Eric Fryson

From: Keating, Beth [BKeating@gunster.com]
Sent: Wednesday, August 08, 2012 1:17 PM
To: Filings@psc.state.fl.us
Cc: 'Napier, Michelle'; Pauline Robinson; Devlin Higgins
Subject: Docket No. 120004-GU
Attachments: 20120808131030164.pdf

Attached for electronic filing, please find Florida Public Utilities Company's Response to Audit No. 12-010-4-7 in the referenced docket.

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b. Docket No. 120004-GU - In re: Natural Gas Conservation Cost Recovery.

c. On behalf of: Florida Public Utilities Company

d. There are a total of pages: 7

e. Description: Audit Response

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August 8, 2012

Electronic Filing

Ms. Ann Cole
Commission Clerk
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Re: Docket No. 120004-GU – Natural Gas Conservation Cost Recovery Clause

Dear Ms. Cole:

Attached for filing, please find the Florida Public Utilities Company's response to Commission Staff Audit Control No. 12-010-4-7 filed in this Docket on July 24, 2012.

Thank you for your assistance with this filing. As always, please don't hesitate to let me know if you have any questions whatsoever.

Sincerely,

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MEK

2011 Florida Public Utilities Company Natural Gas Response to Audit Findings

Audit Control No. 12-010-4-7

Finding 1: Increased Conservation Payroll and Associated Costs:

The Company believes that this Audit Finding confirms what the Company projected in its September 2011 filing - that the Company believed that the current economic conditions had changed the traditional paradigm of new construction dictating the conservation efforts of the Company. The Company has responded, through specific and deliberate efforts, to realign and reorganize itself to the current market conditions. The Company took many specific actions subsequent to the merger between Florida Public Utilities Company and Chesapeake Utilities, as detailed below, so that current customers could receive assistance that would help them reduce costs and conserve energy during the worst economic conditions since the Great Depression. Reviewing the September 2011 filing reveals that, if Labor/Payroll and Travel are combined, the Company projected a total of $932,791 for 2011, but actually incurred $980,179, a 5.1% increase over projection. However, the projected rebates expected to be paid were $538,291 but were actually $882,330, which is a 63.9% increase. Also, when compared to 2007 data, the attached spreadsheet shows that while payroll, adjusted for allocations to Chesapeake Division (see Finding 1, subpart 5), increased by about 55%, the number of rebates for the Appliance Replacement and Appliance Retention programs (the new focus of the Company) increased by approximately 38% and 55%, respectively. Therefore, the increase in payroll has resulted in substantially more customers taking advantage of these conservation programs. Thus, the Company believes that its efforts to focus on those programs that assist existing customers and are designed to add new customers to existing infrastructure have been even more successful than what the Company anticipated.

1. The Company has experienced increased payroll and associated conservation costs in 2011. There are many reasons for the increases, but primarily they are the result of internal changes to job functions and Marketing Department structure. As more fully described herein, the Company has reassessed its conservation efforts and focus to better align itself with current economic and market conditions. This realignment has impacted not only the level of charges to the conservation program, but also the positions that actually perform conservation related activities. This is shown in the Audit Report under Finding 1, subpart 1, where employees in certain departments (i.e. Fleet, Information Management and Propane) were identified that perform certain conservation functions. All Company conservation employees have vehicles, and the Fleet Manager is responsible for coordinating maintenance activities; therefore, a small portion of these individuals' payroll has been allocated to conservation. These same conservation employees also have computers; therefore, some Information Management time is

allocated. And finally, as indicated in the Audit Report, an employee in the Propane Division is utilized to process invoices for contractor work that is outsourced. The Company believes that it is appropriate to identify all conservation related activities and ensure that they are properly recorded in the approved conservation programs.

2. Mr. Kevin Webber is the Vice President of Gas Operations and Business Development (Marketing Department 400), which is a new position for Florida Public Utilities. Although part of his responsibilities include Gas Operations, he is also directly responsible for business development for all of the Company's Utilities (electric, natural gas and propane). Before the new Marketing Director was hired in 2011, Mr. Webber was directly responsible for the Company's marketing strategy, which included conservation activities. Mr. Webber remains significantly involved with the development of the marketing and conservation efforts, and the new Marketing Director reports directly to Mr. Webber. See Organizational Chart attached. Therefore, the Company believes that it is appropriate for payroll and the associated employee expenses of this position be charged to natural gas conservation expense.

