased by \$431 for water and \$899 for wastewater.

Audit finding No. 3 reclassified Plant in Service between water and wastewater accounts. Staff made adjustments of \$1,401 to water depreciation expense and (\$9,086) to wastewater depreciation expense to reflect depreciation related to the reclassifications.

In accordance with the engineering determination that 24 percent of the wastewater treatment plant should be considered nonused and useful, staff made an adjustment of (\$32,955) to reflect non-used and useful wastewater depreciation expense.

The utility's filing included \$125,541 of water CIAC amortization and \$227,098 of wastewater CIAC amortization for the test year. Staff calculated test year CIAC amortization is \$113,913 for water and \$150,033 for wastewater. Staff made adjustments of \$11,628 to water CIAC amortization and \$77,065 to wastewater CIAC amortization to reflect test year CIAC amortization.

Based on the above adjustments, net depreciation expense for water should be increased by \$101,340 and net depreciation expense for wastewater should be increased by \$158,456.

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**Issue 15:** What is the test year water and wastewater operating income before any revenue increases?

**Recommendation:** The test year operating income should be \$119,027 for water and (\$334,724) for wastewater. (Mann, Casey)

**Staff Analysis:** The utility adjusted test year revenues are \$1,184,327 for water and \$1,293,211 for wastewater. Staff made adjustments of (\$183,853) for water and (\$487,912) for wastewater to remove the utility's requested final revenue increase. Staff also made adjustments of (\$110,257) for water and (\$109,236) for wastewater to reflect overstated test year revenues in the utility's filing (see audit finding No. 5). Based on the above adjustments, the staff adjusted test year operating income should be \$119,027 for water and (\$334,724) for wastewater.

**Issue 16:** What is the appropriate pre-repression revenue requirement for the December 31, 2008 test year?

**Recommendation:** The following pre-repression revenue requirement should be approved. (Mann, Casey)

	<u>Test Year</u> <u>Revenues</u>	<u>Increase</u>	<u>Revenue</u> <u>Requirement</u>	<u>Increase</u>
Water	\$890,217	\$170,900	\$1,061,117	19.20%
Wastewater	\$695,973	\$403,436	\$1,099,409	57.97%

**Staff Analysis:** This issue is a summary computation that is subject to the resolution of other issues related to rate base, cost of capital, and is primarily a “fall-out” number. The computation of the revenue requirement is shown on Schedules No. 3-A and 3-B. This results in a revenue requirement of \$1,061,117 which represents an increase of \$170,900 or 19.20 percent for water and \$1,099,40 which represents an increase of \$403,436 or 57.97 percent for wastewater. These recommended pre-repression revenue requirements will allow the utility the opportunity to recover its expenses and earn a overall 8.52 percent return on its investment in water and a 9.47 percent return on its investment in wastewater rate base.

**Issue 17:** What are the appropriate rate structures for the utility's respective water and wastewater systems?

**Recommendation:** The appropriate rate structure for the utility's water system is a three-tiered inclining-block rate structure applicable to residential customers. The appropriate usage blocks should be for monthly consumption of: 1) 0-10,000 gallons (10 kgal); 2) 10,001-20 kgal; and 3) consumption in excess of 20 kgal. The usage block rate factors should be 1.0, 1.5, and 2.0, respectively. The base facility charge (BFC)/uniform gallonage charge rate structure should be applied to the utility's general service water customers. The BFC cost recovery allocation for the water system should be set at 34.8 percent. The appropriate rate structure for the utility's wastewater customers is the BFC/gallonage charge rate structure. Residential wastewater consumption should be capped for billing purposes at 10 kgal per month. The general service wastewater gallonage charge should be 1.2 times the corresponding residential gallonage charge. The BFC cost recovery allocation for the wastewater system should be set at 50 percent. (Lingo)

**Staff Analysis:** The current rate structure for the utility's water system is the BFC/uniform gallonage charge rate structure, with a monthly BFC for a 5/8" x 3/4" meter of \$8.98. Customers are also charged \$0.84 for each 1,000 gallons (kgal) used. This rate structure is considered usage-sensitive, because customers are charged for all gallons consumed. The residential customer base is nonseasonal, with an average consumption per customer of 12.4 kgal per month. The current rate structure for the utility's wastewater system is the BFC/gallonage charge rate structure, with a monthly BFC for a 5/8" x 3/4" meter of \$9.76. Residential customers are charged \$0.86 for each 1,000 kgal used, with a cap on billed monthly consumption of 10 kgal. General service customers are charged \$1.02 per kgal used, with no cap on billed consumption.

Staff takes several things into consideration when designing rates, including the current rate structure, characteristics of the utility's customer base, various conditions of the utility's Consumptive Use Permit, current and anticipated climatic conditions in the utility's service area, and the magnitude of the recommended revenue increase. Based on the magnitude of recommended water system revenue increase, coupled with the need to reduce consumption to the extent possible, staff's recommended rate structure for the water system places the entire revenue requirement increase into the gallonage charge. Staff's recommended rate structure, plus two alternative rate structures, is shown on Table 17-1 on the following page. As indicated by the values shown on Table 17-1, when compared to the current rate structure, Alternatives 1 and 2 both result in price decreases at certain levels of consumption. Therefore, staff believes that its recommended rate structure would be more effective than the alternatives presented in encouraging water conservation.



