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: October 25, 2001

TO: DIRECTOR, DIVISION OF THE COMMISSION CLERK & ADMINISTRATIVE SERVICES (BAYÓ)

FROM: DIVISION OF ECONOMIC REGULATION (CROUCH, MERCHANT, B. DAVIS, WETHERINGTON)
DIVISION OF LEGAL SERVICES (JAEGER)

RE: DOCKET NO. 992015-WU - APPLICATION FOR LIMITED PROCEEDING TO RECOVER COSTS OF WATER SYSTEM IMPROVEMENTS IN MARION COUNTY BY SUNSHINE UTILITIES OF CENTRAL FLORIDA, INC.
COUNTY: MARION

AGENDA: 11/6/2001 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\ECR\WP\992015.RCM

CASE BACKGROUND

Sunshine Utilities of Central Florida, Inc. (Sunshine or utility) is a Class B utility which provides water service to approximately 2,871 water customers in 21 separate small systems around the Ocala area in Marion County (see attached map No. 1). Wastewater service is provided by septic tanks. The utility's last rate proceeding was in Docket No. 900386-WU, resulting in Order No. 25722, issued February 13, 1992. Order No. PSC-94-0738-FOF-WU, issued June 15, 1994, addressed Sunshine's appellate rate case expense for that docket.

On December 21, 1999, Sunshine filed an application for a limited proceeding to increase water rates and charges for all of its customers in Marion County. The rate increase requested is intended to be used to initiate a water facilities plan in which

the utility would interconnect and consolidate five of the 21 separate systems owned by Sunshine. In conjunction, the utility intends to construct a centralized water treatment, pumping, and storage facility (see attached maps Nos. 2 & 3) to serve the five systems specified in the utility's comprehensive plan. Sunshine proposed this plan in order to resolve contamination problems faced by some customers and by a few non-customers near its service area. Further, the plan is designed to meet growth demands in the area of the interconnection.

Contamination

One of the five systems to be interconnected in this proposal is Lakeview Hills. The Lakeview Hills water treatment plant, which consists of a well and a hydro-pneumatic tank, is located across from a county dump along S.E. 115th Avenue in the southeastern portion of Marion County, very near the northwest shoreline of Lake Weir. (See attached map No. 2). The Department of Environmental Protection (DEP) discovered the presence of Dichloroethylene, a carcinogen, in the well serving the Lakeview Hills system. The level detected was below the maximum contaminant level (MCL). While no corrective actions have been ordered by DEP to date, DEP is requiring quarterly Volatile Organic Compound (VOC) tests to monitor these levels.

In addition, a second contamination problem was discovered in private wells serving residents living along S.E. 138th Place Road near the northwest shoreline of Little Lake Weir, midway between the utility's Hilltop system and its Little Lake Weir system (See Map No. 3). The contaminant found in the private wells is Ethylene Dibromide (EDB). The residents are not customers of Sunshine and the contaminated wells are private, residential wells. The DEP makes grants available for private utilities to extend their systems to meet the needs of those residents outside the utility's service area who are victims of contamination and must seek alternate sources of water.

Utility's Proposal

Sunshine has proposed to solve the two contamination problems discussed above by obtaining funding from DEP for its water facilities plan. This plan included the construction of a new water facility, the installation of over twelve miles of transmission mains, and the extension of specific water service to

serve two residents outside the utility's existing territory. In addition, funding for this project would be a combination of a grant and a low-interest "State Revolving Fund" (SRF) loan arranged through the DEP. The DEP Bureau of Water Facilities Funding has a program that has money available for such needs, and the utility has satisfied the criteria and has qualified for a $682,570 grant and could qualify for a low-interest loan of $1,475,314 contingent upon Commission approval of a rate increase. The DEP has issued $153,000 as a Preconstruction Grant, and $32,500 as a Preconstruction Loan toward the total project.

After several meetings with Commission staff, it became apparent to the utility that staff did not support its proposal since the proposal would provide limited benefits to only five of the utility's 21 systems. It was staff's belief that the improvements did little to improve the quality of water or the service provided to the customers of those five affected systems and no benefits whatsoever to the other 16 systems. In its filing, Sunshine requested that the rate increase be passed on to all of its customers, not only to the customers of the five systems involved. In light of staff's comments, Sunshine withdrew the application and asked for and was allowed time to revise its proposal.

