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Sent: Thursday, October 16, 2014 2:52 PM
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Subject: Dkt 140135-WS Labrador Utilities Inc. Rate Case, OPC List of Concerns
Attachments: Dkt 140135 Labrador Rate Case OPC Concerns.docx

Electronic Filing

a. Person responsible for this electronic filing:

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b. Docket No. 140135-WS

In Re: Application for increase in water/wastewater rates in Pasco County by Labrador Utilities, Inc.

c. Document being filed on behalf of Office of Public Counsel

d. There are a total of 10 pages.

e. Dkt 140135 Labrador Rate Case OPC Concerns (File name: Dkt 140135 Labrador Rate Case OPC Concerns.docx)

Thank you for your attention to this request.

Sincerely,

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October 16, 2014

Mr. Andrew Maurey
Division of Accounting and Finance
Florida Public Service Commission
2340 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Re: Docket 140135-WS - Application for increase in water/wastewater rates in Pasco County by Labrador Utilities, Inc. – OPC List of Concerns

Dear Mr. Maurey,

The Office of Public Counsel is actively monitoring the rate case docket for Labrador Utilities, Inc. ("Labrador", "Utility", or "Company"). Attached is a list of issues that OPC has prepared to identify concerns we have with the MFRs and other information filed by Labrador in support its requested rate increase. We have not had time to fully review the information filed in this case, but we would like to bring these to staff's attention to aid staff in its review of the rate case and to allow the staff sufficient time to review our concerns and ask for any additional information that might be needed. If you should have any questions, please fee l free to call or e-m ail me.

Sincerely,

s/ Patricia W. Merchant

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C: Division of Accounting & Finance (Maurey, Galloway, Prestwood, Trueblood, G. Smith, Polk, Fletcher, Brown)
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Division of Auditing and Performance Analysis (Small, Deamer)
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Sundstrom, Friedman & Fumero, LLP (Friedman)
Labrador Utilities, Inc. (Flynn)

<u>OPC Issues and Concerns – Labrador Utilities, Inc. Docket No. 140135-WS</u>

A. <u>Water Tank Maintenance</u>. In Labrador's last rate case, Order No. PSC-12-0206-PAA-WS, issued April 17, 2012, in Docket No. 110264-WS (page 2), the Commission stated the following:

> On MFR Schedule B-11, Labrador provided an analysis of all maintenance projects greater than 2 percent of test year revenue during the test year, 2 years prior to the test year, and 1 year subsequent to the test year. In its analysis, the Utility requested a budgeted amount of $46,204 for the cost to maintain and repair the water tank. The budgeted amount was amortized over 5 years and $9,241 was included in water O&M expense. The basis for Labrador's budgeted amount was the cost incurred in April 2004 to repair and maintain the tank. The cost in 2004 included work to sandblast and recoat the tank inside and out, cut off the old roof, and install a new pre-fabricated roof with handrails.
>
> A tank inspection report from Liquid Engineering, dated January 27, 2010, indicated that the condition of the interior of the tank was in fair condition, but was in need of repairs to continue functioning as designed. Liquid Engineering recommended that the tank be sandblasted and recoated in addition to making other minor repairs. We estimate that the appropriate cost to maintain and repair the water tank is $30,138. This estimate is based on the actual cost of $23,500 to sandblast and recoat the tank in April 2004. We used an inflation factor of 1.156093 to inflate the cost in 2004 to the cost in 2011. We calculated the estimated cost in 2011 to be $27,168. We added the cost of the tank inspection ($2,970) to the cost of sandblasting and recoating for a total estimated cost of $30,138. In accordance with Rule 25-30.433(8), F.A.C., this cost shall be amortized over 5 years. Accordingly, the appropriate estimated annual cost is $6,028. Therefore, we find that the annual cost of water tank maintenance and repair shall be decreased by $3,213 to reflect the appropriate estimated amount of water tank maintenance and repair expense.

