Florida Public Service Commission

Fletcher Building
101 East Gaines Street
Tallahassee, Florida 32399-0850

MEMORANDUM

July 27, 1990

TO : DIRECTOR, DIVISION OF RECORDS AND REPORTING

FROM: DIVISION OF ELECTRIC AND GAS (JENKINS) JDJ
DIVISION OF AUDITING AND FINANCIAL ANALYSIS (DEVLIN)
DIVISION OF LEGAL SERVICES (VANDIVER)

RE : DOCKET NO. 891345-EI, APPLICATION OF GULF POWER COMPANY FOR A RATE INCREASE

AGENDA : AUGUST 9, 10 AND 14, 1990 - SPECIAL AGENDA

CRITICAL DATES : 8-MONTH EFFECTIVE DATE: 08/15/90

Attached are the original, 7 tabbed copies and 14 untabbed copies of the Staff's recommendation in the above referenced docket.

The following table summarizes the Staff's recommendation:

Adjusted Rate Base	$915,892,000
Required Rate of Return	x 8.05%
Required Net Operating Income	$ 73.708,000
Achieved Net Operating Income	-63,290,000
NOI Deficiency	$ 10,417,000
Revenue Expansion Factor	x 1.631699
Revenue Increase	$ 16,998,000
50 Basis Point ROE Reduction	- 2,420,000
Total Revenue Increase	$ 14,577,000

The Cost of Service and Rate Design portions of this recommendation are scheduled to be filed on Monday, July 30, 1990.

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ISSUE 1: Gulf Power has proposed a rate base of $923,562,000 ($1,192,516,000 System) for the test year. What is the appropriate level of rate base for 1990? (MERTA)

RECOMMENDATION: The appropriate level of rate base for 1990 is $915,892,000.

POSITION OF PARTIES

GULF: The appropriate level of rate base for 1990 is $923,562,000 ($1,192,516,000 System).

OPC: The proper level of rate base is $843,931,000.

FEA: The FEA takes the samu position as the Office of the Public Counsel.

STAFF ANALYSIS: The parties' positions are shown on the following table and are discussed in the appropriate issues.

1990 Rate Base
Jurisdictional
(000's)

	Gulf	Staff	Public Counsel
Utility Plant-in-Service	$1,275,624	$1,273,451	$1,211,673
Accumulated Depreciation	(454,964)	(454,774)	(452,005)
Net Plant-in-Service	$820,660	$818,677	$759,668
Const. Work in Progress	14,949	14,949	14,949
Prop. Held for Future Use	3,925	3,790	71
Acquisition Adjustment	2,317	0	0
Net Utility Plant	$841,851	$837,416	$774,688
Working Capital	81,711	78,476	69,243
Total Rate Base	$923,562	$915,892	$843,931

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ISSUE 2: The company has included $1,275,624,000 ($1,307,579,000 System) of plant in service in rate base. Is this appropriate? (ROMIG)

RECOMMENDATION: No. The appropriate amount of Plant-in-Service is $1,273,451 after making adjustments in specific issues.

POSITION OF PARTIES

GULF: Yes.

OPC: No. Based on an actual vs. projected analysis for August, 1989 through March, 1990, the total company plant is overstated by $11,458,000 ($11,178,000 jurisdictional). Plant Scherer should be removed from plant-in-service as not currently needed for retail generation. Net plant-in-service is $1,209,506 ($1,239,805 system).

STAFF ANALYSIS: OPC Witness Larkin has recommended a $11,753,000 reduction in the company's projected plant-in-service based on August, 1989 through February, 1990 actual data (T. 2199). These amounts were then used in a linear regression analysis to determine the over projections of $11,753,000.

Mr. McMillan stated that Mr. Larkin's numbers are significantly understated by using a prior 24-month period, which included some large non-recurring reductions in plant-in-service, i.e., coal car retirements and two refunds related to Scherer Unit 3 (T. 754-755).

Mr. Larkin stated that he did not attempt to update his analysis and adjust his base for these known variations.

Mr. McMillan testified that it is important to consider all components that affect rate base not just the variances that may exist in plant-in-service.

Staff would agree that all components that affect plant should be considered, i.e., plant-in-service, CWIP, and accumulated depreciation. Also, the most current data available should be used and agreed to by Mr. Larkin (T. 2264).

Gulf filed Late-Filed Exhibit 570 which compared actual to budget for the period ended May, 1990. Based on this exhibit Gulf was under budget by a total amount of $4,662,000. After adjusting for the two refunds received from Georgia Power and Oglethorpe Power Corp. in the amount of $5,267,000, the company was over budget by $605,000.

Staff recommends no adjustment to the company's projected plant-in-service.

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ISSUE 3: Gulf capitalized $1,964,394 ($6,937,131 System) in excess of the original cost capitalized by Georgia Power Company for its 25% share of Plant Scherer, Unit No. 3. Is this appropriate? (REVELL)

RECOMMENDATION: No. Plant-in-Service should be reduced by $1,520,118 ($5,279,291 system), Accumulated Depreciation should be reduced by $172,313, and Depreciation Expense should be reduced by $48,702.

POSITION OF PARTIES

GULF: In 1989, subsequent to preparation of the test year budget, Georgia agreed to refund to Gulf a portion of the purchase price related to the tax adder for AFUDC equity and certain deferred taxes related to Unit 3. As a result of the renegotiated price, the following adjustments to our forecast are required:
(McMillan)

	System $	Jurisdictional $
Plant in service	(5,279,291)	(1,520,118)
Accumulated Depreciation	(598,433)	(172,313)
Depreciation Expense	(169,116)	(48,702)
Deferred Income Taxes	1,333,211	383,885

OPC: No. In the event the Commission decides to allow Plant Scherer in rate base, no acquisition adjustment should be included in rate base. (Larkin)

STAFF ANALYSIS: In 1984, Gulf Power purchased a 25% interest in Plant Scherer Unit No. 3 from Georgia Power, an affiliated company. The unit was under construction at the time of purchase. In determining the purchase price, Georgia Power used the amount in Account 107 (Construction Work in Progress) less the AFUDC accrual, plus state income taxes on the sale and a carrying charge based on its incremental debt and equity costs. The difference of $1,520,118 ($5,279,291 System) represents an amount in excess of actual construction costs of the generating unit.

All parties, including Gulf Power, acknowledge that the company paid in excess of the original costs for its 25% share of Unit 3 at Plant Scherer. The figure of $1,964,394 in excess costs was a number prepared by the interim filing for the test period ended September 30, 1989. At that time, negotiations were still on-going with FERC, who had originally pointed out the overpayment, as to the exact amount of excess paid to Georgia Power. A more accurate figure for year end 1990 of Gulf's overpayment is $1,520,118 ($5,279,291 System). Gulf says FERC has tentatively approved these figures but has not received the final audit report.

Based on the above, staff recommends that Plant-in-Service be reduced by $1,520,118 ($5,279,291 System), Accumulated Depreciation be reduced by $172,313, and Depreciation Expense be reduced by $48,702.

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ISSUE 4: As a result of its purchase of a portion of the common facilities at Plant Scherer, Gulf recorded an acquisition adjustment of $2,458,067 ($8,680,507 System). Is this appropriate? (MERTA)

RECOMMENDATION: No. If the Commission allows Plant Scherer in rate base, the acquisition adjustment should be disallowed (Reduce Plant-in-Service by $141,000, Acquisition Adjustment by $2,317,000, and Amortization Expense by $73,000 jurisdictional).

If the Commission allows the acquisition adjustment, then reductions should be made to reflect the impact of the refund and reduction in the cost of the common facilities which were recorded on Gulf's books in 1989. (Reduce Plant-in-Service by $180,976, Acquisition Adjustment by $4,337, Accumulated Depreciation by $21,143, and Depreciation Expense by $5,599 jurisdictional).

POSITION OF PARTIES

GULF: Yes. The acquisition adjustment represents Gulf's share of the carrying charges incurred by the selling utilities, and does not represent a profit over the actual cost for the facilities. These costs are appropriately included in rate base.

OPC: No. In the event the Commission decides to allow Plant Scherer in rate base, no acquisition adjustment should be included in rate base.

STAFF ANALYSIS: If the Commission does not allow Plant Scherer in rate base, this issue will be moot.

Georgia Power Company (Georgia) sold its undivided ownership in Plant Scherer common facilities to joint owners Oglethorpe Power Corporation (Oglethorpe) and the City of Dalton (Dalton) in 1977 and 1980, respectively. Pursuant to the Agreement, Georgia would purchase back these common facilities in proportionate share when Unit 3 came on line in January 1987. Gulf bought into the Scherer facility in 1984 and assumed this responsibility from Georgia. On November 19, 1987, Gulf Power Company purchased its 6.25 percent proportionate share of the production plant facilities common to all four Scherer generating units from Oglethorpe and Dalton thereby fulfilling Georgia's obligation. (TR 335-336).

Gulf paid a net price of $29,131,850 for the facilities. The original cost of the facilities was $24,266,406. The difference of $4,865,444 represents the interest (carrying costs) incurred by Oglethorpe and Dalton until the date of sale to Gulf. The $8,680,507 acquisition adjustment is made up of three components: interest in the amount of $4,865,444; accumulated depreciation of $3,796,376; and legal fees in connection with the purchase of $18,687. (TR 337-338).

In April, 1988, Gulf requested approval from the Federal Energy Regulatory Commission (FERC) of its accounting for the common facilities. In its initial filing with FERC, Gulf requested amortization of the acquisition adjustment to Account 425, Miscellaneous Amortization, a below-the-line account. FERC approved this accounting treatment in May, 1988. Gulf subsequently requested that FERC approve amortization of the acquisition adjustment above-the-line. In a November 2, 1988, letter, FERC ordered Gulf to amortize the acquisition adjustment below-the-line and indicated that Gulf could resubmit its request if Gulf could demonstrate specific offsetting benefits to all customers, or if the adjustment was ruled fully recoverable through rates by the FPSC. In June 1989, May 1990, and again in June 1990, Gulf requested amortization above-the-line and submitted information and justification to FERC. This matter is still unresolved. At the present time, Gulf is amortizing the acquisition adjustment to Account 406, Amortization of Electric Plant Acquisition Adjustment, an above-the-line account. (TR 405-406).

The Company believes that the inclusion or exclusion of the acquisition adjustment should be based on the reasonableness and prudency of the amount paid for the asset purchased. Under the contract between Gulf, Oglethorpe and Dalton, Gulf was required only to reimburse the selling utilities for actual costs incurred through the date of purchase. (Gulf Brief p. 10-12). Mr. Scarbrough testified that the selling utilities made no profit on the sale of the common facilities to Gulf, but were simply made whole on the transfer. Ratepayers received a benefit because generating capacity was obtained at less cost than building a new coal unit. (TR 338).

Public Counsel pointed out that the Commission has always held that no acquisition adjustments should be included in rate base. OPC believes that to allow recovery of this acquisition adjustment in rate base would set a precedent in future cases and open the floodgates to acquisition adjustments of all kinds. (OPC Brief p. 4). Public Counsel also takes exception to Gulf's "value received" argument. Since the fair market value of an asset is very often greater than the book value, the Commission would surely not allow utility companies to start reselling their plant assets between themselves at "fair value" and thus create acquisition adjustments on all over-depreciated plant. (OPC Brief p. 4). Whether or not Dalton and Oglethorpe properly recognized the depreciation on the facilities, the fact remains they are now not worth as much as they would be if they were brand new.

Public Counsel believes that Exhibit 553, December 8, 1989, "Audit of the Oglethorpe Power Corporation Sales Price Adjustment for Plant Scherer Common Facilities" makes the Company's claimed purchase price suspect. The exhibit refers to a "revised gain" which seems to contradict Gulf's claim that there was no profit to anyone. (OPC Brief p. 6, TR 338).

Longstanding Commission policy is to disallow acquisition adjustments in rate base unless the company can demonstrate extraordinary circumstances or prove a net benefit to ratepayers. In Order No. 15598, Docket No. 850552-WU, Southern States Utilities, Inc., the Commission stated:

> Commission policy dictates that positive acquisition adjustments are excluded from rate base absent extraordinary circumstances attending the transfer, under the premise that these excess costs provide no additional benefit to ratepayers....We therefore decline to include any positive acquisition adjustment in the new owner's rate base....

The Commission upheld its policy in Order No. 23166, Docket No. 891179-GU, Central Florida Gas Co. and Plant City Natural Gas Co., Divisions of Chesapeake Utilities Corp.. In this case, the Commission removed the acquisition adjustment from rate base because the Company failed to demonstrate net benefits to its ratepayers.

Docket No. 891309-WS, Investigation of Acquisition Adjustment Policy, is currently open. Staff's recommendation is not to change the Commission's current policy that in the absence of extraordinary circumstances, a subsequent purchase of a utility system at a premium or discount shall not affect the rate base calculation.

In Staff's opinion, Gulf has not demonstrated that ratepayers will receive net benefits by allowing the acquisition adjustment in rate base. There was no showing of cost savings or operating efficiencies warranting recovery.

The Company's accounting for the acquisition adjustment was noted as a compliance exception by FERC in its Compliance Audit for the Audit Period 1985 through 1988. Gulf's accounting treatment is not consistent with the requirements of the Uniform System of Accounts. Gulf is amortizing the acquisition adjustment to Account 406, above-the-line. The instructions for Account 406 state:

> This account shall be debited or credited, as the case may be, with amounts includible in operating expenses, <u>pursuant to approval of the Commission</u>... (emphasis supplied)

The Company has not received FPSC or FERC approval to include the acquisition adjustment and its amortization in rates. Until that time, the acquisition adjustment should be amortized to Account 425, below-the-line, as ordered by FERC in its November 2, 1988 letter.

Based on the foregoing, Staff recommends that Plant-in-Service be reduced by $141,000, Acquisition Adjustment by $2,317,000, and Depreciation and Amortization Expense by $73,000.

During the course of a Southern Company Services audit, it was discovered that certain Scherer Unit 2 amounts had been inappropriately classified as common facilities, and were included in the purchase price that Gulf paid to Oglethorpe. As a result, Oglethorpe made a refund to Gulf in 1989. (TR 404).

In the event that the Commission allows the acquisition adjustment in rate base, Plant-in-Service should be reduced by $180,976, Acquisition Adjustment by $4,337, Accumulated Depreciation and Amortization by $21,143, and Depreciation and Amortization Expense by $5,599 in order to reflect the impact of the refund and reduction in cost of the common facilities.

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ISSUE 5: Is the $31,645,000 total cost for the new corporate headquarters land, building, and furnishings reasonable? (MERTA)

RECOMMENDATION: The costs of the new corporate headquarters should be adjusted to remove $54,099 related to the Business Development Center.

POSITION OF PARTIES

GULF: Yes. The total cost for the Corporate Headquarters is reasonable and should be included in rate base.

OPC: The costs of the new corporate headquarters should be adjusted to remove any excessive costs and costs associated with non used and useful land and building space as determined by this Commission. Numerous inquiries and exhibits were requested concerning this issue (e.g., T. 1603-1612, 1638-1655, 3634-3637, 3640-3642, 3683-3751, 3752-3758, 3835). Once all exhibits are received, the Commission should remove any excess rate base and expense items that are found.

STAFF ANALYSIS: In 1982, faced with overcrowding at the Pace Boulevard building, Gulf commissioned a study to evaluate the space problem. The "Corporate and Western Division Survey" identified a combined deficiency of 30,000 square feet of office for the General Office and Western Division functions. The study evaluated three alternatives. Alternative I: Maintain both the Western Division and General Office functions at the Pace Boulevard site. This would involve major construction additions to the two existing buildings. Alternative II: Construct a new Western Division Headquarters building on a different site and maintain the General Office functions at Pace Boulevard. Construction additions would still be necessary to the Pace building. Alternative III: Construct a new Corporate Headquarters building at a new site to house the General Office functions and relocate Western Division personnel to the Pace Boulevard building. This eliminated the need for office construction additions on the Pace Boulevard site. Alternative III was approved by the Company as being the most cost effective solution. (TR 1605-1606.

Another 1982 study, "Space Allocation Plan" identified the need to secure 62,000 square feet of temporary office space and recommended that the space be obtained as leased office space. The Company rejected this plan as too costly for such a temporary measure. The Company converted 15 residences located on land recently purchased at the Pace Boulevard site into temporary office space and leased two other buildings to provide approximately 40,000 square feet of temporary space. (TR 1608-1609).

Daniels Realty conducted a study in 1982 to examine feasible sites for the new Corporate Headquarters building. Their study evaluated two sites: the Hawkshaw site located in downtown Pensacola and a site in the University Mall area outside the city. The Hawkshaw site was chosen because of certain land use regulations, a substantial transportation network system, adequate supporting utilities, proximity to the central business district, and adequate fire and police protection. In addition, Gulf already owned a 1.2 acre former substation site in the Hawkshaw area and land prices in the Hawkshaw area were comparable to acquisition costs at the Pace Boulevard site and the northeast section of Pensacola. Acquisition of additional land began in 1982. (TR 1609-1610).

In 1984, Marshall Associates, Inc., reevaluated the Hawkshaw location prior to the initiation of final building design. Their conclusion was that the Hawkshaw site was still the best alternative since it could be obtained at cost comparable with other prospective locations. (TR 1610-1611).

The total costs for the building, design fees, site work, plant-in-service land, building equipment, overheads, and furnishings were $31,645 000. (TR 1611-1612).

Mr. Conner discussed the three phases used to provide office growth space in the five story structure. Short range growth was provided in vacant workstation spaces on the first, second, fourth, and fifth floors. Intermediate growth space was provided by leaving the third floor unfinished. It is used as a maintenance and storage area until needed for office space. Provisions were made in the site planning to accommodate another building for growth beyond the year 2010. (TR 3638-3639).

The Business Development Center occupies 495 square feet on the first floor of the Corporate Headquarters Building. The room was designed and furnished for presentations to representatives of businesses that are interested in moving to Northwest Florida, and for press conferences relating to weather-related emergencies. (TR 1638-1641). The Center is equipped with laser disk players, color monitors, and VCR's that allow prospective business customers to view various areas, industrial parks, and cities in Northwest Florida with an eye toward relocation to this area. Mr. Conner testified that the purpose of the laser disk players and VCR's is their use in economic development efforts not for hurricane warnings and the like. (TR 1641). The investment capitalized for the Business Development Center in 1987 was $54,099. There has been no capital investment since 1987 and none is projected for 1990. (TR 1638-1639, Late Filed Exhibit No. 597). Staff recommends that $54,098 be removed from rate base for the Business Development Center, since the recruitment of business and industry to Florida is not the responsibility of a regulated public utility. The Chamber of Commerce and the Florida Department of Commerce perform that function.

The Commission Staff reviewed Gulf's need for and use of the Corporate Office building and associated land and issued a document entitled "Final Report on Corporate Office Building, Gulf Power Company, Project PE-872 (3336), AW 408951 (E-84-14)," dated May 23, 1989. (Exhibit No. 163). The report concludes that the construction costs of the building are reasonable and as designed, would be approximately the same regardless of the site (North Pace Boulevard, University Mall area, or Bayfront).

The corporate office building occupies 17.42 acres on Bayfront Parkway overlooking Pensacola Bay. The building is five stories tall and each floor has approximately 50,000 square feet of space. A level below the building is for parking company vehicles. The building was occupied March 31, 1987.

The 17.42 acres (758,928 square feet) of land is used as follows:

Building	1.31 acres
Roads & Parking	4.87
Sidewalks	1.40
Landscape or green area	9.82
	17.42

The total cost of the land presently in plant-in-service is $3,905,675. The cost is $224,172 per acre. (Exhibit 163)

Staff is recommending no disallowance for land use since Gulf plans to use areas now landscaped for parking facilities in the future. In addition, City zoning regulations require space allotted to landscaping and green areas.

The total building area is 308,634 square feet and consists of 149,945 square feet of office space, 57,057 square feet of parking garage, 51,563 square feet on the third floor, presently unfinished and used as temporary storage and a maintenance area, 41,237 square feet for specialty areas, and 8,832 square feet for the equipment room. The specialty areas are the mailroom and duplicating, cafeteria, system control and ready room, auditorium, MIS computer center, communications, and the like.

Staff believes the cost for the new corporate headquarters is reasonable. It is prudent when planning a new building to provide for the future growth of the company. It makes sense to expand into an initially somewhat oversized structure when the incremental cost of the larger building is less than expanding the existing facilities. Since rates are set prospectively, the growth of the Company into its new building can be justified.

Since 1984, throughout its service area, Gulf has added 15 new buildings demolished 8 and sold 1. The total utility related additions since 1984 is 416,688 square feet of building space (including the new corporate office building) consisting of 142,873 square feet for warehousing and division support, 107,126 square feet for the specialty areas, parking garage and equipment room in the new corporate office building, 76,679 square feet for corporate office functions, 72,438 square feet for customer and line service areas, and 19,100 square feet for training areas. The total investment in land and buildings less depreciation has increased by $35,584,000 since 1984. Since Gulf's last rate case, 129 new utility employees have been hired. The number of employees per number of customers served was .0044 in 1984 and .0041 in 1990. (Late Filed Exhibit No. 598).

In analyzing the total building area square feet per employee, Staff calculated 268 square feet per employee in 1984 and 482 square feet per employee in 1990 using the data in Late Filed Exhibit 598. The "Training,", "Nonutility," and "Other" categories and the "nonutility employees" were removed from the calculations. This calculation is of limited value since it includes warehousing, division support, and customer and line functions which require large space allocations. In the corporate office function, Staff calculated 215 square feet per employee in 1984 and 366 square feet per employee in 1990. The 1990 calculation was skewed by the Pace Boulevard Complex. Five corporate office employees associated with the Employment Center occupy 10,361 square feet at the Pace Complex. This appears somewhat excessive. Looking at the new corporate office alone, there is 346 square feet per employee. The national average for office space is 240 square feet per employee.

While Staff is not proposing an adjustment for Gulf's space utilization, it should be noted that Gulf has more than enough "room to grow."

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ISSUE 6: Is the Caryville "sod farm" operation being properly accounted for by Gulf Power Company? (ROMIG)

RECOMMENDATION: The "sod farm" operations are properly accounted for. However, lease revenues of $3,450 should be removed and rate base should be reduced by $135,200 ($139,800 System).

POSITION OF PARTIES

GULF: Yes. (Scarbrough)

OPC: In the event the sod farm operations are determined to be subsidized by the ratepayers, the Commission should remove these costs as non utility in nature.

STAFF ANALYSIS: Gulf included the following in its brief (pages 17-18)).

> The sod farm, known as "Southern Sod Company", occupies approximately 200 acres of property at the Caryville site, or 10% of the Caryville acreage. (T. 3844) Southern Sod leases this acreage from Gulf, and the lease payments are credited to the ratepayer in electric department Account 455, "Interdepartmental Rents". (T-3783) The lease payments include all of the sod farm's share of property taxes levied on the Caryville property as well. (T-3845) The sod farm operations are accounted for properly, and none of the expenses or investment associated with this activity are being charged to the ratepayer. As Gulf witness Mr. Scarbrough explained, the company's revenues and expenses from the sod farm are recorded in Account 417, "Revenues from Non-Utility Operations", a "below-the-line" account. Income taxes associated with the sod farm are recorded in below-the-line Account 409-2, "Income Taxes - Other Income and Deductions", and payroll taxes for sod farm employees are recorded in below-the-line Account 408-2, "Taxes Other Than Income Taxes - Other Income and Deductions". Investment in the trailer located on the sod farm premises and miscellaneous sod farm equipment is recorded in below-the-line Account 121, "Non-Utility Property". (T-3783)

Staff does not take exception to Gulf's accounting for the "sod farm" operation, i.e., sales of sod and related expenses, and the fact that any related lease payments offset the carrying costs of the Caryville site being included in rate base.

In addition to the "sod farm" operation, Gulf also has two other non-utility activities, Appliance Sales and Service and Vision Design. Gulf properly accounts for these operations below-the-line including the allocation of common use buildings or land space to non-utility operations. Gulf's treatment of the "sod farm" is inconsistent. Therefore, staff recommends the removal of 10% of the amount of the Caryville site included in rate base or $135,200 ($139,800 System) to be consistent with Gulf's treatment of its other non-utility activities. It would also be appropriate to remove from other revenues the $3,450 in lease payments received from Southern Sod.

Mr. Scarbrough asked about the treatment of the electric consumption billed to the sod farm wherein he stated (T. 3856-3847) that its metered at the average generation costs. Mr. Scarbrough further states that a lower electric bill would give the sod farm operation a competitive advantage (T. 3848). Based on a late filed exhibit, staff has recommended a $34,913 adjustment increasing revenues for Gulf's non-utility electric consumption based on the appropriate tariff rate versus average generation costs. (Issue 49)

ISSUE 7: Should the investment and expenses associated with the "Navy House" be allowed?

RECOMMENDATION: No. Reduce rate base $23,257 and reduce expenses $7,516.

POSITION OF PARTIES

GULF: Yes. (Conner)

OPC: Only the necessary and reasonable costs incurred to provide electric service should be included for recovery.

STAFF ANALYSIS: As described by company Witness Conner, the Navy House is "a former residence which became the property of the company when it purchased land needed to install a transmission line from the company's Bayou Chico Substation to serve the Pensacola Naval Air Station." [T-3642] The initial purchase price of the land and the home on the land was $110,000. Staff has no reason to believe the price paid was not proper; this amount is not at issue. In addition to the purchase price, however, the company completely renovated the residence to serve as additional training space for its employees. The company determined that the structure could not be used as a private residence with a substation literally next to the house, and since the substation and residence filled up the property there was no parking for any potential commercial use. The expenses to renovate the property actually amounted to approximately $137,000. Most of these costs were expensed in 1988, not capitalized. These expenses were not an issue in the 1988 tax savings docket because staff was not aware of these expenditures prior to the recommendation due date for that docket.

A sizable portion of the $137,000 was a service connection fee of $44,000 that the county required, which involved laying pipe to the nearest hookup point. Company personnel have indicated that had they known of this service hookup fee prior to the renovations, the renovation itself might never have occurred.

Witness Conner indicated that training personnel are located at the corporate headquarters [T-3661], which is located at least 3 miles from the Navy House, that the Navy House can accommodate only 12 people at a time [T-3654] and that there are at least two training rooms at the Chase Street facility which are far larger [T-3664].

The company maintains that rooms at Bayfront, while suitable for meetings, are not suitable for training. However, various PSC staff members have attended depositions, briefings and exit conferences in several of the rooms at Bayfront with more than 12 people in attendance. No noise or other interferences could be heard inside the rooms; nor did these meetings cause any visible disruption of company business outside the rooms. These rooms also contained easels and electrical hookups for presentations when required.

Since there appears to be ample training space at the Chase Street facility, and there are meeting rooms at Bayfront, which hold more people than the Navy House, staff recommends that rate base be reduced by $23,257, and 1990 operating expenses for the Navy House be reduced by $7,516.

ISSUE 8: Has Gulf properly allocated all of the appropriate capital investment and expenses to its appliance division? (ROMIG)

RECOMMENDATION: No. Plant-in-Service, Accumulated Depreciation and Depreciation Expense should be reduced by $214,000 ($218,000 System), $7,000 ($7,000 System) and $12,000 ($12,000 System), respectively.

POSITION OF PARTIES

GULF: Yes. (Scarbrough)

OPC: The appliance division is being subsidized by the utility operations. The costs identified in Late-Filed Exhibit 564 should be removed.

STAFF ANALYSIS: Gulf Power has an appliance sales and service operation which is operated out of Gulf buildings which are included in rate base. A portion of this investment has been removed from rate base based on usage studies performed by Gulf. In several instances, the appliance operation has its own buildings which are recorded in non-utility plant.

Audit Disclosure No. 15 in the Staff Audit Report found that Gulf made an error in allocating the plant investment to the appliance operation. Therefore, it would be proper to correct the error by reducing plant, accumulated depreciation and depreciation expense $214,000 ($218,000 System), $7,000 ($7,000 System) and $12,000 ($12,000 System), respectively. Public Counsel did not identify any rate base adjustment associated with the appliance operation.

With regard to expenses, those expenses incurred directly by the appliance operation are charged below-the-line. All other expenses for accounting, salaries, fringe benefits, electric consumption, billing, collection, postage, etc. are allocated below-the-line. The allocations are based upon studies performed annually.

Mr. Scarbrough stated that electric consumption allocated to the appliance operation is not tariff based but is based on Gulf's actual cost of generation. (T. 583-591) In addition, Gulf allocated the cost of electricity to the "sod farm" and vision design, other non-utility operations. Staff and Public Counsel are in agreement that providing electrical usage at cost is clearly a subsidization of the non-utility operation by the ratepayers. This gives these operations an unfair competitive advantage. Late-Filed Exhibit 564 compares the amount of electric usage allocated to the non-utility operations to the amount that would be billed under the company's tariff. Based on this exhibit, staff has recommended increasing revenues $34,913 in Issue 49, Operating Revenues.

Public Counsel states in its brief that the appliance operation should be charged for postage. Currently Gulf is not charging the appliance operation for postage costs associated with bill stuffers or billing, merely because there are no incremental costs associated with these items. If a bill stuffer causes the postage to increase then the appliance operation would pay for that amount (T. 577-578). Staff's opinion is that the ratepayers are not subsidizing the non-utility operation since it costs no more to send out the electric bill by itself than with a stuffer. If the ratepayers were asked to pick up the cost of a higher postage, then the appliance operation would be subsidized by the ratepayer. This postage issue as well as others will be explored in Docket No. 900314-EU, Investigation of Gulf's Appliance Operation. No further adjustments are recommended.

Docket No. 891345-EI
July 26, 1990
1706E

ISSUE 9: Should Gulf's investment in the Tallahassee office be included in rate base? (ROMIG)

RECOMMENDATION: Yes in part. Reduce Plant-in-Service by $23,860 ($24,331 System), Accumulated Depreciation by $11,193 ($11,423 System) and Depreciation expense by $1,217 ($1,242 System) for lobbying activities. This represents 25% of the office investment and 100% of the car used by its lobbyist.

POSITION OF PARTIES

GULF: Yes. This property is used and useful, and expenses associated with this investment should be recovered in base rates.

OPC: Plant-in-Service should be reduced by $43,000 and Accumulated Depreciation by $26,000.

STAFF ANALYSIS: Gulf maintains an office in Tallahassee for use by its lobbyist, PSC liaison and other Pensacola-based employees while conducting business in Tallahassee. The office space is leased while the office furniture has been capitalized by the company and included in rate base. In addition, Earl Henderson, Gulf's lobbyist, has a company car which is also included in rate base. Gulf pointed out on page 24 of its brief that this office was fully allowed in the last rate case. Therefore, it would be consistent to make no disallowance in this docket. However, Mr. Scarbrough stated (T. 3785) that in order to avoid controversy in this case 25% of the capitalized investment in this office and 100% of Earl Henderson's car should be removed from rate base.

OPC Witness Larkin took the position in his testimony that 100% of the investment in this office should be removed from rate base. The rationale was that the investment was associated with the "lobbying" activities of Earl Henderson and Jack Connell and should not be borne by the ratepayers.

In staff's opinion, the office space is primarily used for utility purposes. Mr. Scarbrough stated (T. 3784) that in 1988, there were two people permanently assigned to the office, Earl Henderson and Jack Connell. On more than 50 occasions other employees from Pensacola used the facilities while working on PSC activities. In addition, other employees used the facilities while dealing with the Departments of Environmental Regulation, Revenue, Natural Resources and others.

Although it does not appear that Mr. Connell was a lobbyist, if, in fact, he did perform some lobbying activities, they were performed at meetings and other places not in the Tallahassee office. Therefore, no allocation has been made for Mr. Connell's portion of the office investment.

Staff agrees with the company that 25% of the office investment and 100% of Earl Henderson's car should be removed from rate base. This represents, in our opinion, a reasonable amount and results in the following adjustment:

Reduce Plant-in-Service	$23,860 ($24,331 System)
Accoumulated Depreciation	$11,193 ($11,423 System)
Depreciation Expense	$ 1,217 ($ 1,242 System)

This recommendation is consistent with the recommendation in the Gulf's 1988 Tax Savings Docket.

Docket No. 891345-EI
July 26, 1990
1706E

ISSUE 10: Should the total cost of the Bonifay and Graceville offices be allowed in rate base? (MERTA)

RECOMMENDATION: Yes. The total cost of the Bonifay and Graceville offices should be allowed in rate base.

POSITION OF PARTIES

GULF: Yes. These costs were reasonable, and the property is used and useful. The investment should be included in rate base.

OPC: No. In Gulf's previous rate case, the Commission made the determination that total recovery for these offices should not be permitted. In the current case, the Company has merely remade the same arguments on this issue. The Company has not submitted any verifiable support for these costs. Rate base should be reduced by $183,000.

STAFF ANALYSIS: In its 1984 rate case, the Company included in rate base the cost of newly constructed office facilities in Bonifay and Graceville. The Commission disallowed construction costs in excess of $67 per square foot, which was a cost supported by the Means Survey provided by Gulf. In Order No. 14030, the Commission stated:

> ...We are not convinced that sufficient evidence has been introduced to justify the total cost of these buildings.... We shall, likewise, leave this issue open until the Company's next rate case at which time we shall allow a further opportunity to justify the entire costs of these projects....

Since the disallowance was not due to imprudence, Gulf believes it has fully justified the total cost of the Bonifay and Graceville office buildings in this proceeding. The Company stated that consideration was not given to several relevant facts in the 1984 rate case. The Means Survey relied on by the Commission in Docket No. 840086-EI contained data pertaining to buildings in the 20,000 to 100,000 square foot range, while the Bonifay and Graceville office buildings are much smaller, approximately 1,500 square feet each. (TR 1613, 1622-1626). Both of the buildings were competitively bid and represented the true market value for construction given the market and economic conditions at that time. The diseconomies for such small commercial construction, the geographic location, and the functional requirements of the facility resulted in a higher cost per square foot. (TR 1624-1627, 1630-1633).

Mr. Conner testified that the Company has maintained offices in Bonifay and Graceville since 1940 and 1938, respectively. Gulf constructed these offices to more adequately and effectively serve its customers, as the leased offices in those areas were in a dilapidated condition. (TR 1623).

In Staff's opinion, Late Filed Exhibit No. 596, "Facilities Survey and Analysis, Eastern Division, Gulf Power Company" provided justification for constructing new offices but does not present a cost benefit analysis or a lease versus build analysis. The Study shows that the leased facilities were inadequate in meeting the Company's space needs, did not provide adequate parking, and were in need of extensive renovation.

Staff believes that a comparison to a branch bank-type facility which has a means cost of $84 a square foot for a 4,200 square foot building is reasonable. (TR 1625). This cost would be adjusted upward to reflect the smaller 1,528 square foot buildings, and the reduced economies of scale. (TR 1625-1626). In addition, it is possible that construction materials such as concrete, reinforcing steel, etc. had to be delivered from larger cities thereby adding to the cost.

In light of the above, Staff recommends that the total amount of the Bonifay and Graceville offices be allowed in rate base. No adjustment is necessary in this issue.

Docket No. 891345-EI
July 26, 1990
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ISSUE 11: Gulf Power has proposed $454,964,000 ($1,451,703,000 System) as the proper level of accumulated depreciation to be used in this case. Is this appropriate? (REVELL)

RECOMMENDATION: The appropriate jurisdictional amount is $454,774,000.

POSITION OF PARTIES

GULF: The appropriate amounts are $454,964,000 ($1,451,703,000 System). (Scarbrough, McMillan)

OPC: The provision should be increased by $3,715,000. ($3,522,000 juris.) (Larkin)

STAFF ANALYSIS: This calculation is mechanical in nature and dependent upon adjustments derived from resolution of several other specific issues. In addition to these other adjustments, Late-filed Exhibit No. 558, titled "FERC Audit Issues Entries on Resolved Issues" requires Gulf to increase accumulated depreciation by $67,080 ($69,374 System).

ISSUE 12 Should the plant investment made by Gulf to serve the Leisure Lakes subdivision be included in rate base? (COLSON)

RECOMMENDATION: No. Reduce plant-in-service by $142,000 and depreciation expense by $5,000.

POSITION OF PARTIES

GULF : Yes. This issue is misleading as worded. Gulf's investment in the Greenhead Substation should be included in rate base. This investment was originally intended in part to serve the Leisure Lakes Subdivision and represents part of the Company's investment to serve that load. By action of the Commission, Gulf was prohibited from serving Leisure Lakes; consequently, Gulf sold a portion of the facilities constructed for that purpose to the rural electric cooperative to whom the territory was awarded. The remaining investment constitutes Greenhead Substation which is used and useful serving Gulf's customers.

OPC: No.

Staff Analysis: On October 18, 1984, in Docket No. 830484-EU Gulf Coast Electric Cooperative, Inc. (Gulf Coast) petitioned the Commission for resolution of a territorial dispute between itself and Gulf Power Company (Gulf). The dispute involved the Leisure Lakes Subdivision, which consists of approximately 2,300 acres divided into approximately 750 lots. The dispute arose when Gulf Power constructed 2.2 miles of distribution line from its transmission line to the subdivision along a graded county road. After Gulf Coast's petition was filed, and with knowledge of the Commission's jurisdiction over the matter, Gulf Power also constructed the Greenhead substation near the site. In Order No. 13668 the Commission determined that Gulf Coast is entitled to provide electric service to the disputed areas. It was also ordered that Gulf Power is prohibited from serving, either temporarily or permanently, the disputed area. The Commission in its order encouraged Gulf Power to sell the facilities they built to serve leisure lakes to Gulf Coast, should Gulf Coast desire to purchase them.

According to Mr. C. E. Jordan Testimony Gulf subsequently sold all of its facilities built to serve Leisure Lakes and have no facilities in that area. TR 1587-1588. According to Late filed Exhibit No. 594 the book value of the facilities Gulf built to serve Leisure Lakes Subdivision was approximately $131,100 and the sale price to Gulf Coast was $ 130,353. Also, according to Jordan, the Leisure Lakes substation was not needed to serve load since neither the Sunny Hills or Vernon Substations have reach peak capacity. Therefore, staff recommends that the investment made by Gulf to serve Leisure Lakes subdivision not be included in rate base.

LRC/pr

Docket No. 891345-EI
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1706E

ISSUE 13: The company has included $14,949,000 ($15,739,000 System) of construction work in progress in rate base. Is this appropriate? (REVELL)

RECOMMENDATION: Yes, it is appropriate for the company to include $14,949,000 ($15,739,000 System) of construction work in progress in rate base.

POSITION OF PARTIES

GULF: Yes.

OPC: No position at this time.

STAFF ANALYSIS: Staff has examined the company's proposed CWIP additions as contained in the MFRs, B-13a, page 2 of 2. These additions appear reasonable and are similar in nature to projects begun in 1989. The FPSC audit staff examined the CWIP proposed in the 1989 withdrawn rate case and the 1989 actual CWIP balances. The difference between proposed and actual differed by less than one-half of 1%. This indicates that for the prior year at least Gulf was very accurate in forecasting construction plans [Exhibit 383, page 30]. Public Counsel Witness Larkin examined the company's projection for the test year and found the projection reasonable [T-2215], and Public Counsel in its brief did not address this issue.

Staff therefore recommends that Gulf's forecasted CWIP for the test year in the amount of $14,949,000 ($15,739,000 System) be allowed in rate base.

ISSUE 14: Is the company's method of handling non-interest bearing CWIP consistent with the prescribed system of accounting? (REVELL)

RECOMMENDATION: Yes, Gulf's method of recording non-interest bearing CWIP is in accordance with the prescribed system of accounts.

