

FLORIDA PUBLIC SERVICE COMMISSION
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M E M O R A N D U M

May 9, 1996

TO : DIRECTOR, DIVISION OF RECORDS AND REPORTING *WLL* *JA* *CM* *RLT*

FROM: DIVISION OF ELECTRIC AND GAS (MAKIN, GING, MILLS) *WLL* *JA*
DIVISION OF LEGAL SERVICES (JOHNSON) *WLL* *MCB*

RE : DOCKET NO. 960385-GU - ST. JOE NATURAL GAS COMPANY, INC.
PETITION FOR APPROVAL OF SERVICE AGREEMENT FOR FIRM
TRANSPORTATION SERVICE WITH FLORIDA DEPARTMENT OF
MANAGEMENT SERVICE AND FLORIDA DEPARTMENT OF CORRECTIONS

AGENDA: MAY 21, 1996 - REGULAR AGENDA - TARIFF FILING ISSUE 1 -
PROPOSED AGENCY ACTION ISSUE 2 - INTERESTED PERSONS MAY
PARTICIPATE

CRITICAL DATES: MAY 27, 1996 - 60-DAY FILE AND SUSPEND - ISSUE 1

SPECIAL INSTRUCTIONS: S:\PSC\EAG\WP\960385.RCM

CASE BACKGROUND

The Governor's Executive Order No. 92-253, Section 4(c) dated October 8, 1991, requires state agencies to develop a procedure for the cost-effective bulk purchase of natural gas and other energy-efficient fuels. As a result of this order, the Department of Management Services' Division of Purchasing issued a Request for Proposal to establish a centralized contract for the capacity management and acquisition of natural gas supply. The contract was established for all state agencies. The Department of Corrections is the first agency to begin using natural gas immediately. As a result of this Request for Proposal, a contract was executed with Florida Gas Transmission Company (FGT), and became effective November 1, 1994, with an initial period of five years, and a five year renewal option.

Some state sites are currently using natural gas obtained directly from FGT, local distribution companies, or municipalities. In cases where facilities are not presently using natural gas, new gas pipelines will have to be extended to allow delivery of natural gas. Following installation of the pipeline, on-site boilers, heaters, kitchen, and laundry equipment will be converted to natural gas. In most instances, the service-line extensions and on-site piping and equipment conversions are being provided by the

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utility serving those sites. Since some of the state site extensions will exceed the maximum capital investment allowed by tariff, the State will typically repay the remaining amount in equal payments over time as an addition to the monthly gas bill. The additional costs to be borne by the State will be covered by fuel cost reductions or justified by avoided fuel spill clean-up costs, reduced boiler operation and maintenance costs, reduced boiler inspection certification costs, and other factors.

Prior to the establishment of the centralized gas procurement contract, state agencies purchased natural gas on a site-by-site basis while fuel oil and liquified petroleum gas were purchased under state contract. The Division of Purchasing's objective is to minimize the use of fuel oil whenever economical to improve environmental conditions and eliminate delivery concerns.

The centralized gas procurement contract allows for competitive pricing with negotiated transportation rates and reduces the need for on-site staff experienced in gas acquisition. Conversion of on-site equipment will be negotiated with the Local Distribution Companies on a site-by-site basis. The Department of Management Services (DMS) will sign a transportation agreement with each gas utility to allow the State's gas to flow through their system.

It is envisioned that other State Facilities will, from time to time, be added to the centralized gas procurement contract through duly executed modifications for the purposes of effectuating natural gas transportation. Normally, such facilities will be served under the same terms and conditions contained in the contract unless otherwise specified.

The Florida Department of Corrections (DOC) now seeks to use natural gas at the Gulf County Correctional Institution. However, because of the location, the correctional institution cannot obtain the gas directly from FGT. As a result, DMS and DOC have entered into an agreement with St. Joe Natural Gas Company, Inc. (St. Joe) for the transportation of gas by St. Joe to the correctional institution. This recommendation addresses that agreement with St. Joe.

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DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve St. Joe's proposed agreement for firm transportation with the Florida Department of Management Services and Department of Corrections?

RECOMMENDATION: Yes. The Commission should approve the agreement for firm transportation with DMS and DOC, effective the date of the Commission vote.

STAFF ANALYSIS: The purpose of the agreement/special contract is to establish the terms, conditions and rates for transportation of natural gas to state facilities. Under this agreement, DMS will arrange for natural gas transportation on behalf of the State of Florida. St. Joe agrees to provide transportation on its system for DMS for a minimum annual amount of 400,000 therms to the Gulf County Correctional Institution outside the city of Wewahitchka.

The only difference between this agreement and St. Joe's tariff is the inclusion of a minimum take-or-pay provision of 33,340 therms per month, and the issuance of credits for prepaid gas (required to pay for delivery of gas or gas service not received). The rates and charges are the same as the present Contract Transportation Service rate schedule.

DMS recognizes that the specific rate for service (present Contract Transportation Service rate schedule) may be revised or amended from time to time under authority granted by the Commission, and such revisions or amendments will be applicable to the character of and rates for service.

DMS will be responsible for securing its own gas supply, for the transportation of such gas upstream of St. Joe's system, and for all costs incurred in connection with the purchase of gas and upstream transportation. Gas delivered to St. Joe for transportation under this agreement shall remain the property of DMS during such transportation. DMS agrees to comply with all applicable tariff provisions of any pipeline which transports gas for DMS upstream of St. Joe's system. DMS, or its designated agent, will furnish St. Joe copies of all nominations or scheduling which shall be made directly to Florida Gas Transmission or which may be received by Florida Gas Transmission five days prior to the first of the month.

