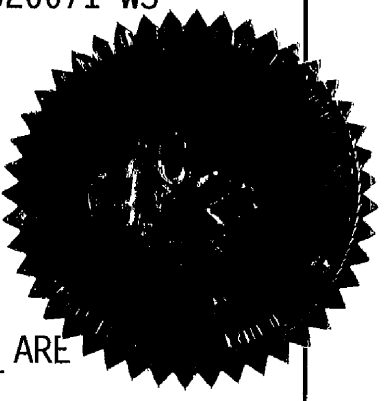
BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 020071-WS

In the Matter of

APPLICATION FOR RATE INCREASE IN MARION, ORANGE, PASCO, PINELLAS, AND SEMINOLE COUNTIES BY UTILITIES, INC. OF FLORIDA.
_____/



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VOLUME 5

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PROCEEDINGS:	HEARING
BEFORE:	COMMISSIONER J. TERRY DEASON COMMISSIONER BRAULIO L. BAEZ COMMISSIONER RUDOLPH "RUDY" BRADLEY
DATE:	Thursday, August 21, 2003
TIME:	Commenced at 9:30 a.m.
PLACE:	Betty Easley Conference Center Room 148 4075 Esplanade Way Tallahassee, Florida
REPORTED BY:	TRICIA DeMARTE, RPR Official FPSC Reporter (850) 413-6736
APPEARANCES:	(As heretofore noted.)

I N D E X

WITNESSES

I N D E X (Continued)

WITNESSES

EXHIBITS

NUMBER:		ID.	ADMTD.
16	MAC-1 and MAC-2	496	533
17	Late-Filed Deposition Exhibit No. 1	532	533
18	JAS-1	536	536
19	KLW-1 and KLW-2	611	637
20	Revised Stipulations 1, 4, and 9	641	641
21	RPR-1 through RPR-10	643	
22	PSC-96-1320-FOF-WS Order, Page 55	698	

PROCEEDINGS

(Transcript continues in sequence from Volume 4.)

COMMISSIONER DEASON: Call the hearing back to order. Mr. Burgess.

MR. BURGESS: Yes, I would call Mr. Cicchetti to the witness stand, please.

MARK A. CICCHETTI

was called as a witness on behalf of the Office of Public Counsel and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. BURGESS:

Q And my first question would be, have you been sworn in, Mr. Cicchetti?

A Yes, I have.

Q Thank you. Would you state your name and business address for the record, please.

A My name is Mark Cicchetti, and my business is 2931 Kerry Forest Parkway, Suite 202, Tallahassee, Florida 32309.

Q Mr. Cicchetti, have you prepared and submitted prefiled testimony in this docket, Docket Number 020071?

A Yes.

Q If the questions that are posed in your prefiled testimony were posed today, would your answers be the same?

A Yes.

Q Mr. Cicchetti, did you file an exhibit attached to your prefiled testimony as well?

A Yes.

MR. BURGESS: Commissioner, may we get an exhibit number for that, for Mr. Cicchetti's exhibit?

COMMISSIONER DEASON: Yes. It will be Exhibit 16.

MR. BURGESS: Thank you.

(Exhibit 16 marked for identification.)

MR. BURGESS: Commissioner, I would ask that Mr. Cicchetti's testimony be entered into the record as though read.

COMMISSIONER DEASON: Without objection, it shall be inserted in the record.

BEFORE THE PUBLIC SERVICE COMMISSION

TESTIMONY

OF

MARK A. CICCHETTI

Q. Please state your name and address and on whose behalf you are testifying in this proceeding.

A. My name is Mark Anthony Cicchetti and my business address is 2931 Kerry Forest Parkway, Suite 202, Tallahassee, Florida 32309. I am testifying on behalf of the Office of Public Counsel.

Q. By whom are you employed and in what capacity?

A. I am a Project Manager and Manager of the Tallahassee Office for C.H. Guernsey & Co. Guernsey is an engineering, architectural and consulting firm that has been in business for 75 years. The services Guernsey provides include: cost-of-service and rate studies; regulatory and litigation support; economic and financial studies; valuation studies; power supply planning, solicitation, and procurement; fuel purchasing; transmission and distribution planning and facilities design; strategic planning; telecommunications and e-business applications; architectural design for headquarters and warehouse facilities; environmental assessments; security systems, and; web site development and internet applications.

For ten years prior to joining C.H. Guernsey & Co., I was President of Cicchetti & Co., a financial research and consulting firm specializing in public utility finance, economics, and regulation. I also have been employed by the Florida State Board of Administration as Manager of Arbitrage Compliance and the Florida Public Service Commission as Chief of Finance. A detailed narrative description of my experience and qualifications is contained in Exhibit No. ____ (MAC - 1).

Q. Have you previously testified before this Commission?

A. Yes, I have testified before this Commission numerous times.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to address the leverage formula and the return on common equity the Commission should allow in this docket and to address the appropriate ratemaking treatment for the gains recognized by Utilities, Inc. of Florida on the sale of the Druid Isle water system and a portion of Oakland Shores water system and the Green Acres Campground water and wastewater systems.

The purpose of my rebuttal testimony is to rebut the testimonies of Hugh A. Gower and Steven M. Lubertozzi as they relate to gain on sale.

ALLOWED RETURN

Q. What is the leverage formula?

A. The leverage formula is a linear equation that, using a given set of assumptions, estimates changes in equity cost for given changes in financial leverage (i.e. the use of debt). The leverage formula has been in use in Florida since the late 1970's.

The theories underlying the leverage formula, as used in Florida, are based on the works of Modigliani and Miller (1958) and Miller (1977). According to Modigliani and Miller, the overall cost of capital remains constant despite changes in financial leverage. Therefore, the major premise underlying the leverage formula is that firms with different equity ratios will have different costs of equity even though they have the same business risk and the same overall cost of capital. This means that the increase in the required return on equity resulting from the use of leverage completely offsets the advantage of the increased use of lower cost debt. (See Modigliani and Miller, "The Cost of Capital, Corporation Finance and the Theory of

Investment," *American Economic Review*, June 1958, pp. 261-297 and Miller, "Debt and Taxes," *Journal of Finance*, May 1977, pp. 261-275.)

Q. Why is the leverage formula used to determine the allowed return on common equity for water and wastewater utilities in Florida?

A. There are over 200 certificated water and wastewater utilities under the jurisdiction of the Florida Public Service Commission ("FPSC"). Without a workable methodology such as the leverage formula, the costs and administrative burdens associated with cost of equity testimony, in potentially 200 rate cases, could become quite onerous. Additionally, many water and wastewater utilities are small operations that find it beneficial to avoid the costs associated with presenting cost of equity testimony. Consequently, applying a workable methodology such as the leverage formula lowers costs to all parties and serves the public interest.

Q. What are the assumptions underlying the leverage formula?

A. As stated in Public Service Commission Order No. PSC-02-0898-PAA-WS, the four basic assumptions are: 1.) Business risk is similar for all water and wastewater utilities; 2) The cost of equity is a function of the equity ratio; 3) The marginal weighted average cost of investor capital is constant over the equity range of 40% to 100%; and 4) The cost rate at an assumed Moody's bond rating of baa3 plus a 50 basis point private-placement premium and a 50 basis point small-utility premium represents the average marginal cost of debt to a Florida water and wastewater utility over an equity ratio range of 40% to 100%.

Q. Are these assumptions reasonable?

A. In general, yes. However, in this docket, the 50 basis point premium for small utilities should not be applied because Utilities, Inc. of Florida is one of the largest

water and wastewater utilities in Florida. The 50 basis point premium for small utilities was incorporated in Order No. PSC-01-2514-FOF-WS because two-thirds of Florida's water and wastewater utilities range from small to very small. Consequently, the premium for small utilities should not be applied to Utilities, Inc., one of the few large water and wastewater utilities in the state.

Q Please explain.

A. In Order No. PSC-02-0898-PAA-WS, the Commission allowed three adjustments to the leverage formula to compensate for risks associated with the small size of the typical Florida water and wastewater utility. The three adjustments increased the leverage formula cost of equity by 140 basis points. The three adjustments are: 1) A bond yield differential of 40 basis points to compensate for the fact that Florida water and wastewater utilities are smaller than the companies used in the indexes to calculate the cost of equity; 2) A private-placement premium of 50 basis points to recognize that investors require a premium for holding privately placed bonds that small firms issue as opposed to publicly issuing debt, and; 3) A small-utility risk premium of 50 basis points to recognize the financial stress, and hence risk, that small water and wastewater systems can experience. However, Utilities, Inc. of Florida is much larger than the average Florida water and wastewater utility.

Historically, Florida water and wastewater utilities have been characterized as small (Class C), medium (Class B), and large (Class A) based on revenues. Typically, small firms have under $200,000 in revenue, medium sized firms have between $200,000 and $1,000,000 in revenue and large firms have over $1,000,000 in revenue. As of 2000, only nine water or wastewater systems had revenues over

$1,000,000. As shown in the Company's 2001 annual Report, Utilities, Inc. of Florida had revenues of over $2,050,000, more than four times the median revenue of the 78 intermediate sized Florida water and wastewater firms and more than 35 times the median revenue of the 170 small Florida water and wastewater utilities cited in Order No. PSC-01-2514-FOF-WS.

Q. Was the fact that the adjusted leverage formula would be applied to large Florida firms as well as small Florida firms -- absent a protest by an interested party -- addressed at the hearing where the three adjustments for small size were proposed?

A. Yes. Commissioner Deason questioned staff witness Lester concerning such application. Page 235 line 15 through Page 237 line 2 of the hearing transcript, which follows, is the dialogue between Commissioner Deason and staff witness Lester:

> COMMISSIONER DEASON: I have a question concerning your adjustment for small companies.
>
> THE WITNESS: Yes, sir.
>
> COMMISSIONER DEASON: Fifty basis points. And I understand in your analysis you chose to compare bond yields for triple B and BB plus. I don't know what the terminology is.
>
> THE WITNESS: That's BB+.
>
> COMMISSIONER DEASON: BB+ and BBB. And you came out with an average of 83 basis points and then a range. And then you tempered that calculation somewhat, and correct me if I'm wrong, but I think you tempered that calculation somewhat for the fact that we really shouldn't consider regulated utility companies as speculative

grade, and so you chose 50 basis points –

THE WITNESS: That's correct.

COMMISSIONER DEASON: –as some type of quantification of the risk factor of a small company; correct?

THE WITNESS: That's correct, yes, sir.

COMMISSIONER DEASON: Okay. First of all, let me ask you this. Do you consider all of the companies that we regulate in Florida to be small companies?

THE WITNESS: No. I consider the average to be.

COMMISSIONER DEASON: The average to be.

THE WITNESS: Yeah.

COMMISSIONER DEASON: Okay. But any company in Florida can come in and choose the leverage formula, and if that is not protested by Public Counsel or someone else, then that's what's used regardless of the size of that company; correct?

THE WITNESS: Yes, sir.

COMMISSIONER DEASON: But since the statute uses the term "average," you think it's appropriate then to allow any company to come in and choose that if they think it's appropriate.

THE WITNESS: Yes, sir. I based my analysis on the statutory language, which I think is an average water and wastewater utility.

Q. What rate of return on common equity should be allowed in this docket?

A. Because Utilities, Inc. of Florida is significantly larger than the average water and wastewater utility in Florida, I recommend the Commission apply the leverage

formula without the third adjustment of 50 basis points for small size. Two adjustments for small size will remain, the 40 basis point bond-yield-differential adjustment to recognize the difference in size between the companies in the indexes used to calculate the cost of equity and Utilities, Inc. of Florida and the 50 basis point private-placement premium to recognize that investors require a liquidity premium to hold privately placed debt. It should be noted, the adjustments for small size are in addition to the recovery of the actual cost of debt. Although many Florida water and wastewater utilities are small, they are still regulated entities and have lower risk than similar non-regulated entities. It is not reasonable to assume, for the purposes of the leverage formula, that a well-managed, prudently-operated Florida water or wastewater utility would not meet the financial criteria necessary for an investment grade rating. Furthermore, bonds below investment grade are characterized, at best, as "uncertain as to position" by Moody's. The ability of Utilities, Inc. of Florida to pay its debts should not be considered "uncertain." It is reasonable to assume the average marginal cost of debt to Utilities, Inc. of Florida WAW is equal to Moody's bond rating of baa3 plus 50 basis points as a private-placement premium. A bond rating below baa3 is not investment grade. The additional third adjustment for size of 50 basis points for financial stress for small size is based on a bond yield below baa3.

In defining its baa rating, Moody's states, "Such bonds lack outstanding investment characteristics and in fact have speculative characteristics as well." It would be unreasonable to assume that the debt of a Florida-regulated water or wastewater utility is below that described by Moody's baa rating and therefore below investment grade. Furthermore, it would be unreasonable to assume it is uncertain that a

prudently operated Florida water or wastewater utility can pay its debts, particularly one of the largest water and wastewater utilities in Florida. Consequently, the allowed return on common equity in this docket should be 10.41% as opposed to 10.91%. The derivation of the leverage formula to arrive at the 10.41% is shown on Exhibit No. ____(MAC-2). A return of 10.41% will allow Utilities, Inc. of Florida to maintain its' financial integrity and attract capital.

GAIN ON SALE

Q. What gains did Utilities, Inc. of Florida recognize on the sale of its Druid Isle water system, the sale of a portion of its Oakland Shores water system and the sale of its Green Acres Campground water and wastewater systems?

A. Utilities, Inc. of Florida recognized a gain on sale of $61,699 for its Druid Isle water system and the portion of its Oakland Shores water system and a gain on sale of $269,661 for its Green Acres Campground water and wastewater systems.

Q. What is the appropriate ratemaking treatment of the gains on sale of these water and wastewater systems?

A. The appropriate ratemaking treatment of the gains on sale of the water and wastewater systems sold by Utilities, Inc. of Florida is to attribute the gains to ratepayers. Cost of service regulation as it is practiced in Florida, as well as most of the rest of the country, is a balancing of the interests of shareholders (i.e., the owners) and ratepayers and is based on the premise that shareholders are given the opportunity to recover their costs, including a fair return on their investment, and that ratepayers pay the reasonable and prudent costs associated with the provision of utility service.

Q. How does appropriate application of cost-of-service regulation achieve the goal

of balancing the interests of shareholders and ratepayers?

A. Cost-of-service regulation evolved as a way to deal with the natural monopoly characteristics associated with the provision of utility service. To understand how cost-of-service regulation benefits society one must understand market structure and its effect on a firm's return on common equity. Market structure is the range of conditions (such as the number of firms, the economies of scale or scope, the type of product sold, and the demand for a product) that affects a firm's behavior and performance. Market structure is best thought of as a continuum stretching between purely competitive markets and natural monopoly. Purely competitive markets are characterized by minimal economies of scale or scope - - that is, no single supplier has a natural cost advantage over other suppliers. In the short run, a firm can earn economic profits, (that is a return above its cost of capital) only if it is efficient or innovative. In the long run, a firm cannot earn above its cost of capital due to the ease of entry into, and exit from, the market. If a firm in an effectively competitive environment is earning above its cost of equity, new firms will try to share those profits.

Another way to look at it is to recall that in economics, long-term is defined as the period of time necessary to change production processes. In the long-term, in an effectively competitive environment, a firm's competitors will match its efficiency by changing their production processes.

Natural monopoly markets, by contrast, are marked by substantial economies of scale or scope and decreasing average costs. This means one supplier can always serve the market at lower unit cost than two or more suppliers. Entry barriers are severe because the single most efficient provider will always be able to price below

any potential entrant. Left unregulated, a natural monopoly market will not produce competitive results. Assuming an industry is a natural monopoly (as are the water and wastewater industries), cost of service regulation benefits society by increasing output while reducing price and economic profits. Regulators achieve this by backing away from the objectives of allocative efficiency and marginal cost pricing, and establishing a "fair-return" price. The "fair-return" price includes the reasonable and prudent costs associated with the provision of utility service including a fair return on invested capital. Although this does not produce a socially optimum price and output, it is an improvement over an unregulated natural monopoly.

Because utilities must meet the peak demand for their products or services, they generally have significant excess capacity during periods of normal demand. This requires a high level of facilities investment, which means that the unit cost of production likely will decrease over a wide range of output. The result is a socially optimum price that is below average cost. Pricing here would likely result in bankruptcy. Therefore again, regulators set a "fair return" price that allows a utility to recover the reasonable and prudent costs associated with providing utility service, including an appropriate return on common equity.

Q. What are the implications, under cost-of-service regulation, if the gains associated with the sale of utility plant are not attributed to ratepayers?

A. Cost-of-service regulation contemplates ratepayers paying the net cost of providing utility service including a fair return on capital. All other things being equal, if the gain on sale of property is not attributed to ratepayers then the utility will be allowed to recover more then the cost of providing service. This is equivalent to consciously allowing a utility a return on common equity above the

required return. Through depreciation, a utility realizes a return *of* capital and through a fair allowed rate of return a utility earns a return *on* capital. Shareholders are rewarded for the risks they take through the allowed return on common equity. The return is not guaranteed which provides an incentive for the firm to be efficient. The allowed return on common equity includes a premium to recognize the risks associated with providing utility service. To contend, all other things being equal, that a utility deserves to be allowed to recover more than the net cost of providing service plus a fair return on common equity is inconsistent with cost-of-service principles.

Furthermore, it is unfair to ratepayers to allocate gains on the sale of regulated assets to shareholders when it is generally accepted that ratepayers should incur the cost of reasonably incurred losses on sales of regulated assets.

Q. When are ratepayers required to incur the cost of losses on sales of utility assets under cost-of-service regulation?

A. In recent years, when electric utilities were required to divest generation or transmission assets under "deregulation" it was generally accepted that ratepayers should bear any stranded costs (loss of value as compared to original cost) associated with the sale of regulated assets. The basic idea was that the utilities had made the investment to provide service under a regulatory compact, i.e. cost-of-service regulation, and that it was only fair that the ratepayers, not the new customers, bear the stranded costs. In fact, to the best of my knowledge, in all states where it was contemplated there would be stranded costs under a plan of deregulation, whether actually implemented or just proposed, stranded costs were to be recovered from ratepayers. Consequently, under cost-of-service principles, the knife should cut both

ways. Gains on sale and reasonable, prudently incurred losses on sale of utility assets (such as through forced divestiture) should be treated above the line for ratemaking purposes. Such treatment is consistent with sound cost-of-service regulation.

Q. Please summarize your direct testimony.

A Regarding the leverage formula and an appropriate allowed return, in Order No. PSC-02-0898-PAA-WS, the Commission allowed three adjustments to the leverage formula to compensate for risks associated with the small size of the typical Florida water and wastewater utility. The three adjustments increased the leverage formula cost of equity by 140 basis points. The three adjustments are: 1) A bond-yield differential of 40 basis points to compensate for the fact that Florida water and wastewater utilities are smaller than the companies in the indexes used to calculate the cost of equity; 2) A private-placement premium of 50 basis points to recognize that investors require a premium for holding privately placed bonds that small firms issue as opposed to publicly issuing debt, and; 3) A small-utility risk premium of 50 basis points to recognize the financial stress, and hence risk, that small water and wastewater systems can experience. However, Utilities, Inc. of Florida is much larger than the average Florida water and wastewater utility. Because Utilities, Inc. of Florida is significantly larger than the average water and wastewater utility in Florida, I recommend the Commission apply the leverage formula without the third adjustment of 50 basis points for small size. Two adjustments for small size will remain, the 40 basis point bond-yield differential adjustment to recognize the difference in size between the companies in the indexes used to calculate the cost of equity and Utilities, Inc. of Florida and the 50 basis point private-placement

premium to recognize that investors require a liquidity premium to hold privately placed debt. It should be noted, the adjustments for small size are in addition to the recovery of the actual cost of debt.

Regarding gains on sale, cost-of-service regulation contemplates that ratepayers pay the net cost of providing utility service including a fair return on capital. All other things being equal, if the gain on sale of property is not attributed to ratepayers than the utility will have been allowed to recover more than the cost of providing service. This would be equivalent to consciously allowing a utility a return on common equity above the required return. Through depreciation, a utility realizes a return *of* capital and through a fair allowed rate of return a utility earns a return *on* capital. Shareholders are rewarded for the risks they take through the allowed return on common equity. The return is not guaranteed which provides an incentive for the firm to be efficient. The allowed return on common equity includes a premium to recognize the risks associated with providing utility service. To contend, all other things being equal, that a utility deserves to be allowed to recover above the net cost of providing service plus a fair return on common equity is inconsistent with cost-of-service principles.

REBUTTAL OF GOWER

Q. On page 4 line 2 Mr. Gower states "Neither gains nor losses on sales of utility systems should be included in cost of service used for rate setting purposes." Do you agree?

A. No. Ratepayers should pay only the net cost of service under cost-of-service regulation. Furthermore, it is generally accepted that utilities that incur stranded costs when forced to sell assets should be kept whole through the ratemaking

process.

Q. On page 12 line 7, Mr. Gower states, "It is the investors whose capital is exposed to the risks of ownership and to whom gains or losses--including those from property sales--should accrue." Do you agree?

A. No. As stated above, ratepayers should only bear the net cost-of-service under cost of service regulation and it is generally accepted that utilities should be allowed to recover stranded costs, i.e. losses, when reasonably incurred. Furthermore, owners are compensated for the risks associated with the provision of utility service through the allowed return on common equity which includes a premium specifically for taking on the risks of ownership. Regarding gains on sale of property under cost-of-service regulation, ownership is not a relevant consideration. What is relevant is determination of the appropriate costs to be borne by ratepayers. For example, salvage value is netted against original cost to determine the amount of capital plant and equipment that is to be recovered through depreciation. I have never heard anyone argue that because shareholders are the owners of the plant and equipment used to provide utility service, salvage value should not be used to reduce the net cost of depreciation to ratepayers but instead should accrue to the owners. Likewise, gains on the sale of regulated property should be netted against the cost of service and accrue to the benefit of ratepayers.

Q. On page 14, line 11 Mr. Gower states, "Failure to assign to investors gains or losses on sales of this type is not only confiscatory, unfair and improper, but also has adverse implications to the utilities ability to raise capital at reasonable costs." Do you agree?

A. No. It is hard to see how *not* assigning losses to investors is confiscatory to

investors and would have adverse implications to raising capital at a reasonable cost. Second, allowing a fair return on common equity, by definition, meets the capital attraction standard for raising capital at a fair price. All other things being equal, allowing gains on sales to be attributed 100% to shareholders allows shareholders to earn more than a fair return--directly the opposite of hampering the utility's ability to attract capital at a reasonable cost.

REBUTTAL OF LUBERTOZZI

Q. On the fourth page, line 29 of Mr. Lubertozzi's direct testimony, he states, "since the investors provide the capital and bear the risks, they are entitled to receive the return. Gains and losses on the sale of utility property are properly assigned to the owners of the facilities, just as in any other business enterprise. Utility investments are not risk free and may bear additional risks beyond the normal, predictable risks borne by other business enterprises." Do you agree?

A. No. As outlined in my rebuttal testimony to Mr. Gower's direct testimony, under cost-of-service regulation, ownership is not a relevant consideration. What is relevant is determination of the appropriate costs to be borne by ratepayers. Furthermore, regulated utilities are not the same as any other business enterprise due to the natural monopoly nature of the utility business and the potential for undue discrimination as outlined in my direct testimony. As shown on page nine of the February 7, 2002, staff recommendation in Docket No. 991890-WS, of the eight states that responded to the staff's survey that had an established policy or practice concerning gains on sale, only one had an established policy or practice of allocating 100% of the gain to shareholders. Six had the established policy or practice of allocating 100% of the gain to ratepayers. Investors in utility stocks are compensated

for the risks incurred through the allowed return on common equity. Finally, it is generally accepted that regulated utilities are less risky than non-regulated companies. For example, rating agencies have recognized this fact in their publications and their financial benchmark criteria.

Q. Please summarize your rebuttal testimony.

A. Both Mr. Gower and Mr. Lubertozzi claim that because investors bear the risks associated with investment in utility assets, the utility should receive the gains on sale of utility property. However, investors are compensated for the risks they bear through the fair return allowed on common equity capital. Furthermore, under cost-of-service regulation, ownership is not a relevant consideration. What is relevant is determination of the appropriate costs to be borne by ratepayers. For example, salvage value is netted against original cost to determine the amount of capital plant and equipment that is to be recovered through depreciation. I have never heard anyone argue that because shareholders are the owners of the plant and equipment used to provide utility service, salvage value should not be used to reduce the net cost of depreciation to ratepayers but instead should accrue to the owners. Likewise, gains on the sale of regulated property should be netted against the cost of service and accrue to the benefit of ratepayers.

Finally, Mr. Gower states, "Failure to assign to investors gains or losses on sales of this type is not only confiscatory, unfair and improper, but also has adverse implications to the utilities ability to raise capital at reasonable costs." However, it is hard to see how *not* assigning losses to investors is confiscatory to investors and would have adverse implications to raising capital at a reasonable cost. Second, allowing a fair return on common equity, by definition, meets the capital attraction

standard for raising capital at a fair price. All other things being equal, allowing gains on sales to be attributed 100% to shareholders allows shareholders to earn more than a fair return--directly the opposite of hampering the utility's ability to attract capital at a reasonable cost.

Q. Does this conclude your testimony?

A. Yes.

BY MR. BURGESS:

Q Mr. Cicchetti, would you provide the Commission with a summary of your testimony, please.

A Yes. Good morning, Commissioners. The purpose of my direct testimony is to address the return on common equity the Commission should allow in this docket and to address the appropriate ratemaking treatment for the gains recognized by Utilities, Inc. of Florida on the sale of the Druid Isle water system, a portion of the Oakland Shores water system, and the Green Acres Campground water and wastewater system.

The company has requested the return on common equity in this docket be set using the leverage formula. Standard application of the leverage formula incorporates three adjustments to compensate for the small size of the average water and wastewater utility in Florida. The adjustments for small size include a 44 basis point adjustment to make the cost of debt equal to the lowest investment grade, a 50 basis point private-placement premium and a 50 basis point small-utility premium which was incorporated in 2001.

In this docket the 50 basis point premium for small size should not be applied because Utilities, Inc. of Florida is one of the largest water and wastewater utilities in Florida. The 50 basis point premium for small utilities was incorporated in 2001 because two-thirds of Florida's water and wastewater utilities range from small to very small.

Utilities, Inc. of Florida is very large relative to the average Florida water and wastewater utility, and consequently, the premium for small size should not be applied. Two adjustments of almost a full percentage point for small size will remain.

Regarding the gains on sale of the water and wastewater system sold by Utilities, Inc. of Florida, the appropriate treatment is to attribute the gains to ratepayers. Cost-of-service regulation contemplates ratepayers paying the net cost of providing utility service, including a fair return on capital. All other things being equal, if the gain on sale of property is not attributed to ratepayers, then the utility will be allowed to recover more than the cost of providing service.

Through depreciation a utility realizes a return of capital, and through a fair allowed rate of return a utility earns a return on capital. All other things being equal, a utility recovering more than the net cost of providing service plus a fair return on common equity is inconsistent with cost-of-service principles.

Finally, it is unfair to ratepayers to allocate the gains on the sale of regulated assets to shareholders when it is generally accepted that ratepayers should incur the cost of reasonably incurred losses on sales of regulated assets. For example, in recent years when electric utilities were required

to divest generation and transmission assets under deregulation, it was generally accepted that ratepayers should bear any stranded costs; that is, loss of value compared to original costs. The basic idea was that the utilities had made an investment to provide service under a regulatory compact, that is, cost-of-service regulation, and that it was only fair that the ratepayers, not the new customers, bear the stranded costs.

Consequently, under cost-of-service principles, the knife should cut both ways. Gains on sale as well as reasonable, prudently incurred losses on the sale of utility assets should be treated above the line for regulatory purposes.

Regarding the rebuttal portion of my testimony, both Mr. Gower and Mr. Lubertozzi claim that because investors bear the risks associated with the investment in utility assets, the utility should receive the gains on the sale of utility property. However, investors are compensated for the risks their bear through the fair return allowed on common equity capital.

Additionally, Mr. Gower, regarding gains or losses on sales, states, "Failure to assign to investors gains or losses on sales of this type is not only confiscatory, unfair and improper, but also has adverse implications to the utilities ability to raise capital at reasonable costs." However, it is

hard to see how not assigning losses to investors is confiscatory to investors and would have adverse implications to raising capital at a reasonable cost.

Allowing a fair return on common equity by definition beats the capital attraction standards for raising capital at a fair price. All other things being equal, allowing gains on sales to be attributed 100 percent to shareholders allows shareholders to earn more than a fair return, directly the opposite of hampering the utilities ability to attract capital at a reasonable cost. That concludes my summary.

MR. BURGESS: Thank you, Mr. Cicchetti. We tender the witness.

COMMISSIONER DEASON: Mr. Friedman.

MR. FRIEDMAN: Thank you.

CROSS EXAMINATION

BY MR. FRIEDMAN:

Q Mr. Cicchetti, in preparing your opinions, did you review prior Public Service Commission orders involving Class A utilities as it relates to the cost of equity?

A In general I did, yes.

Q Was the leverage graph -- leverage formula used in those rate proceedings at least since it's been adopted?

