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ORIGINAL

November 7, 2001

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COMMISSION
CLERK

Ms. Blanca S. Bayó, Director
Division of the Commission Clerk
and Administrative Services
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0870

RE: Docket No. 010503-EI

Dear Ms. Bayó:

Enclosed are an original and fifteen copies of Direct Testimony of Hugh Larkin, Jr. for filing in the above-referenced docket.

Also enclosed is a 3.5 inch diskette containing the Direct Testimony of Hugh Larkin, Jr. in WordPerfect for Windows 6.1. Please indicate receipt of filing by date-stamping the attached copy of this letter and returning it to this office. Thank you for your assistance in this matter.

Sincerely,

Stephen C. Burgess
Deputy Public Counsel

SCB/dsb

Enclosures

- APP _____
- CAF _____
- OMP _____
- COM Strg
- CTR _____
- ECR _____
- LEG _____
- OPC _____
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- SEC 1
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FPSC-BUREAU OF RECORDS DOCUMENT NUMBER-DATE

14178 NOV-7 01

FPSC-COMMISSION

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for increase)
in water rates for Seven Springs)
System in Pasco County by Aloha)
Utilities, Inc.)

Docket No. 010503-WU
Filed: November 7, 2001

DIRECT TESTIMONY OF

HUGH LARKIN, JR.

Respectfully submitted,
Jack Shreve
Public Counsel

Office of Public Counsel
c/o The Florida Legislature
111 West Madison Street
Room 812
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(850) 488-9330

Attorney for the Citizens
Of the State of Florida

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Attorney for the Citizens
Of the State of Florida

1 DIRECT TESTIMONY OF HUGH LARKIN, JR.

2 ON BEHALF OF THE CITIZENS OF FLORIDA

3 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

4 ALOHA UTILITIES, INC.

5 DOCKET NO. 010503-WS

6
7 I. INTRODUCTION

8 Q. WHAT IS YOUR NAME, OCCUPATION AND BUSINESS ADDRESS?

9 A. My name is Hugh Larkin, Jr. I am a Certified Public Accountant licensed in the States of
10 Michigan and Florida and the senior partner in the firm of Larkin & Associates, PLLC,
11 Certified Public Accountants, with offices at 15728 Farmington Road, Livonia, Michigan
12 48154.

13
14 Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCIATES, PLLC.

15 A. Larkin & Associates, PLLC, is a Certified Public Accounting and Regulatory Consulting
16 Firm. The firm performs independent regulatory consulting primarily for public service/utility
17 commission staffs and consumer interest groups (public counsels, public advocates, consumer
18 counsels, attorneys general, etc.). Larkin & Associates, PLLC, has extensive experience in
19 the utility regulatory field as expert witnesses in over 300 regulatory proceedings including
20 numerous water and sewer, gas, electric and telephone utilities.

1 Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE FLORIDA PUBLIC SERVICE
2 COMMISSION?

3 A. Yes. Over the last 25 years, I have testified before the Florida Public Service Commission
4 in numerous rate cases involving water and wastewater utilities.

5
6 Q. BY WHOM WERE YOU RETAINED, AND WHAT IS THE PURPOSE OF YOUR
7 TESTIMONY?

8 A. Larkin & Associates, PLLC, was retained by the Florida Office of Public Counsel (OPC) to
9 review the rate increase requested by Aloha Utilities, Inc., for its Seven Springs Water
10 Division. Accordingly, Donna DeRonne and I are appearing on behalf of the Citizens of
11 Florida (“Citizens”).

12
13 Q. WHAT WILL YOUR RESPECTIVE TESTIMONIES ENCOMPASS?

14 A. Ms. DeRonne’s testimony deals with rate case adjustments and their proper calculations to
15 determining a revenue requirement for Seven Springs Water Division.

16
17 I have been asked by the Florida Office of Public Counsel to provide testimony regarding
18 whether Aloha has met basic ratemaking principles, which would allow the Commission to
19 authorize a rate increase. I have also been asked to review the reasonableness of the
20 Company’s request for rate case expense.

