

April 16, 1996

The Honorable Susan F. Clark, Chairman
The Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

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Re: Test Year Notification Pursuant to Rule 25-7.140, F.A.C.

Dear Chairman Clark:

The purpose of this letter is to comply with the notice requirements set forth in Rule 25-7.140, Florida Administrative Code.

City Gas Company of Florida ("City Gas"), an operating division of NUI Corporation, intends to file a petition to modify City Gas' rates for service on June 18, 1996.

As part of its notification, City Gas submits the following information:

A. Test Year

City Gas intends to use the projected twelve-month period ending September 30, 1997, as the appropriate test year in its forthcoming revenue requirements proceeding. This period represents City Gas' fiscal period for purposes of budgeting and financial reporting. Because the Company has drawn on its budgeting process to project revenues and expenses for the period, and because the timing of the case is such that rates will take effect during the course of the period, City Gas believes that it will be representative of conditions in which the new rates set in the case will function.

B. Major Factors Necessitating an Increase in Rates

The following factors contribute significantly to the need for a rate case at this time:

1. Despite the Company's best efforts to control its costs, the rates established in Docket No. 940176-GU, City Gas' last rate case, have failed to

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produce revenues sufficient to provide an adequate return on the Company's investment. In that docket, the Commission established a range for rate of return of 6.96% to 7.56%. City Gas' actual earned rate of return for the period ending January 31, 1996 was only 5.38%. City Gas projects that, absent rate relief, the earned rate of return will continue to fall below the range established as reasonable. An inadequate return unfairly penalizes the Company's shareholders. Moreover, inadequate rates deny the Company the financial strength and integrity necessary to undertake capital additions designed to improve the Company's quality of service and extend that service to more customers. Rectifying this situation is one of the primary objectives of the forthcoming rate case.

2. The Company has invested \$4.6 million in infrastructure to serve its franchise in City of Port St. Lucie. In Docket No. 940176-GU, the Commission included only a portion of the Company's investment in rate base. However, it ruled that the Company could request additional rate base treatment of the excluded amount when it was prepared to demonstrate that additional portions of that investment meet appropriate criteria of economic feasibility. The Company will do so in the next rate case.

3. NUI Corporation is also well into the process of putting in place an increased investment in managerial infrastructure. City Gas and its customers will benefit from efficiencies associated with the consolidation and centralization of some functions and modernization of others. Examples are newly centralized accounting functions and a new, computerized customer service system. While these tools and measures have the net effect of increasing the O&M portion of the Company's cost of service in the short run, they are needed to position the Company to serve the Company's projected growth in services and the accompanying demands on its resources. In the upcoming case, City Gas will identify and quantify these additional components of City Gas' total cost of service.

4. In the past, City Gas has taken advantage of market opportunities to use short-term debt to finance its operations. While the practice helped minimize the cost of individual capital outlays during the period when short-term interest rates were very favorable, it contributed to the development of an equity ratio that is unacceptably "thin" for the longer term. NUI Corporation, of which City Gas is a part, is currently taking measures to strengthen its capital structure by increasing the equity component to a level that moves closer to industry standards. The next case will reflect the additional costs associated with a higher proportion of equity capital.

5. As the Commission is aware, the natural gas industry is becoming increasingly competitive. On earlier occasions, such as the applications of natural gas distribution companies for pricing flexibility within their interruptible tariffs, the Commission recognized the benefits to other customers of allowing the gas utilities

to compete on the basis of price in order to retain large customers who have the ability to use alternate sources of fuel. The same competitive forces that compel pricing flexibility also require that the Company act to eliminate any artificial subsidies now incorporated in its base rates. Presently, the Company's Commercial rate schedules price service to customers at levels well above the cost to serve them, while residential customers pay rates that are priced below cost. This situation exacerbates the threat that the Company may not be able to compete effectively with alternatives, to the ultimate detriment of its general body of ratepayers. One purpose of the Company's rate case will be to achieve meaningful progress in aligning the rates customers pay with the costs to Company incurs to serve them.

The major cost items and their estimated impacts on revenue requirements are:

Estimated Impact on Revenue Requirements Amount (Approximate)	
I.	Increase in Rate Base (approx. \$9 million) (Plant Growth; System Improvements; Increased Development of Port St. Lucie) \$1.4 million
II.	Increases in Cost of Service Attributed to:
A.	Improvements in Managerial Infrastructure (Gas Control, Purchasing Controls, Human Resources Management, Budgeting and Financial Controls, Rates and Regulatory Administration, Customer Service System) \$ 1.7 million
B.	Re-targeted Sales and Marketing Focus \$.3 million
C.	Strengthened Capital Structure \$.9 million
D.	Other O&M Increases \$.5 million
III.	Offsetting Increase in Revenues \$(1.8 million)
C.	<u>Steps Taken to Avoid an Increase</u>
1.	The Company has reduced its number of employees from 296 in August of 1994 to approximately 250.

2. The Company has attempted to minimize the cost of financing operations by taking advantage of opportunities presented by fluctuating conditions in capital markets.

3. The Company engaged a consultant to conduct a review of its salary levels and benefits relative to those elsewhere in City Gas' labor market, to ensure that City Gas' payroll expense is both reasonable and adequate to attract and retain qualified employees. As one result, the Company replaced its ESOP program with a 401K program.

4. The Company has instituted a program of rigorously reviewing expansion proposals at multiple levels of management, ensuring that the Company will undertake only economically feasible expansions.

Despite these and other measures, the need to restore the Company's financial integrity, the need to realize a return on prudent investment not yet reflected in rate base, the costs of modernizing management tools, and the need to position the Company to meet the demands and challenges of growth in a competitive environment require City Gas to file a rate case at this time.


D. **Procedure**

City Gas requests the Commission to utilize the procedure governing Proposed Agency Action for the processing of its revenue requirements case, as authorized in Section 366.05, Florida Statutes.

City Gas respectfully requests the Commission to approve the period ending September 30, 1997 as to the test period for the case.

Yours truly,

**CITY GAS COMPANY OF FLORIDA,
AN OPERATING DIVISION OF NUI CORPORATION,**


By: Michael A. Palecki, Vice President
of Regulatory Affairs

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