POSITION OF PARTIES

GULF: Yes.

OPC: No position at this time.

STAFF ANALYSIS: As mentioned in the Staff Analysis for Issue 13, the field audit staff examined the projected CWIP for the 1990 test year and the actual and projected CWIP amounts for 1989. The audit report [Exhibit 383] made no mention of any misapplication of the prescribed system of accounts for recording CWIP. Public Counsel did not address this issue in its Brief.

As a result, staff finds that Gulf's treatment of recording non-interest bearing CWIP is consistent with the prescribed system of accounts.

ISSUE 15: Gulf has included in its jurisdictional rate base $3,925,000 ($4,025,000 System) of land held for future use. Is this appropriate? (REVELL)

RECOMMENDATION: No. It is appropriate to include $3,789,800 ($3,885,200 System) of Land Held for Future Use, which is all Land Held for Future Use with the exception of 10% of Caryville which is allocated to the Sod Farm (Addressed in Issue 6).

POSITION OF PARTIES

GULF: Yes. This amount represents the original cost of land held for future use in the provision of electric service and is properly included in rate base. (Parsons, Lee, Conner)

OPC: Due to the current plans for use, the following items should not be included in rate base. Caryville land at $1,398,000; Bayfront office at $1,844,000; Pace Blvd. land at $612,000. (Larkin)

STAFF ANALYSIS: There are several parcels of land that Gulf owns which are presently classified as land held for future use. The properties are listed below:

(1) Caryville land site:

This property consists of approximately 2000 acres and was assembled for the purpose of constructing a generating plant. Due to purchase agreements with other units of the Southern Company, Gulf bought into plants already under construction rather than building its own plant. This site is certified for power plant construction, however. Even though Gulf would be required to undergo additional revisions when a plant is constructed, it would be far less involved than an initial site review. Approximately 10% of the total acreage is used as a sod farm. (Addressed in Issue 6)

(2) Daniel land site:

This land is located at Plant Daniel in Mississippi and was reclassified from Plant in Service to Land Held for Future Use as a result of a FERC audit conducted on Mississippi Power. This land will be used as a future ash disposal site and was identified as a "future" site on maps which the FERC auditors examined during their audit. The property is not an addition to the original site but a part of the original site. Nothing has changed; the reclassification was only made at the suggestion of FERC and will be necessary for future ash storage.

(3) Pace Blvd. land acquisition:

The "Pace Boulevard" location is presently the site of the Western Division headquarters as well as the general warehouse, the general repair shop and other company support functions. The company in an effort to plan for future expansion buys parcels of property adjacent or at least very close to this complex. This acquisition program will enable the company to swap land for parcels contiguous to existing property if necessary to assemble whole parcels big enough to support the future expanded company operations.

(4) Bayfront Office site:

This property is land which will eventually be used for additional parking when the number of employees at the corporate building is increased. Parking at the building under current zoning requirements is sufficient. However, additional parking will be required under zoning regulations when the third floor, which is unoccupied, is utilized.

(5) Panama City:

The entire Panama City District Office and support facilities encompasses 20 acres along Highway 98. The part which is classified as Land Held for Future Use is approximately the N.E. 4.2 acres of this site. The original purchase price was slightly over $80,000. It is staff's opinion that this frontage on Highway 98 could not be obtained for that price now. This land will be used for support facilities expansion as needed.

(6) General repair facility site:

This property is used to support the Pace Boulevard site which is 4 blocks east of this site. A portion of the property was placed in service in March of 1990 because a building used for electric operations was built on it.

There are definite planned uses for all the parcels designated as Land Held for Future Use. It is true that the exact in-service date for many of the projects on these parcels cannot be determined. Gulf, however, does have a long range plan that is put in place as demand or customer growth dictates.

Tracts of land are not always easy to be put together. Often there are multiple owners who must be dealt with separately. Gulf Power or any company which is growing must be able to anticipate future needs and acquire needed properties as they become available over time. In other words, these properties must be obtained in advance of the actual in-service date to avoid "panic" buying and the resulting inflated purchase price Gulf would have to pay if owners knew the company was required to immediately purchase a given parcel.

All of these properties with the exception of the recent "Pace Blvd." acquisitions were allowed in the last rate case and there is a definite intended use for the properties. It is true for the Caryville site that the intended use may be years in the future. However, this site is fully certified and the certification process would be lengthy on any other site. If a certified site is sold, to be purchased when needed, we believe the price demanded by the owner would be substantially above the price of comparable properties in the area. Hence, the carrying cost is not relevant as might be for a more fungible property need.

Staff recommends that $135,200 ($139,800 System) be disallowed since it is being used as a sod farm, a non-utility related function. Staff also recommends that the remaining $3,789,800 ($3,885,200 System) be allowed in rate base. In the event the company discontinues the sod farm operations, we recommend that the company be allowed to include this portion in rate base.

ISSUE 16: Has Gulf allocated the appropriate amount of working capital to Unit Power Sales (UPS)? (ROMIG)

RECOMMENDATION: Yes. No adjustment should be made to working capital.

POSITION OF PARTIES

GULF: Yes. The retail, wholesale, and UPS working capital amounts have been calculated based on the Florida Public Service Commission's requirement to use the balance sheet approach for determining working capital.

OPC: No. Increase the UPS working capital by $4,097,000 and decrease the system working capital by the same amount.

STAFF ANALYSIS: Gulf has used the balance sheet approach in determining its working capital requirement for the test year (T. 750, 751, 761). The system amount of working capital was allocated to the UPS, wholesale and retail jurisdictions based on this methodology although the UPS and wholesale amounts are actually billed to those jurisdictions using the 1/8 O&M formula as required under the FERC jurisdiction. (T. 761) The company's position is that the working capital amounts allocated to each jurisdiction should be on a comparable method (T. 751, 761). "These calculations were reviewed and approved by the Commission in Gulf's last rate case..." (Brief 44)

OPC Witness Larkin takes the position that when the company recovers from the UPS customers a higher level of working capital than needed, the ratepayers should receive full credit for the actual amount allocated to UPS Sales (T. 3337). Using the 1/8th O&M method (as required by FERC) rather than the balance sheet method approved by this Commission would allow the company overrecovery on its UPS sales (T. 2227).

The use of the 1/8 O&M method does result in a higher working capital allowance than the balance sheet approach. Mr. McMillan stated that the retail working capital would be increased by over $40 million using the 1/8 O&M method (T. 761).

In staff's opinion, system working capital should be allocated to each jurisdiction, for ratemaking purposes, using the methodology approved by this Commission. We are also in agreement with Gulf that it would not be appropriate to pick and choose different methodologies in allocating working capital. In addition, since no adjustments were made in the allocation of working capital in Gulf's last rate case, we would recommend no adjustment in this proceeding.

ISSUE 17: The company has included $81,711,0000 ($200,266,000 System) of working capital in rate base. What is the appropriate level of working capital? (MERTA)

RECOMMENDATION: The appropriate jurisdictional amount is $78,476,000.

POSITION OF PARTIES

GULF: The appropriate amounts are $81,711,000 ($200,266,000 System). (McMillan)

OPC: The appropriate level of working capital is $69,243,000.

STAFF ANALYSIS: The level of working capital falls out from the resolution of Issues 16, 18, 19-24, 27, 28, 31-36.

ISSUE 18: Gulf has included $1,358,278 ($1,458,221 System) prepaid pensions expense in its calculation of working capital. Is this appropriate? (SALAK)

RECOMMENDATION: An adjustment should not be made to working capital to exclude $1,358,228 of prepaid pension expense.

POSITION OF PARTIES

GULF: Yes. Gulf prepaid certain pension benefits as allowed by IRS rules in order to maximize its income tax deductions; this decision was prudent in that the retail customer receives the benefit of deferred taxes in the capital structure at no cost, and these expenses should therefore be recovered through base rates.

OFFICE OF PUBLIC COUNSEL: The prepaid pension of $1,484,000 should be removed from working capital.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: In 1987, Gulf made a contribution to its pension fund when the fund was already in an overfunded status. (TR 3822-3823) More was placed in the pension fund than was expensed for book purposes under Statement of Financial Accounting Standard 87. (TR 3786) This resulted in a prepaid pension expense that was included in working capital.

OPC witness Larkin testified that Gulf should not be able to receive a return on the prepaid pension expense because the trust was already fully funded. The pension payment was not necessary. (TR 2220-2221) Staff Audit Disclosure 23 also discusses this issue. The Audit Opinion and Conclusion states: "The Commission may wish to consider the value to the customer from the utility prepaying pension costs." (Exhibit 383, p. 51)

Gulf witness Scarbrough states that the company was allowed a tax deduction greater than book expense under SFAS 87 if the "actuarially determined maximum tax deduction was contributed to the plan before September 15, 1988." Gulf decided to maximize its tax deduction using the higher 1987 tax rate. (In 1987 the tax rate was 39.95% compared to the current tax rate of 34%.) Witness Scarbrough also points out that associated deferred taxes are benefitting the customers as zero cost capital. Scarbrough believes making the prepayment was a prudent decision. (TR 3785-3786) During cross-examination, Witness Scarbrough stated that the additional contribution was made under the advice of Gulf's actuary. (TR 3822, 3823)

On redirect examination, Witness Scarbrough stated that the Company always takes a tax deduction as soon as it can. He reiterated that the it was the last opportunity to take advantage of the higher tax rates. For the first time he states that when Gulf made the deduction there were going to be changes in the regulations. These regulations were going to prohibit Gulf from funding in the future for the accruals that were being expensed. By prefunding, the utility has "some funding to apply to the accrual." (TR 617-618)

There was no cost benefit analysis presented by any party to the case. From the record, it can be seen that the Company permanently saved $270,000 in taxes by making a contribution for 1987. With the change in regulations, it appears that the utility may have saved even more. The customers will pay a return on a rate base equivalent of approximately $827,000 net of deferred taxes. The additional funds in the pension plan should serve to reduce the pension expense for the customers in the future. Whether or not this is in the best interest of the ratepayers depends on how long the Company will earn a return on the prepaid pensions. It will reverse as pension expense is recognized. (It should be noted that Staff believes that if Gulf had not invested in this working capital item, it would have invested in some other asset in the form of cash, reducing a liability, or investing in an asset. These items could also have the effect of increasing working capital.)

To summarize, Gulf maximized its tax deduction for the pension funding by taking advantage of the higher historical tax rate. The prepayment will earn a return, but the return will be partially offset by zero cost deferred taxes included in the capital structure. The additional funds in the pension plan should serve to reduce the utility's pension expense in the future. Since the life of the prepayment is dependent upon the pension expense, it is impossible to tell how long the prepayment will be in working capital. Although Staff does not want to send a signal to utilities to make comtributions to overfunded plans, Staff believes that Gulf made a prudent decision based upon the tax law. Gulf took an aggressive tax posture and this Commission has encouraged that to the extent that it benefits the ratepayers. While it is not clear now that the ratepayers will definitely benefit from Gulf's tax posture, it would have appeared in 1988, when Gulf was filing its tax return, that the customers would benefit from the prepayment. At that time, Gulf's pension expense was much higher and it would have appeared the prepaid would be gone by now and the ratepayers would receive the benefit of the higher tax rate. Staff recommends that no adjustment be made the working capital for prepaid pension expense.

ISSUE 19: Should unamortized rate case expense be included in working capital? (MERTA)

RECOMMENDATION: No. Commission policy is to exclude unamortized rate case expense from working capital. Reduce working capital by $765,385 ($765,385 system)

POSITION OF PARTIES

GULF: Yes. Expenses incurred in connection with preparing, filing, and completing a rate case are legitimate costs of doing business, and are properly included in working capital.

OPC: No, working capital should be reduced by $765,000 to remove this item. (Larkin)

STAFF ANALYSIS: The Company has included $765,385 in working capital for unamortized rate case expense.

Gulf Witness McMillan testified that the Commission recognizes rate case expenses as a legitimate cost of doing business and allows recovery in rates. Therefore, the unamortized balance in deferred debits should be included in working capital and also earn a return. In other words, if an operating expense is allowed to be recovered through rates, then the working capital associated with its unamortized balance should also be recovered. To prohibit a return on the unamortized balance unfairly penalizes the stockholders for costs to process the rate proceeding according to FPSC regulatory guidelines. (TR 3915). Further, since these expenses will be recovered over an amortization period of two or more years, the stockholder incurs the carrying costs. (TR 819-820).

Public Counsel's primary reason for recommending disallowance of this item is that they believe no rate increase is warranted. Should the Commission grant an increase, Public Counsel recommended the exclusion of unamortized rate case expense from working capital on the basis of past Commission policy. (OPC Brief p. 16).

Commission policy is to exclude the unamortized portion of rate case expense. In Order No. 14030, Docket No. 840086-EI, Gulf Power Company rate case, the Commission stated:

> The company has included $439,000 in working capital which represents the unamortized portion of rate case expense. Since Commission policy is to exclude this item from working capital, we are reducing rate base $439,000.

In Order No. 22224, Docket No. 881056-EI, FPUC Fernandina Beach Division rate case, the Commission upheld this policy:

> ...However, consistent with current Commission policy, as noted in Order No. 14030, Docket No. 840086-EI, and as followed in Order No. 21532, Docket No. 880558-EI ... we find that unamortized rate case expense should be excluded from the calculation of working capital, which reduces the utility's originally requested amount by $61,191.

Staff believes that this policy strikes a balance between the ratepayers and stockholders. The stockholders receive the benefit of the additional revenues, and the ratepayers are benefitted by having the cost related to the rate case recoverable in expense over two or more years. In addition, this policy acts as an incentive to the company to hold down the cost of a rate case where possible.

Staff recommends that unamortized rate case expense be excluded from working capital consistent with Commission policy. Working capital should be reduced by $765,385 ($765,385 System).

ISSUE 20: Should the net overrecoveries of fuel and conservation expenses be included in the calculation of working capital? (REVELL)

RECOMMENDATION: Gulf is projecting zero for net overrecoveries of fuel and conservation expenses for 1990. Therefore there is no recommended adjustment to working capital.

POSITION OF PARTIES

GULF: No. All fuel and conservation expenses, including the overrecoveries and underrecoveries are properly handled in separate recovery mechanisms as determined by this Commission. In Order No. 9273, (Docket No. 74680-EI), the Commission established that interest would be paid on over and underrecoveries within the fuel conservation dockets, to counter any possible incentive to bias the projections in either direction. Therefore, since the customers already receive a return on overrecoveries through a reduction in the fuel component of their electric bill, it is inappropriate to reduce working capital and hence base rates for the same overrecovery amount. (McMillan)

OPC: Consistent with past Commission practice, this item should be included in the calculation of working capital.

STAFF ANALYSIS: It has long been the policy of this Commission that net fuel and conservation overrecoveries be included as a reduction to working capital. In this particular instance, however, the company is not projecting any overrecoveries for 1990, as indicated in Schedule B-15, pages 13-25 of the MFRs Gulf filed in this docket. Therefore, staff is recommending no adjustment to working capital.

ISSUE 21: Should temporary cash investments of $6,045,000 ($6,399,000 system) be included in jurisdictional working capital? (YECCO)

RECOMMENDATION: No. Temporary cash investments should not be included in working capital.

POSITION OF PARTIES

GULF: Gulf's filing reflects that temporary cash investments have been removed from jurisdictional adjusted working capital, consistent with the Commission treatment in the last rate case. The appropriate amounts of temporary cash investments for the 1990 test year are $6,045,000. ($6,399,000 system) These funds constitute essentially all of Gulf's available working funds, and are required and necessary for the provision of utility service to our customers. The Company believes that it would be appropriate to include temporary cash investments in jurisdictional working capital.

OFFICE OF PUBLIC COUNSEL: No. Reduce working capital by $6,399,000.

STAFF ANALYSIS: In its initial filing, the Company removed temporary cash investments from rate base, and made a pro rata adjustment to the capital structure to reconcile the capital structure to rate base. The Company made this adjustment because this is how the Commission treated temporary cash investments in the Gulf Power's last rate case. (TR 790)

Witness Seery testified that the appropriate regulatory treatment of either continuing cash balances or temporary cash investments should depend upon their prudency. (TR 2966C) If the utility can demonstrate, through competent evidence, that their cash balances or temporary cash investments are necessary for the provision of regulated utility service, they should remain in rate base and earn at the utility's overall rate of return. Any earnings generated by these funds should then be used to offset revenue requirements. (TR 2966C)

Based on witness Seery's testimony, the Company changed its original position with respect to its temporary cash investments. (TR 790) The Company's revised position is that its temporary cash investments are necessary for the provision of utility service and therefore should be included in working capital.

Staff agrees with witness Seery's position. If the temporary cash investments represent a legitimate working capital requirement then they should not be removed from rate base. A blanket policy of excluding temporary cash investments from rate base could result in an asset, potentially necessary for the provision of regulated service, earning less than a fair rate of return. (TR 2966C) Staff believes, however, the burden of proof is on the Company to demonstrate through competent evidence that their temporary cash investments are necessary for the provision of utility service.

Witness McMillan states, "these funds are required and necessary in providing utility services for our customers." When asked to show why the Company's temporary cash investments are necessary for the provision of utility service witness McMillan provided staff with the following explanation:

The test year amount for Temporary Cash Investments (13-month average amount) of $6,399,000 is approximately 10 percent of the average monthly disbursements. In addition, we are projecting to borrow funds during five months of the test year. The Company again maintains that these funds are required and necessary in providing utility services for our customers. (Ex. 439)

During cross-examination witness McMillan stated:

"...we don't know of any other way to pay our bills than to have cash available. Either you are going to have temporary cash, cash, or short-term debt, one of the three, because if you --once you stop paying your bills, you're going into bankruptcy at that stage, and you'll be shut down. You've got to have liquid assets..." (TR 793)

A company needs to maintain a certain degree of liquidity to operate. Staff notes that the Company maintains some degree of liquidity through short-term debt. The Company budgeted to pay fees of $60,000 in 1990, which the Company is attempting to recover through operating expenses (ISSUE 58), for access to lines of credit totalling $42 million. In addition, the Company continues to keep compensating balances of $436,900 for additional lines of credit totalling approximately $6.2 million. Thus, the Company has access to approximately $48.2 million through lines of credit. (TR 778)

Staff does not dispute that the Company needs to maintain a certain degree of liquidity to operate. Staff believes, however, that the burden is on the Company to demonstrate that the additional liquidity provided by holding $6,399,000 in temporary cash investments is necessary. In staff's opinion the Company has not provided this proof. Statements such as, "its all our available cash" or "temporary cash investments represent less than 10 percent of total monthly expenditures" are meaningless and do not constitute competent evidence. Staff therefore recommends excluding the Company's temporary cash investments from working capital.

ISSUE 22: Gulf has included $1,042,000 (system) for heavy oil inventory. Is this appropriate? (SHEA)

RECOMMENDATION: No. Heavy fuel oil inventory should be reduced to a level equal to seven days burn at a 100% capacity factor. Working capital should be reduced by $596,178 (system), or by $576,462 (jurisdictional).

POSITION OF PARTIES

GULF POWER COMPANY: Yes. The level of heavy oil is necessary for standby fuel at Plant Crist Units 1, 2, and 3.

PUBLIC COUNSEL: Reduce heavy oil inventory by $925,613 ($1,042,000 system).

STAFF ANALYSIS: Heavy fuel oil can be used by Gulf Power Company at Plant Crist Units 1, 2, and 3. These three steam units have a combined demonstrated capability of 85.4 MW's and normally use natural gas as their primary fuel. Heavy oil is used as an alternate fuel when natural gas is not available (Tr. 1067-9.)

Crist Units 1, 2, and 3 have a very low capacity factor and are not projected to consume any heavy oil during the test year. In 1990, each of the three units has a projected capacity factor of less than one percent. (Exhibit No. 448, Page 19 of 20.)

Gulf Power Company maintains these three heavy oil units on 24-hour standby so that the combined capacity of these units can be made available to the Southern System through the intercompany interchange contract. Gulf receives about $6 million through the interchange contract for this capacity (Tr. 1074-6.) In order to receive this benefit, the units must be able to be brought on-line when needed.

Natural gas, the primary fuel for Crist Units 1, 2, and 3, is purchased under interruptible contracts. Heavy oil is used as a backup fuel. Because of the interchange agreement, Staff agrees that some heavy oil should be maintained in inventory as a backup fuel.

In July 1989, Gulf Power burned 995 barrels of heavy oil at Crist Units 1, 2, and 3 during a test burn to make sure the units would come up on heavy oil. Prior to July 1989, the last time heavy oil was consume was in 1986. No heavy oil was consumed during the December 1989 Christmas freeze. (Tr. 1071)

Heavy oil is delivered by truck and it would take a few days to reorder the oil (Tr. 1076.) Since heavy oil can be reordered in a few days, Staff is of the opinion that Gulf Power should maintain only a few days supply. This would ensure that the units could be brought on-line if natural gas was not available. Staff recommends that Gulf be allowed to maintain a seven-day supply of heavy oil for the units if the units were to run at 100% of their demonstrated capability. The seven day figure is arbitrary, but Staff considers it to be reasonable considering the low capacity factor of the units and the fact that natural gas is the primary fuel for these units. A seven-day supply of heavy oil for Crist Units 1, 2, and 3 operating at 100% of their demonstrated capability would equal 32,774 barrels. Gulf Power has requested a heavy oil inventory of 78,533 barrels with an average price of $13.603 per barrel and valued at $1,042,000 (system). Staff is of the opinion that the Commission should allow a heavy oil inventory level of 32,774 barrels at an average price of $13.603 per barrel. Staff recommends that the Commission should reduce working capital by $596,178 (system), or by $576,462 (jurisdictional). These calculations are shown on Attachment 22-1.

Attachment 22-1

GULF POWER COMPANY
7 DAY HEAVY OIL SUPPLY AT 100% CAPACITY

	Demonstrated Capability (MW's)	7 Days Generation at 100% Capacity (MWH's)	Heat Rate (Btu/KWH)	Fuel Requirement (MMBtu)	Heavy Oil Requirement (Bbls.)
Crist 1	23.0	3,864	14,850	57,380	9,108
Crist 2	23.0	3,864	14,740	56,955	9,041
Crist 3	39.4	6,619	13,920	92,139	14,625
Total	85.4	14,347	43,510	206,475	32,774

Average Fuel Price ($/Bbl.)	13.603
Allowed Inventory (System $)	445,822
Gulf Request (System $)	1,042,000
Adjustment (System $)	596,178
Jurisdictional Factor	0.9669295
Adjustment (Jurisdictional $)	576,462

Sources: Tr. 1069, 1077
Exhibit No. 448, Page 19
MFR B-17b, Page 24
Exhibit No. 449, Page 12

ISSUE 23: Gulf has included $359,000 (system) of light oil inventory. Is this appropriate? (SHEA)

RECOMMENDATION: No. The Commission should use the generic inventory policy of Order No. 12645 to determine a reasonable level of light oil inventory. Working capital should be reduced by $123,380 (jurisdictional) if Scherer remains in rate base or by $123,339 (jurisdictional) if Scherer is removed from rate base.

POSITION OF PARTIES

GULF POWER COMPANY: Yes. This nominal level of lighter oil requested to serve all five plants is the minimum inventory level necessary to account for plant consumption, allowances for procurement time, market volatility, and potential supply disruptions.

PUBLIC COUNSEL: Reduce light oil inventory by $234,059 ($263,490 system).

STAFF ANALYSIS: Gulf Power Company has requested that 650,895 gallons of light fuel oil valued at $337,000 (system) be included in working capital. This oil is used for unit start-up and flame stabilization at coal units and in one combustion turbine peaker at Plant Smith. Gulf has no inventory study to justify this request. Gulf maintains that the request is reasonable and that light oil inventory levels have been determined by the experience of their operating people and previous needs.

In Docket No. 830002-EU, the Commission developed a generic inventory policy to be used in a rate case if a utility fails to fully justify its inventory request. This generic inventory policy is contained in Order No. 12645. This order states that the generic policy will not be used automatically in the event that the utility's policy is not justified, rather, the Commission will strive to determine an optimum policy from evidence presented in the rate case. The generic inventory policy for light oil is a level equal to 30 days burn at the highest average monthly rate.

Staff is of the opinion that Gulf Power Company has failed to justify its request for light oil inventory. The Commission should use the generic policy of Order No. 12645 to determine a reasonable light oil inventory level.

Plant Crist can, and does, use natural gas for coal unit start-up and flame stabilization when gas is available. This gas is purchased under interruptible contracts. If the gas is not available, Gulf will use light oil for start-up and stabilization. Since the generic policy allows a 30 day supply of light oil at a reasonably high rate of burn, the Commission should determine the level of light oil allowed at Plant Crist assuming that natural gas will not be available. Exhibit No. 580 shows the volume of natural gas consumed for unit start-up, but does not break out gas used for flame stabilization. Attachment 23-1 shows the volume of light oil which would have been consumed at Plant Crist if natural gas had not been available in 1989.

Attachment 23-2 shows that the generic inventory policy yields a target level of 404,564 gallons if Plant Scherer remains in rate base and 383,210 gallons if Plant Scherer is removed from rate base. These levels assume that natural gas would not be available at Plant Crist. Staff recommends that the Commission adopt this policy to establish a reasonable light oil inventory level. This would require a reduction in working capital of $127,599 system ($123,380 jurisdictional) if Scherer remains in rate base or a reduction of $129,626 system ($125,339 jurisdictional) if Plant Scherer is removed from rate base.

Attachment 23-1

GULF POWER COMPANY
1989 LIGHT OIL AND NATURAL GAS CONSUMPTION
for
START-UP AND FLAME STABILIZATION
PLANT CHRIST

Month	Light Oil Gallons	Natural Gas Start-Up Fuel Mcf	MMBtu	Equiv. Gal.	Total Equiv. Gal. Light Oil
Jan-89	32,712	7,759	7,852	56,966	89,678
Feb-89	36,661	6,124	6,197	44,962	81,623
Mar-89	30,737	11,391	11,528	83,632	114,369
Apr-89	32,147	7,774	7,867	57,076	89,223
May-89	27,292	13,046	13,203	95,783	123,075
Jun-89	26,507	11,584	11,723	85,049	111,556
Jul-89	28,176	9,634	9,750	70,732	98,908
Aug-89	31,584	8,537	8,639	62,678	94,262
Sep-89	26,554	7,402	7,491	54,345	80,899
Oct-89	34,686	18,092	18,309	132,831	167,517
Nov-89	15,631	7,892	7,987	57,943	73,574
Dec-89	17,203	6,714	6,795	49,294	66,497
Total	339,890	115,949	117,340	851,292	1,191,182

NOTES: Light oil Btu content is 137,838 Btu/gallon
Natural Gas Btu content is 1,012 Btu/cubic foot

SOURCES: Exhibit No. 449, Page 7
Exhibit No. 448, Page 18
Exhibit No. 580, Page 1

Attachment 23-2

LIGHT OIL INVENTORY ANALYSIS

Plant	Type Oil	Test Year Average Inventory (Net of U.P.S.) (Gallons)	($/Gal)	($)	High Useage Month	High Month's Consumption (Gallons)
Crist	#2 Lighter Oil	208,956	0.502	105,000	Oct-89	167,517
Daniel	#2 Lighter Oil	86,514	0.555	48,000	Apr-89	57,394
Scholz	#2 Lighter Oil	14,243	0.491	7,000	Apr-89	4,597
Smith	#2 Lighter Oil	23,750	0.505	12,000	May-89	52,480
Smith	C. T. Oil	299,990	0.520	156,000	Dec-89	101,222
Subtotal		633,453	0.518	328,000		383,210
Scherer	#2 Lighter Oil	17,442	0.516	9,000	Jul-89	21,354
Total		650,895	0.518	337,000		404,564

NOTE: Plant Crist consumption figures have been adjusted to account for natural gas used as start-up fuel.

	With Scherer	Without Scherer
Generic Inventory Policy (Gallons)	404,564	383,210
Requested Inventory (Gallons)	650,895	633,453
Excess Inventory (Gallons)	246,331	250,243
Average Price ($/Gallon)	0.518	0.518
System Adjustment ($)	127,599	129,626
Jurisdictional Factor	0.9669295	0.9669295
Jurisdictional Adjustment ($)	123,380	125,339

Sources: MFR Schedule B-17b, Pages 12, 14, 18, 20, 22
Exhibit No. 448, Page 15
Exhibit No. 449, Pages 7, 8, 9, 10, 11, 12
Exhibit No. 580, Page 1

ISSUE 24: Gulf has included $57,426,000 (system) for coal inventory. Is this appropriate? (SHEA)

RECOMMENDATION: No. The Commission should use the generic inventory policy of Order No. 12645 to determine a reasonable level of coal inventory. Working capital should be reduced by $1,833,568 (jurisdictional) if Plant Scherer remains in rate base or by $1,577,068 (jurisdictional) if Plant Scherer is removed from rate base.

POSITION OF PARTIES

GULF POWER: Yes.

PUBLIC COUNSEL: No. Reduce coal inventory by $4,468,010 ($5,029,820 system).

STAFF ANALYSIS: This issue is misstated. Including Plant Scherer, Gulf has requested a total of $52,659,000 (system). This figure excludes U.P.S. coal inventory and includes $45,168,000 for coal inventory at plants and $7,491,000 for coal inventory in-transit.

Staff is of the opinion that no adjustment is needed to in-transit coal. First, this coal is not located at the plant and should not be considered in inventory target calculations. Second, if an adjustment is made to in-transit coal, an almost equal off setting adjustment would need to be made to fuel accounts payable. Test year fuel accounts payable is $13,499,000 (system).

Gulf Power Company used a computer model called the Utility Fuel Inventory Model (UFIM) to justify its coal inventory request. Use of this model requires the input of various parameters, including coal supply disruption scenarios. Gulf Power chose to include four disruption scenarios. Under Gulf's assumptions, UFIM recommended a target level of 105 days projected burn.

Three of the coal supply disruption scenarios assumed by Gulf are relatively minor in nature. One of the disruption scenarios assumed by Gulf is a total nuclear moratorium which occurs with no warning once each forty years. This disruption has a major impact on the results of the model run. Without the nuclear moratorium, UFIM recommended a target level of 4 days nameplate, or about 7 days projected burn. (Tr. 1107)

Staff is of the opinion that the nuclear moratorium assumption is unrealistic. Staff does not consider a total nuclear moratorium to be reasonable. Nor does Staff consider it reasonable that such a disaster could occur without warning. During this disruption, Gulf assumes that outage costs to the residential sector would be $8.50 per Kwh. Witness Parsons stated that this disruption was so severe that the world would be significantly changed. Commissioner Beard correctly made the observation that if this disruption was to occur, electricity might be the least of our problems. (Tr. 1113) Gulf's inclusion of this assumption invalidates the model's results.

Staff is of the opinion that Gulf has failed to justify its coal inventory request. The Commission should use the generic coal inventory policy described in Order No. 12645 to determine a reasonable coal inventory level. This generic inventory policy was developed by the Commission to be used in a rate case when a utility fails to fully justify its inventory request. The generic inventory policy for coal is a level equal to 90 days projected burn.

Attachment 24-1 shows the 90-day policy applied to Gulf's system net of U.P.S. If Plant Scherer remains in rate base, the Commission should reduce working capital by $1,833,568 on a jurisdictional basis ($1,896,279 system). If Plant Scherer is removed from rate base, the Commission should reduce working capital by $1,577,068 on a jurisdictional basis ($1,631,006 system).

GULF RATE CASE COAL INVENTORY ANALYSIS INCLUDING PLANT SCHERER, EXCLUDING U.P.S.

	Total Test Year Burn (Tons)	Average Daily Test Year Burn (Tons)	90-Day Inventory Level (Tons)	System Plant Coal Inventory (Does not include in-transit coal) (Tons)	($/Ton)	($)
High Sulfur Coal	3,214,842	--	--	693,715	44.34	30,759,000
Low Sulfur Coal	699,561	--	--	234,921	61.34	14,409,000
TOTAL	3,914,403	9,885	889,650	928,636	48.64	45,168,000

Inventory Request (Tons)	928,636
Excess Inventory (Tons)	38,986
Average Price ($/Ton)	48.64
System Adjustment ($)	1,896,279
Jurisdictional Factor	0.9669295
Jurisdictional Adjustment ($)	1,833,568

GULF RATE CASE INVENTORY ANALYSIS EXCLUDING PLANT SCHERER, EXCLUDING U.P.S.

	Total Test Year Burn (Tons)	Average Daily Test Year Burn (Tons)	90-Day Inventory Level (Tons)	System Plant Coal Inventory (Does not include in-transit coal) (Tons)	($/Ton)	($)
High Sulfur Coal	3,214,842	--	--	693,715	44.34	30,759.000
Low Sulfur Coal	594,764	--	--	206,036	60.49	12,464,000
TOTAL	3,809,606	9,620	865,800	899,751	48.04	43,223,000

Inventory Request (Tons)	899,751
Excess Inventory (Tons)	33,951
Average Price ($/Ton)	48.04
System Adjustment ($)	1,631,006
Jurisdictional Factor	0.9669295
Jurisdictional Adjustment ($)	1,577,068

ISSUE 25: Should 515 MW of Plant Daniel be included in Gulf Power's rate base? (HARVEY)

RECOMMENDATION: Yes. Plant Daniel should be included in Gulf Power's rate base.

POSITION OF PARTIES:

GPC: Yes. This should be a stipulated issue, as all parties agree that the 515 MW of Plant Daniel should be included in Gulf Power's rate base. The Commission nas recognized the prudency of Gulf's partial ownership in Plant Daniel. Plant Daniel capacity was obtained for the long-term benefits of Gulf territorial customers. This capacity is no longer dedicated to Unit Power Sales (UPS) customers, and provides capacity and energy to Gulf's retail customers.

OPC: No position stated in the brief.

STAFF ANALYSIS:

In Gulf's 1984 rate case, 272 megawatts of Plant Daniel were allowed into rate base. The remainder of Plant Daniel was sold as Unit Power Sales and, therefore, not available to serve Gulf's territorial load. Starting in February, 1989, Gulf's entire ownership of Plant Daniel (515 megawatts) was dedicated to serve Gulf's territorial load (Ex. 65, 73). Because Gulf acquired Plant Daniel before they acquired Plant Scherer, the issue of whether Plant Daniel should be permitted in rate base should be addressed before the issue of whether Plant Scherer should be permitted in rate base; therefore, the analysis of whether Plant Daniel should be included in rate base will not assume that Plant Scherer is available to serve Gulf's customers.

When Gulf's reserve margin is considered with and without Plant Daniel, it is clear that without Plant Daniel, Gulf would be short of capacity in the 1990 test year. With the amount of Plant Daniel permitted in rate base in Gulf's 1984 rate case (and without Scherer), Gulf's reserve margin would be 8.1 percent (Ex. 456, p. 11)--well below Southern's planning reserves of 20 to 25 percent. Gulf's reserve margin with 515 megawatts of Daniel (and without Scherer) would be 21.9 percent (Ex. 456, p. 11), representing a reasonable level of reserves. Southern's reserves are reasonable with or without the addition of this capacity. Adding Plant Daniel increases Southern's reserves from 19.0 percent to 19.9 percent. As long as Southern's reserves are reasonable, it is reasonable for Gulf to target its reserves to match Southern's reserves. Although it would be advantageous to Gulf's ratepayers to purchase capacity through Southern's Intercompany Interchange Contract (IIC) at average embedded cost rather than construct new generation, this would not be fair to the ratepayers of the other operating companies. Therefore, Staff believes that Gulf needs all of the capacity associated with Plant Daniel to serve its territorial customers.

When considering the cost of Plant Daniel, it is clear that--even using hindsight--Plant Daniel was a prudent investment. Gulf is putting Plant Daniel into rate base at a cost of $265 per kilowatt. This compares to a new coal unit cost of $1163 per kilowatt (Ex. 71). It even compares favorably to the cost of a combustion turbine at $348 per kilowatt (Ex. 456, p. 5).

Given Staff's conclusion that Gulf needs the capacity associated with Plant Daniel, and that Plant Daniel is less expensive than new generation, Staff recommends that all 515 megawatts of Plant Daniel be allowed in Gulf's rate base.

ISSUE 26: Should 63 MW of Plant Scherer 3 be included in Gulf Power's rate base? (HARVEY)

RECOMMENDATION: For the test year 1990, 63 MW of Plant Scherer 3 (Scherer) should be included in Gulf's rate base, leaving 149 MW of Scherer which is owned by Gulf power but dedicated to Unit Power Sales in 1990 out of rate base. However, starting in 1992, Scherer should be phased out of Gulf's rate base to reflect the dedication of additional Scherer capacity to Unit Power Sales and Gulf should be required to refund the revenue requirements associated with these megawatts to their territorial customers. Also, if 63 MW of Scherer 3 is included in Gulf's rate base, Gulf's share of the settlement from Gulf States Utilities for the time during which Scherer is in Gulf's rate base should be refunded to Gulf's customers.

POSITION OF PARTIES:

GPC: Yes. The Commission has repeatedly recognized the prudency of Gulf's participation in an ownership interest in Plant Scherer, Unit 3. The Commission has likewise recognized that the Plant Scherer capacity was obtained for the long-term benefit of Gulf's territorial customers. This capacity is currently dedicated to the provision of service to Gulf's territorial customers, and consequently, should be included in rate base.

OPC: The 63 MW of Plant Scherer should be excluded from Gulf Power Company's retail rate base.

FEA: No.

STAFF ANALYSIS: Gulf acquired 25 percent of Plant Scherer 3 in 1984 and it came on line in January, 1987 (Ex. 456, p. 2). Since Plant Scherer came on line after Gulf's last rate case, this is the first time Gulf has requested that a portion of Plant Scherer be included in rate base. Of Gulf's 212 MW share of Scherer 3, 63 MW is available to serve Gulf's territorial customers in 1990 and 149 MW is dedicated to Unit Power Sales. The 63 MW of Scherer 3 that Gulf is requesting to be included in rate base includes 44 MW that would have been sold to Gulf States Utilities if they had not defaulted. Gulf is requesting that 63 megawatts of its 212 megawatt share of Plant Scherer 3 be included in its rate base. Staff has identified three alternatives for the Commission to consider with regard to allowing Scherer into rate base:

1. allow Scherer and phase it out of rate base as the capacity dedicated to territorial load is committed to Unit Power Sales starting in 1992;
2. disallow 63 MW of Scherer; or
3. allow Scherer in rate base and initiate rate case if the future Unit Power Sales cause Gulf to exceed their allowed return on equity.

Although there are valid arguments for choosing any of the three options, staff recommends that the Commission choose Alternative 1--allow 63 megawatts of Scherer in rate base and phase it out as the capacity allowed in rate base is committed to Unit Power Sales starting in 1992. The following discussion will first outline the reasons that staff recommends Alternative 1 and will then discuss the merits of choosing the other two alternatives. Finally, the issue of the Southern/Gulf States Utilities settlement will be discussed as it relates to including Scherer in rate base.

Alternative 1

Staff recommends that the Commission adopt the position of Alternative 1--that Gulf be permitted to include 63 MW of Scherer in rate base and that this capacity be phased out (with refunds) starting in 1992. This recommendation is based on staff's belief that Gulf was prudent in acquiring Scherer, but that Gulf should not be recovering Scherer from its retail customers when it is not available for their use.