A Are you asking me if the leverage formula has been used in all rate cases for Class A utilities since it's been adopted?

Q Yes, based on what you reviewed in preparation for this hearing.

A I didn't -- I thought you were referring to orders with regard to gain on sale. I didn't know you were referring to orders regarding the leverage formula.

Q I'm sorry. I apologize. I was starting at the beginning of your testimony instead of at the end.

In preparation of your testimony on the return on equity, did you review prior orders of the Commission for Class A utilities and how the Commission previously addressed the return on equity issue?

A No, I did not.

Q You didn't think that was relevant to see what the Commission had done in the past?

A No, I did not.

Q So you don't know whether the theory that you espouse here has been espoused in any prior PSC proceeding?

A Which theory are you referring to?

Q I'm talking about your eliminating the 50 basis points.

A That's not a theory. That's just my recommendation in this particular case.

Q So you didn't -- in preparing that recommendation, you didn't think it was important to see if the Commission had ever utilized or accepted that type of recommendation before?

A No, I didn't. I'm not a kind of person that thinks if something was done wrong in the past should continue to do it. I'm someone that thinks we should do what the right thing is regardless of what was done in the past. But I'm not aware that the Commission has ever addressed this issue with regard to the third adjustment for small size that was incorporated in 2001.

Q So you don't know whether the Commission has ever deviated from the use of the leverage formula for Class A utilities?

A Off the top of my head, I don't know that it's always been used. I think it's used in the majority -- by far the majority of cases, but what was allowed in the past is not particularly relevant to me. It's what the cost of equity is and addressing that issue in this docket that's relevant for this docket.

Q With all due respect, I ask you the questions because I think they're relevant.

A Well, I'm giving you my answer, and I don't think it's relevant.

Q On Page 4, Line 1, you state that the 50 basis points was added because two-thirds of the water and wastewater utilities are small to very small; is that correct?

A Yes.

Q All right. And what facts do you base that upon?

What database did you have to base that upon?

A In the hearing in 2001 that was one of the issues that was brought forward, as well as for that particular adjustment in Mr. Lester's testimony, he mentioned that most or many of the water utilities in Florida were small or very small that had revenues below $1 million, and that's not the case in this docket or for Utilities, Inc. of Florida.

Q It's not your opinion, is it, that the leverage formula was not intended when it was adopted to apply to all utilities, including Class As, is it?

A The way you structured the question I think -- it gives me a little bit of a problem. The leverage formula is out there for water utilities, water and wastewater utilities to avail themselves of if they want to; they don't have to. And any party that thinks that that's not an appropriate return for a particular company can petition the Commission to address that issue.

Q Where do you get that last opinion you just gave, that if you don't like the leverage formula, any party can challenge it and ask -- where do you get that factual opinion?

A That's my understanding of how the Commission operates.

Q From whom or what?

A Based on my experience. I don't know that any interested party could not petition the Commission about any

aspect of a rate increase.

Q So you're not directing to a particular rule or statute that says you can do that?

A Well, the Commission's rule on the leverage formula states that it can be used. It doesn't say that it must be used.

Q But it doesn't say whose decision it is to suggest it be used.

A Well, just based on my experience, the Commission will decide what issues are to be allowed in a case. And I don't have any belief that an interested party wouldn't be given an opportunity to make that case before the Commission for them to decide.

Q Are you familiar with the statute that authorizes the Commission to establish the leverage formula?

A Yes.

Q Do you know whether that statute allows a party other than the utility to chose to use something other than the leverage formula? If you don't know, say so.

A Well, it's -- I know what the statute says or what the rule says with regard to the leverage formula. I don't know that that's all encompassing with regard to who may petition the Commission or not.

Q So you don't know whether that statute that authorizes the Commission to set that says that only a utility

or not?

A It's -- having read it many times, it's my understanding that that does not preclude an interested party from petitioning the Commission. That's obviously a legal issue, but as someone that's dealt with it for over 20 years, it's -- I have no knowledge that no one can challenge a utility's use of the leverage formula. That's just not my understanding of how it works. But for a legal opinion, you'd have to ask a lawyer.

Q Isn't it true that the leverage formula when it's adopted each year is intended to apply to all water and wastewater utilities in Florida notwithstanding they're Class A or otherwise?

A Well, I have a problem with your use of the word "apply." It's out there for companies to avail themselves of if they would like to, but it's not required that they do, and it's not a requirement that the Commission use only that number that's derived from the leverage formula as the allowed return on equity.

Q So it's your opinion then that the Commission cannot adopt that leverage formula every year and automatically apply it to every water and sewer utility throughout the industry?

A Oh, they could if they wanted to, but it's my understanding that they don't have to, and that a utility doesn't have to use it, and that a party can petition the

Commission to use something other -- an interested party can petition the Commission to use something other than that.

Q And that leverage formula doesn't differentiate between Class A or other utilities?

A No, it doesn't.

Q So as it's adopted, it's intended to apply to Class A utilities, is it not?

A It's intended to apply to the average utility is what the wording in the rule in the statute says, I believe.

Q So you're saying it doesn't apply -- that leverage formula does not apply to Class A utilities?

A I didn't say that.

Q Well, I'm --

A I'm just saying, the leverage formula is adopted annually by the Commission, and a utility can choose to use that in its filing for a rate case if it choses to do so.

Q Including Class A utilities.

A That's correct.

Q So when the rule is adopted, it was intended to apply to Class A utilities, was it not?

A It's intended to apply to any utility -- water or wastewater utility that wants to avail itself of it.

Q That was a really simple answer. I just asked you, is it applicable to Class A utilities?

MR. BURGESS: Commissioner, that question has been

asked and answered several times at this point. I don't mind the witness answering again; I just don't know how many times we're going to run through this same circle.

MR. FRIEDMAN: He doesn't answer the question. He goes into a discourse instead of saying yes. That's a very simple -- easy answer. All he had to say, does it apply to Class As, yes, and he goes into some discourse about it applying to everybody in the industry. I mean, all I'm asking is simple questions.

COMMISSIONER DEASON: And I'll instruct the witness, to the extent possible, answer "yes" or "no," and then you may elaborate.

THE WITNESS: Yes, it can apply to Class A utilities, but there's nothing in the order or in the rule or in the statute that, to my knowledge, specifically says this applies to Class A utilities. I'm just trying to make it clear that it applies to whatever water and wastewater utility would like to avail itself of it. I'm not trying to be argumentative.

BY MR. FRIEDMAN:

Q The Commission has rules, does it not, that does differentiate between Class A and other classes of utilities?

A Yes.

Q So wouldn't you assume then that if this leverage graph were intended to apply or not apply to Class As, that it would have said so?

A Certainly. And I guess you're just making my point. It doesn't specifically say. I'm just saying it applies to everyone, not just Class A utilities. I'm just trying to be as informative as I can.

Q You testified also that the 50 basis point premium should be applied in this case because of the large size of Utilities, Inc.; is that correct?

A I'm saying it should not be applied based on the large size relative to the arguments that I heard during the hearing that adopted that and the subsequent discussions of that.

Q And you participated in those hearings, did you not?

A Yes.

Q And isn't it true that the opinion that you sought to have adopted was that the 50 basis point risk premium was unnecessary for all water and wastewater utilities and not just the Class As?

A Yes.

Q And that was not adopted by the Commission, was it?

A No. They adopted the 50 basis point third adjustment for small size.

Q Is my understanding of your testimony -- I'm moving on to gain on sale. Is my understanding correct that it's your opinion that by virtue of paying rates, that the customer obtains some proprietary interest in the utility assets?

A Absolutely not.

Q Wouldn't you agree that the sale of a utility's assets is not the provision of a utility service?

A That's not an operating concept. My position has to do with, for lack of a better term, keeping the pot whole and balancing the interests of ratepayers and shareholders, and not every decision is an operating decision that affects rates.

Q On Page 11, Line 10, you state that it is, quote, generally accepted, end quote, that ratepayers incur the loss on sales of regulatory assets. Do you recall that?

A Yes.

Q And what's the factual basis of that opinion?

A Looking at deregulation across the country, in every state that I'm aware of that contemplated that where they addressed how stranded costs or stranded gains would be treated, it was always that ratepayers would bear those costs.

Q And you think that the theory regarding deregulation ought to be equally applicable to a sale of a water and wastewater system in Florida?

A Yes.

Q And the sales of these UIF systems is not the result of deregulation, is it?

A That's correct.

Q You state that -- or make the argument that customers are entitled to return on gain on sales because the

shareholders earn a return on capital through depreciation and return on capital through the rate of return; correct?

A Yes.

Q And can you explain to me why you think the customers should be entitled to the appreciation on any asset --

A I think the basic concept behind cost-of-service regulation is a balancing of the interests of shareholders and ratepayers, and that's accomplished through having ratepayers bear the net costs of utility service, including an appropriate return. I think it's well established that through the regulatory compact, stranded costs, which are assets that are going to be sold by the regulated utility that were devoted to regulated service, if there's a loss associated with those, that the customers should bear that. I think that's fair and reasonable. And I think the knife should cut both ways, that the company would be whole, would remain whole if the net cost is associated with the sale of assets is what the ratepayer bears and any gains go towards the ratepayers.

I think Commissioner Deason mentioned a little earlier a decision where one Commission considered that to be recovery of depreciation, that the ratepayers would have paid more depreciation. I think that's the general concept behind the ratepayers pay the net cost. And so as long as that's done, I think the company remains whole, each side is treated fairly, there's a balancing of the interests, and that's the

way it should be treated.

I believe at deposition Mr. Gower thought that if there was a loss through stranded assets, that the customers should pay that and that the shareholders should receive any gain. I just don't think that's an appropriate balancing of the interest. I think that's ratepayers not getting a fair shake, and I think cost-of-service principles are based on a balancing of the interest.

Q And you think the cost of service includes the appreciation on an asset that the utility owned and you admitted did not have a proprietary interest in and sold?

A I think the principles behind cost-of-service regulation incorporate that, and that's based on keeping the utility whole with regard to what is done to provide utility service. Another example I think is the salvage value associated with plant equipment. At some point if a utility recovers salvage value, no one generally, not that I'm aware of, makes the argument that the shareholder is the owner of that, and therefore, it shouldn't be netted against the cost of the asset. And I think the same thing applies as directly analogous to a gain on sale of assets devoted to regulatory service, that if there's a loss, the ratepayers should bear it as long as it's reasonably and prudently incurred, and if there is a gain, it should be netted against the cost.

Q So you agree with Ms. Dismukes that the abandonment

loss is analogous to a sale of a system?

A I think generally speaking, yes, it is.

Q On Page 15 of your testimony, you discuss the results of the staff survey that we spoke of, I guess, when you were here when Ms. Dismukes was testifying. And you state that gain on sale, that six of seven states have an established policy to give the gain on sale to the ratepayer.

A Partial -- completely or at least partially.

Q And that conclusion doesn't address the jurisdictions that only dealt with water and wastewater systems, does it?

A That's correct. But my experience has been the water and wastewater industry is more of a follower than a leader with regard to a lot of ideas. And it's interesting to see around the country how this issue is treated, and it's treated differently in different industries as well as between different states. And so that's why I think it helps to look at it from the entire context, the basic premise of cost-of-service regulation and balancing the interests between ratepayers and shareholders.

Q But at least thus far, doesn't it appear as if the jurisdiction is not just Florida but the jurisdictions throughout the United States at this point treat water and wastewater system sales differently than they do electric and gas and telephone, at least based on that survey that was attached?

A Well, as I said, there's differences. I mean, some are treated one way, some are treated the other way between industries and between states and that's shown in this survey.

Q But without me going through what I went through with Ms. Dismukes, don't you agree that there are only two jurisdictions that have issued orders dealing with water and wastewater passing the gain on sale on water and wastewater cases to either party?

A Based on that survey?

Q Right.

A Yes.

MR. FRIEDMAN: I have no further questions.

COMMISSIONER DEASON: Staff.

MS. GERVASI: Thank you.

CROSS EXAMINATION

BY MS. GERVASI:

Q Mr. Cicchetti, would you please take a look at Page 3 of your testimony, referring to Lines 5 through 12.

A Okay.

Q Are you indicating here that it would be burdensome for water and wastewater utilities to file cost of equity testimony in rate cases?

A What I'm indicating is it would be burdensome to the Commission to have to hear that many cases, and that the leverage formula is a way of treating everyone fairly and

avoiding that.

Q Do you agree also that it's burdensome for the companies -- for the water and wastewater companies because of the fact that they tend to be small?

A Generally speaking, yes.

Q Isn't it true that reduced rate case expense is one of the benefits for utilities and parties using the leverage formula?

A Yes.

Q Would you please turn to Page 8 of your testimony at Line 3.

A Okay.

Q You're recommending 10.41 percent as the appropriate cost rate for common equity; right?

A Yes.

Q And in your Exhibit MAC-2 attached to your testimony?

A Yes -- well, MAC-2 was just a refiguring of the leverage formula without the 50 basis points. You'd have to apply the company's equity ratio to get the recommended ROE.

Q What is the equity ratio that you applied?

A Whatever it was in the filing, staff's position on that issue. I think it was approximately 46 percent.

Q Was it 46.11 percent, subject to check? Does that sound right?

A That sounds right.

MS. GERVASI: We have passed out an exhibit that I'd like to have marked for identification, please.

COMMISSIONER DEASON: Exhibit 17.

MS. GERVASI: Thank you. And we'll label this, "Late-Filed Deposition Exhibit MAC-1."

(Exhibit 17 marked for identification.)

BY MS. GERVASI:

Q Mr. Cicchetti, do you recognize this exhibit?

A Yes.

Q Does it appear to be a true and correct copy of your Late-Filed Deposition Exhibit MAC-1?

A Yes.

Q And this represents the current leverage formula with your adjustment removing the small utility risk premium; is that correct?

A Yes.

Q With your adjustment and the current leverage formula, do you recommend that the appropriate cost rate for common equity is 10.94 percent?

A I'll accept that, subject to check.

Q Okay. Is your position that with your recommended adjustment to remove the small utility risk premium, the Commission should use the current leverage formula for this case?

A Yes. You said with the removal of the 50 basis point

adjustment?

Q Correct.

A Yes.

MS. GERVASI: Thank you. That's all.

COMMISSIONER DEASON: Redirect.

MR. BURGESS: No, sir.

COMMISSIONER DEASON: Exhibits.

MR. BURGESS: I would ask that Exhibit 16 be moved into --

COMMISSIONER DEASON: Without objection, show that Exhibit 16 is admitted.

(Exhibit 16 admitted into the record.)

MS. GERVASI: And we move Exhibit 17.

COMMISSIONER DEASON: Without objection, show that Exhibit 17 is admitted.

(Exhibit 17 admitted into the record.)

COMMISSIONER DEASON: Thank you, Mr. Cicchetti.

THE WITNESS: Thank you, Commissioners.

(Witness excused.)

COMMISSIONER DEASON: I believe we have a number of witnesses that it has previously been indicated may be stipulated into the record. I would propose that we go through that process at this time.

MS. GERVASI: Yes. Thank you, sir. We have the testimony of seven DEP witnesses that I would like to have

inserted into the record at this time beginning with the testimony of James H. Berghorn consisting of four pages.

COMMISSIONER DEASON: Show that testimony inserted into the record.

Help me. If any of these -- if there's exhibits for any of this, let me --

MS. GERVASI: There are no exhibits for the seven DEP witnesses.

COMMISSIONER DEASON: Very well.

MS. GERVASI: Next is the testimony of Peter H. Burghardt consisting of three pages.

COMMISSIONER DEASON: Show that testimony inserted in the record.

MS. GERVASI: And then Kimberly M. Dodson which consists of six pages. We do have one correction that we would like to read in to her testimony which the parties have no objection to. And that starts at -- it's at Page 5 of her testimony beginning on Line 17. The question is asked, "Is the overall maintenance of the treatment plant and distribution facilities satisfactory?"

And we'd like to replace her prefiled answer which starts on Line 19 of Page 5 and runs through Line 13 of Page 6 with the following language: "Yes, for the Seminole County systems of Bear Lake, Crystal Lake, Jansen, Oakland Shores, Park Ridge, Phillips, Weathersfield, and Little Wekiva.

For the Ravenna Park system, the interior of the aerator was found to be in poor condition. Paint is peeling, and much of the metal structure is heavily corroded. The utility has indicated that the aerator will be replaced with a fiberglass unit with work set to begin on or about September 1, 2003. Correspondence from the utility indicates that the contractor has begun the necessary custom prefabrication steps and that the work is expected to be complete by September 26, 2003."

And that completes the correction.

COMMISSIONER DEASON: Okay. Show that testimony inserted as corrected.

MS. GERVASI: Thank you. Next is Paul J. Morrison consisting of seven pages.

COMMISSIONER DEASON: Show that testimony inserted in the record.

MS. GERVASI: Gary P. Miller, two pages.

COMMISSIONER DEASON: Show that testimony inserted in the record.

MS. GERVASI: William V. Ryland, four pages.

COMMISSIONER DEASON: Show that testimony inserted in the record.

MS. GERVASI: And Pepe Menendez, three pages.

COMMISSIONER DEASON: Show that testimony inserted in the record.

MS. GERVASI: Thank you.

Next, we would call Ms. Kathy Welch to the stand -- I'm sorry, Mr. Jeff Small comes first. I missed one.

It is my understanding that the parties may not have any questions for Mr. Small. Is that the case?

MR. FRIEDMAN: I don't have any questions for Mr. Small.

MR. BURGESS: I had some but I can forego them. When I said that it was yesterday, saying that I didn't mind him being excused. I'll forego cross. I don't have anything.

MS. GERVASI: Okay. I didn't mean to --

MR. BURGESS: That's all right.

MS. GERVASI: Just in the interest of expediency, but if that's the case, then we would request that Mr. Jeffrey A. Small's testimony also be inserted into the record as though read. And he has one exhibit, JAS-1, that we would ask to be identified and also moved in.

COMMISSIONER DEASON: Okay. That will be identified as Exhibit 18. And that's prefiled JAS-1?

MS. GERVASI: Yes, sir.

(Exhibit 18 marked for identification and admitted into the record.)

COMMISSIONER DEASON: And show the prefiled testimony of Jeffrey A. Small inserted into the record.

And just let me -- Commissioners, do you have any questions for this witness?

Okay. I believe the witness may be excused.

MS. GERVASI: Thank you. And did you say it was moved in as well, Commissioner?

COMMISSIONER DEASON: Yes, the testimony and the exhibit, Exhibit 18.

MS. GERVASI: Thank you.

DIRECT TESTIMONY OF JAMES H. BERGHORN

Q. Please state your name and business address.

A. James H. Berghorn, 3804 Coconut Palm Drive, Tampa, FL 33619.

Q. Please state a brief description of your educational background and experience.

A. I have degrees in both Liberal Arts and Biology. A.A. degree in Liberal Arts; B.S. degree in Biology.

I have worked for the State of Florida from 1978 to present. I worked in Research Lab and field collection of environmental samples, drinking water, domestic water, and restaurant inspector.

Q. By whom are you presently employed?

A. Department of Environmental Protection (DEP)

Q. How long have you been employed with the Department of Environmental Protection and in what capacity?

A. Ten years.

Q. What are your general responsibilities at the Department of Environmental Protection?

A. Inspect water plants for compliance with F.A.C. Chapters 62-550; 62-555; 62-699 and all compliance regulations for the State of Florida.

Q. Are you familiar with Utilities, Inc. of Florida's water systems in Marion County, particularly the Golden Hills and Crownwood systems?

A. I am familiar with the water system in Golden Hills that also serves the Crownwood subdivision.

Q. Does the utility have any current construction permits from the Department of Environmental Protection?

A. No. A construction permit is not required for existing water systems.

Q. Are the utility's treatment facilities and distribution systems sufficient to serve its present customers?

A. Yes.

Q. Does the utility maintain the required 20 psi minimum pressure throughout the distribution system?

A. Yes.

Q. Does the utility comply with Section 62-550.515, Florida Administrative Code for an adequate auxiliary power source in the event of a power outage?

A. Yes. However, an auxiliary power plan is not on file.

Q. Are the utility's water wells located in compliance with applicable DEP regulations?

A. Yes.

Q. Does the utility have certified operators as required by Chapter 62-602, Florida Administrative Code?

A. Yes.

Q. Has the utility established a cross-connection control program in accordance with Section 62-555.360, Florida Administrative Code?

A. A file review indicated that on 6/30/00, a sanitary survey; a bacteriological sampling plan; a cross connection control plan; and an auxiliary power plan were requested. As of this date, I have not seen or reviewed any of these plans, nor could I find them in the files.

Q. Is the overall maintenance of the treatment plant and distribution facilities satisfactory?

A. Yes.

Q. Does the finished water produced by the utility meet the State and Federal maximum contaminant levels for primary and secondary water quality standards?

A. Yes.

Q. Does this include the lead and copper rule?

A. Yes.

Q. Has the utility's compliance with the lead and copper rule resulted in a lessening of the monitoring requirements?

A. Yes.

Q. Does the utility monitor the organic contaminants listed in Section 62-55.410, Florida Administrative Code?

A. Yes.

Q. Do recent chemical analyses of raw and finished water, when compared to DEP regulations, suggest the need for additional treatment?

A. No.

Q. Does the utility maintain the required chlorine residual or its equivalent throughout the distribution system?

A. Yes.

Q. Are the plant and distribution systems in compliance with all the other provisions of Title 62, Florida Administrative Code, not previously mentioned?

A. Yes.

Q. Has the utility been the subject of any Department of Environmental Protection enforcement action within the past two years?

A. No.
Q. Do you have anything further to add
A. No, I do not.

DIRECT TESTIMONY OF PETER H. BURGHARDT

Q. Please state your name and business address.

A. Peter H. Burghardt, 3804 Coconut Palm Drive, Tampa, FL 33617.

Q. Please state a brief description of your educational background and experience.

A. B.A. Biology from University of South Florida - 1980

1982 - 1990 - Pasco County Health Department

1990 to present with Florida Department of Environmental Protection as an Environmental Specialist in Domestic Wastewater.

Q. By whom are you presently employed?

A. Department of Environmental Protection (DEP)

Q. How long have you been employed with the Department of Environmental Protection and in what capacity?

A. Since 1990. Domestic Wastewater Compliance/Inspection Section as Environmental Specialist.

Q. What are your general responsibilities at the Department of Environmental Protection?

A. Perform compliance inspections of domestic wastewater facilities to ensure they are operating within permit limits and in accordance with department rules. Pursue enforcement, where applicable, to bring facilities into compliance.

Q. Are you familiar with Utilities, Inc. of Florida's wastewater systems in Marion County, particularly the Crownwood system?

A. Yes.

Q. Does the utility have appropriate current permits from the Department

of Environmental Protection for the Crownwood wastewater system?

A. Yes.

Q. Please state the issuance date and the expiration date of the operating or construction permit.

A. Permit No. FLA012680 was issued 4/23/99. This permit expires 4/22/04.

Q. Is the utility in compliance with its permit?

A. Yes, the plant is in compliance with its permit.

Q. Are the wastewater collection, treatment and disposal facilities adequate to serve present customers based on permitted capacity?

A. Yes.

Q. Are the treatment and disposal facilities located in accordance with Section 62-600.400(1)(c)(2), Florida Administrative Code?

A. Yes.

Q. Has DEP required the utility to take any action so as to minimize possible adverse effects resulting from odors, noise, aerosol drift or lighting?

A. No.

Q. Do pump stations and lift stations meet DEP requirements with respect to location, reliability and safety?

A. Yes.

Q. Does the utility have certified operators as required by Chapter 62-602, Florida Administrative Code?

A. Yes.

Q. Is the overall maintenance of the treatment plant and distribution facilities satisfactory?

A. Yes.

Q. Does UIF meet all applicable technology based effluent limitations (TBELS)?

A. Yes.

Q. Does the facility meet the effluent disposal requirements of Sections 62-611 and 62-600.530, Florida Administrative Code?

A. At the time of the last inspection - yes. The last inspection was on 3/11/03.

Q. Are the collection, treatment and disposal facilities in compliance with all other provisions of Title 62, Florida Administrative Code, not previously mentioned?

A. Yes.

Q. Has the utility been the subject of any Department of Environmental Protection enforcement action within the past two years?

A. No.

Q. No you have anything further to add?

A. No.

DIRECT TESTIMONY OF KIMBERLY M. DODSON

Q. Please state your name and business address.

A. Kimberly M. Dodson, Florida Department of Environmental Protection, 3319 Maguire Blvd., Suite 232, Orlando, Fl. 32803

Q. Please state a brief description of your educational background and experience.

A. I received a B.A. in Environmental Studies from Rollins College, Winter Park, in 1995. From 1991 to 1996 I worked in the environmental analytical laboratory field. From 1996 to present I worked for the Florida Department of Environmental Protection in the potable water program dealing with field inspections, Consumer Confidence Report rule, enforcement and compliance monitoring.

Q. By whom are you presently employed?

A. Florida Department of Environmental Protection (FDEP or Department)

Q. How long have you been employed with the Florida Department of Environmental Protection and in what capacity?

A. I have been employed with the FDEP for 6 years as an Environmental Specialist dealing with inspections, Consumer Confidence Report rule, enforcement, and compliance monitoring.

Q. What are your general responsibilities at the Department of Environmental Protection?

Q. I am responsible for inspecting potable water supply plants; generating inspection reports; entering inspection data in program database; managing the Consumer Confidence Report (CCR) rule program for community water systems; generating reports to determine compliance for CCR;

taking enforcement action against systems not in compliance with FDEP rules; taking and referring drinking water complaints to the appropriate County Health Department for investigation under the DOH-DEP Interagency Agreement.

Q. Are you familiar with Utilities, Inc. of Florida's (utility) water systems in Seminole County, particularly the water treatment systems in Seminole County such as Bear Lake, Jansen, Park Ridge, Phillips, Crystal Lake, Ravenna Park, Weathersfield, Oakland Shores and Little Wekiva?

A. Yes. I have conducted one inspection at each of the systems in Seminole County.

Q. Are the utility's treatment facilities and distribution systems in Seminole County sufficient to serve its present customers?

A. Yes.

Q. Does the utility maintain the required 20 psi minimum pressure throughout the distribution system?

A. Yes. A review of FDEP files does not reveal any consumer complaints regarding low pressure. Lack of consumer complaints was used as a gauge since the Department does not have data regarding continuous monitoring of pressure in the distribution system.

Q. Does the utility comply with Section 62-550.515, Florida Administrative Code for an auxiliary power source in the event of a power outage?

A. Yes, all Seminole systems are in compliance with the rule. Some systems have their own generator, some are interconnected with other water systems and some systems are not required to have a generator. Bear Lake, Jansen, Ravenna Park, and Weathersfield have automatic generators.

The Crystal Lake system utilizes an interconnect with the City of Sanford with an automatic pressure differential valve which opens to supply water when the pressure in the Crystal Lake distribution systems drops below 45 psi. The Oakland Shores system utilizes an interconnect with the City of Altamonte Springs with an automatic pressure differential valve which opens to supply water when the pressure in the Oakland Shores distribution systems drops below 50 psi. For Phillips, based on the number of service connections and population served, this system is not required to have an auxiliary power source, but does have an interconnect with the City of Lake Mary that opens automatically. For Park Ridge and Little Wekiva, based on the number of service connections and population served, these systems are not required to have an auxiliary power source.

Q. Are the utility's water wells located in compliance with applicable FDEP regulations?

A. Yes, for the Seminole County systems of Jansen, Phillips, Oakland Shores, Ravenna Park, and Little Wekiva. For Bear Lake, a septic tank and wastewater plumbing are located within 100 feet of the potable water well. However, this situation has been accepted by the Department provided that the wells are not chemically or bacteriologically compromised, and satisfactory chlorine residual is maintained. For Park Ridge, an irrigation well and wastewater transmission lines are within 100 feet of the potable water well. The Department has accepted this under the condition of continued satisfactory bacteriological and chemical monitoring results, and satisfactory chlorine residual. For

Crystal Lake, wastewater plumbing is located within 100 feet of the potable water wells. This condition has been previously accepted by the Department provided that the wells are not chemically or bacteriologically compromised, and satisfactory chlorine residual is maintained. For Weathersfield, private residences, along with the associated wastewater plumbing and vehicles stored on the property are located within 100 feet of the potable water wells. However, this situation has been accepted by the Department provided that the wells are not chemically or bacteriologically compromised, and satisfactory chlorine residual is maintained.

Q. Does the utility have certified operators as required by Chapter 62-602, Florida Administrative Code?

A. Yes, all Seminole County systems are in compliance with the rule.

Q. Has the utility established a cross-connection control program in accordance with Section 62-555.360, Florida Administrative Code?