3. The conservation-related positions in Marketing Department 413 were realigned and reorganized for 2011. Payroll allocations were updated to be in line with the new job responsibilities which were determined to be 42% conservation-related. The Company retained an outside consultant to validate the 2011 allocation percentages and job functions of all conservation-related positions.

4. Subsequent to the consummation of the merger, a comprehensive review of the marketing department and market assessment was performed to determine if current economic conditions warranted changes within the Company. The review determined that the organizational structure and the functionality of marketing positions were not in alignment with current consumer needs. The Company made significant changes to the marketing department, including the elimination of geographic organizational structure and implementation of functional organization, consolidation of marketing and conservation functions, centralization of administrative functions, elimination of several positions and changes in marketing strategy. The number of personnel in the marketing department since the time of the merger has decreased, and remains at decreased levels today.

   As for the market itself, new residential housing construction continues to be at levels well below previous years' levels, foreclosures have been at record high levels, and existing and potential customers want help in finding ways to save money on their utility bills. The Company's market assessment revealed, among other things, that the Company should shift its focus to the conservation programs that are designed to assist existing customers and potential customers (premises) that are adjacent to natural gas infrastructure (all electric homes that have a natural gas main close by), rather than the traditional new residential construction markets. These conservation programs, however, are more labor and resource intensive than the new residential construction program. Where the new residential construction program is relationship oriented (one builder/developer, many rebates), these conservation programs are transactional (one customer, one rebate). As such, and as stated above, the Company projected the effects of these changes in its September 2011 energy conservation projection filing. Actual 2011 results confirm that the Company has increased its payroll and associated (travel) costs and advertisement costs to its conservation programs. At the same time, however, the number of individual customers assisted, as demonstrated by the number of rebates paid under these programs (Residential Appliance Replacement, Residential Appliance Retention and Conservation Education Programs) has also increased. Thus, additional expenditures have resulted in more participation by customers of these important energy conservation programs.

The Company continues to monitor the economic conditions and its conservation program efforts to ensure that its job functions, work focus and payroll allocations accurately reflect market needs for conservation services. In fact, the Company retained an outside consultant to validate the 2011 allocation percentages and job functions of all conservation-related positions. As significant changes are made in the future to job responsibilities and amount of time spent on conservation activities, allocations will be updated appropriately.

Audit Finding 1, subpart 4, provides a chart comparing 2007 data from the Company's last rate case, the historic year data, with FERC Form 2 data from 2010 and 2011. The report concludes that "the Utility operating and maintenance expenses included in base rates have also increased." The Company disagrees with this conclusion for several reasons.

First, base rates are set on Projected Test Year data, not historic year data. Second, consistent with the Commission's decision, in Docket No. 110133-GU, the Company has not yet been allowed to consolidate the regulatory filings and records of Florida Public Utilities Company and Florida Division of Chesapeake Utilities Corporation. As such, comparisons of pre-merger accounting data with current accounting data present a difficult, "apples to oranges" task. The difficulty is exacerbated, in part, by the following: (1) FPUC now uses Chesapeake's financial system instead of the FPUC financial system used prior to the merger; and (2) employees now charge all of their time to FPUC and allocations are made to Chesapeake.

Finally, the Company fully recognizes that it has the burden to demonstrate, in its next base rate proceeding, that the merger-related savings, approved by the Commission in the above-referenced Docket, continue to be realized. The Company does not, however, believe that this particular audit finding falls within the scope of this Docket, nor is it within the stated scope of the Audit itself. (*See* Purpose and Objective and Procedures of Audit Report). Again, as explained above, the Company believes that the data used in the chart is not comparable and cannot be used to make any determination of O&M payroll changes. The 2010 and 2011 payroll data contains many items that are not recurring and several adjustments would need to be made in order to ensure comparability with appropriate comparison data. Thus, the Company believes that the Audit Finding 1, subpart 4, in not appropriately addressed in this proceeding.

