BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

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In Re: Petition of GULF POWER COMPANY for an increase in its rates and charges	))))	Docket No. 891345-EI Filed: July 9, 1990

CITIZENS' BRIEF

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APP ____
CAF ____
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LEG 1
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OPC ____
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SEC 1
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Respectfully submitted,

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MISCELLANEOUS

REVENUE REQUIREMENTS

COST OF SERVICE ISSUES

Rate Base

ISSUE 1: Gulf Power has proposed a rate base of $923,562,000 ($1,192,516,000 System) for the test year. What is the appropriate level of rate base for 1990?

OPC Position: The proper level of rate base will be provided later with the filing of the rate base schedules.

ISSUE 2: The company has included $1,275,624,000 ($1,307,579,000 System) of plant in service in rate base. Is this appropriate?

OPC Position: No. Based on an actual vs. projected analysis for August, 1989 through March, 1990, the total company plant is overstated by $11,458,000 ($11,178,000 jurisdictional). Plant Scherer should be removed from plant-in-service as not currently needed for retail generation. Net plant-in-service is $1,209,506 ($1,239,805 System).

DISCUSSION: Using the actual plant in service data for August 1989 through February 1990 as compared to the Company's projections, Mr. Larkin determined that the projections are overstated by $11,753,000 [T. 2199]. In further support of this position, Mr. Larkin testified that the Company had over-projected its 13 month average ended December 1989 by over $26.9 million [T. 2200]. To determine the proper adjustment to be made to the Company's projection, Mr. Larkin used a linear regression analysis [T. 2200- 2260].

In response to this adjustment, Mr. McMillan testified that there were other reasons for the previous over projection [T. 3903-3904]. There were three major reductions to plant in service in recent years that taken together would explain the underage. The first reduction was for $9 million to remove the acquisition adjustment for Plant Scherer from plant in service to the acquisition adjustment account in June of 1988 [T. 3903]. While at first this argument seems to have merit, it should be noted that this could not have affected the 1989 13-month average, as the only month in 1988 that was used was December. A major plant reduction in the previous June would not affect the $28.9 million difference for 1989.

The other two items were reductions in 1988 and 1989 for the retirement of the Plant Daniel coal cars ($9.5 million) and the $5.3 million to reduce the Plant Scherer purchase price. These two items amount to $14.8 million which when compared to the $28.9 million overage for 1989 still leaves a $14.1 million over-projection. And this assumes both of these items were removed at the beginning of 1989 which is unlikely.

In furtherance of explaining away the historical over-projection of plant in service, the Company claims that, as of May, the plant in service balance is close to what they had projected [T. 3924]. The Company, after having been significantly behind in its construction program, has evidently accelerated its projects to "catch up " to their projections. This is a good example of cart-before-the-horse mentality.

The fact is, on a 13-month average basis, the plant in service is still significantly below Company projections. Once the Commission makes a determination in this case, based on the historical over-projection results, it is very likely that the construction will fall behind the projections once again. Without any other means to determine what the over projection amount will be by December, the Commission should use Mr. Larkin's calculation and remove $11,753,000.

ISSUE 3: Gulf capitalized $1,964,394 ($6,937,131 System) in excess of the original cost capitalized by Georgia Power Company for its 25% share of Plant Scherer, Unit No. 3. Is this appropriate?

OPC Position: No. In the event the Commission decides to allow Plant Scherer in rate base, no acquisition adjustment should be included in rate base.

DISCUSSION: See Issue 4 discussion.

ISSUE 4: As a result of its purchase of a portion of the common facilities at Plant Scherer, Gulf recorded an acquisition adjustment of $2,458,067 ($8,680,507 System). Is this appropriate?

OPC Position: No. In the event the Commission decides to allow Plant Scherer in rate base, no acquisition adjustment should be included in rate base.

DISCUSSION:

> To pass along these acquisition costs which discharge the obligation of Southern Company related to Oglethorpe Power Corporation and the City of Dalton would be unfair and unequitable to the Gulf Power ratepayers. . . .
>
> [T. 2217-2218]

This quote from Mr. Larkin sums up the reality that would result from this Commission allowing these acquisition adjustments. This Commission has always held that no acquisition adjustments should be included for recovery by Florida ratepayers. To allow this recovery in this case would be to set a precedent in future cases and open the floodgates to acquisition adjustments of all kinds. This should not be done.

Mr. Scarbrough asks this Commission to consider the "value received" when making this decision [T. 3779]. This is the same argument that can be made for any acquisition adjustment and completely misses the point. Very often the fair market value of an asset is greater than the book value of that asset. However, the Commission certainly would not allow utility company's to start reselling their plant assets between themselves at "fair value" and thus create acquisition adjustments on all over-depreciated plant. The Commission policy against allowing acquisition adjustments is designed to prevent exactly the kind of items cited by Gulf as the cause of the adjustment.

Mr. Scarbrough explained that the adjustment was composed of three parts: $4,865,444 for carrying costs; $3,796,376 for accumulated depreciation; and $18,687 for legal costs [T. 337-338, 3780-3781]. Unfortunately for the Company, the only item which should be considered as recoverable is the legal costs. Mr. Scarbrough stated he believed that it is only fair for its ratepayers to pay the carrying costs of these assets during the time the assets were 100% owned by other utilities. At first glance, his reasoning sounds correct in that he claims Oglethorpe (OPC) and the City of Dalton (Dalton) should be able to recover their carrying costs from someone [T. 338]. But consider the other side of this sales transaction.

Each year, OPC and Dalton would pay their debt, and possibly an equity type of return, which would be booked as a cost to the Company in those years. Further, whether booked or not, an allowance for depreciation should have been recognized. It is totally proper to assume that these costs were in fact passed on to their customers. To this question Mr. Scarbrough stated ". . .I do not know how Oglethorpe and Dalton treated this." [T. 390]. He goes on to explain that if we assume that these costs were recovered from their customers, those customers ought to get those dollars back "So they break even. And now we have it on our books." [T. 390]. The fact is, Mr. Scarbrough has no idea what is on the books of OPC or Dalton. When asked by Commissioner Gunter to give a chronological calculation of the costs involved, Mr. Scarbrough responded that they would have to go to OPC and Dalton to get some of that information [T. 393-394].

Part of Mr. Scarbrough's reasoning in allowing for the accumulated depreciation portion of the acquisition adjustment is that Dalton did not depreciate its share and OPC started its depreciation two years late [T. 389, 399-400]. Thus, in effect, the total undepreciated balance is properly included. This argument is without merit. Physical wear and tear on plant assets does not abate when a Company chooses not to recognize that fact on its books and records. The fact is, several years have passed since the common facilities went into operation and they are now not worth as much as they would be if they were brand new facilities.

Another aspect to this issue makes the Company's claimed purchase price suspect. Exhibit No. 553 contains, in part, a copy of the December 8, 1989 "AUDIT OF THE OGLETHORPE POWER CORPORATION SALES PRICE ADJUSTMENT FOR PLANT SCHERER COMMON FACILITIES." On page 19 of this exhibit its states: "Gulf has also requested information from OPC to recompute the revised gain for Gulf's final booking of the Electric Plant Acquisition Adjustment." (Emphasis added). This document which was not provided by Gulf in its original filing, raises some question as to the acquisition amount. Also this document seems to contradict the Company's claim that there was no profit to anyone in this deal [T. 338].

One final point should be considered on this issue. The Federal Energy Regulatory Commission (FERC) has disallowed this item and has decided that the acquisition adjustment is properly recorded below the line [T 405-496]. In Mr. Scarbrough's words, FERC wanted: "First of all, show us that all customers receive benefit of it . . ." The Company has failed to make that showing in its direct case nor its rebuttal of Mr. Larkin. At this point Mr. Scarbrough says: "FERC is waiting for this Commission to make its decision before they make their decision on this issue." [T. 407]. The proper decision that should be made by both this Commission and FERC is to disallow the acquisition adjustments.

ISSUE 5: Is the $31,645,000 total cost for the new corporate headquarters land, building, and furnishings reasonable?

OPC Position: The costs of the new corporate headquarters should be adjusted to remove any excessive costs and costs associated with non used and useful land and building space as determined by this Commission. Numerous inquiries and exhibits were requested concerning this issue (e.g., T. 1603-1612, 1638-1655, 3634-3637, 3640-3642, 3683-3751, 3752-3758, 3835). Once all exhibits are received, the Commission should remove any excess rate base and expense items that are found.

ISSUE 6: Is the Careyville "sod farm" operation being properly accounted for by Gulf Power Company?

OPC Position: In the event the sod farm operations are determined to be subsidized by the ratepayers, the Commission should remove these costs as non utility in nature.

ISSUE 7: Should the investment and expenses associated with the "Navy House" be allowed?

OPC Position: Based on the record, the use of this house as a training center duplicates space already available at the corporate headquarters and the Pace Boulevard location [T. 3652-3681]. All of the expenses and rate base items should be removed for rate setting purposes.

ISSUE 8: **Has Gulf properly allocated all of the appropriate capital investment and expenses to its appliance division?**

OPC Position: **The appliance division is being subsidized by the utility operations. The costs identified in late filed exhibit 564 should be removed.**

DISCUSSION: Mr. Scarbrough testified that the appliance division is not charged postage costs for bill stuffers and credit purchase billings [T. 578-580]. The division is further subsidized in that electrical usage is billed to this division at below the tariff rates. By not billing at tariff rates, Gulf has created a subsidation because the general body of ratepayers support the rate base associated with the electricity supplied [T. 586-590]. Even with these "freebies" the division still does not operate profitably [T. 611, 908]

The primary function of electric utility operations should be to provide electric service. Should the Company choose to operate other ventures, those operations should share in the costs of mailing and should be charged at the tariff rate for electric service. By not sharing in these expenses the division gains an unfair advantage in the marketplace.

ISSUE 9: Should Gulf's investment in the Tallahassee office be included in rate base?

OPC Position: Plant in service should be reduced by $43,000 and accumulated depreciation by $26,000.

ISSUE 10: Should the total cost of the Bonifay and Graceville offices be allowed in rate base?

OPC Position: No. In Gulf's previous rate case, the Commission made the determination that total recovery for these offices should not be permitted. In the current case, the Company has merely remade the same arguments on this issue. The Company has not submitted any verifiable support for these costs. Rate base should be reduced by $183,000.

ISSUE 11: Gulf Power has proposed $454,964,000 ($1,451,703,000 System) as the proper level of accumulated depreciation to be used in this case. Is this appropriate?

OPC Position: The proper balance will be supplied with the rate base schedules.

ISSUE 12: Should the plant investment made by Gulf to serve the Leisure Lakes subdivision be included in rate base?

OPC Position: No. The Commission determined in Gulf's last case that the distribution line and substation should not be included in rate base, as the local cooperative should service this subdivision [T. 2207]. In the current case, Mr. Jordan tried again to justify the substation by giving it a new name and claiming it was designed to serve primarily as back up for the Sunny Hills substation [T. 1571-1572]. The Company has failed to justify the reintroduction of this substation into rate base, and it should be removed.

ISSUE 15: Gulf has included in its jurisdictional rate base $3,925,000 ($4,025,000 System) of plant held for future use. Is this appropriate?

OPC Position: Due to the current plans for use, the following items should not be included in rate base. Careyville because:

1. there are currently no specific plans for this site;

2. the certification is due to run out in 1991; and

3. no study has been performed nor cost benefit shown that it is indeed better to hold and continue to purchase land at this site rather than purchase land later when specific plans for generation capacity are known.

Remove $1,398,000 from rate base. Bayfront office at $1,844,000; Pace Boulevard land at $612,000.

DISCUSSION: The Careyville site was purchased in part in 1964 and 1976 [T. 413] and has been in rate base since 1980 [T. 2212]. Mr. Parsons testified in the Company's direct case that the Careyville site is still a viable certified location for future plant needs [T. 1021-1022]. He further stated that it is better to purchase and hold this land now at lower costs [T. 1023-1024]. Future plans are to acquire up to 3,000 acres at this site to accommodate an 800 mw unit sometime in the future [T. 1204-1205].

Mr. Parsons later admitted under cross examination that the certification for this site runs out next year (1991) [T. 1208]. Further, he admitted that "[i]f we substantially change anything. . ." the Company would have to go back through the environmental process [T. 1208]. At that time, anyone can petition for abandonment of the site and the site would need to be recertified [T. 1209-1210].

Basically what this means is that the current certification is valueless since there is very little chance that recertification will be granted with no opposition. Also, while the Company may be right in its belief that currently holding and continued purchasing of land at the site will result in some future cost savings, the facts are:

1. there are currently no specific plans for this site;

2. the certification for this site is due to run out in 1991; and

3. no study has been performed nor cost benefit shown that it is indeed better to hold and continue to purchase land at this site rather than purchase land later when specific plans for generation capacity are known;

4. holding the current land is truly the less expensive only if all the carrying costs (taxes, interest, equity, etc.) added to the original costs are lower than some other alternative purchase;

5. if it is truly less expensive to hold the current land, then the future ratepayers will still receive the benefit of that bargain when all of the costs (original cost, plus all deferred carrying costs) are put into rate base at the time the land is used for service;

6. if, on the other hand, the carrying costs actually make it more expensive to hold the current land, there is absolutely no reason for current customers to pay the carrying costs in order to create an artificial bargain for the benefit of future customers.