A. Yes, all Seminole County systems are in compliance with the rule.

Q. Is the overall maintenance of the treatment plant and distribution facilities satisfactory?

A. Yes, for the Seminole County systems of Bear Lake, Crystal Lake, Jansen, ~~Yes, for the Seminole County systems of Crystal Lake, Oakland Shores~~, Oakland Shores, Park Ridge, Phillips, Weathersfield, and Little Wekiva. ~~Phillips, Weathersfield and Little Wekiva. The Bear Lake, Jansen and~~ For the Ravenna Park system, the interior of the aerator was found to ~~Park Ridge systems currently do not have an alarm system for gas~~ be in poor condition. Paint is peeling, and much of the metal structure ~~chlorination use. If the utility continues to use gas chlorination they~~ is heavily corroded. The utility has indicated that the aerator will be ~~will be required to provide the appropriate alarm systems. The utility~~ replaced with a fiberglass unit with work set to begin on or about ~~has indicated that they will discontinue gas chlorination and should be~~ September 1, 2003. Correspondence from the utility indicates that the ~~able to submit a permit application to the Department for conversion to~~

contractor has begun the necessary custom prefabrication steps and that ~~hypochlorination sometime after the week ending April 18, 2003. The~~ the work is expected to be complete by September 26, 2003. ~~Department's April 3, 2003 inspection report requires that permit applications be received no later than May 9, 2003. For the Ravenna Park system, the interior of the aerator was found to be in poor condition. Paint is peeling and much of the metal structure is heavily corroded. The utility has indicated that they are presently working with a contractor who will conduct a thorough evaluation of the aerator and associated storage tank to determine the appropriate solution. During the Department's April 3, 2003 inspection, the utility indicated that the contractor's proposal should be received by the middle of the week beginning April 7, 2003. The Department's inspection report requires that the utility submit a plan of action no later than May 5, 2003.~~

Q. Can you comment on the type and number of corrections above.

A. Yes, it is not uncommon to find a number of small deficiencies at facilities. In general the utility is doing a good job of maintaining these facilities.

Q. Does the utility maintain the required chlorine residual or its equivalent throughout the distribution system?

A. Yes, all the Seminole County systems maintain the required chlorine residual.

Q. Are the plant and distribution systems in compliance with all the other provisions of Title 62, Florida Administrative Code, not previously mentioned?

A. Yes all the Seminole County systems are in compliance.

Q. Do you have anything further to add?

A. No, I do not.

DIRECT TESTIMONY OF PAUL J. MORRISON

Please state your name and business address.

A. Paul J. Morrison, Florida Department of Environmental Protection, 3319 Maguire Blvd., Suite 232, Orlando, Florida 32803.

Q. Please state a brief description of your educational background and experience.

A. I received a B.S. in Biology from Florida State University in 1972. From 1972 to 1984, I worked for the Orange County Health Department in the Environmental Health Section. I was involved with the regulation of drinking water systems, restaurants, grocery stores, food processors, public swimming pools and bathing beaches, health facilities, septic tanks, mobile home parks, rabies control, and environmental nuisance complaints. From 1984 to present, I have been working for the Florida Department of Environmental Protection with the regulation of solid and industrial waste facility enforcement (1986 and 1987) and with the regulation of public drinking water systems in the compliance and enforcement section (1984, 1985 and 1988 to present).

Q. By whom are you presently employed?

A. Florida Department of Environmental Protection (FDEP)

Q. How long have you been employed with the FDEP and in what capacity?

A. I have been employed with the FDEP since 1984 (18 years). I am an Environmental Manager, involved with public drinking water systems monitoring compliance and enforcement.

Q. What are your general responsibilities at the Florida Department of Environmental Protection?

A. As an Environmental Manager, I supervise the public drinking water

monitoring compliance and enforcement section. This involves notifying systems of monitoring requirements, reviewing monitoring results submitted by water systems to determine if the results are in compliance with established rule standards, notifying systems when corrective action is necessary because of unsatisfactory results, entering monitoring results into the computer database, issuing and rescinding Boil Water Notices when appropriate, reviewing water system malfunction reports, taking appropriate enforcement action against systems not in compliance with the monitoring rules, and taking and referring drinking water complaints to the appropriate County Health Department for investigation under the DOH- FDEP Interagency Agreement.

Q. Are you familiar with Utilities, Inc. of Florida's (utility) water systems in Seminole and Orange Counties, particularly the water treatment systems in Seminole County, including Bear Lake, Jansen, Park Ridge, Phillips, Crystal Lake, Ravenna Park, Weathersfield, Oakland Shores and Little Wekiva and the water distribution systems in Orange County, including Crescent Heights and Davis Shores?

A. Yes, for monitoring I am responsible for the Seminole County water systems. I have also reviewed the permit and enforcement files for all the systems in Seminole and Orange Counties. In addition, I have reviewed the files for the Crescent Heights and Davis Shores distribution systems in Orange County.

Q. Does the utility have any current construction permits from the FDEP for the Seminole or Orange County systems?

A. No, except for Weathersfield. For Weathersfield there is one active DEP construction permit # WD59-0080885-003 which was issued on 3/22/00 for a main

relocation on State Road 436. DEP issued a partial clearance for this permit on 7/17/00. The permit expires on 3/22/03.

Q. Are the utility's distribution systems for the Orange County systems of Crescent Heights and Davis Shores sufficient to serve its present customers?

A. Yes. The Orange County systems of Crescent Heights and Davis Shores have no treatment facilities. The Crescent Heights distribution system is a consecutive system that purchases its water from the Orlando Utilities Commission water system. The Davis Shores distribution system is a consecutive system that purchases its water from the Orange County Utilities Department/Western Regional water system.

Q. Does the utility maintain the required 20 psi minimum pressure throughout the distribution system for Crescent Heights and Davis Shores in Orange County?

A. Yes. A review of Department files does not reveal any consumer complaints regarding low pressure. Lack of consumer complaints was used as a gauge since the Department does not have data regarding continuous monitoring of pressure in the distribution system. The consecutive system's pressure is largely dependent on the pressure provided by the system it buys its water from.

Q. Has the utility established a cross-connection control program for the Orange County systems in accordance with Section 62-555.360, Florida Administrative Code?

A. Yes.

Q. Does the finished water produced by the utility meet the State and Federal maximum contaminant levels for primary and secondary water quality

standards?

A. Yes. All of the utility's Seminole and Orange County systems meet the primary and secondary quality standards. It should be noted that for the Crystal Lake system, the secondary contaminant iron result for the sample collected on April 11, 2000, was 0.35 milligrams per liter (mg/L). The maximum contaminant level (MCL) for iron is 0.3 mg/L. This system uses Aquadene polyphosphate sequestrant treatment for iron. In accordance with Rule 62-550.325(1), F.A.C., a community water system may, in lieu of meeting the MCL for iron or manganese, sequester iron or manganese using polyphosphates when the maximum concentration of iron plus manganese does not exceed 1.0 mg/L. The level of manganese for the Crystal Lake system of 0.019 mg/L on April 11, 2000, plus 0.35 mg/l of iron equals 0.369 mg/L, which does not exceed 1.0 mg/L. Therefore, Crystal Lake is in compliance with the rules for iron. For the Phillips water system, the secondary contaminant iron result for the sample collected on April 11, 2000, was 0.62 mg/L. This system also uses Aquadene polyphosphate sequestrant treatment for iron. The level for manganese for the Phillips system of 0.012 mg/L on April 11, 2000, plus 0.62 mg/l of iron equals 0.632 mg/L, which does not exceed 1.0 mg/L. Therefore, the Phillips system is in compliance with the rules for iron. As mentioned previously, Crescent Heights and Davis Shores are consecutive systems. These systems receive their water from other providers. The Crescent Heights system is required to test for bacteriologicals, asbestos, and lead and copper only. The Davis Shores system is required to test for bacteriologicals and lead and copper only. The Crescent Heights and Davis Shores systems meet the maximum contaminant levels for those contaminants.

Q. Does this include the lead and copper rule?

A. Yes, for all systems.

Q. Has the Utility's compliance with the lead and copper rule resulted in a lessening of the monitoring requirements?

A. Yes, for the Seminole County systems of Bear Lake, Jansen, Park Ridge, Phillips, Crystal Lake, Oakland Shores, Ravenna Park, and Weathersfield and the Orange County systems of Crescent Heights and Davis Shores. These systems are on reduced monitoring. Monitoring must be done every 3 years during the months of June, July, August or September. Although the Lead and copper sample results for the Little Wekiva system collected on 6/13/02 were below the action level for both lead and copper, of the five required samples collected, only three met the first draw tap sampling requirement of water standing motionless in the plumbing system for at least six hours. As a result of eliminating two sites which had samples collected in less than six hours, a monitoring violation was created since an insufficient number of samples were collected and submitted during the June-September 2002 monitoring period. However, the number submitted shows that an effort was made to comply with the lead and copper rule. As a result of this monitoring violation for Little Wekiva, five additional lead and copper samples must be collected in June 2003.

Q. Does the utility monitor for the volatile organic contaminants (VOCs) listed in Section 62-550.515, Florida Administrative Code?

A. Yes, for all of the Seminole County systems. The Utility's Orange County consecutive water systems, Crescent Heights and Davis Shores, are not required to test for the VOCs.

Q. Does the utility monitor for the synthetic organic contaminants (SOCs) listed in Section 62-550.516, Florida Administrative Code?

A. Yes, for all the Seminole County systems, except for dioxin which has a statewide waiver for monitoring unless the water system is a surface water system or is a system that has been determined to be under the direct influence of surface water. The Seminole County systems are neither of those. The utility's Orange County systems, Crescent Heights and Davis Shores are consecutive water systems, which are not required to test for the SOCs.

Q. Do recent chemical analyses of raw and finished water, when compared to DEP regulations, suggest the need for additional treatment for any of the systems?

A. No.

Q. For the Orange County distribution systems of Crescent Heights and Davis Shores, does the utility maintain the required chlorine residual or its equivalent throughout the distribution system?

A. Yes. The chlorine residual is dependent on the chlorine provided by the system it buys its water from.

Q. Are the Orange County distribution systems of Crescent Heights and Davis Shores in compliance with all the other provisions of Title 62, Florida Administrative Code, not previously mentioned?

A. Yes.

Q. Have the utility's Seminole or Orange County systems been the subject of any FDEP enforcement action within the past two years?

A. No.

Q. Do you have anything further to add?

A. No, I do not.

DIRECT TESTIMONY OF GARY P. MILLER

Q. Please state your name and business address.

A. Gary P. Miller, Florida Department of Environmental Protection, 3319 Maguire Blvd., Suite 232, Orlando, Fl. 32803

Q. Please give a brief description of your educational background and experience.

A. I have a B.S. in Biology. I worked for the Osceola County Health Department in the environmental health section for approximately 5 years and for the Florida Department of Environmental Protection (DEP) in the wastewater and drinking water sections for approximately 19 years.

Q. By whom are you currently employed and in what capacity?

A. I am the Program Manager in the Wastewater Compliance/Enforcement Section of DEP.

Q. What are your general responsibilities at the DEP?

A. I manage the Wastewater Compliance/Enforcement Section which includes reviewing all enforcement documents (warning letters, consent orders, notice of violations etc.) and noncompliance letters of all Type I and II domestic wastewater facilities and conducting enforcement and compliance meetings.

Q. Are you familiar with Utilities, Inc. of Florida's wastewater systems in Seminole County, particularly the Lincoln Heights and Weathersfield Wastewater Treatment Facilities (WWTF)?

A. Yes.

Q. Does the utility have the appropriate current permits from the DEP for these facilities?

A. Domestic wastewater treatment plant permits are not required for those

facilities. The Lincoln Heights WWTF was shut down on July 6, 2001 with the flow being diverted to the City of Sanford WWTF. The Weathersfield WWTF was shut down many years ago with the flow being diverted to the City of Altamonte Springs WWTF.

Q. Do the utility's pump stations and lift stations meet DEP requirements with respect to location, reliability and safety?

A. Yes. No recent deficiencies have been noted for either facility.

Q. Are the collection facilities in compliance with all other provisions of Title 62, Florida Administrative Code, not previously mentioned?

A. Yes.

Q. Has the utility been subject of any DEP enforcement action within the past two years?

A. Yes. Prior to the Lincoln Heights WWTF being shut down, the utility entered into a consent order with the DEP (OGC File No. 98-2102). All of the requirements of the consent order have been completed and the case is closed.

Q. Do you have anything further to add?

A. No, I do not.

DIRECT TESTIMONY OF WILLIAM V. RYLAND

Q. Please state your name and business address.

A. William V. Ryland, 3804 Coconut Palm Drive, Tampa, FL 33619.

Q. Please state a brief description of your educational background and experience.

A. I have a B.S. degree in Biology with minors in Chemistry and Earth Science. I have worked with the State of Florida for over 15 years, mainly in the drinking water program.

Q. By whom are you presently employed?

A. Department of Environmental Protection (DEP)

Q. How long have you been employed with the Department of Environmental Protection and in what capacity?

A. Ten years as an Environment Specialist in the Potable Water Section.

Q. What are your general responsibilities at the Department of Environmental Protection?

A. Regulation of drinking water facilities within a certain geographic area. This includes but is not limited to compliance/enforcement for systems that fall under the Safe Drinking Water Act; conducting yearly inspections, reviewing chemical/bacteriological data, monitoring compliance, and pursuing enforcement activities.

Q. Are you familiar with Utilities, Inc. of Florida's water systems in Pasco County, particularly the Buena Vista, Orangewood, Summertree and Wis-Bar systems?

A. Yes.

Q. Does the utility have any current construction permits from the

Department of Environmental Protection?

A. Summertree - Parcel H - DSGP (distribution system general permit)
Orangewood - 81396 - Col - DSGP
Information obtained from Steven King, Engineer II of our permitting section.

Q. Are the utility's treatment facilities and distribution systems sufficient to serve its present customers?

A. Yes.

Q. Does the utility maintain the required 20 psi minimum pressure throughout the distribution system?

A. Yes.

Q. Does the utility comply with Section 62-550.515, Florida Administrative Code for an adequate auxiliary power source in the event of a power outage?

A. Yes through generators or interconnects with other systems.

Q. Are the utility's water wells located in compliance with applicable DEP regulations?

A. Yes.

Q. Does the utility have certified operators as required by Chapter 62-602, Florida Administrative Code?

A. Yes.

Q. Has the utility established a cross-connection control program in accordance with Section 62-555.360, Florida Administrative Code?

A. Yes. Cross connection control plans are on file at DEP and at the utility. Plans were revised as of June, 2001.

Q. Is the overall maintenance of the treatment plant and distribution facilities satisfactory?

A. Yes.

Q. Does the finished water produced by the utility meet the State and Federal maximum contaminant levels for primary and secondary water quality standards?

A. Yes.

Q. Does this include the lead and copper rule?

A. Yes.

Q. Has the utility's compliance with the lead and copper rule resulted in a lessening of the monitoring requirements?

A. Yes, tri-annual monitoring.

Q. Does the utility monitor the organic contaminants listed in Section 62-55.410, Florida Administrative Code?

A. Yes.

Q. Do recent chemical analyses of raw and finished water, when compared to DEP regulations, suggest the need for additional treatment?

A. No.

Q. Does the utility maintain the required chlorine residual or its equivalent throughout the distribution system?

A. Yes.

Q. Are the plant and distribution systems in compliance with all the other provisions of Title 62, Florida Administrative Code, not previously mentioned?

A. Yes.

Q. Has the utility been the subject of any Department of Environmental Protection enforcement action within the past two years?

A. No.

Q. Do you have anything further to add?

A. No, I do not.

DIRECT TESTIMONY OF PEPE MENENDEZ

Q. Please state your name and business address.

A. Pepe Menendez, P.E., 4175 East Bay Drive, Suite 300, Clearwater, FL 33764.

Q. Please state a brief description of your educational background and experience.

A. Professional Engineer - Fla. License # 21616. Bachelor in Civil Engineering. 28 years experience in drinking water and other environmental areas.

Q. By whom are you presently employed?

A. Pinellas County Health Department.

Q. How long have you been employed with the Pinellas County Health Department and in what capacity?

A. I have been employed with the Pinellas County Health Department for three months, as Assistant Director in the Environmental Engineering Division. Before that, I was the Administrator for Drinking Water with the Florida Department of Health (a Professional Engineer position). I was in that position since 1990. I have been employed by the State of Florida in various positions since 1980.

Q. What are your general responsibilities at the Pinellas County Health Department?

A. I administer the drinking water, USTDS and SUPER programs.

Q. Are you familiar with Utilities, Inc. of Florida's water systems in Pinellas County, particularly the Lake Tarpon Mobile Home Park system?

A. My staff is familiar with the Lake Tarpon Mobile Home Park.

Q. Does the utility have any current construction permits from the Pinellas County Health Department or the Department of Environmental Protection?

A. No. A construction permit is not required for existing systems.

Q. Are the utility's treatment facilities and distribution systems sufficient to serve its present customers?

A. Yes.

Q. Does the utility maintain the required 20 psi minimum pressure throughout the distribution system?

A. Yes, as far as we know.

Q. Does the utility comply with Section 62-550.515, Florida Administrative Code for an adequate auxiliary power source in the event of a power outage?

A. Yes.

Q. Are the utility's water wells located in compliance with applicable DEP regulations?

A. Yes.

Q. Does the utility have certified operators as required by Chapter 62-602, Florida Administrative Code?

A. Yes.

Q. Has the utility established a cross-connection control program in accordance with Section 62-555.360, Florida Administrative Code?

A. Yes.

Q. Is the overall maintenance of the treatment plant and distribution facilities satisfactory?

A. Yes.

Q. Does the finished water produced by the utility meet the State and

Federal maximum contaminant levels for primary and secondary water quality standards?

A. Yes.

Q. Does this include the lead and copper rule?

A. Yes.

Q. Has the utility's compliance with the lead and copper rule resulted in a lessening of the monitoring requirements?

A. Yes.

Q. Does the utility monitor the organic contaminants listed in Section 62-55.410, Florida Administrative Code?

A. Yes.

Q. Do recent chemical analyses of raw and finished water, when compared to DEP regulations, suggest the need for additional treatment?

A. No.

Q. Does the utility maintain the required chlorine residual or its equivalent throughout the distribution system?

A. Yes.

Q. Are the plant and distribution systems in compliance with all the other provisions of Title 62, Florida Administrative Code, not previously mentioned?

A. Yes.

Q. Has the utility been the subject of any Pinellas County Health Department enforcement action within the past two years?

A. No.

Q. Do you have anything further to add?

A. No, I do not.

DIRECT TESTIMONY OF JEFFREY A. SMALL

Q. Please state your name and business address.

A. My name is Jeffrey A. Small and my business address is Hurston North Tower, Suite N512, 400 W. Robinson Street, Orlando, Florida, 32801.

Q. By whom are you presently employed and in what capacity?

A. I am employed by the Florida Public Service Commission as a Professional Accountant Specialist in the Division of Auditing and Safety.

Q. How long have you been employed by the Commission?

A. I have been employed by the Florida Public Service Commission since January 1994.

Q. Briefly review your educational and professional background.

A. I have a Bachelor of Science degree in Accounting from the University of South Florida. I am also a Certified Public Accountant licensed in the State of Florida and I am a member of the American and Florida Institutes of Certified Public Accountants.

Q. Please describe your current responsibilities.

A. Currently, I am a Professional Accountant Specialist with the responsibilities of planning and directing the most complex investigative audits, including audits of cross-subsidization issues, anti-competitive behavior, and predatory pricing. I also am responsible for creating audit work programs to meet a specific audit purpose and integrating EDP applications into these programs. In addition, I serve as the acting supervisor in the absence of the district office supervisor.

Q. Have you presented expert testimony before this Commission or any other regulatory agency?

A. Yes. I testified in the Southern States Utilities, Inc. rate case, Docket No. 950495-WS and the transfer application of Cypress Lakes Utilities, Inc., Docket No. 971220-WS.

Q. What is the purpose of your testimony today?

A. The purpose of my testimony is to sponsor the staff audit report of Utilities, Inc. of Florida (UIF, or utility) in Marion, Orange, Pasco, Pinellas, and Seminole Counties, Docket No. 020071-WS. The audit report is filed with my testimony and is identified as JAS-1.

Q. Was this audit report prepared by you?

A. Yes, I was the audit manager in charge of this audit.

Q. Please review the work you performed in this audit.

A. For rate base, I examined account balances for utility-plant-in-service (UPIS), land, plant-held-for-future-use (PHFU), contributions-in-aid-of-construction (CIAC), accumulated depreciation (AD), accumulated amortization of CIAC (AAC), and working capital (WC) as of the last Commission order. I reconciled rate base balances authorized in Commission Orders to the respective December 31, 2001 general ledger balance.

For net operating income, I compiled utility revenues and operating and maintenance accounts for the year ended December 31, 2001. I chose a judgmental sample of customer bills and recalculated using FPSC-approved rates. I also chose a judgmental sample of operation and maintenance expenses (O&M) and examined the invoices for supporting documentation. I reviewed the allocation of O&M expenses from Water Service Corporation (WSC) and UIF cost centers to the respective counties and verified the accuracy of company allocations based on company-provided allocation schedules. I also tested the

calculation of depreciation and CIAC amortization expense and examined the support for taxes other than income and income taxes and I audited the utility's December 31, 2001, Regulatory Assessment Fee Returns.

For capital structure, I compiled the components of the capital structures for the year ended December 31, 2001 and agreed interest expense to the terms of the notes and the bonds. I also reconciled note balances at December 31, 2001, to supporting documentation.

Q. Please review the audit exceptions in the audit report.

A. Audit Exceptions disclose substantial non-compliance with the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts (USOA), a Commission rule or order, and formal company policy. Audit Exceptions also disclose company exhibits that do not represent company books and records and company failure to provide underlying records or documentation to support the general ledger or exhibits.

Audit Exception No. 1 discusses adjustments to water rate base made in prior orders.

- Commission Order No. PSC-93-0430-FOF-WS, issued March 22, 1993, established the rate base balance for the Pasco County (Summertree PPW) water system as of April 30, 1991.
- Commission Order No. PSC-94-0739-FOF-WS, issued June 16, 1994, required specific rate base adjustments to the Marion and Pinellas Counties water systems.
- Commission Order No. PSC-95-0574-FOF-WS, issued May 9, 1995, required specific rate base adjustments to the Orange, Pasco (Orangewood), and Seminole Counties water systems.

- Commission Order No. PSC-01-1655-PAA-WS, issued August 13, 2001, established the rate base balance for the Pasco County (WisBar/Bartelt) water systems as of June 15, 2000.

The utility made several adjustments in its general ledger in 1995 to record the second and third adjustments above. In several instances the utility adjusted the wrong account or used an incorrect amount. I have corrected these errors and Schedules A through E attached to Audit Exception 1 in the audit report detail my adjustments.

According to utility records, it recorded the acquisition of the Pasco County (Summertree PPW) water system in its 1990 general ledger prior to rate base being established in Order No. PSC-93-0430-FOF-WS. The utility did not make any adjustments to that initial balance following the issuance of this Order. My adjustments are included in Schedule F in the audit report.

According to utility representatives, the utility did not record the acquisition of the Pasco County (WisBar/Bartelt) water system in its general ledger until 2002 which was after the test year ended December 31, 2001. My adjustments are included in Schedule G in the audit report.

These adjustments will also affect the accumulated depreciation and accumulated amortization of CIAC balances as of December 31, 2001, as well as the depreciation expense and amortization of CIAC expense balances for the 12-month period ended December 31, 2001. Furthermore, I calculated additional accumulated depreciation and accumulated amortization of CIAC adjustments for the Pasco County wastewater systems at Summertree PPW and WisBar based on its adjustments to rate base as of the respective transfer dates. These adjustments can be found on Schedule H in the audit report.

Audit Exception No. 2 discusses adjustments to wastewater rate base made in prior orders.

- Commission Order No. PSC-93-0430-FOF-WS, issued March 22, 1993, established the rate base balance for the Pasco County (Summertree PPW) wastewater system as of April 30, 1991.
- Commission Order No. PSC-94-0739-FOF-WS, issued June 16, 1994, required specific rate base adjustments to the Marion County wastewater system.
- Commission Order No. PSC-95-0574-FOF-WS, issued May 9, 1995, required specific rate base adjustments to the Seminole County wastewater system.
- Commission Order No. PSC-01-1655-PAA-WS, issued August 13, 2001, established the rate base balance for the Pasco County (WisBar) wastewater system as of June 15, 2000.

The utility made several adjustments in its general ledger in 1995 to record the second and third adjustments above. In several instances, the utility adjusted the wrong account or used an incorrect amount. I have corrected these errors and Schedules I and J attached to the Audit Exception 2 in the audit report detail my adjustments.

According to utility records, it recorded the acquisition of the Pasco County (Summertree PPW) wastewater system in its 1990 general ledger prior to rate base being established in Order No. PSC-93-0430-FOF-WS. The utility did not make any adjustments to that initial balance following the issuance of this Order. My adjustments are included in Schedule K in the audit report.

According to utility representatives, the utility did not record the acquisition of the Pasco County (WisBar) wastewater system in its general ledger until 2002 which was after the test year ended December 31, 2001. My

adjustments are included in Schedule G in the audit report.

These adjustments will affect the accumulated depreciation and accumulated amortization of CIAC balances as of December 31, 2001, as well as the depreciation expense and amortization of CIAC expense balances for the 12-month period ended December 31, 2001. Furthermore, I calculated additional accumulated depreciation and accumulated amortization of CIAC adjustments for the Pasco County wastewater systems at Summertree PPW and WisBar based on its adjustments to rate base as of the respective transfer dates. These adjustments can be found on Schedule M in the audit report.

Audit Exception No. 3 discusses plant items that should be amortized as nonrecurring expenses. Commission rule 25-30.433(8), Florida Administrative Code, requires that nonrecurring expenses shall be amortized over a five-year period unless a shorter or longer period of time can be justified. NARUC Class A, Balance Sheet, Account 186, states that this account shall include all debits not elsewhere provided for, such as items deferred by authorization of the Commission. The utility recorded the following plant additions in for major repairs to its water and wastewater systems.

- Marion Water: $1,122.23 to rebuild pump motor at Goldenhills.
- Marion Wastewater: $901.00 to refurbish 4M blower assembly.
- Pasco Water: $3,317.57 to pull & recondition pump at Orangewood.
- Pasco Wastewater: $2,784.49 to pull & repair sewer grinder pump at Buena Vista.
- Pasco Wastewater: $3,387.68 to repair lift station control at Summertree PPW.
- Seminole Wastewater: $2,725.00 for a TV video inspection of sewer lines.

I recommend that the utility's water and wastewater UPIS accounts should be reduced by the above amounts to remove nonrecurring expenses and these amounts should be amortized over a five-year period per the Commission and NARUC rules cited above. Additionally, the utility should also increase its operations and maintenance (O&M) expenses for the 12-month period ended December 31, 2001, to record the amortization of the deferred UPIS adjustment over a five-year period.

Audit Exception No. 4 discusses the replacement and retirement of plant. NARUC, Class A, Accounting Instruction 27.B.(2) requires that, when a retirement unit is retired from utility plant with or without replacement, the book cost thereof shall be credited to the utility plant account in which it is included. The book cost shall be determined from the utility's records and if this cannot be done, it shall be estimated. The utility's procedure for recording retirements of UPIS is to indicate on the invoice the amount retired and the calculations. The utility's policy for retirement of UPIS consists of the following four procedures.

- If the amount of the old equipment is given and is less than $250 and the year the original equipment was purchased is 1990 -1996, do not retire.
- If the amount of the old equipment is given and is greater than $100 and the year the original equipment was purchased is prior to 1990, retire the amount given for the old equipment.
- If the amount of the old equipment is not given, but the year the equipment was purchased is provided, use the Handy Whitman Index. Multiply the percentage from the Handy Whitman Index by the total amount of the invoice and use this amount for your retirement.

- If neither the amount of the old equipment or the year of purchase is given, retire 75 percent of the total amount of the invoice.

The utility recorded several additions to its UPIS water and wastewater systems without recording a corresponding retirement. These retirements should have been recorded pursuant to the company's policy. I recommend that the adjustments detailed in the audit report be made to record the retirements, related accumulated depreciation, and depreciation expense.

Audit Exception No. 5 discusses reclassified Utility Plant in Service. Utility records indicate a 1992 addition of $46,944 to Account No. 370, Receiving Wells, in Pasco County for the demolition and removal of the Summertree PPW wastewater treatment plant that was identified as Construction Project CW-625-116-91-04. Utility records also indicate a 2001 addition of $101,518 to Account No. 353, Land, in Seminole County for engineering fees associated with the preliminary planning, design, modification, and construction of a wastewater interconnection with the City of Sanford, Florida, that was identified as Construction Project CW-614-116-98-14.

Commission rule 25-30.115, F.A.C., adopts the NARUC Uniform System of Accounts for Water and Wastewater Utilities (USOA). The Class A report includes the following comments:

1. Accounting Instruction 27.B.(2), states that when a retirement unit is retired, the cost of removal and the salvage shall be charged to or credited, as appropriate, to such depreciation account.

2. Accounting Instruction 27.H., states that when the early retirement of a major unit of property eliminates the existing

depreciation reserve account, the Commission may authorize an alternative treatment such as transferring the balance to Account No. 186 and amortizing it in future periods.

3. Balance Sheet Account 183 states that this account shall be charged with all expenditures for preliminary surveys, plans, investigations, etc., made for determining the feasability of projects under contemplation. If the work is abandoned, the charge shall be to Account 426 - Miscellaneous Nonutility Expenses, or to the appropriate operating account expense account unless otherwise ordered by the Commission.