**TABLE 17-1**

<b>SOUTHLAKE UTILITIES, INC.</b>			
<b>STAFF'S RECOMMENDED AND ALTERNATIVE RATE STRUCTURES</b>			
<b>FOR THE WATER SYSTEM'S RESIDENTIAL CUSTOMERS</b>			
<b>PRE-REPRESSION ANALYSIS</b>			
<b>Current Rate Structure and Rates</b>		<b>Recommended Rate Structure and Rates</b>	
BFC/uniform kgal		Three-Tiered Inclining-Blocks – Monthly Consumption of 0-10 Kgals; 10.001-20 Kgals; 20+ Kgals // BFC = 34.8 percent Rate Factors @ 1.0, 1.5 and 2.0	
BFC	\$8.98	BFC	\$8.98
All kgals	\$0.84	0-10 Kgals	\$0.95
		10.001-20 Kgals	\$1.43
		In Excess of 20 Kgals	\$1.91
<b>Typical Monthly Bills</b>		<b>Typical Monthly Bills</b>	
<b>Cons (kgal)</b>		<b>Cons (kgal)</b>	
0	\$8.98	0	\$8.98
5	\$13.18	5	\$13.73
10	\$17.38	10	\$18.48
15	\$21.58	15	\$25.63
20	\$25.78	20	\$32.78
25	\$29.98	25	\$42.33
<b>Alternative 1</b>		<b>Alternative 2</b>	
Three-Tiered Inclining-Blocks – Monthly Consumption of 0-10 Kgals; 10.001-20 Kgals; 20+ Kgals // BFC = 30 percent Rate Factors @ 1.0, 1.5 and 2.0		Three-Tiered Inclining-Blocks – Monthly Consumption of 0-10 Kgals; 10.001-20 Kgals; 20+ Kgals // BFC = 34.8 percent Rate Factors @ 1.0, 2.0 and 3.0	
BFC	\$7.75	BFC	\$8.98
0-10 Kgals	\$1.02	0-10 Kgals	\$0.76
10.001-20 Kgals	\$1.53	10.001-20 Kgals	\$1.53
In Excess of 20 Kgals	\$2.04	In Excess of 20 Kgals	\$2.29
<b>Typical Monthly Bills</b>		<b>Typical Monthly Bills</b>	
<b>Cons (kgal)</b>		<b>Cons (kgal)</b>	
0	\$7.75	0	\$8.98
5	\$12.85	5	\$12.78
10	\$17.95	10	\$16.58
15	\$25.60	15	\$24.23
20	\$33.25	20	\$31.88
25	\$43.45	25	\$43.33

In order to recognize the capital intensive nature of wastewater facilities, staff recommends that the wastewater BFC should be set to recover 50% of the revenue requirement. Both the residential and general service gallonage charge portions of the utility's wastewater rate structure are consistent with Commission practice. A complete discussion of staff's rate structure methodology is contained in Attachment A.

Based on the foregoing, the information contained on Table 17-1, and the discussion contained in Attachment A, staff recommends that the appropriate rate structure for the utility's water system is a three-tiered inclining-block rate structure, applicable to residential customers,

with usage blocks for monthly consumption of: 1) 0-10 kgals; 2) 10.001-20 kgals; and 3) consumption in excess of 20 kgals. The usage block rate factors should be 1.0, 1.5, and 2.0, respectively. The BFC/uniform gallonage charge rate structure should be applied to the utility's general service water customers. The BFC cost recovery allocation for the water system should be set at 34.8 percent. The appropriate rate structure for the utility's wastewater customers is the BFC/gallonage charge rate structure. Residential wastewater consumption should be capped for billing purposes at 10 kgal per month. The general service wastewater gallonage charge should be 1.2 times the corresponding residential gallonage charge. The BFC cost recovery allocation should be set at 50 percent.

**Issue 18:** Are repression adjustments to the utility's water and wastewater systems appropriate in this case, and, if so, what are the appropriate adjustments to make for this utility?

**Recommendation:** Yes, repression adjustments are appropriate. Residential water consumption should be reduced by 3.1 percent, resulting in a consumption reduction of approximately 7,960 kgals. Total residential water consumption for ratesetting is 246,880 kgals. Total water consumption for ratesetting is 531,728 kgals, which represents a 1.5 percent reduction in overall consumption. The resulting water system reductions to revenue requirements are \$1,013 in purchased power expense, \$417 in chemicals expense and \$67 in RAFs. The post-repression revenue requirement for the water system is \$1,045,475.

Residential wastewater consumption should be reduced by 1.1 percent, resulting in a consumption reduction of approximately 1,492.0 kgals. Total residential wastewater consumption for ratesetting is 133,409.0 kgals. Total wastewater consumption for ratesetting is 355,678.0 kgals, which represents a 0.4 percent reduction in overall consumption. The resulting wastewater system reductions to revenue requirements are \$897 in sludge removal expense, \$492 in purchased power expense, \$134 in chemicals expense, and \$72 in RAFs. The post-repression revenue requirement for the wastewater system is \$1,097,813.

In order to monitor the effects of both the changes in revenues and rate structure, the utility should be ordered to prepare monthly reports detailing the number of bills rendered, the consumption billed and the revenues billed for each system. In addition, the reports should be prepared, for both the water and wastewater systems, by customer class and meter size. **The reports should be filed with staff, on a semi-annual basis, for a period of two years beginning the first billing period after the approved rates go into effect.** To the extent the utility makes adjustments to consumption in any month during the reporting period, the utility should be ordered to file a revised monthly report for that month within 30 days of any revision. (Lingo)

**Staff Analysis:** Using our database of utilities that have previously had repression adjustments made, staff calculated repression adjustments for this utility based upon the recommended increases in revenue requirements for the test year, while **using a price elasticity of demand of -0.2 applied to consumption in the second and third usage blocks, as requested by the Utility in its filing. Although the Commission typically approves a price elasticity of demand of -0.4, staff used the Utility's requested value of -0.2.** Aside from the use of a price elasticity of -0.2 rather than -0.4, the methodology for calculating repression adjustments is same methodology that the Commission has approved in prior cases.<sup>16</sup>

**The filing requirements for these repression reports have traditionally been on a quarterly basis. In the recent Labrador Utilities' case in Docket No. 080249-WS, the Commission approved requiring the reports on a semi-annual, rather than a quarterly, basis.<sup>17</sup> For the purposes of consistency and equal treatment among utilities, staff recommends that, on a going-forward basis, the reporting period be on a semi-annual**

<sup>16</sup> See Order No. PSC-08-0622-PAA-WU, issued September 24, 2008, in Docket No. 060540-WU, In re: Application for increase in water rates in Pasco County by Colonial Manor Utility Company; Order No. PSC-07-0385-SC-WS, issued May 1, 2007, in Docket No. 060575-WS, In re: Application for staff-assisted rate case in Lee County by Useppa Island Utility, Inc.

<sup>17</sup> Docket No. 080249-WS, In re: Application for increase in water and wastewater rates in Pasco County by Labrador Utilities, Inc.

**basis. However, staff does not believe reporting periods should be longer than a semi-annual basis. As staff designs more aggressive conservation-oriented rate structures, we believe it is important to obtain information regarding consumption changes on a frequent basis.**

Based on the foregoing, repression adjustments to the utility's water and wastewater systems are appropriate. Residential water consumption should be reduced by 3.1 percent, resulting in a consumption reduction of approximately 7,960 kgals. Total residential water consumption for ratesetting is 246,880 kgals. Total water consumption for ratesetting is 531,728 kgals, which represents a 1.5 percent reduction in overall consumption. The resulting water system reductions to revenue requirements are \$1,013 in purchased power expense, \$417 in chemicals expense and \$67 in RAFs. The post-repression revenue requirement for the water system is \$1,045,475.

