BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into 1999 earnings of Florida Public Utilities Company - Marianna Division.	DOCKET NO. 001146-EI ORDER NO. PSC-00-1685-PAA-EI ISSUED: September 20, 2000

The following Commissioners participated in the disposition of this matter:

J. TERRY DEASON, Chairman
E. LEON JACOBS, JR.
LILA A. JABER

NOTICE OF PROPOSED AGENCY ACTION
ORDER DETERMINING AND DISPOSING OF
EXCESS EARNINGS FOR 1999

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service Commission that the action discussed herein is preliminary in nature and will become final unless a person whose interests are substantially affected files a petition for a formal proceeding, pursuant to Rule 25-22.029, Florida Administrative Code.

Pursuant to this Commission's continuing earnings surveillance program, we noted that the earnings of the Florida Public Utilities Company - Marianna Division (FPUC-M or the Company) on the December 31, 1999 Earnings Surveillance Report were within three basis points of the maximum authorized return on equity (ROE) of 11.85%. As a result, an earnings audit of the Company's books and records was performed, and the audit report was issued June 15, 2000. The Company's response to the audit was received on July 6, 2000.

On July 19, 2000, FPUC-M submitted a letter to the Commission in which it agreed to cap the earnings of the Marianna Division at 11.85% for calender year 1999. The disposition of any excess earnings was left to the discretion of the Commission. The Company, however, did reserve the right to request alternative dispositions such as additional contributions to its storm damage reserve or the reduction of any depreciation reserve deficiencies. On July 20, 2000, the Company submitted a letter requesting that the 1999 overearnings be applied to the Marianna Division's Storm Damage Reserve.

FPUC-M serves approximately 11,900 customers in portions of Jackson, Calhoun and Liberty Counties. This includes about 9,600 residential and 2,100 commercial customers.

Jurisdiction over the subject matter of this docket is vested in the Commission pursuant to Sections 366.04, 366.05, and 366.06, Florida Statutes.

Rate Base

In its December 1999 Earnings Surveillance Report (ESR), the Company reported a total "FPSC Adjusted" rate base of $12,537,252. Based on the adjustment discussed below, however, we find that the appropriate rate base is $12,551,895. These adjustments and calculations are shown in Attachment A to this Order, which is incorporated herein by reference.

In computing the allowance for working capital, the Company used the 1998 base revenue allocation factor of 20.9% instead of the 1999 factor of 19.1%. This factor is used to allocate accounts payable that are not directly associated with a specific division. As a result of the percentage allocation change, an adjustment of $14,643 should be made to decrease the Marianna Division's portion and thereby increase its working capital.

Rate of Return

After making the following adjustments, we find that the appropriate overall rate of return for FPUC-M for measuring 1999 excess earnings is 8.51%. These adjustments and calculations are shown on Attachment B to this Order, which is incorporated herein by reference.

In making these adjustments, we begin with the 13-month average capital structure from the Company's ESR for the period ending December 31, 1999. In its ESR, the Company removed its investment in Flo-Gas entirely from common equity in a manner consistent with previous cases. The Company specifically identified deferred taxes, investment tax credits and customer deposits.

The Company calculated an effective customer deposit cost rate of 6.30% by using interest expenses for 1999, which included estimated interest expenses for the months of May and October, and a 13-month average balance of customer deposits. Using actual interest expenses for the year and the 13-month average balance of customer deposits, we calculate an effective cost rate of 5.92% for customer deposits. We find that using actual interest expenses in determining the cost rate is appropriate.

We find that a specific adjustment should be made in the amount of $4,244. This amount represents the 13-month average balance of excess earnings for 1999. This amount was included as a separate line item in the capital structure and was assigned an effective cost rate of 5.06%. The cost rate on excess earnings is based on a 12-month average of the 30-day commercial paper rate. The 30-day commercial paper rate is applied as per Rule 25-6.109, Florida Administrative Code. In order to maintain uniformity between divisions, the treatment of excess earnings as an item in the capital structure is consistent with the treatment of excess earnings in the 1998 earnings review of the Fernandina Beach Division (see Order No. PSC-99-2119-PAA-EI, issued October 25, 1999).

We find that the remaining adjustments to rate base should be reconciled on a pro rata basis over investor-supplied sources of capital. The Commission established the return on common equity for FPUC-M as 10.85% with a range from 9.85% to 11.85% (Order No. PSC-94-0170-FOF-EI, issued February 10, 1994). Using the top of the range of 11.85%, we find that the Company's weighted average cost of capital is 8.51%. This is the rate of return to be used to measure excess earnings.

<u>Net Operating Income</u>

In its December 1999 ESR, the Company reported an "FPSC Adjusted" net operating income (NOI) of $1,067,060. Based on the following adjustments, we find that the appropriate NOI for determining the amount of excess earnings for 1999 is $1,073,368. These adjustments and calculations are shown in Attachment A to this Order.

First, we find that an adjustment should be made for refunds the Company made to various companies for overbilling for the period February 1994 through June 1999. Although total refunds were $8,513, the amount of $7,919 was for periods other than calendar year 1999. We find revenues should be increased $7,919 to reflect the correct revenues applicable to 1999.

