

State of Florida



Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

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COMMISSION
CLERK

DATE: August 2, 2012

TO: Office of Commission Clerk (Cole)

FROM: Division of Accounting and Finance (Cicchetti, Maurey, Springer)
Office of the General Counsel (Murphy, Tan, Barrera)

Handwritten initials: MC, ALM, mas, MB, JSC

RE: Docket No. 120001-EI – Fuel and purchased power cost recovery clause with generating performance incentive factor.

Docket No. 120002-EG – Energy conservation cost recovery clause.

Docket No. 120007-EI – Environmental cost recovery clause.

AGENDA: 08/14/12 – Regular Agenda – Proposed Agency Action – Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Balbis

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\AFD\WP\120001.RCM.DOC

Case Background

The cost recovery dockets, Energy Conservation Cost Recovery (ECCR), Fuel and Purchased Power Cost Recovery Clause (Fuel Clause), and the Environmental Cost Recovery Clause (ECRC) are continuing dockets that handle issues pertaining to Florida's Investor-Owned electric Utilities (IOU). These IOUs are Florida Power & Light Company, Progress Energy Florida, Inc., Gulf Power Company, Florida Public Utility Company and Tampa Electric Company. Intervenors for all three cost recovery clauses include the Office of Public Counsel,

Federal Executive Agencies, Florida Industrial Power Users Group, Florida Retail Federation, and White Springs Agricultural Chemicals, Inc. In addition, the Southern Alliance for Clean Energy (SACE) and Florida Solar Energy Industry Association (FLASEIA) intervened in the ECCR clause.

The Commission, when appropriate, allows recovery of a return on capital investments through the fuel clause, the ECCR and the ECRC. Traditionally, the Commission has relied on the jurisdictional capital structure and cost rates for each component of the capital structure approved in each utility's most recent base rate case to determine the appropriate weighted average cost of capital.

In certain instances, significant differences developed between investor-owned electric utilities' weighted average cost of capital authorized in the last base rate case and their current weighted average cost of capital. After a series of noticed meetings, which included parties and intervenors, a methodology addressing the weighted average cost of capital that more closely aligns current costs with current cost recovery was developed. On July 17, 2012, the parties filed a Settlement and Stipulation Agreement (Attachment A) in Docket Nos. 120001-EI, 120002-EG, and 120007-EI¹. A timeline example of the methodology is provided on the last page of Attachment A. This recommendation addresses the Settlement and Stipulation Agreement.

The Commission has jurisdiction pursuant to Chapter 120 and several provisions of Chapter 366, including Sections 366.04 - 366.06 and 366.80 - 366.85, Florida Statutes (F.S.).

¹ The signatories are the five electric IOUs, the Office of Public Counsel, Federal Executive Agencies, Florida Industrial Power Users Group, and White Springs Agricultural Chemicals, Inc.

Discussion of Issues

Issue 1: Should the Commission approve the attached Stipulation and Settlement Agreement of the parties, addressing the methodology for calculating the allowable return on clause-approved investments, that was filed on July 17, 2012, in Docket Nos. 120001-EI, 120002-EG, and 120007-EI?

Recommendation: Yes. The Commission should approve the Stipulation and Settlement Agreement of the parties, addressing the methodology for calculating the allowable return on clause-approved investments. (Cicchetti)

Staff Analysis:

The Commission, when appropriate, allows recovery of a return on capital investments through the Fuel and Purchased Power Cost Recovery Clause, the Conservation Cost Recovery Clause, and the Environmental Cost Recovery Clause. Traditionally, the Commission has relied on the jurisdictional capital structure and cost rates for each component of the capital structure approved in each IOU's most recent base rate case to determine the appropriate weighted average cost of capital. In certain instances, significant differences developed between the IOUs' weighted average cost of capital authorized in the last base rate case and their current weighted average cost of capital. For example, in a recent cost recovery clause docket, the difference between the current cost of capital as reported in the Earnings Surveillance Report and the cost of capital from the last rate case was over 100 basis points. A methodology that more closely aligns current costs with current cost recovery was developed and is set out in the attached stipulation. The new methodology would be applied to clause cycling expenses beginning January 1, 2013. A timeline example of the methodology is provided with Attachment A.