On September 8, 2000, Sunshine submitted an Amended Application in which it presented two alternatives. Under its first alternative, Sunshine submitted essentially the original proposal as discussed above. The utility still proposed passing on a rate increase of 22.19% to all of its customers. Under Alternative No. 2, Sunshine proposed a project of a more limited scope that would address only the contamination problems in Little Lake Weir and Lakeview Hills systems as well as the sulfur concerns in the Oklawaha area.

Within Alternative No. 2, Sunshine proposed two different rate plans. First, the rate increase of 18.2% would be passed on to all of Sunshine's customers. In the second proposal, a rate increase of approximately 88.45% would be passed on to only the 750 customers of the four systems involved.

Staff filed a recommendation on November 16, 2000 for the November 28, 2000 Agenda Conference, but that recommendation was initially deferred to the December 19, 2000 Agenda Conference. However, at the request of the utility, staff's recommendation was

deferred from that Agenda Conference and never presented to the Commission.

On June 7, 2001, Sunshine filed an amendment to its September 8, 2000 amended application. In this second amended application, Sunshine is proposing to interconnect five systems. These five systems are known as Lake Weir, Lakeview Hills, Oklawaha, Belleview Oaks and Hilltop.

According to the utility, the consolidation is to eliminate the existing contamination problems and will improve the level of service that Sunshine can provide to its water customers. The consolidation is proposed to be funded by the combination of grants and low interest loans discussed above. The plan includes a proposed rate increase of 15.73% for all of Sunshine's customers.

This recommendation addresses the prudence of the project and whether this limited proceeding should be approved. The Commission has jurisdiction pursuant to Section 367.0822, Florida Statutes.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve Sunshine's requested limited proceeding to increase its rates for all customers to interconnect five of its water systems?

RECOMMENDATION: No. The utility's proposal to interconnect five separate water supply and treatment systems to eliminate contamination problems and to meet development demands is not prudent or justified, and it should therefore be denied. (CROUCH, WETHERINGTON)

STAFF ANALYSIS: The utility has made the proposal to interconnect the five existing water systems of Little Lake Weir, Lakeview Hills, Belleview Oaks, Hilltop, and Oklawaha with 31,499 linear feet of 10-inch pipe, 15,048 linear feet of 8-inch pipe, and 3,183 linear feet of 6-inch pipe. The utility also proposes to construct a separate water treatment plant to singularly serve this new water main system. The Oklawaha system is currently interconnected with Lake Weir Pines. Technically, the utility would be interconnecting six water systems at an approximate cost of $2,015,339. The reason cited by the utility for this project is that it will address contamination in the water supply, meet peak water demand and fire flow requirements and promote water conservation.

Contamination Problems

The Lakeview Hills water treatment plant is located across from a county dump site which is located along S.E. 115th Avenue in the southeastern portion of Marion County, very near the northwesterly shoreline of Lake Weir. DEP has found the presence of Dichloroethylene in the one well serving the Lakeview Hills systems. The level detected was considered satisfactory, but was very close to the Maximum Contaminant Level (MCL). At present, there are no corrective orders mandating that the utility correct this contamination problem. However, the DEP does require quarterly Volatile Organic Chemical (VOC) tests to monitor the contaminate levels. In addition, the County has stepped in and committed to install a used filter at the Lakeview Hills water treatment plant, without charge to the utility, and with no time limit on the return of the filter. By all appearances, the contamination within the utility's existing water system has been brought under control.

The detection of another contaminant, Ethylene Dibromide, has been found in the private wells of residents located along S.E. 138th Place Road. S.E. 138th Place Road runs along the northwest shoreline of Little Lake Weir, and is about mid-way between the Hilltop system and the Little Lake Weir system. Ethylene Dibromide is used as a grain fumigant, general solvent and in waterproofing preparations. Ethylene Dibromide may enter the environment from industrial discharges or spills, and is a carcinogen. It is considered that any level of this contaminant is unsafe and private wells that contain this substance must be abandoned and an alternate source of water supply must be utilized. The Hilltop system has a 6-inch main that runs along S.E. 100th Avenue. S.E. 100th Avenue extends southerly from the Hilltop system for approximately 7,500 linear feet before it intersects with S.E. 138th Place Road. Staff believes that a main extension along S.E. 100th Avenue would provide those private residents with the alternate source of drinking water they require.