The Company should accrue an AFUDC type account to defer the carrying costs if and when the site is actually needed. At that time, a test of reasonableness can be performed to determine how much of the plant and carrying costs should be included for recovery. This will protect the Company's prudent investment in this site while protecting the ratepayers from imprudent costs. Under the current treatment (ie. inclusion in rate base) the current customers are being charged with a cost which may never be beneficial to them, and there will be no mechanism to reimburse customers for the costs they will have borne over the years.

In order to keep overall costs down, any use of land either in current rate base or plant held for future use AFUDC accrual, should be used to generate revenues to offset these costs. This would include revenues from the sod farm operations, timber sales or similar use.

The Bayfront property is projected to be needed sometime between 1994 and the year 2010 [T. 2213]. This is too far into the future to require ratepayers to carry the cost. The Pace property which has been and will continue to be acquired through 1994 [T. 2214] should also not be included for current recovery.

As with the Careyville site, the land at both the Bay Front office and the Pace Boulevard complex should be removed from rate base and allowed to accrue the carrying costs in as AFUDC type account. The total costs then should be compared to market value when the property is used and useful [T. 2214-2215]. Rate base should be reduced by $1,844,000 and $612,000 respectively.

ISSUE 16: Has Gulf allocated the appropriate amount of working capital to Unit Power Sales (UPS)?

OPC Position: No. Increase the UPS working capital by $4,097,000 and decrease the system working capital by the same amount.

DISCUSSION: Mr. Larkin testified that the Commission's ratemaking approach has been to allocate all non - UPS costs to retail ratepayers. If there were no UPS sales, all of the costs of Plant Scherer would be allocated to retail ratepayers. Therefore, when the Company recovers from UPS sales a higher level of working capital than needed, the ratepayers should receive full credit for the actual investment allocated to UPS sales [T. 2227].

The Company argues that this approach picks and chooses different calculations and that the retail ratepayers already receive significant benefits related to UPS sales [T 3917-3918]. The Company believes that even though FERC uses the formula approach in its calculation, this Commission should use the balance sheet approach [T. 761]. As Mr. Larkin pointed out, however, this would allow the Company to overrecover on its UPS sales investment [T. 2227]. Since the retail ratepayers are expected to cover any non UPS costs, any benefit due to overrecovery should be credited to the retail customers.

ISSUE 17: The company has included $81,711,000 ($200,266,000 System) of working capital in rate base. What is the appropriate level of working capital?

OPC Position: The level of working capital is a fallout issue and will be provided later with the filing of the rate base schedules.

ISSUE 18: Gulf has included $1,358,278 ($1,485,221 System) prepaid pension expense in its calculation of working capital. Is this appropriate?

OPC Position: The prepaid pension of $1,484,000 should be removed from working capital.

DISCUSSION: Mr. Larkin's assertion that the ratepayers have been paying for pension expense in their rates since 1984 [T. 2220], is unrebutted. Since this is the case, if anything, there should be a funded reserve to offset ratebase not a prepaid account that increases it. Mr. Scarbrough testified that the Company chose to prepay this amount in 1988 to take advantage of a tax provision to ". . .maximize the tax deduction. . . ." [T. 617-618]. This may be great for the Company, but if included in ratebase, it increases the cost to the ratepayers who funded the pension costs to begin with.

Mr. Scarbrough further testified that this was a prudent move by the Company [T. 3786]. But what he has not disputed is that it results in higher cost to the ratepayers. What is prudent in the Company's eyes may not be prudent for the customers.

ISSUE 19: Should unamortized rate case expense be included in working capital?

OPC Position: No, working capital should be reduced by $765,000 to remove this item.

DISCUSSION: The primary reason to disallow this item is that no rate increase is warranted. However, should the Commission grant an increase it still would be improper to include this for recovery. As Mr. McMillan testified, it has been past Commission practice to disallow this item for recovery in ratebase as a sharing of this cost with stockholders since they are the ones getting the benefit [T. 819].

ISSUE 21: Should temporary cash investments of $6,045,000 ($6,399,000 System) be included in jurisdictional working capital?

OPC Position: No. Should the Commission determine that some of these funds remain in working capital, they should be removed.

ISSUE 22: Gulf has included $1,042,000 (System) for heavy oil inventory. Is this appropriate?

OPC Position: Reduce heavy oil inventory by $925,613 ($1,042,000 System).

DISCUSSION: The Company is maintaining an inventory of 77,538 barrels of heavy oil at the Crist complex [T. 1068]. The primary fuel used for these peaking units is natural gas and the projected capacity factors for these units are: Crist 1 = 4%; Crist 2 = 4%; and Crist 3 = 14%. Mr. Parsons testified that these units are run very little [T. 1069]. The most recent use of this oil at the complex was 995 barrels used during a test run of the unit to determine if the oil could be used [T. 1070-1071]. Prior to that, Mr. Parsons testified it had not been used since 1986 [T. 1071]. During the 1989 Christmas freeze the oil was not used [T. 1071].

What Mr. Parsons has not shown in this case is that the oil backup at these plants is cost efficient in any way. Nor has Mr. Parsons demonstrated historically that this oil has ever been used to the benefit of the ratepayers. Given the large reserve margins on both Gulf's and Southern Company's system, this oil being held as backup for three peakers is overkill as far as system stability.

In order to support the Company's requested level of heavy oil, Mr. Parsons testified that these plants must be prepared to run as part of the interchange agreement. The plants result in $6 million in capacity payments for Gulf on the system [T. 1076, 3455-3456]. While this may very well be true, the Company has failed in both its direct and rebuttal case to provide the essential link between Gulf's obligation to keep these plants in reserve <u>and</u> have an alternative source of fuel.

Given the Company's rationale, all of Southern Company's coal units, gas units and even their nuclear units should have the capability to run alternate fuels. This, of course, is not the case. There has been no showing by the Company that this inventory is necessary, let alone at a level in excess of $1 million.

ISSUE 23: Gulf has included $359,000 (System) of light oil inventory. Is this appropriate?

OPC Position: Reduce light oil inventory by $234,059 ($263,490 System).

DISCUSSION: The Company has projected an inventory average level of 692,121 gallons of light oil [T. 1081]. The primary use of this oil is to help bring coal units up and to stabilize the units [T. 1082]. The level requested was not determined by the inventory model but rather from experience [T. 1086]. The Company has not shown that this is a prudent, cost effective level of light oil inventory. And since Mr. Parsons has testified that the delivery time for this oil would always be within a week and usually within a few days [T. 1086-1087], this inventory should be substantially reduced, consistent with Mr. Larkin's recommendation [T. 2220].

ISSUE 24: Gulf has included $57,426,000 (System) for coal inventory. Is this appropriate?

OPC Position: No reduce coal inventory by $4,468,010 ($5,029,820 System).

DISCUSSION: Prior to 1984, the Company kept its coal inventory at 60 day nameplate. Since then, computer modeling has been implemented to better track fuel inventory [T. 1043-1035]. The current model that Gulf uses for coal inventory is called the Utility Fuel Inventory Model or UFIM and was devised by EPRI [T. 1037]. The Company also includes coal in transit in its inventory.

While computer modeling can be very beneficial for inventory determinations, one must look at the model closely to guarantee that the proper inputs are used as well the assumptions that are inherent in all models. The model used by the Company includes the assumption that a nuclear moratorium could occur that would require all U. S. nuclear plants to be shut down with no warning [T. 1097-1101]. Mr. Parsons agrees that the Commission should review all the assumptions in the model for reasonableness and if determined to be unreasonable, then the proposed coal inventory should be rejected [T. 1107-1108].

The model proposed includes a nuclear disaster which would "significantly" change the world as we know it [T. 1112-1113]. The costs to be incurred under this scenario are totally unrealistic and should be discarded by the Commission because in the hypothetical scenario electricity availability would be the least of this country's problems. This assumption only serves to inflate the costs of not having sufficient coal supplies on hand and discredits the use of the model in determining proper coal levels.

Mr. Parsons best summed the need for proper assumptions in modeling:

> You can run any assumption, I mean, you know, if you can change the assumption, you can run any program and it will give you an answer, but you just have to be comfortable with the inputs into it.

[T. 1279]

The Commission should take note of this advice. The Company's requested level of inventory is inflated and should be reduced to a level commensurate with the level approved for interim purposes.

ISSUE 26: Should 63 MW of Plant Scherer 3 be included in Gulf Power's rate base?

OPC Position: The 63 MW of Plant Scherer should be excluded from Gulf Power Company's retail rate base.

DISCUSSION: Mr. Richard Rosen, testifying for the Citizens of Florida, recommended that the Commission exclude the 63 MW that Gulf is seeking to include in its rate base. At the beginning of his testimony [T. 233-2334], Dr. Rosen outlined the basic rationale for disallowing the 63 MW from rate base. Dr. Rosen outline his reasoning as follows: (1) the Southern Company and Gulf Power's generation expansion strategy in the 1980's resulted in excess baseload capacity on their systems; (2) an appropriate level of required reserve margin for Southern Company and Gulf is about 15%; (3) even from a conservative perspective, the 63 MW of the Scherer 3 plant which Gulf is not going to sell off-system is excess capacity and furthermore, that capacity is not economical for serving Gulf's retail customers; and (4) of the 63 MW. 44 MW is available for a short period only because Gulf States Utilities (GSU) ceased making the capacity payments of that 44 MW. Thus, Dr. Rosen concludes that this capacity be excluded from Gulf's rate base for the test year.

The record includes a great deal of evidence supporting and expanding each of Dr. Rosen's points. In an expansion of the point on capacity mix, enumerated as (1) above, Dr. Rosen first explained:

> Q. [By Mr. Burgess] Were these expansion plans, with their dependence on new baseload plants, consistent with

the Southern Company's own planning studies during the 1980s?

A. [By Dr. Rosen] No, by basing its expansion plan during the entire 1980s primarily on new baseload units, the Southern Company was overlooking some clear signals from its own planning studies that this might not be the most economical strategy. As far back as July 1984, its "1984 System Generation Mix Study" indicated that the next set of new generating units in the 1990s, after completion of the currently planned baseload units, should be new peaking capacity. While this result does not prove conclusively that some or all of the new units planned for completion during the 1980s should have been peakers, it provides strong evidence that they should have been.

[T. 2338-2339]

So in 1984, Southern Company realized that its next set of generating units should be peaking capacity, which perhaps should provide a signal to review the system baseload capacity plans. As Dr. Rosen pointed out, however, Southern Company did not undertake such a review:

[By Dr. Rosen] Unfortunately, the 1984 System Generation Mix Study did not explore the most economical mix of capacity types to build during the remainder of the 1980s. As stated on page 7 of the report, the computer model that the Southern Company used to compute the most economical mix of new capacity as distributed between new peaking and new baseload capacity "was only allowed to add generation to the system after 1990. Budgeted unit additions scheduled prior to the end of 1992 were considered to be installed on schedule." In other words, the study was constrained to leave the 1980s units unchanged and not consider any alternatives in that time frame. Similarly, the Southern Company's 1982 and 1986 generation mix studies focused on new units beginning in 1993 and thereafter.

Q. [By Mr. Burgess] Did the Southern Company review its baseload capacity plans?

A. No, it did not. During the 1980s, the Southern Company's major generation planning studies focused solely on the capacity mix for new units in the 1990s, while ignoring the prudence of the baseload orientation of its scheduled construction program in the 1980s. This program culminated in the projected completed construction of Miller unit 4 by 1991.

This approach to planning appears to have been imprudent in that a proper economic analysis probably would have shown that the new coal baseload units planned for the late 1980s and early 1990s, such as Miller 3 and 4 and Scherer 4, should have been delayed or cancelled altogether. The addition of at least some new peaking capacity is indicated, interspersed between the completion dates of fewer or deferred baseload units.

[T. 2339-2340]

Based on his considerable experience in generation planning [T. 2327, 2328; Exhibit 331], Dr. Rosen believed that a proper economic analysis would have led to a greater reliance on peaking units and a corresponding reduction and/or deferral of baseload capacity.

In fact, when Gulf performed an economic analysis in 1986, it demonstrated a substantial deviation between the actual generation mix and what an optional mix would call for. Dr. Rosen presented the following excerpt from Gulf's 1986 study:

	Percent of Mix	
Capacity Type	Projected 1995	Optimal
Peaking	13	27
Intermediate	4	16
Base Load	83	57
Total	100	100

[T. 2341]

From Gulf's data, Dr. Rosen commented:

> Thus, the actual outcome of the Southern Company planning process resulted in a very significant deviation from the long run optimum. The Southern Company derived almost identical results in its most recent capacity expansion study dated September 1988.
>
> [Id.]

Gulf's data led Dr. Rosen to the inescapable conclusion that Gulf completely miscalculated what its expansion plan during the 1980s should have been.

In an elaboration on the proper required reserve margin, enumerated as (2) above, Dr. Rosen engaged in an informative exchange with Chairman Wilson:

> **Chairman Wilson:** What is your opinion [of an appropriate capacity reserve margin]?
>
> **Witness Rosen:** Well, as the testimony says, I believe that because of the excellent availability of the Southern Company units, which the Company states is 89% availability on average, that probably as low as 15% would be appropriate, because other utility systems that I've examined such as the American Electric Power System, their own internal criteria for adequate capacity on their system is about 17% and they have average availability far lower than the Southern Company. There is, I think about only 77 - 78, so there's over 10 percentage points lower availability on the AP system, and that would translate into at least 2 or 3%. In fact, probably more of a reduction on, you know, an adequate reserve margin.
>
> [T. 2397-2398]
>
> **Chairman Wilson:** In a growth state like Florida, would you consider 15% to be adequate?

