

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** CS/HB 357 Water and Wastewater Utility Systems

**SPONSOR(S):** Finance & Tax Subcommittee; Santiago

**TIED BILLS:** **IDEN./SIM. BILLS:** SB 1050

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Energy & Utilities Subcommittee	11 Y, 2 N	Keating	Keating
2) Finance & Tax Subcommittee	15 Y, 3 N, As CS	Flieger	Langston
3) Regulatory Affairs Committee	17 Y, 1 N	Keating	Hamon

### SUMMARY ANALYSIS

Chapter 2012-187, Laws of Florida, created the Study Committee on Investor-Owned Water and Wastewater Utility Systems (Study Committee) to “identify issues of concern of investor-owned water and wastewater utility systems, particularly small systems, and their customers” and to research possible solutions. Consistent with the law, the Study Committee submitted a report containing its recommendations to the Speaker of the House, the President of the Senate, and the Governor, on February 15, 2013.

CS/HB 357 adopts several of the Study Committee’s recommendations for legislative action. In particular, the bill:

- Expands the availability of low-interest loans through the State Revolving Fund (SRF) to all for-profit water utilities.
- Directs the Division of Bond Finance to review the allocation of private activity bonds (PABs) in Florida with respect to water and wastewater projects.
- Creates an exemption from Public Service Commission (PSC) regulation for persons who resell water service to individually-metered end-users at a price that does not exceed the purchase price of water plus 9 percent or the purchase price of water plus actual costs of meter reading and billing.
- Authorizes the PSC, during a rate case, to create an individual IOU reserve fund to be used for projects identified in an IOU’s capital improvement plan, with disbursement subject to approval by the PSC.
- 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.
- Provides a mechanism, within a rate case, for the identification and potential resolution of issues involving secondary drinking water standards (e.g., standards related to odor, taste, and corrosiveness) and wastewater operational requirements related to odor, noise, aerosol drift, and lighting.

In addition to the above, the bill provides that IOUs may recover certain costs and expenses related to compliance with secondary water standards through a rate case, separate proceeding, or tariffs establishing a surcharge.

The bill has no fiscal impact.

The effective date of the bill is July 1, 2014.

# FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

### A. EFFECT OF PROPOSED CHANGES:

#### **Present Situation**

##### Background

##### *Water and Wastewater Industry Overview*

In various areas throughout Florida, water and wastewater services are provided through privately-owned and operated water and/or 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.<sup>1</sup> 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.<sup>2</sup> The PSC currently has jurisdiction over water and wastewater IOUs in 37 of 67 counties in Florida, accounting for approximately 120,567 water customers and 74,317 wastewater customers.<sup>3</sup> 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.<sup>4</sup>

For regulatory purposes, the PSC classifies an IOU into one of three categories based on annual operating revenues:<sup>5</sup>

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

As of 2012, there were 14 Class A utilities, 33 Class B utilities, and 93 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)<sup>6</sup> to “identify issues of concern of investor-owned water

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<sup>1</sup> Section 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.

<sup>2</sup> *Id.*

<sup>3</sup> *Facts and Figures of the Florida Utility Industry*, Florida Public Service Commission, April 2013.

<sup>4</sup> Section 367.022(2), F.S.

<sup>5</sup> 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.

<sup>6</sup> 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, as appointed by the Governor: a county commission that regulates investor-owned water/wastewater utilities; a governmental authority created under Chapter 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

and wastewater utility systems, particularly small systems, and their customers” and to research possible solutions.<sup>7</sup> 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.<sup>8</sup>

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.<sup>9</sup> Consistent with the law, the Study Committee submitted a report containing its recommendations to the Speaker of the House, the President of the Senate, and the Governor, on February 15, 2013.

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 State Revolving Fund (SRF) 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 (PABs) 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 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/or 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.

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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.

<sup>7</sup> Chapter 2012-187, Laws of Florida, Section 2.

<sup>8</sup> *Id.*

<sup>9</sup> See Sections II and III, *Report of the Study Committee on Investor-Owned Water and Wastewater Utility Systems*, dated February 15, 2013 (*Study Committee Report*).