DEP Approval

The DEP makes available grant and low interest loan money for private utilities to expand their system to meet the needs of those outside their service territory who must seek an alternate source of drinking water. The utility has made application with DEP, and DEP has approved Sunshine to receive $682,570 in grants and $1,475,314 in a low interest loan subject to proof that the utility's rate structure is sufficient to pay back the loan.

In discussions between PSC staff, DEP staff, and the utility, it was acknowledged that even though DEP approves of this project, DEP is not requiring the work to be done. DEP considers "regional" systems, those combining several small systems into one, as easier to operate and regulate. The current contamination problems, however, are being addressed by either grant monies for main extensions or by existing treatment facilities.

Future Development

Before the utility can begin serving future customers along this main extension project, they must submit to this Commission an application for an amendment to its current certificate. The request must include the addition of any territory between each of the five water systems to be interconnected. It was noted during the engineering field visit that there are several subdivisions

within those areas that have existing, small water systems which are making drinking water available to their residents. Any territorial disputes would need to be settled before the certificate could be amended and before the utility could begin construction.

Once the certificate was amended, the utility would need to apply for an adjustment to its rate structure which would require a study of the potential customer base the additional territory would encompass. Because the main extension is not being mandated by a governing agency, there is no statutory requirement that the project be considered 100% used and useful. It appears that "meeting development demands" is the primary concern that is driving this project. Therefore, the new system would be subject to a used and useful analysis based on the potential customers this new water main system would afford the utility.

Summary

Because the contamination concerns are eliminated by the use of the County's filter system, Sunshine is not under a mandate concerning the high MCL for Dichloroethylene. Interconnecting the five systems and construction of a single plant to serve those existing customers is not required. Neither is the interconnection of the five water systems into one system necessary to provide a source of drinking water to the private residents in need of an alternate drinking water source. It appears that the only viable reason would be to meet future development plans. Staff believes that the cost of future development should be offset mostly by higher service availability charges which the company has not considered in this application. The utility might also consider advance developer agreements wherein developers could guarantee availability of water for areas not yet developed.

Therefore, staff recommends that the utility's proposal to combine and interconnect five separate, existing water supply and treatment systems to eliminate contamination problems and to meet development demands at the expense of all its existing customers is not prudent or justified, and it should therefore be denied.

ISSUE 2: What is the appropriate amount of rate case expense for Docket No. 992015-WU?

RECOMMENDATION: Staff recommends that rate case expense for this limited proceeding should be disallowed. (B. DAVIS)

STAFF ANALYSIS: The utility included a $35,000 estimate in the original filing on December 23, 1999, for current rate case expense: $20,000 for legal and $15,000 for accounting. The utility submitted an amended filing on September 8, 2000, but included no additional rate case expense. Although Staff filed a recommendation for the November 28, 2000 Agenda Conference, it was deferred and was never presented at agenda. Staff met with the utility and the Office of Public Counsel OPC, and subsequent to that meeting the utility filed a second amended filing on June 7, 2001. In that revision the utility requested rate case expense of $115,338, an increase over the original of $85,338. That amended filing increased requested legal fees by $30,439, accounting fees by $19,207 and added an additional $30,439 for engineering. The original filing did not contain any requested rate case expense for engineering, only capitalized engineering expense in the plant additions.

As part of its analysis, staff requested an update of the actual rate case expense incurred, with supporting documentation, as well as the estimated amount to complete. On August 1, 2001, the utility submitted a schedule of revised estimated rate case expense through completion of the Proposed Agency Action (PAA) process of $115,338. The components of the estimated rate case expense are as follows:

	ORIGINAL ESTIMATE	ACTUAL PER UTILITY	ADDITIONAL ESTIMATE	REVISED TOTAL
Legal Fees	$15,000	$42,112	$3,580	$45,692
Accounting Fees	20,000	3,508	5,699	39,207
Engineering	0	30,439	0	30,439
Total Rate Case Expense	$35,000	$106,059	$9,279	$115,338
Annual Amortization	$8,750			$28,835

As discussed in Issue 1, staff has recommended that no increase be granted for this limited proceeding filed by Sunshine. Based on the financial information for December 31, 2000 submitted

by the utility in its annual report, the utility was earning slightly under the rate of return authorized in Order No. 25722, issued February 13, 1992, in Docket No. 900386-WU, the utility's last rate case. Under the Commission's rate setting authority, a utility seeking a change in rates must demonstrate that its present rates are unreasonable. South Fla. Natural Gas v. Florida Public Service Commission, 534 So. 2d 695, 697 (Fla. 1988). Staff recommends that it is inappropriate to approve rate case expense because, without the additional construction costs, no rate increase is warranted.

