

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 Committee on Communications, Energy, and Public Utilities

BILL: CS/CS/SB 534

INTRODUCER: Communications, Energy, and Public Utilities Committee; Environmental Preservation and Conservation Committee and Senator Hays

SUBJECT: Water and Wastewater

DATE: January 12, 2016

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Hinton</u>	<u>Rogers</u>	<u>EP</u>	<u>Fav/CS</u>
2.	<u>Caldwell</u>	<u>Caldwell</u>	<u>CU</u>	<u>Fav/CS</u>
3.	_____	_____	<u>AP</u>	_____

Please see Section IX. for Additional Information:

COMMITTEE SUBSTITUTE - Substantial Changes

I. Summary:

CS/CS/SB 534:

- Directs the Division of Bond Finance to review the allocation of private activity bonds in Florida with respect to water and wastewater projects.
- Provides a sales tax exemption for sales or leases to a water or wastewater investor-owned utility (IOU) that hold a certificate of authorization, if the goods or services are used in the state.
- Creates an exemption from PSC regulation for persons who resell water service to individually-metered residents at a price that does not exceed the purchase price of water service plus the actual cost of meter reading and billing, not to exceed 9 percent of the actual cost of the water service.
- Requires the PSC, upon an IOU's request in a rate case, to create a reserve fund for the IOU to be used for certain infrastructure repair and replacement projects, with disbursement subject to PSC approval.
- Identifies specific types of expenses eligible for "pass-through" treatment in IOU rates and authorizes the PSC, by rule, to identify additional types of expenses eligible for such treatment, provided the expenses are beyond the utility's control.
- Prohibits the recovery of an IOU's rate case expense:
 - o For more than one rate case at any given time; and
 - o Where the rate case expense is incurred to prepare or file a staff-assisted rate case in which no party intervenes.

- Provides criteria the commission must use in determining reasonable rate case expense and authorizes the commission to adopt additional criteria by rule. Requires the commission to make findings for each criteria based upon competent substantial evidence and allocate the benefits between the customers and the shareholders, owners, or affiliates.
- Authorizes the PSC, on its own motion or based on customer complaints, to review water quality issues involving secondary drinking water standards (e.g., standards related to odor, taste, and corrosiveness) and wastewater service issues involving odor, noise, aerosol drift, or lighting.
- Expands the availability of low-interest loans through the State Revolving Fund to all for-profit water utilities.
- Requires a county that regulates water or wastewater services to comply with the requirements for abandoned water and wastewater systems.

II. Present Situation:

Water and Wastewater Industry Overview

In various areas throughout Florida, water and wastewater services are provided through privately-owned and operated water and wastewater companies. These privately-owned companies are referred to as “investor-owned utilities,” or “IOUs.” IOUs can range in size from very small systems, owned by individuals as sole proprietorships and serving only a few dozen customers in a small neighborhood, to systems owned by large interstate corporations which serve tens of thousands of customers in multiple Florida counties.

For IOUs operating within a single Florida county, the county has the option to regulate rates and service or allow the Public Service Commission (PSC) to regulate those utilities.¹ Counties that opt to regulate water and wastewater utilities are required to regulate the rates pursuant to s. 367.081(1), (2), (3), and (6), F.S. That section requires that the county approve rates; that the rates are just, reasonable, compensatory, and not unfairly discriminatory; that reasonable costs may be used in determining the revenue requirement; and that the county may withhold consent to the operation of any rate request under certain conditions. Regardless of whether the county has opted to regulate IOUs, the PSC has jurisdiction over all water and wastewater utility systems whose service transverse county boundaries, except for systems owned and regulated by intergovernmental authorities.² Currently, the PSC has jurisdiction over 146 water and wastewater IOUs in 37 of 67 counties in Florida.³ The remaining water and wastewater customers in the state are served either by IOUs in non-jurisdictional counties, by statutorily exempt utilities (such as municipal utilities, cooperatives, and non-profits), by wells and septic tanks, or by systems owned, operated, managed, or controlled by governmental authorities.⁴

¹ s. 367.171, F.S. If a county chooses to allow regulation by the PSC, it may rescind this election only after 10 continuous years of PSC regulation.

² *Id.*

³ *Facts and Figures of the Florida Utility Industry*, Florida Public Service Commission, March 2015, available at <http://www.psc.state.fl.us/publications/reports.aspx>.

⁴ s. 367.022(2), F.S.

For regulatory purposes, the PSC classifies a water or wastewater IOU into one of three categories based on annual operating revenues:⁵

Class A – Operating revenues of \$1,000,000 or more.

Class B – Operating revenues of \$200,000 or more but less than \$1,000,000.

