

**The Florida Senate**  
**BILL ANALYSIS AND FISCAL IMPACT STATEMENT**

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Communications, Energy, and Public Utilities Committee

**BILL:** CS/SB 950

**INTRODUCER:** Committee on Environmental Preservation and Conservation and Senator Bennett

**SUBJECT:** Water and Wastewater Utilities

**DATE:** April 6, 2011                      **REVISED:** \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Wiggins	Yeatman	EP	Fav/CS
2.	Wiehle	Carter	CU	Pre-meeting
3.			BC	
4.				
5.				
6.				

<b>Please see Section VIII. for Additional Information:</b>	
A. COMMITTEE SUBSTITUTE.....	<input checked="" type="checkbox"/> Statement of Substantial Changes
B. AMENDMENTS.....	<input type="checkbox"/> Technical amendments were recommended
	<input type="checkbox"/> Amendments were recommended
	<input type="checkbox"/> Significant amendments were recommended

**I. Summary:**

The bill creates a mechanism for regulated water and wastewater utilities to recover, through a surcharge, incurred capital costs for investment in non-revenue producing system improvements. The bill defines eligible projects and the manner in which companies may recover costs through the surcharge.

The bill creates section 367.0819 of the Florida Statutes.

**II. Present Situation:**

Chapter 367, F.S., establishes the authority of the Public Service Commission (PSC or commission) to establish rates of regulated water and wastewater utilities. A regulated water or wastewater utility may only impose and collect rates and charges approved by the PSC.<sup>1</sup> Section 367.081(2) (a), F.S., further specifies that the PSC, “on its own motion or upon request of the utility, may fix rates for the utility that are just, reasonable, compensatory, and not unfairly discriminatory.”<sup>2</sup> The section further provides that the PSC consider: the value and quality of the

<sup>1</sup> See s. 367.081, F.S.

<sup>2</sup> See s. 367.081(2)(a)1., F.S.

service and the cost of providing the service, which includes, but is not 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.

Section 367.0822, F.S., authorizes a utility, in a limited proceeding, to come before the PSC for any matter under its jurisdiction including a request to adjust its rates. Within the proceeding, the PSC must identify issues to be considered and can, upon its discretion, expand the scope of the proceeding to other related matters. A limited proceeding cannot be used to adjust rates if the effect of the adjustment would be to change the last authorized rate of return.

Currently, infrastructure improvements have to be incorporated in utility rates via a PSC proceeding under either s. 367.081(2), F.S., or s. 367.0822, F.S. Current law does not permit these infrastructure improvement surcharges without an evidentiary hearing. According to s. 367.081(2), F.S., the portion of unutilized capacity beyond the five-year period cannot be recovered from current customers.

Section 367.091 (6), F.S., provides that an application through a tariff filing to establish, increase, or change a rate or charge, other than through a rate proceeding pursuant to ss. 367.081, or s. 367.101, F.S., must be accompanied by a cost justification. The statute further provides that the PSC may withhold consent to the operation of any or all portions of the new rate schedules by a vote to that effect within 60 days and must give a reason or statement of good cause for withholding its consent. The PSC must make its final decision on the application within eight months after the official date of filing.

The PSC typically approves or denies tariff filings, giving substantially affected persons a point of entry to file a petition and request a hearing to protest any points of contention with the decision. Substantially affected persons, including customers of the utility, may protest the Proposed Agency Action (PAA), potentially triggering a PSC evidentiary proceeding.

In its Report No. 08-63, the Office of Program Policy Analysis & Government Accountability (OPPAGA) addressed the “unique financial challenges” of small water and wastewater utilities regulated by the PSC. The OPPAGA report notes that these small utility systems, because of a lack of economies of scale, frequently face financial challenges in maintaining system reliability, operating in a cost-effective manner, retaining an adequate labor pool, sustaining a stable financial position, and complying with regulatory requirements. The report also notes that these small utility systems may be reluctant to file for rate increases due to the time and expense involved in rate proceedings and the desire to keep rates low in light of the fact that, in contrast to some larger utilities, they have fewer customers over which to spread costs. The report suggests that the long-term financial viability and adequate investment in infrastructure may suffer as a result.<sup>3</sup>