1. Did the company perform the maintenance to the water tank that it received funding for in Order 12-0206? If not, the Company should explain why not.

2. According to the Company's 2013 Annual Report, page F-14, Labrador reflects a $10,884 deferred maintenance balance at the end of 2013 and wrote-off/expensed $2,043 in 2013. Labrador should provide a description of what type of maintenance work was performed on the Labrador system when it wrote-off the $2,043 in 2013? If no work was performed on the water tank, the Company should explain why this amount was written off, the reasons for the write-off and a description of the Company policy that allows such amounts to be written-off.

3. Labrador should provide a list of all maintenance performed on the water tank since 2005, including a description of the work performed and the dollar amount of each project.

4. If the Company has not sandblasted and recoated the tank since the last rate case, it should explain why this maintenance work was not performed.

5. If the Company did not sandblast and recoat the water tank after the last rate case (as specific funding was approved in the last rate case and recovered by ratepayers through rates), the Company should explain what impact not performing this maintenance had on the condition of the water storage tank today.

6. According to the current docket MFR Schedule B-11 the Company reflects deferred maintenance from August 2006 to July 2011 in the amount of $54,260 which was amortized over 5 years.

   a. The Company should provide all invoices to support the $54,260 in deferred costs which reflect descriptions of all work performed.

   b. The Company should explain how this $54,260 differs from the $30,138 amount approved by the Commission in Labrador's last rate case Dkt 110264-WS Order No. PSC-12-0206-PAA-WS.

B. Water Tank Replacement. Questions 7 to 11 relate to Volume 3 of the MFRs Additional Engineering Information, pages 376-383 regarding the pro forma water tank replacement.

7. In MFR Volume 3 Additional Engineering Information- Water Tank Replacement, page 376 states in item No. 1, that "The project's description, justification and project cost information is found in the attached "Labrador WTP GST Replacement". OPC notes that there are no documents provided in the MFRs to show the estimated project cost. In Item No. 4, this page states that the Company will solicit bids from qualified contractors prior to awarding the project. No bids or estimates were included in the MFRs other than the amount shown on MFR Schedule A-3 p 1. The Company should provide a copy of all bids and estimates used to estimate the cost of the water tank replacement prior to being allowed recovery in rates.

8. In Utilities, Inc. Document titled: Justification and Benefits: (Revised January 24, 2014) "Significant metal failure has been found in portions of the top four feet of the structure's vertical walls, the area above the nominal water level. The tank's elements include a roof with locked access hatch, a safety railing and access ladder system, water level controls, and associated piping. The tank's roof was replaced in 2005."

a. The Company should provide the source of the previous statement.

b. Is it an internal assessment provided by Company staff or based on an outside consultant's opinion?

c. If the assessment is based upon an outside consultant's opinion, the Company should provide all documents regarding the consultant's opinion.

9. "After consulting with several vendors following an interior and exterior inspection of the tank structure, all have concluded that it would be less costly to replace the structure rather than attempt to take the tank offline and make repairs. This will also minimize interruptions in the delivery of water service to the customers. The measured tank wall thickness at or above the water line is extremely thin indicating the tank is at the end of its service life."

a. The Company should provide a copy of all documents supporting any and all comments, recommendations or estimates provided by any outside vendors that Labrador consulted.

b. Labrador should be required to provide what impact any failure to sandblast and repaint the tank in 2010 had on the condition of the tank today.

C. <u>Gain on Disposition of Utility Property</u>. According to Labrador's 2013 Annual Report, it reported gains of $743 in 2012 and $411 in 2013.

10. The Company should provide a description of the property that was sold during each of these years, and a copy of the workpapers or calculations that reflect how each gain was determined, including the income tax component.

11. The Company should also provide any allocation calculations, if any, and the journal entries recording the gains for each year.

D. <u>Used and Useful Wastewater Treatment Plant</u>. OPC has concerns about Labrador's calculation of non-used and useful wastewater treatment plant. The Company's interim calculation for wastewater does not comply with the Commission methodology of calculating used and useful for the wastewater treatment plant made in the last rate case.