When considering whether to allow 63 megawatts of Plant Scherer into Gulf's rate base, the issue of Gulf's reserve margin is not as significant as it was with the inclusion of Plant Daniel. Gulf's reserves are reasonable with or without Scherer. Without Scherer (and with Daniel), Gulf's reserves are 21.9 percent and with 63 megawatts of Scherer (and with Daniel), Gulf's reserves are 25.5 percent. Southern's reserves are 19.9 percent and 20.1 percent respectively (Ex. 456, p. 11). It appears that with or without Plant Scherer, Gulf did a pretty good job of achieving its target reserves of 20 to 25 percent and since Gulf's load is expected to grow, based on reserve margin alone, it appears as if Scherer should be permitted in Gulf's rate base.

Staff has also concluded that Gulf was prudent in acquiring 25 percent of Plant Scherer 3. When Gulf started looking at purchasing 25 percent of Scherer 3 and Scherer 4 in 1978, they forecasted that they would need capacity around 1987 to 1989; however, in 1981, Gulf forecasted that they would not need the capacity until 1993 (Ex. 583, p. 13-15). Unfortunately, Scherer 3 and Scherer 4 were available in 1987 and 1989 or not available at all. Gulf entered into a contract for the purchase of a portion of Scherer 3 and Scherer 4 in February, 1981 knowing that the units would be available six years before Gulf's retail customers needed the capacity. They did this because purchasing Scherer was cost-effective to the ratepayers in the long run compared to constructing Carryville with a 1993 in-service year. It was cost-effective for two reasons: 1) the average 1987 and 1989 cost of Scherer was projected to be $855 per kilowatt compared to a 1993 cost of Carryville of $2662 per kilowatt (because of the early commitment of Scherer and the fact that it is not scrubbed); and 2) Gulf expected to sell at least a portion of this capacity to Florida utilities to displace oil in the years that Gulf's customers did not need the capacity. Gulf projected a present value savings of $263 million in 1981 dollars of purchasing part of Scherer 3 and Scherer 4 in 1987 and 1989 compared to constructing Carryville in 1993 (Ex. 583, p. 16-20). In a March, 1983 reevaluation of Gulf's participation in Scherer 3 and Scherer 4, Gulf indicated that if their load forecast does not drop, Scherer is still the "most cost-effective alternative available for base-load generation" (Ex. 583, p. 88). However, the analysis indicated that Gulf could incur surplus capacity if the load forecast falls or if the Unit Power Sales contracts are overturned. In a December 9, 1983 letter from Douglas McCrary to R. W. Scherer, Mr. McCrary wrote, "We have completed our analyses which continue to show that the Scherer capacity is overwhelmingly the lowest cost for providing the future electrical requirements of our customers...However, due to the decline in Gulf's load growth projections, the management of Gulf Power Company has decided to limit Gulf's participation in Plant Scherer to 25% of Unit 3 only, if this arrangement is agreeable to Georgia Power Company" (Ex. 583, p. 177). These facts indicate that Gulf was prudent in assessing a need for capacity in the early 1990's. The documents in Exhibit 583 indicate that Gulf continued to reassess its participation in Scherer 3 and Scherer 4 until it acquired Scherer 3 in 1984.

Weighing the benefits of low cost generation with the risk of lower than projected load forecast and potential loss of some Unit Power Sales contracts, Gulf decided to purchase 25 percent of Scherer 3 and cancel their participation in Scherer 4. Looking at the decisions Gulf made in 1978 through 1984, staff believes that Gulf was prudent in acquiring their ownership of Scherer 3.

The reason that staff is recommending the phase out of Scherer from rate base starting in the year 1992 is because Gulf will be selling increasing amounts of Scherer as Unit Power Sales starting in 1992. The following table is derived from Ex. 73 and shows the amount of Scherer dedicated to Gulf's territorial customers from the year 1990 to the year 2010.

Time	Capacity Available to Retail Customers
Jan. 1990 - May 1992	63 megawatts
June 1992 - Dec. 1992	11 megawatts
Jan. 1993 - May 1993	37 megawatts
June 1993 - Dec. 1993	16 megawatts
Jan. 1994 - May 1994	17 megawatts
June 1994 - May 1995	35 megawatts
June 1995 - May 2010	0 megawatts

Gulf argues that they will be adding other capital items during these years and that they would not earn a return on them until the next rate case; therefore, this would compensate for earning a return on Scherer when it is not being used to serve their territorial customers. Also, if this arrangement caused Gulf to over earn, they would be brought in for another rate case. Staff does not agree with this argument for several reasons. Staff does not believe that Gulf's ratepayers should be paying for a plant that is not available for their use. If Gulf adds other capital expenditures that would cause them to under earn, then Gulf should come in for another rate case (like any other utility would)--they shouldn't use the recovery of Scherer as a cushion to delay the filing of another rate case. Gulf has testified that they do need capacity in the 1995 time frame and that they will replace the coal capacity sold as Unit Power Sales with combustion turbine capacity ( ). If Gulf was permitted recovery of Scherer 3 without a phase-out, rates would be based on a coal unit and instead of benefiting from the unit's low energy costs, Gulf's customers would be paying the higher energy costs of a combustion turbine. Gulf's stockholders will be paying the lower capital cost of the replacement combustion turbine unit while receiving Unit Power Sales revenues based on the higher capital cost coal unit. Although the effect of replacing the coal capacity with combustion turbine capacity results in an overall lower cost, it is possible that the ratepayers could incur a higher cost as a result of paying for more expensive fuel. Whereas, the stockholder is guaranteed to be better off under this arrangement. Phasing Scherer out of rate base starting in 1992, and requiring refunds to Gulf's customers would prevent Gulf's customers from paying for capacity that is not available to serve them.

Staff supports the inclusion of 63 MW of Scherer 3 in Gulf's rate base with a phase-out starting in 1992 because staff believes that Gulf was prudent in acquiring Scherer. Also, the Commission should not penalize Gulf in 1990 for making additional Unit Power Sales from Scherer in 1992 and beyond if such sales are in the best interest of Gulf's customers; however, the territorial customers should receive their share of benefits from these sales--if the plant is not phased out, the territorial customers could be worse off as a result of these sales.

Staff has attached a schedule following the discussion of this issue reflecting the approximate rate reductions in those years where additional megawatts are committed to Unit Power Sales. The calculation of the rate reductions were based on prorating the reduction in megawatts times the 1990 rate base and N.O.I. components. A slight increase in revenue requirements is shown for 1994 over 1993 when an additional 2 MW is dedicated to retail service.

Rate base has been adjusted to remove the acquisition adjustment on the common facilities (Issue 4) and refund received from Georgia Power Company related to the purchase price of Scherer 3 (Issue 3). Net Operating Income has been adjusted to remove the amortization and depreciation expense associated with the rate base adjustments.

Alternative 2

Under Alternative 2, none of Scherer 3 would be permitted in Gulf's rate base. There are merits to this alternative. First, there is the argument that if Gulf does not need Scherer in 1995 (when it is all sold as Unit Power Sales), then they do not need it in 1990. Second, it could be argued that since Gulf was willing to sell 44 MW of Scherer 3 to Gulf States Utilities (GSU) in 1990, then Gulf's ratepayers do not need that capacity in 1990. And finally, it could be argued that since Gulf's stockholders earned the return from Unit Power Sales, then they should bear the risk of the Unit Power Sales falling through.

As discussed under Alternative 1, Gulf is scheduled to sell increasing amounts of Scherer 3 under Unit Power Sales agreements starting in 1992. By 1995, none of Scherer 3 will be available to serve Gulf's territorial customers. This capacity will not be available to serve Gulf's territorial customers until the year 2010. It could be argued that since Gulf is dedicating this unit to Unit Power Sales in years that Gulf's territorial load is expected to be greater than it is in 1990, then Gulf does not need the unit in 1990.

Under Southern's contract with GSU, Gulf had committed to sell 44 MW of Scherer 3 to GSU during the test year 1990 through May, 1992. GSU failed to perform its contractual obligations since July, 1986 and on July 1, 1988, FERC ruled that Southern no longer had to perform under the contract (Ex. 468, p. 3). It is clear that Gulf would not have requested 63 MW of Scherer to be in rate base had GSU not defaulted on their contracts--they probably would have requested the inclusion of 19 MW of Scherer 3. As discussed in Alternative 1, Gulf made the decision to purchase 25 percent of Scherer 3 knowing that their contract with GSU knowing that the contract may not be honored. A March, 1983 Gulf Power document states, "if the [GSU] contracts survive the intervention of the Louisianna (sic) PSC, there is a very slight possibility that the contracts might not be honored if the price of oil continues to decline; however, most forecasters agree that the escalation of oil will be greater than coal..." (Ex. 583., p. 84). It could be argued that since the profits of the Unit Power Sales go to Gulf's stockholder, they should also bear the risks of losses under these contracts; therefore, the 44 MW of Scherer 3 previously dedicated to GSU should not be allowed in rate base.

Issue 27 addresses the appropriate rate base and N.O.I. adjustments if Scherer is excluded from rate base.

Alternative 3

Under Alternative 3, 63 MW of Scherer 3 would be allowed in Gulf's rate base and there would be no refunds to the customers for phasing out this capacity starting in the year 1992. As discussed under Alternative 1, staff believes that Gulf was prudent in acquiring 25 percent of Scherer 3. It can be argued that since Gulf purchased Scherer for the benefit of their territorial customers, that these customers should take the risk of the Unit Power Sales. As discussed in Alternative 1, Gulf maintains that the Commission should not be disturbed by the fact that Gulf's ratepayers will be paying for capacity that is not available to them starting in 1992 because Gulf will be making other capital expenditures that will benefit their customers. These expenditures will not be recovered from Gulf's ratepayers until Gulf has another rate case. These arguments have merit; however, staff believes that the arguments for Alternative 1 are stronger.

Other Issues

Since the hearing in June, Southern Company and Gulf States Utilities have reached a settlement regarding the termination of the power sales contract between the parties. If the portion of Plant Scherer that was previously dedicated to Gulf States Utilities is allowed in Gulf's rate base, Gulf should be required to allocate and refund a portion of this settlement to their territorial customers. The settlement should be discussed in Docket No. 900621-EI, Review of Power Sales Contract Settlement Agreement between GULF POWER COMPANY (Southern Company) and Gulf States Utilities Company.

GULF POWER COMPANY
PHASE - OUT OF PLANT SCHERER
(000)

Rate Base Impact	(1) 63 MW 1990	(2) (30 MW) 1992	(3) (8 MW) 1993	(4) 2 MW 1994	(5) (27 MW) 1995	TOTAL (6) (63 MW) 1996
Rate Base	47,269	(22,509)	(6,002)	1,501	(20,258)	(47,269)
Rate of Return	8.05%	8.05%	8.05%	8.05%	8.05%	8.05%
N. O. I. Requirement	3,805	(1,812)	(483)	121	(1,631)	(3,805)
Expansion Factor	1.631699	1.631699	1.631699	1.631699	1.631699	1.631699
Revenue Requirement	6,209	(2,957)	(788)	197	(2,661)	(6,209)
O & M Impact						
O&M Expenses	2,523	(1,201)	(320)	80	(1,081)	(2,523)
IIC Offset	(4,792)	2,282	609	(152)	2,054	4,792
Net O&M	(2,269)	1,080	288	(72)	972	2,269
Income Taxes	(854)	407	108	(27)	366	854
N.O.I. Effect	(1,415)	674	180	(45)	607	1,415
Expansion Factor	1.631699	1.631699	1.631699	1.631699	1.631699	1.631699
Revenue Requirement	(2,309)	1,100	293	(73)	990	2,309
Total Revenue Requirement	3,900	(1,857)	(495)	124	(1,671)	(3,900)
Rate (Reduction) Increase		(1,857)	(495)	124	(1,671)	(3,900)

ISSUE 27: If Plant Scherer 3 is not included in rate base, what are the appropriate rate base and NOI adjustments to exclude it? (ROMIG)

RECOMMENDATION: The appropriate adjustments are as follows:

Plant-in-service	$52,987,000
Accumulated depreciation	6,557,000
Acquisition adjustment	2,317,000
Working capital	2,187,000
O&M expenses	722,000
Depreciation expense	1,701,000
Amortization of plant acquisition adj.	73,000
Amortization of ITC	(96,000)
Other taxes	245,000
IIC offset	(4,792,000)

POSITION OF PARTIES

GULF: No adjustment is appropriate. Gulf has fully justified inclusion of the 63 MW of Scherer capacity in rate base. If the 63 MW is removed from rate base, with the associated expenses, then the entire impact of the Scherer capacity should likewise be removed. The territorial customers of Gulf receive substantial benefits from the unit power sales (UPS) contracts. If the territorial customers are to bear no burden of the Scherer capacity which Gulf purchased for their benefit, they should certainly receive none of the benefits. Properly taking the UPS benefits and Intercompany Interchange Contract credits into account, the adjustments result in revenue requirements of approximately $2 million. The details of the appropriate revenue requirements and credits are shown on Exhibit 575.

OPC: The proper adjustments to remove Plant Scherer are:

Plant-in-service	$52,987,000
Accumulated depreciation	6,558,000
Acquisition adjustment	2,317,000
Working capital	2,187,000
Production A&G & trans. rentals	843,000
Depreciation	1,688,000
Amortization - aquis. adj. & other	89,000
Other taxes	244,000
Amortization of ITC	(96,000)

STAFF ANALYSIS: Staff's recommendation is based on Exhibit 575. Mr. McMillan introduced this exhibit at the hearing. It provided the rate base and expenses related to the 63 MW of Plant Scherer included in the 1990 test year. According to this exhibit, the impact on revenue requirements was $3,598,000. Gulf reflected on page 2 of this exhibit the various expenses which are allocated to UPS and not directly related to the Plant Scherer production expenses. After making all the adjustments suggested by Gulf, there is a negative revenue requirement of $72,000.

Gulf's basic position is that if the retail ratepayer is not to bear the burden of the Scherer capacity, then those customers should not benefit from the UPS agreements.

Public Counsel's position is that the 63 MW of Plant Scherer should be removed from rate base, and that the adjustments shown above under their position should be made. These adjustments were provided to Public Counsel in response to Interrogatory No. 144, Exhibit 432.

Mr. Larkin testified that he did not agree with Exhibit 575 (T. 2307). Mr. Larkin further stated, "...we would dispute the conclusions reached that there is a net benefit of $1.7 million in the transmission and general amounts and that there is a net benefit to the ratepayers of $1,969,000 in variable O&M" (T. 2315).

Staff has recommended in Issue 26 that the Commission allow the 63 MW in rate base. However, if the Commission removes the 63 MW from rate base, the above adjustments should be made.

The recommended adjustments do not include the UPS credits as proposed by Mr. McMillan on Exhibit 575; inclusion would result in a $72,000 negative revenue requirement. It is difficult to reconcile this negative revenue requirement with the following testimony of Mr. McCrary and Mr. Scarbrough:

Mr. McCrary:

> The principal reason for our need for rate relief is the need to earn an adequate return on the additional investment associated with power generation resources, specifically Plant Daniel and Plant Scherer, and the associated operating and maintenance expenses (T. 38).

Mr. Scarbrough:

> The major factor triggering the company's immediate need for rate relief is that all 515 megawatts of Gulf's portion of the Plant Daniel capacity and 63 MW of Gulf's ownership in the Plant Scherer capacity is now committed for territorial service (T. 298).

It appears that if these expenses are allocated to and recovered from the UPS customers, and if these expenses were also added back to the retail jurisdiction, there would be a double recovery of these expenses.

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<u>ISSUE 28:</u> What adjustment is proper to remove the 1984 cancelled Southern Company Services' building from rate base? (MERTA)

<u>RECOMMENDATION:</u> No adjustment is needed since the dollars associated with the cancelled building have already been removed from rate base by Gulf.

<u>POSITION OF PARTIES</u>

<u>GULF:</u> No adjustment is needed since the expenses associated with the cancelled Southern Company Services building have already been removed from rate base in Gulf's filing.

<u>OPC:</u> This issue was raised by Public Counsel but was not addressed in their Brief.

<u>STAFF ANALYSIS:</u> The parties agree that no adjustment is needed since Gulf made the correcting entry to expense the cancellation costs in May 1989. (TR 2292, 3909).

In 1984, Southern Company Services cancelled the construction of a building, the costs of which were allocated to all the system operating companies. A total of $715,752 was allocated to Gulf. The Company charged $369,305 to operating expense and capitalized $346,447.

According to the Uniform System of Accounts, expenditures for cancelled construction projects should be charged to Account 426.5, Other Deductions (below-the-line), or to the appropriate operating expense account. Gulf agreed with this exception and made the appropriate correcting entry in May 1989.

The financial forecast used in developing the 1990 test year included actual data through August 1989, therefore, the project has been properly removed and there is no impact in the 1990 test year. (TR 3909). Staff's audit verified that the $346,447 was expensed below-the-line May 31, 1989 and that for budgeted 1990, the project was properly removed. (Exhibit 383, TR 2969)

Based on the above, Staff recommends that no adjustment is necessary.

ISSUE 29:: What, if any, adjustment to rate base is necessary to reflect the proper treatment for rebuilds and renovations which were expensed by the Company? (WILKERSON)

RECOMMENDATION: No adjustment is necessary.

POSITION OF PARTIES

GULF: No adjustment is necessary; Gulf properly accounts for rebuilds and renovations.

OPC: Increase plant in service by $369,000 and increase depreciation reserve by $18,000 and decrease O&M by $368,500.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: Public Counsel witness Schultz took the position that, in regard to the vehicle rebuild program the costs should be "capitalized since the rebuild programs will extend the lives of the assets being rebuilt" (Tr. p. 2477), and in regard to the renovation of the Panama City Office building the expenditure represents "an improvement to the structure as opposed to ordinary maintenance" and "should extend the life of this asset" (Tr. p. 2478). Such considerations on an item by item basis might provide a rule of thumb, absent any formal guidelines. However, as Gulf witness Scarbrough pointed out (Tr. p. 3857), there is a Florida Public Service Commission List of Retirement Units, designating items to be capitalized rather than expensed. This list is being followed by Gulf. In regard to the Panama City Office building renovations, Gulf witness Conner states in his testimony (Tr. p. 3646) that changes to existing components not classified as retirement units are to be expensed in accord with the Company's list of retirement units, which conforms to the Rules of this Commission.

ISSUE 30: What, if any, adjustment to rate base is necessary to remove the network protectors from expense to rate base? (WILKERSON)

RECOMMENDATION: No adjustment is necessary.

POSITION OF PARTIES

GULF: No adjustment is necessary; Gulf properly accounts for maintenance of network protectors in O&M expenses.

OFFICE OF PUBLIC COUNSEL: Increase plant in service by $90,000 and depreciation reserve by $5,000 and decrease O&M expenses by $90,000.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: Public Counsel witness Schultz took the position that the overhaul of the network protectors should be capitalized rather than expensed, since the overhaul would extend the life of the assets (Tr. p. 2510). Gulf witness Scarbrough states (Tr. p. 3791) that "the 'remanufacturing process' simply replaces minor items of property" on the network protectors which is nothing more than maintenance and, under FPSC Rule 25-6.0142, such costs are to be expensed.

ISSUE 31: Should the remaining balance in Other Investments be included in Working Capital? (REVELL)

RECOMMENDATION: Yes, the remaining balance of $144,354 of Other Investments should be included in Working Capital.

POSITION OF PARTIES

GULF: Yes. These insurance reserves of deposits were required to obtain reasonable prices and terms of coverage and are properly included in rate base. (McMillan)

OPC: No. This item has not been justified; remove $113,000 from working capital. (Larkin)

STAFF ANALYSIS: These insurance reserves are actually deposits which Gulf made to insurance companies in order to receive reasonable prices and terms of coverages for their public liability and directors and officers liability insurance.

The FPSC Audit Report [Exhibit 383], disclosure No. 28 indicated that a certain policy should be excluded from working capital since the policy provided for dividends to the company. In its response to the Audit [Exhibit 299] the company provided a page of the policy which indicated that any reserve premium paid out by Gulf would be returned upon cancellation less any amounts previously distributed or used to absorb losses or expenses. As a result, it appears that the total to be returned would not exceed the original amount paid.

As a result, staff recommends that the remaining amount of Other Investments totalling $144,354 be included in working capital.

ISSUE 32: Should the working capital item titled "other accounts receivable" be removed? (MERTA)

RECOMMENDATION: No. These receivables are properly included in working capital.

POSITION OF PARTIES

GULF: No. These amounts are properly included in working capital.

OPC: This isssue was raised by Public Counsel but was not addressed in their Brief.

STAFF ANALYSIS: The parties agree that no adjustment is necessary.

The Company included in working capital $1,230,000 net for "other accounts receivable." OPC Witness Larkin initially recommended excluding this amount because he was not certain that the receivables actually pertained to utility service. (TR 2219). Public Counsel took no position on this issue in their Brief.

Gulf Witness McMillan testified that these receivables include all the amounts due the utility except for the amounts related to associated companies and from their electric customers. The majority of the receivables are for pole attachment rentals for which the revenues have been recorded in other operating revenues. The remaining amounts pertain to pole and line damage claims and other miscellaneous utility billings. (TR 3913). The Commission fully allowed Gulf's "other accounts receivable" in working capital in the 1984 rate case. (TR 3953).

Therefore, Staff recommends that no adjustment is necessary.

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ISSUE 33: Has the company overstated the materials & supply level? (ROMIG)

RECOMMENDATION: No. Materials and Supplies should not be reduced for 1990.

POSITION OF PARTIES

GULF: No. The 1990 estimate for materials and supplies is reasonable, utility related and properly included in working capital.

OPC: Yes. Reduce M&S by $2,307,000.

STAFF ANALYSIS: Gulf has included in its 1990 working capital allowance $32,403,000 for Materials & Supplies (M&S) or an increase of $2,307,000 over the partially projected 1989 year.

OPC Witness Larkin has reduced working capital by $2,307,000 based on the historical 13-month average balance ended February, 1990 (T. 2220).

Company Witness McMillan stated in his rebuttal testimony that the balance for the period ending February, 1990 is not representative of the test period (T. 3912). If the actual balance for February, 1990 were used it would significantly lower Mr. Larkin's adjustment.

If Mr. Larkin's adjustment were made to the $32,403,000, 1990 level of M&S, the adjusted balance would be $30,096,000. This is the same amount included in Gulf's 1989 partially projected allowance for materials & supplies, page 5 of MFR Section B, rate base schedules. The $30,096,000 amount for 1989 is over the actual 1989 by $362,000 or approximately 1%. In staff's opinion, it is unreasonable to assume that the level of M&S inventory would remain the same from one year to the next or increase by only $300,000 when considering increases in the company's investment in electric facilities and customers.

Therefore, no adjustment is recommended.

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ISSUE 34: Should the amounts shown as "other current assets" and "other miscellaneous" deferred debits be removed from working capital? (MERTA)

RECOMMENDATION: No. These amounts are properly included in working capital.

POSITION OF PARTIES

GULF: No. (McMillan)

OPC: This issue was raised by Public Counsel but was not addressed in their Brief.

STAFF ANALYSIS: The parties agree that "other current assets" and "other miscellaneous deferred debits" are properly included in working capital.

OPC Witness Larkin initially recommended that $136,000 related to "other current assets" be excluded from working capital because there was no explanation of what the prepaids were and that $30,000 related to "other miscellaneous deferred debits" be disallowed because there was no balance in this account for the period of January through August 1989. (TR 2221-2222). Public Counsel took no position on this issue in their Brief.

Gulf Witness McMillan testified that the prepayments classified as "other" are primarily composed of prepaid licenses for motor vehicles, prepaid taxes, prepaid city and county occupational licenses, and prepaid registrar transfer and fiscal agent fees. (TR 3913-3914).

The $30,000 is a very conservative estimate of the recurring miscellaneous charges that are always present in miscellaneous deferred debits which cannot be identified in advance. McMillan stated that the analysis upon which Witness Larkin based his statement that the account had no balance for January through August 1989 was a workpaper used for the forecasted amounts, not an analysis including actual. The actual amounts for January through August 1989 averaged in excess of $100,000. (TR 3914).

In Gulf's last rate case, the Commission fully allowed "other current assets" and "other miscellaneous deferred debits" in working capital. (TR 3953).

Staff recommends that "other current assets" and "other miscellaneous deferred debits" are properly included in working capital and that no adjustment is necessary.

ISSUE 35: Should the Caryville Subsurface Study be removed from rate base? (REVELL)

RECOMMENDATION: No. The $692,000 in costs for this study should remain in rate base since it relates to engineering work done for the plant site at Caryville.

POSITION OF PARTIES

GULF: No. The subsurface investigation of the Caryville site is still valid and will be utilized in conjunction with the addition of generation at Caryville. (Parsons)

OPC: Yes. Remove $692,000 from rate base. (Larkin)

STAFF ANALYSIS: The subsurface study was a geological study of the Caryville site to determine if the land could support the weight of a power plant and supporting facilities. As pointed out in the company's brief, the results of the study are obviously still valid. Such a study would be necessary before any major construction of this type could be done on any site. Therefore, costs associated with the study should be considered together with the Caryville site itself. If Caryville is removed from Land Held for Future Use in Issue 15, then $692,000 for this subsurface study should also be removed. If Caryville remains in Rate Base, these expenses should be allowed.

ISSUE 36: What, if any, additional working capital adjustments are needed to reflect OPC's expense exclusions? (MERTA)

RECOMMENDATION: If the Commission accepts staff's recommendations in Issues 50, 92 and 100, working capital should be increased by $169,187 ($179,105 System).

If the Commission disallows the expenses related to the plans listed below in Issues 50, 92 or 100, working capital should be increased by an additional $985,000, $2,935,000, $12,000, or $59,000, respectively.

POSITION OF PARTIES

GULF: None. OPC's expense exclusions are inappropriate; therefore, no additional working capital adjustments are necessary. (McMillan)

OPC: The adjustment is to increase working capital by $3,874,000 as provided by OPC in their schedule.

STAFF ANALYSIS: Public Counsel Witness Larkin recommended that $3,874,000 related to the deferred credit balances of expenses which OPC excluded from operating income be removed from working capital. If the expenses are disallowed, then it would be inappropriate to include the deferred credit balances as a reduction of working capital. These reserves are associated with the Supplemental Pension and Benefits Plan ($985,000), Post Retirement Life and Medical Plan ($2,935,000), Deferred School Plan Appliances ($12,000), and the Productivity Improvement Plan ($59,000). (TR 2223-2224). The expenses related to these plans are discussed under Issues 50, 92, and 100.

The Company stated that Public Counsel's expense adjustments and working capital exclusions are inappropriate since Gulf has justified the inclusion of these expenses in rates. (Gulf Brief p. 95).

The parties agree that the reserves associated with expenses which have been disallowed should be removed from working capital. (TR 767, 2223). Staff is not recommending disallowance of the expenses associated with these reserves. Therefore, the reserves should remain in working capital. However, since the Company reduced expenses related to PIP, an adjustment is necessary to reduce the reserve. A reduction to a deferred credit increases working capital since current liabilities will be less. Staff recommends increasing working capital by $169,187 ($179,105 System). (Late Filed Exhibit 571).

If the Commission disallows expenses in Issues 50, 92 or 100, an additional increase to working capital will be necessary as discussed above.

ISSUE 37: What is the appropriate cost of common equity capital for Gulf Power? (YECCO)

RECOMMENDATION: The appropriate cost of common equity capital for Gulf Power is 12.3 %. (This does not include the 50 basis point reduction recommended in Issue 38)

POSITION OF PARTIES

GULF: The appropriate cost of equity capital for Gulf Power is 13.50%.

OFFICE OF PUBLIC COUNSEL: The proper calculated return on equity should be set at 11.75%, however, this ROE should be adjusted downward for mismanagement.

FEA: Same position as the Office of Public Counsel.

STAFF ANALYSIS: Three witnesses presented testimony on the appropriate cost of equity capital for Gulf Power.

Dr. Roger A. Morin, Professor of Finance at the College of Business Administration, Georgia State University and Professor of Finance for Regulated Industry at the Center for the Study of Regulated Industry at Georgia State University. (On behalf of Gulf Power) Dr. Morin recommends the adoption of a return on common equity of 13.5%.

Mr. James A. Rothschild, President, Rothschild Financial Consulting. (On behalf of the Citizens of the State of Florida) Mr. Rothschild recommends that the proper calculated return on equity for Gulf Power is 11.75%.

Mr. Scott A. Seery, Regulatory Analyst, Bureau of Finance, Division of Auditing and Financial Analysis, Florida Public Service Commission. (On behalf of the Florida Public Service Commission Staff) Mr. Seery recommends the adoption of a return on common equity of 12.25%.

SUMMARY OF TESTIMONY

The witnesses used three different equity costing methodologies to arrive at their estimates of Gulf's cost of equity. Witness Morin the risk premium, discounted cash flow (DCF) and capital asset pricing model (CAPM) methodologies. Witness Rothschild relied primarily on the DCF method. Witness Seery used the DCF and risk premium methods.

Witness Morin

Witness Morin performed DCF analyses on two different surrogates for Gulf: the Southern Company and an index of comparable risk electric utilities. (TR 1665) According to witness Morin, since Gulf is a wholly owned subsidiary of the Southern Company, its stock is not publicly traded and thus any market value approach to determine the investor's expected return on equity must be applied indirectly. (TR 1678) Witness Morin applied the DCF model to Southern Company data using an average of security analysts' growth expectations, the sustainable growth rate method, and historical growth rates as a proxy for expected growth. (TR 1678). Witness Morin used the average of historical growth rates and analysts' growth forecasts as a proxy for growth in his DCF analysis of an index of comparable risk electric utilities. Witness Morin adjusted his results upward by 40 basis points to reflect the quarterly timing of dividends and also provided a five percent allowance for flotation costs. (TR 1682 & 1698) For Southern Company, witness Morin used a dividend yield component of 8.55% to which he added an average growth rate of 3.83%. (TR 1695) Adjusting his result to reflect quarterly compounding and an allowance for flotation costs, witness Morin arrived at a DCF cost of equity estimate for Southern Company of 13.25%. (TR 1698)

For an index of comparable risk electric utilities, witness Morin initially examined the 100 electric utilities monitored in Salomon Brothers Electric Utility Monthly that were also included in Value Line's data base and in the IBES summary of analysts' growth forecasts. Witness Morin eliminated utilities that have suspended dividends and from the remaining utilities used the beta coefficient to identify electric utilities with investment risks similar to those of Gulf. (TR 1699) Witness Morin used Southern Company's beta of .75 as a proxy for Gulf. Eighteen companies from his initial sample had a beta of .75. (TR 1701) Using the five year historical growth rate and the IBES analysts' growth forecasts, witness Morin estimated a DCF cost of equity for his index of 13.74% and 12.32%, respectively. Witness Morin averaged the two results to obtain an estimate of 13.03%. (TR 1704)

Witness Morin also used risk premium and capital asset pricing model methodologies. In his first risk premium study, witness Morin estimated the risk premium for Southern Company, by subtracting the average annual bond yield for A-rated utility bonds from the DCF estimate of Southern Company's cost of equity for the time period 1979 through 1988. (TR 1710) Witness Morin then regresses the risk premium on the bond yield to obtain a regression equation in which the interest rate is the independent variable and the risk premium is the dependent variable.

The regression of Southern Company's risk premium on the yields of A-rated utility bonds provides the equation, Risk Premium = .1366 - (.8402 * interest rate). Substituting the yield on A-rated bonds as of May 1990 of 10% into the equation provides a risk premium of 5.26%. Adding a bond yield of 10% to a risk premium of 5.26% produces a cost of equity of 15.26%. (TR 1712)

Witness Morin applies a similar methodology using a monthly time series over the past four years instead of an annual time series. (TR 1712) Witness Morin uses this methodology to calculate a risk premium for Southern Company and for Moody's Electric Utility Index. Using a bond yield of 10%, witness Morin estimated a cost of equity for Southern Company and Moody's Index of 13.77% and 13.47%, respectively. (TR 1714-1715)

Finally, witness Morin estimates the cost of equity using the Capital Asset Pricing Model. Witness Morin uses a beta of .75, the yield on long-term treasuries for May 1990 of 8.7% as a proxy for the risk-free rate, and an expected market return of 16.11%, estimated using the Ibbotson & Sinquefield study, as inputs into the CAPM model. (TR 1716-1717) Plugging these variables into the CAPM model provides an estimate of the cost of equity of 14.25%. (TR 1718) Witness Morin performs a similar analysis using an expectational return on the market of 13.7% instead of 16.11%. (TR 1717) Using an expected market return of 13.7% yields a cost of equity of 12.45%. (TR 1718) Witness Morin takes the average his two CAPM results, 13.35%, and adds 30 basis points for flotation costs to arrive at an estimate of 13.65%. (TR 1718) Witness Morin also estimates a cost of equity of 14.04%, using an expanded form of the CAPM model. (TR 17120)

Witness Rothschild

Witness Rothschild's recommended return on equity of 11.75% is based primarily on the application of the DCF method to the electric utilities comprising Moody's Electric Utility Common Stock Index which are not in the midst of nuclear uncertainties, and to the Southern Company. (TR 2678)

For the dividend yield component of his DCF analysis, witness Rothschild examines both current spot dividend yield data and historic data. Witness Rothschild notes that there is a relatively small difference between the current yields and the average yields over last year. (TR 2702) Witness Rothschild increases the current dividend rate by an amount equal to one-half a year's growth in dividends to reflect the average dividend rate expected by investors in the near future. (TR 2702) For the growth component of his analysis, witness Rothschild uses the b * r method. The "r" component is the future expected return on book equity. For Southern Company, Witness Rothschild uses an expected return on book equity of 13.0% as one of his inputs to calculate the growth rate. (TR 2712) The "b" component or the retention rate is the percentage of earnings not paid out as dividends. Witness Rothschild calculated a retention rate for Southern Company of 24.78%. (TR 2743) Multiplying the expected return on book equity of 13.0% by the retention rate of 24.78% produces a sustainable growth rate of 3.22%. (TR 2712) To the 3.22%, Witness Rothschild added .04% to .05% to reflect the growth in earnings expected to be caused by new stock sales. (TR 2713) Adding Southern Company's growth rate to its dividend yield, witness Rothschild estimated a cost of equity for Southern Company of 11.52%. Witness Rothschild adjusts his estimate upwards by 24 basis points to reflect flotation costs. (TR 2719)

Using the same methodology as described above, witness Rothschild estimated a return on equity of 11.12% for his non-nuclear utilities. Witness Rothschilds determined that Gulf was more highly levered than the utilities comprising this index. To the 11.12% estimate witness Rothschild adds 40 basis points to reflect Gulf Power's higher financial risk and adds 24 basis points for flotation costs. Witness Rothschild recommends a cost of equity for Gulf Power of 11.75%.

Witness Seery

Witness Seery conducted a DCF and risk premium analysis on an index of high quality electric utilities and adjusted the results for the difference in risk between Gulf Power and the index. (TR 2959) Witness Seery used a two-stage growth, annually compounded DCF model that included an adjustment to reflect flotation costs. In his two-stage model, witness Seery estimated dividend growth for an initial growth period. Witness Seery then assumed that dividends would grow infinitely at the expected long-term growth rate. Witness Seery used Value Lines forecast of dividends for 1990 and 1993, and assumed a constant rate of growth in between to estimate the expected dividends during an intitial growth period. Witness Seery calculated the long-term constant rate of growth expected after 1993 by using the earnings retention method. (TR 2961) For the price component of his model, witness Seery used a current stock price determined by averaging the high and the low stock price for April 1990 for each utility in his index. (TR 2961) Witness Seery also adjusted the results produced by his model to reflect issuance costs of three percent. Witness Seery estimated a DCF cost of equity for his index of 11.3%. (TR 2962)

In his risk premium analysis, witness Seery uses the DCF methodology discussed above to estimate the expected market return for his index for each month over the ten year period June 1980 through May 1990. (TR 2962) Witness Seery then takes the expected return on common equity for each month and subtracts the concurrent yield on long-term government bonds to obtain the risk premium for the month. Witness Seery uses the average risk premium over the ten year period of 3.165% as the equity-debt risk premium for the index. (TR 2963) Adding the risk premium to Blue Chip Financial Forecasts' consensus forecast of 8.475% for long-term government bonds, witness Seery calculated a risk premium cost of equity of 11.65% for the index. (TR 2963)

Witness Seery used a bond yield differential to estimate the additional return required by an A-rated utility over his AA-rated index. Witness Seery determined that the average spread between AA-rated bonds and A-rated bonds has been approximately 30 basis points over the past 60 months. (TR 2965) Adding 30 basis points to cost of equity estimates for his index, witness Seery determined that in general the cost of equity for an A-rated electric utility fell within a range of 11.6% to 11.95%. (TR 2965) Finally, witness Seery concluded that Gulf Power was riskier than comparable A-rated utilities and thus an additional adjustment was warranted. Witness Seery added another 30 basis points to the top of the A-rated range to arrive at a cost of equity for Gulf Power of 12.25%. (TR 2966)

Staff Analysis

When analyzing the cost of equity one should realize that it is a subjective process. The cost of equity is impossible to measure precisely. Because of the rate setting process, however, staff must recommend a point estimate of the cost of equity. Based on the following analysis, staff recommends a midpoint cost of common equity of 12.3% for the purpose of setting rates. Staff believes the evidence supports a midpoint cost of equity within a range of 11.75% to 12.75%.

All three witnesses used a discounted cash flow methodology to help determine Gulf Power's cost of common equity. The premise behind the discounted cash flow methodology is that the investors' expected return is the sum of an expected dividend yield plus the expected growth rate of future dividends. In a DCF analysis the current stock price should be used to determine the dividend yield. A utility's current market price is easy to determine. Even the expected dividend for the coming year is easy to determine with a fair degree of accuracy. The variable subject to the most dispute and which has the greatest impact on the final result is the growth rate. Since dividends are the relevant cash flows the growth rate should represent the expected growth in dividends. (TR 1686) Use of a historic growth rate as a proxy for expected growth is appropriate only if the historic rate is expected to persist into the future. (TR 2728) Staff does not dispute the fact that analysts consider historical rates of growth to arrive at their estimates of expected growth rates. But this information has already been taken into consideration when analysts make their projections. Staff finds it hard to believe that analysts make projections of future growth without considering historic performance.

Witness Morin determined growth rates for his DCF analysis using historic rates that are not expected to persist into the future. For example, witness Morin averages an IBES growth forecast of 3.25%, a growth rate of 3.23% calculated using the b * r approach, and a 5-year historic growth rate of 5.0% obtained from Value Line. Witness Morin uses the average of the three results, 3.83%, is his DCF analysis of Southern Company. (TR 1695) Using a historical growth rate that is significantly different than that expected by investors upwardly biases both the dividend yield and growth components of witness Morin's DCF analysis. Using a dividend growth rate of 3.83% yields an expected dividend of $2.223 versus an expected dividend of $2.209 using a dividend growth rate of 3.24%. The difference in dividend yield is six basis points higher using a growth rate of 3.83%. The major impact, however, is the 59 basis point difference in the growth rates since the growth variable is additive. By averaging in a historical growth rate that is significantly different than that expected by investors, witness Morin overestimated the required market return indicated for Southern Company by 65 basis points.

The same criticism applies to witness Morin's DCF analysis of a group of comparable companies. Witness Morin uses historical growth rates that are higher than the growth rates indicated by IBES. The average historical growth rate is 5.24% compared to the average using IBES forecasts of 3.63%. Witness Morin did not use the b * r approach for his analysis of this group of utilities. Staff notes, however, that the b * r approach, using the same methodology employed by witness Morin for Southern Company, provides a sustainable growth rate of 3.53%. Using a historical growth rate produced a cost of equity of 13.74% versus a DCF cost of equity of 12.32% produced using IBES growth forecasts. (TR 1703) Witness Morin averages the two results for an estimate of 13.03% for his group of comparable companies. (TR 1703) By using the higher historical growth rate witness Morin overestimated the DCF cost of equity for his group of comparable companies by 70 basis points.