The OPPAGA report identifies some existing regulatory tools used to address these issues, including staff-assisted rate cases for small water and wastewater utilities, a price index that all

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<sup>3</sup> *The PSC and Legislature Could Consider Several Options to Enhance Services and Consumer Protection*, Office of Program Analysis & Government Accountability, Report No. 08-63, released November 2008.

water and wastewater utilities may apply to major categories of operating costs without a hearing, and pass-through rate adjustments that all water and wastewater utilities may employ for specific types of costs without a hearing. Still, the report suggests that the PSC should monitor small water and wastewater utilities to ensure adequate investment in infrastructure and, if deemed necessary, should consider adopting additional regulatory tools. As an example of such a tool, the report discusses a capital improvement surcharge mechanism by which a temporary surcharge would be added to rates to enable expeditious recovery of costs for qualifying investments and expenditures.<sup>4</sup>

### III. Effect of Proposed Changes:

The bill provides for the recovery of prudently incurred capital costs related to nonrevenue-producing projects to enhance water quality, fire protection reliability, and long-term water system viability through a surcharge. The term “nonrevenue-producing project” is defined to mean a project that is not constructed or installed for the purpose of serving a new customer.

#### Eligibility for surcharge

A project is eligible for recovery of costs through the surcharge if it is:

- Completed and placed into service after the test year upon which base rates were last established by the commission for the utility; and
- For the construction of nonrevenue-producing improvement projects that are used for the production, treatment, transmission, storage, distribution, or provision of potable or recycled water to the public or for the collection, transportation, or disposal of wastewater for the public.<sup>5</sup>

#### Steps to establish a surcharge

To establish a surcharge, a utility must file a proposed surcharge tariff with the PSC. The proposed surcharge tariff must establish a formula for the calculation of rates reflecting the surcharge, with the rates to provide for recovery of depreciation and return on investment for each eligible project. The return on investment for each eligible project must be based on the utility’s last authorized pretax rate of return. The surcharge must be calculated, applied, and recovered in accordance with the utility’s last authorized rate structure.

The utility also must file a sworn affirmation as to the accuracy of the figures and calculations upon which the surcharge is based, stating that the change in rates will not cause the utility to exceed the range of its last authorized rate of return on equity. Any person making a false

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<sup>4</sup> *The PSC and Legislature Could Consider Several Options to Enhance Services and Consumer Protection*, Office of Program Analysis & Government Accountability, Report No. 08-63, released November 2008.

<sup>5</sup> These projects include, but are not limited to, water quality improvement projects designed to achieve primary or secondary water standards as determined by the Department of Environmental Protection, the United States Environmental Protection Agency, or any other governmental entity having similar regulatory jurisdiction; wastewater quality improvement projects; main, service line, and valve replacement projects; main relining and rehabilitation projects; fire and flushing hydrant installation and replacement projects; main extension to eliminate dead ends; interconnection projects; water, wastewater, and reuse meter installation and replacement projects; wastewater collection, replacement, relining, and rehabilitation projects; and manhole replacement and rehabilitation projects.

statement in the affirmation which he or she does not believe to be true in regard to any material matter commits a felony of the third degree.

The utility must also provide notice by mail of the initial surcharge tariff filing to each customer in the affected service areas and publish notice of the surcharge filing in a newspaper of general circulation in the affected service areas.

Upon approval of the surcharge tariff, the utility must maintain and make available for public inspection during normal business hours at each utility location or on the utility's website a detailed schedule for each completed project, including the plant account number and title, the category of the project, the project name and description, the cost of the project in the month of closing, and the month and year of closing.

#### Surcharge costs and oversight

If the utility meets these filing and notice requirements, the PSC must approve the proposed surcharge tariff as a matter of right without hearing within 60 days after the date of filing. The commission has no discretion on whether to approve the surcharge or the amount.

The bill does provide the following limitations on the amount of the surcharge, its effect on earnings, and the accuracy of the surcharge relative to actual costs.

