

STORAGE NAME: h0925a.uco

DATE: March 11, 1999

**HOUSE OF REPRESENTATIVES
COMMITTEE ON
UTILITIES AND COMMUNICATIONS
ANALYSIS**

BILL #: HB925

RELATING TO: Public Service Commission

SPONSOR(S): Representative Arnall and others

COMPANION BILL(S): SB 1352(I)

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

- (1) UTILITIES AND COMMUNICATIONS YEAS 9 NAYS 1
 - (2) WATER AND RESOURCE MANAGEMENT
 - (3) TRANSPORTATION AND ECONOMIC DEVELOPMENT APPROPRIATIONS
 - (4)
 - (5)
-

I. SUMMARY:

This bill prohibits the PSC from imputing (deducting) prospective future contributions-in-aid-of-construction, (ciac), on utility investments in property used and useful in the public service.

The bill authorizes the PSC, during a rate proceeding to consider, as used and useful in the public service, utility property including land acquired or facilities constructed or to be constructed if: a) the property is needed to serve current customers; b) the property is needed to serve customers five years after the end of the test year used in the commission's final order on a rate request as provided in s. 367.081(6), F.S., or c) the property is needed to serve customers more than five years after the end of the test year used in PSC's final order on a rate request as provided in subsection (6) only to the extent the utility presents clear and convincing evidence to justify such consideration.

The bill requires the PSC to approve rates for service that allow a utility to recover from customers the full amount of environmental compliance costs. These rates would not include charges for allowances for funds prudently invested or similar charges.

The bill construes the term "environmental compliance costs" to include all reasonable expenses and fair return on any prudent investment incurred by a utility in complying with the requirements or conditions contained in any permitting, enforcement, or similar decisions of the U.S. Environmental Protection Agency, the Department of Environmental Protection, a water management district, or any other governmental entity with similar regulatory jurisdiction.

The bill deletes a requirement that the PSC consider, in setting final rates, a utility's investment in land acquired or facilities constructed or to be constructed in the public interest within a reasonable time in the future, not to exceed 24 months from the end of the historical test year, unless extended by the commission.

The bill has an indeterminate fiscal impact.

This bill takes effect upon becoming law.

STORAGE NAME: h0925a.uco

DATE: March 11, 1999

PAGE 2

II. SUBSTANTIVE ANALYSIS:

A. PRESENT SITUATION:

Pursuant to s. 367.011, Florida Statutes, the Public Service Commission, (PSC), has exclusive jurisdiction over each privately owned water and wastewater utility with respect to its authority, service, and rates. Moreover, a county may, through a resolution adopted by a board of county commissioners, or a declaration by the appropriate board of a charter county, opt to cede regulatory authority over privately owned water and wastewater utilities to the PSC. However, a county, under s. 367.171, F.S., may elect to regulate water and wastewater utilities within its county. If a private utility's service "traverses county boundaries," it is subject to PSC jurisdiction. Currently, the PSC has jurisdiction over 37 counties which comprises approximately 196 water companies and 155 wastewater companies.

Rate setting procedures, for utilities under PSC jurisdiction, are set forth in s. 367.081, F.S., providing that a utility may only charge rates and charges that have been approved by the commission, except as provided in ss. 367.081(4) and 367.081(6), F.S.

Section 367.081, F.S., reads in part:

The commission shall, either upon request or upon its own motion, fix rates which are just, reasonable, compensatory, and not unfairly discriminatory. In every such proceeding, the commission shall consider the value and quality of the service and the cost of providing the service, which shall include, but not be limited to, debt interest; the requirements of the utility for working capital; maintenance, depreciation, tax, and operating expenses incurred in the operation of all property used and useful in the public service; and a fair return on the investment of the utility in property used and useful in the public service.

These variables, when computed, equate to the figure the PSC uses to determine a rate base, and upon which the utility is allowed to earn a rate of return. Within this computation is an element known as margin reserve. Margin reserve is defined in the PSC's Proposed Rule 25-30.431, Florida Administrative Code, as:

the amount of plant capacity needed to preserve and protect the ability of utility facilities to serve existing and future customers in an economically feasible manner that will preclude a deterioration in quality of service and prevent adverse environmental and health effects.