4. Balance Sheet Account 186 states that this account shall include all debits not elsewhere provided for, such as items the proper final disposition of which is uncertain.

5. Income Account 426 includes expenses disallowed in a proceeding before the Commission and expenses for preliminary survey and investigation expenses related to abandoned projects, when not written off to the appropriate expense account.

Commission rule 25-30.116(1)(d) 3, F.A.C., states that when a project is completed and ready for service, it shall be immediately transferred to the appropriate plant account(s) or Account 106, Completed Construction Not Classified, and may no longer accrue Allowance for Funds Used During Construction (AFUDC).

I recommend that the $46,944 addition to Pasco County-Summertree PPW wastewater Account No. 370 should be removed per Accounting Instruction 27.B.(2) because it was a demolition cost that was related to the retirement

of the wastewater treatment facility. However, there is no depreciation reserve account to transfer the balance to as required. The Commission, in Order No. PSC-93-0430-FOF-WS, retired the Pasco County-Summertree PPW wastewater plant from UPIS and eliminated the balance of the depreciation reserve in 1991. The utility has depreciated the $46,944 and there is a current balance of $12,755 as of December 31, 2001. I recommend that the utility transfer the net unrecovered balance of $34,189 ($46,944 - $12,755) to Account No. 186 pending disposition by the Commission and remove the $46,944 and $12,755 from Accounts Nos. 370 and 108, respectively. Additionally, the utility should be required to reduce its depreciation expense by $1,343 ($46,944 x 2.86%) for Pasco County wastewater for the 12-month period ended December 31, 2001, to account for the effect of the adjustment.

The $101,518 addition to Seminole County-wastewater land should be removed and reclassified to the following four accounts.

Account No. 183: $14,935 represents engineering costs incurred to analyze and develop alternative methods for wastewater treatment at the Lincoln Heights wastewater plant given the anticipated condemnation and acquisition of utility property by the Florida Department of Transportation and Seminole County. These costs were for alternative projects that were studied and abandoned by the utility. Therefore, they should be charged to Account. No 183 pending final disposition by the Commission per the definition for Account No. 183.

Account No. 354: $43,859 represents engineering costs incurred to design and relocate the wastewater discharge facilities for the wastewater

plant and percolation ponds because of the condemnation and acquisition of utility land. Therefore, these costs should be recorded in Account No. 354, Structures & Improvements, with an additional $577 recorded in the respective accumulated depreciation and depreciation expense accounts to reflect the corresponding effect on test year 2001.

Account No. 361: $28,185 represents engineering costs incurred to design and relocate the utility mains for the wastewater plant because of the condemnation and acquisition of utility land. Therefore, it should be recorded in Account No. 361, Collecting Sewers-Gravity, with an additional $313 recorded in the respective accumulated depreciation and depreciation expense accounts to reflect the corresponding effect on test year 2001.

Account. No. 426: $14,541 represents the Allowance for Funds Used During Construction (AFUDC) charged to the above project from March 2000 through December 2001. Construction project schedules indicate that the last recorded activity other than AFUDC accruals for this project was in February 2000. Since there was no subsequent activity after February 2000, I have concluded that the project should be deemed substantially complete at that time, and the total balance should have been transferred to a UPIS account or Account No. 106. Therefore, the $14,541 AFUDC accrued after February 2000 should be disallowed and charged to Account No. 426.

Audit Exception No. 6 discusses organization costs and capitalized labor. Utility records indicate $263 recorded in Account 301 in the Marion county water system in 1996 for an invoiced amount from the Florida Department of Revenue. There are also additions in Account 301 and 351 of $872 to both the water and wastewater systems in Pasco County in 1995 that are a

reclassification of a vendor invoice initially recorded in 1991 that is undefined. The USOA instructions for Plant Account Nos. 301 and 351 state that the account shall include all fees paid to federal or state governments for the privilege of incorporation and expenditures incident to organizing the corporation, partnership or other enterprise and putting it into readiness to do business. I recommend that these three amounts be removed as they do not meet the requirements of the USOA.

The company also capitalized $24,667 in Account 301 in the Pasco County water system in 2000 as capitalized executive salaries. This was itemized as an acquisition and transfer cost for the purchase of the WisBar/Bartelt Enterprises. Two Commission orders (Order No. 25821, issued February 27, 19992, in Docket No. 910020, Petition for rate increase by Utilities, Inc. of Florida, and Order No. PSC-94-0739-FOF-WS, issued June 16, 1994, in Docket No. 930826-WS, Application for a rate increase by Utilities, Inc. of Florida) determined that the purchased cost of utility systems is to be charged as acquisition adjustments, not as organization cost. Therefore, I recommend that the capitalized executive salaries should be removed and recorded as an acquisition adjustment.

The company also capitalized $2,952, $9,724 and $9,579 in Account Nos. 301 and 380 in the Seminole county water system for the years 1999 and 2000 for capitalized executive salaries described as time spent working on condemnation issues related to the Lincoln Heights wastewater treatment plant site. The USOA instructions for Account 186 state that this account shall include all debits not elsewhere provided for, such as items the proper final disposition of which is uncertain. I recommend that these costs for the

Seminole county systems should be removed and recorded in Account No. 186 pending final disposition by the Commission.

Additionally, the accumulated depreciation and depreciation expenses should be reduced for these adjustments.

Audit Exception No. 7 discusses common plant allocations from Utilities, Inc. of Florida (UIF). UIF serves two roles for Utilities, Inc.'s operations in Florida. First, UIF is the administrative and operational headquarters for all of the parent's Florida operations. Second, UIF is the controlling and operating entity for the five counties that are parties for this rate proceeding. UIF allocates a portion or all of its common rate base using a customer equivalent (CE) percentage for each of the five county operations from the following eight cost centers: (1) 600: Office Structures & Communication, (2) 600: Tools & Lab, (3) 601: UIF Cost Center, (4) 603: Orlando Cost Center (Orange & Seminole Counties), (5) 638: Ocala Cost Center (Marion County), (6) 639: West Coast Cost Center (Pasco & Pinellas Counties), (7) 600: Computer Allocation, and (8) 600: UIF Transportation. Included in the amount for Office Structures & Communication listed above is an addition of $29,880 for Work Order CW-0600-117-00-02 that was for the purchase of a new Norstar voice mail system for the UIF office in 2000. Included in the amount for the Orlando Cost Center listed above is an addition of $6,722 for Work Order CW-602-117-97-09 that was for the purchase of a new cellular communications system for service personnel in 1997. These additions were UPIS additions that replaced existing systems that the utility was using at the time. However, the utility did not record any retirements to UPIS or accumulated depreciation when the new systems were installed. I recommend

that the utility's common UPIS should be reduced to properly account for retirement of UPIS. The utility's water and wastewater accumulated depreciation and depreciation expenses should also be reduced.

Audit Exception No. 8 discusses common plant allocations from Water Services Corporation (WSC). WSC, the service corporation for the parent company Utilities, Inc., allocates a portion of its common rate base to each subsidiary utility throughout the United States. UIF received $85,096, net of accumulated depreciation and accumulated deferred income taxes, or approximately 3.7 percent of the total WSC net rate base of $2,300,646. The allocation is based on a calculated customer equivalent (CE) percentage that equates all customers throughout the United States in terms of single family residential equivalent units. UIF then allocates the $85,096 it received from WSC to each of its five county systems based on the same customer equivalent formula. Kathy Welch is sponsoring testimony in this docket to sponsor an undocketed affiliate transaction audit of Utilities, Inc. and its subsidiary WSC for the 12-month period ended December 31, 2001. The scope of the audit included an examination of the WSC rate base components that are allocated to all of its subsidiary operations in 2001. The audit report, issued October 23, 2001, included adjustments that increased UIF's allocated WSC net rate base allocation by $3,588 to $88,684.

The above-mentioned allocation percentages used to distribute WSC's net rate base to the five counties in this rate proceeding do not reconcile to any allocation methodology that was presented by the utility in its filing or its response to the audit staff's inquiries. I have incorporated the increase of $3,588 to WSC's net rate base as referenced above and recalculated the

allocation percentages for each of the five counties that are parties in this rate proceeding to be consistent with the methodology used by UIF to allocate its common rate base as described in Exception No. 7.

Audit Exception No. 9 discusses adjustments to test year UPIS balances. The audit staff performed a tour of utility property in Orange and Seminole Counties with a company representative on October 10, 2002. I noted the following events on the plant tour.

Orange County - Crescent Heights & Davis Shores: The Crescent Heights water system is interconnected with Orlando Utilities Commission for its potable water needs. The utility still has a building, hydro-pneumatic tank, pump, and well head at the site. All other equipment has been removed. At the time of the audit, the utility had plans to dispose of the remaining equipment and demolish the building within the next six months. It does not anticipate any salvage value for the remaining equipment. The physical interconnection with Orlando Utilities is not located on utility property. The Davis Shores water system is interconnected with Orange County Utilities for its potable water needs. The utility has removed all of its equipment from the Davis Shores site and disposed of the utility land. I recommend that all land and water treatment plant be retired from service.

Seminole County - Lincoln Heights Wastewater Plant: The Lincoln Heights wastewater system has been interconnected with the City of Sanford since July 2001. The wastewater plant and treatment facilities have been taken off line and at the time of the audit, the utility had plans to dispose of or demolish them in the coming months. The only equipment remaining at the wastewater plant site is a new master lift station that transfers the untreated sewage

to the interconnect site that is not located on utility property. The wastewater percolation ponds are to be cleaned and filled to grade level. The State Department of Transportation (DOT) and Seminole County have taken approximately 58.52 percent of the existing 14.90 acres of the original land site through condemnation action for road way improvements. The remaining utility land will contain the new transfer lift station (4.75 acres) and an undetermined future use (1.43 acres). The utility is still litigating the outcome of the condemnation with Seminole County and the DOT. The wastewater land contained 14.90 acres prior to the condemnation proceedings and was recorded in Seminole County's books at an original cost of $11,597 for SUB614 Lincoln Heights G/L. I recommend that 58.52 percent of the utility's wastewater land balance for Lincoln Heights, and 100 percent of the wastewater treatment plant be retired from service. Utility records indicate a retirement of $6,000 to Account No. 353, Land, for Seminole County in 1999 which supports the audit staff's estimated retirement calculated above. Therefore, no additional retirement for utility land is recommended.

Audit Exception No. 10 discusses CIAC and Advances. The utility's records reflect balances of $52,000 and $48,000 in Accounts Nos. 2525000 and 2526000, Advances-in-Aid of Construction, in Seminole County as of December 31, 2001. The water and wastewater account balances have been inactive and on the utility's books prior to 1992. The utility stated that it "has researched all available information relating to the accounts noted in this request. However, there is no supporting information pertaining to these balances. However, the Utility has no record of this money ever being paid out. Therefore, it remains in the Advances-in-Aid accounts." The USOA

description for Account 252 includes advances by or in behalf of customers for construction which are to be refunded either wholly or in part. When a person is refunded the entire amount to which he is entitled according to the agreement or rule under which the advance was made, the balance, if any, remaining in this account shall be credited to Account 271, CIAC. I recommend that the utility reclassify the above balances to Account No. 271, CIAC. I also recommend that the accumulated amortization of CIAC and amortization expense for 2001 should be increased to record the additional amortization of the above balances for the test year.

Audit Exception No. 11 discusses depreciation rates. Rule 25-30.140(2), F.A.C., establishes an average service life and corresponding depreciation rates for UPIS asset additions. This rule was used in the prior proceedings for the counties in this rate case (see Order No. PSC-93-0430-FOF-WS, issued March 22, 1993, Pasco County (Summertree PPW), Order No. PSC-94-0739-FOF-WS, issued June 16, 1994, Marion and Pinellas Counties systems, and Order No. PSC-95-0574-FOF-WS, issued May 9, 1995, Orange, Pasco (Orangewood), and Seminole County systems.) My analysis of the utility's test year 2001 depreciation rates from its Annual Reports indicate that for wastewater Accounts Nos. 371 and 380 it used the incorrect depreciation rates when calculating depreciation expense and the respective accruals to accumulated depreciation. I recalculated the accumulated depreciation balances for Accounts Nos. 371 and 380 using the rule rates described above. The utility should be required to increase its accumulated depreciation balance as of December 31, 2001, for Marion, Pasco, and Seminole County by $21,744, $57,828 and $83,141, respectively. Additionally, my recalculation will increase test year

depreciation expense for the 12-month period ended December 31, 2001, for Marion, Pasco and Seminole Counties by $2,636, $7,987, and $12,011, respectively.

Audit Exception No. 12 discusses amortization rates of CIAC. Rule 25-30.140 (8), F.A.C., states that the CIAC amortization rate shall be that of the appropriate account or function where supporting documentation is available to identify the account or function of the related CIAC plant. Otherwise, the composite plant amortization rate shall be used. Utility records indicate that it uses the latter method of calculating its amortization of CIAC for the five counties in this rate proceeding. My analysis of the utility's accumulated amortization of CIAC and CIAC amortization expense balances from its MFRs indicate that it used incorrect composite amortization rates when calculating its CIAC amortization expense for the 12-month period ended December 31, 2001. I recalculated accumulated amortization of CIAC and CIAC amortization expense by applying the correct composite depreciation rates per the rule cited above. The utility should be required to adjust accumulated amortization of CIAC and test year amortization expense.

Audit Exception No. 13 discusses the General Ledger balances of Accumulated Amortization of CIAC. Commission Order No. PSC-93-0430-FOF-WS, issued March 22, 1993, Pasco County (Summertree PPW), established accumulated amortization of CIAC balances of $114,744 and $125,359 for the Pasco County (Summertree PPW) water and wastewater systems, respectively, as of April 30, 1991. The Order states that the utility presented balances of $68,939 and $59,402, for water and wastewater accumulated amortization of CIAC as of

October 30, 1990, in its filing for Docket No. 920834-WS for Pasco County (Summertree PPW). The utility's 1994 general ledger reflects balances of $34,854 and $33,018, for water and wastewater accumulated amortization of CIAC, respectively, as of December 31, 1993, when Accounts Nos. 276-00 and 277-00, Accumulated Amortization CIAC-Water and Accumulated Amortization CIAC-Wastewater, first appeared in its general ledger. The 1994 entries also included yearly accruals of $11,618 and $10,154 for 1994. Prior to 1994, the utility's policy was to record its accumulated amortization of CIAC as a direct offset to yearly accruals of accumulated depreciation in its accumulated depreciation accounts. There is no general ledger record of the above policy taking place for the Pasco County (Summertree PPW) systems since it was initially recorded on the utility's books in 1990.

The utility's conflicting balances for accumulated amortization of CIAC in its filing for Docket No. 920834-WS and in its 1994 general ledger balance above, along with its inadequate records for the period 1990 through 1994, provide sufficient evidence to question its accumulated amortization of CIAC balance of $130,438 and $125,703 as of December 31, 2001, for Pasco County in its MFR filing. Using information from the utility's filings in Docket No. 920834-WS and its 1990 through 1994 general ledgers, I have reconstructed the utility's water and wastewater accumulated amortization of CIAC balances of $62,567 and $70,421, as of April 30, 1991, for its Pasco County (Summertree PPW) systems. As stated above, there is no evidence of the utility accruing amortization of CIAC for the Pasco County (Summertree PPW) systems prior to 1994. I believe that the $34,854 and $33,018 accumulated amortization of CIAC balances recorded as of December 31, 1993, in its 1994 general ledger are

correcting journal entries to record three years of amortization of CIAC since the utility purchased the Pasco County (Summertree PPW) systems in 1990. The $34,854 and $33,018 divided by three years equal $11,618 and $11,006, respectively, which are the same amounts the utility recorded for amortization of CIAC in 1994. The beginning accumulated amortization of CIAC balances that should have been transferred with the accrual in 1994 may still be combined in the utility's accumulated depreciation balances. Without sufficient utility records, it is impossible to determine.

I recommend that the utility's accumulated amortization of CIAC balance for Pasco County (Summertree PPW) be increased by $27,713 and $37,410, which is the difference between the amount recorded as of December 31, 1993, and the utility's beginning balances as of April 30, 1991. ($62,567 - $34,854 and $70,428 - $33,018) This adjustment, at a minimum, will restate the utility's general ledger balances for water and wastewater accumulated amortization of CIAC to its initial balances as of April 30, 1991.

Audit Exception No. 14 discusses the working capital allowance. The MFR rate base filing includes $1,634,531 for working capital as of December 31, 2001. This amount is allocated as follows: Marion-Water: $114,826, Marion Wastewater: $44,914, Orange Water: $80,701, Pasco Water: $244,252, Pasco-Wastewater: $255,410, Pinellas Water: $31,222, Seminole Water: $397,399, and Seminole Wastewater: $465,807. The utility allocated the working capital balance to the five counties in this proceeding based on the December 31, 2001, year-end O&M expense for each system before any utility adjustments. Rule 25-30.433 (2) and (4), F.A.C., requires that working capital for Class A utilities shall be calculated using the balance sheet approach and that the

averaging method used by the Commission to calculate rate base and cost of capital shall be a 13-month average for Class A utilities. I recommend that the utility's total balance sheet working capital is $208,497 as of December 31, 2001, based on the following audit staff findings. ($1,634,531 - $1,794,693 + $368,659)

- The utility's current assets as of December 31, 2001, are overstated by $1,794,693. The major difference is found in the cash balance. The cash balance presented by the utility is the December 31, 2001, book balance from UIF's general ledger. The balance does not accurately reflect the utility's actual cash balance for UIF in this proceeding because it fails to recognize the recurring electronic transfers of cash from Florida to Illinois where the cash is used to fund continuing operations of the parent and all of its subsidiaries. Additionally, the cash account on UIF's general ledger is only a depository account that is used to accumulate customer payments from all subsidiary operations in Florida before being transferred to the Illinois bank. I calculated a 13-month average actual cash balance of $88,985 as of December 31, 2001, in the Florida bank account and allocated $11,328 or 12.73 percent to UIF for this rate proceeding. The 12.73 percent allocation represents UIF's portion of the total revenues generated by all of the Florida operations in 2001.
- The utility's current liabilities are overstated by $368,659. The major difference is related to deferred income taxes. I removed deferred income taxes from working capital because they are included as a component of the utility's cost of capital in this rate proceeding.
- The utility used the December 31, 2001, year-end balances to calculate

its working capital rather than the 13-month average required in the Commission rule cited above.

- The utility allocated its working capital balance for UIF to the five counties in this proceeding based on the December 31, 2001, year-end O&M expense for each system before its adjustments to test year O&M expense rather than after such adjustments.

Audit Exception No. 15 discusses the Utility adjustments to rate base in the test year. The utility's filing includes rate base adjustments to its December 31, 2001, general ledger that it describes as adjustments related to its last rate case proceeding. I determined that the utility's filing was prepared from its 2001 Annual Report and that the majority of the adjustments are to adjust the general ledger balances to the 2001 Annual Report and MFR filing.

The adjustments to UPIS for Marion, Seminole, and Pasco Counties are adjustments that redistribute common UPIS between the water and wastewater systems that have a minimal impact on overall rate base and should be approved.

The adjustments to accumulated depreciation for all the counties are a combination of the effect of the above-described redistributions and the inclusion of an accumulated depreciation balance for Accounts Nos. 301 and 351, Organization Cost, which the utility does not reflect in its 2001 Annual Report which was used to prepare its MFR filing and should be approved.

The adjustments to CIAC and accumulated amortization of CIAC for Orange County are adjustments that add back $17,592 and $10,709 of utility retirements for the Druid Isle water system that was sold in 1999. The

utility properly recorded the retirements in its general ledger but not in its Annual Report which was used to prepare its MFR filing. The MFR adjustments of $17,592 and $10,709 would misstate the actual balances for Orange County CIAC and accumulated amortization of CIAC and should be removed.

The adjustment to CIAC for Marion County increases the MFR filing by $4,550 to the utility's general ledger balance of $138,914. My analysis of the activity in the utility's CIAC account agrees that CIAC should be increased by $4,550.

The adjustments to accumulated amortization of CIAC for Pasco County reduce its general ledger balance by $35,608 to its 2001 Annual Report balance. The adjustments are a combination of the following two amounts.

- The utility recorded $13,837 to its general ledger which increased the Orangewood balance in 1995. This amount was reported as a test year adjustment in a previous rate proceeding in Docket No. 940917-WS. The utility properly recorded the adjustment in its general ledger but not in its Annual Report which was used to prepare its MFR filing. The MFR adjustment of $13,837 would incorrectly report the actual balance for Pasco County CIAC and should be removed.
- The utility's general ledger balance exceeds its 2001 Annual Report balance by $21,843 for the Summertree PPW system. The utility reclassified its accumulated amortization of CIAC balance for the Summertree PPW system in 1994 when it created a separate account for these balances. In Exception No. 13, I reported that the utility did not properly transfer the correct beginning balance for Pasco County, Summertree PPW and recommended corrective action that would make the $21,843 requested utility adjustment moot.

Therefore, the utility's adjustment should be removed.

The adjustments to CIAC and accumulated amortization of CIAC for Pinellas County increase the respective balances by $3,791 as described below.

- My analysis of the CIAC account balance since its last rate proceeding in Docket No. 930826-WS, indicates that the general ledger balance reflected as of December 31, 2001, is the correct balance and that the $3,791 adjustment to increase CIAC is not warranted and should be removed.
- The utility's $3,791 adjustment in its filing is for a perceived difference between its general ledger and its 2001 Annual Report which was used to prepare its MFR filing and should be removed.
- My analysis of the accumulated amortization of CIAC balance indicates that it never recorded a reported test year adjustment that decreased its accumulated amortization of CIAC balance by $2,139 in its last rate proceeding in Docket No. 930826-WS. I recommend that the utility reduce its accumulated amortization of CIAC balance by $2,139 to record the prior test year adjustment approved in its last rate proceeding.

The utility's adjustments to its Seminole County CIAC water and accumulated amortization of CIAC wastewater accounts increase the respective balances by $1,400 and $59,721 as of December 31, 2001. I have reconciled the adjusted utility balances of $738,562 and $448,273 to its general ledger and I agree with the utility's adjustment.

Audit Exception No. 16 discusses the cost of capital for the parent company. The utility's filing indicates that it has calculated the following weighted average cost of capital as of December 31, 2001, for each of the UIF counties: Marion: 9.34%; Orange: 9.10%; Pasco: 9.29%, Pinellas: 9.19%; and

Seminole: 9.29%.

Kathy Welch is sponsoring testimony in this docket to sponsor an undocketed affiliate transaction audit of Utilities, Inc. and its subsidiary WSC for the 12-month period ended December 31, 2001. Exception No. 10 of the audit report in that investigation recommends specific adjustments to the components of the requested Cost of Capital for the parent, Utilities, Inc. and each of the UIF counties in this rate proceeding.

Audit Exception No. 17 discusses test year revenues. The utility's general service tariff for the Crownwood wastewater system in Marion County states that a customer with a 2-inch general service connection will be charged a Base Facility Charge of $464.51 and a Gallonage Charge of $5.46 per 1000 gallons on a bi-monthly basis.

On December 28, 1999, the utility executed a Bulk Sewer Service Agreement with BFF Corporation to provide wastewater treatment services in accordance with its tariff and sewer service policy. Recital No. 7 of the agreement states that the company shall read the sewer meter(s) and deliver a billing to BFF monthly. BFF Corporation's 2001 Annual Report indicates that it has 98 residential customers and that it purchased $20,892 of sewer treatment services from UIF in the 12-month period ended December 31, 2001. My review of UIF's billing records indicates that BFF Corporation is the sole general service customer for UIF's Crownwood system and that it began providing wastewater treatment service, through a 2-inch wastewater meter, to BFF Corporation as of May 2001. The purchase wastewater agreement between UIF and BFF Corporation, cited above, is in direct conflict with the utility's authorized tariff's stated bi-monthly billing period. The utility's billing

registers reflected that it collected $20,813 of wastewater revenues from BFF Corp. for the eight-month period ended December 31, 2001. A normalized 12-month period would be expected to produce approximately $32,187 in wastewater revenues when calculated using the utility's authorized tariff and a six-month historical average gallonage charge. This would result in an increase of $11,374 to the Marion county test year wastewater revenues.

Audit Exception No. 18 discusses direct Operation and Maintenance Expenses.

The utility's accounting system actively records monthly accruals and reversals for internal financial reporting purposes. USOA Accounting Instruction 2.A. states that each utility shall keep its books of account, and all other books, records, and memoranda which support the entries in such books of accounts so as to be able to furnish readily full information as to any item included in any account.

My review of the utility's purchased power (Account No. 615), purchased water (Account No. 610), and purchased wastewater treatment (Account No. 710) indicates that the utility failed to remove excess accruals and reversals for its MFR filing.

Also, my analysis of the purchased wastewater account for Pasco County indicates that it includes three invoices totaling $23,770 from the City of Sanford, Florida. The $23,770 should be removed and recorded in the Seminole County purchased wastewater account.

My sample of utility operation and maintenance expenses for the 12-month period ended December 31, 2001, revealed three journal entries for invoices totaling $2,614 that the utility could not supply any supporting

documentation. Per the USOA accounting instruction cited above, these amounts should be removed from test year expenses.

My analysis of UIF Cost Center 600, which is discussed in detail in Exception No. 20 of this report, indicates that it includes $3,010 in legal fees that should have been directly charged to Contractual Services - Legal (Accounts Nos. 633 and 733) of the Summertree PPW water and wastewater system in Pasco County. The utility should increase Accounts Nos. 633 and 733 by $2,198.50 and $811.50, respectively, based on the percentage of water and wastewater customers in Pasco County, to properly record the legal fees incurred for the Summertree PPW system.

Audit Exception No. 19 discusses Operation and Maintenance Expense Cost Centers 603 and 639. The utility's accounting system includes two cost centers that are used to accrue and distribute common cost to the specified county systems using a calculated customer equivalent (CE) percentage. Cost Center 603 is named "Orlando office" and distributes to Orange and Seminole counties. Cost Center 639 is named "West Coast office" and distributes to Pasco and Pinellas counties. The utility's records reflect that $20,540 and $9,049 of operation and maintenance expenses were recorded in UIF Cost Centers 603 and 639, respectively, for the 12-month period ended December 31, 2001. My analysis of the two cost centers revealed the following information:

- Cost Center 603 included invoices totaling $1,626 for travel and advertising expenses that were not related to any Orange or Seminole County system.
- Cost Center 639 included invoices totaling $591 for travel expenses that were not related to any Pasco or Pinellas County system and $312 of missing

invoices.

The travel expenses were for employee travel to Panama City, Stuart, and Ft. Myers for work related to other Florida utilities and should be removed from Orange, Pasco, Pinellas, and Seminole Counties operation and maintenance expenses accounts. The advertising expense was for a classified advertisement to recruit wastewater plant operators in Ft. Myers and Panama City which are other Florida utilities and should be removed from the Orange and Seminole Counties operation and maintenance expenses accounts. The missing invoices should also be removed for the same reason as discussed in the previous exception.

Audit Exception No. 20 discusses Operation and Maintenance Expense - Cost Center 600. The utility's accounting system includes cost center 600 that is used to accrue and distribute common cost to Orange, Marion, Pasco, Pinellas, and Seminole counties using a calculated customer equivalent (CE) percentage. The utility's records reflect that $750,857 of operation and maintenance expenses were recorded in UIF Cost Center 600 for the 12-month period ended December 31, 2001. The USOA description for Account 186 states that this account shall include all debits not elsewhere provided for, such as items the proper final disposition of which is uncertain. Commission rule 25-30.433 (8), F.A.C., requires that nonrecurring expenses shall be amortized over a five-year period unless a shorter or longer period of time can be justified. My analysis of cost center 600 revealed that it includes the following costs:

- Invoices totaling $20,825 for extraordinary insurance settlements during the test year that should be removed, deferred, and amortized over a five-year

period, per the rule cited above.

- Invoice totaling $3,010 for legal expenses incurred for the Summertree PPW utility system in Pasco County that should be charged directly to the Pasco County systems.
- Invoices totaling $2,399 for legal fees incurred for the continuing lawsuit involving condemnation proceedings in Seminole County that should be deferred pending final disposition and Commission determination per the NARUC rule cited above.
- Invoice for $3,000 for a yearly computer maintenance program that was performed twice during the test year. It should be removed to normalize the expense to an annual recurring cost.
- Invoice for $1,219 for a permit application fee for Sandalhaven Utilities, Inc. which should be removed from UIF's books and transferred to Sandalhaven's books.
- Journal entry for $5,801 for Nextel Communications. No supporting invoice was provided. The missing invoices should be removed per the audit staff's treatment of similar missing invoices in Exception No. 18.
- Deferred rate case accruals of $19,345 that involves the amortization of $79,354 of legal fees related to the condemnation proceedings in Seminole County mentioned previously and the amortization of $5,066 in fees and capitalized executive time of company officers working on Florida rate case issues. The Seminole County legal fees should be deferred pending final disposition and Commission determination per the NARUC rule cited above.

I recommend that UIF Office Cost Center 600 be reduced by $50,167 for the 12-month period ended December 31, 2001.