Class C – Operating revenues less than \$200,000.

Currently, there are 13 Class A utilities, 37 Class B utilities, and 96 Class C utilities under the PSC's jurisdiction.

Study Committee on Investor-Owned Water and Wastewater Utility Systems

Chapter 2012-187, Laws of Florida, created the Study Committee on Investor-Owned Water and Wastewater Utility Systems (Study Committee)⁶ to “identify issues of concern of investor-owned water and wastewater utility systems, particularly small systems, and their customers” and to research possible solutions.⁷ Specifically, the Study Committee was required to consider:

- The ability of a small IOU to achieve economies of scale when purchasing equipment, commodities, or services;
- The availability of low interest loans to a small, privately owned water or wastewater utility;
- Any tax incentives or exemptions, temporary or permanent, which are available to a small water or wastewater utility;
- The impact on customer rates if a utility purchases an existing water or wastewater utility system;
- The impact on customer rates of a utility providing service through the use of a reseller; and
- Other issues that the Study Committee identifies during its investigation.⁸

The Study Committee conducted 12 public meetings at which it heard public comment on these issues, identified additional issues for consideration and research (and heard public comment on the additional issues), and discussed and debated solutions to the issues.⁹ Consistent with the law, the Study Committee submitted a report containing its recommendations to the President of the Senate, the Speaker of the House, and the Governor, on February 15, 2013.

⁵ Rules 25-30.110(4) and 25-30.115, F.A.C. As noted in these rules, this classification system is used by the National Association of Regulatory Utility Commissioners for publishing its system of accounts.

⁶ As required by the law, the Study Committee was comprised of 18 members, including three non-voting members and 15 voting members. The three non-voting members included Commissioner Julie I. Brown (representing the PSC as the Study Committee Chair), a representative of the Florida Department of Environmental Protection, and the Public Counsel. The 15 voting members included State Senator Alan Hays (appointed by the President of the Senate), State Representative Ray Pilon (appointed by the Speaker of the House), and representatives of the following entities or groups, as appointed by the Governor: a county commission that regulates investor-owned water/wastewater utilities; a governmental authority created under ch. 163, F.S.; a water management district; a county health department; two Class A utilities; a Class B utility; a Class C utility; a utility owned or operated by a municipal or county government; customers of a Class A utility; customers of a Class B or C utility; the Florida Section of the American Water Works Association; and the Florida Rural Water Association.

⁷ s. 2, Ch. 2012-187, Laws of Fla.

⁸ *Id.*

⁹ See Sections II and III, *Report of the Study Committee on Investor-Owned Water and Wastewater Utility Systems*, February 15, 2013 (*Study Committee Report*), available at <http://www.psc.state.fl.us/utilities/waterwastewater/>.

The Study Committee's report included recommendations for legislative action, agency rulemaking, and other agency action. Based on the issues that it was required to consider, the Study Committee recommended legislative action to do the following:

- Increase the availability of low-interest loans to small, privately owned water and wastewater utilities by:
 - Expanding availability of low-interest loans through the Drinking Water State Revolving Fund (DWSRF) to all for-profit water utilities;
 - Allowing IOUs to apply “pass-through” treatment for loan service fees or loan origination fees for eligible projects as identified by the PSC; and
 - Directing the Division of Bond Finance to review the allocation of private activity bonds in Florida with respect to water and wastewater projects.
- Provide a sales tax exemption for sales or leases to an IOU owned or operated by a Florida corporation.
- Create an exemption from PSC regulation for persons who resell service to individually-metered end-users at a price that does not exceed the actual purchase price of water plus actual costs of meter reading and billing not to exceed 9%.

Based on additional issues that it identified and considered, the Study Committee recommended legislative action to do the following:

- Authorize the PSC, during a rate case, to create individual utility reserve funds to be used for projects identified in an IOU's capital improvement plan, with disbursement subject to approval by the PSC, as a means of reducing borrowing costs and making funds more readily available.
- Identify specific types of expenses eligible for “pass-through” treatment in utility rates and authorize the PSC to adopt rules identifying such expenses, provided the expenses are beyond the utility's control, to help minimize the need for costly rate case proceedings.
- Reduce the impact of rate case expense on customer rates by prohibiting the recovery of rate case expense in certain circumstances.
- Provide a mechanism for the resolution of issues involving secondary water standards (e.g., odor, taste, corrosiveness, etc.) and wastewater operational requirements.