Second, a review of the January 1999 general ledger showed that the Company recorded expenses of $1,433 and $1,682 in January 1999 which were applicable to December 1998. These two expenses total $3,115, and should be removed from the 1999 income statement.

Finally, we find that an adjustment is necessary to account for the tax effects of the adjustments to rate base and NOI that we found appropriate above. The tax effect of the income statement adjustments is $4,152. The interest reconciliation and ITC interest synchronization are a fallout based on the reconciliation of the rate base and the capital structure due to our adjustments to the rate base. In this instance, income taxes should be increased by $574.

Excess Earnings

Based on our findings above, we find that FPUC-M's 1999 excess earnings are $8,340, plus interest of $221. This represents an earned ROE of 11.99%, which exceeds the maximum authorized ROE of 11.85%. Our calculation of the excess earnings, including interest, is shown in Attachment C to this Order, which is incorporated herein by reference.

Disposition of Excess Earnings

In its July 20, 2000, letter, the Company requested that the 1999 overearnings be applied to the Marianna Division's Storm Damage Reserve. The total Storm Damage Reserve for Marianna amounted to $588,661 as of June 2000. The approved level of the reserve was addressed in Order No. PSC-94-0170-FOF-EI, resulting from Marianna's last rate case. In that Order, we established a targeted storm damage reserve of $1 million, with an annual accrual of $100,000. We agree with the Company that the total reserve is inadequate and will continue to be so for the next several years. Therefore, we find that the $8,561 of excess earnings be included in the Storm Damage Reserve.

Since the excess earnings occurred during 1999 and interest has only been calculated for that year, we find that the increase in the reserve be made effective January 1, 2000, for all regulatory purposes. This would eliminate the need for the calculation of any additional amounts of interest and would include the increased reserve in the determination of earnings for the year 2000.

Increase in Storm Damage Reserve Ceiling

In Order No. PSC-94-0170-FOF-EI, we increased the Marianna Division's Storm Damage Reserve accrual from $17,300 to $100,000 annually. Additionally, a ceiling of $1,000,000 for the Reserve was established. As of June 30, 2000, the Accumulated Storm Damage Reserve for FPUC-M was $588,661. The Storm Damage Reserve is used primarily to replace distribution plant which has been damaged or destroyed by accidents or natural disasters and which is not covered by insurance. Between year-end 1992, which was the last full year before the present cap was set, and year-end 1999, the Company's gross distribution plant has increased 37.4% and net distribution plant has increased 21.6%.

Our previous order required the Company to submit, with its Annual Report, the status and reasonableness of the reserve, the annual accrual amount, and the availability of distribution system insurance. Hurricane Andrew, which struck south Florida in 1992, did not cause any damage to the FPUC-M facilities but made the purchase of insurance, if available, extremely expensive for the coverage provided. The Company has concluded that insurance is still virtually unobtainable, and the establishment of a reserve balance sufficient to cover at least a large portion of storm damages is necessary.

We find that the Company's distribution plant balance has increased enough since 1992 to warrant an increase in its Accumulated Storm Damage Reserve. Therefore, we find that the Company's Storm Damage Reserve be increased from $1,000,000 to $1,400,000.

Increase in Annual Accrual for Storm Damage Reserve

As noted, the Marianna Division's Storm Damage Reserve account has a relatively low balance of $588,661 as of June 30, 2000, compared to the recommended target balance of $1,400,000. At the current accrual amount of $100,000 annually, it will take over eight years to reach the target level, assuming no storm damage. The present amount of the storm damage reserve would be sufficient to replace only approximately 2 1/2% of gross distribution plant in the event of a major storm.

We find that the Company should be given the flexibility to increase its annual accrual to the accumulated provision account, when the Company believes it is in a position from an earnings standpoint to do so, up to the ceiling of $1,400,000. This is similar to the flexibility that the Commission granted Gulf Power Company in Order No. PSC-96-0023-FOF-EI, issued January 19, 1996. FPUC-M is still required to record an annual accrual to the Storm Damage Reserve of at least $100,000 until the Reserve reaches $1,400,000. Also, the Company shall provide a statement on its future earnings surveillance report when the adjustment is made to increase the amount charged to expense.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that the Florida Public Utilities Company - Marianna Division achieved excess earnings for 1999 which, together with applicable interest, total $8,561, as discussed in the body of this Order. It is further

ORDERED that the Florida Public Utilities Company - Marianna Division shall apply its total 1999 excess earnings of $8,561 to its Storm Damage Reserve, effective January 1, 2000, for ratemaking, earnings surveillance, and earnings review purposes. It is further

ORDERED that the Storm Damage Reserve ceiling for Florida Public Utilities Company - Marianna Division be raised to $1,400,000. It is further

ORDERED that Florida Public Utilities - Marianna Division may increase its annual accrual in the Storm Damage Reserve above the present $100,000 yearly accrual until the accumulated provision account balance reaches $1,400,000. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective upon the issuance of a Consummating Order unless an appropriate petition, in the form provided by Rule 28-106.201, Florida Administrative Code, is received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings" attached hereto. It is further

ORDERED that in the event this Order becomes final, this Docket shall be closed.