In addition to the methodology, the Stipulation and Settlement Agreement contained the following elements of note:

- Progress Energy will be allowed to exclude its Clean Air Interstate Rule investments from the application of the new method in 2013 and will be allowed to continue use of the current method on those investments in setting clause rates for 2013.
- No Party will challenge the justness or reasonableness of the new methodology or the appropriateness of the weighted average cost of capital reflected in the May Earnings Surveillance Reports used thereunder in any Clause proceedings. The Settlement Agreement allows that any Party may challenge a mathematical error that it contends has been made in calculating the weighted average cost of capital in an Earnings Surveillance Report.
- The provisions of the Settlement Agreement are contingent on approval of the Settlement Agreement in its entirety by the Commission. The Parties agree to support the Settlement Agreement and will not request or support any order, relief, outcome or result in conflict

with the terms of the Settlement Agreement in any administrative or judicial proceeding relating to, reviewing or challenging the establishment, approval, adoption or implementation of the Settlement Agreement.

- If the Commission rejects or modifies this Agreement in whole or in part, the Parties agree the Settlement Agreement is void unless ratified by the Parties, and that each Party may pursue its interests as those interests exist, and no Party will be bound by or make reference to Agreement before the Commission, any court, any other administrative forum or arbitration panel.
- The Parties respectfully request that the Commission take the following actions:
 - Restate and affirm the Commission's conclusion in Order No. PSC-94-0044-FOF-EI that "potentially controversial and time consuming evidentiary debates regarding the appropriate capital structure and return on equity should be the subject of proceedings [other than the clause proceedings]"².
 - Confirm the appropriateness of the weighted average cost of capital calculation methodology set forth in this Agreement for application to the calculation of projected Clause factors, actual/estimated true-ups of Clause factors and final true-ups of Clause factors in all subsequent dockets unless and until modified by the Commission.

Staff agrees with the Parties that potentially controversial and time consuming evidentiary debates regarding the appropriate capital structure and the return on equity should be the subject of other proceedings other than the clause proceedings. Unless and until modified by the Commission, staff believes that the weighted average cost of capital calculation methodology as established in the Settlement Agreement is appropriate in all subsequent clause dockets. Further, staff believes the Stipulation and Settlement Agreement filed by the parties is in the public interest because the methodology more accurately aligns current costs with cost recovery and sends a more precise price signal. Therefore, staff recommends that the Commission approve the Stipulation and Settlement Agreement of the parties, addressing the methodology for calculating the allowable return on clause-approved investments.

² Order No. PSC-94-0044-FOF-EI, issued January 12, 1994, Docket No. 930613-EI, In re: Petition to establish an environmental cost recovery clause pursuant to Section 366.0825, Florida Statutes, by Gulf Power Company.

Docket Nos. 120001-EI, 120002-EG, 120007-EI
Date: August 2, 2012

Issue 2: Should these dockets be closed?

Recommendation: No. If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, a consummating order should be issued. These dockets should remain open to address the evidentiary issues presented in each. (Tan)

Staff Analysis: If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, a consummating order should be issued. These dockets should remain open to address the issues presented in each.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Fuel and Purchased Power Cost Recovery Clause with Generating Performance Incentive Factor.))) _____)	DOCKET NO. 120001-EI
In re: Energy Conservation Cost Recovery Clause.)) _____)	DOCKET NO. 120002-EG
In re: Environmental Cost Recovery Clause.)) _____)	DOCKET NO. 120007-EI
)	FILED: July 17, 2012

STIPULATION AND SETTLEMENT AGREEMENT

This Stipulation and Settlement Agreement ("Agreement") is entered into by and between Progress Energy Florida, Inc. ("PEF"), Tampa Electric Company ("TECO"), Gulf Power Company ("Gulf"), Florida Power & Light Company ("FPL"), Florida Public Utilities Company ("FPUC"), Florida Industrial Power Users Group ("FIPUG") and Office of Public Counsel ("OPC"), collectively the "Parties" this 17th day of July, 2012.