Private Activity Bonds

Qualified private activity bonds are tax-exempt bonds issued by a state or local government, the proceeds of which are used for a defined, qualified purpose by an entity other than the government issuing the bonds. For a private activity bond to be tax-exempt, 95 percent or more of the net bond proceeds must be used for one of the qualified purposes listed in sections 142-145, and 1394 of the Internal Revenue Code, which includes facilities used to furnish water or sewer services.¹⁰ The Internal Revenue Code limits an issuing authority, such as a state, to a maximum amount of tax-exempt bonds that can be issued to finance a particular qualified purpose during a calendar year. Facilities used to furnish water or sewer services are subject to a limit on the amount of tax-exempt bonds that can be issued in a calendar year.¹¹

¹⁰ IRS, *Tax-Exempt Private Activity Bonds, Compliance Guide, Publication 4708*, 2 (Sept. 2005), available at <http://www.irs.gov/pub/irs-pdf/p4078.pdf> (last visited Nov. 10, 2015).

¹¹ *Id.* at 3.

Private activity bonds are administered in Florida by the Division of Bond Finance of the State Board of Administration (division) pursuant to ss. 159.801-159.816, F.S. Each year, the division determines the amount of private activity bonds that can be issued in Florida under the Internal Revenue Code. This amount is allocated yearly on January 1 as follows:

- An initial amount is allocated to manufacturing facility projects;
- Fifty percent of the amount remaining after the initial allocation is allocated to individual counties and groups of counties identified in s. 159.804(2)(b), F.S., on a per capita basis for any permitted purpose, which may include water and sewer projects;
- Twenty-five percent of the amount remaining after the initial allocation is allocated to the Florida Housing Finance Corporation for use in connection with the issuance of housing bonds;
- Five percent of the amount remaining after the initial allocation is allocated to the state allocation pool and applied to priority projects, which may include water and sewer projects; and
- Twenty percent of the amount remaining after the initial allocation is allocated to the Florida First Business allocation pool for projects certified by the Department of Economic Opportunity.¹²

The study committee was unable to determine the amount of private activity bonds that are allocated to water and wastewater projects, or how the private activity bonds can be fairly distributed.¹³

Sales Tax and Use Tax

Florida's sales and use tax is a 6 percent levy on retail sales of a wide array of tangible personal property, admissions, transient lodgings, commercial real estate rentals, and motor vehicles, unless explicitly exempted. In addition, Florida authorizes several local option sales taxes that are levied at the county level on transactions that are subject to the state sales tax. Generally, the sales tax is added to the price of a taxable good and collected from the purchaser at the time of sale. Sales tax represents the majority of Florida's general revenue stream (75.7 percent for the 2014-2015 fiscal year)¹⁴ and is administered by the Department of Revenue (DOR) under chapter 212, F.S.

Resellers of Water Service

As noted above, the PSC currently has jurisdiction to regulate the rates and service of water and wastewater utilities in 37 of 67 counties in Florida. For purposes of the PSC's jurisdiction, "utility" is defined as every person owning, operating, managing, or controlling a system, who is providing water or wastewater service to the public for compensation.¹⁵ However, certain entities

¹² Section 159.804, F.S.

¹³ Florida Public Service Commission, *Report of the Study Committee on Investor-Owned Water and Wastewater Utility Systems*, 43 (Feb. 2013), available at <http://www.floridapsc.com/utilities/waterwastewater/Water-Wastewater%20Sub%20Committee%20Report.pdf> (last visited Nov. 10, 2015).

¹⁴ Florida Revenue Estimating Conference, *2015 Florida Tax Handbook*, 16 (2015), available at <http://edr.state.fl.us/content/revenues/reports/tax-handbook/taxhandbook2015.pdf> (last visited Nov. 12, 2015).

¹⁵ s. 367.021(12), F.S.

that meet this definition are exempt from PSC regulation as utilities.¹⁶ Included among these exemptions are persons who resell water or wastewater service at a rate or charge which does not exceed the actual purchase price of the water or wastewater service.¹⁷ If the reseller includes any additional costs in the rate or charge to the retail customer, the reseller is considered a utility subject to PSC regulation.

Reseller utilities that are regulated by the PSC generally have significant investment in distribution and collection lines and other utility equipment. Examples include mobile home parks and subdivisions. In a rate proceeding, the PSC determines the utility's investment and expenses related to the facilities it owns and operates, then it sets rates accordingly. The cost of the water or wastewater service purchased from a wholesale provider, which is often a significant portion of the customers' bills, is allowed to be passed through to the customers pursuant to s. 367.081(4)(b), F.S. Resellers that choose not to pass along costs beyond their cost to purchase water or wastewater service (and therefore remain exempt from PSC regulation) generally have very little investment in equipment or lines needed to provide the service. Examples include apartment complexes, condominium buildings and small master-metered shopping centers.¹⁸