Audit Exception No. 21 discusses Operation & Maintenance (O&M) expense allocations. The utility's accounting system includes cost centers 600 (UIF Office) and 601 (Florida office) that are used to accrue and distribute common operation and maintenance expenses to the five counties in this docket as well as all other Florida systems. Utility records reflect that the Cost Center 600 includes $750,857 of expenses for the 12-month period ended December 31, 2001. Of this amount, $311,304 is for accrued operator payroll and benefits. The customer equivalent (CE) percentage incorporates the system(s) where each operator is assigned to work. The balance of $439,553 is allocated to the UIF counties using the CE percentages discussed above.

Utility records also reflect that Cost Center 601 includes $53,534 of expenses for the 12-month period ended December 31, 2001. The entire balance is allocated to the UIF counties using the CE percentages discussed above.

UIF serves as the regional operations center for Utilities Inc.'s (parent) Florida operations. UIF accrues the common O&M costs of its yearly operations in the two cost centers indicated above. Within each cost center, there are specific accounts that accrue the common O&M costs incurred by UIF in its role as the regional operations center. These costs are allocated to all Florida operations, including UIF, using Schedule SE90 for reporting purposes. The allocations are based on customer equivalent percentages. UIF was allocated $158,166, approximately 13 percent, of SE90 common cost for the 12-month period ended December 31, 2001.

Water Service Corporation (WSC), the parent's administrative operations company, allocated $14,640, $36,137 and $98,408 of common cost to UIF which are reflected in WSC Schedules SE51 for computer cost, SE52 for insurance

cost, and SE60 for general and administrative cost for the 12-month period ended December 31, 2001. UIF recorded these allocations in the Sub 600 Cost Center described above.

I recommend that the utility's common costs which are allocated to the UIF systems are overstated by $88,560. Additionally, the utility's allocation of common costs to the UIF systems are materially misstated because of errors in the calculation of its CE percentages for those systems. The $88,560 is determined by the following audit staff adjustments.

- Exception No. 20 of this report removed $50,167 of expenses from Cost Center 600 and should be reflected in this adjustment.
- Kathy Welch is sponsoring testimony in this docket to sponsor an undocketed affiliate transaction audit of Utilities, Inc. and its subsidiary WSC for the 12-month period ended December 31, 2001. The audit report was issued on October 23, 2002. In Exceptions Nos. 2 through 9 of the report, the audit staff reduced the common allocations UIF receives from WSC in Schedule SE51 by $2,728 to $11,912, in Schedule SE52 by $3,963 to $32,174 and Schedule SE60 by $31,702 to $66,706. The total reduction amounts to $38,393 for the 12-month period ended December 31, 2001. I am also including this adjustment.

My analysis of the utility's CE allocation schedule indicates that it did not include 610 customers from the Orangewood water system and understated by 11 the number of wastewater customers in its Summertree PPW system, both of which are located in Pasco County. I have recalculated the CE percentages and the details are included in the audit report.

Audit Exception No. 22 discusses Operation and Maintenance (O&M) expense adjustments to the test year. The utility's MFR filing includes adjustments

to salary and pension & benefits for its 12-month period ended December 31, 2001. The utility's filing states that the salary expense and associated pension and benefit (PB) expense adjustments reflect the difference between year-end expense and present year expense for the utility system operators and UIF office staff. The utility provided the audit staff with detailed schedules that compared the year-end 2001 salary and PB expense to the present year actual expense and calculated the proposed test year adjustments. The schedules illustrated its adjustments for utility system operators, UIF office staff, and WSC office staff salaries and PB expenses. My review of the utility's schedules revealed two errors that materially misstate what the proposed salary and PB expense adjustments should be.

- The utility prepared five separate schedules to calculate the salary and PB expense adjustment for each of the five counties in this rate proceeding. All of the counties except for Pasco County were allocated 14 percent of the UIF office salary and PB expense based on a revised customer equivalent (CE) percentage.
- The utility allocated the UIF office staff and WSC office staff salaries and PB expense to the five counties in this rate proceeding based on the regional vice president's estimate of time that he spends on each Florida utility system. The current test year UIF office staff and WSC office staff salaries and PB expense are allocated based on CE percentages.

I recalculated the utility's adjustment to O&M salary and PB expense and corrected the above-mentioned errors. The audit report includes the details of these adjustments.

Audit Exception No. 23 discusses Operation and Maintenance (O&M) expense

adjustments to the test year for Seminole county. The utility's wastewater treatment plant at Lincoln Heights in Seminole County was removed from service on July 1, 2001. The utility at that time began purchasing wastewater treatment services from the City of Sanford, Florida. The utility's MFR filing includes an adjustment that increases test year O&M expense for the 12-month period ended December 31, 2001, by $100,296 in Seminole County. The utility's MFR filing states that the adjustment was to reflect an increase in O&M expense due to the wastewater interconnection with the city. My analysis of the effect of the wastewater interconnection with the City of Sanford, Florida, has determined that the following adjustments to 2001 test year O&M expenses for Seminole County should be recorded for this rate proceeding to properly account for the change in utility service described above.

- Account 710: Normalize purchased wastewater expense - $55,032. I started with the utility's actual 14-month average purchased wastewater expense of $11,840.52 (July 2001 to August 2002) and calculated a 12-month average of $142,086.24. I compared this to the test year 2001 actual purchased wastewater treatment expense of $87,054.38 and calculated an adjustment of $55,031.82 to purchased wastewater treatment expense.
- Account 715: Remove purchased power expense for treatment plant and include normalized purchased power expense for the new transfer lift station - ($8,461). I started with the utility's actual 6-month average purchased power for the new transfer station of $61.85 (July 2001 to December 2001) and calculated a 12-month average of $742.18. I compared this to the test year 2001 actual wastewater treatment plant purchased power of $9,203.64 and calculated an adjustment of (8,461.46) to total purchased power expense.

- Account 720: Remove percolation pond maintenance expense - ($2,700)
- Account 720: Remove sludge hauling expense - ($17,830)
- Account 742: Remove wastewater testing expense - ($6,496)

For the last three, I removed all expenses related to the wastewater treatment plant that are no longer required. The total of these five adjustments is $19,545. The utility's adjustment to test year O&M expense for Seminole County wastewater should be reduced by $80,751.

Audit Exception No. 24 discusses Property taxes. The utility's MFR filing includes $48,634 for property taxes for the five counties that are party to this rate proceeding. The property taxes are composed of real estate and tangible personal property taxes levied on the utility's property in the five counties for the test year 2001. Included in the amount is a reduction of $3,102 against the tangible property taxes levied on UIF's administrative office that is located in Seminole County. This amount was allocated to the other Florida utility operations in Schedule SE90. My analysis of the utility's property taxes indicates that, of the $48,634 of property taxes mentioned above, $39,034 can be directly traced to a specific utility system. The balance of $9,600 is composed of $7,069 in real property taxes and $3,564 in tangible personal property taxes on the UIF administrative office, $2,069 for allocated property taxes from WSC and the reduction of $3,102 in the tangible personal property tax which is allocated to the other Florida utility operations in Schedule SE90. I determined that the following adjustments are required to properly reflect the actual property tax expense incurred for each respective system.

- The utility should record the $39,034 of property taxes directly to each

UIF system.

- The WSC allocated property taxes of $2,069 should be allocated to each UIF system using the audit staff's corrected allocation formula discussed in Exception No. 21.
- The UIF administrative office real property taxes of $7,069 should be reduced by 87 percent or $6,150, which is the allocation method used by the utility in Schedule SE90, to allocate the real property taxes to all of the other Florida systems that it supports. The balance of $919 should then be allocated to each UIF system using the audit staff's corrected allocation formula discussed in Exception No. 19.

Audit Exception No. 25 discusses Taxes Other Than Income adjustments to the test year. The utility's MFR filing includes payroll tax expense adjustments of $47,763 to its 12-month period ended December 31, 2001. The utility's MFR filing states that the payroll tax expense adjustments reflect the difference between year-end expense and present year expense for the utility system operators and UIF office staff. The utility provided the audit staff with detailed schedules that compared the year-end 2001 payroll tax expense to the present year actual expense and calculated the proposed test year adjustments. The schedules illustrated the adjustments for the utility system operators, UIF office staff, and WSC office staff. My review of the utility's schedules revealed two errors that materially misstate what the proposed salary and PB expense adjustments should be.

- The utility prepared five separate schedules to calculate the payroll tax expense adjustment for each of the five counties in this rate proceeding. All of the counties except for Pasco County were allocated 14 percent of the

UIF office and WSC office payroll tax expense based on a revised customer equivalent (CE) percentage.

- The utility allocated the UIF office staff and WSC office staff salaries and PB expense to the five counties in this rate proceeding based on the regional vice president's estimate of time that he spends on each Florida utility system. The current test year UIF office staff and WSC office staff payroll tax expense are allocated based on CE percentages.

I recalculated the utility's proposed adjustment and the audit report indicates the details for each system.

Audit Exception No. 26 discusses the utility's books and records. I conducted an undocketed compliance investigation of Wedgefield Utilities, Inc.'s books and records as of December 31, 2001. The audit report was issued on August 23, 2002. The scope of the compliance investigation included the determination of Wedgefield Utilities, Inc.'s compliance with Order No. PSC-00-1528-PAA-WU, issued August 23, 2000, and Order No. PSC-00-2388-AS-WU, issued December 13, 2000, in Docket No. 991437-WU. Order No. PSC-00-1528-PAA-WU required the utility to show cause as to why it should not be fined $3,000 for its apparent violation of Rule 25-30.115, F.A.C. The utility filed a timely response and an offer of settlement on September 13, 2000. Order No. PSC-00-2388-AS-WU incorporated the above-mentioned settlement offer with other specific requirements and waived the fine imposed in the Order to Show Cause. Specifically, the utility was ordered to, "correct any remaining areas of noncompliance with the NARUC USOA by January 31, 2001." Exception No. 1 of the compliance investigation audit report determined that Wedgefield Utilities, Inc. was not in substantial compliance with the above Orders and

deferred its recommendation to this rate case proceeding. The utility's position, in summary, states that the utility believes that its books and records are in substantial compliance with NARUC USOA and that the Utility is not aware of any specific corrections required by Staff or the PSC.

The settlement offer, approved in Order No. PSC-00-2388-AS-WU, states that:

> The utility has determined that there are a few accounts remaining, especially Utility Account Nos. 620 and 675, which the Utility may not be utilizing totally in accordance with NARUC Uniform System of Accounts.
>
> The Utility further promises to sufficiently correct these differences by January 31, 2001, if given some guidance by the FPSC audit staff.

Additionally, Order No. PSC-00-2388-AS-WU states that:

> The utility shall correct any remaining areas of non-compliance with the NARUC USOA by January 31, 2001. Further, the utility and its parent shall file, in future rate proceedings before this Commission, MFR which begin with utility book balances, and show all adjustments to book balances after the "per book" column in the MFR. The utility shall file a statement which affirms that the MFR begin with actual book balances.

I believe that the utility's book and records are not in substantial compliance with the NARUC USOA, and the utility has not complied with Order Nos. PSC-00-1528-PAA-WU and PSC-00-1528-PAA-WU, referenced above. My findings are as follows:

- Exception No. 1 for the compliance investigation mentioned above determined that the utility was not in substantial compliance with the stipulated agreement approved in Order No. PSC-00-2388-AS-WU. I determined that the utility's response indicated that no changes have been made to the accounting system in order to comply with the Commission Order.
- Order No. PSC-00-2388-AS-WU, by reference, incorporates the filing requirements for future rate proceedings to the parent and all of its Florida operations. The utility's MFR filing does not comply with filing requirements in the Orders mentioned above. Rate Base Schedules A1, Column (2) Balance per Books, which should be the balance in the utility's general ledger, begins with the balances that the utility reports in its 2001 Annual Report. These balances are not always the same as the General Ledger balances. In addition, as indicated in previously discussed Exceptions, the utility has not consistently recorded adjustments from Commission orders in a timely manner
- Order No. PSC-00-1528-PAA-WU, specifically addressed the utility's noncompliance with NARUC, Accounting Instruction 2. A. and Rule 25-30.450, F.A.C., concerning supporting documentation for the utility's books and records, schedules, and data that it files in rate proceedings. In this rate proceeding, the audit staff requested supporting documentation for the utility's allocation methodologies three different times and was given two additional schedules that did not reconcile to the filing. I was the audit manager of the affiliate transaction audit of Water Service Corporation (WSC), the service operating company for UIF's parent, for the 12-month period ended December 31, 2001. Disclosure No. 2 of the report determined that the utility lacked sufficient supporting documentation, that should have been readily

available, to adequately determine the reasonableness of the utility's methodology in calculating its customer equivalent (CE) percentages which are used to allocate common rate base and cost.

- The utility has a four-step policy for retirement of Utility Plant In Service (UPIS). The utility appears to be inconsistent in applying its policy. I discussed this more fully in Exception No. 4 where I found $299,017.94 of additions which did not have corresponding retirements. It was also discussed in the undocketed affiliate audit, Exception No. 1, sponsored by Kathy Welch where she found inadequate documentation regarding the disposition of old computers that are either transferred or destroyed when new ones are purchased.
- The structure of the utility's accounting system continues to require significant amounts of the audit staff's time to reconcile its MFR filing to its books and records. The combined MFR filings for all UIF systems readily reconciles to UIF's consolidated general ledger. However, UIF's distributions and allocations from and between the five counties, its other Florida operations, and its parent are of concern to the audit staff. Accounts Nos. 620 and 720, Materials and Supplies, and 675 and 775, Miscellaneous Expenses, which were specifically identified in the utility's offer of settlement, continue to require extraordinary audit staff attention to audit because of the number of utility accounts involved and the allocation methodologies applied. For example, Account No. 620/720 includes the following 45 utility accounts:

401.1u: 6759200, 6759210, 6759220, 6759230, 6759240, 6759250, 6759260, 6759290, and 6759295 (These accounts are allocated to MFR Accounts Nos. 620

and 720.)

401.1x - 6755070, 6755090, 6759503, 6759506-7, and 6759509 (These accounts are allocated to MFR Account No. 620.)

401.1y - 7754003, 7754006, 7754007, 7754009, 7755070, and 7758490 (These accounts are allocated to MFR Account No 720.)

401.1z - 6205003, 6751009, 6753008, 6753011, 6754007, 6759017-19, 6759080, 6759081, 6759401-2, 6759405-6, 6759410, 6759412-16, 6759430, 6759490, 6759498, and 7202003 (These accounts are allocated to MFR Accounts Nos. 620 and 720.

All of the above account balances are allocated to the water and wastewater systems of the five counties in this rate proceeding based on the CE percentages described in Exception No. 21 of this report. However, the following accounts are first reduced by the Schedule SE90 allocation discussed in Exception No. 21 of this report. The remaining balance is then allocated as previously indicated.

401.1u: 6759210, 6759220 and 6759290

401.1z: 6205003, 6759018, 6759416 and 6759430

The audit staff encountered problems conducting an efficient audit of the utility's books and records for this filing and expended a considerable amount of time reconciling the filing to the utility's MFR and prior Orders. I recommend that the Commission readdress this issue and require the utility to maintain its books and records per the NARUC USOA and Commission rules.

Q. Please review the audit disclosures in the audit report.

A. Audit Disclosure No. 1 discusses the Lincoln Heights land condemnation proceedings. Utility records reflect that it has been involved in a lawsuit involving the condemnation and subsequent acquisition of a significant portion

of its land located at the Lincoln Heights system in Seminole County. The utility began incurring legal and engineering fees related to the condemnation as early as February 1998 when it created Construction Project (CP) Account No. 614-116-98-14 to accrue its consulting, engineering, legal, and relocation costs for the condemnation issue. At that time, the utility projected a total cost of $148,000. Utility records indicate that in 2001 the utility closed out the above CP by transferring a balance of $101,518 to Seminole County wastewater Account No. 353, Land. I made specific adjustments to this transaction in Exception No. 5 of this audit. I reclassified the entire balance of $101,518 to other utility accounts. Specifically, I transferred $14,935 of preliminary cost studies to Account No. 183.

Utility records indicate that in 2000 the utility recorded $2,952 to Account No 301, Organization Cost, and in 1999 and 2000 the utility recorded $9,724 and $9,579 to Account No. 380, Treatment and Disposal Equipment, for capitalized executive time that related to the condemnation proceeding described above. I made specific adjustments to these transactions in Exception No. 6 of this audit. I reclassified the entire balance for all three transactions to Account No. 186, Miscellaneous Deferred Debits.

Utility records indicate a balance of $79,356 in Account No. 1863030, Deferred Rate Case Expense, as of December 31, 2001, for legal fees related to the condemnation proceeding described above. This balance, along with a balance of $5,006 recorded in Account No. 186321, Deferred Rate Case Expense, was amortized to the five counties in this rate proceeding as described in Exception No. 20 of this audit. I also made specific adjustments that removed $19,345 of test year amortization expense related to the condemnation legal

fees and deferred a net amortized balance of $38,687.

My discussions in Exceptions Nos. 5, 6 and 20 have reclassified and deferred $96,277 of costs related to the condemnation lawsuit per the NARUC and Commission rules cited in Exception No. 5. I also discovered the following additional information related to this issue.

- The utility properly retired $6,000 of land from Account No. 351 to record the effects of its land being acquired by the Department of Transportation (DOT) as discussed in Exception No. 9. However, I discovered that the utility received $154,190.33 on June 22, 1999, from the DOT as compensation for the land it acquired from the utility. The utility does not reflect this event anywhere in its MFR filing.
- The utility closed out CP Account No. 614-116-98-14 for $101,518 as of December 31, 2001. However, utility representatives indicate that the lawsuit is still ongoing. I have not determined where the additional legal fees are being recorded.

I recommend that the above costs and all future costs related to this issue be reviewed for prudency and relevance to the five counties in this rate proceeding.

Audit Disclosure No. 2 discusses the WisBar/Bartelt interconnection with Orangewood. The utility's records reflect that the WisBar/Bartelt water system operation and maintenance expense Account No. 610, Purchased Water, included $7,904.54 of expenses from Holiday Gardens Utility, Inc. for the 12-month period ended December 31, 2001. On October 10, 2002, the audit staff conducted a tour of selected utility systems with UIF's assistant operations manager. He informed us that the WisBar/Bartelt system had been

interconnected with the utility's Orangewood water system as of this summer and that UIF would no longer need to purchase water from the Holiday Gardens system in the future. However, he also stated that the interconnection with Holiday Gardens will remain in place as an emergency source of supply for either system. The utility's construction ledgers indicate that the utility had incurred costs of $12,908 to interconnect the Orangewood and WisBar/Bartelt systems as of December 31, 2001, in Work Order No. 614-116-98-14. I have provided this information for use in this case. I have not made a recommendation in this matter.

Q. Does this conclude your testimony?

A. Yes, it does.

MS. GERVASI: Then staff would call Kathy L. Welch to the stand.

KATHY L. WELCH

was called as a witness on behalf of the Staff of the Florida Public Service Commission and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MS. GERVASI:

Q Ms. Welch, have you been sworn in?

A Yes.

Q Would you please state your name and business address for the record.

A My name is Kathy Welch. My business address is 3625 Northwest 82nd Avenue, Suite 400, Miami, Florida 33166.

Q And are you the same Kathy Welch who prefiled or caused to be prefiled direct testimony in this docket consisting of 13 pages?

A Yes, I did.

Q Do you have any changes or corrections to make to your testimony?

A No, I don't.

Q If I were to ask you the same questions as posed in your testimony, would your answers be the same today?

A Yes, they would.

MS. GERVASI: May we please have Ms. Welch's prefiled

direct testimony inserted into the record as though read.

COMMISSIONER DEASON: Without objection, it shall be so inserted.

BY MS. GERVASI:

Q Ms. Welch, did you also prefile Exhibits KLW-1 and KLW-2?

A Yes, I did.

MS. GERVASI: May we please have those exhibits marked for identification with the next available exhibit number.

COMMISSIONER DEASON: Yes. Composite Exhibit 19.

(Exhibit 19 marked for identification.)

DIRECT TESTIMONY OF KATHY L. WELCH

Q. Please state your name and business address.

A. My name is Kathy L. Welch and my business address is 3625 N.W. 82nd Ave., Suite 400, Miami, Florida, 33166.

Q. By whom are you presently employed and in what capacity?

A. I am employed by the Florida Public Service Commission as a Public Utilities Supervisor in the Division of Auditing and Safety.

Q. How long have you been employed by the Commission?

A. I have been employed by the Florida Public Service Commission since June, 1979.

Q. Briefly review your educational and professional background.

A. I have a Bachelor of Business Administration degree with a major in accounting from Florida Atlantic University and a Masters of Adult Education and Human Resource Development from Florida International University. I have a Certified Public Manager certificate from Florida State University. I am also a Certified Public Accountant licensed in the State of Florida and I am a member of the American and Florida Institutes of Certified Public Accountants. I was hired as a Public Utilities Analyst I by the Florida Public Service Commission in June of 1979. I was promoted to Public Utilities Supervisor on June 1, 2001.

Q. Please describe your current responsibilities.

A. Currently, I am a Public Utilities Supervisor with the responsibilities of administering the District Office and reviewing work load and allocating resources to complete field work and issue audit reports when due. I also supervise, plan, and conduct utility audits of manual and automated accounting

systems for historical and forecasted financial statements and exhibits.

Q. Have you presented expert testimony before this Commission or any other regulatory agency?

A. Yes. I testified in the following cases before this Commission: Tamiami Village Utility, Inc. rate case, Docket No. 910560-WS; Tamiami Village Utility, Inc. transfer to North Fort Myers, Docket No. 940963-SU; General Development Utilities, Inc. rate case, Docket No. 911030-WS; Transcall America, Inc. complaint, Docket No. 951232-TI, Econ Utilities Corporation transfer to Wedgefield Utilities, Inc., Docket No. 960235-WS, Gulf Utility Company rate case, Docket No. 960329-WS; the Fuel and Purchased Power cost recovery clause case, Docket No. 010001-EI; and The Woodlands of Lake Placid, L.P. staff-assisted rate case, Docket No. 020010-WS.

Q. What is the purpose of your testimony today?

A. The purpose of my testimony is to sponsor the staff audit report of the allocations among the affiliated companies of Utilities, Inc. and Utilities, Inc. of Florida (UIF, or utility) in Marion, Orange, Pasco, Pinellas, and Seminole Counties, Docket No. 020071-WS. The audit report is filed with my testimony and is identified as KLW-1.

Q. Was this audit report prepared by you or under your supervision?

A. Yes, I was the primary auditor in charge of this audit.

Q. Please review the work you performed in this audit.

A. For rate base, I examined plant for Water Service Corp. from December 31, 1995 forward, by selecting invoices and tracing to source documents. I also recalculated depreciation using Commission rates and reviewed allowance for funds used during construction. I determined the allocation methodology

and reviewed it for reasonableness. For cost of capital, I compiled the components of cost of capital from consolidated Utilities, Inc. ledgers and tested interest expense by tracing to bank statements and notes. For net operating income, I examined selected expense accounts and judgmentally traced sampled amounts from the ledger to invoices. I also determined the current payroll and compared it to the prior year. I reviewed expenses for items that were nonrecurring because of a recent reorganization. I determined the allocation methodology and reviewed it for reasonableness. I reviewed expenses to determine if they were merger-related, nonrecurring items, acquisition costs, or if they should have been charged to a particular division as opposed to being allocated. I also scanned the process used to record all costs related to one acquisition. I recalculated the allocation methodology and the amounts charged to Florida and reconciled these to the filings. I also obtained supporting documentation for the sources of the components used to calculate the allocation factors and determined that the factors were consistently applied from year to year.

Q. Please review the audit exceptions in the audit report.

A. Audit Exceptions disclose substantial non-compliance with the National Association of Regulatory Utility Commissioners (NARUC) Uniform System of Accounts (USOA), a Commission rule or order, and formal company policy. Audit Exceptions also disclose company exhibits that do not represent company books and records and company failure to provide underlying records or documentation to support the general ledger or exhibits.

Audit Exception No. 1 discusses rate base invoices that were missing and inventory transfers that were not recorded. When I was testing Water Service

Corporation's (WSC) rate base additions, the company could not locate some invoices. In addition, when I was auditing the supporting documentation for computer costs, I found two problems. One was that the company could not locate some invoices and the second was that some equipment transfers or retirements were never posted to the ledgers. When I reviewed the invoices that were found, I noted that new computers replaced old ones which were either transferred or destroyed. I asked the company to prove that these retirements and transfers were booked. It provided a transfer entry for August 31, 2000, and said that no other support existed. The entry did not contain detail as to which computers were being transferred or retired. The company finally provided a list of all transfers and retirements by inventory number. The transfers out of WSC were traced to ledger entries of the same amount for all the years. Because several entries had similar dollar amounts, the exact entry could not be determined. The transfer report contained $120,817.53 of entries that could not be traced to the ledger and therefore never posted. Most of these items were transferred to other divisions. $71,434.83 of the items on the transfer report were for items that were destroyed and therefore debited to accumulated depreciation. The company also provided an inventory dated August 14, 2002, for computer equipment for WSC. The inventory totals $589,322.24. Rate base shows the mainframe computer at $377,085 and minicomputers at $473,693 for a total of $850,778. As detailed further in the audit report, I recommend that the WSC plant should be reduced by the $8,817.35 for invoices not located, and the associated accumulated depreciation should also be reduced. I also recommend that the WSC plant should also be reduced for computer equipment by the $56,774 for invoices that

could not be located and the $120,817 of transfers that were never recorded. I further recommend that computer equipment and accumulated depreciation should reflect a zero balance as of December 31, 2001, for the following reasons.

1) The company could not provide the purchase dates for the computers on its inventory list that would have enabled the Commission to determine the amount of accumulated depreciation relating to its computer equipment

2) When you apply the adjustments recommended above to the company's current balances for mainframe and minicomputers, it creates a negative rate base balance since accumulated depreciation would exceed the balance in both accounts.

Therefore, I have set both accounts and respective accumulated depreciation to zero as displayed in Exhibit I of the audit report. Since the plant appears to be fully depreciated after the adjustments are made, computer depreciation expense of $63,482 should also be removed from expenses. I also recommend that the utility improve the procedures for recording retirements and transfers and expand its inventory data base to include dates of purchase.

Audit Exception No. 2 discusses interest expense. The company included interest expense and interest income in the Water Service Corporation costs which are allocated to the utility divisions. Interest expense is recorded in Account 4192000 and totals $392,910. Interest income is the interest on the cash accounts and is recorded in Account 4272090 and totals $9,426. The Commission does not include interest expense in recoverable expenses because the cost of capital calculation used allows a return sufficient to cover the

interest expenses related to the rate base investment. Interest income is included when cash accounts are included in working capital (see Commission Order No. PSC-96-1404-FOF-GU, issued November 20, 1996 in the City Gas rate case, Docket No. 960502-GU and Order No. PSC-96-1320-FOF-WS issued October 30, 1996 in a Southern States rate case, Docket No. 950495-WS.) The company has not included any working capital for Water Service Corporation. Therefore, I recommend that the interest expense and income should be removed from the income statement and not allocated to the utility divisions.

Audit Exception No. 3 discusses audit fees. The year end balance of account 6329002 contains audit fees paid to Arthur Anderson. The company accrued $132,000 in this account. The invoices showed total audit fees for the year 2000 audit of $119,400. The difference is $12,600. I asked the company why there was a difference in the account and if its fees would increase for the 2001 audit. The response stated that the $119,400 is the actual cost and no increase in costs had been determined. Account 6369090, Other Outside Services, also includes an invoice from Arthur Anderson for $7,550. This invoice is related to the review of year 2000 acquisitions. Acquisition costs are included by the company in a preliminary survey account and then allocated to capital accounts at the individual utility division. I recommend that since the company did not provide any reason for the difference in costs in Account 6329002, the account should be reduced by $12,600. Further, acquisition costs should be charged to the individual divisions. Therefore, allocated costs from Account 6369090 should be reduced by $7,550.

Audit Exception No. 4 discusses directors' fees. Account 6369008 in

Water Service Corp. includes directors' fees of $116,500. Utilities, Inc. has been purchased by Nuon Acquisition Sub, Inc. Since the takeover, the number of directors has been reduced from six to three. Since rates are set on a going-forward basis, expenses should reflect the costs that will be in effect when the new rates are implemented. Costs for directors' fees are expected to be $18,000 (an annual fee of $6,000 times three directors), and $42,000 for meeting fees ($3,500 per meeting times three directors times 4 meetings.) This totals $60,000 on an annual basis. The actual directors' fees in the year 2001 were $116,500, for a difference of $56,500. I recommend that the cost be reduced on a going-forward basis by $56,500.

Audit Exception No. 5 discusses finder's fees. The company provides finder's fees for information about systems that can be purchased. In a prior rate case for Mid-County Services, Inc., Docket No. 971065-SU, the Commission issued Order No. PSC-98-0524-FOF-SU, on April 16, 1998, and removed these costs from rate base but allowed them as expenses. The average rate base included in the MFRs included $46,529 for the deferred portion of employee finder's fees. The company included $21,615 of these costs in expenses in Account 636006, Employee Finder's Fees and allocated this to all systems. I believe these costs should be charged to the acquisition costs of the system being purchased and should be removed from expenses. Since they can be identified with a particular system, they should not be allocated through a process that is for common costs.

