BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Joint Petition of Florida Power Corporation and Sebring Utilities Commission for Approval of Certain Matters in Connection with the Sale of Assets by Sebring Utilities Commission to Florida Power Corporation.	DOCKET NO. 920949-EU ORDER NO. PSC-92-1468-FOF-EU ISSUED: 12/17/92

The following Commissioners participated in the disposition of this matter:

THOMAS M. BEARD, Chairman
BETTY EASLEY

ORDER APPROVING CERTAIN MATTERS IN CONNECTION WITH THE SALE OF ASSETS BY SEBRING UTILITIES COMMISSION TO FLORIDA POWER CORPORATION

BY THE COMMISSION:

CASE BACKGROUND

On September 18, 1992, Florida Power Corporation (FPC) and Sebring Utilities Commission (Sebring) filed a joint petition for approval of several aspects of a Purchase and Sale Agreement by which FPC will acquire Sebring's remaining electric utility system and provide electric service to present and future customers in the territory previously served by Sebring. Citizens for Rate Equity (CURE), The Action Group, The Concerned Citizens of Sebring (CCS), and Tampa Electric Company were granted intervenor status in the case. A customer hearing was held in Sebring on November 4, 1992. A technical hearing was held in Tallahassee on December 7-8, 1992. Nine witnesses presented testimony and evidence on the issues. After closing arguments and our staff's oral recommendation, we made our decision in the case. This final order memorializes that decision.

Sebring's Financial Problems

The Sebring Utilities Commission is in serious financial distress. Faced with escalating debt obligations in 1991, the Sebring Utilities Commission sold its generation facilities and most of its transmission facilities to Tampa Electric Company. At that time Sebring entered into a purchased power contract with Tampa Electric Company to supply all of its capacity needs. The sale to Tampa Electric Company did not solve Sebring's financial problems, however, and debt service on approximately $85 million of bonds that remain outstanding has drained Sebring's resources and brought it to the verge of bankruptcy.

Presently, Sebring is in default of its bond covenants. The rates Sebring levies upon its customer base are not sufficient to cover the debt service and maintain required reserve margins. Sebring maintains that compliance with its bond covenants would require an estimated thirty-seven percent increase in current rates, raising a typical residential electric bill to $151 per 1000 kwh. Sebring has drawn on its reserves to avoid raising its electric customers' rates, because those rates are already the highest in the state.

Sebring's rates compare most unfavorably to those of its nearest neighbor, Florida Power Corporation. Customers of Sebring presently pay $110 per 1000 kilowatt hours (kwh) of electricity, while their neighbors served by Florida Power Corporation pay $71 per 1000 kwh of electricity. Decades of territorial conflict and competition have left the two utilities' service areas entwined and confused, emphasizing the rate discrepancy between the two utilities. Property values in Sebring are depressed, and the community is dissatisfied and divided.

To provide rate relief to its customers and retire its existing bonds, Sebring issued a request for proposals to purchase its electric distribution and remaining transmission facilities. Florida Power Corporation was selected as the successful bidder. Negotiations began soon thereafter, and culminated after more than a year in the contract that is the subject of these proceedings, the "Agreement for Purchase and Sale of Electric System".

Sebring's Alternatives

Sebring considered several alternatives to solve its financial problems before concluding the agreement with FPC. Sebring considered operating in compliance with its bond covenants, but, as mentioned above, Sebring would have had to increase electric rates dramatically through 1996 to do so. Since its rates were already the highest in the state, Sebring determined that further substantial increases would be burdensome and unacceptable. Sebring considered operating in violation of its bond covenants, but this alternative did not assure lower rates to its customers in the long run, because the rate covenants of the bond agreements permit the bond trustee to sue to raise customer rates to cover the debt obligations. Sebring considered refinancing its debt, but rejected that option because refinancing would not have led to decreased rates. Sebring also considered bankruptcy, but the delays and expense, as well as the uncertainty of the outcome, made bankruptcy an unacceptable alternative. Finally, Sebring considered sale of its facilities to the City of Sebring, but the

city refused to consider this alternative unless sale to Florida Power Corporation was not possible. The uncertainty of this alternative led Sebring to conclude that it was not a reasonable one.

Of the options available to it, Sebring determined that the sale to Florida Power Corporation was the most reasonable, because the sale would provide immediate rate relief to Sebring's customers, while allowing Sebring to retire its debt and cease operating permanently as a public utility. The purchase and sale agreement was signed on August 28, 1992. The Sebring City Council approved it on September 15, 1992.