WITNESETH:

WHEREAS, investor-owned electric utilities ("IOUs") regulated by the Florida Public Service Commission (the "Commission") from time to time are authorized by the Commission to recover a return on capital investments through the fuel and purchased power cost recovery clause, the conservation cost recovery clause and the environmental cost recovery clause (the "Clauses") in dockets established annually for the purpose of administering and approving matters related to the Clauses; and

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FPSC-COMMISSION CLERK

WHEREAS, the Commission traditionally has authorized for such purpose a return based on the jurisdictional capital structures and cost rates for each component of the capital structure approved in each IOU's most recent base rate case order; and

WHEREAS, the Commission Staff has expressed concern that as time passes subsequent to an IOU's most recent base rate order the IOU's actual jurisdictional capital structure and cost rates for components in that capital structure become different from those that were approved in the IOU's most recent base rate proceeding; and

WHEREAS, the Parties have differing views on whether any modification of the traditional methodology for calculating the return on Clause-approved investments is needed; and

WHEREAS, notwithstanding these differences in views, in order to resolve their differences and achieve a mutually acceptable settlement, the Parties stipulate and agree to utilize a new methodology for calculating the allowable return on Clause approved investments, subject to the Commission's approval of that methodology; and

WHEREAS, the Parties recognize and acknowledge that section 120.80(13)(a) of the Florida Statutes exempts Commission statements that relate to cost-recovery clauses, factors, or mechanisms implemented pursuant to Chapter 366 of the Florida Statutes, relating to the IOUs, from the rulemaking provisions of section 120.54(1)(a) of the Florida Statutes.

NOW, THEREFORE, in consideration of the foregoing and the covenants contained herein, the undersigned parties hereby stipulate and agree as follows:

1. Upon final Commission approval of this Agreement, the IOUs will utilize the following methodology for calculating the allowable return on Clause-approved investments:

(a) The calculation of the allowable return on Clause-approved investments for the 2012 Actual/Estimated and Final True-up will remain under the current methodology (*i.e.*, the rate of return is based on the jurisdictional capital structures and cost rates for each component of the capital structure that were approved in an IOU's most recent order authorizing base rates issued prior to the effective date of this Agreement).

(b) Beginning with the 2013 cycle of Clause-recoverable expenses, all IOUs will use the following methodology:

(i) For the Projection Filing, use the May Earnings Surveillance Report ("ESR") Weighted Average Cost of Capital ("WACC") for the calendar year in which the filing is made (e.g., for the 2013 Projection which is made in August/September of 2012, the May 2012 ESR would be used; for the 2014 Projection which is made in August/September of 2013, the May 2013 ESR would be used, and so on).

(ii) For the Actual/Estimated True-up Filing, use the May ESR WACC from the prior calendar year for January – June of the year being trued-up, and the current calendar year May ESR WACC for July – December of the year being trued-up (e.g., for the 2013 Actual/Estimated True-up Filing which is made in August/September 2013, the May 2012 ESR would be used for January – June and the May 2013 ESR would be used for July – December; for the 2014 Actual/Estimated filing which is made in August/September 2014, the May 2013 ESR would be used for January – June and the May 2014 ESR would be used for July – December; and so on). The monthly accounting on the books and records of the utility would be performed consistent with this methodology.

(iii) For the Final True-up Filing regarding a particular calendar year use the same WACCs that were used for the Actual/Estimated True-up Filing regarding that same particular calendar year.