Witness Rosen: I would say that for planning purposes, no, that I would go up to about 18 for a system like Gulf.

Now, if there's another -- I mean the Gulf system is not growing all that fast. It's only in the 2 to 3% a year range. Other system may grow faster and you might need to go above 18. But for Gulf, I feel 18 would be an upper limit given the high availability of the Southern Company plants.

[T. 2399]

The Chairman then sought additional information reasoning for Dr. Rosen's conclusion that an adequate reserve level for Gulf is 15%:

Chairman Wilson: What the basis of your opinion that 15% would be adequate? How do you arrive at that?

Witness Rosen: Well, I just gave one example. The AEP system has done a lot of analysis of its units. It defines adequate reserves as up to 90 negative days per year, which means reliance on outside assistance from other system, and it's not -- obviously, its the opposite of extreme from the loss of load probability. And, you know, they meet that at around 17% with a far higher outage rate for their units. So, in fact, probably below 14 would be okay for the Southern Company and Gulf Power has done for the reliability of its own system and there are, in fact, some recent discovery responses on this issue. I believe Staff discovery responses where the

Staff asked the Company to analyze system reliability at different levels of reserves, and a review of all that material convinces me that the Southern Company System would have adequate loss of load by their owner definition or adequate reliability by their own definition, which is EUE. It's basically an energy outage rate. Add 15 [At 15%]. So I've reviewed the Southern Company's studies, I've reviewed reliability studies from many other systems. We've done many of them in our offices. I mean, that's the basis of my conclusion.

[T. 2400-2401]

Quite clearly, a considerable evidentiary basis supports Dr. Rosen's conclusion that an appropriate capacity reserve for Gulf Power Company is 15%.

The third point in Dr. Rosen's analysis, enumerated as (3) above, is that even from a conservative perspective, the 63 MW of Plant Scherer is excess capacity. This point is supported first by simple mathematical computations from the data supplied by Gulf. Using 18% as the conservative end of an appropriate required reserve margin, Dr. Rosen calculated that, in 1990, Gulf has "excess capacity of at least 131 MW." Obviously, the, the 63 MW of Plant Scherer can be considered as excess capacity.

In addition to Dr. Rosen's calculations, Gulf's own action's demonstrate beyond any doubt that the utility itself considers the 63 MW to be excess capacity. First, Gulf is actively seeking to market the 63 MW for off-system sales [T. 1021; 1062]. Secondly, Gulf has sold 44 of the 63 MW to GSU for 1990, until GSU violated the agreement.

The final point of Dr. Rosen, enumerated as (4) above, is that the 44 MW of Scherer is available for retail sales only because a calculated business risk fell through. The 44 MW is available to serve retail load only because GSU chose not to honor its agreement to purchase that capacity from Southern Company [T. 1065-1066].

This circumstances, however, resulted from a business decision into which Gulf entered with its eyes open. As Dr. Rosen explained:

> Equity investors in any utility company take the risk that the utility's business itself might suffer some downturn or reduction in earnings. This is the "business risk" in investing. Because of the possibility of loss, or diminution of value, investors expect and usually receive a rate of return at a premium over that earned by investments that are risk free. In this case, Gulf Power and Southern Company investors were assuming business risks associated with transactions extending beyond their normal retail utility business.
>
> [T. 2356]

It must be understood that Gulf receives compensation for assuming this risk. The Unit Power Sales (UPS), which are under the jurisdiction of FERC [T. 1504). The charges approved by FERC for the UPS include a component for a return on common equity (ROE) of

13.75% [T. 1501]. That ROE is quite generous and is the payment that Gulf's (Southern Company's) shareholders receive in exchange for the risk of participating in the UPS market.

Now, however, Gulf would have its retail ratepayers absorb the risk which Gulf has already been paid to assume. As Dr. Rosen puts it:

> Business risks typically include changes in demand for a product, cost overruns, errors of management, resource shortages and, more to the point here, breach of contract by sellers or purchasers. No investor in the equity securities of an ongoing business should reasonably expect to be insulated from all such risks.
>
> In particular, if Gulf Power's ratepayers were required by the Public Service Commission to absorb such risks -- and thereby insulate the stockholders of the Southern Company from them -- these ratepayers would function, in effect, as insurers. In this case, they would be insuring against a collapse of the Gulf States UPS contract. This is not a proper role for ratepayers to assume, unless the allowed rate of return for Gulf Power <u>excluded</u> a business risk premium which, of course, it does not.
>
> [T. 2347]

The Citizens, therefore, recommend to exclude the costs associated with the 63 MW of Plant Scherer because (1) Gulf's and Southern's generation expansion strategies in the 1980's resulted in substantial excess baseload capacity on their systems; (2) an appropriate level of reserve margin for Gulf is about 15%; (3) even using 18% reserve margin, Gulf shows 131 MW of 1990 excess capacity, so that 63 MW of Scherer can be considered as excess capacity, and furthermore that capacity is not economical for serving Gulf's retail load; and (4) 44 MW of the Scherer capacity is available only because Gulf's business risk, for which it is compensated, has resulted in a loss of unit power sales.

ISSUE 27: If Plant Scherer 3 is not included in rate base, what are the appropriate rate base and NOI adjustments to exclude it?

OPC Position: The proper adjustments to remove Plant Scherer are:

Plant in Service	$52,987,000
Accumulated Depreciation	6,558,000
Acquisition Adjustment	2,317,000
Working Capital	2,187,000
Production A&G/Trans. Rentals	843,000
Depreciation	1,688,000
Amortization/Acquis. Adj. & Other	89,000
Other Taxes	244,000
Amortization of ITC	(96,000)

DISCUSSION: These amounts were provided by the Company in response to Public Counsel Interrogatory No. 144 wherein the Company was asked to provide detailed information on all balance sheet and operating income accounts affected by Gulf's investment in Plant Scherer.

At the hearings, through Mr. McMillan, the Company introduced Exhibit No. 575 which purports to show the net revenue requirements of Plant Scherer [T. 822].

Mr. Larkin testified that he did not agree with what Exhibit 575 purports to demonstrate [T. 2307]. He continued to explain that in part this schedule deducts O&M costs which would not have existed without the 63 MW capacity. Mr. Larkin went on to explain:

> So I've taken up alot of time explaining this, but we would dispute the conclusions reached that that there is a net benefit to the ratepayer of $1.7 million in the transmission and general amounts, and that there's a net

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benefit to the ratepayer of 1,969,000 in variable O&M amounts.

[T. 2315]

This schedule which shows a net negative revenue requirement for Plant Scherer, flies in the face of the evidence in this case. Both Mr. McCrary and Mr. Scarbrough cited Plant Scherer as one of the principal reasons for the rate increase request [T. 38, 53, 298]. For the Company to offer evidence at the trial that Plant Scherer is a net wash is contrary to every public statement issued by Gulf on this subject. The proper adjustments to remove Plant Scherer are those provided to Public Counsel in response to Interrogatory No. 144.

ISSUE 29: What, if any, adjustment to rate base is necessary to reflect the proper treatment for rebuilds and renovations which were expensed by the company?

OPC Position: Increase plant in service by $369,000 and increase depreciation reserve by $18,000 and decrease O&M by $368,500.

DISCUSSION: Mr. Schultz stated that the nature of the rebuilds are such that they extend the useful life of the vehicles and thus are properly capitalized [T. 2477-2478].

Mr. Scarbrough testified that in his opinion expensing the vehicle rebuilds was in conformance with Commission rules [T. 501-502, 3786-3788]. However, in presenting his position he included language from Rule 25-6.0142, F.A.C.:

> When a minor item is replaced independently of the retirement unit of which it is a part, the cost of the replacement shall be charged to the maintenance account appropriated for the item, except that if the replacement affects a substantial betterment (the primary aim of which is to make the property affected more useful, more efficient, of greater durability, or greater capacity) the excess cost of the replacement over the estimated cost at current prices of replacing without betterment shall be charged to the appropriate plant account.
>
> (Emphasis added). [T. 3788].

What should be noted in this passage are the two emphasized phrases.

First of all Mr. Scarbrough is trying to read into the "minor item" limitation something that was not envisioned. That is, in his testimony he states that what is being done is a complete rebuild of these vehicles of every major mechanical part: engine transmission, hydraulic system, brakes; ". . .we rebuild everything except the overall cab, we don't replace the cab." [T.

501, 3856]. It would be stretching it a bit to call some of these items "minor" even on an individual basis, but taken as a whole these rebuilds certainly cannot be considered "minor." By his own words, Mr. Scarbrough describes a process that is substantially changing these vehicles.

The second emphasis shown is the exception to the expensing part of the rule about increasing the efficiency of the vehicle. Mr. Jordan, while trying to justify this new program, testified that the useful life of this equipment is extended and the reliability of the equipment has improved. He states that reliability has increased from 21% in 1987 to 38% in 1988 and 85% in 1989 [T. 1577]. This has resulted in less equipment breakdown and improved crew productivity [T. 1578]. In simple terms, this testimony means that the equipment is more efficient as a result of the rebuilds. Based on the Company's own testimony, this rebuild program is more properly capitalized that expensed.

Also covered in this issue is the proper accounting of the Panama City Office renovation. Mr. Connor testified that this item was expensed to be consistent with past Company practice [T. 3745]. Further, he stated that the total of this project is $622,000 of which only $252,000 was to be expensed [T. 3682].

Since this renovation will extend the useful life of the office, Mr. Schultz testified that this amount of the renovation should be capitalized also [T. 2478]. The Panama City Office renovation has since been postponed until 1991 [T. 3646].

The Company has not given sufficient cause for this portion of the renovation to be expensed. Therefore it should be removed from O&M expenses and capitalized when the project is resumed.

ISSUE 30: What, if any, adjustment to rate base is necessary to remove the network protectors from expense to rate base?

OPC Position: Increase plant in service by $90,000 and depreciation reserve by $5,000 and decrease O&M expenses by $90,000.

DISCUSSION: Mr. Schultz testified that the network protector project was used in part to explain a benchmark variance [T. 2509-2510]. These protectors have been in use for 38 years and the restoration should renew their life for about half this time or about 19 years [T. 2510]. Mr. Scarbrough again relies on his interpretation of Florida Administrative Code to argue that this project should be expensed rather than capitalized [T. 3791]. This explanation fails to refute Mr. Schultz's testimony. Additionally, it should be noted that if it is a recurring item, and therefore an expense item, it cannot also serve as a benchmark justification. That is, if it is recurring in nature then it replaces some other expense in the base year; therefore, it cannot be considered a new expenditure above the benchmark base year.

ISSUE 33: Has the company overstated the materials and supply level?

OPC Position: Yes, reduce M&S by $2,307,000.

DISCUSSION: Mr. Larkin made the determination that this item is overstated based on an actual historic 13 month average balance ended February, 1990 [T. 2220]. This was the most current information at the time. Mr. McMillan rebutted this contention by referring to the single month of February, 1990 [T. 3912]. In further defense of the Company position, Mr. McMillan simply states that prices and investment go up [T. 3912]. Given that the Company has not proffered any evidence to justify this increase in M&S, the Commission should apply Mr. Larkin's adjustment to the test year working capital requirement.

<u>ISSUE 35</u>: Should the Careyville Subsurface Study be removed from rate base?

<u>OPC Position</u>: Yes, remove $692,000 from rate base (also see Issue 15, Careyville site).

<u>DISCUSSION</u>: Mr. Parsons testified that this study is still valid and will be useful in the future [T. 1245, 3445]. The Company does not currently have this site in its Generation Expansion Plan and cannot state when the site will be used [T. 1242]. Part of the site was originally purchased in the mid 1960's with projected need in the late 1970's [T. 1242-1243]. The Study was performed some 15 years ago [T. 1248]. Based on a very conservative return and tax factor of 10% per year, the cumulative compounded cost to the ratepayers for this study is over $2.8 million. This item should be written off below the line so as not to continue to burden the ratepayers for something with no proven benefit.

<u>ISSUE 36</u>: What, if any, additional working capital adjustments are needed to reflect OPC's expense exclusions?

<u>OPC Position</u>: These adjustments fall out of the related O&M issues and will be provided along with the schedules at a later date.

Cost of Capital

ISSUE 37: What is the appropriate cost of common equity capital for Gulf Power?

OPC Position: The proper calculated return on equity should be set at 11.75% (Rothschild), however, this ROE should be adjusted downward for mismanagement.

DISCUSSION: The return on common equity this Commission should allow Gulf Power Company is 11.75%. This return on equity is based primarily upon the application of the DCF method to the electric companies in the Moody's Electric Utility Common Stocks (Moody's 24) which are not in the midst of nuclear construction uncertainties, and to the Southern Company which is the parent of Gulf Power.

The equity cost recommendation has been checked for reasonableness by making a review of the relationship between market-to-book ratios and the earned return on equity and by comparable earnings observations of the actual return on book equity that has been achieved by the Dow Jones 30 industrials. Mr. Rothschild computed the cost of equity by using a properly applied DCF method. By properly applied, he means: " a method that is consistent with the basic assumptions referenced later in my testimony are required to implement the DCF method." [T. 2684]. This essentially means that the estimate of growth is based upon a future sustainable growth rate, not a growth rate that might have by chance happened over any particular historic period.

