

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for approval of special contract
with the Florida Department of Corrections, by
Sebring Gas System, Inc.

DOCKET NO. 130079-GU
ORDER NO. PSC-13-0367-PAA-GU
ISSUED: August 8, 2013

The following Commissioners participated in the disposition of this matter:

RONALD A. BRISÉ, Chairman
LISA POLAK EDGAR
ART GRAHAM
EDUARDO E. BALBIS
JULIE I. BROWN

NOTICE OF PROPOSED AGENCY ACTION
ORDER APPROVING SPECIAL CONTRACT

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service Commission that the action discussed herein is preliminary in nature and will become final unless a person whose interests are substantially affected files a petition for a formal proceeding, pursuant to Rule 25-22.029, Florida Administrative Code (F.A.C.).

On April 5, 2013, Sebring Gas System, Inc. (Sebring or the Company) filed a petition for approval of a Special Contract (contract) with the Florida Department of Corrections (DOC) for transportation of natural gas to the Hardee Correctional Institution (HCI or the Facility) located in Hardee County, Florida. The Company also filed for approval of a Special Contract with the DOC for the DeSoto Correctional Institution (see Docket No. 130130-GU). The contract terms and conditions are substantially similar; however, the costs to serve differ. Sebring provides firm transportation service and does not engage in the sale of natural gas. As of December 31, 2012, Sebring had 397 customers with annual revenues of \$685,538.

HCI currently uses propane to provide heat, hot water, cooking, and laundry services but would like to convert to natural gas. There is no existing natural gas service within the vicinity of the Facility which is located in a rural, sparsely populated area in the northern part of the county. Subject to the terms of the contract, Sebring will transport natural gas on DOC's account from a delivery point on the Gulfstream Natural Gas System (Gulfstream) pipeline through Sebring's distribution system and redeliver the natural gas at the Facility. The contract has an initial term of fifteen years, and may be extended for additional periods of five years each.

Rule 25-9.034(1), F.A.C., requires that whenever a special contract is entered into by a utility for the sale of its product or services in a manner or subject to the provisions not specifically covered by its filed regulations and standard approved rate schedules, such contract must be approved by the Commission prior to its execution. The Commission has jurisdiction over this matter pursuant to Chapter 366, Florida Statutes.

Sebring's tariff addresses main extensions such as the one required for HCI. Specifically, the tariff states that the maximum cost to be incurred for an extension of facilities is defined as the maximum allowable construction costs (MACC), which is equal to four times the estimated annual revenue. Any cost above the MACC must be paid by the customer up front. HCI's MACC is \$252,816, which is below Sebring's investment of \$745,300 to serve HCI. Sebring noted that the DOC was not willing to pay any amount up front, so any contribution-in-aid-of-construction was not an option. After completing its cost analysis and negotiations with the DOC, the Company determined that it had no available tariff options other than a contract.

To provide natural gas transportation service to HCI, Sebring will interconnect with Gulfstream and install the necessary facilities up to the delivery point between it and the Facility. Sebring will obtain certain land rights through an easement from another party via its Interconnection Agreement with Gulfstream. The DOC does have the ability to bypass Sebring and directly interconnect with Gulfstream. However, this option would have resulted in substantial up front costs to the DOC that it was unwilling to pay (Gulfstream tap, gate station, etc.). Also, the DOC would have then been responsible for ownership of the distribution system and the ongoing operating and maintenance costs of the system. To the Company's knowledge, the DOC does not own natural gas distribution assets and does not have the resources to operate and maintain any such system.

To overcome the apparent inability of the DOC to provide any upfront payment toward the interconnection, the project will be financed through a new debt issuance obtained from Sebring's financial institution. As reflected in the cost analysis provided, the interest rate on the long term debt (fifteen years) is 6.25 percent. During the initial term, the DOC will pay approximately \$10,417 per month, escalated by 1.5 percent per year, beginning July 2015. The monthly rate of \$10,417 would initially generate annual transportation revenues of \$125,004, which will cover the estimated annual operating costs of \$109,989. In addition, Sebring noted that since the contract rate (\$10,417 per month) will generate more revenues than the standard tariff rate (\$5,267 per month), there would be no revenue shortfall to recover from the general body of ratepayers.

As noted above, the initial investment to serve HCI will be financed entirely by long-term debt incurred by Sebring. Combined with the investment contemplated in Docket No. 130130-GU to serve the DeSoto Correctional Institution (DCI), this debt issuance will significantly alter the current capitalization of the Company.¹ As of year-end December 31, 2012, Sebring's capitalization was approximately 63 percent equity and 37 percent debt as a percentage of investor capital. Based upon the amount of debt contemplated to fund the new investment,

¹ The total investment to serve both facilities is approximately \$1,554,300.

Sebring's capitalization would be approximately 33 percent equity and 67 percent debt. In response to Commission staff's second data request, the Company provided its projections for revenue, expense, and capitalization over the term of the proposed contracts. Based upon its forecasts, the Company projects to return to an equity ratio of 40 percent by 2014 and to an equity ratio of 50 percent by 2023. We have reviewed Sebring's projections and they appear reasonable. Thus, while the change in Sebring's capitalization as a result of incurring the debt associated with making the investment to serve HCI and DCI is significant, it appears the Company's relative level of capitalization will return to a financially strong position within a reasonable timeframe assuming the net margins associated with the contracts are achieved as represented and both facilities continuously take service over the stated term of the respective contracts.

The contract includes a provision that the DOC's obligation to pay for services is contingent upon an annual appropriation by the Legislature. This provision is standard in contracts with the State of Florida and has been approved by this Commission in the past.² Sebring believes that the likelihood of non-appropriation or insufficient appropriations is remote given that HCI is a maximum security facility. The Company has stated that if this scenario were to occur it would attempt to recover any remaining investment from its ratepayers through a general rate increase filing. However, in that event the Company would have the burden of demonstrating why any remaining investment should be recoverable through rates from its remaining ratepayers.

In light of the above, we hereby approve the contract between Sebring and the DOC. The contract will generate annual revenues of approximately \$125,004, which exceeds the annual cost (\$109,989) to serve by \$15,015, and the Commission will have the opportunity in the future to approve or disallow any request to recover costs associated with a default by the DOC.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the special contract between Sebring Gas System, Inc. and the Florida Department of Corrections for transportation of natural gas to the Hardee Correctional Institution, effective July 30, 2013, is hereby approved. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective upon the issuance of a Consummating Order unless an appropriate petition, in the form provided by Rule 28-106.201, Florida Administrative Code, is received by the Director, Division of the Commission Clerk and Administrative Services, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings" attached hereto. It is further

² See Order No. PSC-05-0784-PAA-GU, issued July 27, 2005, in Docket No. 050327-GU, In re: Petition by Florida Division of Chesapeake Utilities Corporation for approval of special contract with Department of Management Services, Agency of the State of Florida.

ORDERED that in the event this Order becomes final, this docket shall be closed.

By ORDER of the Florida Public Service Commission this 8th day of August, 2013.



ANN COLE
Commission Clerk
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399
(850) 413-6770
www.floridapsc.com

Copies furnished: A copy of this document is provided to the parties of record at the time of issuance and, if applicable, interested persons.

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing that is available under Section 120.57, 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 will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, in the form provided by Rule 28-106.201, Florida Administrative Code. This petition must be received by the Office of Commission Clerk, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on August 29, 2013.

In the absence of such a petition, this order shall become final and effective upon the issuance of a Consummating Order.

Any objection or protest filed in this/these docket(s) before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.