As such, staff believes that the decision to file for rate relief was imprudent and the customers should not have to bear this cost. Chapter 367.081(7), Florida Statutes, states that the Commission "shall disallow all rate case expenses determined to be unreasonable. No rate case expense determined to be unreasonable shall be paid by the customer." The Commission has previously disallowed rate case expense in a limited proceeding in which the rate increase was denied. See Order No. PSC-98-1583-FOF-WS, issued November 25, 1998 in Docket No. 971663-WS, Application of Florida Cities Water Company for Recovery of Environmental Litigation Costs; and Order No. PSC-99-1917-PAA-WS issued September 28, 1999, in Dockets Nos. 970536-WS and 980245-WS, Aloha Utilities, Inc., limited proceedings. Moreover, the Commission enjoys broad discretion with respect to the allowance of rate case expense. Meadowbrook Utility Systems, Inc. v. FPSC, 518 So. 2d 326 (Fla. 1st DCA 1988).

However, if staff's recommendation to deny the project described in Issue 1 is not approved by the Commission, staff does not believe that the full amount of the utility's revised rate case expense is reasonable. On September 20, 2001, the utility submitted the detail behind the actual rate case expense incurred to date. Staff has examined the requested actual expenses, supporting documentation, and estimated expenses as listed above for the current rate case. Staff believes that the revised estimate includes $40,409 incurred to file two sets of revisions to its application in this limited proceeding. This includes $27,239 in legal fees and $13,170 of accounting fees. These are the fees incurred between August, 2000, and the present. Staff believes that these fees were incurred to duplicate the original application and did not add anything that could not have been included in the original. The actual project has remained, essentially, unchanged.

The rate payers are being asked to pay for three filings of the same project. Staff believes that these amounts are unreasonable.

Staff believes that the decision to file this limited proceeding was the utility's choice. It then made a management decision to amend the filing. After discussions with staff, the utility submitted yet another completely revised filing which did little to change the actual project, but did add a used and useful adjustment. Staff believes that these additional and duplicative costs to amend and then to completely re-do the filing should not have been incurred and should not be passed on to the ratepayers. This is consistent with Commission decisions in Order No. PSC-00-1528-PAA-WU, issued August 23, 2000, in Docket No. 991437-Wu for Wedgefield Utilities, Inc.; Order No. PSC-00-2054-PAA-WS, issued October 27, 2000, in Docket No. 990939-WS for Indiantown Company, Inc.; and Order No. PSC-01-0327-PAA-WU, issued February 6, 2001, in Docket No. 000295-WU for Placid Lakes Utilities, Inc. In all three of those cases, the Commission denied recovery of duplicative rate case expense associated with filing revisions of minimum filing requirements.

Staff notes for informational purposes that, if the project were to be approved, the appropriate total rate case expense that staff would recommend is $74,929. A breakdown of this amount is as follows:

	UTILITY REVISED ACTUAL & ESTIMATE	STAFF ADJUSTMENTS	STAFF ADJUSTED BALANCE
Legal Fees	$45,692	($27,239)	$18,453
Accounting Fees	39,207	(13,170)	26,037
Engineering Fees	30,439	0	30,439
Total Rate Case Expense	$115,338	($40,409)	$74,929
Annual Amortization	$28,835		$18,732

If the limited proceeding is approved, the recommended allowable rate case expense should be amortized over four years, pursuant to Chapter 367.0816, Florida Statutes, at $18,732 per year. Based on the data provided by the utility and the staff recommended adjustments mentioned above, staff would recommend that

