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# Public Service Commission

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COMMISSION CLERK

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**DATE:** October 7, 2003
**TO:** Kay Flynn, Division of the Commission Clerk and Administrative Services
**FROM:** John Slemkewicz, Division of Economic Regulation JS
**RE:** Docket No. 030438-EI, Florida Public Utilities Company Rate Case - Documents

Attached are two documents for inclusion in the docket file for Docket No. 030348-EI, Petition for Rate Increase by Florida Public Utilities Company (FPUC). The two documents are:

- Test Year Notification Letter from George Bachman (FPUC) to Chairman Jaber, dated May 9, 2003
- Letter from Chairman Jaber to George Bachman, dated May 16, 2003

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LILA A. JABER
CHAIRMAN

STATE OF FLORIDA

CAPITAL CIRCLE OFFICE CENTER
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850
(850) 413-6044

# Public Service Commission

May 16, 2003

Mr. George M. Bachman
CFO and Treasurer
Florida Public Utilities Company
Post Office Box 3395
West Palm Beach, Florida 33402-3395

Dear Mr. Bachman:

In response to your May 9, 2003, test year notification letter, Docket No. 030438-EI has been opened for Florida Public Utilities Company's forthcoming general rate increase proceeding for its electric division. It has been noted that the Company proposes to utilize a projected twelve-month period ending December 31, 2004, as the test year for the permanent rate proceeding. The Company has also proposed to combine its heretofore two separate (for ratemaking purposes) electric divisions into a single Consolidated Electric Division. However, the appropriateness of the selected test year and the consolidation of the electric divisions may be issues in the proceeding.

The Minimum Filing Requirements and associated testimony will be due at the Commission's offices on or before August 31, 2003. If the Company is unable to file by that date, it must notify the Commission in accordance with the provisions of Rule 25-6.140(3), Florida Administrative Code.

If you should have any questions, please contact John Slemkewicz, Public Utilities Supervisor, in the Division of Economic Regulation, at (850) 413-6420.

Sincerely,

Lila A. Jaber
Chairman

LAJ/JS
cc: Tim Devlin
C:\WINDOWS\Temporary Internet Files\OLK1A2\FPUCRateCaseNotice-LAJ wpd

**Florida Public Utilities Company**

P O Box 3395P O Box 3395
West Palm Beach, FL 33402-3395
(561) 838-1725

May 9, 2003

The Honorable Lila Jaber, Chairman
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Dear Chairman Jaber:

After considerable review and analysis, Florida Public Utilities Company ("FPUC" or the "Company") now finds it necessary to file with the Florida Public Service Commission ("Commission") for an increase in our rates and charges in order that we may have the opportunity to earn a fair rate of return on our investment in utility plant and working capital. Earning a fair rate of return will enable us to continue our high quality of service and maintain financial integrity, which are in the best interest of our customers. The Company has experienced and is expecting to experience continued increases in expenses, and despite efforts to keep expenses down, many are beyond the control of the Company and we expect a significant declining rate of return in our electric operations. Our last Marianna (Northwest Florida Division) electric rate case, Docket No. 930400-EI, authorized an increase in revenues, which went into effect in February 1994 and our last Fernandina Beach (Northeast Florida Division) electric rate case, Docket No. 881056-EI, authorized an increase in revenues, which went into effect in November 1989.

In this proceeding the Company will be proposing to combine their two electric divisions and proceed with a Consolidated Electric Division. The case will be filed on a consolidated basis. We believe this will be to the benefit of our customers as we move forward. The Company shares many resources between electric divisions and this will only increase in the future as measures are taken to increase reliability and safety in our operations. Also, the current total billing cost to customers including fuel is not materially different between the divisions and our customers will benefit in the future by additional savings through lower administrative costs.

In accordance with Rule 25-6.140, F.A.C., Test Year Notification, we have selected the twelve-month period ending December 31, 2004 as the projected test year for our petition to increase our rates and charges. We offer the following reasons for selecting this period:

1. The calendar year serves also as our fiscal year for accounting purposes.

2. The new rates developed in this rate case will be effective on or after January 1, 2004.

3. The Company believes the proposed 2004 test year will accurately reflect the economic conditions in which the Consolidated Electric Division will be operating during the first twelve months the new rates will be in effect.

4. The overall rate of return for the twelve-month periods ending December 31, 2003 and 2004 will decline below our allowable rate of returns based on our projections for 2003 and 2004.

As required in the above rule, we submit the following major factors, which necessitate a rate increase along with their estimated annual revenue requirement impact:

1. Recent events will have a significant unfavorable impact to earnings in upcoming financial periods. The decline of the stock market has greatly decreased the value of the pension plan assets and will significantly increase pension expense in 2003 and 2004. Current actuarial estimates show pension expense increasing by approximately $1,300,000 in 2003 over 2002 and the estimated annual impact to the Consolidated Electric Division is $350,000.

2. Industry events, the events of September 11, 2001, and the stock market decline, have resulted in greatly increased insurance costs. Effective September 2002, insurance costs increased approximately $600,000 annually. Workers' compensation insurance increased about $125,000 per year effective October 1, 2002. Both increases will carry over into 2003 and 2004. Management also believes that medical costs will also increase approximately $1,000,000 due to these same reasons in 2003 and 2004 and the Company made revisions to the medical plan to help minimize the effect on operating income. The estimated annual impact to the Consolidated Electric Division is $500,000.