Residential wastewater consumption should be reduced by 1.1 percent, resulting in a consumption reduction of approximately 1,492.0 kgals. Total residential wastewater consumption for ratesetting is 133,409.0 kgals. Total wastewater consumption for ratesetting is 355,678.0 kgals, which represents a 0.4 percent reduction in overall consumption. The resulting wastewater system reductions to revenue requirements are \$897 in sludge removal expense, \$492 in purchased power expense, \$134 in chemicals expense, and \$72 in RAFs. The post-repression revenue requirement for the wastewater system is \$1,097,813.

In order to monitor the effects of both the changes in revenues and rate structure, the utility should be ordered to prepare monthly reports detailing the number of bills rendered, the consumption billed and the revenues billed for each system. In addition, the reports should be prepared, for both the water and wastewater systems, by customer class and meter size. **The reports should be filed with staff, on a semi-annual basis, for a period of two years beginning the first billing period after the approved rates go into effect.** To the extent the utility makes adjustments to consumption in any month during the reporting period, the utility should be ordered to prepare and file a revised monthly report for that month within 30 days of any revision.

**Issue 19:** What are the appropriate rates for this utility?

**Recommendation:** The appropriate monthly water rates are shown on Schedule 4-A, and the corresponding appropriate monthly wastewater rates are shown on Schedule 4-B. Excluding miscellaneous service revenues, the recommended water rates are designed to produce revenues of \$1,045,475, while the recommended wastewater rates are design to produce revenues of \$1,096,980. The utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. In addition, the rates should not be implemented until staff has approved the proposed customer notice. The utility should provide proof of the date the notice was given no less than 10 days after the date of the notice. (Lingo, Mann, Casey)

**Staff Analysis:** Excluding miscellaneous service revenues, the recommended water rates shown on Schedule No. 4-A are designed to produce revenues of \$1,045,475. Approximately 34.8 percent (or \$363,825) of the water monthly service revenues is recovered through the base facility charges, while approximately 65.2 percent (or \$681,650) represents revenue recovery through the consumption charges. Excluding miscellaneous service revenues, the recommended wastewater rates shown on Schedule No. 4-B are designed to produce revenues of \$1,097,813. Approximately 50 percent (or \$548,907) of the wastewater monthly service revenues is recovered through the base facility charges, while approximately 50 percent (or \$548,907) represents revenue recovery through the consumption charges. The utility's private fire protection rates are based on 1/12 of the recommended base facility charge for the utility's meter sizes, consistent with Rule 25-30.465, F.A.C.

The utility should file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-40.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice. The utility should provide proof of the date notice was given no less than 10 days after the date of the notice.

Date: August 6, 2009

**Issue 20:** In determining whether any portion of the water and wastewater interim increase granted should be refunded, how should the refund be calculated, and what is the amount of the refund, if any?

**Recommendation:** The proper refund amount should be calculated by using the same data used to establish final rates, excluding rate case expense and other items not in effect during the interim period. This revised revenue requirement for the interim collection period should be compared to the amount of interim revenue requirement granted. Based on this calculation, a water refund is required in the amount of \$5,214. For wastewater, no refund is required. (Mann, Casey)

**Staff Analysis:** By Order No. PSC-09-0116-FOF-WS, issued February 25, 2009, the Commission authorized the collection of interim water and wastewater rates, subject to refund, pursuant to Section 367.082, F.S. The approved interim revenue requirement is \$1,038,940 for water and \$1,034,391 for wastewater, which represents an increase of \$47,301 or 4.77 percent for water, and \$238,093 or 29.90 percent for wastewater:

<u>Interim versus Final Rate Increase - Refund Calculation</u>	<u>Water</u>	<u>Wastewater</u>
Total 2007 Test Year Revenues	\$991,639	\$796,297
Less: Miscellaneous Revenues	<u>18,128</u>	<u>0</u>
Test Year Revenues from Service Rates	\$973,511	\$796,297
Revenue Increase	<u>\$47,301</u>	<u>\$238,093</u>
% Service Rate Increase	<u>4.77%</u>	<u>29.90%</u>
2007 Test Year Revenue and Interim Revenue Increase	<u>\$1,038,940</u>	<u>\$1,034,390</u>
2008 Test Year Revenue Increase %	<u>19.20%</u>	<u>57.97%</u>
2008 Test Year Revenue	<u>\$1,061,117</u>	<u>\$1,099,409</u>
2008 Test Year Revenue	<u>\$1,061,117</u>	\$1,099,049
2008 Rate Case Expense Grossed-Up for RAF	<u>(\$32,608)</u>	<u>(\$32,608)</u>
2008 Test Year Revenue less Rate Case Expense	\$1,028,509	\$1,066,801
2007 Test Year Revenue and Interim Revenue Increase	<u>\$1,038,940</u>	<u>\$1,034,390</u>
Excess of Interim Collected	\$10,431	-0-
	1.00%	0%
Excess of Interim Collected	\$10,431	-0-
Months	<u>12</u>	<u>12</u>
Per Month / Collection Period Difference	\$869	-0-
Number of Months Interim Rates Collected (April - Sept 2009)	<u>6</u>	6
Refund Amount (\$0 if 2008 Revenue w/o Rate Case Expense > 2007 Revenue)	<u>\$5,214</u>	<u>-0-</u>

According to Section 367.082, F.S., any refund should be calculated to reduce the rate of return of the utility during the pendency of the proceeding to the same level within the range of the newly authorized rate of return. Adjustments made in the rate case test period that do not relate to the period interim rates are in effect, should be removed. Rate case expense is an example of an adjustment which is recovered only after final rates are established.

In this proceeding, the test period for establishing interim rates was December 31, 2007, and the final rates are based on the 12-month period ending December 31, 2008. Southlake's approved interim rates did not include any provisions for pro forma or projected operating expenses or plant. The interim increase was designed to allow recovery of the last authorized range for equity earnings.

To establish the proper refund amount, staff has calculated a revised interim revenue requirement utilizing the same data used to establish final rates. Rate case expense was excluded because the item is prospective in nature and did not occur during the interim collection period. Staff determined a refund to water customers should be made of \$5,214. Wastewater interim rates produced a revenue deficit of (\$32,411) requiring no refund to wastewater customers. If the customer base had the same number of water customers as wastewater customers, a refund would not be necessary. However, Southlake has 2,321 water and 2,161 wastewater customers, so staff believes a refund to water customers is necessary.