## *Drinking Water State Revolving Fund*

Sections 403.8532 and 403.8533, F.S., establish the SRF. The SRF, which is administered by the Department of Environmental Protection (DEP), provides low-interest loans to eligible entities for planning, designing, and constructing public water facilities. Eligible entities include, among others, investor-owned public water systems that are legally responsible for public water services and which serve no more than 1,500 connections.<sup>10</sup> Projects eligible for SRF loans include new construction and improvements of public water systems, inclusive of storage, transmission, treatment, disinfection, and distribution facilities.<sup>11</sup> Loan funding is based on a priority system which takes into account public health considerations, compliance, and affordability.<sup>12</sup>

Based on data gathered from IOU's 2011 annual reports filed with the PSC, the Study Committee determined that all Class C water IOUs and almost all (28 out of 33) Class B water IOUs serve no more than 1,500 connections and are therefore eligible for the SRF program.<sup>13</sup> The remaining PSC-regulated Class B and Class A water IOUs are, presumably, not eligible to use the SRF program.

## *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% or more of the net bond proceeds must be used for one of the qualified purposes listed in sections 142 through 145, and 1394 of the Internal Revenue Code (the Code). These qualified purposes include facilities used to furnish water or sewer services. The 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 volume cap.<sup>14</sup>

Private activity bonds are administered in Florida by the Division of Bond Finance of the State Board of Administration (the Division) under sections 159.801-159.816, F.S. Each year, the Division determines the amount of private activity bonds permitted to be issued in Florida under the Code.<sup>15</sup> This amount is allocated on January 1 of each year as follows:<sup>16</sup>

- An initial amount is allocated to manufacturing facility projects.
- 50 percent of the amount remaining after the initial allocation is allocated to individual counties and groups of counties<sup>17</sup> on a per capita basis for any permitted purpose, which may include water and sewer projects.
- 25 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.
- 5 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.
- 20 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.

The Study Committee was unable to determine the amount of private activity bonds ultimately utilized for water and sewer projects in Florida.<sup>18</sup>

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<sup>10</sup> Section 403.8532(3), F.S. An investor-owned public water system that serves more than 1,500 connections may qualify for a loan only if the proposed project will result in the consolidation of two or more public water systems.

<sup>11</sup> <http://www.dep.state.fl.us/water/wff/dwsrf/ellocgov.htm> (most recently accessed on January 31, 2014)

<sup>12</sup> Section 403.8532(9)(a), F.S.

<sup>13</sup> *Study Committee Report*, pp. 36-37. The report notes that this data does not include water IOUs that are regulated by counties.

<sup>14</sup> *Tax-Exempt Private Activity Bonds, Compliance Guide*, Internal Revenue Service Publication 4078, Version 09-2005.

<sup>15</sup> Section 159.804, F.S.

<sup>16</sup> *Id.*

<sup>17</sup> These individual counties and groups of counties are identified in section 159.804(2)(b), F.S.

<sup>18</sup> *Study Committee Report*, p. 43.

## *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.<sup>19</sup> However, certain entities that meet this definition are exempt from PSC regulation as utilities.<sup>20</sup> 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.<sup>21</sup> 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 and/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 Section 367.081(4)(b), F.S. Resellers that choose not to pass along costs beyond their cost to purchase water or wastewater (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.<sup>22</sup>

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.<sup>23</sup>

## *Reserve Funds for Water and Wastewater Utilities*

As noted above, the Study Committee was required to consider, among other things, the availability of low interest loans to a small, privately owned water or wastewater utility. 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 short-term needs. 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.<sup>24</sup>

Section 367.081, F.S., establishes the rate-setting procedures for water and wastewater IOUs regulated by the PSC. None of these procedures provides explicit statutory authority for the PSC to establish reserve funds for water and wastewater IOUs during the rate-setting process.

## *Pass-Through Costs*

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<sup>19</sup> Section 367.021(12), F.S.

<sup>20</sup> See Section 367.022, F.S.

<sup>21</sup> Section 367.022(8), F.S.

<sup>22</sup> *Study Committee Report*, p. 61.

<sup>23</sup> *Id.*, pp. 61-62.

<sup>24</sup> *Id.*, p. 67.

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.<sup>25</sup> 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:<sup>26</sup>

- 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.<sup>27</sup>

### *Quality of Service / Secondary Standards*

DEP is the state agency with primary authority to implement and enforce federal and state drinking water and wastewater standards. The focus of 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.<sup>28</sup>

With respect to drinking water, DEP has also adopted secondary standards for contaminants related to color, corrosion, and odor.<sup>29</sup> Testing for these secondary standards is required on a regular basis, though DEP generally requires corrective action only if users (i.e., water customers) voice significant complaints or if a primary contaminant level has also been exceeded.