Further the commission's proposed rule states:

the margin reserve period for water source and treatment facilities and wastewater treatment and effluent disposal facilities will be 18 months. In determining whether another margin reserve period is justified, the Commission shall consider the rate of growth in the number of equivalent residential connections (ERCs); the time needed to meet the guidelines of the Department of Environmental Protection (DEP) for planning, designing, and construction of plant expansion; and the technical and economic options available for sizing increments of plant expansion.

Factors that further serve in the computation to establish a rate base are the variables which are deducted from the utility plant in service. These are outlined in s. 367.081(2)(a), F.S., reads in part:

However, the commission shall not allow the inclusion of contributions-in-aid-of-construction in the rate base of any utility during a rate proceeding; and accumulated depreciation on such contributions-in-aid-of-construction shall not be used to reduce the

rate base, nor shall depreciation on such contributed assets be considered a cost of providing utility service. The commission shall also consider the investment of the utility in land acquired or facilities constructed or to be constructed in the public interest within a reasonable time in the future, not to exceed, unless extended by the commission, 24 months from the end of the historical test period used to set final rates.

Section 367.021(3), F.S., provides the definition of contributions-in-aid-of-construction as:

any amount or item of money, services, or property received by a utility, from any person or governmental authority, any portion of which is provided at no cost to the utility, which represents a donation or contribution to the capital of the utility, and which is used to offset the acquisition, improvement, or construction costs of the utility property, facilities, or equipment used to provide utility services.

The most common examples of these assets are cash contributions such as fees paid by customers for connection or hookup to a system, or property contributions such as developer-donated water and sewer lines.

In June 1997, the commission voted to change its policy of imputing (deducting) 100% of contributions-in-aid-of-construction on the margin reserve to imputing 50% on the margin reserve. In other words, the PSC would prospectively deduct 50% of the dollar amount in aid contributed to a utility and remove that 50% from the amount upon which a utility is allowed to earn a return.

Among the precursors of a utility's presentation of this information to the PSC for a rate determination is permitting by a water management district and the Department of Environmental Protection, (DEP). In this process water and wastewater facilities are addressed separately. This procedure is prefaced on a need being established for a facility.

A public water supply facility first track for permitting or licensing is through the appropriate water management district. A facility must obtain both a consumptive use permit and a well construction permit. Section 120.60, F.S., outlines the 90-day time frame which DEP has to approve or deny an application.

Provided an application is complete, a notice of Proposed Agency Action is issued and a governing board review is done. It is within the board's discretion to modify or change staff's recommendation prior to issuing its final approval. Depending upon the utility's use, location, and environmental impact, a permit term ranges from 5 to 20 years.

An applicant then proceeds to obtain DEP construction permitting for the public water system's above ground facilities.

The information necessary for permitting a public water facility includes the collection, treatment, storage, and distribution of the public water system. Subsequent construction or alteration of any segment of the system requires additional permitting.

As codified in Rule 62-555-520, Florida Administrative Code:

(3) A person applying for a permit to construct or alter a public drinking water system should take note of Chapter 471, F.S., which requires that the planning and design of any project involving the public health or safety must be done by a professional engineer licensed in accordance with the Chapter. Further, Chapter 471, F.S., requires that subsequently permitted construction or alteration of public drinking water systems be supervised during construction by a professional engineer. . .

Upon application approval, a letter of clearance is issued and the term of the permit is indefinite, absent violations.

STORAGE NAME: h0925a.uco

DATE: March 11, 1999

PAGE 4

The industry estimates the time for planning, designing, permitting, constructing, and testing/certifying phases of a public water facility is 2.75 - 7.5 years.

An applicant for a wastewater permit applies only to DEP for a new or substantially modified domestic or industrial wastewater facility. Domestic wastewater means wastewater derived principally from dwellings, business buildings, institutions, and the like commonly referred to as sanitary wastewater or sewage. Industrial wastewater means process and non-process wastewater from manufacturing, commercial, mining and silvicultural (processed rocks and logs) facilities or activities, including the runoff and leachate from areas that receive pollutants associated with industrial or commercial storage, handling or processing, and all other wastewater not otherwise defined as domestic wastewater.