Using the principles discussed above, a water interim rate refund of 1.00%, or \$5,214 is required with no wastewater interim rate refund. The water refund shall be with interest in accordance with Rule 25-30.360(4), F.A.C. The utility shall submit proper refund reports pursuant to Rule 25-30.360(7), F.A.C. The utility shall also treat any unclaimed refunds as CIAC pursuant to Rule 25-30.360(8), F.A.C.

**Issue 21:** What is the appropriate amount by which rates should be reduced, four years after the established effective date, to reflect the removal of the amortized rate case expense as required by Section 367.0816, F.S.?

**Recommendation:** The water and wastewater rates should be reduced as shown on Schedule Nos. 4-A and 4-B to remove \$31,141 of water and \$31,141 of wastewater rate case expense, grossed-up for RAFs, which is being amortized over a four-year period. The grossed-up amount, factoring in a RAF of 4.5 percent, equals \$32,608 for both water and wastewater. The decrease in rates should become effective immediately following the expiration of the four-year rate case expense recovery period, pursuant to Section 367.0816, F.S. The utility should be required to file revised tariffs and a proposed customer notice setting forth the lower rates and the reason for the reduction no later than 30 days prior to the actual date of the required rate reduction. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice. Southlake should provide proof of the date notice was given, no less than 10 days after the date of the notice. (Mann, Casey)

**Staff Analysis:** Section 367.0816, F.S., requires rates to be reduced immediately following the expiration of the four-year amortization period by the amount of the rate case expense previously included in the rates. The reduction will reflect the removal of revenues associated with the amortization of rate case expense and the gross-up for RAFs, which is \$31,141 for water and \$31,141 for wastewater. The grossed-up amount, factoring in a RAF of 4.5 percent, equals \$32,608 for both water and wastewater. The decreased revenue will result in the rate reduction recommended by staff on Schedule Nos. 4-A and 4-B. The utility should be required to file revised tariff sheets and a proposed customer notice to reflect the Commission-approved rates. The approved rates should be effective for service rendered on or after the stamped approval date of the revised tariff sheets pursuant to Rule 25-30.475(1), F.A.C. The rates should not be implemented until staff has approved the proposed customer notice. Southlake should provide proof of the date notice was given no less than 10 days after the date of the notice.

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



**Issue 22:** Should the utility be required to provide proof, within 90 days of the final order issued in this docket, that it has adjusted its books for all applicable National Association of Regulatory Commissioners Uniform System of Accounts (NARUC USOA) associated with Commission approved adjustments?

**Recommendation:** Yes. To ensure that the utility adjusts its books in accordance with the Commission decision, Southlake should provide proof, within 90 days of the final order issued in this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made. (Mann, Casey)

**Staff Analysis:** To ensure that the utility adjusts its books in accordance with the Commission decision, Southlake should provide proof, within 90 days of the final order issued in this docket, that the adjustments for all the applicable NARUC USOA primary accounts have been made.

**Issue 23:** Should this docket be closed?

**Recommendation:** Yes. If no person whose substantial interests are affected by the proposed agency action files a protest within twenty-one days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the utility and approved by staff, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively, and the corporate undertaking should be released. (Brown)

**Staff Analysis:** If no person whose substantial interests are affected by the proposed agency action files a protest within twenty-one days of the issuance of the order, a consummating order will be issued. The docket should remain open for staff's verification that the revised tariff sheets and customer notice have been filed by the utility and approved by staff, and that the interim refund has been completed and verified by staff. Once these actions are complete, this docket should be closed administratively, and the corporate undertaking should be released.

## DETERMINATION OF APPROPRIATE RATE STRUCTURES

### HISTORY OF CURRENT RATES

- (1) The utility's BFC/gallage charge rates were first established in the Utility's original certificate case in Docket No. 900738-WS.<sup>18</sup> The approved monthly rates for the water system included a BFC for a 5/8" x 3/4" meter of \$7.71, with an approved corresponding charge of \$8.12 for the wastewater system. The approved gallage charges were \$0.72 per kgal and \$0.71 per kgal, respectively. The residential wastewater gallage charge was capped at 10 kgal of monthly usage.
- (2) The utility has received price index rate adjustments as a method of increasing its rates. The instant case represents the utility's first full rate relief proceeding.

### PRACTICES WITH THE WATER MANAGEMENT DISTRICTS

- (3) The Commission has a Memorandum of Understanding (MOU) with the five Water Management Districts (WMDs or Districts). A guideline of the five Districts is to set the base facility charges such that they recover no more than 40 percent of the revenues to be generated from monthly service.<sup>19</sup> The Commission follows the WMD guideline whenever possible.<sup>20</sup>
- (4) The utility is located in the St. Johns River Water Management District (SJRWMD) in a Water Resource Caution Area. In addition, the Utility is located within the Central Florida Coordination Area. This represents an area of the state in which the St. Johns River Water Management District, the Southwest Florida Water Management District and the South Florida Water Management District (hereinafter referred to as the Districts) jointly concluded in 2006 that the availability of sustainable quantities of groundwater in central Florida is insufficient to meet future public water supply demands. In addition, the Districts concluded that alternative water supply sources must be developed to meet increased demands in central Florida beyond 2013. The Districts identified the Central Florida Coordination area as the area for which a coordinated and consistent approach to addressing the identified water supply issues would be developed and implemented.<sup>21</sup>
- (5) As discussed in the Case Background and in Issue 9, the utility is not in compliance with its CUP issued by the SJRWMD. Specifically, items of noncompliance include failure of the utility to include well relocation and reuse items as part of the instant proceeding.

### WATER CONSERVATION INITIATIVE

- (6) In response to growing water demands and water supply problems, coupled with one of the worst droughts in Florida's history, the Florida Department of Environmental Protection (FDEP) led a statewide Water Conservation Initiative (WCI) to find ways to improve efficiency in all categories of water use. In the WCI's final report, issued in April 2002, a high-priority recommendation was that the base facility charge portion of the bill usually should not represent more than 40 percent of the utility's total revenues.<sup>22</sup>

<sup>18</sup> See Orders Nos. 23947 and 24564, issued May 21, 1991 in Docket No. 900738-WS, In re: Application for water and sewer certificates in Lake County by Southlake Utilities, Inc.

<sup>19</sup> See Order No. PSC-02-0593-FOF-WS, issued April 30, 2002 in Docket No. 010503-WU, In re: Application for increase in water rates for Seven Springs system in Pasco County by Aloha Utilities, Inc.; and Order No. PSC-03-1440-FOF-WS, issued December 22, 2003, in Docket No. 020071-WS, In Re: Application for rate increase in Marion, Orange, Pasco, Pinellas and Seminole Counties by Utilities, Inc. of Florida.