To properly apply the simplified of D/P + "g" version of the DCF method. Mr. Rothschild testified that it is necessary to make the four following determinations:

1) the dividend yield;

2) the return on equity rate which investors anticipate for the future;

3) the dividend payout ratio (or retention rate) that is consistent with the dividend yield and return on equity expectation;

4) the impact of any sales of new common equity at other than book value.

[T. 2684]

Properly applied, the DCF method is far superior to other equity costing methods. Therefore, it should be given primary weight [T. 2685].

Mr. Rothschild checked the results from his DCF method by observing the relationship between the earned return on equity and the market-to-book ratios, and presented a comparable earnings study. The comparable earnings study is helpful to show that his equity cost recommendation is sufficient to provide a return on equity commensurate with the returns being earned by unregulated firms.

The Discounted Cash Flow, or DCF method, is based upon the principle that there is a time value associated with the money. That is, $1,000 received next year is worth less than $1,000 received today. This is true, if for no other reason, because one person could take the $1,000 received today, put it in a bank account guaranteed by the federal government, then, one year later withdraw those funds plus interest earned from that account.

The concept of time value as explained above is directly applicable to a decision to purchase common stock. The essential difference between an investment in common stock and an investment in the bank account is that, unlike with a bank account, the exact total yield from an investment in common stock is not specified and there is not federal guarantee that either the principal will be returned or that any dividends will ever be paid. While the stock investment is more risky, the basic principal of the time value of money remains the same.

When an investor either buys stock in a company, or deposits money in a bank accounts, he or she gives up cash today in exchange for the right to potential future gains. The investor in the bank accounts gets the specified interest income, whereas the investor in common stock gets any dividends the company may declare plus the right to sell the stock at prevailing market prices. Today's stock price is the present value equivalent of the expected dividends and the proceeds from eventually selling the stock. The interest rates, or, discount rate, that makes the future anticipated dividends and future anticipated selling price equal to the present market price is the cost of equity.

To properly apply the D/P + g formulation of the DCF Method, Mr. Rothschild testified that four determinations need to be made:

1. Dividend yield;

2. The return on equity rate which investors anticipate a company will earn in the future;

3. The dividend payout ratio (or retention rate) that will be maintained in the future;

4. The impact of any sales of new equity at other than book value.

[T. 2696-2697].

Whether using the D/P + g simplified version of the DCF method, or using the full DCF method, it is essential that the above determinations be internally consistent. For example, Mr. Rothschild gave the following.

Market Price = \$14.00/share

Book Value = \$10.00/share

Dividend = \$ 1.00/share

If an analyst concluded that investors anticipated this hypothetical company to be able to earn 12.0% on its equity in the future, the only consistent payout ratio that can be correctly used with the above assumptions is determined as follows:

Anticipated Return on Equity of 12.0% x

Book Value of \$10.00 = \$1.20 earnings per share

$$\text{Ratio} \quad \frac{\text{Dividend of } \$1.00}{\text{Earnings per share of } \$1.20} = 0.833 \text{ payout}$$

The point here is that the dividend yield computation and the growth rates computation are interdependent, not independent determinations. This is because each dollar of earnings available to a company may be either allocated to dividends and sent directly to investors or reinvested in the business to provide a growth in earnings for the future cash flow benefit of investors [T. 2697-2698].

As an example of a comparative earnings observation, Mr. Rothschild offered Exhibit 347. As shown on this Exhibit, pages 1a and 1b of 3, and as graphed on page 2 of 3, the ten year moving average of the actual earned return on equity on average for the 30 companies that make up the Dow Jones Industrial average has been between 10% and 12% since the late 1950s. Even on a single year basis, rather than on a 10 years moving average basis, the range in earned returns during the 1980s has been between the 13.10% high achieved in 1984 and the 7.00% low achieved in 1982 [T. 2715].

The earned return on equity, however, is not the cost of equity. It is the earned return on equity that will be the end result of the rates allowed from these proceedings. Therefore, it is directly comparable to the earned return on equity being achieved by the Dow Jones 30 industrials. The relationship between the market price and the book value of the Dow Jones Industrials shows that investors have been more than satisfied with the returns actually earned [T. 2716].

As shown on Exhibit 347, with a relatively minor exception during the 1978-1981 period, the market-to-book ratio achieved by the Dow Jones Industrials has been at or above book value since 1932, the very depth of the Great Depression. In fact, Mr. Rothschild stated, most of the time the market-to-book ratio has been substantially above 1.0. This shows that most of the time the cost of equity being demanded by investors on average for the Dow Jones Industrials has been less than whatever investors expect the companies will be able to earn on equity in the future [T. 2716].

To compare the risk of the Dow Jones Industrials to the risk of the Moody's 24 electric utilities, Mr. Rothschild stated that a standard of measure of relative risk is the stock's beta. Beta is the number that quantifies the relative volatility of the stock price movements of a particular company with a broad based average such as the New York Stock Exchange Average. As shown on Exhibit 347, page 3, the beta of the Dow Jones Industrials averaged 1.077, as compared to 0.696 for the non-nuclear construction electric and 0.723 for the nuclear construction electrics. In both cases, this indicates that the investment risk is higher, on average, for the Dow Jones Industrials than it is for the average electric utility [T. 2717].

Dr. Morin presented a wide array of DCF analyses, most of which have a theoretical basis that is inconsistent with the requirements of the D/P + g version of the DCF model. Specifically, he used non-constant growth rates as an input to this version of the DCF model which requires that constant growth rates be assumed. The one version of the DCF model he presented which does have some validity, because it at least does depend upon a constant growth rate, was applied in a much more limited way than he applied his other, invalid DCF techniques [T. 2674].

In addition to the problems with his DCF method, he improperly increased his equity cost determination as a result of his view of the impact of the payment of quarterly dividends. In reality, the fact that dividends are paid quarterly instead of annually causes the annual DCF model to overstate, not understate the indicated cost of equity.

In addition to the DCF method, Dr. Morin says that he presented a risk premium analysis. The Risk Premium approach as he presented it is really his DCF method all over again, but with the additional problems that it is dependent upon the incorrect assumption that income tax laws and investors expectations for inflation have remained constant over the years [T.2674].

Dr. Morin filed an update to his cost of capital testimony. Based upon this update, he has increased his recommended cost of equity form 13.0% to 13.5%. A closer analysis of the dynamics behind the updating show that the apparent increase in the cost of equity is caused by flaws in his equity costing techniques rather than any increase in equity cost rates. To further strengthen the illusion that the cost of equity might be higher now than when he originally filed his testimony, he was selective in what he updated.

Dr. Morin decided to increase his equity cost recommendation based upon an update of both the dividend yield and the three different methods he used to estimate the growth rates in his DCF analysis. These methods he updated are the retention growth, analysts consensus growth, and five-year historic growth in dividends.

The DCF method is based upon the principle that the cost of equity is equal to the sum of the dividend yield plus future expected growth. The dividend yield tends to change whenever the stock price changes. However, it is possible that the stock price changed either because the cost of equity changed, or because the future growth as anticipated by investors changed. If there is a change in growth expectations without a change in the cost of equity, the stock price has to change so that the sum of dividend yield plus growth remains the same.

Dr. Morin points out in the updating of his testimony that the dividend yield of the Southern Company increased from 7.99% to 7.55%. However, he also points out in his testimony that Value Line lowered its future expected return on equity from 13.0% to 12.5% since the time of his original testimony. This means that the future cash flow available to maintain a sustainable future growth rate also declined. The retention growth computation that Dr. Morin presents was updated to produce a new growth rate of 3.23%, or 0.37% lower than the original retention growth estimate put forth by Dr. Morin.

The other two methods of estimating growth as put forth by Dr. Morin did not measure a corresponding lowering of the growth rate. But this was merely because of inherent deficiencies in the growth computation methods.

First, looking at the method where Dr. Morin wants to estimate investors future expectations for growth by looking at the five-year historic growth in dividends, the weakness of this method's basic premise is exposed. If an event occurred since November, 1989 which would cause investors to expect a reduction in future cash flows, this would not change the rate at which dividends were paid in the past. Therefore, this method should be expected to be blind to the very changes that need to be evaluated. As it turns out, in the current environment, the method was not quite as blind as Dr. Morin would like it to be.

Both in his original testimony, and his revised update, he kept the historic growth in dividend number for the Southern Company at 5.0%. This cannot possibly be correct. Approximately six months passed since he filed his testimony, and during that time the Southern Company kept its dividend rate constant. This means that an updating of the historic dividend yield computation has to result in a decline in the historic rate. For example, in 1985 the dividends per share for the Southern Company were $1.95 per share and in 1990 are now being paid at the rate of $2.14 per share. They are expected by Value Line to remain at this $2.14 rate at least through the end of 1990.

If the historic growth in dividends were updated to be from 1985 to 1990, then the compound annual growth in dividends drops to 1.9%, or 3.1%, lower than the historic dividend growth number used by Dr. Morin. This five year growth rate drops so sharply because in recent years, the Southern Company has not been increasing its dividend. In fact, the dividend rate has been at the annual level of $2.14 since the fourth quarter of 1986. Therefore, if the historic pattern of dividends is maintained just a short time more, the five year historic growth in dividends number will drop to 0% growth.

Second, Dr. Morin states that analysts' consensus of the earnings per share growth rate for the Southern Company over the next five years went up from 3.03% when he originally filed his testimony to 3.25%. Based upon this, he concluded that his growth rate estimate should be revised upward. A closer look behind the numbers shows that he is improperly using the consensus growth rate number.

Since he originally filed his testimony, the Southern Company reported its 1989 earnings. The 1989 earnings per share were lower than 1988 earning per share. This means that under the assumption that analysts did not change the earnings that were expected in five years, the lower current earnings would have to grow more rapidly to end up on the same place. This kind of catch-up growth is not the kind of growth that is supposed to be included in the D/P + g version of the DCF method. The proper use of analysts estimates of future growth requires that they be mathematically converted to a sustainable growth rate rather than one which is influenced by whether or not the starting year was abnormally good or abnormally bad.

An example of some selective updating done by Dr. Morin can be found on pages 12 to 13 of his testimony as originally filed.

On these pages, he updated his testimony by striking the portion which begins with the word "For . . ." on line 21 of page 12 through line 5 of page 13 [T. 1673]. In this section of his testimony, he discusses what was the total return expected by Value Line. If he had changed his testimony to reflect the total return expected by Value Line in its most recent issue on the Southern Company (dated March 23, 1990), Dr. Morin would have had to note that the total return (dividend yield plus growth) expected by Value Line is 7% to 14%, for a mid-point of 10.5%.

ISSUE 38: Should the newly authorized return on common equity be reduced if it is determined that Gulf has been mismanaged?

OPC Position: Yes. The return on equity should be reduced by 2.00% to reflect mismanagement.

DISCUSSION: Gulf Power Company has been a poorly managed company for several years. The utility would appear to be on the mend, but its management problems have been chronic at the highest levels.

Before examining the specific instances that demonstrate poor management, the Commission must first settle on what constitutes the management of Gulf Power Company. Gulf's approach is to identify management as a moving target, summed up as: "The problems were caused by the Senior Vice President and Board member, not the management." In other words, Gulf simply identifies "management" as that portion of the management team which cannot be directly faulted.

To illustrate that Gulf tries to establish a moving target, suppose Mr. McCrary were the one engaged in the fraudulent activities (understanding that this is offered strictly for illustrative purposes; the Citizens have no reason to believe Mr. McCrary is of anything but the highest moral fiber). Suppose, then that a senior vice president brought those fraudulent activities to light and forced Mr. McCrary out of the company. Would Gulf still be insisting the Mr. McCrary represented management, or would the position then be: "The problems were created by Mr. McCrary, not Gulf's management"? Would Gulf simply move the target?

As another example, suppose that Mr. Horton had never engaged in any improper activity, but rather instituted a number of stellar programs resulting in a Commission decision to reward Gulf for extraordinarily superior management. Would Gulf then say: "Those stellar programs were created by Mr. Horton as an individual, not by Gulf's management"?

The hypotheticals are offered to demonstrate Gulf's definition of management would change as the circumstances change. It is an erroneous conception of management.

The Commission should recognize that Jake Horton was a integral part of Gulf's management team. Mr. Horton's decisions and activities <u>are</u> decisions and activities of Gulf management. As Ms. Bass agreed:

> Q. [By Mr. Burgess] Let me ask specifically, do you consider that Jake Horton was part of the Gulf management team?
>
> A. [By Ms. Bass] Yes, I do.
>
> Q. So that then activities or decisions by Mr. Horton himself reflect part or reflect the Gulf management decisions in some degree or another, is that correct?
>
> A. Yes.
>
> [T. 3050]

Thus, the recognition that Mr. Horton engaged in fraudulent activities is an implicit recognition that Gulf management engaged in fraudulent activities.

Mr. McCrary tried to liken the situation to a bank embezzlement [T. 70]. Mr. McCrary fails to recognize that if a senior vice president and board member of a bank embezzled funds, the consuming public would react to that as though it were a management deficiency at the bank. Business would be damaged accordingly.

In his prefiled testimony, Mr. McCrary summarized the guilty plea entered by Gulf to two federal offenses:

> In order to avoid prolonged, expensive and divisive legal proceedings, the Company pleaded guilty to two federal offenses:
>
> - conspiring to violate a section of the Public Utility Holding Company Act, which prohibits regulated utilities from making political contributions; and
>
> - conspiring to impede the Internal Revenue Service through the creation of false or inflated invoices.
>
> After a thorough review of actions taken by those named in the criminal information filed by the Government, the Company acknowledged with deep regret that federal statutes were violated. As indicated in the Government's Statement of Fact Regarding the Gulf Power Company Plea, the illegal activities were orchestrated by the Company's former Senior Vice President and carried out at his direction by a handful of employees and were unauthorized by Gulf.
>
> [T. 27-28]

The two federal violations orchestrated by Gulf's Senior Vice President and Board member are of themselves proof of mismanagement by Gulf.