All three witnesses have adjusted their results to recognize the cost associated with issuing common stock. An allowance for issuance costs enables the utility to recover the cost incurred for issuing stock. Without an underwriting cost adjustment investors will never be able to earn their expected return since the sales price will exceed the net proceeds to the company. It is the net proceeds plus retained earnings that comprise the earnings base for a regulated utility. For example, if investors expect a return of 12% on an investment of $100 in newly issued stock, but the company receives less than $100 due to the costs associated with issuing the stock, then the company must earn a higher return than 12% on a smaller earnings base in order to provide investors with the opportunity to earn their expected return.

The witnesses have disagreed on the magnitude of the issuance cost adjustment that is necessary. Witnesses Seery and Rothschild allow a three percent adjustment for issuance costs versus the five percent adjustment included in witness Morin's results. (TR 1706, 2719 and 2961) Based on the evidence presented, staff believes that an allowance of three percent is reasonable and should be used unless company specific evidence is available that shows a higher allowance is warranted. Using a five percent adjustment results in cost of equity estimates that are approximately 20 basis points higher than they otherwise would have been if three percent were used.

Staff disagrees with witness Rothschild's implication that the issuance cost adjustment should apply only to the externally raised portion of common equity and not to the retained earnings portion. (TR 2719) Staff notes that for dividends to grow at the rate investors expect, the adjusted return on common equity must be applied to all common equity.

Both witnesses Seery and Morin performed forward looking risk premium analyses. Witness Morin uses Southern Company in two of his three risk premium studies. For his third study witness Morin used Moody's index of electric utilities. In each study witness Morin calculates a regression equation based upon the regression of the risk premium on the interest rate. Witness Morin uses the regression equation to predict a risk premium for a given interest rate. Witness Morin then adds the risk premium to the interest rate to provide an estimate of the cost of equity.

Witness Morin disregards the 15.26% return produced by his long-term risk premium analysis of Southern Company as being upwardly biased. (TR 1720) A close examination of witness Morin's remaining risk premium analyses show that risk premiums are not stable, can vary with interest rates, and can vary significantly with the same interest rate. For example, in witness Morin's risk premium analysis for Moody's Electric Utilities, interest rates of 9.5% to 10.5% had risk premiums associated with them of 2.11% to 4.62%. (Exh. 195) A casual observation of the raw data leads the observer to conclude that other factors in addition to interest rates affect risk premiums. This conclusion is supported statistically by the low r-squared statistic of Witness Morin's regression equations. In layman's terms, the r-squared, or the coefficient of determination, represents the percentage of the variability of the risk premium that can be explained by the variability of interest rates. Witness Morin's regression equation for Moody's Electric Index has an r-squared of .256637. (Exh. 8, p. 3) His regression equation for Southern Company (1984-1989) has an r-squared of .14479563. (Exh. 7, p. 3) In other words, the variability of interest rates explains 25.6637% and 14.479563%, respectively, of the variability of the risk premium. These results strongly suggest there are other factors besides interest rates that determine risk premiums. The ability of witness Morin's regression equations to predict the risk premium based on interest rates is questionable.

In staff's opinion, the results of witness Morin's risk premium analyses should be rejected.

Witness Seery also uses expectational data in his risk premium analysis. Witness Seery calculates the average equity risk premium over long-term treasury bonds for the most current 120 month period. Witness Seery adds the risk premium to Blue Chip's forecast of the long-term treasury yield for the upcoming year. This method weights equally all points under consideration. Staff believes that in this situation witness Seery's methodology yields a reasonable result. However, if the current trend appears to support higher or lower risk premiums that are very different than that suggested by the average, then added emphasis should be placed on the more recent levels of the risk premium than on a historical average. Otherwise, the average risk premium may not be a reasonable estimate of the risk premium expected to persist in the near future.

The remaining methodology used by the witnesses was the CAPM approach employed by witness Morin. The CAPM approach requires estimates of the company's beta, the risk-free rate, and the expected return on the market. Witness Morin used a beta of .75, Southern Company's beta, as a proxy for Gulf Power. (TR 1716) Witness Morin used the yield on long-term treasuries for the end of May 1990 of 8.7%. (TR 1716) Staff believes that Southern Company's beta of .75 overstates the beta that should be used for Gulf Power. As noted by witness Rothschild, Southern Company experiences nuclear exposure through the substantial nuclear exposure of its Georgia Power subsidiary. (TR 2729) Gulf Power has no nuclear exposure. Witness Rothschild observed a beta of .696 for his index comprised of Moody's electric utilities with no nuclear construction. (TR 2717) Using a beta that reflects the risk of utilities with nuclear exposure, causes the return on equity for Gulf Power to be overstated.

A more serious problem with witness Morin's CAPM analysis is the use of earned returns as a proxy for the market return expected by investors. The CAPM is strictly expectational in nature. All the variables used to estimate a company's required return should be based on estimates of the future. Although past values of all the variables may be used to provide a basis for the required estimates, anticipated changes from the past to the future should be incorporated into the variables included in the model.

Based on witness Morin's own analysis, the current required return on the market is different than that calculated using earned returns over an extended period. Witness Morin used the DCF methodology to calculate an expected return on the market of 13.7%. (TR 1718) This expected return contrasts markedly with the 16.11% return estimated by witness Morin using earned returns. (TR 1717) In staff's opinion, using a return of 16.11% overstates the return currently required by investors on the market and should not be used. Using the current market required return determined by witness Morin of 13.7% produces a return on equity for Gulf Power of 12.45%.

The same criticisms staff has of witness Morin's CAPM analyses apply to his Empirical CAPM analyses. In his Empirical CAPM analyses witness Morin adds a premium of the magnitude .25 * (Return to the Market - Risk Free Rate) to his previously derived CAPM results. (TR 1719) Witness Morin claims this adjustment is necessary because the traditional CAPM model produces a downward biased estimate of equity cost for companies with a beta less than 1.00. (TR 1718)

Basically, witness Morin's adjustment will produce the expected market return. If the expected return to the market is 13.7%, then witness Morin's Empirical CAPM equation produces a cost of equity estimate of 13.7% (Ke = 8.7% + .25 * (13.7% - 8.7%) + .75 * (13.7% - 8.7%)). Witness Morin's Empirical CAPM analyses ignores the risk-return relationship for companies that are less risky than the market as determined by a company's beta. Implicit in witness Morin's analyses is the assumption that investors require the market return for investing in a regulated utility. Staff disagrees with this implication. In general, electric utilities are less risky than the average company, and investors establish their return requirements accordingly.

Witness Morin criticizes the DCF methodology. Witness Morin states that the traditional DCF model is not equipped to deal with surges in market-to-book and price-earnings ratios, as has been experienced by utility stocks during 1989. The standard infinite growth DCF model assumes constancy of such ratios. (TR 1672) Staff notes, however, that with the exception of witness Morin's CAPM analyses that rely on earned returns, the DCF methodology is embedded throughout his analyses and results. Furthermore, witness Morin did not present any evidence that shows investors do not expect such "constancy" in the future. Finally, the use of a non-constant growth DCF model, such as the model advocated by witness Seery, addresses witness Morin's concerns.

Witness Morin mistakenly criticizes witness Seery's intermediate term growth estimate for the next four years. Witness Morin calculates an intermediate term growth rate of 3.00% using witness Seery's data. (TR 3254) Witness Morin's calculation of 3.00% is mathematically incorrect. The geometric rate of growth implicit in witness Seery's dividends for 1990 through 1993 is approximately 4.04%. This number is calculated by taking the third root of: (1 + (2.68 - 2.38)/2.38). The 2.38 and 2.68 are the dividends forecasted by Value Line for 1990 and 1993, respectively. Witness Morin took the fourth root of the above equation and thus incorrectly determined a lower growth rate. Multiplying the 1990 dividend by 1.03 each year for three years produces a 1993 dividend of 2.60. Value Line projects a 1993 dividend of 2.68, which is the number that is produced if one uses the geometric growth rate of 4.04%. Staff notes this is close to the IBES forecast of 4.14%. (TR 3254)

The IBES estimates are five year forecasts of earnings growth. DCF theory clearly states that it is expected future cash flows in the form of dividends which constitute investment value. (TR 1686) In witness Seery's analyses, he uses the actual dividends forecasted by Value Line for the period 1990 through 1993. He then uses the b * r approach to estimate the long-term sustainable growth rate that could be expected by investors after 1993. The conceptual premise behind this approach is that the future growth in dividends for existing equity can only occur if a portion of the overall return to the investors is reinvested into the firm instead of being distributed as dividends.

Witness Rothschild also uses the b * r approach. Witness Rothschild adjusted upwards his growth rate by five basis points to reflect the growth in earnings or dividends caused by new stock sales at market prices greater than book value. (TR 2713) Staff believes this is a reasonable adjustment and probably should be recognized when determining growth using the b * r approach.

For the purpose of determining the investors' required return, staff agrees with witness Morin's use of a DCF model that reflects the quarterly receipt of dividends. But, as stated by witness Seery,

> "... the use of models that accurately reflect the receipt and timing of cash flows provides a better estimate of the cost of equity. However, using the results derived from a quarterly DCF model without making a ratemaking rate of return adjustment is inconsistent. The ratemaking rate of return adjustment recognizes the time value of money associated with the Company's receipt of monthly revenues. It is inconsistent to selectively recognize the time value associated with the investors' quarterly receipt of dividends, through the use of a quarterly model, and then not recognize the time value associated with the Company's monthly receipt of revenues." (TR 2966)

To determine the utility's after-tax equity earnings the 13-month average equity balance is multiplied by the cost of equity. In witness Morin's example (Exh. 196, p.2) the average equity balance would simply be the sum of the book equity book value per share each month multiplied by the number of shares outstanding, divided by 12. So, carrying witness Morin's example one step further, multiplying the average book equity book value per share of $31.7027 (calculation) by the investor required return used in his example of 14.04% should produce earnings of approximately $4.19 (the amount of earnings required to produce the growth rate and stock price appreciation implicit in Morin's DCF example). BUT, multiplying the average book equity book value per share of $31.7027 by 14.04% actually will produce earnings of approximately $4.45 per share, an amount greater than necessary to meet investor return requirements.

Staff notes that if witness Morin had multiplied his monthly market required return of 1.1009% (equivalent to .011009) by 12 months he would have obtained a return of 13.21%. Applying 13.21% to the average book equity book value per share of $31.7027 will produce approximately $4.19 in earnings per share, the amount of earnings implicit in witness Morin's Quarterly DCF Model Assumptions. The 13.21% is the ratemaking rate of return alluded to in witness Seery's testimony.

In summary, staff believes the evidence presented supports a midpoint cost of equity for the purpose of setting rates of 11.75% to 12.75%. Staff believes witness Seery's recommendation of 12.25%, adjusted upwards by five basis points to reflect the growth in earnings caused by new stock sales, is well supported by the evidence and in staff's opinion represents the best estimate of the Company's cost of equity. Staff therefore recommends a cost of common equity of 12.3% for Gulf Power. (Prior to any adjustment, See Issue 38) To put this recommendation in perspective, at the time the revised testimony was filed the average yield on long-term treasuries was 8.74% and the yield on A-rated utility bonds was 9.92% for April 1990. (Exh. 381, Schedule 3). The average yield for June 1990 was 8.60% for long-term treasuries and 9.80% for A-rated utility bonds as reported by Moody's Bond Survey, July 16, 1990.

ISSUE 38: Should the newly authorized return on common equity be reduced if it is determined that Gulf Power Company has been mismanaged? (Vandiver)

RECOMMENDATION SUMMARY: Yes, staff recommends that the newly authorized return on common equity be reduced by fifty (50) basis points for a two year period due to mismanagement. Mismanagement is present through the acts of the senior vice president alone. Mismanagement is also present due to the lack of action concerning this individual, by Gulf Power's president, in light of information available at the time.

DISCUSSION

The record is clear that corrupt practices took place at Gulf Power Company from the early 1980s through 1988. The corrupt practices include but are not limited to theft of company property, use of company employees on company time to perform services for management personnel, utility executives accepting appliances without payment, and political contributions made by third parties and charged back to Gulf Power Company. These activities are discussed in greater detail below. The majority of the unethical/illegal activities involved Jacob Horton, the Senior Vice President of Gulf Power Company.

Given that the corruption in a variety of forms was present, the question becomes whether the management of the power company knew or should have known of the illegal and/or unethical conduct that was taking place. At this point it is incumbent upon the staff to note that there is no record evidence to indicate that Mr. Douglas McCrary, President of Gulf Power Company from May of 1983 through the present, knew that illegal or unethical conduct was taking place as it happened. Mr. McCrary testified under oath as to his lack of contemporaneous knowledge of Mr. Horton's activities, and apart from the information discussed below, no evidence of record disputes this testimony. (See R131-32)

Staff does believe that the president should have known of some of these activities and should have acted sooner and with sterner measures with regard to Mr. Horton's activities. This inaction constitutes mismanagement. As a totally independent ground, the activities of Mr. Horton and his subordinates as Senior Vice Present alone constitute mismanagement. This recommendation is premised upon the structure of Gulf Power management with four vice presidents reporting to the president. As one of those vice presidents, Mr. Horton's actions are those of Gulf Power management.

In terms of the president's actions or inaction, staff believes that there were many early warning signals which indicated that Mr. Horton was involved in illegal or unethical conduct. In December of 1983 Mr. McCrary received anonymous letters concerning employee misappropriation of goods. Mr. McCrary commissioned an independent investigation by security personnel from a sister company to avoid one peer investigating another. The result of this investigation was the "Baker Childers report", which was Exhibit 391 at the hearing. This report focused on warehouse thefts directed by Kyle Croft. Also contained in this report were allegations of company personnel performing personal services for Gulf Power executives, including Mr. Horton, on company time with company materials. When Mr. McCrary asked Mr. Horton about these allegations, Mr. Horton denied them, and no further action was taken. (R169) This incident did, however, raise Mr. McCrary's suspicions about Mr. Horton. (R168)

With regard to the principal allegations in the Baker-Childers report, Mr. McCrary fired Mr. Croft on a Sunday morning in late January 1984, based on the report. However, Mr. Horton intervened and persuaded Mr. McCrary to rescind the firing decision and allow Mr. Croft to resign. Unknown to Mr. McCrary at the time, Mr. Horton arranged for Mr. Croft's attorneys fees and health insurance to be paid and billed back to Gulf Power. The president learned of this payment in 1988. (R197) As part of Mr. Croft resigning from Gulf Power, Mr. Croft executed a promissory note for $15,986.62 to Gulf Power Company. This represented an estimate of the property Mr. Croft had stolen from Gulf Power. Concurrent with the execution of this note, Mr. Horton stated that Gulf Power would not enforce the note, and Mr. Horton executed a note payable to Mr. Croft for the same amount. (Ex. 396 at p. 55) This was done to protect Mr. Croft if Gulf Power decided to enforce the note. When the president learned of Mr. Horton's note in 1986 it also heightened the president's suspicion of Mr. Horton. (R199)

In June of 1984 it was learned that Gulf Power had delivered approximately $10,000 worth of appliances to Mr. Addison, former president of Gulf Power Company and now head of the Southern Company, the parent company of Gulf Power. Mr. Addison was not billed for these goods, and it was the intent of Gulf Power employees to give the appliances to Mr. Addison. (R183) The president learned of this scheme and discussed the matter with Mr. Addison. Mr. Addison was billed and then promptly paid for the appliances. (R184) The employees involved reported to Mr. Horton and this again raised suspicion concerning Mr. Horton. (R186) No further investigation of the appliance division was made. (R187)

In July of 1984 Mr. Horton instructed a Gulf Power employee to solicit a $1,000 political contribution from a local architect that worked with Gulf Power Company. The president learned of this several days later. (R223) He spoke to Mr. Horton and "reemphasized" that pressure would not be placed on vendors to make political contributions. (R223) Mr. McCrary conceded that he was very much suspicious about Mr. Horton by July of 1984. (R225) Unknown to the president at the time was the fact that Gulf Power in fact reimbursed the architect for the political contribution. (Ex. 396 at p. 21) In the fall of 1986, the president learned that Gulf Power had reimbursed Mr. Graves (the architect), and had Mr. Graves reimburse Gulf Power Company, and then had Mr. Horton reimburse Mr. Graves. (Id) Any suspicion created in 1984 by this situation must have been greatly increased by the 1986 transactions.

On October 31, 1989 Gulf Power Company entered quilty pleas to two felony counts in the United States District Court for the Northern District of Georgia, Atlanta Division. Gulf Power paid a $500,000 fine for these crimes. (Ex. 413) This negotiated plea agreement grew out of Gulf Power activities from 1981-1988. Over 120 counts were detailed in Exhibit 413. Basically Gulf Power management through Mr. Horton and his subordinates "systematically, repeatedly and willfully instructed its outside vendors, such as its advertising agencies, to submit false or inflated invoices to Gulf Power Company for payment by Gulf Power Company in order to reimburse those vendors for payments they had made to political candidates and others at the direction of Gulf Power Company." (Ex. 413 at p. 13) These illegal acts were not isolated cases and are factually indistinguishable from the Graves contribution which the president knew of 1984 and learned more about in 1986. At the hearing staff questioned Mr. McCrary concerning four illegal transactions in July of 1985. (R245-46) In each case Mr. Horton had to inform the various entities where to send funds, be certain the false vouchers were paid and then check with the payees to be certain the funds had been delivered. These activities consumed a lot of Mr. Horton's time. (R246) The president met with Mr. Horton in one-on-one meetings "every day almost" in addition to regularly scheduled staff meetings. (R219) The president said it was fair to characterize the meetings as "constant inter-reaction". (R219) The president testified he knew nothing of the illegal activities, but given the extent of the activities and suspicion already raised in conjunction with the "constant inter-reaction" of these two men, the president should have known of Mr. Horton's illegal activities. This is especially true in light of the fact that the president testified that he had been warned that Mr. Horton's method of operation was questionable and that "something was not exactly right" with Mr. Horton's behavior. (R231)

Staff believes that the explicit warnings the president received concerning Mr. Horton, coupled with the Baker Childers Report in early 1984, the Addison appliances in June of 1984, the Graves contribution in July of 1984, the 1986 Kyle Croft lawsuit revealing more information concerning Mr. Croft's resignation and the subsequent information in 1986 regarding the 1984 Graves contribution all indicate that the president should have been aware of Mr. Horton's activities. This is especially true in light of the close business relationship between the two men. An investigation of Mr. Horton's activities was clearly indicated by 1986.

In the Fall of 1988 the president saw the Appleyard ledgers. He knew at that time that violations of the law were involved. (R244) These accounts were handled by the organization reporting to Mr. Horton. Mr. Horton was informed that he was to be separated from the company on April 10, 1989.
(R4192) As of May 1, 1989, the company had not undertaken an investigation of Mr. Horton, despite the events described above. See Exhibit 382 at p. 16A. Staff believes that the lack of action regarding Mr. Horton by the president constitutes mismanagement because he should have been aware of Mr. Horton's activities or started an investigation into Mr. Horton's activities based on the events discussed above.

Not only did the president fail to initiate an investigation of Mr. Horton, but Mr. Horton received no written reprimand in the time Mr. McCrary was President of Gulf Power Company from 1983 until the time of Mr. Horton's death in April of 1989. (R4186-87) This lack of written reprimands is troubling when one considers the president's subsequent knowledge of Mr. Horton's promissory note, the Graves Contribution, and paying Mr. Croft's legal and insurance costs. In one case (the Graves situation) Mr. Horton lied to Mr. McCrary in 1984 and Mr. McCrary knew he lied in 1986 and in another case (paying the legal and insurance costs for Mr. Croft) Mr. Horton directly disobeyed the president's explicit instructions. (R197) Mr. Horton also received Productivity Improvement Program payments for his job performance in 1983, 1984, 1985, 1986, and 1988. (Ex. 547) He also saw his base salary rise each year from 1983-1988. Id.

Although staff believes the president's lack of action regarding Mr. Horton constitutes mismanagement, staff believes that given Mr. Horton's position, his actions alone constitute mismanagement irrespective of the president's inaction. Gulf Power has over 1600 employees. Mr. McCrary is the leader of these employees, and four executives reported directly to him, as well as the director of Public Relations. (See R192; Ex. 414) Thus all policy decisions and supervision of all Gulf Power personnel is vested in this management team. Staff does not use the term "management team" loosely. The president expressed it this way:

> I did that [consulted the vice-presidents on the decision to fire Mr. Croft] because we operate that company on a-- in a manner such that all very important decisions that we make, we try to do as a group, so that all vice presidents are satisfied that they have had their input and they agree with the decision.

(R193; See R217; 3050)

Given this management philosophy and practice, staff believes it totally appropriate to find Mr. Horton's actions as those of Gulf Power management. Mr. Horton was one of the five people that ran Gulf Power. In carrying out his duties as Senior Vice President, he committed illegal and unethical acts on behalf of the utility. As such Gulf Power Company was guilty of mismanagement.

In terms of the scope of the corruption taking place at Gulf Power Company, several company programs were initiated to deal with the problem. Among these programs were adoption of a company Code of Ethics in August of 1984 and the implementation of an amnesty program around the same time. The Code of Ethics was adopted in response to the "myriad of things that had been going on in the early 1980s." (R204) The president agreed that every large well run utility should have a Code of Ethics and he couldn't say why Gulf Power lacked a Code of Ethics prior to that time. (Id.) All existing and new employees were required to sign a compliance statement. To implement the Code, Gulf Power had a series of meetings to explain the Code and the reason for it. The president was unable to point to anything Gulf Power did to further implement the Code from August of 1984 through January 5, 1989. On January 5, 1989, the Audit Committee of the Gulf Power Board of Directors adopted a resolution to reiterate the Code of Ethics and ordered management to take certain actions to implement the Code. (R206) The president explained the action as follows:

> We thought it was in -- that what we should do is to reemphasize the Code of Ethics; to have an educational program; to have a program of ethics awareness, and to generally have employees focus on the Code of Ethics being a real and living document. (R206)

The Code of Ethics was adopted in 1984 to combat the embezzlement of Gulf Power property and by 1989 different sorts of ethical violations were apparent, indicating that some employees ignored the Code or failed to take it seriously. (R214-15) Staff believes the 1989 measures should have been in effect in 1984 and there was haphazard enforcement of the Code from 1984-1988.

Gulf Power's amnesty program was initiated in the summer of 1984. This program was implemented in response to numerous allegations against Gulf Power personnel in the Baker-Childers Report. (R128) An outside law firm administered the program in order to shield the identity of the participants from the company. (Ex. 396 at p. 40-41) The program was designed to allow company employees that had improperly obtained goods or services from the company to make restitution to the company and then be subject to no further action. (R128) Gulf Power had no way of knowing whether the amounts collected under the amnesty program were correct. (R136; 140) A total of $13,124.23 was collected pursuant to this program. Of this amount, $10,500 (80%) came from two individuals in leadership positions at Gulf Power Company. (R138; 201; See Ex. 414)

On January 1, 1988, one of the persons who reported directly to the president was involved in three automobile accidents while driving a company vehicle. He was charged with D.U.I. and a number of traffic violations at the scene of the third accident. Mr. Horton informed the president of the employee's arrest. The president believed it would be very damaging to Gulf Power if the incident were reported in the media and he made a conscious decision not to have the accident reported as required by company procedures. (Ex. 396 at p. 66) Mr. McCrary did require the individual to pay for all damages. Although this activity constituted a violation of the Code of Ethics, the individual involved received no written reprimand. (R180) He was orally reprimanded, although it is not clear by whom. (R181) Staff would make two points concerning this incident. First, it would appear that this incident supports the lack of commitment to enforcement of the Code of Ethics from 1984-1988. It also raises the issue of Gulf Power treating executives differently concerning ethical violations than other employees. This is buttressed by the lack of investigation of allegations concerning personal use of company materials involving an ex-president of the Southern Company. (R134) This is especially true when one considers that a lower-level employee was fired for stealing a gallon of gas and certain other unspecified violations. (R107; 128; 182)

Gulf Power also did business in 1983 with Scott Addison, the son of Ed Addison, the Chief Executive Officer of the Southern Company. Although this specific transaction does appear prudent in and of itself, staff does question the propriety of doing business with relatives of the parent company personnel. This is especially true when the transaction was not handled in the normal manner and Gulf Power conceded that absent the family connection, the person would probably not have received the same treatment. (See R3841-3844)

To summarize, staff believes the events described above support a finding of mismanagement on the part of Gulf Power Company. The finding of mismanagement is premised on the activities of Mr. Horton, the president's lack of knowledge of those activities despite the incidents discussed above, the lack of investigation of Mr. Horton, the lack of written reprimands to Mr. Horton, the circumstances relating to the readoption of the Code of Ethics, the uneven enforcement of same, the various executives accepting goods or services without payment and the other factors discussed above. These factual circumstances lead staff to agree with Ms. Bass, "that the corporate culture was such that employees believed these types of illegal activities were, at the least, condoned by top management." (R2994; See Ex. 391 at p. 10; 28; 33) This is particularly true when one considers that illegal activity continued for at least eight years.

If the Commission disagrees with staff's recommendation that mismanagement was present, the remainder of the recommendation on this issue is moot.

If the Commission believes that mismanagement existed at Gulf Power Company, the issue becomes what action the Commission should take. Gulf Power argues that the Commission lacks authority to lower the return on equity in absence of a demonstrable impact on rates or service from the mismanagement. Gulf Power Brief at 110; See Id. at 107-138) In United Telephone Co. of Florida v. Mann, 403 So.2d 962, 966 (Fla. 1981), the court stated that after the rate of return is calculated, "the commission can make further adjustments to account for such things as accretion, attrition, inflation and management efficiency." (Emphasis supplied) Staff believes this case, in conjunction with the fact that public utility regulation is an exercise of the police power (See Section 366.01, Florida Statutes) and other statutory provisions (See Sections 350.117, 366.041, 366.07, and 366.075, Florida Statutes) grant this Commission ample authority to take management efficiency into account in setting rates.

The statutory provisions cited above give the Commission authority to consider management efficiency in setting rates. In consideration of relative efficiency, the Commission should reward the more efficient and give less relief to those operating in a less efficient manner. As the court stated in Deltona Corp. v. Florida Public Service Commission, 220 So.2d 905, 907 (Fla. 1969):

> A statutory grant of power or right carries with it by implication everything necessary to carry out the power or right and make it effectual and complete.

Staff believes the proper method of dealing with mismanagement is through the return on equity. The New Hampshire Public Utilities Commission has acted in conformity with this principle:

> The method of addressing managerial inefficiency which is most soundly rooted in proper regulatory principles and is most appropriate to the instant situation is a reduction in the allowed return on common equity. Re: Public Service Commission of New Hampshire, 57 PUR4th 563, 594

The Commission should take similar action here. In the instant case there were various ongoing criminal conspiracies reaching to the highest levels of management. These events, widely reported in the media, have hurt the company's relationship with its customers, as was made clear from the testimony customers gave at the service hearings. It is axiomatic that the involvement of managerial personnel in criminal activities lessened the efficiency of management in providing electric service.

If the Commission determines that it lacks authority to lower the return on equity of Gulf Power Company or that no reduction is appropriate, the remainder of the recommendation on this issue is moot.

In terms of lowering the authorized return on equity due to management inefficiency, the Commission should be aware of two landmark U.S. Supreme Court cases, Bluefield Waterworks Improvement Co. v. Public Service Commission, 262 U.S. 679 (1923) and Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591 (1944). These cases stand for the proposition that utilities must be permitted the opportunity to earn a fair rate of return. In Bluefield, the Court stated:

> The return should be reasonably sufficient to assure confidence in the financial soundness of the utility and should be adequate, under efficient and economical management, to maintain and support its credit and enable it

> to raise the money necessary for the proper discharge of its public duties. (Emphasis Added)

262 U.S. at 693.

As to the amount of the reduction, this is a matter for the Commission's discretion. The Commission should not set the ROE below the lowest point established by the testimony, however. While staff believes that the Hope and Bluefield line of cases presume honest and efficient management and that arguably criminal activity takes the Commission out of these cases, staff recommends that the ROE be set no lower than the lowest point set forth in testimony, i.e. 11.75%.

Staff has recommended an ROE of 12.30%. Staff recommends that this figure be reduced by 50 basis points for a two year period. This reduction is meant as a message to management that the kind of conduct discussed above will not be tolerated for public utilities which operate in Florida. Staff has recommended that this reduction be in effect for only two years rather than indefinitely. This is to reflect staff's belief that Gulf Power has turned the corner on dealing with the unethical/illegal behavior which was endemic for at least eight years. At the same time a two year reduction in the ROE reflects staff's belief that the disregard for public service and ratepayers as discussed above should not be ignored.

(ISSUE38.JMB)

STIPULATED

ISSUE 39: Should the preferred stock balance appearing in the capital structure be net of discounts, premiums, and issuance expenses? (YECCO)

RECOMMENDATION: Yes. The preferred stock balance should be net of discounts, premiums and issuance expenses.

POSITION OF PARTIES

GULF: The preferred stock balance appearing in the capital structure should be net of discounts, premiums and issuance expenses.

OFFICE OF PUBLIC COUNSEL: The preferred stock balance appearing in the capital structure should be net of discounts, premiums and issuance expenses.

STAFF ANALYSIS: All parties agree that the preferred stock balance appearing in the capital structure should be net of discounts, premiums and issuance expenses. The net effect on the capital structure will be to reduce the preferred stock balance by $948,000 and to increase the common equity balance by $948,000.

ISSUE 40: Should Gulf Power's non-utility investment be removed directly from equity when reconciling the capital structure to rate base? (YECCO)

RECOMMENDATION: Yes. Gulf Power's non-utility investment should be removed directly from equity when reconciling the capital structure to rate base.

POSITION OF PARTIES

GULF: No. Gulf's non-utility activities have no effect on the Company's cost of capital, and to remove these investments directly from equity would unjustly penalize the Company's stockholders. Recognizing that some of the items in the capital structure, such as customer deposits, are not related to non-utility investments from the capital structure using long-term debt, preferred stock, and common equity sources of capital as a reasonable proxy for the cost of capital.

OFFICE OF PUBLIC COUNSEL: Yes. The Company has removed part of this investment from debt. Reduce equity and increase long-term debt by $7,282,000.

STAFF ANALYSIS: The Company's position, supported by witnesses Scarbrough and Morin, is that Gulf's non-utility activities have no effect on the Company's cost of capital, and to remove the investment directly from equity would unjustly penalize the Company's stockholders. Through witness Morin's testimony the Company attempts to shift the burden of proof on staff to demonstrate that unregulated investments affect Gulf's cost of capital. Witness Morin states, "there has been no evidence presented suggesting that the small investment Gulf has in non-utility operations has impacted the cost of capital calculation of any witness". (TR 3258) Witness Morin also states that Gulf Power's diversified activities into both utility and non-utility operations reduces the risk to those investors who are not diversified on their own. (TR 3259) Witness Morin implies that staff witness Seery ignores the potential benefits of diversification to the investor. Witness Scarbrough simply refers to witness Morin's testimony in his discussion of this issue.

Witness Seery testifies that non-utility property and non-regulated subsidiaries be removed from the capital structure directly from equity unless the Company can show, through competent evidence, that to do otherwise would result in a more equitable determination of the cost of capital for regulatory purposes. (TR 2966A) Witness Seery offers two reasons for his recommended treatment of non-utility investments. First, the cost of capital allowed for ratemaking purposes should be the cost of capital associated with the provision of utility service. (TR 2966B) There are very few investments that a utility can make that are of equal or lower risk. Non-regulated investments will almost certainly increase a regulated utility's cost of capital. (TR 2966B) Thus, the effects of the unregulated investment on the regulated capital structure should be removed. Second, there are the signals and incentives associated with the Commission's policies. (TR 2966B) If a utility can finance non-utility property at the utility's cost of capital, it will have an economic incentive to do so. When this occurs, ratepayers subsidize through capital costs investments not necessary for the provision of utility service. (TR 2966C)

Staff agrees with witness Seery's position that non-utility investments should be removed directly from equity. To the extent the Company's non-utility investments are riskier than its utility investment, the Company's overall cost of capital will increase. By removing the non-utility investment directly from equity, staff recognizes that riskier investments have higher required returns and thus a higher cost of capital. (TR 2966B) In addition, removing nonregulated investments from equity helps protect the ratepayer from financial cross-subsidies associated with the capitalization of the nonregulated investment.

With respect to witness Morin's diversification argument, basic financial theory indicates that to intelligent investors, diversifiable risk is meaningless. Investors will diversify their portfolio to eliminate that particular type of risk. The only type of risk for which investors will demand compensation is nondiversifiable risk. The larger a security's non-diversifiable risk, the larger the required return. Nondiversifiable risk is measured by a firm's beta. Since there are very few investments that have lower betas than a regulated utility most non-utility investments will increase the nondiversifiable risk of a regulated utility. Witness Morin chose to ignore this basic tenet of financial theory in his discussion of risk reduction.

In summary, staff recommends that Gulf Power's non-utility investments be removed directly from equity. Removing non-utility investments directly from equity recognizes their higher risks, prevents cost of capital cross-subsidies, and sends a clear signal to utilities that ratepayers will not subsidize non-utility related costs.

ISSUE 41: Should Gulf Power's temporary cash investments be removed directly from equity when reconciling the capital structure to rate base? (YECCO)

RECOMMENDATION: Yes. Gulf Power's temporary cash investments should be removed directly from equity.

POSITION OF PARTIES

GULF: No. These funds are essentially all of Gulf's available working funds, and are required and necessary for the provision of electric service.

OFFICE OF PUBLIC COUNSEL: Yes, to the extent that temporary cash investments are not necessary for the provision of utility service, Gulf Power's temporary cash investments should be removed directly from equity.

STAFF ANALYSIS: In Issue 21, staff recommended that the Commission exclude the Company's temporary cash investments from working capital. In staff's opinion the Company did not show that its temporary cash investments are necessary for the provision of utility service. The Company's position in Issue 21, was that the temporary cash investments are necessary to provide utility service and should therefore be included in working capital. If in Issue 21 the Commission agrees with the Company then Issue 41 becomes moot.

Witness Seery testified the appropriate regulatory treatment of temporary cash investments should depend on their prudency. (TR 2966C) If the company can demonstrate, through competent evidence, that their temporary cash investments are necessary for the provision of utility service they should remain in rate base and earn at the utility's overall rate of return. Any earnings generated by these funds should then be used to offset revenue requirements. (TR 2966C) However, if the utility fails to demonstrate the prudency of their temporary cash investments they should be removed directly from equity when reconciling the capital structure to rate base. As stated by witness Seery:

> "Such treatment removes the capital structure implications of excessive cash or temporary cash investments. In a competitive environment the cost of poorly managed cash resources cannot be passed through to customers, instead shareholders bear the cost. Similar treatment by the Commission would mirror the competitive environment and send appropriate signals to utility owners and managers regarding cash balances and working capital allowances." (TR 2966D)

The Company's position is that if in Issue 21 the Commission finds in favor with staff then the temporary cash investments should be removed pro rata from the capital structure. The pro rata removal of temporary cash investments would be consistent with the Commission's decision in the Company's last rate case.

Staff agrees with witness Seery's proposed treatment. If in Issue 21 the Commission excludes the Company's temporary cash investments from rate base, Staff recommends that the temporary cash investments be removed directly from equity when reconciling the capital structure to rate base.

DOCKET NO. 881345-EI
(GULFREC.JEB) July 27, 1990

<u>ISSUE 42:</u> What is the appropriate balance of accumulated deferred investment tax credits (ITC)? (BRAND)

<u>RECOMMENDATION:</u> The appropriate 13-month average balance of accumulated deferred ITC's is $42,275,000 at a weighted cost and $858,000 at zero cost, before adjustments are made to reconcile capital structure to rate base.

<u>POSITION OF PARTIES</u>

<u>GULF:</u> The appropriate balance is $41,474,000 ($48,926,000 System).

<u>OFFICE OF PUBLIC COUNSEL:</u> This is a fallout number which will be provided later with the filing of the schedules.

<u>INDUSTRIAL INTERVENORS:</u> No position.

<u>STAFF ANALYSIS:</u> Gulf's 13-month average balance of accumulated deferred ITC's for 1990 totalled $48,926,000 on a total Company basis, as shown on MFR B-23. This consists of $48,068,000 at weighted cost and $858,000 at zero cost, on a total company basis. MFR D-1 shows a specific adjustment made by Gulf removing UPS-related ITC's of $5,793,000. Late-Filed Exhibit No. 572 (TR 769) shows ITC's totalling $6,821, related to the rate base adjustments proposed by Staff. Staff would ordinarily recommend that specific adjustments be made for those amounts identified, in order to satisfy the normalization requirements of the Internal Revenue Code. However, such adjustments are not recommended in this case because the difference between the specific identification of deferred taxes and the prorata adjustment is immaterial in its effect on the capital structure, and because there is insufficient basis in the record to support these adjustments.

Staff recommends that the appropriate 13-month average balance of accumulated deferred ITC's is $42,275,000 ($48,068,000 - $5,793,000) at a weighted cost and $858,000 at zero cost, before any adjustments are made to reconcile capital structure to rate base.

ISSUE 43: What is the appropriate balance of accumulated deferred income taxes? (BRAND)

RECOMMENDATION: The appropriate 13-month average balance of accumulated deferred income taxes is $189,038,000, before any adjustments to reconcile capital structure to rate base.

POSITION OF PARTIES

GULF: The appropriate balance is $182,959,000 ($203,823,000 System).

OFFICE OF PUBLIC COUNSEL: This is a fallout number which will be provided later with the filing of the schedules.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: Gulf's 13-month average balance of accumulated deferred income taxes for 1990 totalled $203,823,000 on a total Company basis, as shown on MFR B-24. MFR D-1 shows a specific adjustment made by Gulf removing UPS-related deferred taxes of $14,785,000. Late-Filed Exhibit No. 572 (TR 769) contains deferred taxes totalling $315,913, related to the rate base adjustments proposed by Staff. Staff would ordinarily recommend that specific adjustments be made for those amounts identified, in order to satisfy the normalization requirements of the Internal Revenue Code. However, such adjustments are not recommended in this case because the difference between the specific identification of deferred taxes and a prorata adjustment is immaterial in its effect on the capital structure, and because there is insufficient basis in the record to support these adjustments.

Staff recommends that the appropriate 13-month average balance of accumulated deferred income taxes is $189,038,000 ($203,823,000 - $14,785,000), before any adjustments to reconcile capital structure to rate base.

DOCKET NO. 891345-EI
(GULF.JY) July 27, 1990

ISSUE 44: What is the appropriate weighted cost of capital including the proper components, amounts and cost rates associated with the capital structure for the projected test year ending December 31, 1990? (YECCO)

RECOMMENDATION: The appropriate weighted average cost of capital, including the 50 basis point reduction recommended in Issue 38, is 7.89%.

POSITION OF PARTIES

GULF: The weighted average cost of capital as calculated at the time the Company filed its position for rate relief was 8.34%. Since that time, based on current as of May 1990, Gulf's cost of capital witness has adjusted his recommended return on equity from 13.00 to 13.50%. Due to this modification, the weighted average cost of capital should also increase.

OFFICE OF PUBLIC COUNSEL: The appropriate weighted average cost of capital is 7.24%.