<sup>20</sup> See Order No. PSC-94-1452-FOF-WU, issued November 28, 1994, in Docket No. 940475-WU, In re: Application for rate increase in Martin County by Hobe Sound Water Company; and Order No. PSC-01-0327-PAA-WU, issued January 6, 2001, in Docket No. 000295-WU, In re: Application for increase in water rates in Highlands County by Placid Lakes Utilities, Inc.; and Order No. PSC-00-2500-PAA-WS, issued December 26, 2000, in Docket No. 000327-WS, In re: Application for staff-assisted rate case in Putnam County by Buffalo Bluff Utilities, Inc.; and Order No. PSC-02-0593-FOF-WS, issued April 30, 2002, in Docket No. 010503-WU, In re: Application for increase in water rates for Seven Springs system in Pasco County by Aloha Utilities, Inc.

<sup>21</sup> Central Florida Coordination Area Planning Work Group, Final Report, January 2008.

<sup>22</sup> Florida Department of Environmental Protection, Florida Water Conservation Initiative, April 2002.

**DETERMINATION OF APPROPRIATE RATE STRUCTURES (cont.)**

**WATER  
CONSERVATION  
INITIATIVE (cont.)**

(7) Many participants in the WCI, including the Florida Department of Environmental Protection, the Florida Public Service Commission, the Florida Water Management Districts, the Florida Rural Water Association, the Florida Water Environment Association, and the Florida section of the American Water Works Association are signatories on the Joint Statement of Commitment for the Development and Implementation of a Statewide Comprehensive Water Conservation Program for Public Water Supply (JSOC) and its associated Work Plan.<sup>23</sup>

**FLORIDA STATUTES  
re: WATER  
CONSERVATION**

(8) Section 373.227(1), Florida Statutes, states in part: "The Legislature recognizes that the proper conservation of water is an important means of achieving the economical and efficient utilization of water necessary, in part, to constitute a reasonable-beneficial use. The overall water conservation goal of the state is to prevent and reduce wasteful, uneconomical, impractical, or unreasonable use of water resources."

**CLIMATIC  
CONDITIONS**

(9) Staff evaluates available drought information to better design rates that achieve conservation. Based on information from the National Drought Mitigation Center's U.S. Drought Monitor, the utility is not currently located in an abnormally dry area of Florida.<sup>24</sup>

(10) Based on information from the Southeast Regional Climate Center, the utility's service area will experience greater than average temperatures and precipitation through October 2009.<sup>25</sup>

**WATER SYSTEM  
USAGE PATTERNS:**

(11) The utility has a nonseasonal residential customer base, but a more seasonal multi-family / general service customer base. The average monthly consumption per residential customer is approximately 12.4 kgal. A review of the utility service area indicates that most of the customers' lawns are well kept. Many homes are well landscaped and well irrigated.

**WATER SYSTEM  
BFC COST  
RECOVERY:**

(12) Staff performed detailed analyses of Southlake's billing data in order to evaluate various BFC cost recovery percentages. The goals of the evaluation were to select the rate design parameters that: 1) allow the utility to recover its revenue requirements; and 2) equitably distribute cost recovery among the utility's customers. Based on a detailed billing analysis of the residential class, only 40 percent of the residential bills and 32 percent of the corresponding consumption has been accounted for at monthly consumption of 5 kgals or less, while 54 percent of the bills and kgals have been accounted for at 10 kgals or less. This is indicative of greater than average consumption.

(13) As discussed in Issue 16, staff's preliminary recommended revenue requirement increase is 19.2 percent. Based on the magnitude of preliminary increase, for conservation purposes, the entire increase was placed into the gallonage charge.

(14) In order to comply with the WMD and WCI guidelines regarding the percentage of BFC cost recovery, staff evaluated BFC cost recovery percentages at 34.8 percent and 30 percent. The results are presented in Table 17-1. When compared to the current rate structure, Alternatives 1 and 2 both result in price decreases at certain levels of consumption. Therefore, staff believes that its recommended rate structure would be more effective than the alternatives presented in encouraging water conservation.

<sup>23</sup> Joint Statement of Commitment for the Development and Implementation of a Statewide Comprehensive Water Conservation Program for Public Water Supply, February 2004; Work Plan to Implement Section 373.227, F.S. and the Joint Statement of Commitment for the Development and Implementation of a Statewide Comprehensive Water Conservation Program for Public Water Supply, December 2004.

<sup>24</sup> National Drought Mitigation Center, U.S. Drought Monitor, July 28, 2009.

<sup>25</sup> Southeast Regional Climate Center, July 16, 2009.

**DETERMINATION OF APPROPRIATE RATE STRUCTURES (cont.)**

**STAFF'S  
RECOMMENDATION FOR  
THE WATER SYSTEM:**

The appropriate rate structures for the utility's water system are a three-tiered inclining-block rate structure applicable to residential customers. The appropriate usage blocks are for monthly consumption of: 1) 0-10,000 gallons (10 kgals); 2) 10,001-20 kgals; and 3) consumption in excess of 20 kgals. The base facility charge (BFC)/uniform gallonage charge should be applied to the utility's general service water customers. The BFC cost recovery allocation for the water system should be set at 34.8 percent.

**WASTEWATER  
SYSTEM:**

- (15) Based on the initial accounting allocation, approximately 33 percent of the utility's costs were recovered in the BFC. Staff believes no less than 50 percent of the revenue requirement recovery should be in the BFC. This is to recognize the capital intensive nature of wastewater treatment facilities.
- (16) For billing purposes, residential usage charges should be capped at 10 kgals of monthly usage. The general service gallonage charge should be set at 1.2 times greater than the residential gallonage charge rate. These recommendations are consistent with Commission practice.

**STAFF'S  
RECOMMENDATION FOR  
THE WASTEWATER  
SYSTEM:**

The appropriate rate structure for the wastewater system is a continuation of the BFC/gallonage charge rate structure. The BFC cost recovery allocation should be set at 50 percent. For billing purposes, residential usage charges should be capped at 10 kgals of monthly usage. The general service gallonage charge rate should be 1.2 times greater than the corresponding residential rate with no cap on billed monthly usage.