The Agreement for Purchase and Sale of Electric System

The agreement provides for FPC to purchase the remaining assets of the Sebring electric system for a base purchase price of not more than $54 million, plus an additional amount to cover Sebring's miscellaneous debts and expenses and any amounts owed by Sebring to Tampa Electric Company for power purchases under the power purchase agreement. The base purchase price is the amount the parties have estimated will be necessary to repay in full all of Sebring's outstanding bonds. The City of Sebring will pay $21.5 million to purchase Sebring's water system, and that amount and the balance of Sebring's reserve funds will also be applied to repay the bonds.

The base purchase price includes three components: 1) the net book value of Sebring's assets as of the closing date. That amount will be based on a net book value of $17,813,753 as of September 30, 1991; 2) an amount for "Going Concern" the Commission determines appropriate; and 3) the remainder that represents the amount above net book value and going concern value needed by Sebring to retire its debt.

The agreement provides that Florida Power Corporation will recover the remainder of the base purchase price above net book and going concern value specifically from customers that Sebring was serving as of the date of closing, and all new customers in the Sebring service area over a period of 15 years. That amount, plus costs to finance the purchase, interest expense, and certain fees and taxes, would be charged only to those customers as a separate rate, the "SR-1 Rate Rider", in addition to Florida Power Corporation's approved rates. The rate rider would not be charged to Florida Power Corporation's general body of ratepayers.

Other provisions of the agreement relevant to this case include Florida Power Corporation's assumption of Sebring's obligations under the TECO Power Purchase agreement, Florida Power Corporation's assumption of the Sebring/Glades Electric Cooperative territorial agreement, an amendment to the Sebring/FPC territorial agreement that gives FPC the exclusive right to operate an electric distribution system in Sebring's retail service territory, and termination of the parties' Settlement Agreement for the transfer of customers and elimination of duplicate facilities.

Conditions Precedent to Closing

The agreement contains a series of conditions precedent to closing that require our approval of certain relevant matters. The agreement provides that if the parties do not receive our approval of those matters, the parties each have the option to withdraw from the agreement. The conditions form the relief that Sebring and FPC have requested in their Petition, to wit:

1) Our approval of the imposition of the Sebring Rider rate and the methodology for changing that rate;
2) Our approval of inclusion of the SR-1 rate schedule as part of FPC's rates;
3) Our approval of the net book value of Sebring's facilities of $17.8 million as of September 30, 1991;
4) Our approval of any additional amount above net book value for going concern as a prudent investment;
5) Our approval of FPC's purchase of those rate base assets as a prudent investment;
6) Our approval of the prudence of FPC's assumption of the Purchased Power Agreement with TECO for cost recovery purposes;
7) Our approval of the amendment to the Petitioners' territorial agreement and withdrawal of the Settlement agreement; and
8) Our approval of FPC's assumption of the Sebring/Glades territorial agreement.

DECISION

Jurisdiction

We have jurisdiction of these matters by the provisions of Chapter 366, Florida Statutes. That chapter grants us exclusive jurisdiction over the rates and charges of investor-owned electric utilities, exclusive jurisdiction over the rate structures of all

electric utilities in the state, and exclusive jurisdiction over territorial agreements and disputes between all electric utilities. The Legislature intends that the provisions of Chapter 366 are to be liberally construed to protect the public welfare.

The Action Group, one of the three customer associations from Sebring that intervened in this case, argued that we are without subject matter jurisdiction to approve the Sebring rate rider, because that rider is not a "rate" as contemplated by Chapter 366, Florida Statutes. The Action Group characterized the rider as a "loan" from Florida Power Corporation to Sebring that FPC will recover from Sebring's customers to pay off Sebring's bond indebtedness. The Action Group argued that the only "service" to be rendered in return for the rider had nothing to do with the provision of electric service to a customer base. (See The Action Group's Prehearing Memorandum, p. 3.) Since the proposed rider does not relate to the delivery of electric power, the argument goes, it is not a "rate", and we have no jurisdiction over it.

It is axiomatic that if we have exclusive and plenary jurisdiction over the rates and charges of public utilities, and we are charged with the obligation to ensure that the rates and charges are fair just and reasonable, we must have jurisdiction to determine what is a rate in the first place. There is no other forum to make that determination. If there were, our authority to set appropriate rates and charges would be effectively subverted. No rate decision we made would be final until another authority had determined whether the rates we had set were actually "rates". See Lake Worth Utilities Authority v. Barkett, 433 So.2d 1278 (Fla. 4th DCA 1983).