Rule 62-620.410(3), Florida Administrative Code, General Application Requirements, governs the required documents which describe the proposed facility or modification. It states:

An applicant shall submit as part of application for a wastewater permit a preliminary design or engineering report and other information in accordance with the Department of Environmental Protection Guide to Wastewater Permitting. A report substantively addressing all of the elements listed in the Guide shall be submitted at least 90 days before construction commences on a facility or activity which discharges solely to surface waters or on a component of a facility or activity which discharges solely to surface waters if the applicant can demonstrate that the component is separable from the entire facility or activity. For all other facilities or activities, the report shall be submitted and made complete with the application for permit.

An applicant for a wastewater permit for an industrial wastewater facility or activity is required to provide an engineering report containing a description of the plant and plant operations, the types and quantities of all waste material, waste control facilities, treatment objectives, design criteria for control facilities, all discharge points, or outfall discharging to ground or surface water.

Applicants for a wastewater permit for a domestic wastewater facility are required to provide a preliminary design report containing information on the current and design year projections for the service area population, the description and map of service area and land use, the forecasts of flow and wastewater characteristics, site plan showing operations and unit processes, flood elevations, an assessment of environmental effects of project, disposal methods or reuse options, technical information and design criteria for the treatment facilities.

According to DEP, an engineering report should typically describe a facility with a 20 year life expectancy.

Rule 62-620.320, Florida Administrative Code, addresses the standards for issuing or denying permits. Rule 62-620.320(8) Florida Administrative Code, provides that DEP can issue a permit for five years or less.

With the issuance of a construction/operational permit, construction begins within 90 days. Throughout the construction phase, status checks of the facility are performed until the facility is completed and ready to go on line.

Rule 17-600.405, Florida Administrative Code, requires a permittee to routinely compare flows being treated at a wastewater facility with the permitted capacities of the treatment, residuals, reuse, and disposal facilities. When the three-month average daily flow exceeds 50% of the permitted capacity of the treatment plant or reuse and disposal systems, the permittee is required to submit an initial capacity analysis report to the Department's appropriate district office. Based on the results of this initial report, the permittee will be required to submit updated capacity analysis reports to the DEP and, possibly, initiate planning, design, and construction of new facilities.

The state permitting requirements for wastewater facilities also incorporate federal permitting requirements.

The industry estimates the time for planning, designing, permitting, constructing, and certifying phases of a wastewater facility is 2.75 - 10 years.

A formal administrative hearing was conducted in December 1997, which challenged the PSC's Proposed Rule 25-30.431, Florida Administrative Code which provides the establishment of the margin reserve. The case is styled Florida Waterworks Association, vs. Florida Public Service Commission, Florida Water Services Corporation vs. Florida Public Service Commission, (Consolidated) Case Nos. 96-3809RP, 97-3480RP, 96-3949, and 97-3481RP. On March 2, 1998, the PSC's rule was determined as an invalid exercise of delegated legislative authority and was not to be utilized by the PSC for its stated regulatory purposes. The PSC and Public Counsel have appealed the decision. Oral arguments have been held before the 1st District Court of Appeal, and a decision is pending.

B. EFFECT OF PROPOSED CHANGES:

The margin reserve in water and wastewater rate cases has been a controversial issue for many years. In June, 1997, the Public Service Commission, (PSC), adopted rules for its policy on margin reserve which provides for the establishment of an 18 month growth allowance. Statutory guidelines describe the variables the PSC is to consider when determining rate base. The bill would broaden the PSC's ability to recognize additional value in certain computation variables.

The bill prohibits the PSC from imputing (deducting) prospective future contributions-in-aid-of-construction on utility investments in property used and useful in the public service.

The bill authorizes the PSC, during a rate proceeding to considers, as used and useful in the public service, utility property including land acquired or facilities constructed or to be constructed if: a) the property is needed to serve current customers, b) the property needed to serve current and future customers for five years after the expected date of a final order on a rate request, or c) the property is needed to serve customers for more than more than five years after the expected date of a final order on a rate request, if the utility presents clear and convincing evidence to justify consideration. It would delete the current requirement that the PSC consider the investment of the utility in property within a "reasonable time in the future, unless extended by the commission, 24 months from the end of the historical test period used to set final rates."