12. The Company should provide a detailed explanation reflecting all factors and circumstances that have changed since the last rate case which might warrant a change from the facts considered and the method used by the Commission in calculating used and useful.

E. Rate Case Expense. Based on our comparison of the amount of rate case expense requested in the current case and the amounts requested, allowed and actual amounts in incurred in prior Labrador rate cases, OPC believes the following questions should be addressed by the Company.

13. In the MFRs in the current case, the Company has estimated $95,000 in WSC In-house Staff rate case expense. In the last rate case, the Company requested an original estimate for WSC staff of $87,928 and revised actual and estimate to complete was $89,906. In the final order the Commission disallowed all of the WSC requested costs as unsupported and duplicative of salaries and benefits already included in rates. When the Company filed its actual rate case expense incurred in that docket, as of June 30, 2012, the amount reflected for total WSC costs incurred was only $38,975.

    a. OPC requests an explanation why the company has requested an estimate of more than 100% of the amount actually incurred in the last rate case.

    b. Given that the case concluded just over two years ago, an explanation of what factors might necessitate such a high increase in in-house costs and why the costs should not be at or lower than those incurred for the last rate case.

14. In Labrador's last rate case, the Commission disallowed all WSC In-house Staff rate case expense because the Company did not sufficiently document that the requested in-house labor was not duplicative of the salaries and wages included in the rate case.

    a. The Company should provide proof showing that its pro forma salary adjustment and rate case expense request for WSC in-house employees does not reflect a requested double recovery of those employee's salary and benefit dollars.

    b. Also, the Company should provide a detailed breakdown by hour including a description of the specific work performed of all WSC employees that spend and allocate time to the rate case.

15. OPC would note that historically Milian, Swain and Associates firm has not provided the level of detail that Staff has requested.

a. Utilities Inc. should explain why it does not obtain or require its accounting consultants to breakdown their billable hours with detailed descriptions in the same manner than their attorney and engineering consultant provide.

b. Given that the staff rate case expense data requests for detailed breakdowns by hour have contained standard, identical questions for at least the last 15 years, the Company should explain why such fees should be allowed to be recovered if the Company continues to not provide the requested detail, and thus fails to meet its statutory burden.

F. Deferred Income Taxes. On MFR Schedule D-2, the Company reports an accumulated deferred income tax (ADIT) net credit balance of $23,472 for 2012 and a net debit balance of $29,994 for 2013, for an average test year debit balance of $3,261. Based on this net debit balance, OPC has performed several analyses to see why a company that has been in existence for approximately 25 years[1] would not have credit deferred taxes, especially those related to accelerated depreciation. We have compiled a schedule that takes Labrador's current and all prior MFR filings from Schedule C-6 related to ADITs. The PDF version of the schedule is attached to this letter and any Excel worksheets will be forwarded by separate email. The analysis starts in 2002 and breaks out each entry from the MFRs into federal, state and combined total. The compilation brings out several questions that the Company should address to answer why Labrador's net ADITs are debit instead of credit balances. One would expect a 25 year old company that has an estimated 15 remaining years of an average 40-year life amortization period for treatment plant and lines would start with and maintain a credit ADIT balance for at least accelerated depreciation until the useful life of the average plant has expired. OPC's questions regarding ADIT and the reflected balances are as follows:

16. ADIT Federal and State Depreciation. The Company should explain how since 2002 Labrador has maintained a debit instead of a credit balance for ADITs related to accelerated depreciation.

17. The Company in Docket No. 080249-WS, MFR Schedule C-6 page 3 of 3, for the years 2003, 2004 and 2005, made adjustments of $3,880, $33,538 and $77,441, respectively, to "flowback to current year" deferred federal income taxes, which essentially reversed the deferred tax accruals for those years. The Company should explain why this was done.