Action Group's argument is a rate discrimination argument, not a jurisdictional one. The proper question to ask here is not whether the proposed Sebring Rider is a rate. The proper question to ask is whether the proposed Sebring Rider unduly discriminates between customers who are similarly situated and who receive essentially the same service. Action Group does not question our jurisdiction to answer the question when it is posed this way. See City of Tallahassee v. Mann, 411 So.2d 162 (Fla. 1981), and CF Industries v. Nichols, 234 So. 2d 536 (Fla. 1988). We hold that the matters proposed for our approval in this proceeding, including the Sebring rider rate, fall well within the purview of our jurisdiction in all respects.

The Sebring Rider

The "Agreement for Purchase and Sale of Electric System" provides that the amount of the base purchase price in excess of the net book value and going concern value that is needed to retire Sebring's debt obligations will be collected by Florida Power Corporation from all customers of Sebring as of the date of closing and all future customers in Sebring's service area. Sebring's service area was delineated in the Sebring/FPC territorial agreement. The basic reasoning behind this proposal is that the costs of repayment of the Sebring Utilities Commission's debts are costs associated with the provision of electric service to Sebring's customers, and those costs should not be borne by Florida Power Corporation's general body of ratepayers. The petitioners have asked for our approval of a "Sebring rider rate" to accomplish this purpose.

The rate will be applied to the Sebring customers as an addition to FPC's current rates. The rate is structured as a formula rate, to be recovered on a kwh energy basis over a period of fifteen years. The rate will be routinely reviewed and adjusted to ensure that the amounts collected accurately reflect the amounts remaining to satisfy the debt.

There are three basic components needed to calculate the amount of the rider: 1) The total dollars to be recovered - the difference between the purchase price and the depreciated net book value of the Rate Base Assets, plus any going concern value determined by the Commission to be a prudent investment, 2) the number of kwh's forecast, and 3) the fifteen year time period. The amount of the rider is simply the total dollars to be recovered divided by the total number of kwh's forecast for the next fifteen years.

We find that the method FPC has proposed to calculate the amount of the rider is reasonable. The rate is designed as a formula rate similar to other formula rates the Commission has approved. The record reflects that a medium load forecast was used to project growth in the Sebring area of 2.09% annually. That forecast is reasonable and comparable to other forecasts for the Sebring area. To the extent that the load forecast proves to be inaccurate, the rider can be recalculated to correct the inaccuracies.

We find that the fifteen year period FPC has proposed to collect the rider is appropriate. The time period of the rider influences the amount of the rider. If the Sebring debt were to be recovered over a longer period, as the customer association CCS proposed, the amount of principal to be recovered annually would be

less, but there would be an additional 10 years of interest and other related expenses Sebring customers would have to pay. A shorter period would retire the debt faster but increase the customers' rates for that period. We approve the 15 year period, because it provides immediate rate relief for Sebring customers and aggressively reduces the amount of the outstanding debt.

We find that the method used to identify customers who will be subject to the rider is appropriate. The Sebring rider will be assessed against all retail electric customer locations that receive electric service through a Sebring meter at the time of closing. After closing, all retail customers at new locations within Sebring's territory as delineated in its 1986 territorial agreement will be subject to the rider. Growth in the Sebring service territory will reduce the amount of the rider. The Sebring airport and retail customers in and around it that are presently served by Florida Power Corporation will not be subject to the rider.

The exact amount of dollars to be recovered, and thus the exact amount of the rider, will not be known until the closing date of the purchase; and the amount will fluctuate over the life of the rider. The initial rider is estimated to be 1.851 cents per kwh based on an estimated $32,393,631 worth of debt to recover. The amount of actual kwh growth will undoubtedly differ to some degree from estimated kwh growth over the fifteen year time period, and this will affect the amount of the rider. If actual growth in the Sebring area is less than forecasted, the amount of the rider will increase; but conversely, if actual growth is greater than the amount forecasted the amount of the rider will decrease. The kwh sales will be monitored over time.

FPC will issue medium term notes as part of its normal debt issuance to pay the rider amount. It will establish and maintain a balance account for the Sebring rider that nets revenues collected from the rider against payments made for principal, interest, and other expenses. Any monies refunded from Sebring Utilities Commission's operations will be credited to the account for the Sebring ratepayers' benefit.

We intend to retain jurisdiction over all aspects of the rider. FPC proposed that the rate of the rider would be reviewed no less frequently than every four years. At the hearing, however, FPC agreed to provide reports on the Sebring rider as part of its monthly surveillance reports. FPC also agreed to review all aspects of the rider on a yearly basis, and provide the Commission with the results of that annual review.