In addition, however, there were numerous other improper activities and irregularities that indicated mismanagement at Gulf. As Ms. Bass summarized:

> To facilitate understanding, I will list the allegations and events and then describe them individually. They are as follows:
>
> 1. Inventory shortages of potentially $2,000,000;
> 2. Theft of inventory by Kyle Croft;
> 3. A kick-back to a Gulf employee from a contract vendor;
> 4. Gulf's continued business dealings with vendors once involved in schemes to defraud Gulf;
> 5. Potential conflicts of interest;
> 6. Recommended dismissal of Jacob Horton; and
> 7. Atlanta Federal Grand Jury.
>
> [T. 2980]

Ms. Bass then describes in some detail each of these problems [T. 2980-2993]. The recount of these circumstances lead to the inescapable conclusion that mismanagement abounded at Gulf over a course of several years.

Finally, Ms. Bass expressed extreme concern with the reaction (or lack thereof) by Gulf's top management, stating:

> Although collusion and management override can circumvent and render ineffective even the strictest internal controls, the criminal activity documented as having occurred at Gulf Power extended over a period of approximately eight years. The inability of Gulf management to discover and correct these overt illegal actions leads me to believe that the corporate culture was such that employees believed these types of illegal actions were, at the least, condoned by top management. [T. 2993-2994]

The reaction to these events by Mr. McCrary and by other members of Gulf's top management was explored in considerable depth during the cross-examination of Mr. McCrary.

Those discussions reveal that after numerous instances of criminal activity came to light, Gulf never made any efforts to see that any individuals were prosecuted criminally. Mr. McCrary stated:

> Q. [By Mr. Shreve] Would you please tell me when you went down and gave the information so that the State could prosecute the people that had either defrauded or committed some type of theft from Gulf Power?
>
> A. Well, I didn't do down and give that information to the State. IN 1986, I believe it was early 1986, the IRS and the FBI got extensively involved in the investigations that had been going on at Gulf. When they got involved we pulled out of the investigations, left

that up to them. We cooperated, gave them our records, everything that we had, and continued to give them our records and cooperate with them.

Q. And you initiated that with the IRS?

A. No, we did not.

Q. Did you initiate any criminal action anywhere?

A. No.

Q. Or give any information to anyone?

A. No.

[T. 142-143]

Mr. McCrary's testimony also demonstrates a failure to take definitive internal action in response to the improprieties which had surfaced. After explaining a multitude of specific examples, Mr. McCrary agreed with Mr. Vandiver:

Q. The plea agreement details 120 separate illicit transactions on a more or less continuous basis from 1981 until late 1988. Would you agree with that?

A. Yes.

[T. 247]

That testimony reflects an astounding number of illicit transactions over an amazing continuous period, during which Mr. McCrary, as Mr. Horton's direct supervisor, received numerous signals of trouble. Yet Mr. McCrary did not take definitive action against Mr. Horton. The Citizens reaction is similar to that of Ms. Bass, who stated:

> The information recounted above establishes a patter of continuous and serious mismanagement of this utility for at least a period of eight years. Although Gulf has worked hard in the recent past to eliminate many of the factors which made the above described illegal activities possible, the utility should be held accountable for its previous lack of effective and ethical management. Thus, the Commission should make the factual finding that Gulf Power has been grossly mismanaged and its return on equity should be appropriately adjusted downward to reflect this finding.
>
> [T. 2994]

The Citizens agree that a downward adjustment to return on equity is appropriate. The Citizens recommend that Gulf's authorized ROE be reduced by 200 basis points.

ISSUE 40: Should Gulf Power's non-utility investment be removed directly from equity when reconciling the capital structure to rate base?

OPC Position: Yes. The Company has removed part of this investment from debt (see MFR Sch. D 12a). Reduce equity and increase L-T debt by $7,282,000.

DISCUSSION: This Commission removed non utility assets from the equity account in Gulf's last case [T. 338-339]. Mr. Scarbrough testified that the non-utility property is made up mostly of appliance sales assets and that most of that is made up of accounts receivable for merchandise sales [T. 339]. However, he takes exception to removing it from only equity [T. 339, 615, 3792]. Mr. Scarbrough argues that removing this from equity will penalize the stockholders [T. 3793].

Mr. Scarbrough fails to recognize two points. First, if the non-utility accounts cannot generate enough interest to cover the cost of Gulf's equity, then the charge should to up. Secondly, the appliance receivables are certainly more risky than Gulf's electric sales operations.

Mr. Seery testified that the Company should show a more equitable method if they object to this treatment. [T. 2966a]. Further, he testified that it is not simply a matter of tracing funds but rather:

1. the ratemaking cost of capital should be that cost of capital associated with the provision of electric service only; and

2. because risk can be traced and the provision of electric service is very low risk, investment in non-utility services will increase the risk and cost of capital [T. 2966a-2966b].

While removing all non utility assets out of equity may not be a perfect solution, it is better than Gulf's proposal in identifying and removing non utility assets. Since the stockholders (not the customers) have chosen to get into the appliance business, it is better that the stockholders absorb this additional risk.

ISSUE 41: Should Gulf Power's temporary cash investment be removed directly from equity when reconciling the capital structure to rate base?

OPC Position: Yes, to the extent that temporary cash investments are not necessary for the provision of utility service, Gulf Power's temporary cash investment should be removed directly from equity.

ISSUE 42: What is the appropriate balance of accumulated deferred investment tax credits?

OPC Position: This is a fallout number which will be provided later with the filing of the schedules.

ISSUE 43: What is the appropriate balance of accumulated deferred income taxes?

OPC Position: This is a fallout number which will be provided later with the filing of the schedules.

ISSUE 44: What is the appropriate weighted average cost of capital including the proper components, amounts and cost rates associated with the capital structure for the projected test year ending December 31, 1990?

OPC Position: This information will be filed later with the schedules to be provided for rate of return.

ISSUE 45: Should an adjustment be made to negate the effect of the Company's corporate goal to increase its equity ratio?

OPC Position: Yes. Since equity is the highest cost of capital and is further increased by taxes, any increase in this source of capital should be justified on a cost-benefit basis. Based on the lack of evidence to justify this policy, the Commission should consider reducing the equity percentage to the 1984 level.

Net Operating Income

ISSUE 46: The company has proposed a net operating income of $60,910,000 ($78,848,000 System) for 1990. What is the appropriate net operating income for 1990?

OPC Position: The test year level of operating income is a fall out amount based on revenue and expense issues and will be provided later with the schedules.

ISSUE 47: Should revenues be imputed to Gulf for the benefit derived by the appliance division from the use of Gulf's logo and name?

OPC Position: Yes. Any value attributable to the operation of the electric sales division should be recognized and an appropriate allowance should be credited to the Company above the line. No amount is proposed.

DISCUSSION: Mr. Bowers testified that there was very little name recognition of Gulf Power appliance sales [T. 904]. Yet later he admits that appliance sales advertisements are sent in the electric bills sent out [T. 906]. It is highly unlikely that the appliance division does not benefit from its use of Gulf's name and logo. Since the appliance division is operated to earn a profit for the stockholders [T. 908], it should be allocated a fair share of the costs incurred by Gulf. This would include a nominal charge for the use of Gulf's name and logo.

ISSUE 48: Should revenues be imputed at applicable standby rates for 1990 for the PST customer who experienced an outage of his generation capacity and took back-up power from Gulf but was not billed on the standby power rate?

OPC Position: Yes, revenues should be imputed for the standby service capacity of 7959 KW.

ISSUE 49: The company has projected total operating revenues for 1990 of $225,580,000 ($262,013,000 System). Is this appropriate?

OPC Position: The Company's sales projections should be increased by $2,493,000 to reflect a more accurate sales projection.

DISCUSSION: Mr. Kilgore testified that the Company's short term forecasts have always been very accurate [T. 1731-1732]. The word "accurate" needs to be defined, in this case, in relative terms.

Dr. Rosen cautions the Commission to use the appropriate focus in assessing the accuracy of the Company's forecast method [T. 2367]. He states in part:

> Any forecast of sales or number of customers involves a small change in a large number. . . . Compared to the large number for the base year with which one begins, the difference in forecast growth and actual growth will always be fairly small, independent of the quality of the forecast.
>
> (Emphasis added). [T. 2367]

The Company bases its whole defense of the forecasted level of revenues on providing glowing examples of how accurate their forecasts have been. Yet when examined in light of the true deviation as it relates to the growth amounts instead of total revenues, it becomes clear that their forecasted revenues for the test year are underprojected by at least one percent of revenues or $2,493,000 [T. 2229, 2335].

In support of his position, Dr. Rosen demonstrates that while weather-adjusted sales have grown 318 GWH's per year from 1986 - 1989, the Company has projected growth in 1990 of <u>only 124</u> GWH's [T. 2335]. The Company's own average forecast of sales growth for the years 1990 - 1993 show an average increase per year of 204 GWH's. This represents a 2.7 % increase over 1989 [T. 2234-2235].

Exhibit 337 shows Company actual and projected retail sales for the years 1983 through 1989 and the months of January and February 1990. This exhibit shows that in 6 out of the 7 years, the Company underestimated its retail sales [T. 2366]. Also, this exhibit shows that the smallest increase from one year to the next since 1983, was <u>260 GWH's</u> as compared to the Company's projected increase for 1990 of <u>124 GWH's</u> [T. 2366].

In order to conservatively adjust the 1990 sales forecast, Dr. Rosen recommended that the revenue forecast level be increased by one percent [T. 2370-2371]. Dr. Rosen derived this number simply by accepting Gulf's own medium-term forecast and taking the annual average of Gulf's own projection for the period 1990-1993. Using Gulf's medium-term forecast, rather than the short-term (one year) estimate as the Utility proposes, has the added value of being more representative of the period of time that rates will actually be in effect [T. 2414].

ISSUE 50: Has Gulf budgeted a reasonable level for salaries and employee benefits?

OPC Position: Employee benefits should be reduced by $1,405,445.

DISCUSSION: The Company has projected an increase in employee benefits of $443,000 for 1990. This brings to total fringe benefits to $11,500,000 [T. 657]. In analyzing these benefits, Mr. Schultz created Exhibit 309 from information provided by the Company.

The first two adjustments on this schedule is to reduce postretirement medical and life insurance benefits to reflect a cash basis accounting for these [T. 2565-2566]. The Company in the past has also accounted for these on a cash basis. Mr. Scarbrough testified that the Company decided to start accruing for these costs in 1990 [T. 3796].

The rationale for this change is that FASB has issued an exposure draft to consider accruing for post retirement benefits and may adopt this procedure later this year [T. 3797]. The Company evidently did not originally budget this item since the planning unit work papers for 1990 did not include this change [T. 2466]. Even if FASB passes this rule, it should in no way affect the regulatory treatment of these benefits. The test year post retirement amounts transferred to non-O&M accounts should be removed.

Also to be removed is the $363,800 in supplemental benefits which go to three executives. These benefits are above the IRS limitations and do not benefit the ratepayers [T. 2467].

__ISSUE 54__: Should the 1990 projected test year be adjusted for any out-of-period non-recurring, non-utility items or errors found in 1989?

__OPC Position__: Yes. Remove $116,000 for heavy equipment rebuilds and $252,000 for renovations to the Panama City office.

__DISCUSSION__: Please refer to the discussion on Issue 29 for support of this issue.

__ISSUE 55__: Are Gulf's budgeted industry association dues in the amount of $199,343 during 1990 reasonable and prudent?

__OPC Position__: In addition to those removed by the Company, based on the latest EEI report, an additional $21,608 should be removed [T. 2474-2475].

ISSUE 56: What is the appropriate amount of rate case expense to be allowed in operating expenses?

OPC Position: Since no rate increase is necessary, no expense should be allowed for recovery. Reduce expenses by $500,000. In the event this Commission determines that a rate increase is appropriate, the expense should be adjusted based on the ratio of the total rate relief granted to the total relief sought. This adjusted amount should then be amortized over 5 years [T. 2464]. Reduce operating expenses by $300,000.

DISCUSSION: Gulf's last base rate increase was implemented in December of 1984 and included a two year amortization of rate case expense [T. 348-349]. The reasons cited by Mr. Scarbrough for requesting a two year amortization are:

1. this was the amortization period allowed in the last case; and

2. since 1979 the Company has had five rate cases thus averaging one every other year [T. 350, 3800].

Mr. Scarbrough agrees that if a shorter period is granted than is actually experienced, there will be an overrecovery of this expense [T. 349]. Further, he admits that a mechanism can be set up to recoup any unamortized balance whereas any overamortized balance cannot be recovered [T. 351].

In order to assure fairness on any amortization, the Commission should follow the advice of Mr. Schultz and amortize the rate case expense over five years [T. 3464].

ISSUE 58: Should Bank Fees and Line of Credit charges be included in operating expenses?

OPC Position: The total budgeted amount for this item should be borne by the stockholders; expenses should be reduced by $223,400.