5. The Company's payroll allocations are reviewed each year. The Company inadvertently did not allocate payroll of approximately $165,432 to the Florida Division of Chesapeake Utilities Corporation which would reduce the amounts charged to Florida Public Utilities Electric and Natural Gas divisions by $44,936, and $120,496 respectively. The Company has since corrected this allocation.

   The Company did not allocate to Indiantown because the percentage was immaterial (less than ½ of a percent).

Finding 2: Developer Agreements

The Company recognizes that the Developer Agreements identified by the audit contained inaccurate rebate information. The Company will review its Developer Agreement documents and utilize appropriate language, such as that suggested in this Finding, in future Agreements. As stated to the auditor, the Company only pays the currently approved rebate levels for each qualifying appliance to developers/builders, regardless of the information contained in such Agreements.

Finding 3: Non-recoverable Costs Allocated:

The Company will make the adjustment for these non-recoverable costs in 2012, reducing natural gas conservation expense and under-recovery account for $7,971.93.

Year	Program	Labor/Payroll	Travel	Advertising	Rebates	Number Of Rebates	Percentage Change				Number	Change from 2007	
							Labor/Payroll	Travel	Advertising	Rebates	Of Rebates		
2007	New Construction				$197,445	710							
	Appliance Replacement				$179,206	352							
	Appliance Retention				$328,250	735							
	Other				$617								
		$473,194	$8,068	$970,780	$705,518								
2008	New Construction				$322,090	1038				63.1%	46.2%		
	Appliance Replacement				$127,650	267				-28.8%	-24.1%		
	Appliance Retention				$327,050	960				-0.4%	30.6%		
	Other				$525					-14.9%			
		$488,948	$4,040	$542,225	$777,315		3.3%	-49.9%	-44.1%	10.2%			
2009	New Construction				$133,050	498				-58.7%	-52.0%		
	Appliance Replacement				$113,730	892				-10.9%	234.1%		
	Appliance Retention				$325,075	735				-0.6%	-23.4%		
	Other				$350					-33.3%			
		$537,466	$1,666	$429,522	$572,205		9.9%	-58.8%	-20.8%	-26.4%			
2010	New Construction				$299,932	506				125.4%	1.6%		
	Appliance Replacement				$123,125	203				8.3%	-77.2%		
	Appliance Retention				$274,351	853				-15.6%	16.1%		
	Other				$31,907					9016.3%			
		$471,414	$25,491	$693,604	$729,315		-12.3%	1430.1%	61.5%	27.5%			
2011	New Construction				$174,188	545				-41.9%	7.7%	-11.8%	-23.2%
	Appliance Replacement				$235,975	485				91.7%	138.9%	31.7%	37.8%
	Appliance Retention				$452,460	1143				64.9%	34.0%	37.8%	55.5%
	Other				$19,707					-38.2%			
		$853,163	$127,016	$1,151,853	$882,330		81.0%	398.3%	66.1%	21.0%			
	Change from 2007	80.3%	1474.3%	18.7%	25.1%								
												Change from 2007	
2011 Adjusted	New Construction				$174,188	545				-41.9%	7.7%	-11.8%	-23.2%
	Appliance Replacement				$235,975	485				91.7%	138.9%	31.7%	37.8%
	Appliance Retention				$452,460	1143				64.9%	34.0%	37.8%	55.5%
	Other	($120,496)			$19,707					-38.2%			
		$732,667	$127,016	$1,151,853	$882,330		55.4%	398.3%	66.1%	21.0%			
	Change from 2007	54.8%	1474.3%	18.7%	25.1%								

Florida Public Utilities Company

GAS OPERATIONS & BUSINESS DEVELOPMENT

Kevin Webber
VP Gas Operations and Business Development

- **Mark Cutshaw** — *Electric General Manager, NE*
- **Buddy Shelley** — *Electric General Manager, NW*
- **Barry Kennedy** — *Director, Gas Operations*
- **Bob Hill** — *Director, Propane Operations*
- **Aleida Socarras** — *Director, Marketing & Sales*
- **John McClelland** — *Business Development Mgr*
- **Bonnie Erdek** — *Contracts & Community Administrator*

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