In its report, the Study Committee noted that a metered charge for water sends an appropriate price signal to end users and is a means of discouraging indiscriminate use of this resource. However, if a reseller wishes to install sub-meters for its users and bill those users for their actual water use, it will be unable recover those metering and billing costs from its customers without becoming regulated and incurring the costs of regulation.¹⁹

Reserve Funds for Water and Wastewater Utilities

The Study Committee considered the availability of low interest loans to small IOUs. In its report, the Study Committee noted the following:

Affordable, accessible financing is an ongoing issue for the water and wastewater industry and is a particularly acute need for smaller systems. Smaller utilities ... have difficulty securing low-cost, long-term financing because the characteristics and track record of the industry make smaller systems more risky in the view of lending institutions. Timing is also an issue, particularly when critical system failures occur and small utilities do not have the cash reserves to address such needs short-term. In addition, regulatory policy frequently does not provide sufficient cash flow to fully service the debt over the term of the loan. The establishment of individual utility reserve funding and/or establishment of a broader statewide reserve fund could reduce borrowing costs and make funding more readily available.²⁰

Section 367.081, F.S., establishes the rate-setting procedures for water and wastewater IOUs regulated by the PSC. However, these procedures do not provide explicit statutory authority for the PSC to establish reserve funds for water and wastewater IOUs during the rate-setting process.

¹⁶ See s. 367.022, F.S.

¹⁷ s. 367.022(8), F.S.

¹⁸ *Study Committee Report*, p. 61.

¹⁹ *Id.*, pp. 61-62.

²⁰ *Id.*, p. 67.

Public Service Commission Ratemaking

Pursuant to s. 367.081, F.S., the PSC establishes rates that are just, reasonable, compensatory, and not unfairly discriminatory. The PSC must consider the value and quality of the service and the cost of providing the service, including:

- Debt interest;
- A utility's working capital requirements;
- 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.

In order for an IOU to increase rates, the utility must file an application for a rate increase with the PSC. This process is referred to as a rate case. The application includes schedules and reports containing the operational, financial, economic, and rate information in order for the PSC staff to evaluate the request. The utility is also required to forecast how much funding is necessary to cover expenses for the next year and the potential return on investment from assets used to provide services. Utilities are limited to adjusting their rates twice during any 12-month period.

In setting rates, the PSC staff reviews the utility's records, conducts site inspections, and evaluates the value and quality of service based on customer input at a rate case hearing or in writing. Following the rate case hearing, the PSC issues a written order with the commissioners' decision on the rate increase. The utility is required to notify the customers of the revised rates.

Pass-Through Costs

Outside of a rate case, PSC-regulated water and wastewater IOUs are entitled to "pass through" specific types of expenses without the requirement of a PSC hearing.²¹ This mechanism provides quick rate relief to a utility when it experiences an increase in one of these types of costs and may help defer the need for a full rate case. Currently, the types of expenses eligible for pass-through treatment are limited by statute to the following:²²

- Purchased water or wastewater service.
- Electric power.
- Ad valorem taxes.
- Regulatory Assessment Fees.
- DEP fees for the National Pollutant Discharge Elimination System Program.
- Water quality or wastewater quality testing required by DEP.

Prior to changing rates using this mechanism, the IOU must file, under oath, an affirmation as to the accuracy of the figures and calculations upon which the change in rates is based and a statement that the change will not cause the utility to exceed the rate of return on equity last approved by the PSC.²³

²¹ s. 367.081(4)(b), F.S.

²² *Id.*

²³ s. 367.081(4)(c), F.S.

Recovery of Rate Case Expense

In a rate case conducted by the PSC, a water or wastewater IOU is entitled to recover its reasonable expenses incurred in preparing and proceeding with the rate case.²⁴ These expenses (referred to as “rate case expense”) typically include legal, engineering, and accounting expenses and are reviewed by the PSC as part of the rate case. Any rate case expense deemed unreasonable by the PSC may not be recovered by the IOU through its rates.²⁵ The amount of rate case expense deemed reasonable is apportioned for recovery through the IOU’s rates over a period of 4 years. At the end of this 4-year period, the IOU’s rates are reduced to remove the impact of the rate case expense.²⁶ According to the Study Committee, the impact of rate case expense on customer bills varies from case to case and is often negligible.²⁷ However, one analysis presented to the Study Committee noted three cases between 2006 and 2011 in which the annual rate impact attributed to rate case expense (over the 4-year recovery period) exceeded the annual revenue increase approved in the rate case, excluding rate case expense. In addition, this analysis noted six additional cases over the same period in which the annual rate impact attributed to rate case expense equaled more than 25 percent of the annual revenue increase approved in the rate case, excluding rate case expense.²⁸

There is no legal limit on the frequency of rate cases. In some instances, an IOU may file for approval to change its rates less than 4 years after its previous rate case. In these cases, the IOUs rates may, for a certain period of time, include rate case expense for more than one rate case, provided that the PSC has determined that there is a reasonable level of rate case expense to be recovered.