STAFF ANALYSIS: Schedule 4 details each parties position with respect to the appropriate components, amounts and cost rates. Attachment 1 is staff's reconciliation. Staff specific adjustments were made to common equity to reflect the removal of nonutility assets (Issue 40, Adjustment -$14,880) and temporary cash investments (Issue 41, Adjustment -$6,399). As stipulated in Issue 39 an adjustment was made to reflect the effective cost of preferred stock by recognizing the issuance expenses, discounts and premiums in the preferred stock balance as opposed to the common equity balance (Adjustment to preferred stock -$948 and to common equity +$948). Staff prorated over all sources of capital the remaining adjustments to rate base. By making the remaining adjustments on a pro rata basis, staff removes the capital cost associated with the disallowed assets at the company's overall cost of capital.

Staff's recommended cost of capital includes the 50 basis point reduction (Issue 38) to the return on equity recommended in Issue 37. Staff's recommended cost of capital excluding the 50 basis point reduction to the equity return is 8.05%.

Gulf Power Company
13-Month Average Capital Structure
Test Year Ending 12/31/90

STAFF POSITION	LONG TERM DEBT	LONG TERM NOTE	SHORT TERM DEBT	PREFERRED STOCK	COMMON EQUITY	CUSTOMER DEPOSITS	DEFERRED TAXES	ITC's Zero Cost	ITC's Wtd. Cost	TOTAL
Company Per Book	439,734	42,089	4,432	67,432	367,404	15,775	203,823	858	48,068	1,189,615
Company Adjustments (Specific)	(98,837)	(42,089)		(10,278)	(63,994)		(14,785)		(5,793)	(235,776)
Subtotal	340,897	0	4,432	57,154	303,410	15,775	189,038	858	42,275	953,839
Staff Adjustments (Specific)	7,282	0	0	169	(14,246)	0	0	0	0	(6,795)
Subtotal	348,179	0	4,432	57,323	289,164	15,775	189,038	858	42,275	947,044
Prorata Adjustments	(11,453)	0	(146)	(1,886)	(9,512)	(519)	(6,218)	(28)	(1,391)	(31,152)
TOTAL	336,726	0	4,286	55,437	279,652	15,256	182,820	830	40,884	915,892
Ratio	36.76%	0.00%	0.47%	6.05%	30.53%	1.67%	19.96%	0.09%	4.46%	100.00%
Cost Rate	8.72%	0.00%	8.00%	7.75%	12.30%	7.65%	0.00%	0.00%	10.13%	
Weighted Cost	3.21%	0.00%	0.04%	0.47%	3.76%	0.13%	0.00%	0.00%	0.45%	8.05%
50 basis pt reduction to equity	8.72%	0.00%	8.00%	7.75%	11.80%	7.65%	0.00%	0.00%	9.92%	
Weighted Cost With Reduction	3.21%	0.00%	0.04%	0.47%	3.60%	0.13%	0.00%	0.00%	0.44%	7.89%

Calculation of JDIC Rate

Capital Components	Adjusted Amount	Ratio	Cost Rate	Wtd. Cost
Common Equity	279,652	41.63%	12.30%	5.12%
Preferred Stock	55,437	8.25%	7.75%	0.64%
Long-Term Debt	336,726	50.12%	8.72%	4.37%
Total	671,816	100.00%		10.13%

Calculation of JDIC Rate with 50 basis pt reduction on the equity cost rate.

Capital Components	Adjusted Amount	Ratio	Cost Rate	Wtd. Cost
Common Equity	279,652	41.63%	11.80%	4.91%
Preferred Stock	55,437	3.25%	7.75%	0.64%
Long-Term Debt	336,726	50.12%	8.72%	4.37%
Total	671,816	100.00%		9.92%

ISSUE 45: Should an adjustment be made to negate the effect of the Company's corporate goal to increase its equity ratio? (YECCO)

RECOMMENDATION: No. Gulf Power's common equity corporate goal to maintain a strong "A" bond rating is reasonable.

POSITION OF PARTIES

GULF: No. The common equity corporate goal is a long-term goal which reflects a desire to maintain a strong "A" bond rating, which is in the long-term best interest of the Company and its ratepayers as well as the stockholders.

OFFICE OF PUBLIC COUNSEL: Yes. Since equity is the highest cost of capital and is further increased by taxes, any increase in this source of capital should be justified on a cost benefit basis.

STAFF ANALYSIS: Gulf Power has a long-term capital structure goal to attain a common equity ratio of 40 to 45 percent. This common equity target reflects Gulf Power's desire to maintain a strong "A" bond rating. (TR 3793) Standard & Poor's (S&P), a major bond rating agency, has developed financial standards for rating investor owned electric utility bonds. (TR 3794) Among the standards developed by S&P is a debt leverage ratio. S&P defines debt leverage as total debt divided by total capital (debt ratio). S&P's debt leverage standard for "A" rated electric utilities is a debt ratio of 44 to 54 percent. Currently, Gulf Power's debt ratio is 48.9 percent, well within the standards set by S&P for an "A" rated electric utility. Gulf Power's equity ratio (as a percentage of investor sources of capital) is 42.9 percent.

The significance of a bond rating is that it reflects the rating agency's assessment of credit risk. The credit risk of a security is a measure of the likelihood that the issuer of the security, the borrower, will be unable to pay the interest or principal of the security when due. Credit risk is thus a measure of the creditworthiness of the issuer of the security. (TR 3793) Interest rates are higher for securities with greater credit risk, since investors have to be compensated for the additional risk. The highest grade bonds (or the bonds with the lowest credit risk) are designated by a "AAA" rating. Bonds rated AAA, AA, A or BBB are considered investment grade. Many institutional investors are restricted from purchasing bonds rated lower than investment grade.

Witness Scarbrough testified that an "A" bond rating is the lowest rating that permits Gulf Power ready access to financial markets at desirable terms and conditions. (TR 3795) Witness Scarbrough noted that when credit market conditions tighten, "BBB" rated companies often have difficulty selling their securities as investors attempt to upgrade their holdings. (TR 3794) Under a tight credit market scenario, investors prefer low credit-risk instruments because they perceive higher credit-risk borrowers as vulnerable. Witness Scarbrough further testified that an "A" bond rating provides a buffer that allows a utility to finance ongoing capital requirements even if unexpected adverse developments result in a downgrade. (TR 3795)

No evidence was presented that contradicted Witness Scarbrough's testimony or demonstrated that the Company's capital structure goal is unreasonable. Gulf Power's equity position is weaker than many other electric utilities in the southeast. Witness Scarbrough compared Gulf Power to the other 26 electric utilities comprising the Southeastern Electric Exchange. Witness Scarbrough testified that of the Southeastern Electric Exchange utilities, only four were more highly levered than Gulf Power. (TR 3819)

Staff believes that the Company's desire to maintain a strong "A" bond rating is reasonable and in the long-term best interest of ratepayers. Thus attaining a capital structure which helps the Company maintain an "A" rating is also reasonable. Staff recommends that no adjustment be made to negate the effect of the Company's corporate goal to increase its equity ratio in order to maintain a strong "A" bond rating.

Docket No. 891345-EI
July 26, 1990
1706E

ISSUE 46: The company has proposed a net operating income of $60,910,000 ($78,848,000 System) for 1990. What is the appropriate net operating income for 1990? (MERTA)

RECOMMENDATION: The appropriate jurisdictional amount is $63,290,000.

POSITION OF PARTIES

GULF: The appropriate amounts are $60,910,000 ($78,848,000 System).

OPC: $70,394,000.

STAFF ANALYSIS: The parties' positions are shown on the following chart:

Jurisdictional Net Operating Income
(000's

	Gulf	Staff	Public Counsel
Operating Revenues	$255,580	$255,688	$258,089
Operating Expenses			
O&M	113,382	110,213	99,297
Deprec. & Amort.	47,701	47,561	44,957
Taxes - Other	20,822	20,793	20,501
Current Income Taxes	13,185	14,198	22,596
Def. Income Taxes (net)	1,621	1,674	2,187
ITC (net)	(2,041)	(2,041)	(1,843)
Total Operating Exp.	194,670	192,398	187,695
Net Operating Income	$60,910	$63,290	$70,394

*Operating revenues and expenses are net of fuel and conservation.

Docket No. 891345-EI
July 26, 1990
1706E

ISSUE 47: Should revenues be imputed to Gulf for the benefit derived by the appliance division from the use of Gulf's logo and name? (MERTA)

RECOMMENDATION: No. Revenues should not be imputed to Gulf for use of Gulf's logo and name by the appliance division.

GULF: No. (Bowers)

OPC: Yes. Any value attributable to the operation of the electric sales division should be recognized and an appropriate allowance should be credited to the Company above the line. No amount is proposed.

STAFF ANALYSIS: The appliance division uses the Gulf Power name and logo. It does not pay a royalty fee or in any way reimburse Gulf for his privilege.

Gulf Witness Bowers testified that based on a survey conducted by the company, the appliance division does not possess significant name recognition in the market as only about 20% of the 600 people surveyed knew that Gulf Power was in the appliance sales business. He concluded that the use of the company's name and logo did not give the appliance division a competitive advantage over other appliance dealerships in the area. (TR 904) Mr. Bowers is currently charged with determining whether Gulf should continue in the appliance business since the operation has incurred significant losses over the last few years. (TR 908-909) Gulf Witness Scarbrough testified that the appliance division, in fact, wishes to change its name. (TR 464)

Public Counsel believes it highly unlikely that the appliance division does not benefit from the use of Gulf's name and logo since appliance sales advertisements are enclosed as bill stuffers along with the electric bills. (OPC Brief, p. 61) Public Counsel recommended a nominal charge for the use of Gulf's name and logo, but did not propose a method of calculating the charge.

In staff's opinion, the record does not support imputing revenues to Gulf or charging a fee for the use of its logo and name. Therefore, staff recommends that no revenues be imputed to Gulf.

There is precedent for charging a royalty fee based on Order No. 18939, Docket No. 870285-TI, United Telephone Company of Florida. Here, United Telephone Long Distance (UTLD) was ordered to compensate United Telephone Company of Florida for use of the United name, logo and reputation. The actual fee was 2.8% of the difference between net revenues (gross revenues minus uncollectibles) and originating and terminating access charges. The fee was not to exceed, on an after tax basis, 17.5% of UTLD's net operating income to be computed without the fee.

ISSUE 48: Should revenues be imputed at applicable standby rates for 1990 for the PXT customer who experienced an outage of his generation capacity and took backup power from Gulf but was not billed on the standby power rate? (MEETER)

RECOMMENDATION: Revenues of $16,325 should be imputed for 1990 on the basis of the customer having a standby service capacity of 7959 KW. The company testified that the customer experienced a forced outage of his generator and took standby service for backup power of 7959 KW.

POSITION OF PARTIES

GULF: Yes, revenues should be determined for this customer as Gulf filed in the revised "No Migration" Study. (Exhibit 231) In that study, the customer's contracted standby service KW's were used for the test year, 1990 (0 KW standby in January, 3000 KW in February, and 7,500 KW for each of the remaining ten months of the 1990 forecast period). These demands are the actual standby service contract KW's of this customer, and Gulf expects that the customer will limit its standby to no more than 7500 KW in the reasonably foreseeable future.

OPC: Yes.

STAFF ANALYSIS: Company Witness Haskins stated that the customer in question experienced a forced outage during September 2 and 3 of 1989 (TR 1965) and that the customer took standby power of 7959 KW during that outage (TR 1966). Witness Kisla, who testified on behalf of the customer stated that Stone has taken the generator off line for maintenance to repair the boiler during the period in question. (Tr, 2782)

According to the definition of standby power in Order No. 17159 at pages 3 and 4 and on the Company's Standby Service tariff, Sheet Number 6.32, the energy or capacity supplied by the company during this time period to replace energy or capacity ordinarily generated by the customer's own generating equipment was standby service in the form of backup or maintenance service. Furthermore, Order No. 17159 at page 21 provides that the utility will be responsible for analyzing the metered data to determine what amount of the customer's service was supplemental and what amount was standby service, either backup or maintenance. The fact that the customer had subscribed for zero standby service capacity and failed to report the outage is immaterial to the determination that the 7959 KW taken during the time period was standby service.

Furthermore, staff believes the issue is moot because Gulf stipulated to staff's position on Issue 113, identifying the additional standby taken and 7059 KW. If Gulf had properly billed the customer for standby service for September, 1989, as required by Order No. 17159, the test year revenue and billing determinants for standby service for the customer would be based on the 7959 KW of standby service that the company calculated this customer used during September, 1989. Gulf has based its revenues and billing determinants on the customer's contracted standby service KWs for the test year. Staff believes the use of the 7959 KW of standby power on which the customer should appropriately be billed during 1990 is more appropriate than the actual contracted level of KW because the previously contracted levels of zero and 3000 KW have been shown to be unrealistically low. Furthermore, it was the company's decision or mistake not to have billed the customer for the 7959 KW of standby service. The estimated effect of basing the test year standby service billing determinants on 7959 KW instead of the customer's contracted standby service KW for the test year in the No-Migration study is $16,325 (Exhibit 513, page 5).

If the Commission decides that was not standby power, the customer does not qualify for the PXT rate due to his annual load factor and the appropriate revenues and cost to be used in the rate case for this customer must be based on the LPT rate, as originally filed by the company. Unfortunately, there is no cost of service study with this customer in LPT which incorporates the corrections made by the company and supported by staff to the service class nor any of the revisions requested by staff in the record. The company should also have billed the customer pursuant to the PXT minimum bill provision.

ISSUE 49: The company has projected total operating revenues for 1990 of $255,580,000 ($262,013,000 System). Is this appropriate? (ROMIG)

RECOMMENDATION: The appropriate amount of revenues for 1990 is $255,687,463 ($262,120,463 System).

POSITION OF PARTIES

GULF: Yes.

OPC: The company's sales projections should be increased by $2,493,000 to reflect a more accurate sales projection.

STAFF ANALYSIS: This issue is basically a fallout of other NOI and rate issues discussed under other sections of this recommendation. The company's projected revenues should be increased by $107,463 as described below:

1. Sod Farm: Staff has recommended, under Issue 6, that the percent of acreage devoted to the sod farm or 10% be excluded from rate base. Therefore, it would be appropriate to remove from other operating revenues $3,450 in rental revenues received from the sod farm operation.

2. Non-Utility Operations: The company has several non-utility operations; sod farm, visision design and the appliance sales and service. In the past and currently, Gulf has allocated cost of the metered electric consumption to these operations at the actual cost of generation.

   In staff's opinion, these non-utility operations are being subsidized in part by cost of electricity that it would otherwise pay if its consumption were billed out at the appropriate tariff rate. Gulf filed Late-Filed Exhibit No. 564 which provided the KWH consumption, amount allocated and the dollar amount if billed under the tariff rate. Based on this exhibit, it would be appropriate to increase revenues by $34,913.

3. Additional Standby Revenues: Staff has recommended in Issue 48 that the utility's revenues be increased by the amount which would have been received if the customer had been properly billed for standby service taken in 1989. ($16,000)

4. Adjustment to OS-I and OS-II Classes: The company failed to use the revenues shown on their most recently revised E-16 for these classes (Exhibit 480). These revisions were offered by the company and were not in response to any staff requested recalculation. ($66,000)

5. Adjustment of OS-III and OS-IV Revenues: The company failed to correctly transfer the revenues from E-16d to E-16a. This results in the utility overstating its current revenues. (-$6,000)

ISSUE 50: Has Gulf budgeted a reasonable level for salaries and employee benefits? (REVELL/SALEK)

RECOMMENDATION: Yes, Gulf's budget level for salaries and fringe benefits is reasonable.

POSITION OF PARTIES

GULF: Yes. (Scarbrough, Jackson)

OPC: Employee benefits should be reduced by $1,405,445.

STAFF ANALYSIS: Although this issue addresses Gulf's level of salaries and fringe benefits, no party to this proceeding has any specific concern over base salary levels at Gulf. The company has access to a large number of salary benefits surveys which show the company is not out of line with its level of salaries [T-332] compared to other companies even though Gulf did exceed the 1990 benchmark for salaries [T-330].

The necessity of certain fringe benefits is the highest concern on the part of Public Counsel, not base salaries. The three areas of concern are supplemental pension benefits and post retirement life and medical benefits.

Supplemental benefits are benefits offered to certain high paid employees who would otherwise have their benefits capped due to IRS limitations. The purpose of the plan is to avoid discrimination due to these arbitrary limits. The supplemental benefits plan for these employees includes pensions and the matching of employee savings which is addressed in Issue 91. Both of these have limitations set by the IRS for highly paid employees.

Staff believes that the supplemental benefits plan should be considered as part of the total compensation package for the employees. With lack of evidence to the contrary, the compensation plans for the employees appear to be reasonable. It is also reasonable that the high paid employees of Gulf should not be discriminated against due to tax considerations. Gulf's top employees, even with this plan, are still below the 75th percentile which is the level Gulf wishes to compensate its employees [T-3967]. A survey conducted by the Edison Electric Institute, "Executive Compensation for 1990", indicated that 82% of the 103 surveyed companies had a comparable supplemental benefits plan [T-3973]. For these reasons, staff believes there should be no disallowance of expenses related to the supplemental benefits package at the company.

Gulf pays medical and life insurance benefits to its retired employees. (TR 3795-3796) In 1987, Gulf changed from the "pay-as-you-go" basis (cash basis) of accounting to accrual accounting for other postretirement benefits. (TR 3796) OPC witness Schultz testified that "as a result of a proposed, but not yet adopted accounting standard, the Company began accruing an expense for the future costs of other post retirement benefits." (TR 2465) He believes that using the accrual accounting would allow the utility to collect funds before the payments are due and the "pay-as-you-go" basis should be considered when setting rates. (TR 2465-2466) Witness Schultz further recommends that no postretirement benefits should be allowed if Gulf is not funding the benefits. (TR 2466)

Utility witness Scarbrough explains that Gulf began revising its accounting treatment of other postretirement benefits after implementing SFAS 87 (Employees' Accounting for Pensions). The company determined that it is appropriate to use an accrual basis to account for the benefits. (TR 3796) In support of accrual accounting for other post retirement benefits, Witness Scarbrough states that accrual accounting recognizes the expense in the proper period and matches the recovery of the costs from the the customers that receive the benefit of the employees' services. (TR 3797)

With regard to the proposed accounting standard referenced by Witness Schultz, Witness Scarbrough states that the Financial Accounting Standards Board has issued an exposure draft requiring accrual accounting. The final version is expected to be issued by the end of the this year. (TR 3798) Although the exposure draft does require accrual accounting, Gulf did not use the actuarial method required by the exposure draft. Gulf uses an aggregate cost method and the exposure draft requires a benefit method. Gulf filed Late-filed Exhibit 625 that calculated the amount that would be accrued under the terms of the exposure draft.

As to Witness Schultz' concerns about the other postretirement benefits being funded, the company did fund for the benefits in 1988 and 1989. (TR 3827) During these years Gulf received a tax advantage for the funding as the result of a letter ruling requested by Gulf. The Internal Revenue Service later revoked the tax advantage of funding the amount. (TR 3827) Witness Scarbrough points out that the amounts that Witness Schultz wishes to exclude because they are not funded are actually payments made for the postretirement benefits.

The expense for medical and life insurance benefits would be $518,000 and $110,000, respectively, if the the cash basis of accounting were used. (Exhibit 426) Under the criteria of the exposure draft, the accruals for medical and life insurance benefits would be $1,194,000 and $1,008,000, respectively. (Late-filed Exhibit 625) Under the accrual method as filed by Gulf, the medical and life insurance expense is estimated to be $993,000 and $917,000, respectively. Gulf updated its estimate of the expense associated with the benefits with a letter submitted by the actuary. The updated amounts would be $922,000 and $917,000 for medical and life insurance benefits, respectively. (Exhibit 422, p. 2) This same letter also updated the pension expense. (See Issue 75) In the pension issue, Staff recommends that the updates included in this letter not be recognized. To be consistent, Staff recommends that the letter be unrecognized for purposes of this issue also.

Staff recommends that Gulf's medical and life insurance benefits be recognized using the accrual basis of accounting. Staff believes that accrual accounting does more accurately charge the cost of the employee providing a service to the customer who is receiving the service. At this time, Staff believes that Gulf should not be required to follow the exposure draft of accounting for postretirement benefits that has been released. It will not be implemented until some date in the future. Staff believes that no adjustments should be made to Gulf's other postretirement benefits.

ISSUE 51: Is Gulf Power's projected $510,524 ($510,852 System) bad debt expense for 1990 appropriate? (ROMIG)

RECOMMENDATION: Yes. No adjustment is recommended for bad debt expense.

POSITION OF PARTIES

GULF: Yes. Gulf's approved accrual method of calculating Bad Debt expense is appropriate.

OPC: No adjustment was proposed by Public Counsel.

STAFF ANALYSIS: Gulf was allowed $523,000 in bad debt expense in its last rate case, page 22 of Order No. 14030. In 1989, the company changed its method in determining the accruals for bad debt expense; the 1990 projected accrual is $510,852.

Public Counsel Witness Schultz stated, "The company's recent change in determining the uncollectible expense of $510,852 in my opinion, produces a representative amount for 1990. Therefore, I am not recommending that the 1990 budget for uncollectibles be adjusted." T-2463

Staff is in agreement with the other parties and therefore recommends no adjustment to bad debt expense.

ISSUE 52: Should fuel revenues and related expenses, recoverable through the fuel adjustment clause, be removed from NOI and if so, what amount? (ROMIG)

RECOMMENDATION: No additional adjustments should be made to the amounts removed by Gulf for fuel revenues and related expenses.

POSITION OF PARTIES

GULF: Yes. The fuel revenues are $198,128,000 and fuel related expenses are $198,132,000.

OPC: Yes. No amount available.

STAFF ANALYSIS: Gulf adjusted its 1990 revenues and expenses to remove fuel revenues and expenses which are recoverable through the fuel adjustment clause. This adjustment is consistent with Commission policy. Public Counsel did not take issue with the company's adjustment.

Staff is in agreement with Gulf's adjustment and therefore recommends it be accepted.

ISSUE 53: Should conservation revenues and related expenses, recoverable through the conservation cost recovery clause, be removed from NOI and if so, what amount? (ROMIG)

RECOMMENDATION: No additional adjustments should be made to the amounts removed by Gulf for conservation revenues and related expenses.

POSITION OF PARTIES

GULF: Yes. The conservation revenues are $1,878,000 and the conservation related expenses are $1,877,000.

OPC: Yes. No amount available.

STAFF ANALYSIS: Gulf adjusted its 1990 revenues and expenses to remove conservation revenues and expenses which are recoverable through the conservation cost recovery clause. This adjustment is consistent with Commission policy. Public Counsel did not take issue with the company's adjustment.

Staff is in agreement with Gulf's adjustment and therefore recommends it be accepted.

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ISSUE 54: Should the 1990 projected test year be adjusted for any out-of-period non-recurring, non-utility items or errors found in 1989? (ROMIG)

RECOMMENDATION: Yes, reduce O&M expenses by $189,840 ($194,229 Jurisdictional) for other non-recurring expenses.

POSITION OF PARTIES

GULF: No. No such items have been included in the 1990 Test Year.

OPC: Yes. Remove $116,000 for heavy equipment rebuilds and $252,000 for renovations to the Panama City office.

STAFF ANALYSIS: Mr. Scarbrough stated that if Gulf's budget contained any truly non-recurring, out-of-period or non-utility items that it would have no objection to the removal of those items (T. 505), that in Gulf's opinion no such items are contained in the filing. Mr. Gilbert testified that non-recurring items are budgeted each year. Although those specific activities will not recur next year, similar activities will occur (T. 645).

Public Counsel stated in its brief that the discussion in support of this issue has been included in Issue 29.

Gulf includes in its budgeted O&M expenses amounts for non-recurring items. Staff is in agreement with the company that the same items will not recur each year but will be replaced by other activities. Staff reviewed Late-Filed Exhibit 629 which presented actual and budgeted non-recurring expenses for 1990. In staff's opinion only a reasonable level of non-recurring expense should be allowed in O&M expenses. For 1990, Gulf budgeted $1,701,705 for other non-recurring expenses compared to a 5-year average of actual expenses of $1,507,476 or a difference of $194,229 system amount. The company stated on page 2 of the exhibit that the amount of the 1985-1990 average is greater than the amount requested in the 1990 test year. Gulf did not offer any explanation as to what activities were projected for 1990 in support of the $1,701,705 non-recurring expenses. Since these expenses affect all functional categories of expenses, the adjustment has been included on the O&M benchmark schedule as a single adjustment to total O&M expenses.

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ISSUE 55: Are Gulf's budgeted industry association dues in the amount of $199,343 during 1990 reasonable and prudent? (McLEAN)

RECOMMENDATION: A total of $147,172 of industry association dues should be allowed. This reflects the company's removal of $32,150 of industry association dues to comply with Commission guidelines, the staff's disallowance of $19,378 (33 1/3% of the requested EEI administrative dues of $58,133), and the staff's disallowance of $643 associated with miscellaneous organizations that were not identified by the company except as "Organizations to be joined in 1990." (100% jurisdictional)

POSITION OF PARTIES

GULF: The company has removed $32,150 of industry association dues (Schedules C-3 and C-27) and, as such, is requesting $167,193 for industry association dues ($199,343 originally budgeted minus $32,150 removed).

OPC: In addition to those dues removed by the company, based on the latest EEI report, an additional $21,608 should be removed. (Tr. 2474-2475)

STAFF ANALYSIS: In regard to EEI dues, the company did not remove one-third of the EEI administrative dues which has been disallowed by the Commission in the past as lobbying expenses based on Commission Order No. 13537 (Docket No. 830465-EI, FPL Rate Case). During cross examination, company Witness Scarbrough stated that EEI informed the company that approximately one percent of the EEI dues should be considered lobbying for the 1990 test year (Tr. 3811-3812). Public Counsel Witness Schultz stated that, based on a review of a report prepared for NARUC that addressed EEI expenses for the year 1987, he believes that a 37.17% disallowance of EEI membership dues ($21,608) is appropriate based on the percentage of EEI dues (Tr. 2474-2475). Since Witness Schultz failed to identify the report and enter it into the record, the staff was unable to examine the report to address the amount of EEI dues recommended for disallowance by this witness. The Commission's past rate case decisions to disallow one-third of EEI dues as lobbying are based on the recommendations of the NARUC Staff Subcommittee on Accounts, which was requested by the NARUC Executive Committee to analyze the expenditures of EEI, and on the testimony of FPL Witness Douglas Bauer, Vice President of EEI, during Docket No. 830465-EI. Since the company has not presented an adequate segregation of EEI expenditures, the staff suggests that one-third of EEI administrative dues ($19,378) should be disallowed for the test year in keeping with Commission Order No. 13537.

In addition to the company's adjustments, the staff suggests the additional removal of $643 associated with miscellaneous organizations that were not identified by the company except as "Organizations to be joined in 1990."

As regards the EEI Media Communications Program, no adjustment is required since the company stated in response to interrogatories that contributions to the Media Communications Program are charged to Account 930-170, and have been adjusted out of net operating income on MFR Schedule C-3, Page 6 of 7, Line 10.

The staff's suggested test year system dues adjustments are shown in the following industry association dues tabulation.

Docket No. 891345-EI
Industry Association Dues Evaluated by Staff[a]
(MFR Schedule C-27, Page 3 of 3)

Organization	$Amount Budgeted by Company 1990	$Amount Recommended by Staff to be Allowed 1990	$Amount Recommended by Staff to be Disallowed 1990
A. Organizations that are requested by the Company for the 1990 test year			
1. American Compensation Association	225	225	0
2. American National Standards Institute	1,911	1,911	0
3. American Society of Heating, Refrigerating and Air Cond.	40	40	0
4. American Society of Industrial Security	300	300	0
5. American Society for Personnel Administration	160	160	0
6. The Association of Edison Illuminating Companies	801	801	0
7. Better Business Bureau	1,075	1,075	0
8. Electrical Contractors Association of Northwest Fla.	350	350	0
9. Edison Electric Institute	58,133	38,755	19,378(b)
10. Florida Electric Power Coordinating Group	84,275	84,275	0
11. Florida Public Relations Association	198	198	0
12. Gulf Coast Economics Club	1,000	1,000	0
13. Homebuilders Association of West Florida	280	280	0
14. International Criminal Investigators Association	25	25	0
15. International Foundation of Employee Benefit Plans	350	350	0
16. National Association of Chiefs of Police	30	30	0
17. National Cash Management Association	150	150	0
18. National Safety Council	950	950	0
19. Northwest Florida Safety Council	500	500	0
20. Southeastern Electric Exchange	6,420	6,420	0
21. Southeastern Electric Reliability Council	6,895	6,895	0
22. Utilities Telecommunications Council	2,482	2,482	0
23. Organizations to be joined in 1990	643	0	643(c)
SUBTOTAL - Amount requested in Company's Brief	167,193	147,172	20,021

Docket No. 891345-EI
Industry Association Dues Evaluated by Staff[a]
(MFR Schedule C-27, Page 3 of 3)

Organization	$Amount Budgeted by Company 1990	$Amount Recommended by Staff to be Allowed 1990	$Amount Recommended by Staff to be Disallowed 1990
B. Organizations removed by the Company in its filing to comply with Commission Guidelines - (MFR Schedule C-3, Line 9, Page 6 of 7)			
1. Associated Industries of Florida	4,000	0	4,000
2 Bay County Chamber of Commerce Resort Council	140	0	140
3 Bay County Motel and Restaurant Association	100	0	100
4. Chambers of Commerce	15,870	0	15,870
5. Committees of 100	1,875	0	1,875
6. Crestview Board of Realtors	40	0	40
7. Emerald Coast Improvement Council	1,000	0	1,000
8. Florida Economic Development Council	400	0	400
9. Florida Tax Watch, Inc.	5,000	0	5,000
10. Graceville Area Development Council	125	0	125
11. International Society of Arboriculture	65	0	65
12. Leadership Pensacola	25	0	25
13. Military Affairs Committee	700	0	700
14. National Association of Manufacturers	2,000	0	2,000
15. Pensacola Historical Society	300	0	300
16. Utility Arborist Association	10	0	10
17. Warrior-Tombigbee Development Association	500	0	500
SUBTOTAL	32,150	0	32,150
TOTAL (A+B) - Original Filing Request	199,343	147,172	52,171

Notes:

(a) All dollar amounts shown are per books (system) - jurisdictional factor is 1.0
(b) One-third of the $58,133 EEI administrative dues (i.e., $19,378) was disallowed by staff based on Commission Order No. 13537 from Docket No. 830465-EI, FPL Rate Case
(c) The Company neglected to remove and to identify the organizations associated with $643 specified for "Organizations to be joined in 1990"

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ISSUE 56: What is the appropriate amount of rate case expense to be allowed in operating expenses? (MERTA)

RECOMMENDATION: The appropriate amount of rate case expense to be allowed in operating expenses is $333,333. Projected rate case expense of $1,000,000 should be amortized over 3 years, therefore expenses should be reduced by $166,667.

POSITION OF PARTIES

GULF: The appropriate amount of rate case expense amortization for the test year is $500,000. The total cost of the case is budgeted at $1,000,000. The amortization period of two years is appropriate.

OPC: Since no rate increase is necessary, no expense should be allowed for recovery. Reduce expenses by $500,000. In the event this Commission determines that a rate increase is appropriate, the expense should be adjusted based on the ratio of the total rate relief granted to the total relief sought. This adjusted amount should then be amortized over 5 years (TR 2464). Reduce operating expenses by $300,000. (Schultz)

STAFF ANALYSIS: The Company projected rate case expense at $1,000,000. This amount is not contested and consists of:

Outside Consultants	$248,000
Legal services	164,000
Meals and Travel	37,000
Paid overtime	7,000
Other Expenses*	544,000
Total	$1,000,000

*Includes SCS expenses, postal charges, printing costs and transcripts.

At issue is the amortization period over which the expense will be spread. Commission policy is to amortize rate case expense over a period of time because a rate case benefits not only the current period, but future periods as well. In Gulf's last rate case, the Commission in Order No. 14030, allowed a two year amortization period. In Gulf's 1982 rate case, the Commission in Order No. 10557, allowed a three year period. In the FPUC-Fernandina Beach Division rate case, the Commission approved a 5 year amortization period since it had been approximately 15 years since the company's last rate case. (Order No. 22224, Docket No. 881056-EI).

Gulf Witness Scarbrough testified that a two year amortization period was appropriate because over the past ten years, Gulf has had five rate cases for an average of one rate case every two years. In addition, the Commission ordered a two year amortization in Gulf's last rate case. (TR 349-350).

OPC recommends that rate case expense be disallowed since they believe that an increase is unnecessary. A five year amortization period is recommended, if the Commission grants Gulf an increase. (TR 2464). Public Counsel pointed out and Witness Scarbrough agreed that when a shorter amortization period is granted than is actually experienced, there will be an overrecovery of rate case expense. For example, if rate case expense was ordered to be recovered over two years and the company came in for a rate increase in five years, the expense would have been fully recovered in two years but would continue to be in rates for an additional three years. (TR 349). On the other hand, if the company is granted a five year amortization period and comes in for rate relief in two years, the company would not have fully recovered the expense. The unamortized balance could be allowed in rates by the Commission and thus fully recovered, however, there is no mechanism for recapturing the overrecovery. (TR 349-351).

It has been six years since Gulf's last rate case. (TR 348). Pursuant to Chapter 366, F.S., Gulf must file Modified Minimum Filing Requirements (MMFR's) in 1994. (TR 351-352). Based on these facts and the arguments presented above, Staff believes the amortization period should be greater than the two years ordered in Gulf's last rate case but less than the six years between cases, since the Company must file MMFR's in four years. Staff recommends that rate case expense be amortized over three years. Expenses should be reduced by $166,667. $1,000,000/3 - $500,000 = $166,667.

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ISSUE 57: Should Gulf be allowed to recover any costs associated with Docket No. 881167-EI, the withdrawn rate case? (REVELL)

RECOMMENDATION: No. Gulf should not be allowed to recover any expenses associated with the withdrawn case. Furthermore, any deferred debits associated with the withdrawn case should be removed from working capital. However, Gulf is not requesting any recovery of expenses from the withdrawn rate case and the company has removed the associated deferred debits from working capital.

POSITION OF PARTIES

GULF: Gulf has no O&M expenses budgeted in the 1990 test year for the withdrawn rate case, Docket No. 881167-EI. (McMillan)

OPC: No.

STAFF ANALYSIS: We have adopted the position that no expenses will be recovered from the ratepayers for the withdrawn rate case, Docket No. 881167-EI, nor would we allow any deferred debits in working capital which would earn a return for the company.

The company fully expensed all charges associated with the withdrawn case in June, 1989, and is not projecting any additional O&M expenses for 1990. In addition, the company has removed all deferred debits associated with the rate case. As a result, staff recommends that no further adjustment be made for any expenses or deferred debits associated with the withdrawn case.

DOCKET NO. 891345-EI
(GULF.JY) July 27, 1990

ISSUE 58: Should bank fees and line of credit charges be included in operating expenses? (ROMIG, YECCO)

RECOMMENDATION: Yes. To the extent bank fees and line of credit charges are necessary for the provision of utility service they should be included in operating expenses.

POSITION OF PARTIES

GULF: Yes. These bank fees are for our utility banking services and are properly included in electric operating expenses.

OFFICE OF PUBLIC COUNSEL: No. The total budgeted amount for this time should be borne by the stockholders. Reduce expenses by $223,400.

STAFF ANALYSIS: OPC's position is that the total budgeted for bank fees and line of credit charges should be borne by the company's stockholders. OPC witness Schultz testifies that the cash previously held by the company as compensating balances, can now be invested to earn a return that is not included in net operating income. Gulf Power's position is to the extent that the banking fees and line of credit charges are necessary and prudent for the provision of utility service they should be included in the O&M budget.

Staff agrees with the Company's position. The bank fees and line of credit charges are for a controlled disbursement account and the payment of fees to maintain lines of credit. According to Company witness McMillan using a controlled disbursement account and paying fees to maintain lines of credit have reduced Gulf's banking cost, cash required for working capital, and the Company's revenue requirements.

Staff evaluated the amount budgeted for bank fees and line of credit charges on the basis of need and prudence. In staff's opinion the company needs to maintain some liquidity to meet short term cash requirements. The Commission should allow the Company to recover the cost associated with maintaining a reasonable level of liquidity. In prior rate cases the Commission included the amount of cash held for compensating balances in rate base permitting the Company to earn a return on this asset equal to the Company's overall cost of capital. Thus, the effect on revenue requirements of maintaining compensating balances was the Company's compensating balances multiplied by its authorized cost of capital. Staff notes that the Company's current banking practices will result in a lower revenue requirement than its previous practice of maintaining large compensating balances.

In a related matter, the FERC has taken an exception to the Company's recording of Line of Credit Fees in account 921, Office Supplies and Expenses, instead of the account, Other Interest Expense. (PSC Audit Disclosure, FERC Violation 12) (Exh. 383) FERC's basis is that these are committment fees paid for bank loans committed but not borrowed and should be considered interest. Staff believes that if these fees are for "Letters of Credit" the fees should be treated as interest. Letters of credit are bank guarantees of bonded debt. As such they are expenses associated with issuing specific bonds and thus should be recovered over the life of the bond. In staff's opinion, line of credit charges are for the purpose of maintaining sufficient liquidity to meet short term cash needs and should be expensed.

ISSUE 59: Gulf budgeted $8,963,407 ($9,459,943 System) for Outside Services expenses for 1990. Is this amount reasonable? (REVELL)

RECOMMENDATION: Yes. The $8,963,407 ($9,459,943 System) for 1990 Outside Services expense is reasonable.

POSITION OF PARTIES

GULF: Yes. The amount if reasonable for A&G Outside Services charged to Account 923. (Scarbrough)

OPC: This account should be reduced for the affect of other issues.

STAFF ANALYSIS: Staff's initial position was that expenses for outside services for anything connected with the grand jury investigation would be disallowed. After a review of MFR C-65, pages 1-5, which listed no grand jury related activities, as well as discussions with Gulf employees and a review of FPSC Audit Report, staff is satisfied that the $8,963,407 ($9,459,943 System) reflects genuine needs of the company and contains no expenses related to the grand jury investigation. Therefore, staff recommends that $8,963,407 $(9,459,943 System) in expenses for Outside Services is proper.

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ISSUE 60: Gulf has projected $7,775,000 ($7,780,000 System) in Customer Accounts expenses for 1990. Is this amount reasonable? (MERTA)

RECOMMENDATION: Yes.

POSITION OF PARTIES

GULF: Yes. (Scarbrough)

OPC: Public Counsel did not address this issue in their Brief.

STAFF ANALYSIS: The parties agree that no adjustment is necessary to Customer Accounts.

Customer Accounts expenses are recorded under three major categories: General Expense (Supervision, Customer Records and Collections, and Miscellaneous), Meter Reading Expense, and Uncollectible Accounts Expense.

Gulf's projected expenses in the Customer Accounts function are below the benchmark by $1.6 million. Gulf Witness Scarbrough testified that improvements in the processing of customer bills and increased computer enhancements have allowed the Company to hold these expenses below the benchmark level. (TR 333).

Staff recommends no adjustment in this issue.

ISSUE 61: Should the expenses related to the Industrial Customer Activities and Cogeneration Program be allowed in base rates? (BALLINGER)

RECOMMENDATION: No. Expenses should be reduced by $426,464. This program appears to be a load retention program for large industrial customers.

POSITION OF PARTIES:

GPC: Yes. Gulf should be allowed to include the expenses for this program in base rates. The activities contained in this program contribue to our on-going goal to reduce the average cost of electric service to our customers. Gulf is required as a result of changes in FEECA, to address cogeneration as part of its plan to reduce the growth rate in peak demand. It is only logical that the Commission allow Gulf to continue a program that is now required by statute.