18. The Company should provide an analysis of how deferred income tax balances are calculated each year especially for accelerated depreciation, including which amounts are

[1] See Order No. PSC-01-1483-PAA-WS in Docket No. 000545-WS, issued July 16, 2001, In re: Application for original certificates to operate a water and wastewater utility in Pasco County by Labrador Services, Inc., page 2.

direct to Labrador and which amounts are allocated from any business unit. The Company should also provide a copy of all calculations showing how each accrual and any adjustments amounts by account were calculated for the test year 2013.

19. The Company should explain how the negative acquisition adjustment and the related annual amortization are incorporated into the amount of deferred income taxes that are calculated and reflected in credit deferred income taxes.

20. The Company should explain why Labrador has a debit balance of $110 for Federal tax tap fees (Account 190.1012) that has not changed since 2008. It should also explain how these debit deferred taxes originated, when will they reverse, and why there is no annual amortization on this account.

21. Labrador should explain how the deferred tax federal and state rate case ADITs (Account 190.1020) arise and are calculated on a system specific basis including any allocations from any other business unit for Labrador. It should also provide a copy of the workpapers that show how the annual accrual/deferral, flowback to current year and any adjustment amounts were determined from annually from 2010 to 2013.

22. The Company should explain how the deferred tax federal and state Maintenance Fees ADITs (Account 190.1021) arise and are calculated on a system specific basis for Labrador including any allocations from any other business unit. It should also provide a copy of the workpapers that show how the annual accrual/deferral, flowback to current year and any adjustment amounts were determined from annually from 2010 to 2013.

23. Labrador should explain how the deferred tax federal and state Organization Expenses ADITs (Account 190.1024) arise and are calculated on a system specific basis including any allocations from any other business unit for Labrador. It should provide a copy of the workpapers that show how the annual accrual/deferral amounts were determined from annually from 2010 to 2013.

24. The Company should explain how the deferred tax federal and state bad debt ADITs (Account 4436) arise and are calculated on a system specific basis including any allocations from any other business unit for Labrador. It should also provide a copy of the workpapers that show how the annual accrual/deferral and any adjustment amounts were determined from annually from 2010 to 2013.

25. In 2013 the Company added new account line items as a debit account Acct 4389 190.1 Def. Fed. Tax NOL for federal taxes and Acct 4389 190.1 Def. State Tax NOL for state taxes. The entries made to these accounts have increased the debit ADITs by $36,744. The company should explain if this is a Labrador system specific amount or if it is a

Company allocated amount and explain how the 2013 amounts were calculated on a system specific basis including any allocations from any other business unit for Labrador. It should also provide a copy of the workpapers that show how the annual accrual/deferral and any adjustment amounts were calculated in 2013. Further, Labrador should explain why it is reasonable for the ratepayers to pay for the Company's investment in a NOL when the customers have not received the benefit associated with any reduction in income tax expense associated with the NOL.

26. Pursuant to Order No. PSC-14-0044-FOF-WS, issued January 22, 2014, Utilities, Inc. agreed as part of its stipulation in Issue 6 that for rate cases, it would make adjustments to its capital structure as necessary to reflect the proper amount of deferred income taxes on proforma plant additions. Labrador should explain where in its MFRs UI has reflected the adjustments to reflect the credit ADITs on the proforma adjustments, and if not, provide all adjustments and workpapers necessary to show what amounts would be added to ADITs to comply with the Commission approved settlement regarding this issue.

G. Accumulated Depreciation Balances. OPC has concerns regarding the balances of accumulated depreciation for the following accounts.

Water

301.1 Organization
333.4 Services
335.4 Hydrants
336 Backflow Prevention Devices

Wastewater

360.2 Collection Sewers – Force
371.3 Pumping Equipment
375.3 Reuse Transmission and Distribution System
381.4 Plant Sewers
382.4 Outfall Sewer Lines

27. The Company should explain why it is appropriate for each of the above accounts to have negative balances in accumulated depreciation.