Southlake Utilities, Inc. Schedule of Water Rate Base Test Year Ended 12/31/08		Schedule No. 1-A Docket No. 080597-WS			
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Staff Adjust- ments	Staff Adjusted Test Year
1 Plant in Service	\$7,078,292	(\$33,425)	\$7,044,867	\$87,686	\$7,132,553
2 Land and Land Rights	133,286	0	133,286	(57,386)	\$75,900
3 Non-used and Useful Components	0	0	0	\$0	0
4 Accumulated Depreciation	(1,071,790)	100,814	(970,976)	(315,817)	(1,286,793)
5 CIAC	(3,952,991)	6,756	(3,946,235)	(8,958)	(3,955,193)
6 Amortization of CIAC	953,376	(62,770)	890,606	(66,597)	824,009
7 Construction Work in Progress	778,064	0	778,064	(193,790)	584,274
8 Advances for Construction	(123,121)	0	(123,121)	0	(123,121)
9 Working Capital Allowance	69,761	0	69,761	(8,796)	60,965
10 Avg Unamortized Project Costs.	<u>117,088</u>	<u>0</u>	<u>117,088</u>	<u>(117,088)</u>	<u>0</u>
11 <b>Rate Base</b>	<u>\$3,981,965</u>	<u>\$11,375</u>	<u>\$3,993,340</u>	<u>(\$680,746)</u>	<u>\$3,312,594</u>

Southlake Utilities, Inc. Schedule of Wastewater Rate Base Test Year Ended 12/31/08			Schedule No. 1-B Docket No. 080597-WS		
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Staff Adjust- ments	Staff Adjusted Test Year
1 Plant in Service	\$7,342,299	(\$27,498)	\$7,314,801	(\$43,968)	\$7,270,833
2 Land and Land Rights	558,446	0	558,446	(207,861)	350,585
3 Non-used and Useful (NUU) Plant	0	0	0	(1,052,860)	(1,052,860)
4 Accumulated Depreciation	(1,721,598)	131,790	(1,589,808)	(282,804)	(1,872,612)
5 CIAC	(5,364,589)	11,640	(5,352,949)	(7,525)	(5,360,474)
6 Amortization of CIAC	1,677,834	(113,549)	1,564,285	(162,935)	1,401,350
7 Advances for Construction	(295,893)	0	(295,893)	0	(295,893)
8 Construction Work in Progress	0	0	0	0	0
9 Working Capital Allowance	111,684	0	111,684	(18,470)	93,214
10 Avg Unamortized Project Costs.	<u>67,088</u>	<u>0</u>	<u>67,088</u>	<u>(67,088)</u>	<u>0</u>
11 <b>Rate Base</b>	<u>\$2,375,271</u>	<u>\$2,383</u>	<u>\$2,377,654</u>	<u>(\$1,843,511)</u>	<u>\$534,143</u>

Southlake Utilities, Inc. Commission Adjustments to Rate Base Test Year Ended 12/31/08		Schedule No. 1-C Docket No. 080597-WS	
Explanation	Water	Wastewater	
<u>Plant In Service</u>			
1 To adjust filing to staff calculated general ledger amount.	(\$21,224)	(\$17,106)	
2 To remove undocumented plant in service (AF No. 1).	(142,789)	(176,812)	
3 To reclassify capital costs (AF No. 6).	34,476	57,436	
4 To adjust PIS for lack of documentation (AF No. 3).	0	(102,466)	
5 To eliminate duplicate amount (AF No. 3).	0	(15,000)	
6 To reflect averaging adjustment.	(5,645)	382,800	
7 To transfer PIS from wastewater to water (AF No. 3).	222,868	(222,868)	
8 To transfer from water CWIP to wastewater PIS (AF No. 3).	0	50,048	
Total	<u>\$87,686</u>	<u>(\$43,968)</u>	
<u>Land and Land Rights</u>			
1 To adjust land values. (AF No. 2).	<u>(\$57,386)</u>	<u>(\$207,861)</u>	
<u>Construction Work in Progress</u>			
1 To adjust CWIP for lack of documentation (AF No. 3).	(145,941)	0	
2 To include test year additions to CWIP.	11,046	0	
3 To transfer from water CWIP to wastewater PIS (AF No. 3).	(50,048)	0	
4 To adjust from CWIP to expense (AF No. 3).	<u>(8,847)</u>	<u>0</u>	
	<u>(\$193,790)</u>	<u>\$0</u>	
<u>Non-used and Useful</u>			
1 To reflect non-used and useful adjustment.	<u>\$0</u>	<u>(\$1,052,860)</u>	
<u>Accumulated Depreciation</u>			
1 To adjust filing to staff calculated general ledger amount.	(\$493,910)	(\$810,595)	
2 To remove related A/D for undocumented PIS (AF No. 1).	\$29,050	\$35,972	
3 To adjust related A/D for reclassification from capital costs (AF No. 6).	(431)	(899)	
4 To reflect averaging adjustment.	146,988	195,824	
5 To adjust A/D for reclassification of CWIP/PIS (AF No. 3).	2,486	30,794	
6 To reflect A/D non-used and useful adjustment.	0	266,100	
Total	<u>(\$315,817)</u>	<u>(\$282,804)</u>	
<u>CIAC</u>			
1 To adjust filing to staff calculated general ledger amount (AF No. 4).	(\$22,786)	(\$27,191)	
2 To reflect averaging adjustment.	13,828	19,666	
	<u>(\$8,958)</u>	<u>(\$7,525)</u>	
<u>Accumulated Amortization of CIAC</u>			
1 To adjust filing to staff calculated general ledger amount.	(\$18,403)	(\$99,460)	
2 To reflect averaging adjustment.	<u>(48,194)</u>	<u>(63,475)</u>	
	<u>(\$66,597)</u>	<u>(\$162,935)</u>	
<u>Working Capital Allowance</u>			
1 To reflect the appropriate working capital allowance.	<u>(\$8,796)</u>	<u>(\$18,470)</u>	
<u>Avg. Unamortized Project Costs</u>			
1 To remove unamortized project costs (Rate Case Expense & CUP).	<u>(\$117,088)</u>	<u>(\$67,088)</u>	



Southlake Utilities, Inc.  
 Capital Structure - Average Balance  
 Test Year Ended 12/31/08