Audit Exception No. 6 discusses FICA expenses. Account 4081201 showed FICA expenses at $246,309. These costs were allocated to the utility divisions. I calculated actual FICA costs for Water Service Corp. using 7.65

percent of salaries up to a maximum salary level of $80,440. The total was $122,911.71 or $123,397.29 less than the booked amount. The company did not allocate any of this account to capitalized wages, computers, or customer service expense. I recommend that the expense account should be reduced by $123,397.29. I reviewed the division FICA costs to determine if there is a misallocation that would result in the division costs being understated. This was not the case. The company response indicated that an error had been made in booking the costs. No further explanation was provided. The audit report includes an adjustment to payroll and benefits for the Northbrook office, detailed for each division.

Audit Exception No. 7 discusses payroll and benefits. Utilities, Inc. was taken over by Nuon Acquisition Sub, Inc. in 2001 and several employees left the company. The company made "change of control pay-outs" in 2001. The net payroll at December 31, 2001, is more than the annual salary for staff employed at June 30, 2002, because several employees left and were not replaced. The total reduction is $220,022.50 for salaries, $10,288.70 for FICA, $6,600.68 for pension and $6,671.45 for the Employee Stock Option Plan (ESOP). The actual salaries are charged to three allocation pools: computers, customer service, and regular administrative and general. The administrative and general salaries were adjusted by the company for capitalized salaries. No adjustment was made to charge payroll taxes, pension or employee benefits to these allocation groups. I recommend that the FICA and pension benefits related to the capitalized salaries should be removed and capitalized since they create a mismatch of payroll and related expenses. The audit report details the specific adjustment amounts that should be made.

Audit Exception No. 8 discusses training costs charged to Water Service Corp. Account 7048055, Office Education Training includes $7,849.96 for tuition for David Orr who is a Florida employee. This account was allocated using allocation factor five. The allocated costs should not include those costs that relate to a specific state or division. Therefore, I recommend that the $7,849.96 be removed from Water Service Corp. expenses.

Audit Exception No. 9 discusses Northbrook employees life insurance. The life insurance charged through Water Service Corp. included some insurance for officers who are no longer with the company. These costs total $6,427.21. Commission Order PSC-98-0524-FOF-SU, issued April 16, 1998, removed life insurance where the utility is the beneficiary and fiduciary policies protecting directors, officers, and pension funds. The amounts for these policies, added to the nonrecurring costs of $6,427, total $104,112. I recommend that this amount be removed from allocated expenses.

Audit Exception No. 10 discusses cost of capital. The company included a credit for accumulated deferred taxes of $339,113 in rate base. The Commission routinely includes deferred taxes in the capital structure at zero cost (see Commission Order No. 11487, issued January 5, 1983, in Docket No. 820014-WS, rate case for Avatar Utilities, Inc of Florida, Barefoot Bay Division.) In addition, the amount the company included is the portion of deferred taxes that relates to Water Service Corp. and is not the consolidated Utilities, Inc. balance. The MFRs in this case included $2,788 for deferred taxes in all counties except Marion, on Schedule D-1. I believe this is the average of Account 237 for one division, which is accrued interest. The company also has a regulatory asset that offsets deferred taxes. The average

balance for the consolidated Utilities, Inc. deferred income tax is $16,345,859, net of the regulatory asset. The company also has unamortized investment tax credits averaging $1,318,251.

All counties used an amount for customer deposits that did not agree with the division's general ledger. The audit report details the specific differences. I used the general ledger balances for the customer deposits for the five counties in Exhibits VII through X of the audit report.

I also reviewed the notes related to short-term debt. I determined that the amounts in MFR Schedule D-4 for short-term debt did not agree to the MFR Schedule D-1. The company corrected this in the revised filing but included an adjustment to interest that removed interest related to acquisitions. I used the bank statements to calculate an effective rate for short-term debt of 5.18 percent and used the 13-month average balances from the general ledger.

I traced long-term debt in MFR Schedule D-5 to the notes. I could not reconcile it to the lead schedules. In addition, a note paid off during the year was left off of MFR Schedule D-5. I recalculated MFR Schedule D-5 using all notes and the 13-month average balances from the general ledger. The effective rate is 8.63 percent.

The company used different rates of return for equity for each division. The equity ratio should be the same for all companies so using the formula should provide the same rate for all companies. The equity rate for all companies was changed to 10.914 percent based on the Consummating Order PSC-02-1252-CO-WS, issued September 11, 2002 and Proposed Agency Action Order PSC-02-0898-PAA-WS, issued July 5, 2002.

My calculated overall weighted cost of capital for Utilities, Inc. is 8.42 percent. I calculated the weighted cost rates for the five Utilities, Inc. of Florida counties using a portion of the consolidated deferred taxes. These rates are: Marion - 8.39%; Orange - 8.29%; Pasco - 8.40%; Pinellas - 8.38%; and Seminole - 8.39%. I also calculated the weighted cost rates for the five Utilities, Inc. of Florida counties using the direct deferred taxes, by division. These rates are: Marion - 4.96%; Orange - 4.96%; Pasco - 5.22%; Pinellas - 4.93%; and Seminole - 5.94%. The schedules calculating these rates are attached as Exhibit KLW-2.

Q. Please review the audit disclosures in the audit report.

A. Audit Disclosure No. 1 discusses Allowance for Funds Used During Construction. Water Service Corp. capitalized interest for a few projects over the years. These costs are included in plant allocated to the subsidiaries. There is no approved AFUDC rate for Water Service Corp. However, there are approved rates for Seminole, Orange, Pasco, Marion and Pinellas Counties. The capitalized rates used at Water Service Corp. are higher than the rates approved for the counties. The rates range from 8.61 percent to 9.01 percent. However, the difference is immaterial and after an allocation to each division, the amount would not be material. I performed no additional follow-up work. However, if the company requested one rate for the entire company, this problem would be eliminated.

Audit Disclosure No. 2 discusses Water Service Corp. allocation factors. Water Service Corp. allocates rate base and expenses using 11 different allocation factors. Most of these factors are based on the customer equivalent factor. To determine customer equivalents, the company records

single family equivalents for each development as of the end of June of the year the allocation is to take place. It then determines the customer equivalents by taking the single family equivalents and adjusting it to one half for the following reasons.

1. The division has both water and wastewater. The wastewater is counted at one half.

2. The customer is an availability customer only. The customer is counted at one quarter.

3. The water company is distribution only. The customer is counted at one half.

4. The wastewater company is collection only. The customer is counted at one half.

The company could not provide a formula or methodology for determining the single family equivalent number. The company is also the contract operator for two water plants and three wastewater plants. According to a company representative, no costs were ever allocated to these operations.

I believe that the lack of a formalized methodology for determining single family equivalents can cause inconsistency between divisions. According to a company representative, the company determines the estimated gallons at the time of purchase and inputs a number for single family equivalents based on gallons. This may not be based on the same number of gallons per single family as a different person may use the next year or year after. The company did not state how the single factor equivalent is adjusted for new customers. I attempted to determine gallons of water purchased and pumped and gallons of wastewater treated so that I could determine my own

calculation of equivalent residential connections (ERCs) for each company. I planned on using these ERCs to prepare my own customer equivalent schedule and to compare it to the Florida allocations using customer equivalents. If it was significantly different, almost all 11 allocation factors would have to be redone. The company could not provide gallons of wastewater treated for states other than Florida. It claimed that operating reports were not available to provide the information. In addition, some small water plants did not have usage reports. The report of number of customers that the company provided showed water customers and did not break down wastewater number of customers by division. Therefore, I was unable to determine ERCs and unable to determine if the company's computation is reasonable. I believe that the company should be required to provide to the Commission the calculation based on ERCs using a method consistent between each division. The ERC calculation should be compared to the customer equivalent factors provided by the company to determine if the company allocation methodology is reasonable. If not, the company should revise all 11 allocation factors so that the allocations of expenses and rate base can be reallocated. The allocation methodology also needs to allocate costs to the divisions that the company is acting as a contract operator and billing agent for.

Q. Does this conclude your testimony?

A. Yes, it does.

BY MS. GERVASI:

Q Have you prepared a summary of your testimony?

A Yes, I have. The purpose of my testimony is to submit my prefiled exhibits and my testimony into the record. And my work was done to support my audit of the affiliate transactions of Utilities, Inc. and WSC Corp. (sic).

MS. GERVASI: Thank you. We'll tender the witness for cross-examination.

COMMISSIONER DEASON: Mr. Burgess.

CROSS EXAMINATION

BY MR. BURGESS:

Q Good afternoon, Ms. Welch.

A Hello.

Q Am I correct that in -- under regulatory philosophy, allocations from affiliates would bear particular scrutiny, more scrutiny perhaps than expenses incurred from arm's-length transactions?

A That's true.

Q Isn't there as well a Public Service Commission rule that basically recognizes that by requiring certain specific items to be filed by companies with regard to allocations when a company is in for a rate case?

A Yes.

Q You're familiar with that rule? You're familiar with most of the items that are included in that?

A Yes.

Q And as part of that, is part of that additional scrutiny that led to the purpose -- or that is the purpose for the audit that you undertook?

A Yes.

Q With regard to that audit, I would like to ask you some specific questions of your findings, and most of what I have to ask is from Audit Disclosure Number 2. So if I could get you to refer -- do you have a copy of your audit?

A My box is over here.

Disclosure 2?

Q Audit Disclosure 2, yes, ma'am.

A Uh-huh.

Q Now, am I correct that in allocating its expenses the company used, depending on the particular expense involved or expenditure involved, the company used 1 of 11 different methods or some combination thereof; is that correct?

A That's true.

Q And am I correct that the vast majority of the allocations involved the customer equivalent factor; is that correct?

A That's true, as part of the allocation.

Q As part of the allocation.

Am I correct as well that the customer equivalent factor is derived in some fashion or another from the single

family equivalents; is that correct?

A That's true.

Q So the single family equivalents -- the measure of the single family equivalent is the lynchpin of a large amount of the allocated expenditures and expenses; is that correct?

A True.

Q Given that, when you began this audit, did you expect to find some documentation as to the calculation of the single family equivalent?

A I did.

Q Did you seek to obtain that from the company?

A I did.

Q Were you able to obtain documentation to that effect?

A I received an e-mail about the single family equivalents. That was the only documentation I actually received about single family equivalents.

Q Can you tell me the nature of that e-mail?

A If I can refer to my work papers, I can.

Q Thank you.

A It's an e-mail from Steve Lubertozzi, and it has single family equivalents, and it has an example of how it was computed. It was supposed to be what the billing department had on file about how the single family equivalent was computed.

Q When I look at your Audit Disclosure Number 2, it

indicates that the company could not provide a formula or methodology for determining the single family equivalent number. Should I understand then that you did not consider the e-mail that you received to be sufficient to meet a description of a formula or methodology for determining the equivalent; is that correct?

A That's correct.

Q And that's why in your recommendation you begin with the recommendation that they did not have a formalized methodology for making this determination?

A That's correct.

Q Now, as I understand it, again, and some of this I'll need you to correct me if I'm wrong, but as I understand it from your disclosure, the estimates of what the single family equivalents are are provided at the time of the purchase according to your disclosure?

A That's what I was told.

Q Now, should that be understood to be the time of the purchase of a particular system?

A That was my understanding.

Q So that when Utilities, Inc. would purchase a system, as you understood it, they would ask that system or the system operator what the number of single family equivalents are?

A I'm not sure if it was the operator or someone at the division level. I don't really know who was supposed to do it.

Q So they would ask somebody, though, at the new company, the newly purchased company what the single family equivalents were, but they did not provide that company, obviously, a formalized methodology for determining single family equivalents; is that correct?

A I don't really know what they asked them to do. All I know is that I asked for backup for the single family equivalent calculations, and I did not receive it because I was told they did not have them.

Q And is that what led you to conclude that one of the problems is that one person might come up with a single family equivalent that's based on something different from what another person might come up with?

A That was my conclusion.

Q So we have a situation where the utility is purchasing various subsidiaries, and it is seeking a central piece of information from the subsidiaries for its allocation, but it does not have a formalized method for measuring this. What about additional customers? What about when once a unit has been purchased and they have additional customers brought into the system? Do you know how those were dealt with?

A I asked the same question, but I never got an answer.

Q Okay. So we don't know what it was based on and no formalized method to begin with, and we don't know how they dealt with new customers. I understand from that then that you

as the staff auditor thought it best to seek to calculate your own method using ERCs, and then examine whether the company's equivalents were reasonable in light of that; is that right?

A I had planned to do that calculation before I found out that the company did not have --

Q I see. So that was going to be your comparison all along?

A Yes.

Q And as I understand it from this, that you asked the company for the information that you would need to calculate the ERCs; is that correct?

A Yes, I did.

Q And as of the time of this audit report, they did not give you information that you needed to calculate the ERCs; is that correct?

A That's correct.

Q And one of the central pieces of information that you needed to calculate ERCs is the gallons of wastewater treated in the various states; is that correct?

A That's correct.

Q And from this, I understand they could not provide that?

A They provided me with some of them.

Q But not all states?

A No.

Q Is it your understanding that various regulatory agencies would require this kind of information to be kept for purposes of environmental impacts and that sort of thing?

A Florida certainly does, but I wouldn't know about other agencies or other states.

Q Isn't it correct as well that a company's determination of customer equivalent for the test year allocation is based on a year ending June 2001?

A Yes, it is.

Q And the test year in this rate case, do you know -- can you confirm that it's based on year-end December 2001?

A That's correct.

Q So even the data that was collected in the fashion that we've discussed is one that did not incorporate additional customers that have come on-line -- that would have come on-line subsequent to June 2001; is that correct?

A That's correct.

Q Are you aware of a number of customers that had been added to the system since June 2001?

A I need to look at my work papers for that.

Q Okay. Thank you.

A I don't think I have the number of customers. I have the new systems that were added, but I don't believe I have the number of customers in here. I don't think I do.

Q If it was a significant number, would you think that

should be something that should be considered for a determination of the reasonableness of the allocation for the particular year in question?

A I understand the utility's concept of using an average, which is what they did. They assumed that June was an average because the systems coming on-line could have been before or after, and therefore, the systems that were incurring the expense were the ones that probably incurred it -- or were in service as an average as opposed to a year-end. So I understood their concept. I don't have an opinion either way.

Q Would it be reasonable for me -- should I understand that based on all of the reasons that we've discussed that that is why your conclusion in your audit disclosure is that you were unable to determine if the company's computation of allocations is reasonable?

A That's correct.

MR. BURGESS: Thank you. That's all we have.

COMMISSIONER DEASON: Mr. Friedman.

CROSS EXAMINATION

BY MR. FRIEDMAN:

Q Ms. Welch, does the Public Service Commission have any rule that sets forth a specific method of allocating these type of expenses?

A Not for water and wastewater.

Q So you could probably think of many different ways

that would be reasonable to allocate those expenses, couldn't you?

A That's true.

Q Did UIF provide you with a schedule of computer purchases during the test year and for the two prior years?

A Computer purchases?

Q A schedule showing the computer purchases.

A Yes. I'm not sure that that happened -- that did not happen during the audit, not during this audit. I received it for other audits.

Q That wasn't provided to you after the audit in connection with this case?

A Not to me.

Q Have you looked at that schedule?

MR. BURGESS: Excuse me. I'm going to argue that if we get into this, this is irrelevant if it's something that has to do with some other case entirely. I don't think it has anything to do with this case. She's testified and specified that it was not in association with the audit for this case.

COMMISSIONER DEASON: I have an objection on relevancy.

MR. FRIEDMAN: Well, let me -- I'll agree if it's not. If it's not in this case, then I agree with Mr. Burgess, it's not relevant. I just want to see if I can jog the witness's memory about which case she got it because she's

working on a lot of different cases. And if I could just ask another question, and if she says no, then I'll withdraw any further questions about that.

COMMISSIONER DEASON: I'll give you that latitude.

MR. FRIEDMAN: Thank you.

BY MR. FRIEDMAN:

Q Ms. Welch, do you know Amanda Ross who works at the company? Do you -- are you familiar with her?

A Yes.

Q Do you not recall her giving you this schedule of computer purchases in connection with this case?

A Not in connection with this case, no. I received it recently when I was in Chicago working on a different case. I did not receive it during the time I was doing this audit. I believe it was filed with the Commission as a response maybe to our audit.

Q In this case?

A Probably, but, I mean, I did not get it. It was filed with Tallahassee, and it wasn't audited --

Q I see.

A -- in this case.

Q I'm sorry. So if something is filed in response to an audit, you never see it?

A I might have seen it, but I don't believe it was ever sent to our office at that time. We got the letter from the

company talking about the audit but not what they filed in response to give additional information. We did not get that, and we did not audit it at that time.

Q So when a company files something in response to an audit, the staff doesn't ever get that back to you and ask you to address it or have an opinion or anything about it?

A I was asked some questions, but I didn't get it, no.

Q Is that typical that that's the way it happens?

A Yes.

Q Well, this may fit in that same category. Let me ask you if you recall UIF providing you with a schedule showing the four employees who hired in the test year by which the company used employment agencies?

A The finder's fees, you mean. If that was filed as a response, I don't believe it's in my work papers. I mean, I have things on the finder's fees, but if it was filed as a response, it's not going to be in here.

Q Same as we just went through?

A Uh-huh.

Q In your audit -- you heard some witnesses this morning testifying that they did not believe that the nonregulated business was included in the allocations. Were you here for that testimony? I can't remember whether it was Ms. Dismukes or Ms. DeRonne.

A I've been in and out, so I'm sorry, you'll have to

tell me what you're referring to.

Q You're familiar that there is some nonregulated business activities at Water Service Corporation?

A Biotech, is that what you're referring to?

Q Yes, correct. That's exactly right.

A Okay.

Q Isn't it true that allocations were included for that?

A There was an allocation made to that, yes.

MR. FRIEDMAN: Okay. That's all the questions I have.

MR. BURGESS: Excuse me. Mr. Friedman characterized testimony of our witness, and I would say he mischaracterized it. So, you know, to the extent --

MR. FRIEDMAN: Then I apologize.

MR. BURGESS: Thank you.

COMMISSIONER DEASON: Commissioners, questions? Redirect.

MS. GERVASI: No redirect.

COMMISSIONER DEASON: Okay.

MS. GERVASI: Thank you, Ms. Welch.

THE WITNESS: Thank you.

(Witness excused.)

COMMISSIONER DEASON: Exhibits. Exhibit 19.

MS. GERVASI: We would move Exhibit 19.

COMMISSIONER DEASON: Without objection, show that Exhibit 19 is admitted.

(Exhibit 19 admitted into the record.)

MS. GERVASI: We would next call Richard P. Redemann to the stand.

COMMISSIONER DEASON: Let me kind of pose a question at this point that I posed before we concluded yesterday evening. We're still on schedule to finish this hearing today even if we take a lunch break; is that correct?

Mr. Friedman, is that your opinion?

MR. FRIEDMAN: I'd sure like to try to.

COMMISSIONER DEASON: So you think we have the luxury of taking a lunch break? So I guess that's my question.

MR. FRIEDMAN: Steve, you got a lot for Frank? I mean, I guess that would be -- yeah, it's still Steve.

MR. REILLY: Yes, this Steve has reappeared. A fair amount for Seidman, a little bit more for Mr. Redemann. I don't see a problem with today being concluded.

COMMISSIONER DEASON: Okay. So we can blame you if we don't conclude; is that --

MR. FRIEDMAN: I agree with that.

MR. REILLY: If I'm the cause of it -- let me say I will not take up between now and the end of the day.

COMMISSIONER DEASON: I think we're going to take a lunch recess at this time, and we will reconvene at 1:15.

That's just a little less than an hour.

(Lunch recess.)

COMMISSIONER DEASON: Call the hearing back to order. Staff, you may call your next witness.

MS. GERVASI: Thank you. And, Commissioner, maybe before we even do that, earlier during the hearing today Mr. Burgess mentioned that the parties and staff were all conferring as to whether we needed to make certain changes to some of the stipulations and that has happened, and everybody is in agreement that three of the stipulations actually need to be changed. And I don't know if you'd like to take that up now or at the end of the hearing, whatever is your pleasure. We have distributed copies of the changes.

COMMISSIONER DEASON: Well, let's do this. Let's go ahead, let you describe in brief terms or, if applicable, staff describe in brief terms what's being changed and why. And then depending on whether there are questions or not, we may wish to go ahead and take it up now, or we may wish to defer it until the end of the hearing.

MS. GERVASI: Okay. Because of the fact that we have dropped Stipulation Number 2, there's some adjustments that need to be made to some of the other stipulations and that includes Stipulation Number 1. What has changed with respect to Stipulation Number 1 is adjustments to reflect prior Commission-ordered water and wastewater rate base adjustments.

That schedule for the Summertree PPW system for plant, land, and accumulated depreciation, those three columns, the numbers should be zero as opposed to the numbers that were shown previously. That's on Page 63 of the prehearing order.

And then the table -- the last table of Stipulation Number 1, the Pasco-Summertree columns for average accumulated depreciation year-end and depreciation expense should also be zero.

And then Stipulation Number 4, which appears on Page 65 of the prehearing order, should be dropped entirely because there would be a double adjustment if we were to leave that in.

And then Stipulation Number 9, which appears on Page 67, should be revised entirely so that it should read the way it appears on Page 2 of the new handout to spell out what those adjustments are.

COMMISSIONER DEASON: And all parties are in agreement?

MS. GERVASI: I believe so.

COMMISSIONER DEASON: Mr. Burgess?

MR. BURGESS: Yes, we are.

MR. FRIEDMAN: Yes, we are.

COMMISSIONER DEASON: Commissioners, do you have any questions?

COMMISSIONER BAEZ: No questions. If nobody else has

any questions, I can move acceptance.

COMMISSIONER BRADLEY: Second.

COMMISSIONER DEASON: Moved and seconded. All in favor say "aye."

(Simultaneous affirmative responses.)

COMMISSIONER DEASON: Show that those changes to the stipulations are approved.

MS. GERVASI: Thank you.

RICHARD P. REDEMANN

was called as a witness on behalf of the Staff of the Florida Public Service Commission and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MS. GERVASI:

Q Mr. Redemann, have you been sworn in?

A Yes, I have.

Q Would you please --

COMMISSIONER DEASON: Excuse me. Just a moment.

MS. GERVASI: Sure.

COMMISSIONER DEASON: Should -- just a procedural question. Should we identify this as an exhibit since it's actually not part of the prehearing order, or how should we do that?

MS. GERVASI: I don't know that it's necessary so long as it comes in, but to make it perfectly clear, I suppose

we could, as long as it gets put into the record.

COMMISSIONER DEASON: Just in an abundance of caution, let's go ahead and do that so there's no question. This will be identified as Exhibit Number 20.

(Exhibit 20 marked for identification.)

COMMISSIONER DEASON: And as indicated, all parties are in agreement, and there's no objection, so show that Exhibit Number 20 is admitted.

MS. GERVASI: And maybe the title could be, "Stipulations 1, 4, and 9."

COMMISSIONER DEASON: Very well.

MS. GERVASI: Thank you.

(Exhibit 20 admitted into the record.)

BY MS. GERVASI:

Q Would you please state your name and business address for the record.

A Richard P. Redemann, Florida Public Service Commission, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399.

Q And did you prefile direct testimony in this case consisting of 29 (sic) pages?

A Yes, I did.

Q Do you have any changes or corrections to make to your testimony?

A Yes, I have one correction.

Q Could you please make it now?

A Yes. On Page 28 of my testimony, starting on Line 21, my answer reads, "No."

The next sentence after the word "no" should read, "For the Summertree system, there does not appear to be an infiltration/inflow problem."

Q And remove all of the language in that sentence and substitute it with what you just read?

A Yes, that is correct.

Q Thank you. Do you have any further changes to make to your testimony?

A No.

Q If I were to ask you the same questions as posed in your testimony, would your answers be the same today?

A Yes.

Q Thank you.

MS. GERVASI: May we please have Mr. Redemann's prefiled testimony inserted into the record as though read.

COMMISSIONER DEASON: Without objection, it shall be so inserted.

MS. GERVASI: Thank you.

BY MS. GERVASI:

Q Mr. Redemann, did you also prefile Exhibits RPR-1 through RPR-10?

A Yes, I did.

Q Do you have any changes to make to any of your exhibits?

A No, I do not.

MS. GERVASI: May we please have those exhibits marked for identification.

COMMISSIONER DEASON: Composite Exhibit 21.

MS. GERVASI: Thank you.

(Exhibit 21 marked for identification.)

DIRECT TESTIMONY OF RICHARD P. REDEMANN, P.E.

Q. Please state your name and business address.

A. Richard P. Redemann, Florida Public Service Commission, 2540 Shumard Oak Blvd., Tallahassee, FL 32399

Q. Please give a brief description of your educational background and experience.

A. I received a B.S. Degree in Civil Engineering from the University of Wisconsin-Platteville, Platteville, WI, in May, 1984. From June, 1984, to present I have worked for the Florida Public Service Commission. Prior to my work at the Commission I worked for the Wisconsin Department of Transportation during the summers in 1980 and 1982 through 1983. In May through November, 1981, I worked for an engineering testing lab in Appleton and LaCrosse, WI. I have been employed by the Florida Public Service Commission (FPSC or Commission) for 19 years. A copy of my resume is attached. (EX__ RPR-1)

Q. What is your current position at the Commission?

A. I am a Utility Systems/Communications Engineer and have worked in this position since 1990.

Q. Are you a Registered Professional Engineer?

A. Yes, I became a Registered Professional Engineer in the State of Florida in 1989.

Q. What are your general responsibilities at the Florida Public Service Commission?

A. I review, analyze, and make recommendations regarding the engineering aspects of original, grandfather, transfer, and amendment certification cases, rate cases, and overearnings cases. I have also prepared and presented expert

testimony concerning quality of service and used and useful issues before the Commission.

Q. How many cases have you testified in before the Commission?

A. I testified in Docket No. 860149-WU, (Application of Sunnyland for a rate increase). I also filed testimony in Docket No. 940761-WS (Request for approval of special service availability contract with Lake Heron in Pasco County by Mad Hatter Utility, Inc.), Docket No. 850206-WS (Application of Useppa Island Utilities, Inc. for interim and permanent rate increase in Lee County), Docket No. 860544-SU (Investigation of rates of Rookery Bay Utility Company in Collier County for possible overearings), and Docket No. 861441-WS (Investigation into the earnings of Mangonia Park Utility Company, Inc. for 1985).

Q. What is the purpose of your testimony in Docket No. 020071-WS?

A. The purpose of my testimony is to discuss and recommend the appropriate methodology to be used for determining the amount of used and useful plant and review of expenses for the Utilities, Inc. of Florida (UIF or utility) water and wastewater systems.

Q. What information have you relied on in preparing your testimony?

A. I reviewed UIF's minimum filing requirements (MFRs) for the water and wastewater systems in this case (Docket No. 020071-WS), as well as Commission orders in which a used and useful determination was made for the UIF systems and other water utilities. I conducted an inspection of the Seminole and Orange County systems on October 28-31, 2002, and November 1, 2002. I also reviewed several American Water Works Association (AWWA) publications related to water distribution system design and some of the consumptive use permit

(CUP) and water conservation rules for the Water Management Districts (WMDs).

Q. Can you explain your recommended methodology for determining the amount of used and useful plant for small water systems?

A. Yes. I prepared EX__ RPR-2 to summarize my recommended methodology and assumptions for determining the amount of used and useful plant for water systems. There is no current rule on evaluating used and useful for water systems. Although water systems are uniquely designed to meet the anticipated demands for a particular development, I believe that the formulas and assumptions shown on EX__ RPR-2 reflect a reasonable approach to determine the amount of used and useful plant for most water systems. The bases of the recommended formulas and assumptions are Commission practice and other generally accepted industry standards.

Q. What is the basic formula for determining used and useful plant for water system?

A. The sum of the utility's current demand on the system, reduced by excessive unaccounted for water, plus required fire flow, plus an allowance for growth, is compared to the system capacity to determine the percentage of plant that is used and useful.

Q. What are some of the basic assumptions inherent in your recommendation?

A. The used and useful formula I am recommending is for systems with potential growth in the service territory. I assume that the wells for a given service territory are not oversized. If the wells or other system components are oversized, then prudence and economies of scale should be considered. However, if the utility's service territory is built out and there is no apparent potential for expansion in the surrounding area, the

system should be considered 100% used and useful.

Q. Has the Commission previously found utility water systems to be 100% used and useful if the utility's service territory is built out and there is no apparent potential for expansion in the surrounding area?

A. Yes. In Order No. PSC-98-0130-FOF-WS, issued January 26, 1998, in Docket No. 970633-WS; in Order No. PSC-99-0243-FOF-WU, issued February 9, 1999, in Docket No. 980726-WU; in Order No. PSC-00-0807-PAA-WU, issued April 25, 2000, in Docket No. 991290-WU; and in Order No. PSC-96-1320-FOF-WS, issued: October 30, 1996, in Docket No. 950495-WS.