28. Water Organization accumulated depreciation is especially inappropriate as there is no associated plant balance and annual depreciation expense is being charge to this account. The Company should explain why this accumulated depreciation balance exists and why depreciation expense is charged for this non-existent plant account.

H. Plant Retirements. In 2013 for Account 360 Collection Sewers-Force, the beginning balance for this account was $6,057. The Company added a $56,306 addition and a retirement of $18,925. The accumulated depreciation for this account had a beginning balance of ($7,082), an annual accrual of $458 and a retirement of $18,925. This left a negative (debit) balance of $25,548.

29. Labrador should explain why the Company made a retirement entry to a plant account that did not contain the dollar amount of the amount retired.

30. Further, in 2011, the Company reflected a retirement entry of $656 to accumulated depreciation without a corresponding retirement entry to plant. The Company should explain why this retirement entry adjustment is appropriate.

I. Tools Shop and Garage Equipment. OPC has concerns regarding the level of changes in this account for water and wastewater.

31. The Company should explain why the water balance in Account 343.5 increased more than double from $19,210 to $39,571 for 2012 to 2013.

32. For wastewater in 2013, the Company reflected a negative addition of $16,895 (with no retirement adjustment) in this account. The Company should explain why this negative addition was made without a retirement entry.

J. Legal Fees. Legal fees during 2012 and 2013 have increased substantially.

33. Please provide a copy of invoices associated with all legal fees incurred and charged to Labrador in 2012 and 2013. The invoices should include the breakdown by attorney, by hour and include a description of the type of work performed during each year.

K. Workpapers for All Proforma Rate Base, Net Operating Income and Capital Structure Adjustments. The Company should provide a copy of all of its workpapers used to make all of its proforma adjustments in its rate case.

L. Lease Expense. OPC notes that the Company made a proforma adjustment to allocate parent company lease expenses which appears to be inconsistent with the methodology used by the Commission to establish the allowed lease expense.

34. If this lease expense relates to property allocated from the parent company and is not related to the Labrador treatment plant land, The Company should explain to what this allocation relates and why this additional amount should be allowed.

35. If the allocation relates to an affiliate charge and is specifically related to the Labrador water and wastewater land lease, the Company should explain why it is appropriate for the parent Company to allocate additional costs to Labrador in addition to the original cost of the land on which the value of the annual lease amount was determined by the Commission.

M. Short-term Debt. In Labrador's MFRs, Schedule D-4, it reflects a simple average parent company level of short-term debt from a Chase Revolving Line of Credit of $3,100,000, with annual interest expense of $262,837 for a cost rate of 8.48%. On MFR Schedule D-2, Labrador reflects a beginning balance of $500,000 and an ending balance of $5,700,000 for short-term debt. The Sanlando rate case in Docket No. 140060-WS uses the same test year ended December 31, 2013 with a thirteen month average capital structure as contrasted with a simple average due to the difference in size between the two systems. In that case, the Company reflected a cost rate of 2.82%for Sanlando compared to the 8.48% for Labrador. According to Labrador's 2012 Annual Report (pages F-5 and F-6), the balance of total company short-term debt was $500,000 at a cost rate of 0.00% and on the same pages in the 2013 Annual Report the balance of total company short-term debt was $262,837 at a cost rate of 4.61%. As a note, the 2012 and 2013 Sanlando Annual Reports reflect the same amounts and cost rates for the parent company as reflected for Labrador.

36. The Company should provide the test year monthly balances of short-term debt and the monthly amount of interest expense.

37. Labrador should provide a copy of the line of credit documents that reflect the terms of the debt and how the interest rate is determined.

38. The Company should explain why an interest rate of 8.48% for short-term debt in today's market is a reasonable cost rate for a company the size of Utilities, Inc.

39. Labrador should also explain why the amount and cost rate of the parent's short-term debt reflected in the MFRs does not agree with the amounts reported in the Annual Reports.