Schedule No. 2  
 Docket No. 080597-WS

Description	Total Capital	Specific Adjustments	Subtotal Adjusted Capital	Prorata Adjustments	Capital Reconciled to Rate Base	Ratio	Cost Rate	Weighted Cost	
<b>Per Utility (Year End)</b>									
1 Long-term Debt	\$0	\$0	\$0	\$0	\$0	0.00%	0.00%	0.00%	
2 Short-term Debt	0	0	0	0	0	0.00%	0.00%	0.00%	
3 Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%	
4 Common Equity	6,159,377	0	6,159,377	0	6,159,377	96.68%	9.56%	9.24%	
5 Customer Deposits	211,614	0	211,614	0	211,614	3.32%	6.00%	0.20%	
6 Tax Credits-Zero Cost	0	0	0	0	0	0.00%	0.00%	0.00%	
7 Deferred Income Taxes	0	0	0	0	0	0.00%	0.00%	0.00%	
8 <b>Total Capital</b>	<u>\$6,370,991</u>	<u>\$0</u>	<u>\$6,370,991</u>	<u>\$0</u>	<u>\$6,370,991</u>	<u>100.00%</u>		<u>9.44%</u>	
<b>Per Commission (Simple Average)</b>									
9 Long-term Debt	\$0	\$0	\$0	\$0	\$0	0.00%	0.00%	0.00%	
10 Short-term Debt	0	0	0	0	0	0.00%	0.00%	0.00%	
11 Preferred Stock	0	0	0	0	0	0.00%	0.00%	0.00%	
12 Common Equity	6,159,377	(90,070)	6,069,307	(2,434,419)	3,634,888	94.49%	9.67% *	9.13%	
13 Customer Deposits	211,614	235	211,849	0	211,849	5.51%	6.00%	0.33%	
14 Tax Credits-Zero Cost	0	0	0	0	0	0.00%	0.00%	0.00%	
15 Deferred Income Taxes	0	0	0	0	0	0.00%	0.00%	0.00%	
16 <b>Total Capital</b>	<u>\$6,370,991</u>	<u>(\$89,835)</u>	<u>\$6,281,156</u>	<u>(\$2,434,419)</u>	<u>\$3,846,737</u>	<u>100.00%</u>		<u>9.47%</u>	
						<b>LOW</b>	<b>HIGH</b>		
RETURN ON EQUITY						<u>8.67%</u>	<u>10.67%</u>		
OVERALL RATE OF RETURN						<u>8.52%</u>	<u>10.41%</u>		

\* The 1% reduction in ROE for Water results in a return on common equity for water rate base of 8.67% with an overall rate of return of 8.52%.

Southlake Utilities, Inc. Statement of Water Operations Test Year Ended 12/31/08		Schedule No. 3-A Docket No. 080597-WS					
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Staff Adjust- ments	Staff Adjusted Test Year	Revenue Increase	Revenue Requirement
1 Operating Revenues:	<u>\$1,000,474</u>	<u>\$183,853</u>	<u>\$1,184,327</u>	<u>(\$294,110)</u>	<u>\$890,217</u>	<u>\$170,900</u> 19.20%	<u>\$1,061,117</u>
<b>Operating Expenses</b>							
2 Operation & Maintenance	\$624,964	\$0	\$624,964	(\$137,243)	\$487,721		\$487,721
3 Depreciation	201,627	0	201,627	89,712	291,339		291,339
4 Amortization	(125,541)	0	(125,541)	11,628	(113,913)		(113,913)
5 Taxes Other Than Income	98,121	8,273	106,394	(\$351)	106,043	\$7,691	113,734
6 Income Taxes	0	0	0	0	0	0	0
7 Total Operating Expense	799,171	8,273	807,444	(36,254)	771,190	\$7,691	778,880
8 Operating Income	<u>\$201,303</u>	<u>\$175,580</u>	<u>\$376,883</u>	<u>(\$257,856)</u>	<u>\$119,027</u>	<u>\$163,210</u>	<u>\$282,237</u>
9 Rate Base	<u>\$3,981,965</u>		<u>\$3,993,340</u>		<u>\$3,312,594</u>		<u>\$3,312,594</u>
10 Rate of Return	5.06%		9.44%		3.59%		8.52%

Southlake Utilities, Inc. Statement of Wastewater Operations Test Year Ended 12/31/08		Schedule No. 3-B Docket No. 080597-WS					
Description	Test Year Per Utility	Utility Adjust- ments	Adjusted Test Year Per Utility	Staff Adjust- ments	Staff Adjusted Test Year	Revenue Increase	Revenue Requirement
1 <b>Operating Revenues:</b>	<u>\$805,299</u>	<u>\$487,912</u>	<u>\$1,293,211</u>	<u>(\$597,238)</u>	<u>\$695,973</u>	<u>\$403,436</u> 57.97%	<u>\$1,099,409</u>
<b>Operating Expenses</b>							
2 Operation & Maintenance	\$834,446	\$92,571	\$927,017	(\$181,305)	\$745,712		\$745,712
3 Depreciation	263,580	0	263,580	81,391	344,971		344,971
4 Amortization	(227,098)	0	(227,098)	\$77,065	(150,033)		(150,033)
5 Taxes Other Than Income	80,427	24,888	105,315	(15,268)	90,047	18,155	108,202
6 Income Taxes	0	0	0	0	0	0	0
7 <b>Total Operating Expense</b>	<u>951,355</u>	<u>117,459</u>	<u>1,068,814</u>	<u>(38,117)</u>	<u>1,030,697</u>	<u>18,155</u>	<u>1,048,852</u>
8 <b>Operating Income</b>	<u>(\$146,056)</u>	<u>\$370,453</u>	<u>\$224,397</u>	<u>(\$559,121)</u>	<u>(\$334,724)</u>	<u>\$385,281</u>	<u>\$50,557</u>
9 <b>Rate Base</b>	<u>\$2,375,271</u>		<u>\$2,377,654</u>		<u>\$534,143</u>		<u>\$534,143</u>
10 <b>Rate of Return</b>	<u>-6.15%</u>		<u>9.44%</u>		<u>-62.67%</u>		<u>9.47%</u>