A water or wastewater IOU with gross annual revenues under \$275,000 is permitted by law to request and obtain assistance from the PSC staff in preparing the IOU’s rate case.²⁹ These rate cases are referred to as staff-assisted rate cases (SARCs). In these cases, the PSC staff reviews the IOUs books and records, inspects the IOU’s premises, prepares a quality of service analysis, and presents recommended rates and charges to the PSC for consideration. In requesting staff assistance, the IOU agrees to accept the final rates and charges approved by the PSC unless these rates and charges produce less revenue than the existing rates and charges.³⁰ An IOU that uses the SARC process may still seek assistance from other professionals in preparing and proceeding with its case and may submit the associated expenses for recovery as rate case expense.³¹ One analysis presented to the Study Committee showed an average rate case expense of \$4,563 for 23 SARCs conducted between 2007 and 2011 in which some level of rate case expense was approved.³² The average drops to \$3,025 by removing one case.³³

²⁴ s. 367.081(7), F.S.

²⁵ *Id.*

²⁶ s. 367.0816, F.S.

²⁷ *Study Committee Report*, p. 83.

²⁸ *Study Committee Report*, p. 88.

²⁹ s. 367.0814, F.S.

³⁰ *Id.* However, a person other than the utility may protest or appeal the PSC’s order approving the rates and charges.

³¹ *Study Committee Report*, pp. 84-91.

³² *Study Committee Report*, p. 87.

³³ *Id.* Information provided by the PSC indicated that there were approximately 48 SARCs conducted during this time frame, thus the average rate case expense for all SARCs is likely to be lower than this amount.

Secondary Water Standards and Quality of Service

The DEP has the primary authority to implement and enforce federal and state drinking water and wastewater standards. The focus of the DEP's permitting, monitoring, and enforcement of water and wastewater systems is to ensure compliance with primary drinking water standards and wastewater operational requirements to protect the health and safety of the public and the environment.³⁴

The DEP has adopted secondary drinking water standards for aluminum, chloride, copper, fluoride, iron, manganese, silver, sulfate, zinc, color, odor, pH, total dissolved solids, and foaming agents.³⁵ Testing for the secondary standards is required on a regular basis, though the DEP generally requires corrective action only if users voice significant complaints or if a primary contaminant level has also been exceeded.³⁶

The DEP requires that new wastewater treatment plants and modifications to existing plants be designed to minimize odors, noise, aerosol drift, and lighting, which may have an adverse effect on neighboring residential and commercial areas.³⁷ The utilities must provide reasonable assurance that such effects will not be potentially harmful to human health or welfare or unreasonably interfere with the enjoyment of life or property.³⁸ If the existing facilities fail to function as intended and create such adverse effects, the permittee must take corrective action.³⁹ The DEP may also require corrective action if there are significant complaints or if a primary contaminant level has been exceeded.⁴⁰

The PSC considers an IOU's quality of service in rate cases by evaluating the quality of the product, the operating condition of the IOU's plant and facilities, and the IOU's efforts to address customer satisfaction.⁴¹ Sanitary surveys, outstanding citations, violations, and consent orders on file with the DEP and county health departments are also considered. In addition, the DEP and county health department officials' testimony and customer testimony concerning quality of service is considered.⁴² In most cases, the emphasis of this evaluation is on compliance with standards related to the health and safety of the public and the environment.⁴³

³⁴ See ch. 403, F.S., and Rules 62-550, 62-555, 62-602, and 62-699, F.A.C., for drinking water regulations, and Rules 62-600, 62-604, 62-610, 62-620, 62-621, and 62-640, F.A.C., for wastewater regulations.

³⁵ Rule 62-550.320, F.A.C.

³⁶ Florida Public Service Commission, *Report of the Study Committee on Investor-Owned Water and Wastewater Utility Systems*, 113 (Feb. 2013), available at <http://www.floridapsc.com/utilities/waterwastewater/Water-Wastewater%20Sub%20Committee%20Report.pdf> (last visited Nov. 10, 2015).

³⁷ Rule 62-600.400(2)(a), F.A.C.

³⁸ *Id.*

³⁹ Rule 62-600.410, F.A.C.

⁴⁰ Florida Public Service Commission, *Report of the Study Committee on Investor-Owned Water and Wastewater Utility Systems*, 113 (Feb. 2013), available at <http://www.floridapsc.com/utilities/waterwastewater/Water-Wastewater%20Sub%20Committee%20Report.pdf> (last visited Nov. 10, 2015).

