

MAY 1 1998



Public Service Commission

-M-E-M-O-R-A-N-D-U-M-

**DATE:** May 11, 1998  
**TO:** Dr. Mary Bane, Deputy Executive Director/Technical  
**FROM:** Charles H. Hill, Director, Division of Water and Wastewater *CH*  
 Rosanne Gervasi, Division of Legal Services *RS*  
**RE:** Docket No. 971186-SU - Sanlando Utilities Corporation Application for Approval of Reuse Project Plan and Increase in Wastewater Rates

The above referenced docket is scheduled as Item 28 for the May 12, 1998 agenda conference. On May 8, 1998, staff received a facsimile of Sanlando's Response to staff's recommendation. In its response, the utility respectfully requests that the Commission determine that staff's recommendation is flawed. The utility further requests a deferment of this matter for 2 months. The utility further voluntarily requested a 2 month extension of the mandatory 5 month statutory time frame. Upon review staff has determined that the utility has not raised any material facts which would justify a deferral of this item. The utility has had sufficient time to supply the Commission with any relevant information it believed should have been considered by this Commission. Staff believes that the utility will have an opportunity to present its concerns and address staff's recommendation at the May 12th Agenda Conference.

Therefore, staff is **opposed** to any deferral of this item. Further, in its recommendation, staff has recommended that the utility be found to be overearning. Staff believes that these overearnings must be addressed in a timely manner.

It should be noted that there are several interested parties and several other Florida agencies which will be traveling in order to attend the scheduled agenda conference.

- ACK \_\_\_\_\_
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  - SEC \_\_\_\_\_
  - WAS \_\_\_\_\_
  - OTH \_\_\_\_\_
- cc: Noreen Davis  
 Lila Jaber  
 William Lowe  
 Marshall Willis  
 Troy Rendell  
 Neil Bethea

*5/11/98*  
*Julian*  
*I support staff*  
*WC*

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TO: Rosanne Gervasi, Senior Attorney

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## BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Application for approval )  
of reuse project plan and )  
increase in wastewater rates in )  
Seminole County by Sanlando )  
Utilities Corporation )  
\_\_\_\_\_ )  
DOCKET NO. 971186-SU

SANLANDO UTILITIES CORPORATION'S RESPONSE TO  
COMMISSION STAFF'S MEMORANDUM DATED APRIL 30, 1998

The Staff filed its Memorandum of Recommendations ("Recommendations") regarding issues 1 through 33 in the above docket on April 30, 1998 and furnished a copy of the same by Federal Express to Sanlando Utilities Corporation (the "Utility") which was received on Tuesday, May 5, 1998. The following is the Utility's response to the Staff's Recommendations.

Rather than addressing each issue, which will serve no purpose if the fundamental policy issues embodied in the Recommendations are not resolved, this response shall deal only with what the Utility believes are fundamental policy issues and the Utility's position on those issues.

I. SECTION 367.0817 SCOPE

The Staff has by its recommendation effectively engaged in a rate making process which is outside the scope of Section 367.0817 (Florida Statutes 1997), and therefore is inconsistent with the intent of Section 367.0817. The Utility believes that Section 367.0817 was intended by the Legislature to provide a simple, inexpensive, and focused procedure to establish rates for a proposed reuse project. Specifically, Section 367.0817 provides that the Commission review the Utility's reuse project plan and determine whether the projected costs are prudent and the proposed rates are reasonable and in the public interest.

Rather than reviewing the Utility's filing and recommending rates based upon the prudent costs of the reuse project, the Staff has instead engaged in a far more expansive limited proceeding, more in the nature of that provided for in Section 367.0822 (adjusting utility rates) or Section 367.081(8) (PAA for a general rate case). Neither of those sections are intended to be applied to reuse projects in light of the Legislature's specific mandate set out in Section 367.0817 as to how to consider a reuse project, and what to consider in setting rates for that project.

## II. IMPRACTICABLE CALCULATION OF REVENUE REQUIREMENTS

The Staff through adjustments in rate base, adjustments in the filing made by the Utility, adoption of a return on equity which is different than that which was approved in the last general rate case for the Utility in 1990, a significant reduction in working capital, and various other assumptions and accounting procedures has concluded in its Recommendation that the Utility is over earning FIVE HUNDRED TWENTY-ONE THOUSAND AND TWENTY-FIVE AND NO/100 DOLLARS (\$521,025.00) per year. The end result of the Staff's Recommendation is to allocate THREE HUNDRED NINETY-SIX THOUSAND ONE HUNDRED THIRTY-FOUR AND NO/100 DOLLARS (\$396,134.00) of those alleged overearnings to the cost of the reuse project and to allocate the balance of ONE HUNDRED TWENTY-FOUR THOUSAND EIGHT HUNDRED NINETY-ONE AND NO/100 DOLLARS (\$124,891.00) of the alleged overearnings to an escrow account until a later determination regarding its application. From a purely accounting viewpoint this may be appealing and even appear logical, but the result fails to recognize the practical effects of operating the Utility, or for that matter any utility.

As an example, in making its various adjustments the Staff failed to consider almost \$400,000 in capital expenses which were incurred by the Utility in 1997 and will continue to be incurred on an annual basis to maintain an aging physical plant, a significant portion of which is twenty-five (25) years or more old. This fact alone would make a significant difference in the revenue allowed the Utility if taken into account.