Southlake Utilities, Inc. Commission Adjustments to Operating Income Test Year Ended 12/31/08		Schedule 3-C Docket No. 080597-WS	
Explanation	Water	Wastewater	
<u>Operating Revenues</u>			
1 Remove requested final revenue increase.	(\$183,853)	(\$487,912)	
2 To reflect actual test year revenues (AF No. 5).	<u>(110,257)</u>	<u>(109,326)</u>	
Total	<u>(\$294,110)</u>	<u>(\$597,238)</u>	
<u>Operation and Maintenance Expense</u>			
1 To adjust filing to 12/31/2008 actual general ledger (AF No. 6).	(\$35,948)	\$2,914	
2 To reflect staff calculated test year Rate Case expense.	31,141	31,141	
3 To reflect consumptive use permit amortized over 5 years.	9,401	0	
4 To reflect test year purchased power.	1,715	1,973	
5 To remove land lease expense (AF No. 6).	(11,778)	(45,299)	
6 To adjust contractual services - other.	(8,250)	(8,250)	
7 To adjust communication expense.	(426)	(426)	
8 To reflect audit finding regarding reclassification of Capital Costs (AF No. 6).	(34,476)	(57,436)	
9 To reflect audit finding regarding Undocumented Costs (AF No. 6).	(20,315)	(38,615)	
10 To remove utility test year Rate Case expense (AF No. 6).	<u>(68,307)</u>	<u>(67,307)</u>	
Total	<u>(\$137,243)</u>	<u>(\$181,305)</u>	
<u>Depreciation Expense</u>			
1 To adjust filing to staff calculated depreciation expense.	\$92,349	\$128,067	
2 To reflect audit finding No. 1.	(\$4,469)	(\$5,534)	
3 To reflect audit finding No. 6 - reclassify capital costs.	431	899	
4 To adjust depreciation expense on reclassified plant in service (AF No. 3).	1,401	(9,086)	
5 To adj. for non-used and useful depr. Expense.	0	<u>(32,955)</u>	
Total	<u>\$89,712</u>	<u>\$81,391</u>	
<u>CIAC Amortization Expense</u>			
1 To adjust filing to staff calculated amortization expense.	<u>\$11,628</u>	<u>\$77,065</u>	
<u>Taxes Other Than Income</u>			
1 RAFs on Revenue Adjustments Above.	(\$13,235)	(\$26,876)	
2 To Reflect Audit Finding No.7 - Adjust TOTI.	12,884	17,114	
3 To adjust property tax for non-used and useful PIS.	0	<u>(5,506)</u>	
Total	<u>(\$351)</u>	<u>(\$15,268)</u>	

**Southlake Utilities, Inc.  
 Water Monthly Service Rates  
 Test Year Ended 12/31/08**

**Schedule No. 4-A  
 Docket No. 080597-WS**

	<b>Rates Prior to Filing</b>	<b>Commission Approved Interim</b>	<b>Utility Requested Final</b>	<b>Staff Recommended Final</b>	<b>4-Year Rate Reduction</b>
<b>Residential</b>					
<b>Base Facility Charge by Meter Size:</b>					
5/8" x 3/4"	\$8.98	\$9.42	\$8.82	\$8.98	\$0.28
1"	\$22.45	\$23.54	\$22.05	\$22.45	\$0.69
1-1/2"	\$44.90	\$47.08	\$44.11	\$44.90	\$1.38
2"	\$71.85	\$75.34	\$70.58	\$71.84	\$2.21
3"	\$143.70	\$150.68	\$141.17	\$143.68	\$4.42
4"	\$224.51	\$235.42	\$220.55	\$224.50	\$6.90
6"	\$449.03	\$470.85	\$441.11	\$449.00	\$13.80
Gallage Charge, per 1,000 Gallons 0-10	\$0.84	\$0.88	\$0.92	\$0.95	\$0.03
10,001 to 20,000 gals.	\$0.84	\$0.88	\$1.37	\$1.43	\$0.04
Over 20,000 gals.	\$0.84	\$0.88	\$1.83	\$1.90	\$0.06
<b><u>Multi-Residential and General Service</u></b>					
<b>Base Facility Charge by Meter Size:</b>					
5/8" x 3/4"	\$8.98	\$9.42	\$8.82	\$8.98	\$0.28
1"	\$22.45	\$23.54	\$22.05	\$22.45	\$0.69
1-1/2"	\$44.90	\$47.08	\$44.11	\$44.90	\$1.38
2"	\$71.85	\$75.34	\$70.58	\$71.84	\$2.21
3"	\$143.70	\$150.68	\$141.17	\$143.68	\$4.42
4"	\$224.51	\$235.42	\$220.55	\$224.50	\$6.90
6"	\$449.03	\$470.85	\$441.11	\$449.00	\$13.80
Gallage Charge	\$0.84	\$0.88	\$1.05	\$1.26	\$0.04
<b>Fire Protection</b>					
1-1/2"	\$14.98	\$14.98	\$14.56	\$3.74	\$0.11
2"	\$23.75	\$23.75	\$23.29	\$5.99	\$0.18
3"	\$74.83	\$74.83	\$46.58	\$11.97	\$0.37
4"	\$149.67	\$149.67	\$72.78	\$18.71	\$0.57
6"	\$149.67	\$149.67	\$145.56	\$37.42	\$1.15
8"	\$149.67	\$149.67	\$232.89	\$59.87	\$1.84
10"	\$149.67	\$149.67	\$334.78	\$82.32	\$2.53
<b><u>Typical Residential Bills 5/8" x 3/4" Meter</u></b>					
3,000 Gallons	\$11.50	\$12.06	\$11.58	\$11.83	
5,000 Gallons	\$13.18	\$13.82	\$13.42	\$13.73	
10,000 Gallons	\$17.38	\$18.22	\$18.02	\$18.48	

Southlake Utilities, Inc. Wastewater Monthly Service Rates Test Year Ended 12/31/08		Schedule No. 4-B Docket No. 080597-WS			
	Rates Prior to Filing	Commission Approved Interim	Utility Requested Final	Staff Recommended Final	4-Year Rate Reduction
<u>Residential</u>					
Base Facility Charge All Meter Sizes:	\$9.76	\$12.68	\$10.02	\$14.76	\$0.44
Gallage Charge - Per 1,000 gallons (10,000 gallon cap)	\$0.86	\$1.12	\$1.76	\$1.37	\$0.04
General Service					
Base Facility Charge by Meter Size:					
5/8" x 3/4"	\$9.76	\$12.68	\$10.02	\$14.76	\$0.44
1"	\$24.41	\$31.71	\$25.06	\$36.90	\$1.09
1-1/2"	\$48.80	\$63.39	\$50.10	\$73.80	\$2.19
2"	\$78.08	\$101.43	\$80.16	\$118.08	\$3.50
3"	\$156.18	\$202.88	\$160.34	\$236.16	\$7.00
4"	\$224.02	\$291.00	\$229.99	\$369.00	\$10.94
6"	\$448.02	\$581.98	\$501.03	\$738.00	\$21.89
Gallage Charge, per 1,000 Gallons	\$1.02	\$1.32	\$2.11	\$1.64	\$0.05
<u>Typical Residential Bills 5/8" x 3/4" Meter</u>					
3,000 Gallons	\$12.34	\$16.04	\$15.30	\$18.87	
5,000 Gallons	\$14.06	\$18.28	\$18.82	\$21.61	
10,000 Gallons	\$18.36	\$23.88	\$27.62	\$28.46	
(Wastewater Gallage Cap - 10,000 Gallons)					