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MEMORANDUM

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July 18, 2006

COMMISSION
CLERK

TO: DIVISION OF THE COMMISSION CLERK AND ADMINISTRATIVE SERVICES

FROM: OFFICE OF THE GENERAL COUNSEL (BRUBAKER) *JB*

RE: DOCKET NO. 041272-EI Petition for approval of storm cost recovery clause for recovery of extraordinary expenditures related to Hurricanes Charley, Frances, Jeanne, and Ivan, by Progress Energy Florida, Inc.

Attached is a letter dated July 18, 2006 to Jennifer Brubaker, Senior Attorney from Progress Energy, signed by R. Alexander Glenn, to be filed in the above-referenced docket.

DATE DOCUMENT SENT TO CCA 7/18/06

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(Writer's Direct Dial No. 727-820-5587)

R. ALEXANDER GLENN
Deputy General Counsel - Florida

By Hand Delivery and Electronic Mail

July 18, 2006

Jennifer Brubaker, Esq.
Senior Attorney
Florida Public Service Commission
Capitol Circle Office Center
2450 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

Re: Docket No. 041272-EI – Petition for approval of storm related cost recovery clause for recovery of extraordinary expenditures related to Hurricanes Charley, Frances, Jeanne, and Ivan, by Progress Energy Florida, Inc.

Dear Ms. Brubaker:

This letter is provided in response to your request for additional information regarding the Stipulation and Settlement Agreement (“Stipulation”) negotiated by the parties in this case. More specifically, this letter discusses the appropriateness of approving the Stipulation, including the provision authorizing a prospective interim storm surcharge to be implemented if Progress Energy Florida’s (“PEF”) storm reserve account is exhausted.

I. The Commission’s Approval of the Stipulation is Consistent With the Commission’s Policy of Encouraging Settlements

The Commission should approve the Stipulation, which was negotiated and approved by PEF, the Office of the Public Counsel, AARP, Sugarmill Woods Civil Association, Inc., Buddy L. Hansen, the Florida Industrial Power Users Group (“FIPUG”), and the Florida Retail Federation, because doing so is consistent with and supports the Commission’s long-standing policy of looking favorably upon and encouraging fair and reasonable settlements between parties. *See In re: Petition for rate increase by PEF, Docket No. 050078-EI, Order No. PSC-05-0945-S-EI (Sept. 28, 2005)* (“this Commission has a long history of encouraging settlements, giving great weight and deference to settlements, and enforcing them in the spirit in which they were reached by the parties.”); *In re: Petition for rate increase by Florida Power & Light Company (“FPL”), Docket No. 050045-EI, Order No. PSC-05-0902-S-EI (Sept. 14, 2005)*(same); *In re: Application for rate increase in Bay County by Bayside Utility Services,*

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Inc., Docket 030444-WS, Order No. PSC-05-0146-AS-WS (Feb. 7, 2005)(approving a settlement agreement, which had indicated that it was entered into by the parties "in order to avoid the time, expense and uncertainty associated with adversarial litigation, and in keeping with the Commission's long-standing policy and practice of encouraging parties in protested proceedings to settle issues whenever possible"). Further, as with any settlement approved by the Commission, nothing in the Stipulation "diminishes this Commission's ongoing authority and obligation to ensure fair, just, and reasonable rates." Order No. PSC-05-0902-S-EI.

II. Provision of Stipulation Authorizing Interim Storm Surcharge

You expressed some concerns regarding the basis upon which the Commission has the authority to approve the implementation of an interim surcharge, as outlined in Paragraph 3 of the Stipulation. The Commission does have the authority to approve the Stipulation negotiated and accepted by PEF, the Office of the Public Counsel, AARP, Sugarmill Woods Civil Association, Inc., Buddy L. Hansen, the Florida Industrial Power Users Group, and the Florida Retail Federation, including the proposed interim storm surcharge set forth in Paragraph 3. Approval of the Stipulation would not be an abdication of the Commission's authority to set rates in accordance with statutes and rules because the storm surcharge is nothing more than a prospective rate, which the Commission has the power to approve and which the Commission regularly does approve. Further, the process to be used in implementing the surcharge (tariff filing) is subject to the "file and suspend" process set forth by statute, which permits the increase of rates without Commission approval, subject to the Commission's authority to suspend the rates. Finally, the interim surcharge is subject to refund, with interest, upon a formal evaluation by the Commission in a full hearing.