However, this fact, as well as other facts germane to a full rate analysis, has not been considered by the Staff in its limited scope rate making analysis. This is illustrated by the Staff's comment in Issue 6 at page 22 of the Recommendation which states "Although staff agrees that there are existing utility plant costs and other expenses which may apply to the reuse project, allocation of existing utility plant costs and other expenses is beyond the scope of this limited filing and should be examined in the utility's next full rate case."

## III. FAILURE TO REALIZE SPECIAL NATURE OF REUSE PROJECT

The Utility, while not unique, is certainly not an average utility. It has plant in service totalling \$25,541,220, over \$20,000,000 of which is CIAC, and only \$2,707,956 in rate base if the Staff's calculations are used. Without considering the special nature of the Utility, the Staff applied the Commission's leverage formula established June 10, 1997, to determine appropriate ROE for the Utility.

This ignores the fact that a Utility with a disproportionately large CIAC when compared to rate base is affected

far more dramatically when the Commission's leverage formula is applied without consideration for the special nature of the Utility. Section 367.081(4) (f) states that:

"The commission may regularly . . . establish by order a leverage formula or formulae that reasonably reflect the range of returns on common equity for an average water, or wastewater utility which, for purposes of this section, shall be used to calculate the last authorized rate of return on equity for any utility which otherwise would have no established rate of return on equity." Section 367.081(4) (f) (Florida Statutes 1997) [emphasis added]

Several parts of the quoted language are pertinent and have been underlined. The Utility is not average. The calculations made for a reuse facility are not being made for the purposes of Section 367.081, but are being made for the purposes of Section 367.0817. Finally, the Utility already has an established rate of return on equity.

The Staff has inappropriately applied the leverage formula in this proceeding. The Utility should be entitled to use of the established return on equity until a full rate case or a specific limited proceeding establishes another rate of return on equity for the Utility.

#### IV. ABILITY TO ATTRACT CAPITAL

By making its determination that the Utility is overearning and then recommending the alleged overearning be used to fund the reuse project, the Staff has advanced a plan that will prevent construction of the reuse project. The Utility does not reasonably believe that a lender will make an approximately \$2,200,000 loan to the Utility to build the reuse facility when the only revenue available to repay the loan is existing revenue of the Utility. This is especially true when existing revenue is generating only \$210,620 in net income on an annual basis as reported by the Utility in its 1996 Annual Report. If all the net income was applied to the debt service on the loan for the reuse facility (assuming a loan could be obtained) there would still be a real cash shortfall of almost \$180,000. There is no practical way that a lender would make a loan to the Utility under this set of facts.

The United States Supreme Court established the criteria for determining the return on investment in Federal Power Commission v. Hope Natural Gas Co., City of Cleveland, 320 U.S. 591, 64 S.Ct. 281 (US 1943) when it stated:

"The return should be sufficient to assure confidence in the financial integrity of the

enterprise, so as to maintain its credit and to attract capital." *Id.* at 601. [emphasis added]

The Staff has recommended a rate structure which negates any ability of the Utility to attract capital. If the Staff's analysis is correct, then the Utility did not need to file a limited proceeding for rates at all. Instead, it needed only to ask the Commission to authorize it to reallocate existing rates to the reuse project. It should have been able to go out in the capital market place and borrow money on its current revenue stream and net income. The simple fact is, it could not, and will not be able to do so without a rate being established for the reuse project

#### V. CONCLUSION

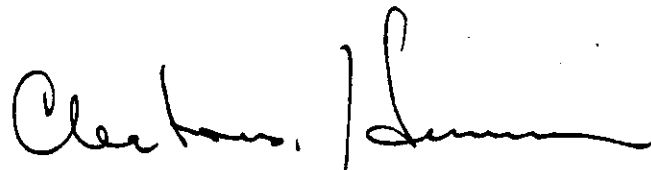
The Staff's Recommendation is counter the law, and counter any practical business logic. Further, the Staff's Recommendation sends the message to all utilities that it is perilous and counterproductive to make a reuse project filing. The Utility believes that such a message is counter to Commission's stated policy, and the Legislature's intent in adopting Section 367.0817, to encourage reuse.

The Utility respectfully requests that the Commission determine that the Staff's Recommendation is flawed, and instead issue a PAA which establishes a fair rate of return for the reuse project.

If the Commission is convinced that the Utility is overearning, it is well within the Commission's authority to order a limited proceeding under Section 367.0822 to deal specifically with overearning, or to order a full rate making proceeding under Section 367.081. The establishment of rates for the reuse project should be, and must be, a separate proceeding as stated above.

The Utility would respectfully request a deferment of this matter for two (2) months. The Utility will, and hereby does, voluntarily request a two (2) month extension of the mandatory five (5) month period provided by statute. This will enable the Utility time to respond more fully to the Staff's Recommendation and also to provide additional information regarding financing requirements and other matters which the Utility believes will be helpful to the Commission in deciding the relevant issues.

Respectfully submitted,



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Attorneys for  
Sanlando Utilities Corporation.

**CERTIFICATE OF SERVICE**

I HEREBY CERTIFY that a true and correct copy of the foregoing has been mailed by U.S. Mail to Jennifer B. Springfield, Esquire, St. Johns River Water Management District, Post Office Box 1429, Palatka, Florida 32178-1429 and to Stephen C. Reilly, Esquire, Office of Public Counsel, c/o the Florida Legislature, 111 West Madison Street, Room 812, Tallahassee, Florida 32399-1400; this 8th day of May, 1998.