DISCUSSION: Mr. McMillan testified that the new policy of reducing compensating balances and paying bank fees to secure lines of credit is a prudent move on Gulf's part [T. 777-789]. The savings to the customers is claimed to be that under the old method, the customers would support a working capital amount of $4.4 million or an approximate cost of $585,000. Under the new method, the ratepayers will pay the test year level of bank fees of $223,400 for a net savings of $361,600. While this sounds like a good deal for the ratepayers, it is even a better deal for the stockholders. They will receive the earnings on the temporary cash investments below the line without bearing any of the costs.

Mr. Schultz testified that the shareholders will receive $491,000 in interest on the temporary cash investments in 1990 [T. 2483]. The Commission should consider the bank fees as below the line costs to offset the interest the stockholders will receive.

__ISSUE 62__: Gulf has budgeted $50,000 for the Good Cents Inventive program. Is this expense appropriate?

__OPC Position__: In the event this or any other program is contrary to Commission policy on conservation or cannot be justified as a legitimate expenditure, it should be disallowed.

DISCUSSION: Refer to discussion in Issue 63.

__ISSUE 63__: Gulf has budgeted $457,390 for the Good Cents Improved and $1,023,995 for the Good Cents New Home programs. Are these expenses appropriate?

__OPC Position__: No. Remove $1,023,995 for the Good Cents New Home Program and $609,783 for the Good Cents Improved Home Program.

DISCUSSION: In disallowing the Improved Home program, the Commission wrote the following passage which equally applies to all conservation programs on either new or retrofit homes:

> On cross examination, Mr. Young admitted that:
>
> The Company __does not have data on what efficiency equipment would be installed without the Good Cents Program__, __nor does it know with precision what efficiency equipment is being replaced__ by this program. This leads us to conclude that even the demand savings Gulf claims for that program may be __overly optimistic and perhaps even nonexistent__. We find that Gulf __has not demonstrated__ that enough demand and energy savings result from the program to provide benefits to all of the Utility's ratepayers. The Utility has __done no retrofit analysis.__

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Side-by-side demand metering of participating and nonparticipating homes would be prohibitively expensive.

Further, without reference to this program, <u>the marketplace is rapidly improving equipment efficiencies</u>. As laudable as Gulf program objectives may be, we cannot permit the Utility to subsidize participating customer's comfort or value.

(Emphasis added). Order No. 21317, p.39. [T. 2613-2614].

While this quote refers to the Good Cents - Improved program, the philosophy behind the Commission's decision applies equally to the Good Cents New program.

In 1987, the Commission disallowed from inclusion in the ECCR clause, the Good Cents New Home program [T. 881]. The reason for this disallowance was that the Commission determined that the cost benefit was marginal for participating customers [T. 881]. And of course if there is only marginal benefit for participating customers, there can be no benefit to nonparticipating customers. Thus, if the Commission allows recovery of the New Home program, the only one who will benefit is Gulf Power Company.

For much the same reasons as cited from Order No. 21317, the Commission last year disallowed the Good Cents Improved program and ordered it to be fazed out by May of this year [T. 2614].

Part of the rationale Mr. Bowers gave for including the Good Cents New program is that the Florida Model Energy Efficiency code is not universally enforced in Gulf's service area [T. 881, 887]. This argument completely misses the point this Commission made in disallowing this item from ECCR recovery. Gulf has no obligation to provide its service area with enforcement of the energy code any more than it has an obligation to sell refrigerators, stoves or water heaters in its service area. Gulf has decided on its own to get into these areas and is now asking to have its general body of ratepayers pay for the over $1.5 million annual cost of this "service."

What the Commission has said in the past about such programs is "show us" the cost benefit of it and we will consider it. Evidently the Company still cannot provide this showing, since no verifiable proof has been offered by Gulf. Rather, Mr Bowers cites a part of the Commission conservation rule that says that this rule does not:

> . . .preclude the Commission from approving a program shown not to be cost-effective.

[T.4005]

While this part of Rule 25-17.008(3), F.A.C., would allow the Commission to approve a non-cost effective program, the Commission certainly should not apply this provision without a great deal of evidence that the general body of ratepayers will benefit from it. And the evidence is just not forthcoming.

In a further effort to justify these two programs, Mr. Bowers stated:

> Programs included in ECCR do not necessarily have to be quantifiable on their own nor do they have to be cost-effective on their own. The burden of proof

> on a Company is that the entire conservation plan must be cost effective.
>
> [T. 4403]

Mr. Bowers' curious perspective does explain to some extent why the he has failed to provide justification for the Good Cents programs: he believes that the individual programs do not need justification.

Mr. Schultz testified that the Good Cents programs have not been justified and should not be included for recovery [T. 2487-2490]. If the programs are beneficial to some customers, then those customers should be the ones to pay for it. The Company has failed to provide hard evidence that these programs provide energy savings <u>beyond</u> what the free market would provide without this program. And this is the only evidence that could justify it. The Commission should not pass these costs on to the general body of ratepayers.

ISSUE 65: Gulf has budgeted $425,474 for its Energy Education Program. Is this expense appropriate?

OPC Position: No. It should be removed for O&M expenses.

DISCUSSION: What must be kept in mind is that this is not a "one shot" deal. Almost a half million dollars a year is being spent on this program at a time when people are more aware of energy conservation than they have ever been. The entire amount should be disallowed as the Company provides no cost benefit for it.

Mr. Bowers describes this program as services to all customers that are not specifically provided elsewhere. It consists of general education concerning appliances, lighting, energy management, lifestyle information, etc [T. 888]. In 1989, the Commission ordered these costs to be removed from the ECCR.

The Company has not provided adequate support for the need of these services nor their cost effectiveness. Reduce expenses by $425,474.

ISSUE 66: Gulf has budgeted $55,429 for its Presentations/Seminars Program. Is this expense appropriate?

OPC Position: No. They should be removed from O&M expenses.

DISCUSSION: The Commission rightly removed these costs from ECCR as not having been proven to be conservation oriented [T. 891, 2492]. The program consists of presentations requested by commercial customers that help to lower investment risk, lower the life cycle costs and increased product quality [T. 890].

While this program may be beneficial to a few customers, there is no support to include the costs in base rates. If Gulf believes that this is a valuable service, then the customers benefitting should pay for the seminars.

<u>ISSUE 68</u>: Gulf has projected $687,000 ($687,000 System) for economic development expense in the sales function for 1990. Is this amount reasonable?

<u>OPC Position</u>: No. O&M expense should be reduced by $687,000.

<u>**DISCUSSION**</u>: The Company has tried to justify these costs as a <u>benchmark</u> <u>variation</u>. This program is totally inappropriate and the total amount for economic development expenses should be excluded from recovery. Mr. Bowers' own definition of economic development was stated as:

> [E]conomic development is creating wealth through the mobilization of human, financial, capital, physical and natural resources to generate marketable goods and services.
>
> [T. 893-894]

This activity has nothing to do with providing electric service.

Mr. Bowers has testified that since these costs were not in the 1984 benchmark, they are appropriate justification for over three quarters of a million dollars in annual expense overruns. As explained above, Utility people should not be in the business of marketing Florida to businesses. That's the Governor's job.

When asked why Gulf is in the business of community development, Mr. Bowers stated:

> [Gulf's] well-being is directly tied to that of our community and we have a direct stake in the community's overall well being.
>
> [T. 894].

Later he testified:

> Ours [existence] is to evaluate the community's infrastructure needs; determine <u>what's best for that community</u>. . . .

(Emphasis added). [T. 928]

This need to judge what is best for its communities' economies is too far removed from providing electric service to even remotely justify a cost overrun. In fact it proves the Public Counsel's and Staff's contention that these costs should be removed.

Mr. Schultz testified that the Commission policy is to disallow these costs and that these costs were removed in Gulf's last rate case [T. 2502-2503]. Mr. Bowers said of Mr. Schultz's position:

> [Y]ou must believe that uncontrolled and unpredictable growth is better, than or least equal to, controlled and predictable growth.
>
> [T. 4026]

Again, Mr. Bowers has not recognized that Gulf's concerns should not be in managing the growth in its service territory, but rather in managing the growth in its expenses.

ISSUE 69: Gulf has projected $5,358,179 ($5,655,000 System) in Production-Related A&G expenses for 1990. Is this amount reasonable?

OPC Position: No, this amount should be reduced as recommended in other issues.

ISSUE 70: Gulf has projected $31,070,804 ($32,792,000 System) in Other A&G expenses for 1990. Is this amount reasonable?

OPC Position: No, this amount should be reduced as recommended in other issues.

ISSUE 71: Has Gulf included any lobbying and other related expenses in the 1990 test year which should be removed from operating expenses?

OPC Position: No. Mr. Scarbrough has now agreed to remove an additional $101,997 of lobbying expenses, along with $126,566 related to information gathering and administrative activities of its registered lobbyists [T. 3810-3811]. Also, any further expenses that may show up in late-filed exhibit 626 should be removed [T. 3853].

ISSUE 73: For each functional category of expenses, what is the appropriate level of expenses for services provided by the Southern Company?

OPC Position: The Company's amount related to steam production should be reduced by $734,595.

DISCUSSION: Mr. Schultz testified that Gulf does not have the same level of control over these expenses as it does with its own budgeted items [T. 2454-2455]. Since these costs represent over $15 million or 10% of Gulf's budget, the detail should be scrutinized. Yet when asked for the detail of these budgeted items in Public Counsel's first production of documents, the Company responded that the budget detail available for other costs are not used for SCS [T. 2457-2458]. Rather, the Company provided a list of work orders which total $18,253,795. This is too large of a budget item for Gulf not to keep very detailed descriptions of the work performed [T. 2458-2459].

Since the detail has not been provided for in this case, the Commission should consider establishing an investigation docket to examine these expenses in a line-by-line fashion. In the meantime, at a minimum, the Commission should disallow the $734,595 as proposed by Mr. Schultz.

ISSUE 74: Has the company properly removed from 1990 expenses all costs related to IRS, grand jury and other similar investigations?

OPC Position: Any amounts remaining should be removed.

ISSUE 80: Gulf has budgeted $3,017,000 for Transmission rental for Plants Daniel and Scherer. Are these expenses appropriate?

OPC Position: For the reasons cited in Issue 27, Plant Scherer costs should not be included for retail recovery at this time. Based on this position, the transmission rental of $1,822,000 should be removed.

ISSUE 81: Gulf has budgeted $1,047,000 for its Public Safety Inspection and Maintenance program. Is this expense reasonable?

OPC Position: No. This expense should be reduced by $740,000 to reflect the 1990 benchmark.

ISSUE 82: Gulf has budgeted $47,701,000 ($54,079,000 System) for Depreciation and Amortization expense. Is this amount appropriate?

OPC Position: Test year depreciation should be reduced by the effects of removing Plant Scherer and other plant-in-service issues. The final amount will be supplied later in the Operating Income Schedules.

ISSUE 83: Gulf has budgeted $20,822,000 ($31,106,000 System) for Taxes Other. Is this amount appropriate?

OPC Position: This amount should be adjusted based on other issues raised. The final amount will be supplied later in the Operating Income schedules.

ISSUE 84: What is the appropriate amount of income tax expense for the test year?

OPC Position: This amount should be adjusted based on other issues raised. The final amount will be supplied later in the Operating Income schedules.

ISSUE 85: What is the proper interest synchronization adjustment in this case?

OPC Position: This amount should be adjusted based on other issues raised. The final amount will be supplied later in the Operating Income schedules.

ISSUE 86: Should an adjustment be made to the test year reference level of $2,630,877 for the Employee Relations Planning Unit?

OPC Position: Until and unless valid documentation is supplied, the Commission should remove $728,826 for O&M expenses.

DISCUSSION: Due to an error in the Company's calculation of the of the 1988 reference level for this planning unit, the Company believes that this adjustment is not warranted [T. 3897-3899]. As of the hearing date, the Company had not provided documentation detailing this error [T. 3899]. Gulf has agreed to provide this documentation in late filed Exhibit No. 628.

Once this exhibit is received and if it is indeed indisputable evidence of an error, then the requested amount is appropriate. However, since there has been no verifiable evidence submitted at this point, the Commission should remove $728,826 from O&M expenses as not being justified [T. 2434-2436].

ISSUE 87: Has the company made the proper adjustment to remove the effect of vacancies on the labor complement?

OPC Position: No. The labor complement adjustment is understated by $990,381. This also requires a payroll tax decrease of $78,406.

DISCUSSION: In this rate case, Gulf agreed that this issue, brought up in their last (withdrawn) case, has merit. The current case was filed with an adjustment to the labor complement of $378,417 [T. 655-656, 2438]. This adjustment was based on an average of 38 vacancies for the first eight months of 1989. Mr. Bell, for the Company, stated that in his opinion this adjustment: "does not necessarily reflect the Company's hiring plans and may result in an overstatement of O&M expenses in the forecast." [T. 702]. Mr. Bell, who was hired to review the Company's forecast for accuracy, did not provide information as to how much the Company's adjustment was overstated.

In reviewing the forecast information in this case, Mr. Schultz concurs with Mr. Bell's finding that the Company's adjustment may result in an overstatement of O&M expenses. Mr. Schultz, however, does recommend an additional reduction in O&M expenses of $990,381 and a related reduction in other taxes of $78,406 [T. 2438-2439].

This adjustment is based on the most current information available at the time of his prefiled testimony. The Company had budgeted 1,625 positions, but at February, 1990 there were only 1,567 filled [T. 2438]. This is under budget by 58 vacancies. On

Exhibit 303, Mr. Schultz calculated an additional adjustment based on average employee salaries.