OPC: No position stated in the brief.

STAFF ANALYSIS: As justification for this expense, Gulf states that this program provides benefits to the general body of ratepayers by preserving revenues. This is the age old question of the benefits of high load factor customers to the general body of ratepayers. While this may have some benefits, there is some concern with Gulf's program because on one hand, they contend that the retention of high load factor customers benefits all customers and on the other hand, the Company does not have any firm purchases of cogenerated power and is requesting that additional plant be placed in base rates. This seems to be contradictory in nature and staff fails to see the clear benefit of this program and would recommend that the budgeted amount of $426,464 be disallowed from base rates.

Also, Gulf has proposed an Energy Audit and Technical Assistance Program as part of its overall conservation plan. This program not only addresses conservation measures, but cogeneration applications as well. In other words, it appears that these may be a duplication of activities between cost recovery and base-rate expenses.

ISSUE 62: Gulf has budgeted $50,000 for the Good Cents Incentive program. Is this expense appropriate? (BALLINGER)

RECOMMENDATION: No. The expenses for this item are split between Issues 63 and 100. Therefore, staff would recommend that this expense only be disallowed once and not double counted in the following issues.

POSITION OF PARTIES:

GPC: Yes. This activity has contributed to the overall success of Gulf's new home and improved home programs. The result has been improved efficiency in equipment and construction techniques. All ratepayers have benefited through reduced peak demand on Gulf's system. This activity has contributed to Gulf's commitment to conservation. The expenses ($50,000) for this activity are contained within Issue No. 63 ($25,000) and Issue No. 100 ($25,000).

OPC: In the event this or any other program is contrary to Commission policy on conservation or cannot be justified as a legitimate expenditure, it should be disallowed.

STAFF ANALYSIS: The Good Cents Incentive program offers merchandise and travel packages to contractors for the installation of energy efficient appliances. It also offers these incentives for the retrofit of gas furnaces to electric heat pumps. The provision of these appliances does not require the use of an incentive for two reasons. First, the appliance market place does not cater to inefficient appliances. Even if a contractor wanted to save some money and install an inefficient system, he would have a hard time finding one. Secondly, the general public, as well as the real estate community, is well aware of the benefits of having an energy efficient home. This has become a major selling point for many houses and is the result of the demand from the customer to have an energy efficient home.

Since the provision of incentives to contractors is not necessary, staff would recommend that the $50,000 budgeted for the Good Cents Incentive program be disallowed from base rates.

ISSUE 63: Gulf has budgeted $457,390 for the Good Cents Improved and $1,023,995 for the Good Cents New Home programs. Are these expenses appropriate? (BALLINGER)

RECOMMENDATION: Yes. While these programs may be only marginally cost-effective, they do provide a valuable customer service.

POSITION OF PARTIES:

GPC: Yes. Gulf has demonstrated that these programs are cost-effective, have a high participation rate and that the services provided as part of the programs fulfill the demands of our customers for a source of unbiased information concerning energy efficient residential dwellings.

OPC: No. Remove $1,023,995 for the Good Cents New Home Program and $609,783 for the Good Cents Improved Home Program.

STAFF ANALYSIS: Pursuant to Order number 19742 issued July 28, 2988, Gulf Power and the staff stipulated to the removal of the Good Cents New Home program from the ECCR factor. This stipulation was reached because it was shown that the program was marginally cost-effective based on the Commission's cost-effectiveness test. Cost recovery for the program was not denied, it was simply removed from the preferential treatment of the ECCR. This was done to insure that a program whose cost-effectiveness depended on questionable assumptions could not abuse the "limitless" amount available through direct cost recovery.

The Good Cents Improved program was removed from the ECCR for many of the same reasons. Also, this program showed a long pay back period for participating customers which cast doubt on the participation rates assumed in the cost-effectiveness calculations. As with the new home program, cost recovery was not denied, only removed from ECCR.

Based on witness Bowers testimony, both Good Cents programs are customer service programs. (TR 4032) These programs provide information and services to Gulf's customers which would probably be asked for even without the programs. Such services are energy awareness, appliance selection and assuring compliance with the State's energy building code. These types of services are a component of the utility's business and are appropriate to include as a budgeted expense item in base rates. The ECCR factor should only apply to conservation programs. Customer service programs are better suited for inclusion in base rates and don't require special cost recovery treatment.

While the facts that led to the removal of these programs from the ECCR have not changed, the nature of these programs still provides customers with services and information. For this reason, staff would recommend that the budgeted expenses for these two programs are reasonable.

ISSUE 64: Gulf has budgeted $767,609 for the Essential Customer Service Program. Is this expense appropriate? (BALLINGER)

RECOMMENDATION: Yes. This is a support program to other customer service programs.

POSITION OF PARTIES:

GPC: These expenses support activities required by our customers but are not contained within specific program headings. This activity is merely an accounting mechanism to which these activities are allocated. Specific expenses included are related to preparation and monitoring of the O & M budget; development of the customer, KWH, and revenue forecast; travel to meetings with the Florida Coordinating Group, Edison Electric Institute, the Department of Community Affairs, etc.,; general supply expenses, as well as vehicle expense. Also included in "Essential Customer Services" are the expense related to the Company's Safety Information Program.

OPC: No position stated in brief.

STAFF ANALYSIS: This program is primarily a backup or support program to Gulf's other customer service programs. Expense for this program include rate comparisons, development of inputs from field data for kwh and revenue forecasts, and some travel expenses. This program was separated to ease the accounting procedures since the information collected is common to several programs throughout the company.

ISSUE 65: Gulf has budgeted $425,474 for its Energy Education Program. Is this expense appropriate? (BALLINGER)

RECOMMENDATION: Yes.

POSITION OF PARTIES:

GPC: Yes. The energy education program is a vehicle Gulf uses to inform our customers of the conservation and energy management programs and services available to them and to receive feedback from them on how to continue to meet their needs for new products and services.

OPC: No. It should be removed for O&M expenses.

STAFF ANALYSIS: This program is a direct education program geared towards adults as well as school aged children. The expenses contained in this program are for materials such as brochures and charts, labor, and advertising. The information provided is directed towards the efficient use and choice of electrical appliances and other conservation and customer service programs offered by Gulf. This is also a service that would probably be asked for by Gulf's customers even if a specific program did not exist.

In its brief, OPC argues that basically, people do not need to be educated any more on energy conservation. Nothing could be further from the truth especially as new technologies emerge and fuel prices are remaining stable. Education is a customer service that is always changing and being requested by Gulf's customers.

ISSUE 66: Gulf has budgeted $55,429 for its Presentation/Seminar program. Is this expense appropriate? (BALLINGER)

RECOMMENDATION: No. This program is only a promotion for local contractors and should not be included in base rates.

POSITION OF PARTIES:

GPC: Yes. These presentations are customized for the needs of Gulf's commercial and industrical customers and are used to educate them regarding advanced end-use technologies and the services the Company makes available to them.

OPC: No. They should be removed from O&M expenses.

STAFF ANALYSIS: Gulf contends that this program provides presentations to local contractors about the energy efficiency of electric appliances. This appears to be a partial duplication of the Company's Education program and the Good Cents programs. Today's contractors are well aware of the importance of an energy efficient home and additional presentations and seminars should not be required by Gulf Power. While these presentations and seminars do foster a better relationship between Gulf and the local contractors, staff does not see any additional benefits accruing to the general body of rayepayers. In other words, the ratepayers would probably get the same service from the contractor without this program. Therefore, staff would recommend that this expense be disallowed from base rates.

ISSUE 67: Gulf has budgeted $145,652 for its Shine Against Crime program. Is this expense appropriate? (BALLINGER)

RECOMMENDATION: The percentage of this expense attributable to new installations should be disallowed because this promotes the use of electricity and increases kwh consumption. This would result in a disallowance of $91,761.

POSITION OF PARTIES:

GPC: Yes. This program provides direct benefits to the participating customers by reducing the energy consumed in street lighting. This program benefits all customers through the better utilization of electrical plant and the significant societal benefits from a lower crime rate.

OPC: No position stated in brief.

STAFF ANALYSIS: The Shine Against Crime program is simply an outdoor lighting program. These types of programs have been in existence for some time mainly to change out inefficient lighting with more efficient high pressure sodium lighting. This practice actually reduces kwh consumption and conserves vital resources.

Section 366.80-.85 of the Florida Statutes, also known as the Florida Energy Efficiency and Conservation Act (FEECA), mandates that utilities control energy growth. While the replacement of inefficient outdoor fixtures helps to reduce energy requirements, the promotion of "new" outdoor installations increases energy requirements. It is this facet of the Shine Against Crime program that staff takes exception with. The promotion of off-peak load does not contribute to reducing energy requirements and is contrary to FEECA. The Company's witness Bowers stated that approximately 35 to 37% of the expenses for this program are attributable to changeouts of existing fixtures. (TR 4038) This means that 63% the expenses, or $91,761, is attributable to new installations and the promotion of off-peak sales and should not be recovered through base rates.

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ISSUE 68: Gulf has projected $687,000 ($687,000 System) for economic development expense in the sales function for 1990. Is this amount reasonable? (REVELL)

RECOMMENDATION: No. Expenses should be reduced by $687,000. Expenses for economic development promotes the use of additional electricity. Also, Staff does not think that Gulf should be duplicating the efforts of Chambers of Commerce or other development boards in its service area.

POSITION OF PARTIES

GULF: Yes. Gulf's service area is going to continue to grow. Our economic development activities are for the purpose of influencing the type of growth. We recognize that some growth is going to occur. Gulf wants to be in a position to assist in the management of growth so that our communities and ratepayers will receive lasting benefits. (Bowers)

OPC: The total amount for economic development should be excluded from recovery. (Schultz)

STAFF ANALYSIS: Mr. Bowers states that Gulf's well-being is directly related to that of the community, and that it has a direct stake in the community's overall development. [T-894] As a result, Gulf has developed a marketing and promotional campaign to develop the appropriate infrastructure, information and data base to combine with local communities for a "maximum effort" [T.895]. Mr. Bowers further states that, "... economic development has become a key part of our electric utility demand-side marketing plans due to the greater opportunities provided to increase load factor, by adding or expanding customers that have a higher load factor themselves or have need for utilizing energy during non-peak hours." [T-895]

What this means is that Gulf has assumed some of the responsibilities of local chambers of commerce or development boards. Traditionally, those organizations have been in the forefront of attracting businesses to expand and particularly relocate in their area. What Gulf is doing is duplicating these efforts. Even the company admits that it has "assumed a leadership role in furthering the capability of communities in its service territory to attract and/or expand the industrial base." [T-896] In actively seeking to expand industry or business activity in general, Gulf is actively setting out to increase sales of electricity.

Even with a projected 1990 expenditure of $687,000, the company admits that utilities have a limited ability to directly cause a new industry to relocate or an existing industry to expand. [T-895] Also stated is the belief that the affected community themselves are responsible for providing whatever incentives are necessary to attract new industry.

Obviously, various types of marketing expenses would be expected of a company operating in a non-regulated environment. A desire to increase sales or market share against the competition is normal and healthy when there is, in fact, competition. The reason Gulf is regulated, however, is that Gulf has no competitors supplying electrical power in the same geographic area it serves. Being regulated is the price that is paid for having a monopoly on the customer base for electrical power.

Staff does not believe that operating in a monopolistic situation Gulf should pass on to the general body of ratepayers expenses for marketing itself and the region when it is the "only game in town" for electricity. Besides, such efforts are directly related to increasing sales of electricity which the Commission, in general, opposes. The Commission disallowed similar expenses in the last rate case. The company is over the benchmark for the entire $687,000 budgeted amount because it was not allowed. The company is attempting to include it in this docket. Public Counsel agrees with staff that this expense should not be allowed for recovery from the ratepayers. If new businesses relocate and want power, Gulf not only would be required to provide service but would be more than happy to work with the new company to serve them efficiently. Therefore, we recommend that the entire $687,000 in 1990 expenses for economic development be disallowed.

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ISSUE 69: Gulf has projected $5,358,179 ($5,655,000 System) in Production-Related A&G expenses for 1990. Is this amount reasonable? (ROMIG)

RECOMMENDATION: Yes. The 1990 Production-Related A&G expenses are reasonable.

POSITION OF PARTIES

GULF: Yes. (Scarbrough)

OPC: No, this amount should be reduced as recommended in other issues.

STAFF ANALYSIS: In the company's last rate case, the company did not separate A&G expenses between Production-Related and A&G Other for O&M benchmark purposes. The Production-Related expenses represented Gulf's 50% share of A&G expenses. The Commission, in Order No. 14030, reduced expenses $1,464,000 as not being justified since the company applied CPI and Customer Growth to all A&G expenses, including the Production A&G. (CPI only is applied to Production expenses for purposes of the benchmark calculation.) The Commission in that order found that "...We reject it not because we find the amount to be unreasonable or imprudent, but because we find that Gulf has not already included this amount in a previous justification."

In this docket, the company restated the 1984 A&G expense by separating this function into A&G Production-Related and Other and then recalculating the benchmark variance. After restatement, the company was under the benchmark for A&G Production by $790,000. In calculating the benchmark variance, the company added back the disallowance to the base amount and also included A&G expenses related to Plant Scherer.

Public Counsel addressed the Production-Related A&G expenses under Issue 89, Plant Daniel expenses wherein they recommended a reduction in A&G expense by $1,172,000 to reflect the proper benchmark level.

OPC Witness Schultz testified that based on his review of the budgeting process for Plant Daniel, Gulf has very little control over these expenses. (T. 2446-2448) Gulf took exception to this statement by Mr. Lee who testified that the budgets submitted to Gulf from Mississippi are reviewed for reasonableness. Throughout the year the budget comparison report regarding expenditures versus budget are reviewed (T. 3593).

OPC's concerns are that Gulf does not actively participate in the budgeting and operations of Plant Daniel.

Public Counsel on pages 85 and 86 of their brief.

> Setting aside the argument of operation expense input, the Commission must look at the "bottom line" on this issue. That is, are the expenses at Plant Daniel reasonable? In Gulf's last case the Commission determined that based on the benchmark the expenses were not reasonable [T. 2449, 2450]. Using the same test in this case and considering the shallow justification for the overages, the Commission should reduce the Plant Daniel expenses as outlined above.

In Gulf's last case the Commission on Page 27 of Order No. 14030 stated the following with regard to A&G expenses.

> We reject Gulf's attempted justification for this amount in excess of CPI and customer growth benchmark. We reject it, not because we find the amount to be either unreasonable or imprudent, but because we find that Gulf has already included this amount in a previous justification.

With regard to expenses billed Gulf by Mississippi, these billings are audited by the Internal Auditors of Southern Company Services on a periodic basis in order to determine whether such billings are in compliance with the terms of the operating agreement. These audits have found in certain instances where Gulf has been over billed. The overbillings were corrected by Mississippi.

In our opinion, the company has attempted to cure any problems the Commission may have had in its last case by separating the A&G expenses. The Commission did not reduce expenses in the last case based on unreasonableness or imprudency. The adjusted benchmark is a negative $790,000; no adjustment is recommended.

ISSUE 70: Gulf has projected $31,070,804 ($32,792,000 System) in Other A&G expenses for 1990. Is this amount reasonable? (ROMIG)

RECOMMENDATION: No. The appropriate amount is $29,837,434 ($31,500,000 System) based on adjustments made in other issues.

POSITION OF PARTIES

GULF: The correct amounts are $32,037,266 ($33,812,000 System). These expenses are reasonable.

OPC: No, this amount should be reduced as recommended in other issues.

STAFF ANALYSIS: This issue is a fallout of the other A&G issues.

Staff has recommended adjustments in other issues which reduce A&G expenses $1,233,370 ($1,292,000 System). Deducting the system amount from Gulf's $43,000 benchmark variance results in a $1,249,000 negative benchmark variance. No further adjustments are recommended.

During the hearing, staff addressed the area of Provision for Property Damage and Injuries and Damages. Gulf Power maintains Accumulated Provisions for Property Damage and Injuries and Damages in accordance with Commission Rule 25-6.0143. Included in the rule is a provision that the provision level and annual accrual will be evaluated at the time of a rate case or by separate petition outside of a rate case. Neither staff or Public Counsel proposes any adjustments to the accrual or balance in the accounts.

Provision for Property Damage: In the company's last case, the balance in this account was $3.2 million and projected to be $7.0 million at the end of 1990. The company is currently accruing $1.2 million per year. The company noted on page 94 of the C schedules the desired balance should be maintained from $5 to $10 million. Mr. Scarbough stated that the company has not increased the accrual since the last rate case and that in the event the balance reached the upper limits of the desired balance, Gulf would petition the Commission to cease or reduce the accrual (T. 438-439). With regard to losses charged against the reserve, Mr. Scarbrough stated that in 1985 $3.8 million was charged to the reserve as a result of hurricane damage and in 1979, Gulf carried a negative balance as a result of Hurricane Frederick (T. 439). Staff recommends that Gulf continue its $1.2 million annual accrual.

Provision for Injuries and Damages: In the company's last case the balance in this account was $1.8 million and projected to be $1.3 million at the end of 1990. The company is currently accruing $1.2 million per year. The company noted on page 95 of the C schedules the desired balance should be from $2 to $4 million.

Mr. Scarbrough stated that the desired balance of $2 to $4 million was based on Gulf's recent experience, the size of claims and the deductibles in insurance policies (T. 440). Mr. Scarbrough also stated that if the upper limit for the injuries and damages reserve was reached, Gulf's action would be the same as with the Provision for Property Damage (T. 441-442). Staff recommends that Gulf continue its $1.2 million annual accrual.

ISSUE 71: Has Gulf included any lobbying and other related expenses in the 1990 test year which should be removed from operating expenses? (ROMIG)

RECOMMENDATION: Yes. Expenses should be reduced $263,534 ($278,133 System).

POSITION OF PARTIES

GULF: Yes. Gulf has agreed to remove a total of $253,265 (System) from its projected operating expenses in the 1990 test year.

OPC: No. mr. Scarbrough has now agreed to remove an additional $101,997 of lobbying expenses, along with $126,566 related to information gathering and administrative activities of its registered lobbyist [T. 3810-3811]. Also, any further expenses that may show up in late-filed exhibit 626 should be removed [T. 3853].

STAFF ANALYSIS: Mr. Scarbrough at T. 3811 stated that Gulf inadvertently included $101,997 of lobbying expenses which should be removed from expenses. In addition, Gulf has also agreed to remove $126,566 of expenses related to the information gathering and administrative activities of its registered lobbyists. It should be noted that the $253,265 adjustment reflected in Gulf's position above does not agree with their stipulated amount of $228,563. The difference of $24,722 represents the salary of a Governmental Affairs Analyst, $23,722, and $1,000 in dues which have been adjusted out of NOI. Staff does not recommend an adjustment for the $23,722 salary.

The above expenses were reflected on Late-Filed Exhibit 626. These expenses were associated with the Tallahassee Office and Mr. Earl Henderson's expenses, $126,566 and $101,997 in expenses charged to SCS Workorder 4750-30, Outside Consultants.

In addition to the above, staff noted on late-filed exhibit that Gulf incurred expenses for the following: Regulatory Matters Coordinator position, $5,673 recorded below-the-line in 1989 and agreed to remove from expense for the 1988 tax savings docket; SCS Workorder 4750-01, Governmental Affairs, $173,667 and SCS Workorder 4759-30, Governmental Affairs-Atlanta, $720.

Mr. Scarbrough was asked the following with regard to SCS Workorders 4750-01, 21 and 30 (T. 3855-3856). Question: Could you tell me whether the services provided by the Southern Company pursuant to these workorders would be similar in function to ... similar to the function fulfilled by Gulf's Tallahassee Office? Mr. Scarbrough in response: "It's similar in that there are a lot of activities carried on in that building, some of which are lobbying; and so yes, it's similar."

Staff, therefore, recommends a further reduction in expenses for the following consistent with the company's agreement for the 1988 tax savings docket and 25% reduction associated with the Tallahassee Office.

State Regulatory Matters Coordinator	$ 5,673
SCS Workorder 4750-01	$43,717
SCS Workorder 4750-30	$ 180

Based on the above, staff recommends reducing O&M expenses by $263,534 ($278,133 System).

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ISSUE 72: What is the appropriate C.P.I. factor to use in determining test year expenses? (REVELL)

RECOMMENDATION: The appropriate CPI factor to use is 4.7% for calendar year 1990.

POSITION OF PARTIES

GULF: The inflation (C.P.I.) factors used in MFR C-56 are appropriate:

	%
1985	3.552
1986	1.920
1987	3.662
1988	4.082
1989	4.910
1990	4.369

The most recently projected 1990 C.P.I. from Data Resources Institute (4.758% as of 5/90) would also be consistent with th methodology used by the Commission in Order No. 14030. (Gilbert)

OPC: To the extent the Company's projected expenses were based on their inflation factor and the resulting expense level is excessive, the Commission should make its own determination as to the proper factor to use.

STAFF ANALYSIS: Gulf originally used an inflation factor of approximately 4.4% for calendar year 1990 in MFR C-56 filed in its request for a rate increase. Gulf in its prehearing statement projected a factor of 4.75% as of May, 1990, as reported by Data Resources Institute (DRI). In keeping with our policy of using the latest factor available, we are recommending that the factor of 4.7% be used for calendar year 1990. This represents the June, 1990 factor from DRI.

ISSUE 73: For each functional category of expenses, what is the appropriate level of expenses for services provided by the Southern Company? (ROMIG)

RECOMMENDATION: No specific adjustments to SCS expenses are recommended in this issue. The appropriate level of SCS expenses by function are as follows:

	System
Production	$3,496,551
Transmission	584,945
Distribution	108,945
Customer Accounts	1,173,025
Cust. Serv. & Info.	199,177
Administrative & Gen.	8,246,591

POSITION OF PARTIES

GULF: The appropriate levels of SCS Operation and Maintenance expense are as follows: (1) Production - $3,496,551 (System); (2) Transmission - $584,945 (System); (3) Distribution - $108,945 (System); (4) Customer Accounts - $1,173,025 (System); (5) Customer Service and Information - $199,177 (System); (6) Administrative and General - $8,392,165 (System).

OPC: The Company's amount related to steam production should be reduced by $734,595.

STAFF ANALYSIS: Public Counsel Witness Schultz expressed concern about the amount of input Gulf has in the development of the SCS budget (T. 2454-2459). It appears that the majority of the budget discussions between Gulf and SCS are related to activities specifically requested by Gulf. The budgeted amounts also include costs for services performed for all of the participants of SCS and allocated to those companies. These costs are not subjected to the same scrutiny as that of the specifically requested items.

In 1986 and 1987 Larkin & Associates were retained by the Georgia PSC to review Georgia Power Company's budget. Their review included an attempt to substantiate the SCS budget items from the SCS workpapers. They were unable to do so since no workpapers were available. Mr. Schultz further testified that he was not provided support for the SCS budgeted changes (T. 2456-2457).

In response to Mr. Schultz' concerns, Gulf has input in the budget process to ensure that expenses are minimized and necessary to provide electric service (T. 1454). Before the budget is submitted, Gulf and SCS personnel review the SCS workorders. Before the SCS budget is presented to the company's management for approval, SCS personnel review the budget with appropriate company personnel (T. 1454-1455). Throughout the budget year actual changes are continually reviewed. Any concerns by Gulf are discussed and resolved between SCS and Gulf.

With regard to the study performed by Larkin & Associates for the Georgia PSC, Mr. Scarbrough testified that Mr. Schultz bases his recommendation on a three-year old review in another jurisdiction. Mr. Schultz has not performed such a review in this proceeding (T. 3801).

Gulf Witness Mr. Parsons testified that allocated costs and costs for specific services are subjected to the same scrutiny by Gulf, not just the specific activities (T. 2455).

In reviewing steam production workorders, Mr. Schultz states that he pulled 4 out of 28 workorders for purposes of comparing budget to actual amounts, and those which he pulled represented the larger variances (T. 2543-2544). As Commissioner Gunter recognized, Mr. Schultz could show the results significantly, one way or another, by not having randomness in the sample. If all 28 workorders had been analyzed and averaged, the total actual expenses exceed the budget for these activities (T. 2543-2544).

In staff's opinion, the record does not support the concern expressed by Mr. Schultz and his recommended disallowance of $734,595 in SCS Steam Production expenses. Gulf's budgeting process should be the same for each functional category of expenses; yet Mr. Schultz only expressed concern and proposed adjustments in the Steam Production area. In addition, no concerns were raised in the staff audit report regarding the budgeting of SCS expenses.

Staff reviewed Late-Filed Exhibit 630, non-recurring expenses. This exhibit contained budgeted SCS non-recurring expenses for 1987-1990 and actual amounts for 1987-1989. Based on a three-year average of actual, non-recurring expenses of $349,208 and 1990 budgeted amount of $873,151, it would appear that a reasonable level of non-recurring SCS expenses for 1990 would be $523,943. Included in the budgeted amount was $415,000 related to investigation expenses which have been removed by Gulf for a difference of $108,943. Also included in these expenses was $408,040 in Environmental Ground Testing expenses. This program was discussed on page 198 of the MFR C Schedules. Since staff has not recommended a specific adjustment for this program, no adjustments are recommended to the level of SCS non-recurring expenses.

The recommended level of SCS functional expenses in the recommendation of this issue has been reduced $145,574 for the recommended disallowance discussed in Issue 71, Lobbying Expenses.

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ISSUE 74: Has the company properly removed from 1990 expenses all costs related to I.R.S., grand jury and other similar investigations? (REVELL)

RECOMMENDATION: Yes. The company has removed from 1990 expenses all costs related to IRS, or the grand jury investigations, including an additional $5,000 in expenses which were identified since the filing of the MFRs.

POSITION OF PARTIES

GULF: The Company has made a concerted effort to identify and adjust from this case all costs associated with these investigations. Since filing this case the Company has discovered an additional $5,000 associated with outside auditing related to the investigation and stipulates to remove that amount at this time. (Gilbert)

OPC: Any amounts remaining should be removed.

STAFF ANALYSIS: MFR Schedule C-7, page 2 lists approximately $615,000 for outside services expenses related to the grand jury and IRS investigations which have been removed from the 1990 test year. At [T-645-46) company Witness Gilbert states that this $615,000 has been removed from the 1990 O&M budget. However, this does not include a $5,000 expense for the company's outside auditors to provide support for any presentations or reviews by the Board of Directors [T-670]. Commissioner Gunter at [T-670] asked Mr. Gilbert if any additional employee expenses incurred in 1989 were factored up in calculating 1990 expenses. Witness Gilbert indicated that salaried employees worked additional hours with no additional compensation to accomplish the dual tasks of regular company business and the IRS/grand jury business, and any overtime and copying costs or travel expenses had been identified and removed in 1989 [T-674]. Arthur Andersen & Company auditors, Gulf Power's outside auditors, reviewed the 1990 O&M budget forecast and found no expenses relating to the IRS or grand jury investigations which the company had not removed [T-700-701].

Public Counsel and staff, from the beginning, have agreed that any expenses in the 1990 test year relating to IRS/grand jury matters should be removed. It appears that Gulf has identified expenses of $615,000 which have been removed. Staff also recommends that the $5,000 for outside services subsequently identified also be removed.

ISSUE 75: What is the appropriate amount of pension expense for 1990? (SALAK)

RECOMMENDATION: The appropriate amount of pension expense is $0.

POSITION OF PARTIES

GULF: Gulf has budgeted $0 dollars for pension expense accrual in the test year.

OFFICE OF PUBLIC COUNSEL: No position.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: Gulf presented three projections for pension expense in 1990. First, the company budgeted $0 for pension expense and included this in its petition for a rate increase. (Exhibit 383, p. 51) OPC witness Schultz stated that he concurred that no amount should be budgeted for pensions since the Company will not be expending money for pensions in the foreseeable future. (TR 2465)

The second amount presented by Gulf was on MFR Schedule C-66 (p. 253), Pension Cost. This MFR reports projected net periodic pension cost to be ($11,020). This is an early projection of pension cost under SFAS 87.

Exhibit 422 contains the third amount presented by Gulf to project pension expense for 1990. Exhibit 422 is a letter dated June 1, 1990, from the actuary retained by Southern Company. The letter indicates that the revised estimate of pension cost under SFAS 87 for 1990 is $199,000. Of this amount, Witness Scarbrough testified that $156,252 would be expensed. (TR 445) For this projection, all assumptions remained constant, except the discount rate for the liabilities was reduced from 8.5% to 8%. (Exhibit 422, p. 1)

Historically, Gulf's pension expense has been on the decline for the past three years. For 1987, 1988, and 1989; Gulf's pension expense was $1,538,000, $1,385,000, and $47,000, respectively. These are the amounts recorded under SFAS 87. (TR 443-444)

Consistent with utility's treatment of pension expense for 1987-1989, Staff believes that pension expense should be recorded under SFAS 87; however, the estimates of pension cost vary from ($11,020) to $199,000. Although the $199,000 is the most current estimate available, it is not supported by a full actuarial valuation. Because of the new estimate provided, Staff believes that the pension cost will probably be greater than ($11,020). Since the 1990 pension costs are still estimates and the 1987-1989 trend of pension expense is downward, Staff recommends a pension expense of $0 as filed by Gulf. This is a conservative approach in favor of the ratepayers.

ISSUE 76: Are the projected O&M expenses for additional personnel reasonable in the steam production function? (BALLINGER)

RECOMMENDATION: Yes.

POSITION OF PARTIES:

GPC: Yes.

OPC: No position stated in brief.

STAFF ANALYSIS: Prior to the hearing, staff was unclear as to how the additional personnel from this function were accounted for. We were unsure if the "new" positions were actually new or a shift in personnel. Testimony presented by witness Lee indicates that these positions were not included in the 1984 base year but were filled prior to the 1990 test year. This caused the benchmark for this function to be exceeded. While most of these employees were previously with Gulf, they were not part of the power production department. These positions are necessary for the provision of electric service and the variance from the 1990 benchmark appears reasonable.

ISSUE 77: Gulf has budgeted $210,000 in O&M expenses for research and development projects. Are these expenses reasonable? (BALLINGER)

RECOMMENDATION: The $43,000 system ($31,813 jurisdictional) budgeted for the Acid Rain Monitoring program is an extension of a previous acid rain program and not a new R&D program. Therefore, the Company has not justified this variance from the 1990 benchmark and this amount should be disallowed from base rates.

POSITION OF PARTIES:

GPC: Yes. Gulf has justified each of these projects as reasonable and in the best interests of the ratepayer.

OPC: No position stated in brief.

STAFF ANALYSIS: In 1981, the Florida Electric Power Coordinating Group began funding of the Florida Acid Rain Deposition Study. In 1986, this study was concluded but the monitoring of acid rain continues today as an outgrowth of the study. In other words, Gulf spent money on this program during their last rate case and presumably had those expenses approved by this Commission. Their justification for the benchmark variance in the R&D function is the development of the monitoring program as if it were a new program. This just isn't true and is not a justification for the benchmark variance of $43,000 in this function. Therefore, staff would recommend that the benchmark excess of $43,000 for the R&D function should be disallowed from base rates.

In Issue 102, Public Counsel has raised a concern with the EMF studies being performed by Gulf. At the time the EMF standards were adopted, the Florida Environmental Regulation Commission established a task force to study methods of reducing EMF levels from electric facilities. The FCG agreed to to fund the $1 million project and Gulf's contribution is the $39,000 in question. Since this project is the result of new legislation, it is appropriate to consider this expense as justification of the benchmark variance in this catagory.

ISSUE 78: Has there been any "double counting" of expenses for services rendered by Southern Company Services or EPRI? (BALLINGER)

RECOMMENDATION: There were no specific audit exceptions that would indicate "double counting" of services provided by these companies.

POSITION OF PARTIES:

GPC: No. The projects undertaken by these groups are complimentary to, but do not duplicate, one another.

OPC: No position stated in brief.

STAFF ANALYSIS: This issue arose because of the appearance of double counting between Southern Company Services and EPRI in the R&D function. Staff requested that this be investigated as part of the general audit. Since no specific audit exceptions were mentioned, there is no evidence in the record that would indicate double counting between Southern Company Services and EPRI.

ISSUE 79: STIPULATED ISSUE: Gulf has budgeted $332,000 for ash hauling at Plant Daniel. Is this expense reasonable? (BALLINGER)

RECOMMENDATION: All the parties in this proceeding have stipulated that the $332,000 budgeted expense for ash hauling at Plant Daniel is reasonable.

POSITION OF PARTIES:

GPC: These expenses are reasonable and justified as this activity is now required by new environmental regulations. These expenses are a component of and included in the Company's total O&M expenses for Plant Daniel which have been identified for consideration and review under Issue 89.

OPC: No position stated in brief.

STAFF ANALYSIS: Plant Daniel has a wet ash pond that stores ash produced from the burning of coal. Additional storage capacity is needed so Gulf will begin digging and hauling the ash from the pond to a landfill in 1990. The budgeted expense represents Gulf's 50% share of the expense. Actual construction and capping of the landfill will be a capital item but the expenses for digging and hauling the ash will continue annually. The expenses for this function were not incurred in 1984 which is why there is a benchmark variance of $332,000. As mentioned in the recommendation, all parties have stipulated that this is a reasonable expense and should be included in base rates.

ISSUE 80: Gulf has budgeted $3,017,000 for Transmission Rents for Plants Daniel and Scherer. Are these expenses reasonable? (BALLINGER)

RECOMMENDATION: Yes if Plant Scherer is included in the Company's rate base. If Plant Scherer is not allowed, this expenses catagory should be reduced by $1,825,000.

POSITION OF PARTIES:

GPC: Yes. These amounts result from agreements which secured the least expensive alternative available to provide necessary transmission service to Gulf's service territory from Plant Daniel and Plant Scherer.

OPC: For the reasons cited in Issue 27, Plant Scherer costs should not be included for retail recovery at this time. Based on this position, the transmission rental of $1,822,000 should be removed.

STAFF ANALYSIS: As with any power plant, transmission facilities are necessary to transport the power to where it is needed. The transmission rents, or facilities charges, are a cost effective alternative to Gulf building its own transmission lines to receive power from Plants Daniel and Scherer. As testified by witness Howell, the expense for these facilities is below the fully embedded cost of the utility which owns the lines and below Gulf's own cost of construction. (TR 1494-1495) Since these expenses are similar to plant additions, this expense catagory should only be escalated at the rate of inflation for future benchmark analysis.

If the Commision does not allow Plant Scherer into Gulf's rate base, then the associated transmission expenses should also be removed. This would exclude all responsibility for Plant Scherer from Gulf's ratepayers and would result in an adjustment of $1,825,000 to the entire transmission expense catagory.

ISSUE 81: Gulf has budgeted $1,047,000 for its Public Safety Inspection and Maintenance program. Is this expense reasonable? (BALLINGER)

RECOMMENDATION: Yes. Gulf has expanded several existing programs and added some new programs since the Company's last rate case.

POSITION OF PARTIES:

GPC: Yes.

OPC: No. This expense should be reduced by $740,000 to reflect the 1990 benchmark.

STAFF ANALYSIS: Gulf's justification for the $740,000 benchmark variance was the addition of several new programs under this function. The purpose of these programs is to reduce the risk of personal injury and property damage at Gulf's facilities. Therefore, any additional expenses should be offset somewhat by reduced claims.

Exhibit number 595 was presented at the hearing by Gulf's witness Jordan. This exhibit shows the actual expense for each program as well as the claims paid in each year. Since 1985, two of the existing programs have increased dramatically. These are the relocation of distribution poles and safety inspections of facilities. Also, the Company has implemented two new programs since its last rate case. This exhibit also shows that the total expense, program cost and claims paid, has declined over the last three years. This is a good indicator that the programs are worthwhile since the program portion of the total expense will lag the claims portion. Therefore, staff would recommend that the budgeted expense of $1,047,000 is reasonable.

ISSUE 82: Gulf has budgeted $47,701,000 ($54,079,000 System) for Depreciation and Amortization expense. Is this amount appropriate? (REVELL/LEE)

RECOMMENDATION: No. The appropriate jurisdictional amount is $47,561,000.

POSITION OF PARTIES

GULF: The appropriate amount is $47,701,000 ($54,079,000 System).

OPC: Test year depreciation should be reduced by $967,000.

STAFF ANALYSIS: Except for specific adjustments addressed in other issues, there are no other adjustments.

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ISSUE 83: Gulf has budgeted $20,822,000 ($36,106,000 System) for Taxes Other. Is this amount appropriate? (MERTA)

RECOMMENDATION: No. If the Commission accepts staff recommendation in Issues 48 and 87, the appropriate amount of Taxes Other is $20,793,000 and no adjustment is necessary here. Otherwise this amount should be adjusted based on the Commission's decisions.

POSITION OF PARTIES

GULF: Yes.

OPC: The adjustment is a $321,000 decrease to Taxes Other as provided in OPC's schedules.

STAFF ANALYSIS: The Company's projected Taxes Other includes adjustments to remove tax expenses related to revenues recoverable through the Conservation Clause, franchise fees, and the gross receipts taxes and FPSC assessment fees associated with fuel, conservation, and franchise fee revenues which were removed. (TR 742, 744).

Staff agrees with Gulf's calculation of Taxes Other, however based on the adjustments to revenues and payroll taxes in Issues 48 (Increase $1,000), and 87 (Decrease $30,000), a reduction of $29,000 is appropriate. Public Counsel agrees with Staff on Issues 48 and 87 according to OPC's Operating Income Schedules. However, OPC makes an additional adjustment in Issue 27 decreasing Taxes Other by $244,000. (OPC Brief p. 79). These adjustments will be made in the specific issue and no adjustment is necessary here.

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ISSUE 84: What is the appropriate amount of income tax expense for the test year? (BRAND)

RECOMMENDATION: Jurisdictional income tax expense is $13,831,000, consisting of $14,198,000 current, $1,674,000 deferred, and $(2,041,000) ITC amortization.

POSITION OF PARTIES

GULF: $12,765,000 ($18,999,000 System), including the amortization of investment tax credits.

OFFICE OF PUBLIC COUNSEL: This amount should be adjusted based on other issues raised. The final amount will be supplied later in the Operating Income schedules.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: Income tax expense is a fallout number based on other adjustments to NOI.

Gulf's budgeted jurisdictional income tax expense for 1990 was $12,765,000, consisting of $13,185,000 current, $1,621,000 deferred, and $(2,041,000) ITC amortization. Staff increased current taxes by $1,293,000 and deferred income taxes by $53,000 for the tax effect of other recommended adjustments to revenues and expenses. As discussed in Issue 85, the combined interest reconciliation and ITC interest synchronization adjustments decrease current taxes by $231,000. No parent debt adjustment is necessary, Gulf's parent has incurred no debt and does not expect to incur debt for the projected test year. (MFR C-47). The resulting current tax is $14,247,000, deferred tax is $1,674,000, and ITC amortization remains $(2,041,000). Total jurisdictional income tax recommended by Staff is therefore $13,880,000.

ISSUE 85: What is the proper interest synchronization adjustment in this case? (BRAND)

RECOMMENDATION: The interest synchronization adjustment should be $231,000.

POSITION OF PARTIES

GULF: The jurisdictional interest synchronization adjustment results in a reduction in income taxes of $442,000.