With respect to wastewater, DEP requires that new treatment plants and modifications to existing plants be designed and sited to minimize adverse effects on neighboring residential and commercial areas resulting from odors, noise, aerosol drift, and lighting.<sup>30</sup> Permittees must give 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.<sup>31</sup> Likewise, if existing facilities fail to function as intended and create such adverse effects, the permittee must take corrective action, or DEP may require corrective action.<sup>32</sup> DEP generally requires corrective action only in response to significant complaints or if a primary contaminant level has also been exceeded.<sup>33</sup>

As previously noted, the PSC considers an IOU’s quality of service in rate cases. In doing so, the PSC evaluates the quality of the product, the operating condition of the IOU’s plant and facilities, and the IOU’s efforts to address customer satisfaction.<sup>34</sup> Sanitary surveys, outstanding citations, violations and consent orders on file with DEP and county health departments are also considered. In addition, DEP and county health department officials’ testimony and customer testimony concerning quality of service is considered.<sup>35</sup> In most cases, the emphasis of this evaluation is compliance with standards related to

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<sup>25</sup> Section 367.081(4)(b), F.S.

<sup>26</sup> *Id.*

<sup>27</sup> Section 367.081(4)(c), F.S.

<sup>28</sup> See Chapter 403, F.S., and Chapters 62-550, 555, 602, and 699, F.A.C., for drinking water regulations, and Chapters 62-600, 604, 610, 620, 621, and 640, F.A.C., for wastewater regulations.

<sup>29</sup> Rule 62-550.320, F.A.C.

<sup>30</sup> Rule 62-600.400(2)(a), F.A.C.

<sup>31</sup> *Id.*

<sup>32</sup> Rule 62-600.410, F.A.C.

<sup>33</sup> *Study Committee Report*, p. 105.

<sup>34</sup> Rule 25-30.433(1), F.A.C.

<sup>35</sup> *Id.*

health and safety of the public and the environment.<sup>36</sup> If the PSC finds that an IOU has failed to provide its customers with water or wastewater service that meets the standards set by DEP or the water management districts, the PSC may reduce the IOU's return on equity until the standards are met.<sup>37</sup>

## Effect of Proposed Changes

CS/HB 357 adopts several of the Study Committee's recommendations for legislative action. In particular, the bill:

- Expands the availability of low-interest loans through the SRF to all for-profit water utilities.
- Directs the Division of Bond Finance to review the allocation of PABs in Florida with respect to water and wastewater projects.
- Creates an exemption from PSC regulation for persons who resell water service to individually-metered end-users at a price that does not exceed the purchase price of water plus 9 percent or the purchase price of water plus actual costs of meter reading and billing.
- Authorizes the PSC, during a rate case, to create an individual IOU reserve fund to be used for projects identified in an IOU's capital improvement plan, with disbursement subject to approval by the PSC.
- 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.
- Provides a mechanism, within a rate case, for the identification and potential resolution of issues involving secondary drinking water standards (e.g., standards related to odor, taste, and corrosiveness) and wastewater operational requirements related to odor, noise, aerosol drift, and lighting.

In addition to the above, the bill provides that IOUs may recover certain costs and expenses related to compliance with secondary water standards through a rate case, separate proceeding, or by filing tariffs establishing a surcharge.

### *Drinking Water State Revolving Fund*

The bill removes the current size restrictions on water IOUs eligible to utilize the SRF. Water IOUs of any size will be eligible to seek low-interest loans through the SRF for planning, designing, and constructing public water facilities, including storage, transmission, treatment, disinfection, and distribution facilities.

### *Private Activity Bonds*

The bill directs the Division of Bond Finance of the State Board of Administration to review the allocation of PABs to determine the availability of additional allocation or reallocation of PABs for facilities used to furnish water or sewer services.

### *Resellers of Water Service*

The bill creates an exemption from PSC regulation for a person who resells water service to his or her tenants or to individually metered residents for a fee that does not exceed the reseller's actual purchase price of the water plus: (1) up to 9 percent of the actual purchase price; or (2) the actual cost of meter reading and billing.

Absent this exemption, a water reseller who charges more than the actual purchase price of the water would be subject to PSC regulation and would incur the costs and obligations of such regulation. While

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<sup>36</sup> *Study Committee Report*, p. 106.

<sup>37</sup> Section 367.111(2), F.S.

the costs would be recoverable from the reseller's customers through PSC-approved rates, a reseller may not wish to incur the additional regulatory obligations.

This provision may encourage resellers to utilize individual metering more often for their tenants. Through individual metering, water users can be charged more accurately for the water they consume. Thus, customers of resellers who utilize individual metering may be more likely to use water more efficiently.