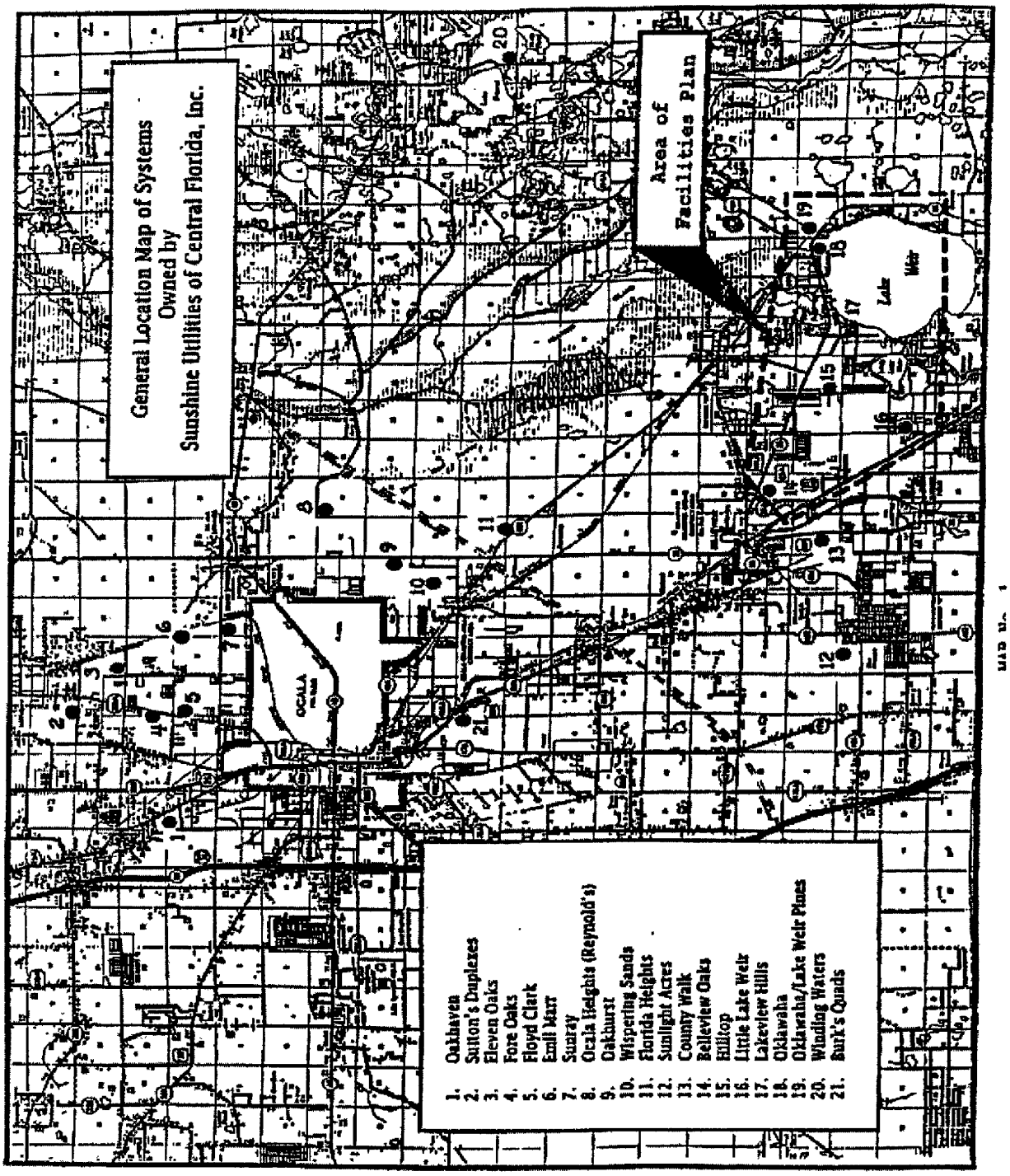
the rate case expense should be reduced by $40,409 if the project were approved.

However, based on staff's recommendation in Issue 1, staff recommends that all rate case expense for this limited proceeding be disallowed.

ISSUE 3: Should Docket No. 992015-WU be closed?