We believe, under the particular circumstances of this case, that the proposed Sebring rider does not unduly discriminate against the Sebring customers who will be subject to it. To the contrary, we believe the rider accurately represents the additional cost to serve the Sebring customers because of Sebring's financial difficulties, and we believe that it would be discriminatory to pass that additional cost to Florida Power Corporation's general body of ratepayers. That is the fundamental regulatory principle we are bound to uphold in this most difficult decision. As the Supreme Court said in C.F. Industries v. Nichols, Supra., where it affirmed our approval of standby rates to be charged cogenerators:

> In setting rates, the PSC has a two-pronged responsibility: rates must not only be fair and reasonable to the parties before the PSC, they must also be fair and reasonable to other utility customers who are not directly involved in the proceedings at hand. Standby rates which did not properly recover the cost-of-service would unfairly discriminate against other customers by requiring them to subsidize the standby service.

We believe we are properly fulfilling our regulatory responsibility by approving the Sebring Rider rate. The record of this proceeding makes it perfectly clear, despite many Sebring customers' wish that it be otherwise, that the cost of the Sebring debt is a cost to serve the Sebring customers. That cost attaches to that class of customers, and distinguishes it from other classes of customers, no matter who provides the electric service. It will not simply go away. In fact there is substantial evidence in the record that if FPC's acquisition of the Sebring system is not consummated, the cost to serve Sebring customers, and the rates that reflect that cost to serve, will rise dramatically. The cost of debt is a cost of service, even when that cost is very high. We find that the Sebring rider rate appropriately identifies the additional cost to serve Sebring customers, appropriately allocates that cost to those customers, and appropriately insulates Florida Power Corporation's general body of ratepayers from the costs that were not incurred for their benefit. We hold, therefore, that the Sebring rider rate is not unduly discriminatory, and we approve the SR-1 rate schedule as part of Florida Power Corporation's rate schedule. When the purchase of the Sebring system is completed and Florida Power Corporation submits the SR-1 tariff, our staff may administratively approve it if it conforms to the principles we have approved here.

The rate base assets

In 1991, when Sebring decided that its financial difficulties required it to sell its remaining electric system assets, it retained an independent consultant, Research Management International, Inc. (RMI), to conduct a valuation of those assets. The valuation was necessary, because over many years, contrary to the repeated advice of its accountants, Sebring had not kept its books and records in compliance with the Federal Energy Regulatory Commission's Uniform System of Accounts. Sebring's records were thus inadequate to establish an accurate net book value for its tangible assets. RMI recalculated the net book value of Sebring's tangible assets and arrived at a figure of $17,813,753 as of September 30, 1991.

We find that the cost study RMI performed to value Sebring's distribution system, transmission system, and other tangible assets was reasonable and appropriate and consistent with established practice in the valuation of utility assets. We approve the depreciated net book value as of September 30, 1992 as $17,813,753. We find that the methodology used to arrive at that amount is consistent with generally accepted accounting principles, and we approve the use of that methodology to calculate the value of the Sebring assets at the time of purchase. For federal income tax purposes Florida Power Corporation shall treat the acquisition of Sebring's tangible and intangible assets in a manner that is consistent with the provisions of the Internal Revenue Code and cost-effective for its ratepayers.

For the reasons mentioned above, we approve at this time the prudence of the acquisition of Sebring's electric system assets for recovery from Florida Power Corporation's general body of ratepayers. We will review this acquisition in Florida Power Corporation's next rate case.

Going Concern Value

The Sebring electric utility system is a mature system with an established customer base. Customer load in the Sebring area is growing at a reasonable pace. The system itself is in reasonably good repair, and Florida Power Corporation does not anticipate that it will have to make substantial upgrades to the system in the near future. Florida Power Corporation and its ratepayers will benefit from the acquisition of this system through increased revenues, improved system efficiencies, and the resolution of longstanding territorial conflict.

Sebring's customers will benefit from the sale to FPC because they will receive immediate rate relief, even with the rider. Sebring's customers will also receive improved customer services from a professionally managed public utility, and the opportunity to participate in FPC's energy conservation programs, including FPC's successful load management program. The customer association, CURE, asserted at the hearing that the customers of Sebring would benefit from the sale because they would then receive electric service from a public utility subject to full regulation by the Commission. All commercial customers of Sebring who testified at the customer hearing supported the sale. Even the Sebring customers who opposed the sale at the customer hearing implicitly recognized the benefits they will receive when they testified that they approved of the acquisition by FPC, but simply did not approve of the rider.