#### *Reserve Funds for Water and Wastewater IOUs*

The bill authorizes the PSC, in a rate case proceeding, to create a reserve fund for a water or wastewater IOU. The bill directs the PSC to adopt rules to govern such a fund. These rules must include, but are not limited to:

- Provisions related to the expenses for which the fund may be used.
- Segregation of the reserve fund accounts.
- Requirements for the IOU to maintain a capital improvement plan.
- Requirements for PSC authorization prior to disbursements from the fund.

The establishment of individual reserve funds may reduce borrowing costs and make funding more readily available for PSC-regulated water and wastewater IOUs. IOUs may be able to avoid the need to access capital markets to finance certain projects and repairs and/or to request a rate increase to cover the costs of the projects and repairs.

#### *Pass-Through Costs*

The bill expands the types of expenses eligible for "pass-through" treatment in IOU rates by adding the following expense items:

- Fees charged for wastewater sludge removal.
- A loan service fee or loan origination fee associated with a loan related to an eligible project, as specified by PSC rule, provided that the project is associated with new infrastructure or improvements to existing infrastructure needed to achieve or maintain compliance with primary or secondary drinking water standards or wastewater treatment standards that relate to:
  - The provision of water or wastewater service for existing customers;
  - The violation or prevention of a violation of primary or secondary health standards;
  - The replacement or upgrade of water or wastewater infrastructure if needed to achieve or maintain compliance with primary or secondary regulations; or
  - Projects consistent with the most recent long-range plan of the IOU on file with PSC, except for projects primarily intended to serve future growth.
- Costs incurred for a tank inspection required by DEP or a local government authority.
- Operator and distribution license fees required by DEP or a local government authority.
- Water or wastewater operating permit fees charged by DEP or a local government authority.
- Consumptive or water use permit fees charged by a water management district.

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 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.

### *Quality of Service / Secondary Standards*

The bill creates a mechanism, within the context of a rate case, for the identification and potential resolution of issues involving secondary drinking water standards (e.g., standards related to odor, taste, and corrosiveness) and wastewater operational requirements related to odor, noise, aerosol drift, and lighting.

The bill requires the PSC, in determining the value and quality of water service provided by an IOU, to consider the extent to which the IOU meets secondary drinking water standards established by DEP and the local government. In making this determination, the PSC must consider: testimony and evidence provided by customers and the utility; relevant complaints filed during the previous 5 years with the PSC, DEP, county health departments, or the local government; results of past tests required by DEP or county health departments to measure compliance with secondary standards; and results of other tests that the PSC deems necessary.

The bill also requires the PSC, in determining the value and quality of wastewater service provided by an IOU, to consider the extent to which the IOU provides service in a manner that does not cause odor, noise, aerosol drift, or lighting that adversely affects customers. In making this determination, the PSC must consider: testimony and evidence provided by customers and the utility; and relevant complaints filed during the previous 5 years with the PSC, DEP, county health departments, or the local government.

If, as a result of these analyses, the PSC determines that the IOU's water service does not meet secondary drinking water standards or that the IOU's wastewater service adversely affects customers due to odor, noise, aerosol drift, or lighting, the IOU must take the following steps:

- Provide estimates of the costs and benefits of various solutions to the problems;
- Meet with its customers to discuss the costs and benefits of the various solutions; and
- Report the conclusions of these customer meetings to the PSC.

The bill requires the PSC to adopt rules necessary to assess and enforce the IOU's compliance with these provisions. These rules must prescribe penalties, including fines and reduction of return on equity of up to 100 basis points, if an IOU "fails to adequately address of offer solutions to the water or wastewater problems."

The bill does not explicitly require that the IOU take any action, such as repairs or improvements, to remedy the problem. Thus, the circumstances in which an IOU could be penalized for failure to "adequately address" a particular problem are unclear. Further, given the somewhat subjective nature of some of these issues (e.g., what is an acceptable odor, taste, or noise level) and the possibility for localized problems on an IOU's system, there may not be consensus among all customers as to whether a problem has been adequately addressed.

### *Cost Recovery for Secondary Water Standard Compliance*

The bill provides that a utility may recover its prudently incurred costs and expenses to resolve deficiencies found by the PSC or the DEP regarding secondary drinking water standards related to taste, odor, color, or corrosiveness or regarding wastewater service issues related to odor, noise, aerosol drift, or lighting. These costs will be recoverable either through a rate case or through a separate proceeding initiated by petition of the utility.

The bill also authorizes a water utility to file a tariff establishing a surcharge by which the utility may recover prudently incurred fixed costs of a system improvement project completed and placed in service between rate cases. To qualify, the purpose of the project must be to achieve or maintain

compliance with secondary drinking water standards related to taste, odor, color, or corrosiveness. The bill requires PSC approval of a project as a condition of cost recovery through the surcharge.