⁴¹ Rule 25-30.433(1), F.A.C.

⁴² *Id.*

⁴³ Florida Public Service Commission, *Report of the Study Committee on Investor-Owned Water and Wastewater Utility Systems*, 106 (Feb. 2013), available at <http://www.floridapsc.com/utilities/waterwastewater/Water-Wastewater%20Sub%20Committee%20Report.pdf> (last visited Nov. 10, 2015).

Chapter 2014-68, Laws of Florida, created s. 367.072, F.S., to provide a process for customers to petition the PSC to require compliance with secondary water quality standards. If a utility fails to comply with PSC orders, the process could result in revocation of the utility's certificate of authority. The law provides petition criteria and factors the PSC must consider in its review of the petition and the action it may take to dispose of the petition. Once a petition has been filed in compliance with the section, a utility is prohibited from filing a rate case until the PSC has issued a final order.

Chapter 2014-68, Laws of Florida, also created s. 367.0812, F.S., to add secondary water quality standards to the criteria that the PSC must consider when setting rates for water service. The law authorizes the PSC to reduce the utility's return on equity up to 100 basis points (1 percent) or deny all or part of a rate increase for a utility's system or part of a system if it determines that the quality of water service is less than satisfactory for the time the system remains unsatisfactory. The law requires a utility to provide an estimate of the costs and benefits of plausible solutions for each concern that the PSC finds, meet with the customers to discuss the costs and benefits of the solution, and periodically report on the progress of implementation. The PSC may require the utility to resolve certain problems and require benchmarks and periodic progress reporting. The law authorizes the PSC to adopt rules to assess and enforce compliance with the secondary water standards and prescribe penalties for a utility's failure to adequately address each concern.

Section 367.111, F.S., requires each utility to provide service to its service area within a reasonable time. It authorizes the PSC to amend the service territory or rescind the certificate of authorization of a utility that has failed to provide service as required or it is more feasible for another utility to provide such service. The section also requires each utility to provide safe, efficient, and sufficient service as prescribed by Part VI of ch. 403, F.S., and Parts I and II of ch. 373, F.S. If the PSC determines that an IOU has failed to provide its customers with water or wastewater service that meets the standards set by the DEP or the water management districts, the PSC may reduce the IOU's return on equity until the standards are met.⁴⁴

III. Effect of Proposed Changes:

Section 1 creates s. 159.8105, F.S., to require the Division of Bond Finance of the State Board of Administration to review the allocation of private activity bonds to determine the availability of additional allocations of reallocations of private activity bonds for water and wastewater infrastructure projects.

Section 2 amends s. 212.08, F.S., relating to sales and use tax to provide a tax exemption for sales or leases to investor-owned water or wastewater utilities holding a certificate of authorization under the jurisdiction of the commission if the sole or primary function of the utility is to construct, maintain, or operate a water or wastewater system in Florida and if the goods or services purchased or leased are used in Florida.

⁴⁴ Section 367.111(2), F.S.

Section 3 amends s. 367.022, F.S., relating to exemptions from PSC regulation to provide that any person who resells water service to his or her tenants or to individually metered residents for a fee that does not exceed the actual purchase price of the water service plus the actual cost of meter reading and billing, not to exceed nine percent of the actual cost of the water service, is exempt from regulation by the PSC as a utility and from the provisions of ch. 367, F.S., which concerns water and wastewater systems.

Section 4 amends s. 367.081, F.S., relating to fixing and changing rates to authorize the PSC on its own motion or upon the request of a utility to create a utility reserve fund for infrastructure repair and replacement for a utility for distribution and collection infrastructure that is nearing the end of its useful life or is detrimental to water quality or reliability of service. The fund is to be funded by a portion of the rates charged by the utility, by a secured escrow account, or through a letter of credit.

The bill requires the PSC to adopt rules to govern the implementation, management, and use of the fund, including but not limited to:

- Expenses for which the fund may be used;
- Segregation of reserve account funds;
- Requirements for a capital improvement plan; and
- Requirements for PSC authorization before disbursements are made from the fund.

In addition, the bill adds the following items to the list of costs eligible for pass-through treatment:

- Fees charged for wastewater biosolids disposal;
- Costs incurred for any tank inspection required by the DEP or local governmental authority;
- Treatment plant operator and water distribution system operator license fees required by the DEP or local governmental authority; and
- Consumptive use or water use permit fees charged by a water management district.