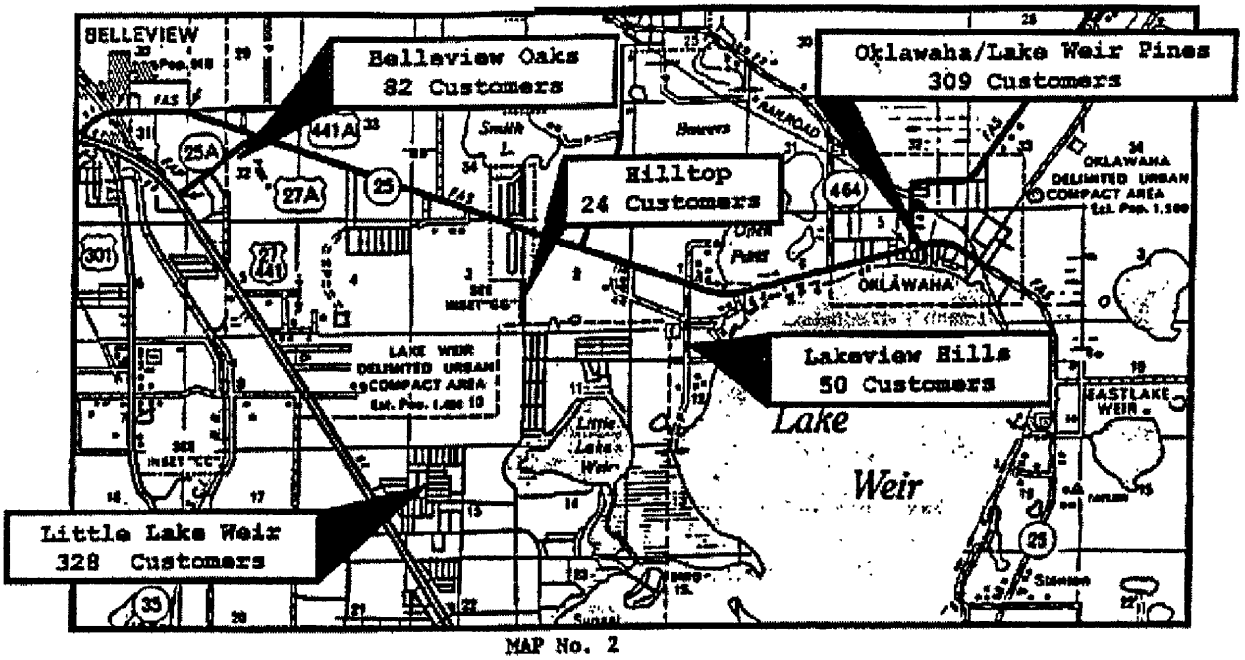
RECOMMENDATION: Yes. If no timely protest is filed by a substantially affected person, the order should become final and effective upon the issuance of a consummating order and the docket should be closed at that time. (JAEGER)

STAFF ANALYSIS: If no timely protest is filed by a substantially affected person, the order should become final and effective upon the issuance of a consummating order. The docket should be closed at that time.


General Location Map of Systems
Owned by
Sunshine Utilities of Central Florida, Inc.
Area of
Facilities Plan
Lake
Weir
OCALA
1. Oakhaven
2. Sutton's Duplexes
3. Eleven Oaks
4. Fore Oaks
5. Floyd Clark
6. Emil Narr
7. Sunray
8. Ocala Heights (Reynold's)
9. Oakhurst
10. Whispering Sands
11. Florida Heights
12. Sunlight Acres
13. County Walk
14. Belleview Oaks
15. Hilltop
16. Little Lake Weir
17. Lakeview Hills
18. Oklawaha
19. Oklawaha/Lake Weir Plnes
20. Winding Waters
21. Burk's Quads