3. Accounting, auditing, and tax service expenses are increasing by an estimated $250,000 annually. This is due to additional work requirements of recent regulations on the external auditors including Sarbanes-Oxley Act and an expanded internal audit and tax program. The estimated annual impact to the Consolidated Electric Division is $100,000.

4. On December 3, 2002 the Company entered into an agreement to sell certain assets comprising its water utility system to the City of Fernandina Beach. Condemnation by the city had also been a concern and was a factor in our decision to sell the water division. The sale and closing of this transaction took place on March 27, 2003. The Company lost synergies as a result of this sale and the estimated annual impact to the Consolidated Electric Division is $400,000.

5. Based on a review of the adequacy of storm reserves, the reserves are believed to be currently deficient. To bring the reserves to an adequate level over a period of ten years, the estimated annual impact to the Consolidated Electric Division will be determined prior to the conclusion of this rate proceeding.

6. The Company requires a new office/warehouse complex in our Fernandina Beach area. The Marianna office was replaced in 1993. Our FB office/warehouse complex ranges in age of 20 years to primarily over 70 years of age and the current facilities are inadequate to fulfill our current and future requirements. The estimated annual impact to the Consolidated Electric Division is $60,000.

7. Significant upgrades to other facilities and equipment. The estimated annual impact to the Consolidated Electric Division is $250,000.

8. New marketing programs to assist with customer growth and competition with alternative energy sources. The estimated annual impact to the Consolidated Electric Division is $250,000.

9. Additional reliability and safety measures are necessary and are expected to result in additional tree trimming crews, system monitoring equipment, safety personnel programs, and associated software, etc. The estimated annual impact to the Consolidated Electric Division is $390,000.

10. Inflationary effect on new and replacement utility plant and on operating expenses over the 10 to 15 year period since our last rate cases. The estimated annual impact to the Consolidated Electric Division is unknown at this time.

11. Adjustments in annual depreciation expense that may result from revised new depreciation rates effective with the finalization of our consolidated electric depreciation study to be filed in conjunction with this rate proceeding. The estimated annual impact to the Consolidated Electric Division is unknown at this time.

Since our last electric rate cases, the following measures were implemented for the purpose of reducing revenue requirements:

1. Managing capital expenditures to stay in line with expected increases in customer growth and inflation. Reviewed capital expenditures to try and ensure the increase in net plant per customer amount was kept consistent.

2. Improved productivity in the construction crews by purchasing improved equipment, implementing the use of two-man crews and measurement of productivity results.

3. Consolidated the divisional operations into one location in the Northwest Florida Division (Marianna).

4. Improved purchasing functions in order to reduce costs and achieve better inventory control.

5. Implemented shift work in Northwest Florida (Marianna) to include a weekday evening crew and Saturday crew to reduce overtime costs and better respond to customer requests.

6. Improved efficiencies in the office productivity by expanding the use of computers. This included the use of email to increase communication productivity and reduce paperwork.

7. Issuance of short-term and long-term debt with favorable interest rates to assist in the financing requirements of capital and operating expenditures.

8. Changed external audit firms to help offset the cost increases as a result of expanding requirements from the SEC and accounting regulations.

9. Sale of the water division at a favorable price to eliminate the possibility of condemnation that could have resulted in a lower sales price and increased costs of sale. This reduced our need to issue additional equity, and allowed us to pay down our line of credit. It also allows us to delay the need to obtain additional equity financing sources at a higher cost to the customers.

10. To hold down rising medical insurance costs we have made changes in medical programs, premiums and deductibles over the years including 2002.

11. The Company historically has been able to manage costs. Steps are taken to budget and find ways to keep costs down on a continual basis.

FPUC will be filing MFR schedules consistent with current Commission minimum filing requirements and those filed in our last rate case for our Marianna Division, Docket No. 930400-EI with certain modifications and waivers noted in Attachment A, which is a copy of a Petition for Waiver of Certain MFR schedules. This petition was developed after consultation with Staff and is being filed with the Commission Clerk for handling. Also, as noted the Company is filing this as a Consolidated Electric Division filing with one combined set of data for Cost of Service and all financial information and requests that the Commission acknowledge and accept this proposal. Finally, the calendar year 2004 will be presented as the projected test year, calendar year 2003 will be presented as the projected prior year and the calendar year 2002 will be presented as the historic year.

The Company has not undertaken this filing without a considerable amount of study. We have undertaken to provide quality service to our customers and to tightly control our expenses. Our rates are among the lowest in Florida; but we are experiencing increases which are beyond our control and we cannot continue to maintain a high quality of service and customer satisfaction at the current rates.

We plan to file the minimum filing requirements (MFRs) for rate relief on or before August 31, 2003 and will advise you if this date cannot be met. We are not requesting that this be processed as a PAA. If you need any additional information, please let me know.

Sincerely,

George M. Bachman

George M. Bachman
CFO and Treasurer

CC:
Office of Public Counsel
Norman Horton, Esq.
Mark Cutshaw
Jack English
Mario Lacaci
Cheryl Martin
Chuck Stein