The bill authorizes the PSC, by rule, to establish additional specific expense items eligible for pass-through treatment. To be eligible for such treatment, an additional expense item must be imposed by a local, state, or federal law, rule, order, or notice and must be outside the control of the utility. If the PSC uses this authority, it must review its rule at least once every 5 years to determine if each specific expense item should remain eligible for pass-through treatment or if any additional expense items should become eligible.

The bill continues the current requirement that an IOU wishing to change its rates to reflect a change in any of these costs must provide verified notice to the PSC 45 days before implementing a change in its rates. The bill provides that the new rates must reflect, on an amortized or annual basis, as appropriate, the cost or amount of change in the cost of the specified expense item. Further, the bill provides that the new rates may not reflect the costs of any specific expense item already included in the IOU's rates. The bill also continues the current prohibition on use of the pass-through mechanism for increases or decreases in a specific expense item that occurred more than 12 months before the IOU's filing.

The bill requires the commission to consider specific criteria to determine reasonable rate case expense and disallow rate case expense it does not find reasonable. The commission may adopt additional criteria by rule. In addition, the commission must make its findings for each criteria based upon competent, substantial evidence. Finally, the commission may allocate accordingly the benefits of the rate case expense between the customers and the shareholders, owners, or affiliates.

Section 5 amends s. 367.0814, F.S., relating to changing rates and charges in a staff assisted rate case to detail expenses associated with rate cases that may and may not be recovered.

The bill prohibits the PSC, where the IOU has requested a staff-assisted rate case, from approving rate case expense to cover fees for attorneys and other outside consultants who are engaged by a utility for purposes of preparing or filing the case, unless another party has intervened in the case. The bill provides two exceptions. It authorizes the recovery of rate expense for such fees if the fees are incurred to provide consulting or legal services to the utility after the initial PSC staff report is issued to customers and the utility. It also requires that the PSC allow recovery of rate case expense for such fees incurred after any protest or appeal of the PSC's decision by a party other than the IOU.

The PSC is required to adopt rules to administer this provision by December 31, 2016.

Section 6 amends s. 367.0816, F.S., relating to recovery of rate case expenses to prevent a utility from recovering the four-year amortized rate case expense for more than one rate case at any given time. The bill requires a utility, when it begins recovery of approved rate case expense associated with a new rate case, to discontinue the recovery of any uncollected rate case expense approved in a prior rate case. This provision appears intended to discourage the frequent filing of rate cases to avoid "pancaking" of rate case expense in customer rates from more than one rate case at a time. In some instances, this may discourage a utility from filing a necessary rate case, though it may also result in more careful consideration by a utility of the costs, timing, and need to file a rate case.

Section 7 amends s. 367.111, F.S., to allow the PSC, on its own motion or based on complaints of customers of a water utility subject to the PSC's jurisdiction, to review water quality as it pertains to secondary drinking water standards established by the DEP or review wastewater service as it pertains to odor, noise, aerosol drift, or lighting.

Section 8 amends s. 367.165, F.S., to require a county that regulates water or wastewater services to comply with the requirements for abandoned water and wastewater systems.

Section 9 amends s. 403.8532, F.S., to increase the number of entities that are eligible for DWSRF loans by allowing the DEP to make loans to for-profit, privately owned, or investor-owned water systems.

In order to conform to this change, the bill also deletes an existing provision relating to loans for projects for a for-profit, privately owned or investor owned water system that serves 1,500 service connections or more within a single certified or franchised area.

Section 10 provides an effective date of July 1, 2016.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

With regard to the provisions that limit the collection of rate case expense to one case in any given four years or in staff assisted rate cases, according to the PSC “by denying or limiting reasonable rate case expense, the legislation may result in confiscatory ratemaking, or a regulatory taking, in violation of federal and state constitutional protections against taking private property for public use without just compensation.”⁴⁵ Whether these provisions prove confiscatory may depend on how the provisions are implemented.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

The revenue estimating conference estimates that the total impact of the sales-tax exemption in section two of the bill for fiscal year 2016-2017 is a reduction of \$3.4 million (\$3.7 million recurring) of which a reduction of \$2.7 million (\$3.0 million recurring) is on General Revenue, and a reduction of \$700,000 (\$700,000 recurring) is on local government. The impact on state trust funds is negative but insignificant.

B. Private Sector Impact:

The water and wastewater IOUs that qualify for the sales tax exemption in s. 212.08, F.S., will realize a positive fiscal impact.

By allowing for the recovery of expenses associated with meter reading and billing, the bill may encourage resellers to use individual metering more often for their tenants. Water users can be charged more accurately for the water they consume; therefore, they may experience a positive or negative fiscal impact, depending on their water use.

⁴⁵ PSC, *Senate Bill 534 Agency Analysis* (Nov. 12, 2015) (on file with the Senate Committee on Communications, Energy, and Public Utilities).