21

1 Q. DO YOU THINK THAT ALOHA HAS MET BASIC RATEMAKING PRINCIPLES THAT
2 WOULD ALLOW THE COMMISSION TO AUTHORIZE A RATE INCREASE FOR ITS
3 SEVEN SPRINGS WATER DIVISION?

4 A. No, I do not.

5
6 Q. WHAT RATEMAKING PRINCIPLE HAS NOT BEEN MET BY ALOHA WHICH
7 WOULD REQUIRE THE COMMISSION TO NOT AUTHORIZE ANY RATE
8 INCREASE FOR THE COMPANY'S SEVEN SPRINGS WATER DIVISION?

9 A. Aloha's Seven Springs Water Division has failed to meet a competitive standard for service,
10 which would allow a rate increase. In other words, in a competitive environment, Aloha
11 would not be able to raise prices because the quality of its water was below comparable
12 service from other water companies.

13
14 Q. WHY SHOULD ALOHA BE DENIED A RATE INCREASE BASED ON ITS FAILURE
15 TO MEET A COMPETITIVE STANDARD?

16 A. Since my first exposure to rate regulation in 1970, the underlying principle upon which rates
17 and service have been based is the competitive model. James C. Bonbright set forth this
18 principle in his text, Principles of Public Utility Rates, as follows:

19 Regulation, it is said, is a substitute for competition. Hence its objective should be
20 to compel a regulated enterprise, despite its possession of complete or partial
21 monopoly, to charge rates approximating those which it would charge if free from
22 regulation but subject to the market forces of competition. In short, regulation should
23 be not only a substitute for competition, but a closely imitative substitute.¹

¹Public Utility Rates, Columbia University Press, Copyright 1961, p. 93.

1 The competitive principle requiring that regulation be a substitute for competition would view
2 both price and service from a competitive standpoint. If the provision of water services were
3 a competitive product, and the customers of the Seven Springs Water Division of the Aloha
4 Utility had a choice, they would clearly reject to deal with Aloha because of the poor quality
5 of the water service provided. Aloha's water quality would not meet a competitive standard,
6 and in a competitive environment would be rejected by customers. In Docket No. 960545-
7 WS, overwhelming evidence demonstrated that a vast number of the Seven Springs water
8 division customers found Aloha's overall product and service to be completely unacceptable.
9 In that docket, Aloha touted a plan that it claimed would resolve much of the problems. In
10 the current rate docket, however, Aloha has not offered any evidence that any of the problem
11 areas identified in Docket No. 960545-WS have been eliminated or even improved in any
12 manner whatsoever. OPC Witness Ted L. Biddy discusses the "black water problem" and the
13 lack of progress made by the Company in improving or eliminating this water quality problem.
14 I was a witness in Aloha's Seven Springs Wastewater increase request in Docket No. 991643-
15 SU. Even though this was a wastewater hearing dealing with wastewater service only,
16 customer after customer testified regarding the quality of Seven Springs water quality and
17 service. A number of customers expressed disdain for both the Company and its
18 management.

19
20 Q. WHY SHOULD ALOHA'S TERRIBLE SERVICE DISQUALIFY THE UTILITY FROM
21 RECEIVING HIGHER RATES?

1 A. It is a well-established principle of regulation that the regulatory process should act as a
2 surrogate for a competitive market. This principle is grounded in both logic and legal
3 precedent.

4
5 Q. WHAT IS THE LOGIC BEHIND THE PRINCIPLE THAT REGULATION ACT AS A
6 SURROGATE FOR COMPETITION?

7 A. If there were an open market for water services, any customer who was dissatisfied in any
8 way with a water company's product could simply purchase water from a competitor. It is
9 this freedom that keeps a supplier "honest" and creates a supply of a reasonable product at
10 a reasonable price.