The Company, through Mr. Bell and Mr. Gilbert, disputed this calculation because the average total salaries is higher than would be expected for new employees in these positions [T. 3370, 3886]. Yet, in their rebuttal, neither witness supplied the proper average salary to use. Only upon cross examination did Mr. Gilbert agree to provide this information as it relates to his rebuttal schedule 9 [Exhibit 565] [T. 657].

The Company also challenged Mr. Schultz's calculation as being unrepresentative since he used only one month [T. 3770, 3887]. Yet, Mr. Gilbert employs the same reasoning in his reliance on the most recent month (May) as being representative of the test year [T. 657].

Even though Mr. Bell and Mr. Schultz believe that the Company's calculation of the labor complement will cause the O&M to be overstated, the Company has failed to produce any reasonable alternate calculation of the adjustment. The Commission should use the adjustment recommended by Mr. Schultz.

ISSUE 88: The company has included $5,340,000 in Turbine and Boiler inspections, is further adjustment necessary?

OPC Position: Yes, based on a five year projected average of amounts supplied by Gulf, the Company will average $4,602,000 in annual expenditures for 1990 through 1994. Therefore, the Company's amount should be reduced by $ 738,000

DISCUSSION: Mr. Lee testified that Gulf was committed to perform Turbine and Boiler (T&B) inspections on recommended inspection cycles. Except to accommodate operations, these inspections are very predictable [T. 1443-1444]. For 1990, Mr. Lee testified that the inspection was to be performed on "one of our larger units on Gulf's system in this year." [T. 1463]. Further, Mr. Lee stated that in 1987 "we only inspected Scholz No. 1, and it was only $800,000." [T. 1475].

Mr. Schultz agrees with Mr. Lee that the T & B inspections are cyclical in nature [T. 2444]. However, since different units are inspected at different times, the cycles are erratic in that the amount of cost varies from year-to-year. Based on the Company's records since 1984, and as projected for 1990 through 1994, Mr. Schultz created Exhibit 304 [T. 2444-2446].

Exhibit 304 shows the most recent projections of the T & B inspection cycle for the five years ending 1994. The projection (which is factored for inflation) shows the highest single year to be 1994 with an expense of $5,880,000 and the lowest to be 1992 with only $900,000 [Exhibit 304]. This projection demonstrates that this program is too volatile to allow inclusion of the projected test year amount. Rather, an average of expected expenditures over a period of years should be used as this is the time period the approved rates in this case will be in effect. For this case, the Company's forecasted 1990-1994 projections, which average $4,602,000, would be the most appropriate amount. This results in a reduction of $738,000.

__ISSUE 89__: What, if any, adjustments should be made to the level of expenses for Plant Daniel?

__OPC Position__: Plant Daniel steam production costs should be reduced by $646,000 and the A & G expenses should be reduced by $1,172,000 to reflect the proper benchmark level.

__DISCUSSION__: Based on an appropriate benchmark calculation, the Plant Daniel steam production expenses should be reduced by $646,000 [T. 2449]. Mr. Schultz testified that based on his review of the budgeting process for Plant Daniel, Gulf has very little control over these expenses [T. 2446-2448]. The Company took exception to this claim and Mr. Lee testified:

> [W]e review the budgets submitted to Gulf from Mississippi Power for reasonableness. Throughout the year, we review the budget comparison report regarding Plant Daniel expenditures verses budget.
>
> [T. 3593]

Noticeably missing from Mr. Lee's description, as well as others presented in this case, is any support that Gulf is an "active" party in the budgeting and operations of Plant Daniel. Reviewing the proposed budget is an activity performed outside the mainstream of the budget process, as is reviewing the deviation reports during the year. Participation in the operation of a plant requires "hands on" management which Gulf has failed to demonstrate that they have in the operations of Plant Daniel.

Setting aside the argument of operation expense input, the Commission must look as the "bottom line" on this issue. That is, are the expenses at Plant Daniel reasonable? In Gulf's last case the Commission determined that based on the benchmark the expenses were not reasonable [T. 2449, 2450]. Using the same test in this case and considering the shallow justification for the overages, the Commission should reduce the Plant Daniel expenses as outlined above.

ISSUE 90: Would it be proper to amortize the 1989 credit to uncollectibles, which arose due to an accounting change, above the line?

OPC Position: Yes. Since the customers have paid for prior year uncollectibles, they should receive any credits that arose due to excess accruals. A four year amortization results in a yearly credit of $203,250.

DISCUSSION: In Gulf's last case, they originally requested an annual accrual of $823,000. This accrual was later reduced by Gulf by $147,000 and by this Commission by an additional $153,000 for a net allowance of $523,000. The Company has had a history of over accruing for bad debt. In 1983, Gulf's actual accrual was $269,109 below the $937,000 that the Commission had allowed in its 1983 rate case [Order No. 14030, p. 22].

Since the Commission's last full rate case order, Gulf has again reverted to over-accruing this reserve. Mr. Scarbrough testified that since 1985, the Company has accrued an average of $782,670 each year [T. 3799]. While Mr. Scarbrough insists that this shows that the customers have not been overcharged for bad debt expense, quite the contrary is true. Each month the Company is required to file a surveillance report showing the Company's revenues and expenses, and the expenses which have been overstated by the difference in this accrual. This overstatement will artificially understate the income that Gulf reported and reduce any refund in the tax refund dockets.

The reason Gulf is making this $813,000 credit to the reserve is that it has changed its method of accounting. The aging method is now used and it requires a reduction to this account because it was determined under the new method to be overfunded [T. 353-355]. When asked if the Company could have amortized this credit over a number of years, Mr. Scarbrough responded: "You could have done that. I don't think that's the proper <u>accounting</u> procedure. . . ." (Emphasis added). [T. 360]. The question for this Commission to address is the proper <u>ratemaking</u> treatment.

Mr. Schultz testified that the proper ratemaking treatment is to amortize this back to the rate payers who contributed to this reserve [T. 2463]. This amortization would result in a credit to expenses of $203,250 per year [T. 2464].

ISSUE 92: Should the Commission remove all or part of the costs of the Productivity Improvement Plan (PIP)?

OPC Position: Yes. The entire $464,177 should be removed from test year expenses.

DISCUSSION: The PIP plan is limited to 11 senior executives in 1990 [T. 2470]. Mr. Jackson described it as long term incentive plan based on an average Return on Common Equity [T 2967]. Mr. Scarbrough, however, admitted that the ratepayers are not concerned with employees creating a higher return due to their efficiencies [T. 563].

In fact, since this plan is based on Southern Company's return on equity [T. 376, 2469], this plan is nothing more than an above-the-line profit sharing incentive that should be below-the-line where it belongs. The Company has agreed to remove $358,209 from this plan [T. 767, 2968]. However, the balance of $105,968 should also be removed [T. 2471].

<u>ISSUE 93</u>: What amount of the Performance Pay Plan should be approved for retail recovery?

<u>OPC Position</u>: None of this amount is appropriate for recovery in retail rates and operating expenses should be reduced by $1,021,637.

<u>DISCUSSION</u>: This incentive was started in 1989 when the payout was only $198,953 [T. 545, 2473]. The plan was set up in order to reward better employees with bonuses of up to 20% of their base pay [T. 2473].

Mr. Schultz testified that this program is not properly recovered from the ratepayers and that the bonuses are awarded along <u>with</u> normal pay raises. The ratepayers are entitled to receive efficient service which results from highly motivated, professional employees without having to pay extra for it. The Commission should not allow this new programs costs to be recovered through rates.

ISSUE 94: What amount of the $326,808 for EPRI nuclear research should be included for setting retail rates?

OPC Position: The entire amount should be removed from expenses.

DISCUSSION: Mr. Schultz testified that there are four reasons that these costs should not be borne by the ratepayers. First, Gulf has no nuclear plants. Second, Gulf currently has excess capacity and will not benefit from this in the near future. Three, Gulf has not demonstrated any benefit for the ratepayers to justify this cost. Finally, when Gulf needs to add power,it is not likely to be nuclear.

Mr. Parsons, on the other hand stated that while Gulf has no nuclear plants and is not planning to build one, Gulf does benefit from this research [T. 1250-1252]. He argues that much of the research is generic to steam plants. Yet there is no verifiable showing by the Company that this is the case. He further argues that Gulf benefits since it is a member of the Southern System which has nuclear plants on line. Certainly he does not suggest that the benefits of the lower generation costs of Georgia Powers nuclear plants flow through to Gulf's ratepayers.

Based on the record in this proceeding, the Commission should reject the Company's "showing" of benefit to Gulf's ratepayers for nuclear research.

<u>ISSUE 95</u>: Should an adjustment be made to the Plant Smith ash hauling expenses?

<u>OPC Position</u>: Yes. This expense is overstated by $360,000.

<u>DISCUSSION</u>: The following passage from the Company's response to OPC Document Production No. 8 shows that the test year level for this expense is unrepresentative of future years.

> As power is generated, the resultant ash is sluiced to a large pond where it settles and accumulates. In order to comply with environmental regulations, Smith Plant has diked and drained the southern half of this pond so that the ash can be removed and hauled to permanent dry storage sites called cells. This work has been going on for years. Completion of cells 9 and 10 will "clean out" the remaining ash from the drained area, <u>allowing the plant to operate for many years</u>. Since this area is drained and diked, it is economically wise to complete this work before the area must be reflooded next year to accommodate ash again.

Mr. Schultz pointed out that $360,000 of this cost for 1990 is nonrecurring and should be removed from O & M [T. 2479-2480]. The only rebuttal testimony is that of Mr. Lee and he does not rebutt the claim that this work is nonrecurring, his rebuttal only states that this work is to be performed in the test year [T. 3597-3598].

<u>ISSUE 96</u>: What, if any, adjustment should be made to the Company's employee relations budget associated with the relocation and development programs?

<u>OPC Position</u>: The development program costs of $72,250 should be removed as well as the $172,460 in costs associated with selling homes of relocated employees.

<u>DISCUSSION</u>: The question here is not <u>should</u> relocation costs be recoverable through rates but rather <u>how much</u> should be paid. The 1989 increase for this program was $176,690 or double the previous year [T. 2480].

Mr. Schultz testified that he found that 22% of the average price of the homes was included as costs of relocation. Given that ten employees are projected to be relocated in 1990, this comes to an average of $32,410 per home [T. 2480]. This is excessive and should be disallowed.

The executive training program should be disallowed because it was not justified.

ISSUE 98: How much if any, of the officer and management "perks" for tax services and fitness programs should be borne by the ratepayers?

OPC Position: Both of these items should be removed. Reduced expenses by $65,000.

ISSUE 99: The company has projected $1,109,000 for duct and fan repairs for the test year. Should an adjustment be made to this level?

OPC Position: Yes. In Exhibit 312, Mr. Schultz calculated the average for this cost over the period 1984 through 1989. His average of $833,914 shows that the test year amount is not representative and should be reduced by $ 275,086 [T. 2485].

ISSUE 100: Should an adjustment be made to the Customer Services and Information benchmark?

OPC Position: Yes. Conservation costs not allowed for ECCR recovery should be disallowed in base rates also. Reduce expenses by $1,207,237.

DISCUSSION: Refer to discussion on Issues 62, 63, 64 and 65.

ISSUE 101: The company has included expenses for marketing in the test year. Should an adjustment be made to remove this cost?

OPC Position: Yes. The identifiable level of marketing expense which should be removed is $303,814.

DISCUSSION: Mr. Schultz testified that Gulf should not justify its increased marketing activities by claiming that there is increased competition [T. 2498]. The fact is that Gulf has no real competition in its service area. In its 1990 Base Case Budget forecast, Gulf claimed it serves an 80% share of its territory's population [T. 2499]. Gulf's customers do not benefit from marketing activities aimed at increasing sales.

Of the $1,148,489 of identifiable marketing expenses, $303,814 is not justified or covered by other issues. See the discussion of Issue 68 concerning economic development.

ISSUE 102: **What adjustments are necessary to reflect a proper benchmark test of expense levels?**

OPC Position: The following expenses have not been adequately explained or verified in the Company's benchmark analysis and should be reduced accordingly.

a. Plant Crist-condensing & cooling proj.	$ 289,000
b. Distrib.-work order clearance	$ 418,154
c. Distrib.-underground line extensions	$ 351,000
d. Distrib.-network protectors	$ 90,000
e. Electric & magnetic fields study	$ 39,000
f. Acid rain monitoring	$ 43,000

	$ 1,230,154

DISCUSSION: The Plant Crist cooling tower project has been used to justify a benchmark variance of $289,000 [T. 2504]. While this project may be a necessary one, it is not a justification of a benchmark excess. In the base year 1984, there would have been similar projects that have been replaced in this test year by this project. Further, in 1988 the Company shows a budget variance for this expense under the 1988 budget of $360,000 [T. 2505]. This serves as a test of the reasonableness in the test year, in that there is an indication that the current expense may be overstated.

The Company has only justified part of the distribution work order clearance excess. This expense should be reduced by $418,154 [T. 2506-2508].

The Company has also failed to justify the excess amount for underground line maintenance expenses. Mr. Schultz testified that the new underground lines should be less expensive to maintain than above ground lines [T. 2508-2509]. O&M expenses should be reduced by $351,000.

The Company's claim that the network replacement program should be expensed rather than capitalized is erroneous. The network protectors are over 38 years old and this project will significantly extend their life [T. 2510]. The $90,000 should be removed from expenses and capitalized (see discussion of issue 30).