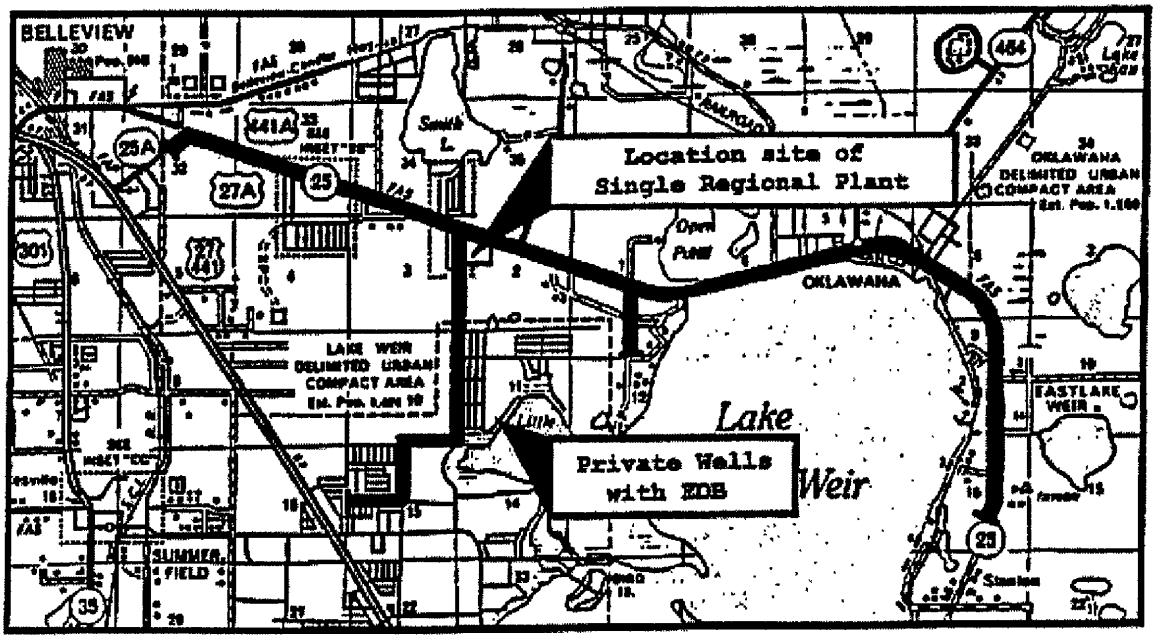
Map No. 1

Existing Five Independent Water Systems



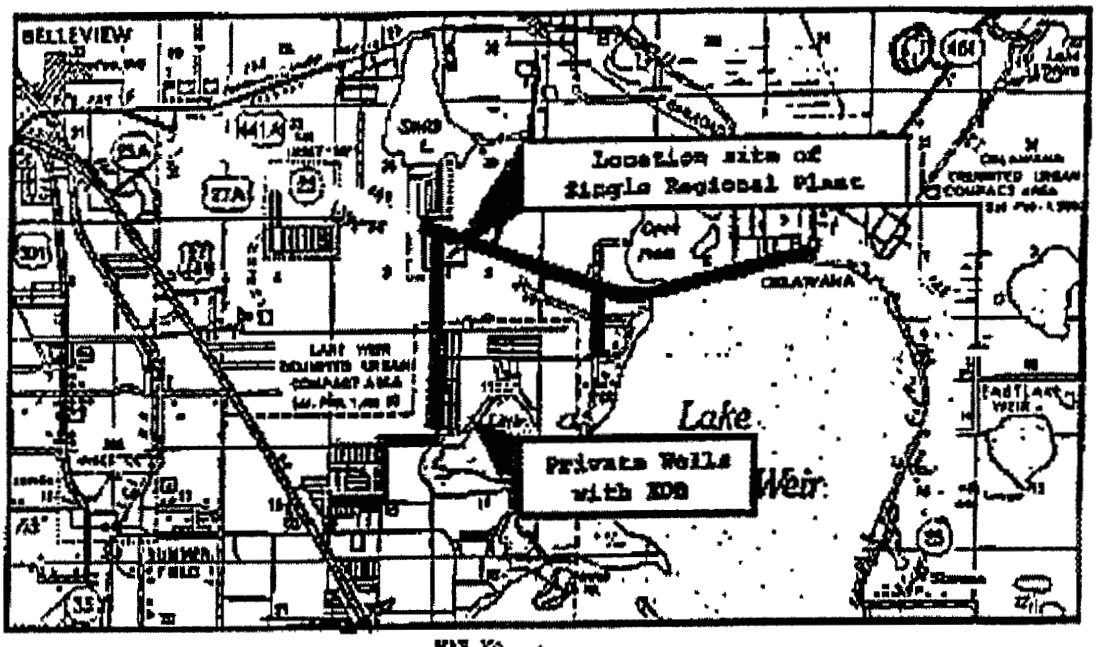
MAP No. 2

Proposed Plant and Regional Transmission System



MAP No. 3

Alternative #2
Proposed Plant and Regional
Transmission System



EXF No. 4

0 1 mile
Scale - |_____|