The Commission has broad authority to set rates. The Commission has jurisdiction to regulate and supervise each public utility with respect to its rates and service, *see* Section 366.04(1), Florida Statutes, and has the power to prescribe fair and reasonable rates and charges to be applied to each public utility, *see* Section 366.05(1), Florida Statutes. The Commission has considerable discretion and latitude in the ratemaking process. *See Citizens v. Public Serv. Comm'n*, 425 So. 2d 534, 540 (Fla. 1982)("This Court has consistently recognized the broad legislative grant of authority which these statutes [Sections 366.06(2) and 366.05(1), Florida Statutes] confer and the considerable license the Commission enjoys as a result of this delegation."); *Gulf Power Co. v. Bevis*, 296 So. 2d 482, 487 (Fla. 1974)("As pointed out by the Commission, it has considerable discretion and latitude in the rate-fixing process."); *Storey v. Mayo*, 217 So. 2d 304, 307 (Fla. 1968)("The regulatory powers of the Commission . . . are exclusive and, therefore, necessarily broad and comprehensive."); *City of Miami v. Fla. Public Serv. Comm'n*, 208 So. 2d 249, 253 (Fla. 1968)("It is quite apparent that these statutes [Sections 364.14 and 366.06, Florida Statutes,] repose considerable discretion in the Commission in the rate-making process."). As part of its broad power to set rates, the Commission has authority to approve and regularly does approve prospective rate increases.

A. PEF's Interim Storm Recovery Surcharge is Nothing More Than a Prospective Rate Increase, Which the Commission Has the Authority to Approve

The Commission has the power to approve prospective increases and routinely does so. The Commission's authority to approve prospective rate increases has been expressly recognized by the Florida Supreme Court. In *Floridians United for Safe Energy, Inc. v. Public Service Commission*, the Commission had granted FPL a rate increase for 1984 and a subsequent rate increase in 1985. 475 So. 2d 241 (Fla. 1985). The Floridians United group challenged the Commission's authority to grant the subsequent year increase based on the then-newly created Section 366.076, Florida Statutes (addressing limited proceedings and rules on subsequent adjustments). *Id.* at 242. The Florida Supreme Court found that the Commission had authority and had always had authority (even prior to the enactment of Section 366.076) to grant subsequent year rate increases. *Id.* The Court also clarified that:

At the heart of this dispute is the authority of PSC to combat "regulatory lag" by granting prospective rate increases which enable the utilities to earn a fair and reasonable return on their investments. We long ago recognized that rates are fixed for the future and that it is appropriate for PSC to recognize factors which affect future rates and to grant prospective rate increases based on these factors.

Id. (citing *Citizens of Fla. v. Hawkins*, 356 So. 2d 254 (Fla. 1978); *Gulf Power Co. v. Bevis*, 289 So. 2d 401 (Fla. 1974); *City of Miami*, 208 So. 2d 249). Thus, the Court acknowledged the Commission's authority to approve prospective rate increases and affirmed the Commission's order which had established prospective increases for FPL. *Id.*¹

The Commission's authority to approve prospective increases has been regularly recognized and exercised by the Commission. See *In re: Application for a rate increase by Tampa Electric Company ("TECO")*, Docket No. 920324-EI, Order No. PSC-93-0165-FOF-EI (Feb. 2, 1993)(authorizing a revenue increase in 1993 and an additional increase to be effective January 1, 1994); *In re: Petition for a rate increase by Florida Power Corporation*, Docket No. 910890-EI, Order No. PSC-92-1197-FOF-EI (Oct. 22, 1992)(authorizing three prospective rate increases to take effect in November 1992, in April 1993 and in November 1993). See also *In re: Fuel and purchased power cost recovery clause with generating performance incentive factor*, Docket No. 050001-EI, Order No. PSC-05-1252-FOF-EI (Dec. 23, 2005)(the Commission explained that "we will sometimes approve step increases over a period of time to reduce rate shock to the extent we find the costs to be prudent and reasonable.").