11
12 In a regulated industry, however, this customer choice is taken away. Customers are required
13 to purchase water (a product that one must have to live) from a single designated supplier.
14 Since the customer choice is removed, a strong regulatory process is the only thing that
15 remains to keep the supplier "honest."

16
17 Fundamental fairness demands that if the government removes a customer's right to choose
18 the supplier of his preference, it must replace that right with a regulatory process that
19 produces results that approximate what would have been achieved through a market choice.
20 That is the logic underlying the principle that regulation should act as a surrogate for
21 competition.

22

1 Q. IN WHAT WAY DO YOU BELIEVE COMPETITIVE PRINCIPLES SHOULD BE
2 APPLIED TO ALOHA'S CURRENT RATE CASE?

3 A. Based on the customer testimony that has been presented in the two recent Aloha dockets,
4 vast numbers of customers would go elsewhere if they had a choice. I have never
5 encountered a higher level of customer dissatisfaction. If Aloha faced any competition, it
6 would lose customers in droves – even at the current rates. At this level of disapproval with
7 its product, if a competitive enterprise were to actually be brazen enough to increase prices,
8 it would assure a mass exodus of its customers.

9
10 In the competitive market, a company with similar customer dissatisfaction could not increase
11 its prices and stay in business. Instead, if it wanted to stay in business, the competitive
12 company would first improve its product to an acceptable level, and only then would it try to
13 increase prices to recoup the costs.

14
15 Aloha, on the other hand, is trying to manipulate the regulatory process to turn this
16 competitive reality on its head. Aloha says first give us an increase in our prices, and only
17 then will we set about to improve our product to a level that our customers will find
18 acceptable.

19
20 I contend that Aloha should be held to the same standards that apply in a competitive market.
21 Just as it would in a competitive environment, Aloha should first be required to demonstrate
22 a product acceptable to customers, and then be considered for increased rates.

1 Q. DO YOU BELIEVE THE RATE CASE EXPENSE PROJECTED BY ALOHA IS
2 REASONABLE?

3 A. No. Aloha just completed a wastewater rate case which was filed in February, 2000. Had
4 Aloha consolidated that case with this one, it would have avoided virtually the entire amount
5 of rate case expense associated with this case. By filing a wastewater case and almost
6 immediately afterward filing a separate water case, Aloha has been extravagant to the point
7 of wastefulness. If Aloha were extravagant with its own money, I would not object. Aloha,
8 however, chooses to be extravagant with the customers' money.

9

10 Q. WHO IS HARMED BY ALOHA'S WASTEFULNESS ON RATE CASE EXPENSE?

11 A. Aloha is expecting its customers to pay for this wasteful approach. Because it expects the
12 customers to pay for the redundant rate case, Aloha does not seem to care about its extreme
13 inefficiency. I assure you that if rate cases were funded by the utility - rather than the
14 customers - Aloha would have found a more efficient way to proceed.

15

16 Q. IS IT TYPICAL FOR A WATER AND WASTEWATER UTILITY TO FILE SEPARATE
17 CASES FOR WATER AND WASTEWATER?

18 A. No. A utility generally files its water and wastewater cases together. This is because a
19 company's concern is with its overall financial health.

20

21 Aloha should have consolidated its water and wastewater needs into a single case. Because
22 it chose to file two separate cases, Aloha itself should be required to pay for the second one.

1 Q. DOES THAT COMPLETE YOUR TESTIMONY?

2 A. Yes, it does.

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CERTIFICATE OF SERVICE
DOCKET NO. 010503-WU

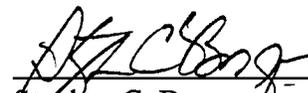
I HEREBY CERTIFY that a true and correct copy of the foregoing Direct Testimony of Hugh Larkin, Jr. has been furnished by hand-delivery(*) or U.S. Mail to the following parties on this 7th day of November, 2001:

Marshall Deterding, Esquire*
Rose Law Firm
2548 Blairstone Pines Drive
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Stephen C. Burgess
Deputy Public Counsel