The establishment of individual utility reserve funds may reduce borrowing costs and make funding more readily available for PSC-regulated water and wastewater IOUs to make needed improvements and repairs. In some instances, the availability of these reserve funds may allow IOUs to avoid or defer the need for a rate case, providing a cost savings to the ratepayers for this expense.

The expanded availability of pass-through treatment for new expense items may, in some instances, allows IOUs to avoid or defer the need for a rate case, providing a cost savings to the ratepayer.

The limitation of rate case expenses for staff assisted rate cases may benefit the rate payer; however, the utilities' rates may increase to ensure compliance with secondary water and wastewater standards.

If the utility has to petition for new rates within four years, it may be forced to forfeit the unamortized rate case expense, increasing costs to the utility and decreasing costs to the ratepayer.

Proving up each criteria for reasonable rate case expense may increase the utility's cost for rate case expense.

The expanded availability of low-interest financing through the DWSRF to additional water and wastewater IOUs may encourage more of these utilities to make investments in water infrastructure at a lower cost to ratepayers. Lending institutions that have the ability to evaluate the credit worthiness of the large private systems may experience an increase in revenue.

C. Government Sector Impact:

The bill appears to have an insignificant impact on state government expenditures.

The PSC has not identified an impact on agency expenditures; however, it may be required to expend resources to complete rulemaking as required by the bill. In its analysis of a similar bill filed in 2015, the Department of Revenue identified an insignificant impact on its expenditures. DEP, in its analysis of the same bill filed in 2015, estimated additional expenditures of between \$10,000 and \$100,000 to employ additional expertise needed to evaluate the credit worthiness of large, complex water systems that become eligible under the bill to seek low-interest loans through the DWSRF; however, it indicated that these costs will be covered by service fees collected in the normal course of the DWSRF program and the actual costs would depend on the number of systems that request funding.

VI. Technical Deficiencies:

None.

VII. Related Issues:

According to the PSC, the bill does not address how the provision of the bill concerning the surcharge a person who resells water service to his or her tenants is allowed to charge would be enforced or what proof the water reseller may need to provide to the PSC. Additionally, the change may require the PSC to adopt rules to implement this provision. It is unclear if the bill provides specific rulemaking authority for this provision.⁴⁶

Section 5 of the bill seems to anticipate intervention by parties other than the Office of Public Counsel prior to the issuance of a proposed agency action. According to the PSC, this is inconsistent with how staff-assisted rate cases are processed.⁴⁷

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 212.08, 367.022, 367.081, 367.0814, 367.0816, 367.111, 403.8532, and 367.171.

This bill creates section 159.8105 of the Florida Statutes.

IX. Additional Information:**A. Committee Substitute – Statement of Substantial Changes:**
(Summarizing differences between the Committee Substitute and the prior version of the bill.)**CS/CS by Communications, Energy, and Public Utilities on January 12, 2016:**

- Adds language to clarify that investor-owned water or wastewater utilities holding a certificate of authorization under the jurisdiction of the commission are exempt from the sales and use tax.
- Revises the new provision relating to exemptions to conform terms: the exemption applies to water service.
- Authorizing the commission on its own motion or upon the request of a utility to require a utility to create a utility reserve fund for infrastructure repair or replacement.
- Removes the cap of 50 percent on the amount of reasonable rate case expense that can be recovered by a utility. Instead, the commission is given criteria it must evaluate in determining reasonable rate case expense and disallow rate case expense it does not find reasonable. The commission may adopt additional criteria by rule. In addition, the commission must make its findings for each criteria based upon competent, substantial evidence. Finally, the commission may allocate accordingly the benefits of the rate case expense between the customers and the shareholders, owners, or affiliates.
- Requires a county that regulates water or wastewater services to comply with the requirements for abandoned water and wastewater systems.

⁴⁶ PSC, *Senate Bill 776 Agency Analysis* (Mar. 13, 2015) (on file with the Senate Committee on Environmental Preservation and Conservation).

⁴⁷ *Id.*

- Removes s. 367.171, F.S., from the bill as the changes are made now in s. 367.165, F.S.

CS by Environmental Preservation and Conservation on November 18, 2015:

Removes a provision that limits a tax exemption for investor owned water and wastewater utilities to those that are owned or operated by a Florida corporation. This change allows the tax exemption to apply to investor owned water and wastewater utility, regardless of whether the utility is owned or operated by a Florida corporation.

Changes a provision that a tax exemption applies to utilities that are owned by a corporation. The amendment changes the word “corporation” to “utility.”

Changes the date the PSC must adopt certain rules from December 31, 2015 to December 31, 2016.

B. Amendments:

None.