Q. Are some of the UIF water service territories built out?

A. Yes. All of the UIF water service territories in Seminole, Pinellas, and Orange Counties and all of the water systems in Pasco County except Summertree appear to be built out. Many of these subdivisions are 20 - 50 years old and no significant growth has occurred in these systems in years.

Q. Should the UIF water systems in Seminole, Pinellas, and Orange Counties and all of the water systems in Pasco County except Summertree be considered 100% used and useful because the service territories are built out?

A. Yes. It does not appear that the wells were oversized and there is no apparent potential for expansion in those areas. Therefore, they should be considered 100% used and useful.

Q. Has the Commission previously determined used and useful for those water systems?

A. Yes. In the last rate case for the Seminole and Orange County systems and the Orangewood system in Pasco County, Docket No. 940917-WS, all of the systems were found to be 100% used and useful except for the Crescent Heights

water system that has now been taken off-line (Order No. PSC-95-0574-FOF-WS, issued May 9, 1995). The last rate case for the Lake Tarpon system in Pinellas County was Docket No. 930826-WS. By Order No. PSC-94-1104-FOF-WS, issued September 7, 1994, in that docket, a partial stipulation of Order No. PSC-94-0739-FOF-WS, issued June 16, 1994, was approved finding the Lake Tarpon water system 100% used and useful. I do not believe that a rate case order exists for the Buena Vista water system in Pasco County. However, transfer Order No. PSC-01-1655-PAA-WS, issued August 13, 2001, in Docket No. 000793-WS indicates that the system was virtually built out when it came under Commission jurisdiction in July, 1972.

Q. Which of the UIF water systems are not built out?

A. The Summertree water system in Pasco County and the Golden Hills water system in Marion County are not built out.

Q. How should used and useful be calculated for water systems with only one well?

A. For systems with only one well, the system should be considered 100% used and useful unless it appears that the well is oversized. As with any used and useful calculation, prudence and economies of scale are always considered.

Q. Has the Commission found water utilities with only one well to be 100% used and useful in other cases?

A. Yes. This method has been used by the Commission in several dockets including Docket No. 991290-WU, by Order No. PSC-00-0807-PAA-WU, issued April 25, 2000 and in Docket No. 950495-WS, by Order No. PSC-96-1320-FOF-WS, issued October 30, 1996.

Q. How should firm reliable capacity be determined for those water systems that have more than one well and are not built out?

A. For systems that have more than one well and are not built out, Commission practice has been to remove the largest well and base the capacity on the remaining well(s). This is known as the system's firm reliable capacity. The assumption is that the largest well should be removed to recognize that the utility must be able to meet its demand when one of the wells is out of service. This is consistent with the "Recommended Standards for Water Works" 1997 Edition, published by Heath Education Services, which is commonly referred to as the Ten States Standards.

Q. Has the Commission approved used and useful calculations for water systems based on firm reliable capacity?

A. Yes. This method has been used by the Commission in Order No. PSC-02-0656-PAA-WU, issued May 14, 2002, in Docket No. 992015-WU; in Order No. PSC-96-1320-FOF-WS, issued October 30, 1996, in Docket No. 950495-WS; in Order No. PSC-93-0423-FOF-WS, issued March 22, 1993, in Docket No. 920199-WS; and in Order No. PSC-02-1449-PAA-WS, issued October 21, 2002, in Docket No. 011451-WS.

Q. How does water storage capacity affect the utility's ability to meet peak demand?

A. The utility must be able to meet the peak demands on the system. For example, most water utilities experience a peak demand in the morning when customers are first waking up and again in the late afternoon when customers are coming home from work and cooking the evening meal. If storage capacity is available, the utility can meet the peak demand periods by relying on water

stored in elevated or ground storage tanks that are filled during off peak hours. If the system does not have storage, then the utility must meet the peak demand periods from its well capacity. However, most water utilities do not record water usage on an hourly basis; they maintain records of daily water flows.

Q. How should the utility's firm reliable capacity be determined for water systems that have storage capacity?

A. For systems with ground or elevated storage, the firm reliable capacity should be based on the capacity of the well(s), with the largest removed from service, and with the remaining well(s) operating 12 hours per day. The assumption is that the wells should have some down time to allow the aquifer to recharge. It is environmentally responsible and prudent to rest a well for 12-hours per day so that the ground water can recharge. Excessive pumping has caused wells to draw air, sand and gravel into the water system, and has caused saltwater intrusion, land subsidence and wells to collapse. The use of 12 hours per day of pumping also reflects the general usage pattern of customers. In addition, usable storage should be included in the system capacity. All elevated storage capacity is typically usable, however, a portion of the ground storage capacity is not usable because all of the water (approximately 10%) cannot physically be pumped into the system.

Q. Has the Commission previously used a 12 hour day to determine well capacity?

A. Yes. This method has been used by the Commission in numerous rate cases, including Order No. PSC-02-1449-PAA-WS, issued October 21, 2002, in Docket No. 011451-WS; Order No. PSC-02-0656-PAA-WU, issued May 14, 2002, in

Docket No. 992015-WU; Order No. PSC-01-1574-PAA-WS, issued July 30, 2001, in Docket No. 000584-WS; Order No. PSC-00-1774-PAA-WU, issued September 27, 2000, in Docket No. 991627-WU; Order No. PSC-01-2385-PAA-WU, issued December 10, 2001 in Docket No. 010403-WU; and Order No. PSC-96-1320-FOF-WS, issued October 30, 1996, in Docket No. 950495-WS.

Q. How should the utility's current demand be determined for water systems that have storage capacity?

A. For systems with storage, the single maximum day flow during the test year as reflected in the utility's DEP monthly operating reports should be used unless it appears that some extraordinary event occurred during the period, such as a main break or a fire. If such an anomaly is believed to have occurred during the test period, the average of the five highest days within a 30 day period during the test year should be used.

Q. How should the utility's firm reliable capacity be determined for water systems that have little or no storage capacity?

A. For systems with little or no storage, the firm reliable capacity should be based on the gallons per minute capacity of the well(s), with the largest well removed from service. Consistent with my previous testimony regarding firm reliable capacity, removing the largest well is consistent with the "Recommended Standards for Water Works" or 10 states standards.

Q. How should the utility's current demand be determined for water systems that have little or no storage capacity?

A. For systems with little or no storage, the demand should be based on a peak hour instead of a peak day. Since utilities do not have hourly flow data, the peak hour demand should be estimated based on the maximum day flow

divided by the number of minutes in a day (1440) to get an average flow rate per minute for the maximum day and then multiplied times 2. The assumption is that the average gallons per minute on the peak day does not reflect the peak hourly demand and therefore, should be multiplied by 2 to recognize that the utility must be able to meet the peak hour demand.

Q. What is the basis for multiplying the maximum day flows by 2 to estimate peak hour flows for water systems?

A. The peaking factors are based on the American Water Works Association (AWWA) Manual of Water Supply Practices, Distribution Network Analysis for Water Utilities, M32. According to the manual, ratio of peak hour demand to maximum day demand has been observed to vary from 1.3-2.0:1.0. (EX__ RPR-3)

Q. Has the Commission approved used and useful calculations using the peak hour for water systems without storage capacity in other cases?

A. Yes. This method has been used by the Commission in numerous rate cases. By Order No. PSC-96-1320-FOF-WS, issued on October 30, 1996, in Docket No. 950495-WS, the Commission approved used and useful calculations based on the use of estimated peak hour flows for systems that did not have storage capacity. A peaking factor of 2 was applied to the maximum day demand to estimate the peak hour demand. Although that case was appealed to the First District Court of Appeal on certain issues, the parties did not appeal the use of a peak hour calculation for systems without storage. Southern States Utilities, Inc. v. FPSC, 714 So. 2nd 1046 (1st DCA 1998).

Q. How should the utility's current demand be determined for water systems that do not have adequate Department of Environmental Protection (DEP) monthly operating reports (MORs) with a record of daily master metering readings?

A. For systems that do not have adequate DEP MORs with a record of daily master metering readings, the current demand should be estimated based on a peak hour. The peak hour design criteria is 1.1 gallons per minute per equivalent residential connection (ERC). The assumption is that the system should be designed to provide at least 1.1 gallons per minute of water for each ERC in a peak hour. This is consistent with the assumptions of AWWA M32 manual regarding average to peak hour flows.

Q. Has the Commission approved used and useful calculations using estimated peak hour demand of 1.1 gallons per minute per residential connection for other water systems that do not have a record of daily flows?

A. Yes. This method has been used by the Commission in dockets such as Docket No. 020406-WU, by Order No. PSC-03-0008-PAA-WU, issued January 2, 2003.

Q. Do you agree with the conclusions in the testimony of Mr. Frank Seidman on used and useful for the water systems?

A. Yes. I generally agree with his conclusions on used and useful for the water systems.

Q. Do you agree with Mr. Frank Seidman's use of instantaneous flows to determine customer demand for the water systems?

A. No. Mr. Seidman used instantaneous flows to represent the customer demand for all of the UIF water systems, regardless of whether actual usage data was available. Instantaneous flow is a design criteria that is used to estimate the water capacity needed for a development based on the anticipated number of customers. The instantaneous flow requirements per customer are assumed to be high for a small customer base and taper off for a larger customer base. There is limited information available on instantaneous flow

criteria. Typical references for the design of water systems include the maximum day and peak hour. I believe that if water flow data is available, used and useful should be based on actual flows using the formulas and assumptions I have previously described. If actual flow data is not available, I believe that peak hour demand of 1.1 gallons per minute per residential connection should be used to determine used and useful plant for small water systems with little or no storage.

Q. Has the Commission commented on the use of instantaneous demand in determining used and useful recently?

A. Yes. In Order No. PSC-03-0647-PAA-WS, issued May 28, 2003, in Docket No. 020407-WS the Commission found that "... without actual measurements for the peak hour or minute demand, some type of estimation is appropriate in order to recognize the utility's demand requirements based on the number of customers during the test year. While we find that the water system is 100% used and useful, we disagree with the utility's method to determine the water customer demand factor. The utility's instantaneous demand estimate was based on a 1965 publication by Joseph S. Ameen, entitled *Community Water Systems Source Book*." The order also states, "We note that instantaneous demand to determine the amount of customer demand on a system without water storage is not commonly used. While maximum day and peak hour demand calculations are common in engineering design manuals for building water systems, the publication referenced by the utility is 38 years old, and is not commonly used today. We believe that this document does not necessarily reflect current water usage patterns by the utility's customers or the trend toward water conservation."

Q. Have you compared Mr. Seidman's methodology with the formulas and assumptions you are recommending to determine used and useful plant for the water systems in this case?

A. Yes. I prepared EX__ RPR-4. This table shows the number and size of wells for the small UIF water systems (excluding the Crescent Heights and Davis Shores systems in Orange County and Wis-Bar in Pasco County, where all water is purchased). The table provides a comparison of the maximum day flows, estimated peak hour demand based on a peaking factor of 2, design peak hour demand based on the number of connections, and Mr. Seidman's proposed instantaneous demand criteria.

Q. How do the estimated peak hour flows compare with the design peak hour and instantaneous demand criteria?

A. In each instance, the instantaneous demand criteria is significantly higher than the estimated peak hour demand based on actual customer usage. Further, in most instances the instantaneous demand criteria is significantly higher than the total available well capacity. If the instantaneous demand actually occurred, there would be pressure problems in many of the systems.

Q. Are you aware of any pressure problems in the water systems?

A. No. I am not aware of any pressure problems.

Q. Has the utility proposed adding any pro forma water plant to increase the capacity of the water systems?

A. No.

Q. What do you conclude?

A. The instantaneous demand criteria does not appear to correlate with the actual demands of the customers.

Q. Based on your proposed assumptions and formulas, what is the appropriate used and useful percentage for the Summertree water system in Pasco County and the Golden Hills water system in Marion County?

A. The Summertree water system has four wells and no storage capacity. If the largest well is removed, the firm reliable capacity is 720 gpm. The sum of the peak hour demand of 460 gpm plus the required fire flow of 1,000 gpm equals 1,460 gpm, which exceeds the firm reliable capacity of 720 gpm. The approximate 2% growth and 6.2% excessive unaccounted for water would have little effect on the calculation. Because the demand on the water system is greater than the firm reliable capacity, the Summertree water system should be considered 100% used and useful. The Golden Hills water system has two wells and no storage capacity. If the largest well is removed, the firm reliable capacity is 330 gpm. The sum of the peak hour demand of 535 gpm and the required fire flow of 500 gpm equals 1,035 gpm, which exceeds the firm reliable capacity of 535 gpm. The approximate 3% growth and 12.2% excessive unaccounted for water would have little effect on the calculation. Because the demand on the water system is greater than the firm reliable capacity, the Golden Hills water system should be considered 100% used and useful.

Q. Has the Commission ever made a used and useful determination for the Summertree and Golden Hills water systems?

A. Yes. In the last rate case for the Summertree water system in Pasco County (previously known as Paradise Point West), Docket No. 910020-WS, the water system was found to be 100% used and useful in Order No. 25821, issued February 27, 1992. The last rate case for the Golden Hills system in Marion County was Docket No. 930826-WS. By Order No. PSC-94-1104-FOF-WS, issued

September 7, 1994, in that docket, a partial stipulation of Order No. PSC-94-0739-FOF-WS, issued June 16, 1994, was approved finding the Golden Hills system 100% used and useful.

Q. What is unaccounted for water?

A. The difference between the amount of water produced (or purchased) and the amount sold to customers or documented as being used for fire fighting, testing, or flushing or resulting from documented line breaks is referred to as unaccounted for water. Unaccounted for water is typically the result of unmetered usage, faulty meters, and leaks in the water system.

Q. Why isn't the water used for fire fighting, testing, flushing or the amount of water lost through line breaks considered to be unaccounted for water?

A. Some water is used by the utility to flush its distribution system, service lines, mains, hydrants, and tanks to properly maintain the system. Water loss can also occur when lines break during construction. The utility should maintain a record of the amount of water used to maintain the system or lost through line breaks. The fire department should measure or estimate the amount of water used for firefighting or testing and report the usage to the utility. If water used for maintaining the system or lost through line breaks is properly documented, then it should not be considered unaccounted for usage.

Q. Why is unaccounted for water a concern?

A. Unaccounted for water is a concern for two reasons. One, water is a limited natural resource that must be conserved to assure adequate supply and water utilities should be taking reasonable steps to avoid losses through line

leaks and other unaccounted for losses. Two, the cost of excessive unaccounted for water should not be borne by rate payers.

Q. Do some of the utility's Seminole, Orange, Marion, Pasco and Pinellas Counties systems have unaccounted for water?

A. Yes. According to the utility's Financial, Rate and Engineering Minimum Filing Requirements, Schedule F-1, the following systems have unaccounted for water:

<u>Seminole County</u>	
Weathersfield	10.2%
Little Wekiva	13.0%
Phillips	16.8%
Crystal Lake	3.2%
Ravenna Park	10.8%
Bear Lake	5.6%
Jansen	1.5%
<u>Orange County</u>	
Crescent Heights	10.3%
Davis Shores	2.1%
<u>Marion County</u>	
Golden Hills/Crownwood	22.2%
<u>Pasco County</u>	
Buena Vista	10.2%
Orangewood	17.5%
Summertree	16.2%
Wis-Bar	2.4%

Pinellas County

Lake Tarpon 20.6%

Q. Should an adjustment be made for unaccounted for water?

A. It is Commission practice to allow 10% of the total water produced or purchased as acceptable unaccounted for water. The chemical and electrical costs associated with unaccounted for water in excess of 10% should be adjusted so that rate payers do not bear those costs. The Commission has also required utilities to take corrective action to reduce the excessive unaccounted for water.

Q. How was over 10% determined to be an excessive amount of unaccounted for water?

A. This has been a long-standing Commission practice. In addition, I reviewed several American Water Works Association (AWWA) publications and some of the water management district rules related to consumptive use permits and water conservation that seem to support 10% as a reasonable amount of unaccounted for water. The AWWA M8 Manual on Water Distribution Training Course published in 1962 states on page 11, "A fair average of unaccounted for water might be 10-20% for fully metered systems with good meter maintenance programs and average conditions of service." (EX__ RPR-5) In a more recent publication, page 31 of the AWWA M32 Manual on Distribution Network Analysis for Water Utilities published in 1989 states, "The percentage of unaccounted-for water can vary widely from system to system. Values ranging from 4-30 percent of the total accounted-for consumption are found, although 10-15 percent may be more prevalent. The percentage can also vary from year to year in the same system. The higher values generally are associated with older

systems, in which leakage, no meters or faulty meters are more common place than in newer systems. Systems operating at high pressures usually will experience a high loss percentage." (EX__ RPR-6) The St. Johns River Water Management District Rule 12.2.5 on Consumptive Use Permits (CUPs) and water conservation requires the utility to perform a meter survey. If the initial unaccounted for water is 10% or greater the utility may need to initiate a meter change-out program and must complete a leak detection evaluation. (EX__ RPR-7) The Southwest Florida Water Management District Consumptive Use Permit handbook requires water systems in the Northern Tampa Bay Water Use Caution Area (Pasco and Pinellas County) to perform water audits. If the annual report reflects a greater than 12% unaccounted water, the permittee must complete a water audit within 90 days of submittal of the annual report. For water systems that are not in a Water Use Caution Area (Marion County), applicants with unaccounted for use greater than 15% may be required to address the reduction of such use through better accounting or reduction of unmetered uses of system losses. (EX__ RPR-8)

Q. Should an adjustment be made for unaccounted for water for these systems?

A. For those water systems that have over 10% unaccounted for water, if the utility has performed a water audit and is in the process of reducing the amount of water loss, no adjustment is needed because the cost the company will incur to correct the problem will likely exceed the expenses that would be removed. Also, for those systems that are slightly over 10% unaccounted for water, the adjustment on such small amounts of unaccounted for water would be immaterial. For those water systems with unaccounted for water in excess

of 10% and the utility has not taken steps to reduce the water loss, a reduction in chemical and electrical expense should be made. In addition, the utility should investigate the source of the water loss and reduce the amount of unaccounted for water, if it has not done so already. It is important to reduce the amount of unaccounted for water because water is a limited resource that should be protected.

Q. Which systems have over 10% unaccounted for water?

A. For the systems in Seminole County of Weathersfield (10.2%), and Ravenna Park (10.8%), the Crescent Heights system in Orange County (10.3%), and the Buena Vista system in Pasco County (10.2%), which have over 10% unaccounted for water, staff believes that unaccounted for water is reasonable. In addition, the adjustment on such small amounts of unaccounted for water would be immaterial. Staff believes that only Little Wekiva (13.0%) and Phillips (16.8%) in Seminole County, Golden Hills/Crownwood (22.2%) in Marion County, Orangewood (17.5%), Summertree (16.2%) in Pasco County, and Lake Tarpon (20.6%) in Pinellas County have excessive unaccounted for water.

Q. Has the utility addressed the unaccounted for water for those systems with more than 10% unaccounted for water?

A. Yes. In response to Staff Interrogatory No. 69 and Staff's Production of Document Request No. 5, the utility provided a copy of a water audit and a letter dated January 24, 2003 from Mr. David Hanna, State Water Circuit Rider for the Florida Rural Water Association to Mr. Scotty Haws. In the letter, Mr. Hanna made specific recommendations for several of those systems. For example, he recommended that the utility change out the meters determined to be 10 years old or older and repair main leaks. The utility is currently

developing a meter change out program for the Little Wekiva system which is expected to be completed by September, 2003, at the recommendation of the Florida Rural Water Association. A main leak at the Phillips system has been repaired and the master meter is being scheduled for replacement. The Phillips system customers are billed bi-monthly and only one bill has been sent since the repair was completed. When the results of the next billing are available, the utility will be able to better quantify the relationship between pumped and unaccounted for water.

Q. What adjustments should be made for unaccounted for water?

A. The electrical and chemical expenses for systems with unaccounted for water in excess of 10% should be reduced. For the Golden Hills/Crownwood water system, a reduction of $140.42 ($1,150 x .122 = $140.42) should be made to Account No. 618 Chemicals and a reduction of $1,325.03 ($10,852 x .122 = $1,325.03) should be made to Account No. 615 Purchased Power. The utility combined all chemical and electrical expenses for its water systems in Pasco County. Therefore, an adjustment for unaccounted for water should be based on the sum of the total water pumped less the total gallons accounted for in Pasco County. Since the Wis-Bar system purchases water and does not use any chemicals or electricity to repump the water, it would not have any chemical or purchased power costs. The total unaccounted for water for the Pasco County water systems is 14.49%. Therefore, a reduction of $210.99 ($4,699 x .0449 = $210.99) should be made to Account No. 618 Chemicals and a reduction of $699.90 ($15,588 x .0449 = $699.90) should be made to Account No. 615 Purchased Power for excessive unaccounted for water. For the Lake Tarpon water system, the total unaccounted for water was 20.63%. Therefore, a

reduction of $22.32 ($210 x .1063 = $22.32) should be made to Account No. 618 Chemicals and a reduction of $271.81 ($2,557 x .1063 = $271.81) should be made to Account No. 615 Purchased Power for excessive unaccounted for water. The calculations are detailed in EX__ RPR-9.

Q. Do you agree with the utility's used and useful calculations for its water distribution systems?

A. Yes. I agree with the utility's proposal that all of its water distribution systems be considered 100% used and useful. All of the water systems are built-out, with the exception of Summertree in Pasco County and Golden Hills in Marion County. The Summertree water distribution system is fully contributed and therefore a used and useful adjustment is not necessary. The Golden Hills water distribution system should be considered 100% used and useful based on the existing connections, plus an allowance for growth.

Q. Have you looked at the utility's used and useful calculations for its wastewater systems?

A. Yes. The utility currently has only one wastewater treatment plant, and that plant is the Crownwood plant in Marion County.

Q. Did the utility use the proper used and useful methodology for the Crownwood wastewater treatment plant?

A. Yes. The utility proposed a 68.65% used and useful allowance for the Crownwood wastewater treatment plant and I agree with that calculation. The utility's calculations appear to be consistent with Rule 25-30.432, Florida Administrative Code.

Q. Do you agree with the utility's used and useful calculations for the wastewater collection systems?

A. Yes. The wastewater service areas are built-out, with the exception of Summertree in Pasco County. The systems that are built-out are 100% used and useful. In the last rate case order for Summertree, the Commission found that the wastewater interconnection (master lift station and force main) was 100% used and useful and the collection lines were contributed and therefore, a used and useful adjustment was not necessary.

Q. Has the Commission previously determined used and useful for the wastewater collection systems?

A. Yes. The Commission determined that they were 100% used and useful.

Q. Does the utility have infiltration/inflow problems in any of the wastewater collection systems?

A. Yes. The utility has an infiltration/inflow problem in the Ravenna Park/Lincoln Heights wastewater system in Seminole County.

Q. What causes infiltration/inflow problems in a wastewater collection systems?

A. Infiltration results from groundwater entering a wastewater collection system through broken or defective pipe and joints. Inflow results from water entering a wastewater collection system through manholes and lift stations.

Q. How did you determine that infiltration/inflow was a problem for the Ravenna Park/Lincoln Heights wastewater collection system?

A. The total amount of water sold was compared to the amount of wastewater treated. For the seven bi-monthly billing cycles in the test year, the total water sold to the residential customers was 21.205528 million gallons (mg), and the total water sold to the general service customers was 3.145380 mg.

The annualized amount for 12 months would be 20.647469 mg. The Commission has recognized that not all water is returned as wastewater. The Commission typically assumes that 80% of the water purchased by residential customers is returned as wastewater and 96% of the water purchased by general service customers is returned as wastewater. In Staff's Interrogatories Nos. 25 and 26, Mr. Lubertozzi responded that these percentages are reasonable. Therefore, the water returned as wastewater would be expected to be 16.920644 mg for the test year. In the Financial, Rate and Engineering Minimum Filing Requirements - Seminole County - Ravenna Park - Page 182, Schedule F-2 shows that the total wastewater treated was 31.155 mg for the test year. Therefore, it appears that approximately 184.1242% of the customers' water purchased was returned as wastewater. I would expect no more than 100% from this estimation.

Q. Please describe the Ravenna Park/Lincoln Heights wastewater collection system.

A. The Ravenna Park/Lincoln Heights wastewater collection system is made up primarily of vitrified clay pipes (VCP), which are more brittle and the construction joints are not as tight when compared to more modern pipes. Also, as explained by Mr. Steven M. Lubertozzi in response to Staff's Interrogatory No. 54, the Ravenna Park system was dedicated to public service on March 5, 1959.

Q. What do you believe is the appropriate method for estimating the amount of infiltration/inflow?

A. Based on the Water Pollution Control Federation Manual of Practice No. 9, Design and Construction, the allowance for infiltration should be 500

gpd/inch-diameter/mile for all pipes. In addition, I recommend that an additional allowance be added for inflow. Mr. Lubertozzi agreed that these numbers are reasonable in response to Staff's Interrogatory No. 27.

Q. Based on your proposed methodology, did the utility estimate the amount of infiltration in the Ravenna Park/Lincoln Heights wastewater collection system?

A. Yes. In response to Staff Interrogatory No. 65, Mr. Orr responded that there are 6,068 linear feet of 8-inch diameter VCP collection mains along with an additional 2,400 to 5,000 feet of service laterals. In response to Staff Interrogatory No. 66, Mr. Orr also responded that the infiltration allowance from the collection mains is about 4,559 gpd or 1,664,035 gallons per year and adding the length of service laterals in the system could increase the allowance to 8,300 gpd or 3,030,000 gallons per year.

Q. Based on your proposed methodology, did the utility estimate the amount of inflow in the Ravenna Park/Lincoln Heights wastewater collection system?

A. Yes. In response to Staff Interrogatory No. 67, Mr. Orr responded that for the period of October 2001 to September 2002, the water sold to wastewater customers was equal to 20.775 mg. Therefore, the inflow allowance based upon 10% of the water sold would be 2.0775 mg. While the period of October 2001 to September 2002 is not the test year, staff believes that this is a reasonable estimate for the test year, because the customers live there year round.

Q. What is the appropriate amount of water returned from the customers as wastewater, plus an allowance for infiltration and inflow for the Ravenna Park/Lincoln Heights system for the test year?

A. The estimated amount of water the customers returned as wastewater was 16.920644 mg. In addition, 3.030 mg should be allowed for infiltration and 2.0775 mg should be allowed for inflow, for a total of 22.028164 mg for the test year.

Q. What is the appropriate purchased wastewater expense for the Ravenna Park/Lincoln Heights system?

A. According to Mr. Lubertozzi, in response to Staff's Interrogatory No. 21, the City of Sanford charges a base charge of $469.32 and a usage charge of $4.13/1000 gallons. Based on flows of 22.028164 mg, the cost would be $96,608 for the test year.

Q. Should an adjustment be made to Account No. 710 Purchased Sewage Expense for the Ravenna Park/Lincoln Heights system?

A. Yes. An adjustment should be made to Account No. 710 Purchased Sewage Expense to remove the cost of excessive infiltration/inflow for Ravenna Park/Lincoln Heights. According to the Audit Work Papers - Page (43-15)/2p2, the 12 month average for purchased wastewater treatment for Ravenna Park/Lincoln Heights is $142,086. Therefore, the cost of treating the excessive infiltration/inflow of $45,478 should be removed.

Q. How should the utility's costs associated with calibrating the meter, disposing of the volume of liquid within the aeration bays, clarifier, digester, and cleaning water that was sent through the meter be treated?

A. According to Mr. Orr, in response to Staff Interrogatory No. 68, the utility estimates that 827,000 gallons was utilized for start-up purposes, including calibration of the meter and cleaning and draining of the wastewater plant tanks. Mr. Orr reported that the cost was $3,416 (827,000 gallons x

$4.13/1000 gallons = $3,416) and recommended that this cost be treated as startup cost to be amortized over 5 years as a non-recurring expense or capitalized as part of the project cost. I agree that the cost should be amortized over 5 years for an annual cost of $683.20.

Q. Have your reviewed the testimony of Mr. Ted L. Biddy, P.E./P.L.S. on behalf of Public Counsel?

A. Yes. I will be providing comments on Mr. Biddy's testimony related to fire flow, storage, used and useful, unaccounted for water, and infiltration/inflow into the wastewater system.

Q. Do you agree with Mr. Biddy's position on the allowance for fire flow?

A. No. The Commission has consistently recognized the need for fire flow protection and considers it in its determination of used and useful. While fires hopefully do not occur frequently, I believe that it is important to allow the utility to include fire flow in its used and useful calculation if there is a local requirement to provide fire flow and fire hydrants exist in the service area. This is consistent with Order No. PSC-96-1320-FOF-WS, issued October 30, 1996, in Docket No. 950495-WS in which the Commission found that, while the Commission does not test fire hydrants or require proof that hydrants are functional or capable of the flows requested, an investment in plant should be allowed.

Q. Do you agree with Mr. Biddy's position on evaluating used and useful for storage tanks separately?

A. No. Used and useful should only be evaluated on a component basis when some portion of the system is oversized relative to the size of other components. The storage capacity for any of the systems does not appear to

be oversized, therefore there is no need to evaluate used and useful for the storage tanks separately in this case. The AWWA and the Ten State Standards recommend general guidelines for storage capacity; however, these are general guidelines. Florida has frequent hurricanes and floods which can cause power outages for an extended period of time or well contamination. The only source of water would be the amount in the ground or elevated storage tanks. The Commission has recognized that one full day of storage may be needed for a system. See Order No. PSC-97-0847-FOF-WS, issued July 15, 1997, in Docket No. 960329-WS.