**B. SECTION DIRECTORY:**

- Section 1.** Creates s. 159.8105, F.S., requiring the Division of Bond Finance to review the allocation of private activity bonds.
- Section 2.** Amends s. 367.022, F.S., relating to exemptions to regulation by the Public Service Commission.
- Section 3.** Amends s. 367.081, F.S., relating to the procedure for fixing and changing rates.
- Section 4.** Amends s. 367.0814, F.S., conforming a cross-reference.
- Section 5.** Amends s. 403.8532, F.S., relating to use of the drinking water state revolving loan fund.
- Section 6.** Provides an effective date of July 1, 2014.

**II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT**

**A. FISCAL IMPACT ON STATE GOVERNMENT:**

1. Revenues:

None.

2. Expenditures:

None. 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.

**B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

1. Revenues:

None.

2. Expenditures:

None.

**C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

*Drinking Water State Revolving Fund*

The expanded availability of low-interest financing through the State Revolving Fund to additional water IOUs may encourage more of these utilities to make investments in water infrastructure in the state at a lower cost to ratepayers than would otherwise result from such expenditures.

*Private Activity Bonds*

To the extent that additional private activity bonds are made available for eligible projects, more water and wastewater IOUs may be encouraged to make investments in water and wastewater infrastructure in the state at a lower cost to ratepayers than would otherwise result from such expenditures.

*Resellers of Water Service*

The creation of a regulatory exemption for water resellers who add no more than the costs of meter reading and billing or, alternatively, up to a 9 percent charge to their purchase price for water, will remove the costs and obligations of regulation for these resellers and may encourage them to invest in individual metering apparatus.

#### *Reserve Funds for Water and Wastewater IOUs*

The establishment of individual 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, the expense of which ultimately would be borne by ratepayers.

#### *Pass-Through Costs*

The expanded availability of “pass-through” treatment for new expense items may, in some instances, allow IOUs to avoid or defer the need for a rate case, the expense of which ultimately would be borne by ratepayers.

#### *Quality of Service / Secondary Standards*

Depending on the PSC’s application of the mechanism established to identify and potentially resolve secondary drinking water quality issues and wastewater operational issues, IOUs may be compelled to incur additional costs to resolve these issues. To the extent that an IOU is compelled to incur additional costs, these costs will likely be recovered from ratepayers through the mechanisms provided by the bill.

#### D. FISCAL COMMENTS:

None.

### **III. COMMENTS**

#### A. CONSTITUTIONAL ISSUES:

##### 1. Applicability of Municipality/County Mandates Provision:

Not Applicable. This bill does not appear to require counties or municipalities to spend funds or take action requiring the expenditures of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of state tax shared with counties or municipalities.

##### 2. Other:

None.

#### B. RULE-MAKING AUTHORITY:

The bill requires the PSC to adopt rules:

- To assess and enforce compliance with the provisions that create a mechanism for the identification and potential resolution of issues involving secondary drinking water standards and wastewater operational requirements, including the prescription of penalties if an IOU fails to adequately address or offer solutions to the issues identified.
- To govern the operation of individual utility reserve funds created by the PSC.

- To govern the determination of projects for which loan service fees or loan origination fees are eligible for pass-through treatment in IOU rates.

The bill authorizes the PSC to adopt rules establishing additional specific expense items eligible for pass-through treatment in IOU rates.

#### C. DRAFTING ISSUES OR OTHER COMMENTS:

The bill provides a list of specified expense items eligible for pass-through treatment in IOU rates but indicates that the list is not exclusive. Thus, the bill is ambiguous as to what types of other expense items might also be eligible for pass-through treatment.

With respect to the mechanism established to identify and address issues involving secondary drinking water standards and wastewater operational requirements, the bill does not require that the IOU make repairs or improvements to resolve an identified issue but requires the PSC to establish, by rule, penalties for an IOU's failure to "adequately address" the problem. Thus, it is unclear what is required of a utility to "adequately address" a problem.

#### **IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES**

The Finance and Tax Subcommittee adopted four amendments on March 13, 2014. These amendments:

- Removed a proposed sales tax exemption.
- Allowed utilities to recover costs incurred to resolve deficiencies found by the PSC or DEP with respect to secondary drinking water standards or certain wastewater service issues.
- Authorized water utilities to establish a surcharge to recover fixed costs of system improvements intended to maintain or achieve compliance with secondary drinking water standards.
- Removed proposed limits on rate case expense recovery.

This analysis is drafted to the committee substitute that incorporates the amendments.