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ISSUE 2: Should the Commission approve St. Joe's request that its proposed investment is prudent, and should be included in rate base upon the completion of the expansion project?

RECOMMENDATION: Yes. The Commission should approve St. Joe's request that its investment is prudent, and should be included in rate base upon completion of the expansion project.

STAFF ANALYSIS: Currently, there is no pipeline through which gas can be transported to the correctional institution. Thus, the fifteen-year agreement, will require St. Joe to expand its existing facilities. The expansion project will consist of 8.52 miles of four-inch steel high pressure mains, and associated facilities. The estimated cost of the expansion to serve the correctional institution is \$452,843. The estimated revenue, based on the Commission approved Maximum Allowable Construction Cost (MACC) formula is \$125,000. St. Joe will finance the expansion by procuring a loan of up to \$450,000.

Because the investment required by St. Joe to serve the correctional institution is significant when compared to the rate base of \$4,200,000, St. Joe has requested preliminary determination by the Commission that the correctional institution expansion project investment is prudent. Further, St. Joe seeks approval from the Commission that at the conclusion of the expansion project, the projected investment of \$452,843 be added to its rate base. This request for prudent investment and rate base inclusion, is the same as St. Joe requested in Docket No. 940548-GU, Order No. PSC-94-0833-FOF-GU, for the Wewahitchka expansion.

The cost estimates as detailed in the filing appear reasonable. To minimize labor costs and maintain control over the project, St. Joe will use existing personnel to construct the facilities rather than subcontractors. As previously stated, the total cost of the project is projected to be \$452,843. While these costs represent approximately 10 percent of St. Joe's existing rate base, St. Joe is not seeking to increase its rates at this time.

St. Joe currently serves approximately 3,090 residential, commercial, and industrial customers in the City of Port St. Joe, Mexico Beach, and unincorporated areas of Gulf County. St. Joe has not petitioned for rate relief since 1967. However, since 1967, the Commission has reduced St. Joe's rates twice due to over earnings.

St. Joe has one very large industrial customer, St. Joe Paper Company. This company takes approximately 66 percent of St. Joe's volumes equating to a 75 percent contribution to revenues. Until 1988, St. Joe provided gas service to St. Joe Paper under a

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negotiated rate. While the two entities were satisfied with the negotiated rate, the revenues received from St. Joe Paper continually lead to overearnings for St. Joe. Exacerbating the over earnings problem is the continued decline of St. Joe's rate base. Since St. Joe's ability to expand its system, is limited, the existing rate base is being depreciated.

While it is not the Commission's normal practice to make a determination of cost effectiveness before construction of an expansion project, St. Joe has requested prior approval for this project. Ordinarily, the risk of imprudent investment is assumed by the stockholders. However, because of the significance in the dollar amount of the investment relative to St. Joe's current rate base, staff believes it is appropriate for the Commission to address the issue of prudence at this time. An after-the-fact disallowance of the investment would have a detrimental impact upon the Company. Prior approval will assist the Company in obtaining financing for the project.

This project is different from most large industrial gas loads in that it is a government owned facility. There is a low risk of contract default. The Department of Corrections, by accepting a take-or-pay provision, is guaranteeing revenue to St. Joe. There is also potential for increased gas load with any future expansion of the facility. Any additional increase in gas load by the prison or new customers on the line has not been factored into the review. Increased gas usage is likely and would result in a more favorable feasibility analysis.

Because of the unique circumstances relating to this project and St. Joe, staff believes the project should be approved even though it does not meet the Commission approved Maximum Allowable Construction Cost (MACC) formula at this time. If approved, this project will benefit all parties involved and will not impact the existing ratepayers at this time unless St. Joe files for rate relief. As indicated above, St. Joe has not petitioned for rate relief since 1967.

The service agreement for firm transportation service between St. Joe and DMS/DOC will provide natural gas service to customers who otherwise would not have natural gas available, will increase customer base, will provide savings to the State of Florida, and will not effect existing customers. Accordingly, given the circumstances, Staff recommends the Commission approve St. Joe's petition, effective the date of Commission vote.

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ISSUE 3: Should St. Joe be required to file a detailed costing report after completion of the expansion project?

RECOMMENDATION: Yes. St. Joe should be required to file a detailed costing report with the Division of Records and Reporting 30 days after completion of the expansion project.

STAFF ANALYSIS: To assist the Commission in its continued prudence evaluation, St. Joe should be required to file a detailed costing report 30 days after completion of the expansion project. The report should show the detail of all construction costs. If a deviation from the Company's projections of costs is determined, this matter would be brought before the Commission for disposition.

ISSUE 4: Should this docket be closed?

RECOMMENDATION: No. This docket should remain open pending receipt of St. Joe's detailed costing report. With the adoption of Staff's recommendation in Issue 1, this agreement should become effective the date of Commission vote. If a protest is filed within 21 days from the issuance date of the order, the agreement should remain in effect pending resolution of the protest. If no timely protest is filed, and if upon review of the report, no variance is detected, this docket should be closed administratively.

STAFF ANALYSIS: This docket should remain open until St. Joe submits its final detailed costing report and staff has analyzed the data. If Staff's recommendation in Issue 1 is adopted, this agreement should become effective the date of Commission vote. If a protest is filed within 21 days from the issuance date of the order, the agreement should remain in effect pending resolution of the protest.