These provisions would increase the margin reserve to five years. According to the industry this would ensure that there is more consistency between PSC economic decisions, DEP, and water management districts planning, design, and construction requirements.

Additionally, with an increased margin reserve, the industry maintains that the bill would encourage the construction of plant in larger increments thereby providing an opportunity to achieve more economies of scale, and arguably in the long run, result in rates lower than would have been possible otherwise.

According to the PSC, the changes in the margin reserve and CIAC would allow the costs of future plant expansion to be recovered from current and future customers. However, this change will effects rates only if a utility files a rate case.

The bill construes the term "environmental compliance costs" to include all reasonable expenses and fair return on any prudent investment incurred by a utility in complying with the requirements or conditions contained in any permitting, enforcement, or similar decisions of the U.S. Environmental Protection Agency, the Department of Environmental Protection, a water management district, or any other governmental entity with similar regulatory jurisdiction.

The bill deletes a requirement that the PSC, in setting final rates, a utility's investment in lands acquired or facilities constructed or to be constructed in the public interest within a reasonable time in the future, not to exceed, unless extended by the commission 24 months from the end of the historical test period used to set final rates.

C. APPLICATION OF PRINCIPLES:

1. Less Government:

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

N/A

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

N/A

(3) any entitlement to a government service or benefit?

N/A

b. If an agency or program is eliminated or reduced:

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

N/A

(2) what is the cost of such responsibility at the new level/agency?

N/A

(3) how is the new agency accountable to the people governed?

N/A

2. Lower Taxes:

a. Does the bill increase anyone's taxes?

N/A

b. Does the bill require or authorize an increase in any fees?

N/A

c. Does the bill reduce total taxes, both rates and revenues?

N/A

d. Does the bill reduce total fees, both rates and revenues?

N/A

e. Does the bill authorize any fee or tax increase by any local government?

N/A

3. Personal Responsibility:

- a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

N/A

- b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

N/A

4. Individual Freedom:

- a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

N/A

- b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

N/A

5. Family Empowerment:

- a. If the bill purports to provide services to families or children:

- (1) Who evaluates the family's needs?

N/A

- (2) Who makes the decisions?

N/A

- (3) Are private alternatives permitted?

N/A

- (4) Are families required to participate in a program?

N/A

- (5) Are families penalized for not participating in a program?

N/A

- b. Does the bill directly affect the legal rights and obligations between family members?

N/A

- c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

STORAGE NAME: h0925a.uco

DATE: March 11, 1999

PAGE 8

(1) parents and guardians?

N/A

(2) service providers?

N/A

(3) government employees/agencies?

N/A

D. STATUTE(S) AFFECTED:

Section 367.081, F.S.

E. SECTION-BY-SECTION ANALYSIS:

N/A

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

4. Total Revenues and Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

STORAGE NAME: h0925a.uco

DATE: March 11, 1999

PAGE 9

1. Direct Private Sector Costs:

Indeterminate.

2. Direct Private Sector Benefits:

According to the industry, allowing for an extended growth margin, utilities would be able to construct in larger plant increments allowing for benefits to be obtained through economies of scale which may allow for long run cost savings to rate payers.

3. Effects on Competition, Private Enterprise and Employment Markets:

None.

D. FISCAL COMMENTS:

According to calculations performed by the PSC last year, based on a rate case, incorporating these provisions, the percentage increases for combined water and wastewater ranged from 0.16% to 7.92%. The percentage increases for water only ranged from 0.00% to 22.34%, and the percentage increases for wastewater only ranged from 0.08% to 31%. The PSC is currently updating these figures.

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

This bill does not require counties or municipalities to spend funds or to take action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This bill does not reduce the authority that municipalities or counties have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

None.

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

N/A

VII. SIGNATURES:

COMMITTEE ON UTILITIES AND COMMUNICATIONS:

Prepared by:

Staff Director:

Wendy G. Holt

Patrick L. "Booter" Imhof