Recently, the Commission approved prospective rate increases in PEF's and FPL's 2005 rate settlement cases. See Order No. PSC-05-0945-EI (approving an increase to base rates "to recover the full revenue requirements of the installed cost of Hines Unit 4 and the unit's non-fuel operating expenses," starting "on the commercial in-service date of Hines Unit 4"); Order No. PSC-05-0902-S-EI (approving an increase to base rates reflected on customer bills for "any

¹ Further, in *City of Miami*, the Florida Supreme Court, quoting from a policy statement made by the Commission, stated that in periods of instability, unusual activity or increasing costs, "conventional notions of rate making must be adjusted to the circumstances." 208 So. 2d at 253.

power plant that is approved through the Power Plant Siting Act and that achieves commercial operation within the term of the Stipulation and Settlement," beginning on "the commercial in-service date of the plant.").

Further, regarding storm recovery losses specifically, the Commission has indicated that it has the power to adopt a pass-through mechanism:

Our vote today does not foreclose or prevent further consideration of some type of a cost recovery mechanism, either identical or similar to what has been proposed in this petition. The Commission could implement a cost recovery mechanism, or defer costs, or begin amortization, or such other treatment as is appropriate, depending on what the circumstances are at that time.

In re: Petition to implement a self-insurance mechanism for storm damage to transmission and distribution system and to resume and increase annual contribution to storm and property insurance reserve fund by FPL, Docket No. 930405-EI, Order No. PSC-93-0918-FOF-EI (June 17, 1993). Just last year, in Docket No. 041291-EI, the Commission quoted this same paragraph, in determining that FPL could initiate a storm recovery surcharge based on a prior stipulation. *See In re:* Petition for authority to recover prudently incurred storm restoration costs related to 2004 storm season that exceed storm reserve balance, by FPL, Order No. PSC-0500187-PCO-EI (Feb. 17, 2005). In addition, the Commission recognized that it had established "pass-through mechanisms for certain costs" and that it was within the Commission's discretion to consider a surcharge as a means of cost recovery. *Id.*

Thus, the Commission's approval of the Stipulation would not be an abdication of its ratemaking authority because the Commission's approval of the Stipulation's interim storm recovery surcharge would be, in effect, the approval of a prospective increase. This instance is no different from the Commission's approval of the prospective rate increases for plant additions as part of the PEF and FPL rate case settlements. PEF's interim storm recovery surcharge, as originally described in Paragraph 3 of the Stipulation and Settlement Agreement, would operate as follows:

3. The Parties agree that if a future storm claim exhausts the reserve account, PEF shall be able to collect, subject to refund, an interim surcharge for 80% of the claimed deficiency, upon 30 days notice to PEF's customers and on the first billing cycle following the thirtieth day after customer notification is given, while the total claim is being formally evaluated by the Commission in a full hearing, if any such hearing is requested.

Like the prospective rate increases cited above, PEF's proposed surcharge would go into effect upon a specified event (future storm claim exhausts PEF's reserve account) at a specified time (first billing cycle following the 30th day after customer notification) and with specified conditions (reserve account exhausted, notification to customers, surcharge subject to refund, full hearing if requested).

To address any further concerns that the Commission Staff may have regarding the implementation of any initial automatic surcharge² and to underscore the surcharge's identity as a prospective rate increase, we would further commit that any initial automatic surcharge would be limited to 5% on a typical residential bill of 1,000 kwh and that the recovery period would not exceed 24 months. The impact to non-residential customers will be a default of having met the residential limitation. If any initial surcharge is not sufficient due to the size of the needed recovery, PEF would still be limited to a 5% increase over the period not to exceed 24 months until the Commission has issued a final order on a permanent surcharge and its order is implemented. Further, the provisions in paragraph 3 of the Stipulation will apply until PEF's next filed rate case. With these additional parameters as to the maximum initial automatic recovery amount and duration, the proposed settlement is clearly in line with the case law cited above regarding prospective rate increases, in which the parameters of the rate increase are known and approved. Accordingly, the Commission does have the authority to approve this prospective storm recovery rate increase.