(c) The term WACC as used above is meant to reflect the capital structure ratios and associated cost rates when calculating the revenue requirement rate of return. The proportions of the various components of the capital structure (including common equity) and cost rate information for all components of the capital structure other than ROE contained on Schedule 4 (Midpoint Average Rate of Return – FPSC Adjusted Basis) of the relevant ESR as described above shall be utilized to arrive at the relevant WACC.¹ The equity components shall also be grossed up for the statutory income tax rate. The cost rates for the components of the capital structure other than common equity shall be the actual cost rates shown in the ESR. The cost rate for common equity will be the last authorized rate of return on equity (“ROE”). In the past there have been instances where the Commission authorized a specific ROE for projects being recovered through a clause. To the extent the Commission issues an order authorizing an ROE different from the midpoint on Schedule 4 of the relevant ESR for a particular clause or project within a clause, that ROE will be used to calculate the relevant WACC.

(d) Exceptions to Section (1)(b) above,

(i) In the event that a base rate decision² is rendered by the Commission subsequent to the period captured by the relevant May ESR to be used in Section

¹ In calculating the WACC for a Clause-approved investment, the proportion of ITC in the capital structure shall reflect the amount of ITC approved by the Commission for financing that investment. (Reference Commission Order PSC-10-0153-FOF-EI, page 106).

² The parties agree that the term “base rate decision” encompasses any decision by the Commission that determines or approves by settlement or through a litigated case the ROE and/or capital structure that will be used for setting and evaluating an IOU’s base rates.

(1)(b), then the Commission's decision on the cost of capital and capital structure as reflected in the order implementing the base rate decision (the "Order") will supersede the actuals used in the May ESR from the effective date of the Order, until the next actual May ESR after the effective date of the Order.

(ii) PEF will be allowed to exclude its CAIR investments from the application of the new method in 2013 and will be allowed to continue use of the current method on those investments in setting clause rates for 2013. This is consistent with the intent of the Settlement and Stipulation which transfers those investments to base rates effective with the first billing cycle for 2014.

The new methodology set forth above is illustrated on Attachment A hereto.

2. The Parties recognize that an IOU's current actual overall cost of capital at any given point in time may be higher or lower than the overall rate of return approved by the Commission in the IOU's most recent base rate proceeding. It is the intent of the Parties that the new methodology prescribed herein for more closely tracking and utilizing the IOU's current actual overall cost of capital in calculating the allowed return on Clause-approved investments is appropriate for use without regard to whether the resulting return is higher or lower than that approved in the IOU's most recent base rate proceeding. Accordingly, no Party will challenge the justness or reasonableness of the new methodology or the appropriateness of the WACC reflected in the May ESRs used thereunder in any Clause proceedings; provided, however, that any Party may challenge a mathematical error that it contends has been made in calculating the WACC in an ESR. It is contemplated that a party who believes that the WACC presentation in the ESR is inconsistent with the most recent base rate proceeding may provide the basis for this

belief to Commission Staff for evaluation in the Staff's role in monitoring the IOU's ESR compliance.

3. The provisions of this Agreement are contingent on approval of this Agreement in its entirety by the Commission. The Parties further agree that they will support this Agreement and will not request or support any order, relief, outcome or result in conflict with the terms of this Agreement in any administrative or judicial proceeding relating to, reviewing or challenging the establishment, approval, adoption or implementation of this Agreement or the subject matter hereof.