OFFICE OF PUBLIC COUNSEL: This amount should be adjusted based on other issue raised. The final amount will be supplied later in the Operating Income schedules.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: On page 6 of his rebuttal testimony (TR 3,908-3,909), Gulf Witness McMillan stated that OPC Witness Larkin had calculated the interest reconciliation and ITC interest synchronization adjustments incorrectly. He had used the per-books interest amount of $30,871,000, instead of the correct jurisdictional synchronized interest amount of $32,045,000, and had also decreased tax expense, rather than increasing it. Witness Larkin acknowledged his error and agreed with the numbers submitted by the Company. (TR 2271-2275). The correct adjustment, based on Staff's recommended capital structure and reflecting the appropriate amount of interest from the Company's tax expense calculation, decreases income taxes by $231,000.

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ISSUE 86: Should an adjustment be made to the test year reference level of $2,630,877 for the Employee Relations Planning Unit? (REVELL)

RECOMMENDATION: All parties now agree that no adjustment should be made.

POSITION OF PARTIES

GULF: No. A miscalculation of the 1988 reference level stated in the budget message was corrected by Corporate Planning. The correction was approved by the Budget Committee and reflected in the approval letter. The Employee Relations reference level is appropriate. The reference level as used in Gulf's budgeting process only affects the amount of documentation provided by the planning units. The budget, however, is developed independently of the reference level. (Gilbert, Bell)

OPC: No adjustment should be made [T-2520].

STAFF ANALYSIS: This issue was originally raised by Public Counsel's Witness Schultz. In examining company budget documents, he found that this unit showed a large, unexplained increase from budget year 1988 to 1989, meaning that if it were unexplained for 1989, it shouldn't be "carried over" to the test year, 1990. Therefore, he recommended a reduction of $648,000. At [T-2520] Witness Schultz admitted the unexplained increase was in fact a correction of an error and he withdrew his recommended adjustment. This issue, therefore, is moot; no adjustment is necessary or recommended by any party to this docket.

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ISSUE 87: Has the Company made the proper adjustment to remove the effect of vacancies on the labor complement? (ROMIG)

RECOMMENDATION: No. O&M expenses and payroll taxes should be reduced by $403,222 ($412,544 System) and $29,982 ($31,560 System), respectively.

POSITION OF PARTIES

GULF: Yes.

OPC: No. The labor complement adjustment is understated by $990,381. This also requires a payroll tax decrease of $78,406.

STAFF ANALYSIS: In Gulf's last rate case, the Commission made an adjustment for excessive budgeting of number of employees. In that case, Gulf budgeted for 109 additional employees assuming all would be hired for the entire year with no vacant positions.

In this proceeding, Gulf analyzed its vacant positions for the eight month period and identified that, on average, there were 42 vacant positions. Included in the 42 positions were 4 positions which were eliminated in the 1990 budget resulting in 38 vacancies. These 38 vacant positions were the basis for Gulf's adjustment reducing O&M expenses $378,000 to reflect this hiring lag. (T.642)

Public Counsel Witness Schultz has recommended an additional reduction in O&M expenses and payroll taxes of $990,381 and $78,406, respectively (T. 2438-2439). This adjustment was based on the most current information available when Mr. Schultz prepared his testimony (Brief 81). For the month ending February, 1990 there were 1,567 positions filled compared to 1,625 budgeted positions or a difference of 58 vacancies (T. 2438-2439).

In staff's opinion, the most current data available should be utilized in determining the number of vacant positions. Mr. Schultz also agrees with this position (T. 2524). Also, it is more appropriate to use an average number as being more representative than using the number of vacant positions as of a single point in time. As Mr. Gilbert stated in his rebuttal testimony, "The vacancy rate is a fairly volatile number" (T. 3887).

Gulf filed Late-Filed Exhibit No. 565 which provided the actual and budgeted number of employees for January, 1989 through May, 1990. Using this exhibit, staff calculated an average of 1,575 employees for the 12 months ended May, 1990 or an average of 50 vacancies.

The company reestimated its hiring lag adjustment on Late-Filed Exhibit No. 565 or an additional adjustment of $229,244. This revised amount considers the average salary amount used by Mr. Schultz, hiring of unbudgeted temporary employees to fill some vacant permanent positions (T. 2526) and actual salary increases for union personnel.

Late-Filed Exhibit No. 565 was the basis for staff's recommended adjustment using 50 vacant positions less the 4 positions removed from the budget by Gulf for a net average vacancy rate of 46 positions. O&M expenses and payroll taxes should be reduced $403,222 and $29,982, respectively.

ISSUE 88: The Company has included $5,340,000 in Turbine and Boiler Inspections, is further adjustment necessary? (BALLINGER)

RECOMMENDATION: No.

POSITION OF PARTIES:

GPC: No. This is a reasonable and justified expense which is necessary and beneficial to the customer, and is appropriately recovered through base rates.

OPC: Yes, based on a five year projected average of amounts supplied by Gulf, the Company will average $4,602,000 in annual expenditures for 1990 through 1994. Therefore, the Company's amount should be reduced by $738,000.

STAFF ANALYSIS: Turbine and boiler inspections are necessary to maintain the reliability and enhance the performance of generating units. Witness Lee testified that these inspections, as well as other maintenance programs, have increased the availability of Gulf's units from 83.7 to 88.7 percent. These inspections have also led to the increase in system capability of 74.9 MW. (TR 1456) All of these increases in performance have resulted in a fuel savings of approximately $67 million. (TR 1457)

For this function, Gulf exceeded the 1990 benchmark by 202,000 or approximately 4% of the benchmark amount. This is a small amount considering the cyclical nature of turbine and boiler inspections. It is also very small considering the fact that the cost of turbine and boiler inspections do not necessarily track inflation and customer growth. They are more related to the age and use of the unit. For these reasons, staff would recommend that the budgeted expense of $5,340,000 for turbine and boiler inspections is reasonable.

ISSUE 89: What, if any, adjustments should be made to the level of expenses for Plant Daniel? (BALLINGER/ROMIG)

RECOMMENDATION: None other than those specifically addressed elsewhere in this recommendation.

POSITION OF PARTIES:

GPC: None. Expenses for Plant Daniel are necessary, reasonable, and prudent.

OPC: Plant Daniel steam production costs should be reduced by $646,000 and the A & G expenses should be reduced by $1,172,000 to reflect the proper benchmark level.

STAFF ANALYSIS: Staff views this issue as a "catch all" issue. At the time of the prehearing, staff and all the parties listed specific issues and included some "catch all" issues in case some information surfaced from the outstanding discovery. There were no additional concerns after reviewing the discovery so staff would consider this issue moot.

OPC is contending that since Gulf is not involved with the actual budget preparation, it can not control costs at Plant Daniel. Gulf does review the budget for reasonableness and reviews actual vs. budgeted expenditures. (TR. 3593) Staff believes that this is a reasonable way to control costs of a facility that is outside the utility's service territory. Also, no production related A&G expenses have been recommended for disallowance as discussed in Issue 69.

ISSUE 90: Would it be proper to amortize the 1989 credit to uncollectibles, which arose due to an accounting change, above the line? (ROMIG)

RECOMMENDATION: No. The company properly accounted for the adjustment to uncollectibles and did not adversely impact Gulf's customers.

POSITION OF PARTIES

GULF: No. The change in the method of accruing for uncollectibles occurred in 1989, and the adjustment to restate the reserve balance was properly recorded in the year the accounting change was made. (Scarbrough)

OPC: Yes. Since the customers have paid for prior year uncollectibles, they should receive any credits that arose due to excess accruals. A four year amortization results in a yearly credit of $203,250.

STAFF ANALYSIS: In 1989, the company changed its method in determining the level of the bad debt accrual resulting in a $813,000 credit to expense in that year. The 1990 projected accrual is $510,852 which appears to be reasonable. No adjustment to the level of expense is proposed by staff or OPC as discussed under Issue 51.

Public Counsel stated in its brief (Pages 87-88) that the company has a history of over-accruing the reserve for bad debt. In Gulf's last case, Gulf requested an accrual of $823,000 which was reduced by $300,000 by the Commission for a net allowance of $523,000. In Gulf's 1983 case, the company's actual accrual was $269,109 less than allowed by the Commission in that case.

Since the last full rate case, Gulf has overaccrued its reserve for uncollectibles by accruing $782,670 each year (T. 3799). Public Counsel's position is that any over charges have overstated expenses in its surveillance reports and tax refund dockets.

The company has changed its method in calculating the accrual for bad debt because it was determined that the reserve for uncollectibles was overfunded (T. 353-355). Accordingly, OPC Witness Schultz has recommended that the $813,000 adjustment be amortized over four years, or a reduction in expenses of $203,250, on the basis that the customer has been overcharged over a period of years.

Gulf stated in its brief (Pages 265-266) that it is necessary to estimate how much of the company's revenues for a particular year will be uncollectible in setting the reserves for bad debt (T. 358-359). Gulf determined that its accrual for bad debts had been excessive and as a result, changed its method of accruing for uncollectibles, resulting in a $813,000 reduction to expenses in 1989.

During cross examination, OPC Witness Schultz was asked if he had compared the amount collected from the customers since the company's rates were placed into effect to the net write-offs. His response was no (T. 2606). Mr. Schultz was further asked that if Gulf had actually written off more than recovered from the customers would his position be the same. His response - "I'd have to rethink my position."

Based on Staff Exhibit 155, it can be determined that Gulf has recovered $2,615,223 from its customers for 1985-1988 through base rates or the tax savings docket. For this same period, Gulf's net write-offs were $2,666,197 which were in excess of the amounts recovered from its customers. In addition, the $812,000 credit to expense will be considered in the "1989" Tax Savings Docket (T. 3859). Therefore, staff recommends no adjustment in this proceeding.

ISSUE 91: Should an adjustment be made to remove part or all of the costs associated with the employee savings plan? (MERTA)

RECOMMENDATION: No adjustment should be made for the Employee Savings Plan.

POSITION OF PARTIES

GULF: No. The Employee Savings Plan is a reasonable and integral component of Gulf's overall salary and benefits program which is necessary to enable the Company to attract and retain well qualified, highly motivated and talented employees. (Jackson)

OPC: Public Counsel did not address this issue in their Brief.

STAFF ANALYSIS: No party has recommended any adjustment to the expenses associated with the Employee Savings Plan. Gulf's 1990 contribution to the Employee Savings Plan (Plan) is budgeted at $1,398,500. This is approximately 6.9% over the benchmark for the Plan. (TR 3979).

The Employee Savings Plan is part of Gulf's overall salary and benefits program and enables the Company to attract and retain well qualified, highly motivated and talented employees. The plan was implemented to encourage employee ownership in the company and to supplement retirement income. The Company's witnesses testified that Gulf's base salaries are below the market median for total direct compensation. (TR 3966). Incentive Plans such as the Productivity Improvement Plan and Performance Pay Plan and benefits such as the Employee Savings Plan enable Gulf's employees to partially make up this difference. (TR 3974).

A 1989 EEI Benefits Survey, the Benval Report, indicated that 94% of the 130 companies surveyed had comparable savings plans. (TR 3974). However, Gulf Witness Jackson did not know whether these plans were allowed in rates by their respective Public Service Commissions. (TR 3980).

Public Counsel did not recommend an adjustment for the Plan but did suggest that the Commission consider placing a cap on the costs in light of the numerous benefits received by Gulf employees. (TR 2468).

In Florida Power and Light Company's last rate case, the Commission disallowed the amount over the benchmark for their Thrift Savings Plan. (Order No. 13537). However, in Gulf's 1984 rate case the Employee Savings Plan expenses were fully allowed.

Based on the above, Staff recommends no adjustment for Gulf's Employee Savings Plan.

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ISSUE 92: Should the Commission remove all or part of the costs of the Productivity Improvement Plan (PIP)? (REVELL)

RECOMMENDATION: Yes. The O&M expenses of this plan should be reduced by $339,407 ($358,209 System). This adjustment reduces Accounts Payable thereby increasing Working Capital. Working capital should be increased by $169,187 ($179,105 System). Expenses of $99,066 ($105,968 System) should be allowed for this program.

POSITION OF PARTIES

GULF: Yes. Gulf has changed its PIP program. Expenses should be reduced $339,407 ($358,209 System). The PIP program is a reasonable and integral component of Gulf's overall salary and benefits program designed to enable the Company to attract and retain well qualified, highly motivated employees. (Jackson)

OPC: Yes. The entire $464,177 should be removed from test year expenses. (Schultz)

STAFF ANALYSIS: The Productivity Improvement Plan (PIP) is a part of the total compensation plan for the top 11 employees of the company. There are two components to this plan. There is an individual component which can be directly influenced by the hands-on performance of an individual and there is a corporate component which is paid to these individuals if Gulf and the Southern Company exceed predetermined corporate goals on the preceding four years average return. Public Counsel in its brief (p. 89) states that "since this plan is based on Southern Company's return on equity..., this plan is nothing more than an above-the-line profit sharing incentive that should be below-the-line where it belongs."

Staff believes, however, that this is a very narrow focus on the issue. Rather, the focus should be on the overall compensation and benefits package of Gulf and whether it is sufficient to attract and retain quality employees, or if the overall package is excessive and certain expenses should be disallowed.

Gulf has the philosophy to pay employees at the 75th percentile level [T-3967]. To only receive a base salary would mean Gulf employees would be compensated at a lower level than other companies who were in competition with Gulf for employees [T-3966]. Gulf has stated that this program is not in addition to a full competitive salary for the qualifying employees, but that it makes it possible if the incentive payment is paid to achieve close to, but still shy of the 75th percentile goal [T-3967]. One other benefit noted by the company is that these payments are not automatic; these payments represent a variable cost not a fixed cost on a year to year basis.

Due to a change in the design of the PIP program after the budgeting process was completed, the company feels a reduction in the program is in order. The original amount for this program was $438,473 ($464,177 System). The company's new amount is $99,066 ($105,968 System). Since it appears that Gulf's overall salary and benefits program is not excessive, and this plan was allowed in the last rate case, staff recommends that the expenses in the amount of $99,066 ($105,968 System) for this program continue to be allowed for ratemaking purposes.

Since this plan reduction represents a reduction in Accounts Payable, a current liability in working capital, the 13-month average of working capital should be increased by $169,187 ($179,105 System)

ISSUE 93: What amount of the Performance Pay Plan should be approved for retail recovery? (REVELL)

RECOMMENDATION: O&M expenses totalling $1,021,637 for the Performance Pay Plan should be allowed.

POSITION OF PARTIES

GULF: All expenses associated with PPP should be allowed. It is reasonable to put part of an employee's pay at risk and it increases management's control of overall salary expense. The PPP program is a reasonable and integral component of Gulf's overall salary and benefits program designed to enable the Company to attract and retain well qualified, highly motivated employees. (Jackson)

OPC: None of this amount is appropriate for recovery in retail rates. Remove $1,021,637. (Schultz)

STAFF ANALYSIS: The Performance Pay Plan (PPP) is similar to the PIP plan discussed in Issue 92. PPP is for all non-union employees except the highest level of management which is eligible for the PIP plan. This plan also places at risk a portion of the available compensation for these employees. Mr. Johnson points out that 68% of 71 utilities surveyed have implemented such a plan [T-3969].

Gulf has the philosophy to pay employees at the 75th percentile. [T-3967] To only receive a base salary would mean Gulf employees would be compensated at a lower level than other companies who were in competition with Gulf for employees [T-3966]. One benefit of this plan is that this portion of compensation is not automatic; these payments represent a variable cost not a fixed cost on a year to year basis.

In any event, Gulf's overall compensation even with the addition of the PPP component, does not appear excessive. In Issue 50, the issue most directly related to base salaries, the Public Counsel does not take exception to salary levels, only fringe benefit levels (also see PC brief, p. 64). However, in a 1989 survey comparing overall benefits, the Edison Electric Institute found that Gulf was "... well below the population mean when considering those benefits paid for by the ratepayer." [T-3978]

As stated in other issues by staff, the focus should be on the overall compensation package of Gulf's employees, not the individual components unless there is evidence that a particular component is out of line with other companies of similar size. The Performance Pay Plan appears to be a part of overall compensation of many companies in private industry as noted above. It should be noted that unlike the PIP component of benefits for upper management, which was approved in Gulf's last rate case, this plan is new within the last one or two years. However, it allows all non-union employees the same opportunity as top management to improve productivity and cut costs.

Therefore, staff recommends that all expenses projected for the Performance Pay Plan, $1,021,637, be approved for retail recovery.

ISSUE 94: What amount of the $326,808 for EPRI nuclear research should be included for setting retail rates? (BALLINGER)

RECOMMENDATION: None.

POSITION OF PARTIES:

GPC: All of the $326,808 system ($309,654 jurisdictional) budgeted in the test year for EPRI nuclear research is reasonable and should be included in base rates.

OPC: The entire amount should be removed from expenses.

STAFF ANALYSIS: Staff is mainly concerned with the amount of expenses associated with nuclear research as opposed to the entire amount of EPRI dues. The expense in this function represents approximately 20% of the total EPRI dues and Gulf doesn't own a nuclear plant. While it may be true that research may lead to benefits to the Southern system, who has ownership in nuclear facilities, there was no evidence introduced as to the sharing of costs among the operating companies. For all staff knows, Gulf is picking up the tab for all the operating companies in the area of nuclear research. Staff believes that Gulf has not fully justified this expense and would recommend that this expense not be allowed in base rates.

ISSUE 95: Should an adjustment be made to the Plant Smith ash hauling expenses? (BALLINGER)

RECOMMENDATION: No. These expenses are necessary to increase the ash disposal capacity at Plant Smith.

POSITION OF PARTIES:

GPC: No. This is a justified expense which is necessary and beneficial to the customer.

OPC: Yes. This expense is overstated by $360,000.

STAFF ANALYSIS: The need for additional ash disposal capacity at Plant Smith was identified in 1982. Final approval for the construction of a new landfill was obtained in 1985. The construction and capping of the new landfill are capital expenditures but the digging and hauling of ash from Plant Smith to the landfill are O&M expenses. These expenses were first incurred in 1986 and will continue annually and staff would recommend that this expense be allowed in base rates. (TR 1431-1432)

ISSUE 96: What adjustment, if any, should be made to the Company's Employee Relations budget associated with the relocation and development programs? (REVELL)

RECOMMENDATION: No adjustment should be made for the employee development program, however a reduction of $55,988 should be made in expenses associated with the employee relocation program.

POSITION OF PARTIES

GULF: No employee relocation expense adjustment is warranted. The Company budgets a reasonable amount of funds in order to allow management to put the most qualified person in vacant positions. (Jackson)

OPC: The development program costs of $72,250 should be removed as well as the $172,460 in costs associated with selling homes of relocated employees. (Schultz)

STAFF ANALYSIS: (1) The executive development program is designed to keep upper level employees "up to date on issues affecting the business world." [T-3975] Most companies have some sort of training or development program for its employees. Some examples of courses offered include a 2-week Corporate Financial Management Program at Harvard University, sessions on employment benefits issues, and the PUR Utility Management Program.

Public Counsel has stated that these expenses should be disallowed unless they are justified through a cost benefit analysis. [T-2481] Unfortunately, the benefits of programs such as these probably cannot be quantified. However, one result certainly is that employees gain a greater understanding of the business world and know that the company is interested enough in them and their career to fund this program. We therefore recommend no reduction in allowed expenses for this program.

(2) Staff also disagrees with Public Counsel's Witness Schultz on the overall necessity of the employee relocation program. As the Public Counsel's brief stated, "The question here is not should relocation costs be recoverable through rates but rather how much should be paid." Staff could not agree more; however, unlike Mr. Schultz, we do not recommend disallowing all relocation costs.

Mr. Schultz is under the mistaken impression that relocation costs only consist of realtor commissions for selling transferred employees' homes. [T-2480] The total requested amount for the 1990 test year is $324,100. Witness Schultz states that part of this cost, 22%, relates to the costs incurred in selling employees homes. [T-2480] This 22% equals $71,300. However, Mr. Schultz justifies his recommended disallowance by dividing the entire $324,100 by the expected 10 transferees in 1990 to say that the average cost per transfer is $32,410, "...well in excess of any fees charged by a realtor for selling a home." [T-2480] The correct amount using his argument is $7,130 per home. In any event, this amount is a "fee" rather than just a selling commission and covers a variety of items such as appraisals, inspections, insurance, closing costs, mortgage costs, and brokers expenses. [T-3970] The remainder of the relocation budget covers the employee and the employee's family's moving expenses and living costs until a new home is bought.

The relocation budget approved in the 1984 rate case was an unrealistically low $50,000. Even if Gulf is held to the position that the benchmark approved in 1984 and subsequent adjustments will be blindly followed, even if a mistake in budgeting is acknowledged, this category of expense is one in which year to year changes are in most cases impossible to forecast. It is not possible up to 1 1/2 years in advance to know what positions will become vacant and who will be chosen to fill these vacant positions. Relocation expenses cannot be neatly extrapolated by year to year percentages like salary expenses or plant maintenance can be, because relocation expenses show wide variations from year to year as can be seen from the yearly amounts listed below:

Year	Actual Amount
1984	$263,066
1985	121,536
1986	113,552
1987	285,361
1988	205,287
1989	468,246
1990 (budget proj.)	324,100

The large amount for 1989 was primarily due to the company reorganization.

Staff believes strongly that Gulf should not be penalized for budgeting errors six years ago. However, while admitting that predicting the 1990 actual expenses is impossible, we believe that $324,100 is too high considering the fact that it follows a year of extensive changes which are unlikely to reoccur anytime soon. We believe a more reasonable approach is to allow an amount which is equal to the 1986-1989 average yearly expense for relocation. This average equals $268,112. We recommend therefore that Gulf's 1990 budget for relocation expense be reduced by $55,988 from $324,100 to $268,112.

ISSUE 97: Should an adjustment be made to reduce the level of obsolete material to be written off in the test year? (WILKERSON)

RECOMMENDATION: No adjustment is necessary.

POSITION OF PARTIES:

GULF: No.

OFFICE OF PUBLIC COUNSEL: Yes. The Company has included a write off for distribution material of $109,000; this should be reduced by $83,000.

INDUSTRIAL INTERVENORS: No position.

STAFF ANALYSIS: Public Counsel witness Schultz took the position that $83,000 of write off should be removed as that is "the amount in excess of the benchmark which the Company has not justified" (Tr. p. 2483). Further, he says that this may be an indication that the Company "over-purchased or imprudently purchased such items in the past"; this may be true, but there is nothing in the record to support the assumption. Gulf witness Jordan (Tr. pp. 3611-3614) discusses the Company's efforts to identify and reduce unnecessary inventory, and the change "from the former practice of writing-off obsolete materials initially to the FERC 163 Clearing Account to the current practice of writing these materials off directly to the proper O&M Accounts." He then goes on to show that the projected 1990 Budget amount is in line with the average of the last five years.

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ISSUE 98: How much if any, of the officer and management "perks" for tax services and fitness programs should be borne by the ratepayers? (MERTA)

RECOMMENDATION: Gulf's ratepayers should not pay for tax services and fitness programs for executives. These expenses should be borne by the stockholders. Expenses should be reduced by $65,100.

POSITION OF PARTIES

GULF: Both the tax services program and the fitness program are reasonable and integral components of Gulf's overall salary and benefits program and are designed to enable the company to attract and retain well qualified, highly motivated and talented employees. Both of these programs are beneficial to the ratepayers and thus are appropriate for recovery through base rates.

OPC: Both of these items should be removed. Reduce expenses by $65,000. (Schultz)

STAFF ANALYSIS: Gulf has budgeted $6,600 for personal tax services for its executives and vice presidents. In addition, the Company has budgeted $58,500 for a fitness program available to only 167 employees from supervisors through executives. The Company stated that these programs are typical employee benefits and necessary components of the Company's total salary and benefits package and allow Gulf to compete for qualified top management employees in a market in which such services are routinely offered to executives. (Gulf Brief p. 286).

Gulf Witness Scarbrough testified that the tax program relieves executives of the responsibility of preparing complicated tax returns and ensures that the returns are correctly prepared thereby avoiding the wasted time and distractions associated with Internal Revenue Service inquires. (TR 3811).

The Company budgeted $5,000 for Arthur Anderson & Co. to provide tax services to Gulf's President and an additional $1,600 for a local CPA firm to provide services to the four vice presidents. Gulf budgeted $400 per vice president with a $1,500 cap per individual. There is no cap on the amount of tax services Arthur Anderson can provide to the President. (TR 3861-3861). The services provided by Arthur Anderson may include income tax return preparation, tax planning, representation at IRS audits and preparation of personal financial statements. The vice presidents are only eligible for income tax return preparation. (TR 3860- 3861).

Gulf Witness Jackson testified that the fitness program was fully allowed in Gulf's last rate case. (TR 3980). The program has been effective in reducing employee time off due to illness, producing an average of 2.69 days per year less in sick days for participating employees as compared to nonparticipating employees. (TR 3972).

In Order No. 7843, Docket No. 760727-EU, Florida Power & Light Company's 1976 rate case, the Commission disallowed expenses for tax planning services. The Commission stated:

> ...This type of expenditure is not an employee benefit that is normally incurred in the everyday course of business, and is not, in our opinion, the type of benefit that should be paid for by the ratepayers. The benefits of this plan are enjoyed only by a few key employees of the company. Furthermore, the company did not adequately show that the dollars spent on this service actually increased the productivity of the employees who used the service. Therefore, we are disallowing the entire expenditure....

Staff believes that the tax services and the fitness program provided Gulf executives should be disallowed for the same reasons the Commission disallowed FPL's tax planning services. Tax services and fitness programs are not the type of employee benefit normally incurred in the everyday course of business. These "perks" are provided to a few top executives and are not available to other employees. Other large corporations may provide these type benefits to their executives and Gulf may wish to continue their programs, but Gulf's stockholders should bear the costs just as the stockholders bear these costs in the large corporations.

The company did not convince staff that the dollars spent on these benefits increased the productivity of the employees who participate. If Gulf did not provide tax services, staff doubts the executives would personally prepare and "make inadvertent errors on complicated tax returns which would take them away from their work to respond to Internal Revenue Service questions."

Even though expenses related to the fitness program were not disallowed in the last rate case, staff has found no evidence that they were specifically identified and analyzed. In addition, the argument regarding the reduction in employee time off due to illness is not convincing since Gulf Witness Jackson testified that upper level employees normally take less time off due to illness than the remainder of the company. (TR 3981-3982) Mr. Jackson testified that the fitness program was designed to provide an exercise program, physical examinations, health counseling, and a facility in which executives could work out. He defined active participants in the fitness program as "People who receive their annual physical, the counseling, and any other tests that are prescribed in that program." (TR 3980-3981) In staff's opinion, these are services best provided by personal physicians, HMOs, or similar health care providers not by a fitness center.

Based on the above, staff recommends the expenses be reduced by $6,000 for the tax services program and $58,500 for the fitness program for a total disallowance of $65,100.

ISSUE 99: The Company has projected $1,109,000 for duct and fan repairs for the test year. Should an adjustment be made to this level? (BALLINGER)

RECOMMENDATION: No.

POSITION OF PARTIES:

GPC: No. This is a justified expense which is necessary and beneficial to the customer.

OPC: Yes. In Exhibit 312, Mr. Schultz calculated the average for this cost over the period 1984 thorugh 1989. His average of $833,914 shows that the test year amount is not representative and should be reduced by $275,086 [T.2485].

STAFF ANALYSIS: As discussed in Issue 88, this regular maintenance program, as well as other programs, has increased the efficiency of Gulf's power plants. Duct and fan repairs are a normal part of power plant maintenance and are determined more by the age and use of the unit than by customer growth or inflation. This maintenance practice also contributes to fuel savings which offset the cost of the program and would flow directly to Gulf's ratepayers through the fuel adjustment clause.

Since this program is a necessary component of regular maintenance and will result in fuel savings and enhance reliability, staff would recommend that this expense is reasonable.

ISSUE 100: Should an adjustment be made to the Customer Services and Information benchmark? (BALLINGER)

RECOMMENDATION: This is a summary issue and no other adjustments should be made that have not been specifically addressed in this recommendation.

POSITION OF PARTIES

GPC: No. The expenses identified in Mr. Schultz' Schedule HWS-13 (Exhibit 314) relating to "Essential Customer Service" (items 16, 17, 20, 21, 24, and 25), amounting to $626,135 are being addressed in Issue 64. This could result in double disallowance. Items 11 and 12 ($226,883) consist of expenses related to Issue 61. (Industrial Activities) The remaining NON_ECCR expenses of $399,006 are related to Residential and Commercial Technology Transfer.

OPC: Yes. Conservation costs not allowed for ECCR recovery should be disallowed in base rates also. Reduce expenses by $1,207,237.

STAFF ANALYSIS: At the time of the prehearing, this issue was raised as a "catch all" issue that may surface from the information contained in outstanding discovery. The only additional issue that was raised was by Public Counsel with regard to the Technology Transfer program. The Company has budgeted $399,006 for this program which provides information on emerging technologies to trade allies. By participating in the Technology Transfer program, Gulf's customers benefit by receiving information on the latest technologies. This program will also help Gulf in its forecasting efforts as these new technologies become commercially available. Therefore, staff would recommend that no other adjustments be made to the Customer Services and Information benchmark.

ISSUE 101: The Company has included expenses for marketing in the test year. Should an adjustment be made to remove this cost? (BALLINGER)

RECOMMENDATION: No.

POSITION OF PARTIES:

GPC: No. The expenses detailed in Items 9-18 (Totalling $685,500) on Mr. Shultz' schedule HWS-14 are contained in Issue no. 68. These are expenses related to the Company's Economic Development program. Items 1 and 2 (totalling $108,510) are administrative and general expenses related to personnel administration program performance documentation and expense budgeting. These expenses ($108,510) are necessary for the proper management of the Company's marketing resources. Items 3 and 4 ($50,665) are the same expenses as those related to Issue 61. Items 508 ($303,814) are expenses incurred in the development of the Company's load forecasts, economic analysis and market and load research activities. All of these activities are critical in providing the basis for sound business decisions which result in reliable, low cost service to Gulf's customers.

OPC: Yes. The identifiable level of marketing expense which should be removed is $303,814.

STAFF ANALYSIS: Again, this was a "catch all" issue raised by Public Counsel. Of all the expenses listed by Public Counsel, only the $303,814 budgeted for the load forecasts and load research activities were not identified in other issues.

The load forecats and research activities of a utility are the foundation for virtually every aspect of the utility's business. Generation, transmission, and distribution planning all require load forecasts and market research. Also, many PSC requirements are based on the load forecast of the Company. This information is also used to develop conservation programs. For these reasons, staff would recommend that the expenses associated with marketing should not be adjusted any further than where specifically discussed elsewhere in this recommendation.

ISSUE 102: What adjustments are necessary to reflect a proper benchmark test of expense levels? (BALLINGER)

RECOMMENDATION: No other adjustments than those previously mentioned are needed.

POSITION OF PARTIES:

GPC: This issue relates to the calculation of the benchmark itself, and not to whether any expenses should be disallowed due to inadequate justification of excesses over the benchmark. In calculating the benchmark, the Company made adjustments to the base in connection with three functional areas: Production related A & G, Customer Service and Information, and Plant Daniel Transmission facility charges (line rentals). These adjustments are reasonable and appropriate and should be approved. No other adjustments are necessary.

OPC: The following expenses have not been adequately explained or verified in the Company's benchmark analysis and should be reduced accordingly.

a.	Plant Crist-condensing & cooling proj.	$ 289,000
b.	Distrib.-work order clearance	$ 418,154
c.	Distrib.-underground line extensions	$ 351,000
d.	Distrib.-network protectors	$ 90,000
e.	Electric & Magnetic fields study	$ 39,000
f.	Acid rain monitoring	$ 43,000
		$ 1,230,154

STAFF ANALYSIS: This issue is intended to address the actual calculation of the benchmark level, not the budgeted variance justification. Public Counsel has used this issue to try and address other items that should have been separate issues. Public Counsel's concerns over the EMF studies and the Acid Rain monitoring should be addressed in Issue 77, research and devlopment projects. The other four areas of concern should be addressed in Issue 30 and Issue 103 which is a summary issue for the entire O&M expense catagory.

The adjustments in question are to Production related A&G, Customer Services and Information, and Plant Daniel transmission rents. These adjustments are discussed in issues 61 through 67, 69, 80, 100, and 101. There were no other areas of the benchmark calculation that require adjustment to reflect prior Commission action and therefore, staff would recommend that no further adjustments to the calculation of the 1990 benchmark are necessary.

ISSUE 103: Gulf has budgeted $129,712,291 for O&M expenses. Is this amount appropriate? (BALLINGER/ROMIG)

RECOMMENDATION: The proper level of O&M expenses should be $110,213,000. This is a fall out issue from other previous issues.

POSITION OF PARTIES:

GULF: Yes.

OPC: This is a fall-out issue and will be provided with separately filed schedules.

STAFF ANALYSIS: See staff discussion for Issues 46 through 102. Public Counsel also raised four areas of concern in Issue 102 which should be addressed in this issue. The first of these concerns is the benchmark variance associated with the cooling tower and condenser corrosion maintenance at Plant Crist. Gulf's justification was the variance was caused by an increase in the cost of chemicals needed to reduce corrosion of condenser tubes. This prevention is important because it increases the availability of the unit and saves fuel dollars. Gulf contends that the costs increased for two reasons, increased generation and inflation of chemical cost. Increased generation will cause the consumption of chemicals to increase and the actual cost of the chemical used has increased approximately 74% since 1984. Therefore, staff would recommend that the expense budgeted for cooling tower and condenser corrosion maintenance is reasonable. (TR 1433, Exhibit 541)

The second area of concern raised by Public Counsel is the expense associated with distribution work order clearances (DSO's). Gulf's justification for the variance is that following an evaluation of their distribution accounting practices, they were better able to identify and separate cost to plant and O&M functions. This was done in 1985 and resulted in the increase of expense in this catagory by 61%. While the overall cost of the total function did not increase much, the allocation to O&M increased significantly. This justification seems reasonable and staff would recommend that this expense item be included in base rates. (TR 3609-3611)

Public Counsel also took issue with the benchmark variance for underground line extensions. This expense is for the maintenance of underground lines, not the installation. Gulf's justification for the variance is the fact that maintenance costs on underground lines has increased as well as the demand for underground lines. In fact, the amount of underground wiring in Gulf's service area has increased approximately 67% since 1984. This is well above the rate of customer growth and staff would recommend that this variance is reasonable. (TR 3607-3609)

Lastly, Public Counsel takes issue with the repair of the underground network system in Pensacola. They don't take issue with the actual expense, only the treatment of the item. This is the subject of Issue 30. Therefore, this item should be discussed in that issue.

Issue 104: Was the production and promotion of the appliance video known as "Top Gun" contrary to the Commission's policy regarding fuel neutrality? (BALLINGER)

Recommendation: Yes.

POSITION OF PARTIES:

GULF: Gulf does not believe that it was. Any violation was unintentional. There are no dollars associated with any activity of this kind included in the 1990 test year expenses. Therefore, this issue is irrelevant. Moreover, it was Gulf's understanding at the time that the fuel source neutrality policy, as espoused by the Commission, was applicable to incentives (rebates) recovered through the conservation cost recovery mechanism. This event occurred in 1987. The controversial portion of the video constituted approximately 6 seconds. The remaining almost seven minutes was dedicated to the promotion of energy efficient homes. Gulf's intent with respect to the video, as with all of our promotion efforts, is to provide information and technical expertise to customers on the most energy efficient application for their particular circumstance. Ours and the Commission's philosophies are identical--the best interest of the customers. The video was intended to be shown only one time, at a seminar to less than 200 people. Since that time, Gulf's management has on a number of occasions acknowledged that the controversial portion of the video was an inappropriate response to the promotional efforts of other energy suppliers.

OPC: Yes.

STAFF ANALYSIS: While there are no expenses associated with this item in the test year, Issues 104 through 108 serve to show several instances of Gulf's disregard for the Commission's policy on fuel source neutrality. The video was produced in 1987 and shown to a group of contractors and builders at Gulf's annual awards seminar. Portions of the video show fighter aircraft shooting gas appliances out of the air and indicates that you too, meaning the contractors, could be a top gun in your area. Even though this portion of the video was short in duration, one has to wonder at the overall intent of not only the video but Gulf's entire seminar presentations.

The fuel neutrality policy can be summarized best by saying a utility does not have to mention the competitive fuel, they just shouldn't put it in a bad light. These policy objectives were the content of Orders 9974 and 12179 which were issued in 1981 and 1983 respectively. However, witness Bowers stated that Gulf interpreted these orders in such a way that these items would not violate the principle of the orders. (TR 956-957) This video was blatant in its message that Gulf's intent with its contractor programs is to promote electricity and displace gas.

The production and distribution of this video are also indicators of Gulf's managerial view towards the Commission's policy on fuel source neutrality. Gulf has also admitted that this, and other actions, may have been inappropriate but that they will not happen in the future. (TR 4045-4046) It is staff's opinion that Gulf is requesting that the Commission disregard the basic premise of regulation which is after the fact review of the Company's actions. The production and distribution of this video were presumably approved by Gulf's management and they should be held accountable for this action. As Commissioner Gunter pointed out, if utilities are going to innovatively read orders to fit what you might want to do, why do we waste our time voting and having attorneys writing orders. (TR 957-958)

ISSUE 105: Was the production and distribution of tee-shirts with the "Gas Busters" symbol contrary to the Commission's policy regarding fuel neutrality? (BALLINGER)

RECOMMENDATION: Yes.

POSITION OF PARTIES:

GULF: Gulf does not believe that it was. Any violation was unintentional. There are no dollars associated with any activity of this kind included in the 1990 test year expenses. Therefore, this issue is irrelevant. Moreover, it was Gulf's understanding at the time that the fuel source neutrality policy, as espoused by the Commission, was applicable to incentives (rebates) recovered through the conservation cost recovery mechanism. This event occurred in 1985 and since that time, Gulf's management has on a number of occasions acknowledged that, in hindsight, the shirts were an inappropriate response to the promotional efforts of other energy suppliers.

OPC: Yes.

STAFF ANALYSIS: A total of 559 of the tee-shirts in question were distributed in 1985 to Gulf Power employees. In respone to Staff Interrogatory #88, Gulf states that "[t]he shirts were made available to employees who wanted them during a series of meetings during 1985 and were intended to explain and gain commitment to the Company's strategic marketing plan, titled EMPACT (EMPloyee ACTion). The shirts themselves were an inappropriate reaction to the promotional efforts of other energy suppliers that was very much in the public focus during this timeframe". (Exhibit 443) Again, Gulf is asking that the Commission forgive and forget their fuel neutrality policy. For more details on this, see staff analysis contained in Issue 104.

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ISSUE 106: Was the incentive program known as "Good Cents Incentive" which utilized electropoints that were redeemable for trips, awards, and merchandise contrary to the Commission's policy regarding fuel neutrality? (BALLINGER)

RECOMMENDATION: Yes.

POSITION OF PARTIES:

GULF: No. This issue duplicates Issue No. 62. This promotional tool is source neutral as it is available to any contractor who wishes to participate and has resulted in increased numbers of energy efficient homes in Northwest Florida.

OPC: Yes. These costs should not be included for recovery.

STAFF ANALYSIS: This issue is intended to address the Good Cents Incentive programs that were in existence during 1987 through 1989. These programs were specifically tailored to award contractors, in some manner, for the replacement of gas furnaces with heat pumps. The contractors were paid anywhere from $25 to $100, in cash or merchandise, for each installation. See Exhibit 171.