Q. Do you agree with Mr. Biddy's position that used and useful should be based on pumping wells for a 24 hour period for a small water system with little or no storage capacity?

A. No. The proper method, as I discussed earlier, is to determine the well capacity based on pumping 12 hours to properly manage the aquifer. According to the AWWA Manual M21:

> It is commonly assumed that one obtains water from a well, but nothing could be further from the truth. A well is a means of access to a water-bearing formation, and it serves the same purpose as a straw in conducting fluid from a glass to your mouth. A well typically includes a pump, which moves water from the aquifer to a distribution system for delivery to the water user.
>
> Cone of depression. To move water from a formation into a well, a gravitational force must be created. The gallonage first pumped from a well removes water in storage from the well bore, then removes water from storage in the aquifer....

See EX__ RPR-10.

Q. Do you agree with Mr. Biddy that the flow of water is steady and equal on a 24-hour basis?

A. No. Water demand is not consistent in a 24-hour period. Typically, there is a peak in the morning around 6 AM, around noon, and around 6 PM. There us generally very little demand on the system between 10:00 PM and 6 AM (8 hours).

Q. Is there an inconsistency with respect to Mr. Biddy's testimony regarding pumping a well for 24 hours and the equalization storage of 20 to 25% of the average daily flow?

A. As I just discussed, the water systems have peak demand periods and water is minimally used during the night. The testimony does not explain where the water, when pumped for 24 hours, would be stored, so that it could be used during the peak periods of the day. In order to fully utilize the well that is pumped for 24 hours the storage amount would need to be about 1/3 to 1/2 of the capacity of the well times 24 hours to allow the utility to obtain 100% used and useful for the well and storage system.

Q. Do you agree with Mr. Biddy's position regarding infiltration and inflow for the Summertree, Weathersfield, and Golden Hills wastewater collection systems?

A. No. ~~For the Summertree system, Mr. Biddy failed to include the wastewater flow from the commercial customers of Summertree/Paradise Pt. which is approximately equal to the wastewater flow from the residential customers~~. For the Summertree system, there does not appear to be an infiltration/inflow problem. For the Weathersfield system, the total wastewater treated of

90.956 mg reported by Mr. Biddy does not agree with Schedule F-2 of the utility's MRFs which shows that the total wastewater treated was 72.208 mg for the test year. There is no flow meter at Weathersfield. For the Crownwood system, the infiltration/inflow reported of 1.43% is not material.

Q. Do you have anything further to add?

A. No. I do not.

BY MS. GERVASI:

Q Have you prepared a summary of your testimony?

A Yes, I have.

Q Please give that now.

A The purpose of my testimony is to discuss and recommend the appropriate methodology to be used for determining the amount of used and useful plant; also to review the expenses of Utilities, Inc. of Florida's water and wastewater systems in Marion, Orange, Pasco, Pinellas, and Seminole Counties.

MS. GERVASI: Thank you. We will tender the witness for cross-examination.

COMMISSIONER DEASON: Mr. Reilly.

MR. REILLY: Thank you.

CROSS EXAMINATION

BY MR. REILLY:

Q Mr. Redemann, you're a civil engineer and a registered professional engineer; correct?

A That is correct.

Q Have you ever designed any water and wastewater system?

A I've designed components of water and wastewater systems.

Q And when did you do that?

A During my college years, and also I have reviewed

many water and wastewater system designs at the Commission.

Q In doing this work during college, how many years ago was that?

A About 20 years.

Q And obviously you were doing that in an assistance of some professional engineer who would sign and seal those designs, I presume?

A As part of the engineering training, yes, there's usually a professional engineer, you know, assigned to review your work. I am a registered professional engineer.

Q The designs that you involved yourself in 20 years ago, did they result in systems actually being constructed?

A I believe in a few of the courses they were -- we used -- the class designed different components. I don't recall exactly what we designed, but we designed different components, I believe.

Q These were just hypothetical or actual real world designs for a client?

A I believe the instructor used the designs for a client in some cases.

Q And what state are we talking about?

A Wisconsin.

Q Have you ever submitted any designs to the state of Florida or any other agency?

A Yes.

Q And when did this happen?
A Recently, when I designed my culvert system at my house.
Q Are you familiar with the DEP rule criteria for sizing of various components of water systems?
A Generally, yes.
Q Could you describe your understanding of what the DEP requirements are for water supply and wells, pumping?
A Well, you need to -- well, there's many reference materials that are used in the design, and you need to base your components on the different reference materials that they've listed, you know, for the recommended sizes and stuff for design.
Q How about the Ten States Standards? Is that pretty much the -- we had testimony earlier that that's sort of the gospel. Is that your understanding, or is your understanding different than that?
A No, that's one of many different reference materials used in the design of water systems.
Q Do you know what the Ten States Standards requirements are for source of supply?
A Yes. There are components in there that require different -- or they have recommended sizes for the source of supply.
Q Could you tell me what those two basic formulas are?

A I don't recall what they are right now.

Q Do you recall what the Ten States Standards requirement is for water treatment plant, and is it the same as for water source?

A I don't recall.

Q Are you familiar with Chapter 62-555.330, Florida Administrative Code?

A Generally.

Q Is this not the portion of the code that sets forth the DEP rules for water system designs by referencing other publications?

A Yes. There's different publications recommended in the design of systems.

Q And this is the very rule that references them?

A Well, I don't have the rule in front of me, so I don't have the numbers memorized.

Q Okay. Do you know whether these design rules are mandatory or optional?

A I believe they're for the engineer to use, and they list, you know, the minimum requirements that the Department of Environmental Protection would require for these systems.

Q And if you don't meet these minimum requirements, can you expect your permit request to be denied?

A Yes. If the minimum requirements are not met, the DEP will deny your permit or -- well, I guess they will send

you a letter telling you you need to fix your permit to comply with our standards.

Q So would your answer to my question be that there are mandatory requirements?

A I believe you could use alternative methods, you know, that are not actually listed in there as long as those methods complied with the requirements by the Department of Environmental Protection.

Q I have -- and you don't have it in front of you, but I have 62-555.330 in front of me, and they use the word shall be applied, these technical publications. Subject to check, would you agree with that language?

A Yes.

Q Is the recommended standards for Water Works commonly known as the Ten States Standards, which we've talked a lot about during this hearing? Is it one of the publications cited in this rule?

A Yes, I believe it's listed as Number 3.

Q Do you know if these Ten States Standards and the design guidelines therein are used by FDEP in reviewing submittal approvals for permitting of water systems?

A I'm sure they are.

Q Are you familiar with Section 3.2.1.1 of the Ten States Standards as it relates to groundwater source capacity?

A I've reviewed it a while ago. I don't remember

exactly what it says.

Q And if I asked you -- okay. So you could not quote what that standard is today?

A No.

Q Okay. Are you familiar enough with this standard to know whether there's anything in the standard or the rule that requires groundwater source capacity to be based on either peaked hourly or instantaneous flows to the system?

A Well, the first book listed water treatment plant design in the listed standards. In that book there is maximum hour and peak day references.

Q I'm trying to focus your attention on the Ten States Standards as it relates to source of supply, not treatment. So my question to you, is there anything in this Ten States Standards as it relates to source of supply that would require either a peakly hour -- a peaked hour or instantaneous flow requirement?

A I don't believe the Ten States Standards has that information in it, but other design books do.

Q What is the FDEP rule for sizing water treatment plants? Do you know?

A I don't know. You have the rule in front of you.

Q How do you know that?

A Well, I believe you do.

Q I just read the rule concerning source of supply, not

water treatment. Is there -- are you familiar with the rule, the FDEP standard?

A Well, I've read through it a number of times a while ago, yes.

Q Subject to check, would it surprise you that the DEP standard is that you would look at the max day flow plus other demands?

A That's probably what it says, yes.

Q And in context of our PSC proceedings, that is historically meant that we're by statute adding the five-day maximum day -- excuse me, the five -- well, we use the five max days instead of the max day, but we do include fire flow plus five years growth minus excess -- not -- yeah, excess unaccounted for water, those three factors. Do you want me to restate that?

A Yes.

Q I'd like to restate it myself. That the standard is max day flows plus other uses. In the context of the PSC, we add a fire flow, we look at five years growth, and we also subtract excess unaccounted for water; is that correct?

A I don't understand the question. We the Public Counsel? Is that what you're saying?

Q No. I think that's been the practice here at the Public Service Commission, has it not?

A Repeat the question. I'm not following you.

Q Is it not true that the practice at the Public Service Commission in evaluating -- determining a used and useful for a water treatment plant evaluates max day flow plus other uses, and those other uses include fire flow, five years growth but subtracting any excess unaccounted for water?

A Yes. The Commission has used that formula. They have also used some peak gallon per minute formulas in calculating used and useful.

Q Are you familiar with the changing water use patterns and the trend towards water conservation in Florida?

A Generally, yes.

Q Isn't it a fact that water usage has substantially decreased in Florida as a result of these factors?

A I don't know substantially. It has decreased I would say, yes.

Q Did you examine the current water usage for these 17 systems, water systems in this case?

A On Exhibit RPR-3, I list -- or let's see. Exhibit RPR-4, I list the peak demands of the system.

Q Would it surprise you to know that such usages range from about 67 gallons per day per ERC to just over -- now, I'm talking about average daily flow of 67 gallons per day per ERC to just over 300 gallons per ERC with the average being about 211 gallons per day per ERC?

A I have not made that calculation, so I don't know,

but it's possible.

Q Okay. May I have you refer to your Page 4 of your testimony?

A Yes.

Q Here you state -- I think we're on Line 21. You say that you assume that the wells in these systems are not oversized; is that correct?

A That is correct.

Q And could you share with us the basis for that assumption or what calculation you made?

A Yes. Let me refer you to Exhibit RPR-4. On Exhibit RPR-4 many of these systems, if you look at the design peak hour, come pretty close to the firm reliable capacity of the system. In addition, most of these wells are relatively small, less than 500 gallons per minute.

Q Would it surprise you to know that 8 of the 17 systems have groundwater source capacity greater -- greatly in excess of the FDEP required capacities?

A If you're looking on a 24-hour basis on these small systems, I recommend the gallon per minute basis in calculating the used and useful.

Q I understand that, but under the FDEP standard.

A Well, in the Ten States Standards, correct, they don't have a peak hour, but in the water treatment plant design book there's references to peak hour. In addition, they

reference the American Water Works Association which is an industry standard, in my opinion, and that you could use the peak hour numbers in those -- in evaluating the systems.

Q Well, when you calculated your used and useful percentages for these water systems, you used a peak flow for the demand equal to two times the maximum daily flow; is that correct?

A Yes, I did.

Q And you also added fire flow as a flow rate as opposed to a particular quantity of flow?

A Yes, I did.

Q And then you further added five years growth factor and allowed for a 10 percent unaccounted for water?

A Well, I only actually evaluated two of the systems because they're growing and the other systems I considered to be built out and concluded that they were 100 percent used and useful.

Q When determining whether there's a fire flow requirement, did you look to the local authorities to determine whether they required a fire flow or not?

A I based it on Mr. Seidman's -- in the MFRs and also I'm aware of just general fire requirements in certain counties.

Q And it's your understanding that certain counties have a fire flow requirement and others do not?

A Yes.

Q And for those jurisdictions that have a fire flow requirement, is it your understanding that that requirement applies only to new systems, or is there any attempt to enforce -- to retrofit an existing system to meet some fire flow requirement?

A In some situations, if you rebuild some of the service area, they require you to have the new fire flow requirement.

Q Repeat that. I'm sorry.

A In some of the systems if you rebuild the system or change their usage of the land use, if you -- for example, if you had a residential home, then converted it to commercial, you may have to go up to the higher fire flow requirement.

Q I'm talking about a water system now as opposed to a particular -- not a fire requirement for a commercial building such as a sprinkler system. Is that what you're talking about? I'm talking about a water system providing fire hydrants and sufficient flow to meet some fire requirement, fire flow requirement. Do you know of any jurisdiction that requires a retrofitting of existing systems to meet a fire flow requirement when it does not -- when it did not currently meet that requirement?

A Yes. We just had a case in Pasco County where the system did not meet the fire flow, and I guess they refurbished

the commercial area. I guess it was a mall. And the utility decided that they did not want to meet the fire flow, but the county fire department insisted that they had to meet the fire flow requirement. So it ended up actually Pasco County started serving the area because the utility couldn't provide the fire flow.

Q So in that case -- okay. But even in that specific instance of providing fire flow to some shopping small, you're not aware of any instance where a jurisdiction requires a system to retrofit to provide fire flow when they do not currently provide it?

A No.

Q Explain why you're using these fire flow volumes or rates as opposed to a discrete two-hour fire flow quantity.

A The utility on these small systems only have generally wells, and the wells, since they don't have ground storage and high service pumping, the wells have to meet the fire flow demand along with the residential demand.

Q But historically hasn't fire flow requirement and fire flow allowance been stated in terms of so much flow of water for a period of -- for a time period of two hours so it always would produce some sort of a quantity?

I mean, to give you an example, the gallons per minute requirement of any particular jurisdiction can change from 500 gallons per minute to 750 gallons per minute or a

thousand gallons per minute; is that correct? That can change from jurisdiction to jurisdiction?

A Yes.

Q However, is it -- in your experience, in your many years of experience at the PSC, hasn't the duration of that particular flow always been two hours as a standard in the industry for fire flow?

A Sometimes two, sometimes four hours, it just depends.

Q But it's always for some discrete time?

A Yes.

Q And the reason for that is the allowance for fire flow does not contemplate a 24-hour fire but a fire incident that lasts for a certain length of time.

A Yes.

Q And so let's consider the used and useful consequences of using what you are proposing versus what -- let me ask you this. Strike that.

Did we agree that historically the Commission in the past has used a volume requirement?

A No, the Commission has used both. Sometimes they've evaluated on a gallon per day, and they've also evaluated on a gallon per minute basis.

Q Can you give me any cases, you know, beyond one or two years from today that the Commission was adopting this gallons per minute flow rate versus a volume requirement?

A When I initially decided to look at the used and useful, we look at about five years of data on all the different rate cases that we had, and in some systems they used the gallon per minute and some systems they used the gallon per day calculation when there was sufficient storage.

Q Did you give me any case?

A No. I can't recall them right now, but looking over the last five years, there probably were a couple dozen cases, but I don't recall what they are right now.

Q Isn't it not true, though, that in case after case after case over literally decades that fire flow allowances have been granted by this Commission and that those fire flow allowances were expressed in terms of so much gallons per minute times two hours; is that correct or not?

A Not always, no. When you don't have sufficient storage, you need to consider that the well has to provide the fire flow.

Q But how long does it have to provide it? Twenty-four hours or 2 hours?

A Well, with a well you can't save up the water or pump it into a ground storage tank where it can be used later. The well has to meet the fire flow when the fire is needed.

Q I understand, but let's say we have a case like you say. And there's no storage and all we have is the wells and high service pumps. And now we're doing a used and useful

analysis of that, wells and pumping, because we have no storage. Nevertheless, we determine what the gallons per minute requirement of the fire incident is, and then we put on that used and useful calculation a demand on those pumps to produce that quantity of water for a certain duration. Why would that change?

A If you have ground storage and high service pumps, you can do that, but if you only have a well, let's say a 500 gallon per minute well, and there's 500 gallons per minute fire flow required, the well has to produce the water for the fire. It can't pump to a ground storage tank if there isn't one reasonably sized to use.

Q Depending on how we go will have a tremendous effect on the used and useful calculation; is that correct?

A Repeat your question.

Q Depending on whether we go with a flow rate per minute versus an actual volume requirement has a vast impact on the used and useful calculation?

A Yes, it does.

Q And if we can go through just an example to make the point. If the gallons per minute requirement is even as high as a thousand gallons per minute, if we limit that requirement for two hours, that would create a volume requirement of 120,000 gallons of total flow; is that correct?

A Repeat your question.

Q I'm giving you an example of the tremendous impact of what we're talking about, whether it's going to be a volume of flow versus a rate of flow.

If we allow a certain volume of flow for fire flow requirement and under our scenario if the requirement per minute is the same for both examples, 1,000 gallons per minute, but we limit that rate for a two-hour period, what is the total fire flow allowance under that scenario?

A Well, the 1,000 gallons per minute times 2 hours times 60 minutes per hour.

Q Correct. And that produces a total fire flow allowance of 120,000 gallons.

A That sounds correct.

Q Okay. Now, if we approach it from the way that you are now suggesting, what would be the fire flow equivalent requirement? You would have to multiply a thousand gallons per minute times 60 times 24, would you not, for a higher used and useful calculation?

A I don't understand your question.

Q Well, if we convert the 120,000 gallon per day flow that we just arrived at and calculate that down into a gallons per minute figure, subject to check, would that not create an 83.33 gallons per minute rate?

A Well, the fire required is a thousand gallons per minute.

Q Would there not be a 1,200 percent difference in the fire flow allowance if we use the fire flow rate that you're referring without limiting it in any way to the duration of that requirement; is that true?

A I don't know. I haven't made that calculation.

Q Could we do it real quickly? How do you translate the gallons per day requirement that we said exists and translate that down into the flow that's required to produce that number of gallons in that day?

A It's 1,000 gallons per minute for two hours.

Q Right. And we said that's 120,000 gallons total.

A Yes.

Q But I'm saying I'm trying to compare -- they are apples and oranges, but I'm trying to quantify for the Commission what the used and useful impact is of approaching fire flow in the manner that you are recommending today.

And is it not fair to translate this 120,000 gallons per day into something that can be related to the thousand gallons per minute by making it 83.33 gallons per minute?

A No. The fire requirement is 1,000 gallons per minute. That's what is required. You can't really divide that over a 24-hour period. That when the fire department goes to put out the fire, they want a thousand gallons per minute either in the middle of the night or during the peak hour. They don't want 83 gallons per minute over a 24-hour period, I

don't believe.

Q But the question still remains the same. And I'll go on in a minute. What is the effect on the used and usefulness of these components if you use what you are proposing? Is it not about a 1,200 percent difference in the impact?

A It would be higher. I don't understand your calculation.

MR. REILLY: Could we wait for one -- let me talk to my consultant for one second.

(Off the record.)

BY MR. REILLY:

Q Subject to check, a mathematical computation, could it be by a factor by 12, a difference, by not limiting it to the 2 hours?

A Well, if it's for 2 hours and divide it by 24, it would be times 12. Yeah, I think that would be correct.

Q A factor of 12. Thank you.

Should peak flows in a system be furnished by storage and pumping?

A The peak flows have to be furnished with whatever you have. If you have only a well system, then you have to serve the peak flows with the well. If you have ground storage and high service pumps, you can serve the peak flows with the high service pumps in the ground storage tank.

Q The question is -- well, the question might be, well,

what is the most economical and engineeringly sound way to meet peak demand?

A Well, it's usually pretty inexpensive to put in a well and a high service -- and a hydro-pneumatic tank. According to the design books, once you reach about a thousand customers, then it may be more economical to put in a ground storage and high service pumping.

Q Does insurance rating agencies such as Insurance Services Office recognize fire flow from systems operating on hydro-pneumatic tanks?

A I don't know.

Q Could I refer you to Page 5, Lines 13 and 18 of your testimony? My question is, what do you mean in your testimony when you say the system appears to be built out? And then on Page 6 you say it's virtually built out.

A Well, in evaluating the systems to determine if they were built out, I first looked at the previous orders, which I've listed in my testimony. I looked at the certificates to see if they had any additional territory being added during the field inspection. I looked to see if there were houses on more than one lots, and some houses had three or four lots. Some were vacant lots -- or vacant houses. Some houses were for sale. Some houses have wells. Some houses have septic tanks.

I did make the mathematical calculation versus taking the number of lots versus the number customers, and after I

analyzed all the data, I determined that the systems were built out.

Q Now, you say you did do a lot-to-lot analysis?

A On some of the systems I counted the lots, yes.

Q And which were those systems?

A The systems in Orange and Seminole Counties.

Q And are any of these calculations or analysis in the record?

A No.

Q And what was the result of these -- you say in Orange, in which counties?

A Orange and Seminole.

Q Was this just the water systems or wastewater?

A Well, I don't recall.

Q And do you recall which systems you did this lot-to-lot analysis in those two counties?

A Well, I did it for the systems in Orange and Seminole Counties.

Q All the systems?

A I think so.

Q And the results of these lot-to-lot counts were what, that it was 100 percent used and useful, 90 percent?

A I don't recall. They were pretty high. And then like I said, when I considered that, you know, some lots couldn't be built on and that there were very few vacant lots

there, I concluded that the systems were built out.

Q Could you define "pretty high" for me?

A I think somewhere in the high 90s. I don't recall the numbers.

Q Could it be in the 80s?

A I don't recall.

Q I mean, it's possible?

A It's possible.

Q And that didn't give rise to any concern of it being built out or not if it was in the 80s?

A No. Most of these systems have very little growth.

Q So it was really more the lack of growth than the lot-to-lot analysis that finally persuaded you?

A Well, also the age of the systems.

Q Did you also examine the maps that were provided both initially and later?

A Yes.

Q And did you do an analysis from those maps?

A I think I used the current maps.

Q Define "current maps." That means the amended maps?

A The latest, yes.

Q The latest.

Would it surprise you to know that 10 of the 17 systems still have positive annual growth?

A I believe I've heard that before, yes.

Q And that wouldn't surprise you?

A No.

Q If a water system with only one well is deemed 100 percent used and useful for source of supply and pumping and treatment, does this automatically mean that the distribution system for this system, though not built out, should be considered 100 percent used and useful?

A It would depend on the system.

Q Explain how it would depend.

A Well, it would depend, like I said, on all the different factors that I've just explained: The growth and the density and the number of available lots.

Q Can we get specific and just look at a few of these systems that were deemed 100 percent used and useful as far as source of supply and treatment, but according to our calculation it was in the low 80s that -- the distribution system according to our understanding of the lot count, could we just look at your -- do you have your results of your analysis with you?

A I don't believe so.

Q Do you have any understanding, sitting where you are, about the Little Wekiva system which was deemed 100 percent used and useful as far as water treatment and source of supply, but according to our lot count analysis, it was 83.6 percent used and useful on the distribution system?

A Well, I took a drive through the service area, and I didn't see that many empty lots, so I considered it 100 percent used and useful.

Q Did that have more influence on you than looking at the maps supplied by the utility?

A Yeah, because there's some, you know, houses for sale and some houses with -- on more than one lot and some people probably with their own wells. There probably also were some areas that, you know, couldn't be developed in there. I didn't see a lot of vacant lots. So I considered the systems to be 100 percent used and useful.

Q So when you're making your recommendation to the Commission as to whether the distribution system should be used and useful or not, you'll just drive around the neighborhood and get a feeling as to whether it's fully occupied or not?

A I base it on the MFR filings, the maps, and a number of different things.

Q Well, now, according to the maps, though, Little Wekiva was 83.6 percent; Park Ridge, 82.8 percent; Phillips, 82.5 percent. But you went and drove around the community and then had a feeling that that needed to -- your overall assessment would just call it 100 percent?

A Well, I recall the Park Ridge. There's one huge commercial area that was vacant, but I don't know how many ERCs you guys counted it for, and I didn't see any -- there was very

few vacant lots in Park Ridge. The age of the system, I think it's about 50 years old. So I concluded it was 100 percent used and useful.

Q Was this one of the systems you did the lot count method?

A That would be one of them.

Q What was the result of that count?

A I don't recall.

Q But whatever it was, it wasn't enough to offset your impression that you got when you inspected the area?

A Right. I considered it to be 100 percent used and useful.

Q Would not a community that's 80 percent, 80-something, 82, 83, 84 percent built out, appear to be largely built out, and yet it's still some distance away from being totally built out, is it not?

A Well, it depends on the system.

Q Let's take these systems we're talking about. Little Wekiva.

A Little Wekiva, they have 61 customers. The best I can recall, there are very few empty lots. The system has been in the ground for, you know, an extended period of time. I don't remember exactly. I think on our exhibit we identify the age of the system. And the system has already been considered 100 percent used and useful in the past by the Commission. And

the system has not had any change in, you know, probably about 40 or 50 years. It's the same system. They haven't added on any territory. And so I concluded it was 100 percent used and useful.

Q Now, you just added another factor in there and that is prior Commission determinations. That's just another factor that might cause you just to not be worried about the lot count method currently?

A It needs to be taken into consideration.

Q What is your opinion about the deference you should give to a prior determination of the Commission in your recommendation?

A Well, in my recommendation, I stated that previously the Commission considered these systems to be 100 percent used and useful.

Q And what effect did that have on your recommendation?

A I considered it.

Q How?

A As part of the total analysis of the system.

Q If the Commission -- do you believe that the lot count method is a legitimate basis -- a current evaluation of the lot count method is a basis to set aside a prior Commission determination as the used and usefulness of a distribution and collection system?

A No. These are old little systems, and most of

these -- you know, the lines in these systems do not meet the Ten States Standards, so I also considered that. They're one-inch-and-a-half, two-inch, you know, two-and-a-half-inch lines. And so when I considered that also, you know, I believe these systems are 100 percent used and useful.

Q Is that a no?

A Repeat your question.

Q Is a current counting using the lot count method a basis upon which to set aside an earlier higher used and useful determination in a Commission order?

A I think that's a legal question.

Q Well, in your opinion, is it a basis from you as to make from an engineering recommendation that if engineering went out to a system and did a current lot count method that turned out to be lower than what was determined in a prior Commission order, what is your view as a staff engineer of that lot -- what is your view of what the results of that lot count method should be in setting aside an earlier decision of the Commission?

A Well, for these systems I don't believe that they would apply. But if I would go out to a system and concluded that there's many lots and we did that lot count and considered, you know, the lines, the vacant lots, the customers that are on more than one lot and are on septic tanks, if I didn't believe it was 100 percent used and useful, I would

submit that recommendation to the Commission.

Q Okay. Let my try again. In this case again and again the Commission in prior orders determined that these distribution systems were 100 percent used and useful; is that correct?

A That is correct.

Q And my question to you is if in this docket you went out and did a lot count check and found out that that system was actually 80 percent used and useful applying the lot count method, is that a basis to set aside the earlier determination by the Commission, in your mind?

A No.

MR. REILLY: I have an exhibit to pass out that I'd like to use as a cross-examination exhibit.

This exhibit I'd like to have identified for cross-examination purposes.

COMMISSIONER DEASON: It will be identified as Exhibit 22.

(Exhibit 22 marked for identification.)

BY MR. REILLY:

Q What is being handed out is just one page of a 178-page order. It's an order that is referred to again and again and again by this witness as a basis for many of the recommendations that have been made. It is the PSC-96-1320-FOF-WS. That's the final order in the Southern

States case. And I've attempted to -- I picked this page because it -- it's the language I was able to find that speaks of the efficacy of these prior rulings and the various reasons that the Commission would consider setting aside a prior determination.

And if I could direct your attention, basically, I guess, to the second full paragraph. It goes on to explain the different reasons why they -- why the Commission would not and in other circumstances why they might and why they would consider setting aside earlier determinations. And one of the -- well, in the first instance, it says that we find that the level of used and useful plant determined in an earlier proceeding shall not be decreased if used and useful plant is now less because of a decline in demand. So that's one reason they said they would not set aside a prior determination. But after that, there are several reasons they said they would. And one of those reasons if I'd have you read it, it would be the -- I guess it's the third sentence. If you could read that for me?

A Which is the --

Q This is the third sentence in the second full paragraph from the top.

A Is it "In addition"?

Q Yes, that's correct.

A The order says what it says. It says, "In addition,

in this proceeding, we find it appropriate to authorize a decreased level of used and useful plant if that is indicated through the application of the lots connected-to-lots available methodology for transmission, distribution and collection lines, which methodology we have herein adopted."

Q Now, I read this -- my understanding of this sentence is that in the Southern States case they readopted and reaffirmed their use of the lot count method, and that this was one of the several factors that could be looked at to set aside a higher used and useful determination made in a prior order. Is that a fair characterization of this sentence?

A That appears to be what it says.

Q And yet you do not share this view.

A No, because I've considered these systems to be 100 percent used and useful.

Q For the reasons previously stated.

A That's correct.

(Transcript continues in sequence with Volume 6.)

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STATE OF FLORIDA)
: CERTIFICATE OF REPORTER
COUNTY OF LEON)

I, TRICIA DeMARTE, RPR, Official Commission Reporter, do hereby certify that the foregoing proceeding was heard at the time and place herein stated.

IT IS FURTHER CERTIFIED that I stenographically reported the said proceedings; that the same has been transcribed under my direct supervision; and that this transcript constitutes a true transcription of my notes of said proceedings.

I FURTHER CERTIFY that I am not a relative, employee, attorney or counsel of any of the parties, nor am I a relative or employee of any of the parties' attorneys or counsel connected with the action, nor am I financially interested in the action.

DATED THIS 2nd DAY OF SEPTEMBER, 2003.

Tricia DeMarte

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