4. The Parties shall support the approval of this Agreement by the Commission at the earliest possible time in order to facilitate the implementation of the new methodology for calculating the allowable return on Clause investments, starting with projections of Clause factors for 2013 that are scheduled to be filed in the above-referenced dockets in August and September 2012. To accomplish this end while also clearly stating the Commission's continuing support for using the new methodology in subsequent Clause dockets unless and until modified by the Commission, the Parties respectfully request that the Commission take the following steps:

(a) enter an order in each of the above-referenced dockets attaching and approving this Agreement for application to the 2013 projected Clause factors that will be filed by the IOUs in August and September 2012; and

(b) attach and approve this Agreement in the final order issued in each of the above-referenced dockets, with such final order (i) restating and affirming the Commission's conclusion in Order No. PSC-94-0044-FOF-EI that "potentially controversial and time consuming evidentiary debates regarding the appropriate capital structure and ROE should be the subject of

proceedings [other than the clause proceedings]" and (ii) confirming the appropriateness of the WACC calculation methodology set forth in this Agreement for application to the calculation of projected Clause factors, actual/estimated true-ups of Clause factors and final true-ups of Clause factors in all subsequent Clause dockets unless and until modified by the Commission.

5. This agreement shall survive the closure of Docket Nos. 120001-EI, 120002-EG and 120007-EI, shall apply in future annual dockets established for the Clauses and shall remain in effect until the Commission modifies or rescinds the order approving this Agreement, whether on its own motion or as a result of a motion or petition by a party to this stipulation or another substantially affected person.

6. In the event the Commission rejects or modifies this Agreement in whole or in part, the Parties agree this Agreement is void unless ratified by the Parties, and that each Party may pursue its interests as those interests exist, and no Party will be bound by or make reference to this Agreement before this Commission, any court, any other administrative forum or arbitration panel.

7. This Agreement dated as of July 17, 2012 may be executed in counterpart originals, and a facsimile of the original signature shall be deemed an original.

IN WITNESS WHEREOF, the Parties evidence their acceptance and agreement with the provisions of this Agreement by their signatures below.

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**Florida Power Corporation dba
Progress Energy Florida, Inc.**

By 

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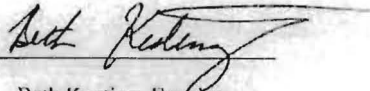
Florida Power & Light Company

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By *Vicki Gordon Kaufman*

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By



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Table 1:

Type of Filing	Clause Cycle Expense	Date of Filing	WACC Method
Final True-up	Jan-11 through Dec-11	Apr/May - 12	LAST AUTHORIZED
Act/Est True-up	Jan-12 through Dec-12	Aug/Sept - 12	LAST AUTHORIZED
Projection	Jan-13 through Dec-13	Aug/Sept - 12	May - 12 ESR
Final True-up	Jan-12 through Dec-12	Apr/May - 13	LAST AUTHORIZED
Act/Est True-up	Jan-13 through Dec-13	Aug/Sept - 13	May-12 ESR (Jan - Jun) / May - 13 ESR (Jul - Dec)
Projection	Jan-14 through Dec-14	Aug/Sept - 13	May - 13 ESR
Final True-up	Jan-13 through Dec-13	Apr/May - 14	May-12 ESR (Jan - Jun) / May - 13 ESR (Jul - Dec)
Act/Est True-up	Jan-14 through Dec-14	Aug/Sept - 14	May-13 ESR (Jan - Jun) / May - 14 ESR (Jul - Dec)
Projection	Jan-15 through Dec-15	Aug/Sept - 14	May - 14 ESR

Table 2:

		Jan-13	Feb-13	Mar-13	Apr-13	May-13	Jun-13	Jul-13	Aug-13	Sep-13	Oct-13	Nov-13	Dec-13	
IN YEAR W/O RATE CASE DECISION	Projection	ESR	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	
	Act/Est	ESR	May-12	May-12	May-12	May-12	May-12	May-12	May-13	May-13	May-13	May-13	May-13	
	Final	ESR	RESULTS SAME AS ACT/EST											
		Rate Case Effective												
IN YEAR OF RATE CASE DECISION	Projection	ESR	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	May-12	
	Act/Est	ESR	RATE CASE ORDER FOR WACC						May-13	May-13	May-13	May-13	May-13	May-13
	Final	ESR	RESULTS SAME AS ACT/EST											

Note 1: assumes for illustrative purposes a January 1, 2013 effective date for the rate case order.