- The total cumulative amount of the surcharge revenue recovered by the utility may not exceed 8 percent of the utility's total revenues for the preceding calendar year, excluding revenues collected through the surcharge.
- The surcharge is to be reevaluated, and if necessary adjusted, on a quarterly basis to reflect the costs of eligible projects placed into service. The utility must file the supporting data to increase or reduce the surcharge with the commission for each revaluation, along with another sworn affirmation that the change in rates will not cause the utility to exceed the range of its last authorized rate of return on equity. The utility must contemporaneously deliver copies of the supporting data and the sworn affirmation to the Office of Public Counsel.
- The surcharge is also subject to an annual reconciliation of revenues and costs with the 12-month period to begin on the date the surcharge tariff is approved. Within 30 days after the end of each reconciliation period, the utility must file with the commission, and deliver to the Office of Public Counsel, a reconciliation report that compares the actual surcharge revenues received and the actual eligible costs incurred by the utility during the prior period, along with another sworn affirmation. A reconciliation report that meets these requirements must be approved without hearing within 45 days after filing. The difference between revenue and costs must be recovered or refunded, as appropriate, by the utility without hearing as an automatic adjustment to the subsequent surcharge calculation. Revenues in excess of system-improvement costs must be refunded with interest to customers pursuant to the commission's rule on interest for water and wastewater utilities.
- If, within 15 months after the filing of a utility's annual report, the commission finds that the utility exceeded the range of its last authorized rate of return on equity, the commission may order the utility to refund, with interest, the difference to the ratepayers and adjust rates accordingly.

- The bill also requires a bond or corporate undertaking in order for the utility to implement the surcharge.

If the utility obtains new base rates that provide for prospective recovery of costs that had previously been recovered under the surcharge, the surcharge amount is to be reset at zero as of the effective date of those base rates. During the proceeding to establish the new base rates, the commission may review the prudence of all projects subject to the surcharge. Revenues from the surcharges are subject to refund if the commission subsequently determines that the costs of a project were not prudently incurred or that the project is not used and useful in the public service, and any such refund must be made pursuant to the commission's rule on refunds for water and wastewater utilities.

The bill takes effect July 1, 2011.

#### **IV. Constitutional Issues:**

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

#### **V. Fiscal Impact Statement:**

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The bill will encourage investment by water and wastewater utilities in infrastructure projects. Utilities who choose to undergo these capital improvements will incur costs for attorney's fees and consulting fees. If their request is protested, the companies will further incur costs associated with defending the request. The proposed changes might allow some companies to obtain quicker rate relief. These capital improvements may improve the job market for occupations related to executing those improvements. Customers of utilities who opt to use this new mechanism will incur surcharges associated with the water and wastewater improvement projects.

C. Government Sector Impact:

According to the PSC, there will be increased costs and up to two FTE's including the cost of two regulatory analysts.

In general, the bill allows more expedient recovery of infrastructure improvement investments by investor owned water and wastewater utilities if no substantially affected person formally protests the PSC's decision. Florida law requires the PSC to give substantially affected persons a point of entry to contest tariff decisions. The likelihood for consumer intervention escalates as the costs of the projects increase. It is not clear whether costly PSC proceedings can be avoided since the decision to approve a tariff may be protested, potentially triggering a PSC evidentiary proceeding. There will be staff time devoted to rulemaking, including, drafting forms as well as writing administrative procedures.

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

According to the PSC, providing rulemaking authority to the PSC would permit the PSC and the industry to develop rule guidance on the appropriate return on equity and mechanisms for updating the procedures related to the collection of surcharges. Further, this could address some of the issues related to increased workload to the agency.

**VIII. Additional Information:**

**A. Committee Substitute – Statement of Substantial Changes:**

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

**CS/SB 950 by the Committee on Environmental Preservation and Conservation on March 23, 2010:**

- deletes “quarterly” as a payment schedule option for the surcharge;
- specifies that surcharge is calculated on the pre-tax rate of return;
- details customer notification requirements;
- requires the utilities to affirm financial data provided that would affect the surcharge calculation, including requiring a detailed reconciliation report, and imposes a third degree felony for providing false statements; and
- specifies that if within 15 months after the filing of a utility's annual report the PSC finds that the utility exceeded the authorized rate of return on equity the PSC may order the utility to offer refunds with interest to the customers and adjust the rates accordingly.

**B. Amendments:**

None.