It is our opinion that this acquisition will benefit all concerned, and thus we will permit Florida Power Corporation to include a "going concern value" for the purchase of the Sebring system in its rate base as a positive acquisition adjustment. We approve a going concern value in the amount of $5,741,000; which includes $4,491,000 for acquisition of the established customer base, $250,000 for the value of Sebrings' maps and records, $900,000 for the value of trained and experienced Sebring personnel that FPC will employ, and $100,000 for the avoidance of the costs of further territorial and annexation disputes. CCS argued that the "going concern value" should be considerably higher than the amount we have approved, but we cannot find reasonable support for a higher amount in the record, and we must insure that the amount we approve for recovery from FPC's general body of ratepayers is related to the benefits that they receive.

For the reasons mentioned above, we hold at this time that it is prudent for Florida Power Corporation to include $5,741,000 of going concern value for recovery from its general body of ratepayers. We will review the going concern value in Florida Power Corporation's next rate case to insure that the expected benefits materialize.

Assumption of the Purchased Power Contract with TECO

The "Agreement for Purchase and Sale of Electric System" provides that FPC will assume Sebring's obligations under its purchased power contract with TECO. By the terms of that contract FPC will purchase the amount of capacity needed to serve the Sebring system load. FPC intends to treat the capacity purchases from TECO as a system purchase to be combined with FPC's other

generation, and FPC expects that the TECO capacity purchases will benefit all of its ratepayers. We have reviewed the contract and we approve at this time the prudence of FPC's assumption of it. The fuel and capacity costs associated with the contract are appropriate for recovery through the fuel and capacity cost recovery clauses.

The Territorial Agreements

The petitioners have requested our approval of an amendment to their 1986 territorial agreement that reflects FPC's acquisition of the Sebring territory. The territorial agreement will continue in effect in order to determine which customers will be charged the Sebring rider. The petitioners have also requested our approval of the termination of the settlement agreement that attempted to eliminate duplicate facilities and provide for the orderly transfer of customers in the Sebring area. The settlement agreement is no longer necessary, because FPC will acquire Sebring's facilities. We approve the proposed amendment to the territorial agreement and the termination of the settlement agreement.

We also approve Sebring's assignment of its territorial agreement with Glades Electric Cooperative to FPC. FPC's assumption of that territorial agreement will prevent territorial conflict in Highlands County.

CONCLUSION

We believe that it is in the public interest to grant the relief the petitioners have requested here. On the record before us, it is clear that FPC's acquisition of the Sebring electric system is the most reasonable resolution of Sebring's financial problems. From our regulatory perspective the case has been a difficult one. As a general rule, we do not preapprove the prudence of rate base acquisitions outside of a rate case, nor do we usually permit acquisition adjustments, particularly outside of a rate case. As a general rule, we do not permit utilities to identify a pool of debt costs and apply those costs to a particular set of customers. Nevertheless, unique problems require unique solutions, and under this particular set of extraordinary circumstances, we believe our decision is in the best interest of all concerned. To those who would view our decision here as precedent, we uncategorically state that this decision has no precedential value. It is limited to the unique set of facts in this case. It does not signal a change in our regulatory policies in any way.

It is, therefore,

ORDERED, as explained in the body of this order, that the Sebring Rider rate and the methodology for changing that rate is approved. It is further

ORDERED that the inclusion of the SR-1 rate schedule as part of FPC's rates is approved. It is further

ORDERED that the net book value of Sebring's facilities of $17.8 million as of September 30, 1991 is approved. It is further

ORDERED that $5,741,000 of going concern value is approved as a prudent investment. It is further

ORDERED that Florida Power Corporation's purchase of Sebring's assets, including going concern value is approved as a prudent investment. It is further

ORDERED that Florida Power Corporation's assumption of the Purchased Power Agreement with TECO is prudent for cost recovery purposes. It is further

ORDERED that the amendment to the Petitioners' territorial agreement and withdrawal of the Settlement agreement is approved. It is further

ORDERED that Florida Power Corporation's assumption of the Sebring/Glades territorial agreement is approved. It is further

ORDERED that this docket shall be closed.

By ORDER of the Florida Public Service Commission this 17th day of December, 1992.

STEVE TRIBBLE, Director
Division of Records and Reporting

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Civil Procedure. The notice of appeal must be in the form specified in Rule 9.900 (a), Florida Rules of Appellate Procedure.