B. The "File and Suspend" Process Would Permit Commission Suspension of the Proposed Surcharge

Additionally, the interim storm recovery surcharge is not an abdication of ratemaking authority as it would still be subject to the "file and suspend" process.

Section 366.06(4), Florida Statutes is the "file and suspend" provision of Chapter 366. *Citizens of the State of Fla. v. Mayo*, 333 So. 2d 1, 2 (Fla. 1976). The provision was "expressly designed to reduce so-called 'regulatory lag'" and "to provide a series of alternatives for the Commission" in approving a rate increase. *Id.* at 4. Under this statute, if the Commission does not act within the statutorily specified timeframe, then the proposed rates become effective without further Commission action. *See id.* ("If the Commission does not affirmatively act . . . to suspend the proposed new rate schedule filed . . . the new rates go into effect automatically . . ."). Such automatic increases, without additional Commission action, are appropriate and were intended by the Legislature. *See id.* at 5 ("The Legislature did not intend a full rate hearing before all new rate schedules become effective. Had it intended that result, there would have been no need to enact subsection 366.06(4) at all."). *See also Citizens of the State of Fla. v. Wilson*, 567 So. 2d 889, 891 (Fla. 1990) ("when a utility files a tariff changing its rates, the Commission may allow the tariff to go into effect on an interim basis without the necessity of a hearing.").

The application of the "file and suspend" law is not limited to full base rate proceedings. In Docket No. 041291-EI, the Office of the Public Counsel and FIPUG argued that the "file and

² The Commission expressed concern that the surcharge proposed by Gulf Power Company ("Gulf") was of an "unspecified amount," that it gave the Commission no opportunity to "set limits on the amount, duration or nature of the charges" and, as originally proposed, would "operate in perpetuity." *In re: Petition for issuance of storm recovery financing order pursuant to Section 366.8260, F.S. (2005), by Gulf*, Docket No. 060154-EI, Order No. PSC-06-0601-S-EI (July 10, 2006). The commitments and clarifications by PEF eliminate these concerns.

Jennifer Brubaker, Esq.
July 19, 2006
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suspend" process only applied to full base rate proceedings and, thus, could not be used by FPL for its storm recovery surcharge. Order No. PSC-05-0187-PCI-EI. The Commission disagreed, finding that the "file and suspend" procedure is "not limited to full base rate proceedings," that the "plain language of Section 366.06 has always specified that it applies to "all applications for changes in rates," and that "for years" the "file and suspend" provision has been the "procedural basis for handling proposed tariffs outside of full base rate proceedings." *Id.*

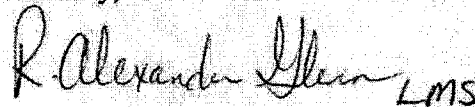
Thus, a tariff filing which would be subject to the "file and suspend" procedure is an appropriate process for the implementation of the interim surcharge provided for in the Stipulation. The Commission can suspend the interim charge pending formal evaluation by the Commission in a full hearing if it is concerned about PEF's surcharge.

III. Conclusion

The Commission should approve the Stipulation in keeping with its long-standing policy to encourage settlements. The Commission has the authority to approve the Stipulation, including the interim storm surcharge. The surcharge is, in effect, nothing more than a prospective rate increase, which the Commission clearly has authority to approve and which it does regularly approve. Finally, the Stipulation itself and the "file and suspend" process provide appropriate safeguards regarding the Commission's ability to suspend the charge or order refunds of the charge.

Please do not hesitate to contact me if you have any questions regarding this information.

Sincerely,

Handwritten signature of R. Alexander Glenn in cursive, with the initials "LMS" written at the end.

R. Alexander Glenn

cc: Division of Commission Clerk and Administrative Services
Office of Public Counsel (McLean)
Florida Retail Federation (Wright)
Florida Industrial Power Users Group (McWhirter)
AARP, Buddy L. Hansen, and Sugarmill Woods Civil Association, Inc. (Twomey)