By ORDER of the Florida Public Service Commission this 20th day of September, 2000.

BLANCA S. BAYÓ, Director
Division of Records and Reporting

By: Kay Flynn
Kay Flynn, Chief
Bureau of Records

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing that is available under Section 120.57, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, in the form provided by Rule 28-106.201, Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on October 11, 2000.

In the absence of such a petition, this order shall become final and effective upon the issuance of a Consummating Order.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

FLORIDA PUBLIC UTILITIES COMPANY
MARIANNA ELECTRIC DIVISION
DOCKET NO. 001146-EI
REVIEW OF 1999 EARNINGS

	As Filed FPSC Adjusted Basis	Accounts Payable Allocation	Revenue Adjustment	Out of Period Adjustments	Interest Reconciliation/ ITC Synchronization	Total Adjustments	Total Adjusted Rate Base
RATE BASE							
Plant in Service	$22,678,529					$0	$22,678,529
Accumulated Depreciation	9,332,439					0	9,332,439
Net Plant in Service	13,346,090					0	13,346,090
Property Held for Future Use	0					0	0
Construction Work in Progress	100,777					0	100,777
Net Utility Plant	13,446,867					0	13,446,867
Working Capital	(909,615)	14,643				14,643	(894,972)
Total Rate Base	$12,537,252	$14,643				$14,643	$12,551,895
INCOME STATEMENT							
Operating Revenues	$5,827,140		$7,919			$7,919	$5,835,059
Operating Expenses:						0	0
Operation & Maintenance - Fuel	0					0	0
Operation & Maintenance - Other	2,266,241			(3,115)		(3,115)	2,263,126
Depreciation & Amortization	863,094					0	863,094
Taxes Other Than Income	1,338,797					0	1,338,797
Income Taxes - Current	234,084		2,980	1,172	574	4,726	238,810
Deferred Income Taxes (Net)	81,861					0	81,861
Investment Tax Credit (Net)	(23,997)					0	(23,997)
(Gain)/Loss on Disposition	0					0	0
Total Operating Expenses	4,760,080		2,980			1,611	4,761,691
Net Operating Income	$1,067,060		$4,939	($1,943)		$6,308	$1,073,368
EQUITY RATIO	45.07%					0.00%	45.07%
OVERALL RATE OF RETURN	8.51%					0.04%	8.55%
RETURN ON EQUITY	11.83%					0.16%	11.99%

MARIANNA ELECTRIC DIVISION
DOCKET NO. 001146-EI
REVIEW OF 1999 EARNINGS

CAPITAL STRUCTURE AS FILED - FPSC ADJUSTED	Amount	Ratio	Cost Rate	Weighted Cost
Long Term Debt	$3,927,051	31.32%	9.93%	3.11%
Short Term Debt	1,474,022	11.76%	5.56%	0.65%
Preferred Stock	103,212	0.82%	4.75%	0.04%
Customer Deposits	627,815	5.01%	6.30%	0.32%
Common Equity	4,516,259	36.02%	11.85%	4.27%
Deferred Income Taxes	1,716,739	13.69%	0.00%	0.00%
Tax Credits - Zero Cost	364	0.00%	0.00%	0.00%
Tax Credits - Weighted Cost	171,790	1.37%	10.10%	0.14%
Total	$12,537,252	100.00%		8.53%

ADJUSTED	Amount	Adjustments Specific	Adjustments Pro Rata	Adjusted Total	Ratio	Cost Rate	Weighted Cost
Long Term Debt	$3,927,051		$4,075	$3,931,126	31.32%	9.93%	3.11%
Short Term Debt	1,474,022		$1,530	1,475,552	11.76%	5.56%	0.65%
Preferred Stock	103,212		$107	103,319	0.82%	4.75%	0.04%
Customers Deposits	627,815			627,815	5.00%	5.92%	0.30%
1999 Excess Earnings		4,244		4,244	0.03%	5.06%	0.00%
Common Equity	4,516,259		$4,687	4,520,946	36.02%	11.85%	4.27%
Deferred Income Taxes	1,716,739			1,716,739	13.68%	0.00%	0.00%
Tax Credits - Zero Cost	364			364	0.00%	0.00%	0.00%
Tax Credits - Weighted Cost	171,790			171,790	1.37%	10.10%	0.14%
Total	$12,537,252	$4,244	$10,399	$12,551,895	100.00%		8.51%

ATTACHMENT C

FLORIDA PUBLIC UTILITIES COMPANY
MARIANNA ELECTRIC DIVISION
DOCKET NO. 001146-EI
REVIEW OF 1999 EARNINGS

Adjusted Rate Base	$12,551,895
ROR @ 11.85% ROE	X 8.51%
Maximum allowed Net Operating Income	1,068,166
Achieved Net Operating Income	1,073,368
Excess Net Operating Income	5,202
Revenue Expansion Factor	X 1.6033
Excess Revenues	8,340
Interest	221
TOTAL 1999 EXCESS REVENUE	$8,561