Gulf seems to be unsure of which arguement it wants to sponsor. On one hand, the Company contends that the "Top Gun" video and the Gas Buster T-shirts were O.K. because the Commissions fuel neutrality policy was interpreted to apply to rebates and incentives. (pps 308,312, and 315 of Gulf's brief, TR 958-959) On the other hand, the Company contends that the Good Cents Incentive programs resulted in more efficient homes being built in the panhandle. These programs not only provided incentives for the replacement of gas heat but also increased the Company's winter peak demand and annual energy. (Exhibit 171, TR 932) Staff is of the opinion that a promotion of energy sales and an increase in demand is contrary to FEECA. When asked what the distinction was between these old Good Cents Incentive programs and the one proposed for the test year, witness Bowers stated that there is no distinction on fuel source and the related points attributable to a changeout. (TR 933) This can only mean that the old progreams did have a distinction with regard to fuel source and promoted electric over gas appliances.

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Issue 107: In 1987, a commercial building received energy awards from both the U.S. Department of Energy and the Governor's Energy Office yet did not receive Good Cents certification because of a small amount of backup gas power. Was this practice contrary to the Commission's policy regarding fuel neutrality? (BALLINGER)

Recommendation: Yes.

POSITION OF PARTIES:

GULF: No. As originally conceived, the Commission's fuel source neutrality policy only applied to incentives paid through the conservation cost recovery mechanism. Gulf's program, as originally approved by the Commission, required a building to be all electric in order to receive Good Cents certification. The building referred to was built in 1984; Gulf's standards were revised in 1986, and now allow certification of buildings utilizing natural gas.

OPC: Yes.

STAFF ANALYSIS: The referenced building was completed in 1985. At that time, Gulf's Good Cents commercial program required that a building receive all of its energy from Gulf Power. This program was approved by the Commission in 1981. However, in 1986, this program was revised to remove the restriction of energy supplier at the staff's request. This request was primarily the result of the Company's EMPACT program which also had the Gas Buster T-shirts. The EMPACT program was in effect during the 1984-85 timeframe. While the Company was following its approved program guidelines at the time, staff has to question why those guidelines were included by the Company in the first place.

Another troublesome area for staff is why the building wasn't certified after the gas restrictions were removed from the program? Gulf has contended all along that the Good Cents logo is synonymous with energy efficiency. Why then wouldn't a highly efficient building that received other awards be granted Good Cents certification? It seems as though Gulf is not practicing what it preaches, the promotion of the most energy efficient building for its ratepayers.

ISSUE 108: Has Gulf participated in misleading advertising in order to gain a competitive edge on gas usage? (BALLINGER)

RECOMMENDATION: Yes.

POSITION OF PARTIES:

GULF: No. There is no advertising of the nature which this issue addresses contained in the 1990 budget. This issue is therefore irrelevant. The ads which this issue is apparently intended to address were in response to natural gas company advertising which misled Gulf's customers by overstating the cost of electric service in a Good Cents Home. Gulf's ads were implemented in response to the inaccurate gas company ads. Gulf is not attempting to gain a competitive edge on gas usage through use of advertisements. The Company does have a desire to present the truth to its customers.

OPC: Yes.

STAFF ANALYSIS: A sampling of the advertisements in question are contained in Exhibit 447. When cross examined by staff, witness Bowers agreed that the savings stated in the ads are not derived from identical homes. (TR 948-952) In fact, the homes had different levels of insulation and sizes of equipment. Both of these attributes will affect the energy usage of the home that is modeled, yet the advertisements did not mention this fact. Staff is of the opinion that if the general public were to read these ads, they would believe that the homes were identical. This is misleading to Gulf's general body of ratepayers.

The Company's justification for these ads is that they were responding to advertising by local gas companies that Gulf thought was misleading. Staff does not find this justification acceptable because the Commission can not control the actions of unregulated companies and even if we could, two wrongs do not make a right.

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STIPULATED
ISSUE 109: What is the appropriate revenue expansion factor for 1990? (ROMIG)

RECOMMENDATION: The appropiate expansion factor for the 1990 test year is 1.631699.

POSITION OF PARTIES

GULF: The Revenue Expansion factor is 61.2858 percent and the NOI multiplier is 1.631699.

OPC: .612858. (NOI Mult. = 1.631699). This should be adjusted for any change in the bad debt allowance.

STAFF ANALYSIS: All parties agreed that the revenue expansion factor is 61.2858 percent and the N.O.I. multiplier is 1.631699 adjusted for any change in the bad debt expense allowance.

Since no adjustments were proposed to the level of bad debt expense, no revision is necessary in the above recommended expansion factor.

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ISSUE 110: Gulf has requested an annual operating revenue increase of $26,295,000. Is this appropriate? (MERTA)

RECOMMENDATION: The appropriate jurisdictional amount is $14,577,000.

POSITION OF PARTIES

GULF: Yes.

OPC: ($15,164,000) is the amount provided by OPC in their schedule.

STAFF ANALYSIS: This issue falls out from the resolution of all the other issues. The following schedule shows the parties' positions.

Calculation of Revenue Requirements
(000's)
December 31, 1990 Test Year

	COMPANY	STAFF	PUBLIC COUNSEL
Rate Base	$923,562	$915,892	$843,931
Rate of Return	8.34%	8.05%	7.90%
Required NOI	77,025	73,708	66,671
Adj. Achieved NOI	60,910	63,290	70,394
NOI Deficiency	16,115	10,417	(3,723)
Rev. Expansion Fac.	1.631699	1.631699	1.631699
Revenue Inc./Dec.	26,295	16,998	(6,076)
ROE Reduction	0	(2,420)	(9,088)
Total Rev. Inc./Dec.	$26,295	$14,577	$(15,164)

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ISSUE 111: Should any portion of the $5,751,000 interim increase granted by Order No. 22681 issued on 3-13-90 be refunded? (MERTA)

RECOMMENDATION: Yes. $2,693,000 should be refunded on an annual basis since the 8.05% overall rate of return recommended by staff is less than the 8.26% used in calculating the interim increase. The $2,693,000 is an annual amount and does not represent the actual amount to be refunded.

POSITION OF PARTIES

GULF: No. The Company's requested rate relief of $26,295,000 is appropriate and since the interim relief granted is less than the appropriate permanent relief, all interim amounts collected are properly retained by the company.

OPC: Yes, the entire amount should be refunded.

STAFF ANALYSIS: Order No. 22681 issued on March 13, 1990, granted Gulf an interim rate increase of $5,751,000 pursuant to Section 366.071, Florida Statutes. The interim increase was calculated based on a December 31, 1990 test year which is the same test year used in the permanent case. The Commission approved the interim rate increase for collection, subject to refund, pending the outcome of further evaluation of the Company's request for permanent rates. Now that the evaluation is complete, the question as to the appropriate level of interim relief must be addressed.

The Company based its refund position on total dollars and stated in its Brief that no refund is necessary since the interim relief granted ($5,751,000) is less than the appropriate permanent relief ($26,295,00).

In the most recent electric rate case, FPUC-Fernandina Beach Division, Order No. 22224, Docket No. 881056-EI, the Commission based its refund on the rate of return and stated:

> ...In general, a refund should be ordered if it is necessary to reduce the rate of return during the pendency of the proceeding to the same level within the range of the newly authorized rate of return which is found fair and reasonable on a prospective basis, as is provided by Chapter 366,071, Florida Statutes.
>
> In this docket, the interim increase of $456,195 was calculated using an 9.63% rate of return, which is higher than the rate approved herein. Therefore, we will require a refund of $67,725 on an annual basis, with the refund to be made on a "per KWH" basis.

Based on the Commission's order in the FPUC-Fernandina Beach rate case, Staff recommends that since it would be necessary to reduce the rate of return during the pendency of the proceeding (8.26%) to the same level within the range of the recommended rate of return (8.05%) a refund would be necessary. Therefore, $2,693,000 of the interim increase should be refunded.

If the Commission were to base its refund position on total dollars, then no refund would be required since the interim award of $5,751,000 is less than the recommended increase of $14,577,000.

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STIPULATED
ISSUE 112: Should Gulf be required to file, within 30 days after the date of the final order in this docket, a description of all entries or adjustments to its future annual reports, rate of return reports, published financial statements and books and records which will be required as a result of the Commission's findings in this rate case? (REVELL)

RECOMMENDATION: Yes. The utility should be required to fully describe the entries and adjustments which will be either recorded or used in preparing reports submitted to the Commission.

POSITION OF PARTIES

GULF: Gulf will make all appropriate filings, as required by the Commission.

OPC: Yes.

STAFF ANALYSIS: Various adjustments will be made to the records of Gulf Power Company as a result of findings in this rate case. Gulf should be required to fully describe all entries to the accounting records which are affected by changes ordered by the Commission. In some cases, these changes will be reflected in information filed with the Commission in the future. Staff must be adequately informed of the changes the company has made to adequately evaluate the financial integrity and records of the company.

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

COMPARATIVE RATE BASES

SCHEDULE 1
26-Jul-90
02:12 PM

LINE NO.	CO. ADJ. NO.	ISSUE NO.	DESCRIPTION	COMPANY FILING SYSTEM PER BOOKS	COMPANY FILING JURISDICTIONAL PER BOOKS	COMPANY FILING ADJUSTMENTS	COMPANY FILING JURISDICTIONAL ADJUSTED	STAFF RECOMMENDATION ADJUSTMENTS	STAFF RECOMMENDATION JURISDICTIONAL ADJUSTED	PUBLIC COUNSEL ADJUSTMENTS	PUBLIC COUNSEL JURISDICTIONAL ADJUSTED	NOT USED ADJUSTMENTS	NOT USED JURISDICTIONAL ADJUSTED
1			PLANT IN SERVICE		$1,275,624								
2		2	PLANT IN SERVICE					(55)		(11,178)			
3		3	SCHERER TAX ADDER ADJUSTMENT					(1,520)		0			
4		4	SCHERER ACQUISITION ADJUSTMENT					(141)		0			
5		5	NEW CORPORATE HEADQUARTERS					(54)		0			
6		7	NAVY HOUSE					(23)		(23)			
7		8	APPLIANCE DIVISION					(214)		0			
8		9	TALLAHASSEE OFFICE					(24)		(43)			
9		10	BONIFAY/GRACEVILLE					0		(39)			
10		12	LEISURE LAKES					(142)		(140)			
11		16	UNIT POWER SALES					0		0			
12		25	PLANT DANIEL					0		0			
13		27	PLANT SCHERER					0		(52,987)			
14		29	REBUILDS \ RENNOVATIONS					0		459			
15		30	NETWORK PROTECTORS					0		0			
16													
17			Total plant in service	0	1,275,624	0	1,275,624	(2,173)	1,273,451	(63,951)	1,211,673	0	1,275,624
18													
19													
20			ACCUMULATED DEPRECIATION		454,964								
21		3	SCHERER TAX ADDER ADJUSTMENT					(172)		0			
22		8	APPLIANCE DIVISION					(7)		0			
23		9	TALLAHASSEE OFFICE					(11)		(26)			
24		11	JDITC UNDERSTATEMENT					0		3,622			
25		16	UNIT POWER SALES					0		0			
26		25	PLANT DANIEL					0		0			
27		27	PLANT SCHERER					0		(6,558)			
28		29	REBUILDS \ RENNOVATIONS					0		3			
29		30	NETWORK PROTECTORS					0		0			
30													
31			Total depreciation reserve	0	454,964	0	454,964	(190)	454,774	(2,959)	452,005	0	454,964
32													
33			Net plant in service	0	820,660	0	820,660	(1,983)	818,677	(60,992)	759,668	0	820,660
34													
35													
36			CONSTRUCTION WORK IN PROGRESS		14,949								
37		13	LEVEL OF CWIP					0		0			
38		14	NON-AFUDC CWIP					0		0			
39													
40			Total CWIP	0	14,949	0	14,949	0	14,949	0	14,949	0	14,949
41													
42													

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

COMPARATIVE RATE BASES

SCHEDULE 1
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LINE NO.	CO. ADJ. NO.	ISSUE NO.	DESCRIPTION	COMPANY FILING: SYSTEM PER BOOKS	COMPANY FILING: JURISDICTIONAL PER BOOKS	COMPANY FILING: ADJUSTMENTS	COMPANY FILING: JURISDICTIONAL ADJUSTED	STAFF RECOMMENDATION: ADJUSTMENTS	STAFF RECOMMENDATION: JURISDICTIONAL ADJUSTED	PUBLIC COUNSEL: ADJUSTMENTS	PUBLIC COUNSEL: JURISDICTIONAL ADJUSTED	NOT USED: ADJUSTMENTS	NOT USED: JURISDICTIONAL ADJUSTED
43			PROPERTY HELD FOR FUTURE USE		3,925								
44		6	CARYVILLE SOD FARM					(135)		0			
45		15	LEVEL OF PHFFU					0		(3,854)			
46													
47			Total prop. held for future use	0	3,925	0	3,925	(135)	3,790	(3,854)	71	0	3,925
48													
49													
50													
51			ACQUISITION ADJUSTMENT		2,317								
52		4	SCHERER ACQUISITION ADJUSTMENT					(2,317)		(2,317)			
53													
54													
55			Total acquisition adjustment	0	2,317	0	2,317	(2,317)	0	(2,317)	0	0	2,317
56													
57													
58			Net utility plant	0	841,851	0	841,851	(4,435)	837,416	(67,163)	774,688	0	841,851
59													
60													
61			WORKING CAPITAL		81,711								
62		16	UNIT POWER SALES					0		(4,097)			
63		18	PREPAID PENSIONS					0		(1,358)			
64		19	RATE CASE EXPENSES					(765)		(765)			
65		20	FUEL/CONSERVATION OVERRECOVERIES					0		0			
66		21	TEMPORARY CASH INVESTMENTS					0		0			
67		22	HEAVY OIL INVENTORY					(576)		(926)			
68		23	LIGHT OIL INVENTORY					(123)		(234)			
69		24	COAL INVENTORY					(1,834)		(4,468)			
70		25	PLANT DANIEL					0		0			
71		27	PLANT SCHERER					0		(2,187)			
72		28	CANCELED SCS BUILDING					0		0			
73		31	OTHER INVESTMENTS					(106)		0			
74		32	OTHER ACCOUNTS RECEIVABLE					0		0			
75		33	MATERIALS & SUPPLIES					0		(2,307)			
76		34	OTHER CURR. ASSETS & MISC. DEF. DEBITS					0		0			
77		35	CARYVILLE SUBSURFACE STUDY					0		(672)			
78		36	OPC EXPENSE ADJUSTMENTS					169		3,874			
79		N/A	OPC MATH ERROR					0		672			
80													
81			Total working capital	0	81,711	0	81,711	(3,235)	78,476	(12,468)	69,243	0	81,711
82													
83													
84			TOTAL RATE BASE	0	923,562	0	923,562	(7,670)	915,892	(79,631)	843,931	0	923,562

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

COMPARATIVE NET OPERATING INCOME

SCHEDULE 2
26-Jul-90
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LINE NO.	CO. ADJ. NO.	ISSUE NO.	DESCRIPTION	COMPANY FILING SYSTEM PER BOOKS	COMPANY FILING JURISDICTIONAL PER BOOKS	COMPANY FILING ADJUSTMENTS	COMPANY FILING JURISDICTIONAL ADJUSTED	STAFF RECOMMENDATION ADJUSTMENTS	STAFF RECOMMENDATION JURISDICTIONAL ADJUSTED	PUBLIC COUNSEL ADJUSTMENTS	PUBLIC COUNSEL JURISDICTIONAL ADJUSTED	NOT USED ADJUSTMENTS	NOT USED JURISDICTIONAL ADJUSTED
1			REVENUE FROM SALES OF ELECTRICITY		249,813								
2		48	PXT / STANDBY RATES					16		76			
3		49	NON-UTILITY ELECTRIC BILLINGS					95		2,433			
4													
5			Total sales of electricity	0	249,813	0	249,813	111	249,924	2,509	252,322	0	249,813
6													
7													
8			OTHER OPERATING REVENUES		5,767								
9		6	CARYVILLE SOD FARM					(3)		0			
10		47	APPLIANCE DIVISION - USE OF LOGO					0		0			
11													
12			Total other operating revenues	0	5,767	0	5,767	(3)	5,764	0	5,767	0	5,767
13													
14													
15			Total operating revenues	0	255,580	0	255,580	108	255,688	2,509	258,089	0	255,580
16													
17													
18			OPERATING EXPENSES:										
19			OPERATION & MAINTENANCE		113,382								
20		7	NAVY HOUSE					(8)		(8)			
21		27	PLANT SCHERER					0		(843)			
22		29	REBUILDS & RENNOVATIONS					0		(360)			
23		30	NETWORK PROTECTORS					0		(88)			
24		50	SALARIES & BENEFITS					0		(1,374)			
25		51	BAD DEBT EXPENSE					0		0			
26		52	FUEL REVENUE & EXPENSES					0		0			
27		53	CONSERVATION REVENUE & EXPENSES					0		0			
28		54	OUT-OF-PERIOD, NON-RECURRING, etc.					(190)		(360)			
29		55	INDUSTRY ASSOCIATION DUES					(20)		(21)			
30		56	CURRENT RATE CASE EXPENSES					(167)		(500)			
31		57	881167-EI RATE CASE EXPENSES					0		0			
32		58	BANK FEES & LINES OF CREDIT					0		(218)			
33		59	OUTSIDE SERVICES					0		0			
34		60	CUSTOMER ACCOUNTS					0		0			
35		61	COGENERATION & INDUSTRIAL PROGRAMS					(426)		0			
36		62	GOOD CENTS INCENTIVE PROGRAM					(50)		(50)			
37		63	GOOD CENTS IMPROVED & NEW HOME PROGRAMS					0		(1,597)			
38		64	ESSENTIAL CUSTOMER SERVICE PROGRAM					0		0			
39		65	ENERGY EDUCATION PROGRAM					0		(416)			
40		66	PRESENTATION / SEMINARS PROGRAM					(55)		(54)			
41		67	SHINE AGAINST CRIME					(92)		0			
42		68	ECONOMIC DEVELOPMENT					(687)		(671)			
43		69	PRODUCTION RELATED A&G					0		0			
44		70	OTHER A&G					0		0			
45		71	LOBBYING EXPENSES					(264)		(229)			
46		73	SCS EXPENSES					0		(718)			
47		74	IRS, GRAND JURY, etc.					(5)		0			

COMPANY:	GULF POWER COMPANY	COMPARATIVE NET OPERATING INCOME	SCHEDULE 2
DOCKET NO.:	891345-EI		26-Jul-90
TEST YEAR:	DECEMBER 31, 1990		02:12 PM

LINE NO.	CO. ADJ. NO.	ISSUE NO.	DESCRIPTION	COMPANY FILING				STAFF RECOMMENDATION		PUBLIC COUNSEL		NOT USED	
				SYSTEM PER BOOKS	JURISDICTIONAL PER BOOKS	ADJUSTMENTS	JURISDICTIONAL ADJUSTED	ADJUSTMENTS	JURISDICTIONAL ADJUSTED	ADJUSTMENTS	JURISDICTIONAL ADJUSTED	ADJUSTMENTS	JURISDICTIONAL ADJUSTED
48		75	PENSION EXPENSE					0		0			
49		76	STEAM PRODUCTION PERSONNEL					0		0			
50		77	RESEARCH & DEVELOPMENT PROJECTS					(32)		0			
51		78	EPRI / SCS DOUBLE COUNTING					0		0			
52	S	79	PLANT DANIEL ASH HAULING					0		0			
53		80	TRANSMISSION RENTS					0		(1,781)			
54		81	PUBLIC SAFETY INSPECTION & MAINT.					0		(740)			
55		86	EMPLOYEE RELATIONS PLANNING UNIT					0		(712)			
56		87	LABOR COMPLEMENT VACANCIES					(403)		(1,045)			
57		88	TURBINE & BOILER INSPECTIONS					0		(721)			
58		89	PLANT DANIEL					0		(1,777)			
59		90	1989 UNCOLLECTIBLES CREDIT					0		(199)			
60		91	EMPLOYEE SAVINGS PLAN					0		0			
61		92	PRODUCTIVITY IMPROVEMENT PLAN					(339)		(454)			
62		93	PERFORMANCE PAY PLAN					0		(999)			
63		94	EPRI NUCLEAR RESEARCH					(310)		(319)			
64		95	PLANT SMITH ASH HAULING					0		(352)			
65		96	EMPLOYEE RELOCATION & DEVELOPMENT PROGRAMS					(56)		(240)			
66		97	OBSOLETE MATERIAL					0		0			
67		98	MANAGEMENT PERKS					(65)		(64)			
68		99	DUCT & FAN REPAIRS					0		(269)			
69		100	CUSTOMER SERVICES & INFORMATION					0		(399)			
70		101	MARKETING EXPENSES					0		(297)			
71		102	O&M BENCHMARK					0		(1,202)			
72		OPC	UNIT POWER SALES					0		3,790			
73		N/A	OPC MATH ERROR					0		1,202			
74													
75													
76													
77			Total operation & maintenance	0	113,382	0	113,382	(3,169)	110,213	(14,085)	99,297	0	113,382
78													
79													
80			DEPRECIATION AND AMORTIZATION		47,701								
81		3	SCHERER TAX ADDER ADJUSTMENT					(49)		0			
82		4	SCHERER ACQUISITION ADJUSTMENT					(73)		0			
83		8	APPLIANCE DIVISION					(12)		0			
84		9	TALLAHASSEE OFFICE					(1)		0			
85		12	LEISURE LAKES					(5)		0			
86		27	PLANT SCHERER					0		(1,777)			
87		OPC	EFFECT OF OPC ADJUSTMENTS					0		(967)			
88		82	REASONABLENESS					0		0			
89													
90			Total depreciation and amortization	0	47,701	0	47,701	(140)	47,561	(2,744)	44,957	0	47,701
91													

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

COMPARATIVE NET OPERATING INCOME

SCHEDULE 2
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LINE NO.	CO. ADJ. NO.	ISSUE NO.	DESCRIPTION	COMPANY FILING: SYSTEM PER BOOKS	COMPANY FILING: JURISDICTIONAL PER BOOKS	COMPANY FILING: ADJUSTMENTS	COMPANY FILING: JURISDICTIONAL ADJUSTED	STAFF RECOMMENDATION: ADJUSTMENTS	STAFF RECOMMENDATION: JURISDICTIONAL ADJUSTED	PUBLIC COUNSEL: ADJUSTMENTS	PUBLIC COUNSEL: JURISDICTIONAL ADJUSTED	NOT USED: ADJUSTMENTS	NOT USED: JURISDICTIONAL ADJUSTED
98			TAXES OTHER THAN INCOME		20,822								
99		27	PLANT SCHERER					0		(244)			
100		48	PXT / STANDBY RATES					1		1			
101		83	REASONABLENESS					0		0			
102		87	LABOR COMPLEMENT VACANCIES					(30)		(78)			
103													
104													
105			Total taxes other than income	0	20,822	0	20,822	(29)	20,793	(321)	20,501	0	20,822
106													
107													
108			INCOME TAXES CURRENTLY PAYABLE	0	13,185								
109		84	REASONABLENESS					0		0			
110		85	Interest expense reconciliation					(231)		587			
111		N/A	Effect of other adjustments					1,244		8,824			
112													
113			Total income taxes - current	0	13,185	0	13,185	1,013	14,198	9,411	22,596	0	13,185
114													
115													
116			DEFERRED INCOME TAXES (NET)	0	1,621								
117		N/A	EFFECT OF STAFF ADJS. TO DEPREC.					53		0			
118		27	PLANT SCHERER					0		604			
119													
120													
121		OPC	EFFECT OF OPC ADJUSTMENTS					0		(38)			
122													
123			Total deferred income taxes (net)	0	1,621	0	1,621	53	1,674	566	2,187	0	1,621
124													
125													
126													
127			INVESTMENT TAX CREDIT (NET)		(2,041)								
128		27	PLANT SCHERER					0		96			
129		OPC	EFFECT OF OPC ADJUSTMENTS					0		102			
130													
131			Total investment tax credit (net)	0	(2,041)	0	(2,041)	0	(2,041)	198	(1,843)	0	(2,041)
132													
133													
134			(GAIN)/LOSS ON SALE		0								
135													
136													
137			Total (gain)/loss on sale	0	0	0	0	0	0	0	0	0	0
138													
139													
140			TOTAL OPERATING EXPENSES	0	194,670	0	194,670	(2,272)	192,398	(6,975)	187,695	0	194,670
141													
142													
143			NET OPERATING INCOME	0	60,910	0	60,910	2,380	63,290	9,484	70,394	0	60,910
144													

GULF POWER COMPANY
DOCKET NO. 891345-EI
O & M BENCHMARK VARIANCE BY FUNCTION
1990

	Steam Production (000)	Other Production (000)	Other Power Supply (000)	Trans. Rents (000)	Trans. Other (000)	Total Trans. (000)	Distribution (000)	Customer Accounts (000)	Customer Service (000)	Sales (000)	Prod Rel Adm.& Gen. (000)	Other Adm. & General (000)	Total Adm.&Gen. (000)	Total (000)
1984 FPSC Allowed O&M Less Direct Fuel, ECCR & Purchased Power-System	$35,502	$81	$1,020	$962	$2,335	$3,297	$7,670	$6,074	$1,505	$0	$3,043	$21,006	$24,049	$79,198
Reconciling Adjustments														
Amort. of Unavailable Oil	(51)													(51)
Capacity Payments	716													716
UPS Allocation Error											342		342	342
Adjusted 1984 FPSC Allowed O&M	36,167	81	1,020	962	2,335	3,297	7,670	6,074	1,505	0	3,385	21,006	24,391	80,205
True-Up of 1984 Comp. Multiplier Adj. to actual CPI-Cust. Growth	0	0	0	0	0.0368 53	53	0.0368 167	0.0368 140	0.0368 33	0.0368 0	0	0.0368 373	373	766
1984 Allowed O&M less Direct Fuel, ECCR & Purchased Power-System	36,167	81	1,020	962	2,388	3,350	7,837	6,214	1,538	0	3,385	21,379	24,764	80,971
Add Plant Daniel Related Adj. Docket 840036-EI				425		425					1,573		1,573	1,998
Former ECCR Programs Moved to Base Rates									2,248			348	348	2,596
Total O&M Base Adjusted for Plant Daniel & Fromer ECCR	36,167	81	1,020	1,387	2,388	3,775	7,837	6,214	3,786	0	4,958	21,727	26,685	85,565
1984 - 1990 Compound Multiplier	1.2468	1.2468	1.2468	1.2468	1.5073		1.5073	1.5073	1.5073	1.5073	1.2468	1.5073		
1990 O&M Benchmark - System	45,093	101	1,272	1,729	3,599	5,328	11,813	9,366	5,707	0	6,182	32,749	38,931	117,611
Plant Scherer & Associated Trans Line Rents	1,957			1,822	3	1,825					263		263	4,045
1990 Benchmark less Direct Fuel & Pur. Power-System	47,050	101	1,272	3,551	3,602	7,153	11,813	9,366	5,707	0	6,445	32,749	39,194	121,656
1990 Actual O&M less Direct Fuel & Pur. Power-System	51,547	47	1,143	3,017	4,280	7,297	14,530	7,780	7,066	835	5,655	33,812	39,467	129,712
NOI O&M Adjustments	0	0	0	0	0	0		0	(1,640)	(148)	0	(1,020)	(1,020)	(2,808)
1990 Actual Adjusted O&M -System	51,547	47	1,143	3,017	4,280	7,297	14,530	7,780	5,426	687	5,655	32,792	38,447	126,904
Benchmark Variance - Adj. System	4,497	(54)	(129)	(534)	678	144	2,717	(1,586)	(281)	687	(790)	43	(747)	5,248
Staff Adjustments-System	(42)	0	0	0	0	0	0	0	(531)	(779)	0	(1,292)	(1,292)	(2,644)
Adjustments to all Functions														(607)
Adjusted Variance-System	4,455	(54)	(129)	(534)	678	144	2,717	(1,586)	(812)	(92)	(790)	(1,249)	(2,039)	1,997

GULF POWER COMPANY
DOCKET NO. 891345-EI

COMPOUND MULTIPLIERS

Year	Total Customers	% Increase	Compound Multiplier	CPI Amount	% Increase	Compound Multiplier	Inflation and Growth Multiplier
1984	239,956		1.00000	1.039335		1.00000	1.0000
1985	253,135	5.492%	1.05492	1.076250	3.552%	1.03552	1.0924
1986	263,646	4.152%	1.09873	1.096917	1.920%	1.05540	1.1596
1987	271,448	2.959%	1.13124	1.137084	3.662%	1.09405	1.2376
1988	277,883	2.371%	1.15806	1.183500	4.082%	1.13871	1.3187
1989	283,659	2.079%	1.18213	1.241614	4.910%	1.19462	1.4122
1990	290,092	2.268%	1.20894	1.295854	4.369%	1.24681	1.5073

TRUE - UP OF BASE YEAR MULTIPLIERS (1979 - 1984), PROJECTED TO ACTUAL*

	Compound Multiplier	CPI Compound Multiplier	Inflation and Growth Multiplier
1984 ACTUAL	1.23006	1.4316	1.7610
1984 PROJECTED	1.20439	1.4316	1.7242
DIFFERENCE	0.0257	0.0000	0.0368

* 1984 ACTUAL CPI WAS 4.3% AND CUSTOMER GROWTH WAS 5.503%.
1984 PROJECTED ASSUMES CPI WAS 4.3% AND CUSTOMER GROWTH WAS 3.31%.

GULF POWER COMPANY
DOCKET NO. 891345-EI
1990 O & M BENCHMARK VARIANCE BY FUNCTION (SYSTEM)

SCHEDULE 3

Issue	Steam Production (000)	Nuclear Production (000)	Other Production (000)	Other Power Supply (000)	Trans-mission (000)	Distribution (000)	Customer Accounts (000)	Customer Service (000)	Sales (000)	Prod Rel Adm & Gen (000)	Other Adm & Gen (000)	Total Adm & Gen (000)	Total (000)
7 NAVY HOUSE											(8)	(8)	(8)
54 OUT OF PERIOD/NONRECURR.													(194)*
55 INDUSTRY ASSOC. DUES											(21)	(21)	(21)
56 RATE CASE EXPENSES											(167)	(167)	(167)
61 COGEN/INDUSTRIAL CUST.								(426)					(426)
62 GOOD CENTS INCENTIVE								(50)					(50)
66 PRESENTATIONS/SEMINARS								(55)					(55)
67 SHINE AGAINST CRIME									(92)				(92)
68 ECONOMIC DEVELOPMENT									(687)				(687)
71 LOBBYING											(278)	(278)	(278)
74 GRAND JURY, ETC.											(5)	(5)	(5)
77 RESEARCH & DEVLOP.	(42)												(42)
87 VACANT POSITIONS													(413)*
92 PIP											(358)	(358)	(358)
94 EPRI NUCLEAR RESEARCH											(327)	(327)	(327)
96 EMPLOYEE RELATIONS											(59)	(59)	(59)
98 MANAGEMENT PERKS											(69)	(69)	(69)
													0
													0
													0
													0
TOTAL SYSTEM	(42)	0	0	0	0	0	0	(531)	(779)	0	(1,292)	(1,292)	(3,251)

*These adjustments relate to all functions

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

COMPARISON OF COST OF CAPITAL POSITIONS

SCHEDULE 4
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		COMPANY FILING				STAFF RECOMMENDATION WITHOUT 50 BASIS POINT REDUCTION			
LINE NO.	COMPONENT	AMOUNT	RATIO	COST RATE	WEIGHTED COST	AMOUNT	RATIO	COST RATE	WEIGHTED COST
1	Long Term Debt	329,936	35.72%	8.72%	3.12%	336,726	36.76%	8.72%	3.21%
2	Short Term Debt	4,290	0.46%	8.00%	0.04%	4,286	0.47%	8.00%	0.04%
3	Preferred Stock	55,316	5.99%	7.75%	0.46%	55,437	6.05%	7.75%	0.47%
4	Customer deposits	15,659	1.70%	7.65%	0.13%	15,256	1.67%	7.65%	0.13%
5	Common Equity	293,655	31.80%	13.00%	4.13%	279,652	30.53%	12.30%	3.76%
6	Accumulated Deferred Income Taxes	182,959	19.81%	0.00%	0.00%	182,820	19.96%	0.00%	0.00%
7	Deferred ITC - Zero Cost	831	0.09%	0.00%	0.00%	830	0.09%	0.00%	0.00%
8	Deferred ITC - Weighted Cost	40,916	4.43%	10.49%	0.46%	40,884	4.46%	10.13%	0.45%
10		923,562	100.00%		8.34%	915,891	100.00%		8.05%

		PUBLIC COUNSEL WITHOUT 200 BASIS POINT REDUCTION				STAFF RECOMMENDATION WITH 50 BASIS POINT REDUCTION			
18	COMPONENT	AMOUNT	RATIO	COST RATE	WEIGHTED COST	AMOUNT	RATIO	COST RATE	WEIGHTED COST
20	Long Term Debt	308,012	36.50%	8.72%	3.18%	336,726	36.76%	8.72%	3.21%
21	Short Term Debt	3,989	0.47%	8.00%	0.04%	4,286	0.47%	8.00%	0.04%
22	Preferred Stock	50,525	5.99%	7.75%	0.46%	55,437	6.05%	7.75%	0.47%
23	Customer deposits	14,575	1.73%	7.65%	0.13%	15,256	1.67%	7.65%	0.13%
24	Common Equity	261,571	30.99%	11.75%	3.64%	279,652	30.53%	11.80%	3.60%
25	Accumulated Deferred Income Taxes	167,113	19.80%	0.00%	0.00%	182,820	19.96%	0.00%	0.00%
26	Deferred ITC - Zero Cost	773	0.09%	0.00%	0.00%	830	0.09%	0.00%	0.00%
27	Deferred ITC - Weighted Cost	37,372	4.43%	9.91%	0.44%	40,884	4.46%	9.92%	0.44%
29		843,930	100.00%		7.90%	915,891	100.00%		7.89%

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

RECONCILIATION OF AVG. RATE BASE AND AVG. CAPITAL STRUCTURE

LINE NO.	ADJ. NO.	DESCRIPTION	LONG-TERM DEBT	SHORT-TERM DEBT	PREFERRED STOCK	CUSTOMER DEPOSITS	COMMON EQUITY	TAX CREDITS ZERO COST	TAX CREDITS WTD COST	DEFERRED INC. TAXES	TOTAL
1		Total Company Per Books	481,823	4,432	67,432	15,775	367,404	858	48,068	203,823	1,189,615
2	1	PEABODY	(30,116)	0	0	0	(22,976)	0	0	0	(53,092)
3	2	DANIEL	(42,089)	0	0	0	0	0	0	0	(42,089)
4	3	COMMON DIVIDENDS DECLARED	0	0	0	0	5,400	0	0	0	5,400
5	4	NON UTILITY	0	0	0	0	(14,880)	0	0	0	(14,880)
6	5	TEMPORARY CASH INVESTMENTS	0	0	0	0	(6,399)	0	0	0	(6,399)
7	6	MISCELLANEOUS SPECIFIC ADJS.	0	0	(948)	0	948	0	0	0	0
8	7	UNIT POWER SALES	(61,439)	0	(9,161)	0	(40,333)	0	(5,793)	(14,785)	(131,511)
9	8		0	0	0	0	0	0	0	0	
10	9		0	0	0	0	0	0	0	0	
11	10		0	0	0	0	0	0	0	0	
12	11		0	0	0	0	0	0	0	0	
13	12		0	0	0	0	0	0	0	0	
14	13		0	0	0	0	0	0	0	0	
15	14		0	0	0	0	0	0	0	0	
16	15		0	0	0	0	0	0	0	0	
17											
18		Subtotal	348,179	4,432	57,323	15,775	289,164	858	42,275	189,038	947,044
19											
20		Total company pro-rata adjustments	(11,453)	(146)	(1,886)	(519)	(9,512)	(28)	(1,391)	(6,218)	(31,152)
21											
22		Subtotal	336,726	4,286	55,437	15,256	279,652	830	40,884	182,820	915,892
23											
24		Jurisdictional separation factor	1.000000	1.000000	1.000000	1.000000	1.000000	1.000000	1.000000	1.000000	
25											
26		Subtotal	336,726	4,286	55,437	15,256	279,652	830	40,884	182,820	915,892
27											
28		Total Staff Pro-rata adjustments	0	0	0	0	0	0	0	0	0
29											
30											
31		Jurisdictional capital structure	336,726	4,286	55,437	15,256	279,652	830	40,884	182,820	915,892
32											
33											
34		Percent of total capital	36.76%	0.47%	6.05%	1.67%	30.53%	0.09%	4.46%	19.96%	100.00%
35											

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

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SCHEDULE OF PRORATA ADJUSTMENTS

LINE NO.	ADJ. NO.	DESCRIPTION	COMPANY (TOTAL CO.)	STAFF (JURISDICTIONAL)
1	1	ALL PRORATA ADJUSTMENTS	(31,152)	
2	2			
3	3			
4	4			
5	5			
6	6			
7	7			
8	8			
9	9			
10	10			
11	11			
12	12			
13	13			
14	14			
15	15			
16				
17		Total	(31,152)	0
18				
19				
20		TAKEN OUT AS FOLLOWS:		
21		Long term debt	(11,453)	0
22		Short term debt	(146)	0
23		Preferred stock	(1,886)	0
24		Customer deposits	(519)	0
25		Common equity	(9,512)	0
26		Deferred ITC - zero cost	(28)	0
27		Deferred ITC - weighted cost	(1,391)	0
28		Deferred income taxes	(6,218)	0
29				
30			(31,152)	0
31				

COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

COMPARISON OF
REVENUE EXPANSION FACTORS

SCHEDULE 5
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LINE NO.	DESCRIPTION	COMPANY	STAFF	PUBLIC COUNSEL
1	Revenue Requirement	100.000000	100.000000	100.000000
3	Uncollectible Accounts	(0.113300)	(0.113300)	(0.113300)
5	Gross Reciepts Tax	(1.500000)	(1.500000)	(1.500000)
7	Regulatory Assessment Fee	(0.125000)	(0.125000)	(0.125000)
9	Net Before Income Taxes	98.261700	98.261700	98.261700
11	State Income Tax Rate	5.5000%	5.5000%	5.5000%
13	State Income Tax	5.404394	5.404394	5.404394
15	Net Before Federal Income Taxes	92.857307	92.857307	92.857307
17	Federal Tax Rate	34.0000%	34.0000%	34.0000%
19	Federal Income Tax	31.571484	31.571484	31.571484
21	Net Operating Income	61.285822	61.285822	61.285822
24	Net Operating Income Multiplier	1.631699	1.631699	1.631699

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COMPANY: GULF POWER COMPANY
DOCKET NO.: 891345-EI
TEST YEAR: DECEMBER 31, 1990

SCHEDULE 6
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COMPARATIVE REVENUE REQUIREMENTS

DESCRIPTION [1]	COMPANY AS FILED [2]	STAFF RECOMMENDATION [3]	PUBLIC COUNSEL [4]	STAFF - 50 BASIS POINT REDUCTION [5]
Adjusted Jurisdictional Rate Base	$923,562	$915,892	$843,931	$915,892
Required Rate of Return	8.34%	8.05%	7.90%	7.89%
Required Net Operating Income	77,025	73,708	66,671	72,224
Adjusted Achieved Test Year Jurisdictional Net Operating Income	60,910	63,290	70,394	63,290
Jurisdictional NOI Deficiency	16,115	10,417	(3,723)	8,934
Revenue Expansion Factor	1.631699	1.631699	1.631699	1.631699
Revenue Increase (Decrease)	26,295	16,998	(6,076)	14,577
ROE Basis Point Reduction	0	(2,420)	(9,088)	---
TOTAL REVENUE INCREASE (DECREASE)	$26,295	$14,577	($15,164)	$14,577