The Company has tried to justify part of its excess over the benchmark by citing the cost of the electric-magnetic fields study. It is highly unlikely (and the Company did not dispute this claim) that there were not other research projects in 1984 that this project replaces [T. 2511]. Therefore, this should not be used as benchmark excess justification, and the $39,000 should be removed from O&M expenses. The final item that the Company has failed to justify is research for Acid Rain Monitoring. The Company contends that the amount in 1984 was zero, so that this expenditure explains part of the excess over the benchmark. Gulf's contention is not true. Based on the Company's response to Staff Interrogatory 4-1 in Docket No. 881167-EI, the 1984 expenses included $47,452 [T. 2512]. Based on this, operating expenses should be reduced by $43,000 for excess over the benchmark.

<u>ISSUE 103</u>: Gulf has budgeted $129,712,291 for O&M expenses. Is this amount appropriate?

<u>OPC Position</u>: This is a fall-out issue and will be provided with separately filed schedules.

Miscellaneous

ISSUE 104: Was the production and promotion of the appliance video known as "Top Gun" contrary to the Commission's policy regarding fuel neutrality?

OPC Position: Yes.

ISSUE 105: Was the production and distribution of tee-shirts with the "Gas Busters" symbol contrary to the Commission's policy regarding full neutrality?

OPC Position: Yes.

ISSUE 106: Was the incentive program known as "Good Cents Incentive" which utilized electropoints that were redeemable for trips, awards, and merchandise contrary to the Commission's policy regarding fuel neutrality?

OPC Position: Yes. These costs should not be included for recovery.

ISSUE 107: In 1987, a commercial building received energy awards from both the U.S. Department of Energy and the Governor's Energy Office yet did not receive Good Cents certification because of a small amount of back up gas power. Was this practice contrary to the Commission's policy regarding fuel neutrality?

OPC Position: Yes.

ISSUE 108: Has Gulf participated in misleading advertising in order to gain a competitive edge on the gas usage?

OPC Position: Yes.

Revenue Requirements

ISSUE 110: Gulf has requested an annual operating revenue increase of $26,295,000. Is this appropriate?

OPC Position: This is a fall-out issue and will be provided with separately filed schedules.

ISSUE 111: Should any portion of the $5,751,000 interim increase granted by Order No. 22681 issued on 3-13-90 be refunded?

OPC Position: Yes, the entire amount should be refunded.

Cost of Service & Rate Design

*STIPULATED ISSUE 113: Are the company's estimated revenues for sales of electricity based upon reasonable estimates of customers, KW and KWH billing determinants by rate class?

OPC Position: Yes, with the exception that the utility should have included billing determinants for the PXT customer who used 7959 KW of standby power in 1989. The billing determinants are based on the no migration filing.

*STIPULATED ISSUE 114: The present and proposed revenues for 1989 are calculated using a correction factor. Is this appropriate?

OPC Position: Yes. While proper estimating procedure would eliminate the need for correction factors, the method used by Gulf requires that the revenue forecast done by revenue class in aggregate be reconciled with the forecast developed by the rate section.

ISSUE 115: What is the appropriate cost of service methodology to be used in designing the rates of Gulf Power Company?

OPC Position: The Equivalent Peaker Cost methodology proposed by Citizens' witness, Robert Scheffel Wright. However, if the Commission decides to use a Refined Equivalent Peaker cost study, it should require that Gulf perform a study of energy consumption in the Company's actual on-peak hours, not their energy use in the highest-demand hours under the load duration curve, to allocate the energy-related component of production plant. Additionally, the revised study should classify fuel inventory as energy-related and should directly assign the rate base value of primary and higher voltage level conductor that functions as dedicated distribution facilities to the rate classes that these dedicated facilities serve.

DISCUSSION: The Citizens support the Basic Equivalent Peaker cost of service method sponsored by Mr. Wright as the most appropriate study for use as a guide to allocating class cost responsibility in this case. As Mr. Wright testified, the EP method tracks the cost-causing factors that affect utilities' production plant investment decisions better than any other study in the case [T. 2093-2094]. It is superior to the Refined Equivalent Peaker method for several reasons, enumerated by Mr. Wright [T. 2077-2079]. Additionally, the EP method is superior to methods that classify all production plant costs as demand-related because such methods simply ignore "the fact that plant costs are incurred not only in consideration of meeting peak demands but also because of the energy loads to be served." (emphasis in original) [T. 2082-2083]. The witnesses addressed several specific sub-issues relating to the appropriate cost of service methodology; these included the relationship of the various methods to utility generation planning practices, the effects of the EP method on industrial sales, the relative merits of the Basic EP method vs. the Refined EP method, and the alleged "fuel symmetry" problem with peaker type methods. These are addressed separately below.

<u>Generation Planning Foundations for the Equivalent Peaker Method</u>. No one seriously argued that energy requirements do not play a significant role in determining the utility's capital investment in production plant. Even II's Mr. Pollock acknowledged in his direct testimony that capital substitution principles represent a "valid theory." [T. 2800-2801]. Mr. Pollock characterized the EP method as an "oversimplification" of the planning process [T. 2802], and Mr. Howell characterized it as an "overly simplistic generalization" of the process [T. 3534]. They did not, indeed they could not, deny the Ep method's fundamental correspondence to the roles of reliability considerations, driven by peak demands, and economic considerations, driven by energy requirements, in utility generation expansion planning processes.

Mr. Howell also attempted to characterize the EP method as "not at all applicable on a system such as Southern." [T. 3534]. However, on redirect examination, Mr. Wright quoted several passages from the Southern Company's <u>Generation Expansion Planning Document</u> prepared by the System Planning Department of Gulf Power Company, and filed with this Commission in the 1989 Planning Hearings, Docket No. 890004-EU, that directly support his proposal to use system energy at the generation level as the appropriate allocation factor for allocating energy-related production plant costs [T. 2157-2159]. Additionally, even Mr. Howell recognized that economic considerations determine Gulf's decisions as to type of capacity to be added [T. 3556]. Although Mr. Howell made the point that Gulf's current generation planning optimization practices were not in place when most of Gulf's units were planned or committed, he admitted on cross-examination that he "did not go back and look at what type of economic evaluations were done for all the baseload type capacity which Gulf added prior to" his joining the System Planning Department in 1976 [T. 3558]. Thus, he did not deny that at least some relevant economic analyses were done to support the decisions to add Plants Daniel and Scherer, which together account for more than 55 percent of Gulf's net production plant [See Exhibit 351, page 3].

Gulf's witnesses suggested that the EPM will lead to increased oil consumption, because it would make on-peak energy less expensive relative to off-peak energy. This is a disingenuous argument because Gulf's own planning documents show that the Company's long-run capacity mix will move substantially away from its current coal-dominated status, and that its actual generation mix will also show increasing reliance on other fuels.

Effect on Industrial Sales. On cross-examination, Mr. Wright was implicitly asked whether the observed decline in Tampa Electric's industrial sales was attributable to the implementation of rates based on the EP study adopted by the Commission in TECO's last general rate case. Mr. Wright stated that this conclusion was unwarranted [T. 2127]. On redirect, Mr. Wright stated that it was certain that Tampa Electric's industrial sales would decline anyway

[T. 2159-2160]. He stated that TECO's rate base would increase by more than 55%, that TECO already knew of several large industrial customers that were in the process of installing or planning or evaluating cogeneration options, and that the substantial reduction in Tampa Electric's industrial sales was not an unusual event. [T. 2159-2160]. He also stated that the rates approved by the Commission were in fact lower than those proposed by Tampa Electric for its Interruptible Service rate classes [T. 2161, Exhibit 607]. While this was true as stated, Mr. Wright acknowledged that the comparison proffered in Exhibit 607 was not an "apples-to-apples" comparison because the values were based on different total revenue figures. Therefore, at the outset of his rebuttal testimony, Mr. Wright presented Exhibit 613, which included a comparison of the rates proposed by TECO, at its full requested revenue increase, to the rates that would have been indicated by the unit costs from the EP study, also at the Company's full requested revenue increase. Exhibit 613 also presented comparative bottom line bills for TECO's three rate classes, IS-1, IS-3, and GSLD, that would include industrial customers. The comparison for each class was based on a representative industrial customer with a 5,000 kW load and the class average load factor for the test year, and under the full requested increase. These comparisons showed that an average IS-1 customer would experience rates approximately 9.0 percent higher under the EP method, that an average IS-3 customer would experience rates approximately 4.9 percent higher under the Company's proposal than under the EP method, and that an average GSLD customer's bottom-line bill would have been one-quarter of one percent higher under the EP rates. [Exhibit 613]. Together with the fact that none of the other probable causes of TECO's decline in industrial sales observed by Mr. Wright was controverted, this information comparing the rates indicated by the EP study to those proposed by the Company surely supports Mr. Wright's statement that the observed decline in TECO's industrial sales following the 1985 rate case could not be attributed to the implementation of rates based on the EP cost of service method. The magnitude of the price change relative to TECO's own proposed rates, even for the group most seriously affected, was only 9 percent on a representative bottom-line bill; with all the other known factors mitigating toward a decline in industrial sales, this simply is not that significant. Although the Commission sustained an objection to inclusion in Exhibit 613 of a copy of testimony by Mr. Pierce Wood of Tampa Electric in the TECO case, it should take official notice of the following language from its Order No. 15451:

> He [Mr. Wood] stated that the existing interruptible customers should gradually receive rate increases at a level that would ultimately allow the IS-1 and proposed IS-3 classes to be merged.
>
> [Order No. 15451 at 42].

This directly corroborates Mr. Wright's point that TECO's interruptible rates were going to be increased substantially regardless of whether the Commission adopted the EP study, and more importantly, that TECO's interruptible customers were on notice of that fact.

EPM vs. Refined EPM. Mr. Wright's direct testimony supports the Basic EPM as superior to the Refined EPM because, relative to the EPM, the Refined EPM suffers from the following deficiencies:

> 1. it does not track utilities' actual generation expansion planning processes;
>
> * * * *
>
> 2. it does not recognize potential long run marginal or incremental plant costs of off-peak energy use;
>
> * * * *
>
> 3. it results in a lesser degree of "fuel cost matching," or less fuel equity than the basic EPC study. This is particularly pronounced in the case of Gulf Power Company, because some 99.8 percent of Gulf's energy sales are generated from coal-fired generating plants;
>
> * * * *
>
> 4. using the highest-demand hours under the load duration curve is not appropriate;
>
> * * * *
>
> 5. Adopting this approach would place the Commission in a clearly and uncomfortably inconsistent position with respect to production plant cost allocation and the pricing of cogeneration power purchased by utilities.
>
> [T. 2077-2079]

Even Mr. Pollock agreed that a utility would probably not build a baseload unit to serve only during the actual 1430 peak demand hours. [T. 2901]. Additionally, Mr. Howell acknowledged that the economic analysis component of generation expansion planning analyses includes "all the territorial load that we anticipate having an obligation to serve," [T. 3567], and thus is not conducted for only some break even subset of hours over the planning horizon.

Fuel Symmetry Argument. Although Mr. Pollock, in response to a question from the bench regarding Mr. Wright's Exhibit 333, stated that he did not believe that it was "complete," [T. 2945], he did not deny either the veracity of any of the numbers contained therein. The fact of the matter is that Exhibit 354 stands for what Mr. Wright represents that it stands for, namely, that with one very slight exception, the Basic EP method yields a closer match between the classes' allocated shares of baseload plant cost responsibility and their allocated shares of inexpensive baseload energy under the Commission's current average-cost-based fuel pricing practices. [T. 2072-2073].

Gulf's witness O'Sheasy stated that he believed that some fuel symmetry adjustment would be appropriate, but that he was "not sure at this juncture what is the correct fuel symmetry adjustment to make." [T. 3328]. On cross-examination regarding his criticism of the Basic EP method as to its failure to achieve "fuel symmetry," Gulf's Mr. Howell admitted that he is not familiar with the way that the Basic EP allocates costs to the rate classes [T. 3569]. Because Mr. Howell was not familiar with the allocation of costs to the ratepayers (and did not "even understand the terms,"

for that matter) his testimony on this subject cannot be considered persuasive.

*<u>STIPULATED ISSUE 115a</u>: How should Gulf's GS rates be designed?

<u>OPC Position</u>: Gulf's GS rates should be set equal to the company's RS rates.

<u>ISSUE 116</u>: How should distribution costs be treated within the cost of service study?

<u>OPC Position</u>: The costs of dedicated facilities should be directly assigned to the classes whose members are served by the dedicated facilities. Other distribution costs, except service drops and meters, should be classified as demand-related and allocated on the basis of class NCP demands.

<u>DISCUSSION</u>: To the extent practicable, distribution facilities that serve as dedicated facilities serving individual customers or small, identifiable groups of customers within identifiable rate classes, including conductors that function as service drops or dedicated tap lines, dedicated substations, and any redundant distribution facilities serving individual customers (e.g., local capacitors and redundant transformers), should be directly assigned to the classes whose members the facilities serve. These facilities should be classified as demand-related and recovered through a local facilities charge or maximum demand charge (i.e., a charge applicable to a customer's maximum demand, regardless when it occurs). Secondary service drops should be classified as customer-related, allocated to classes on the basis of the mix of metering facilities serving the class (e.g., PXT should be allocated no share of standard secondary voltage level watt-hour high-voltage level metering facilities), and recovered

through cost-based customer charges. Common distribution facilities should be classified as demand-related, allocated on the basis of class NCP demand, and recovered through maximum demand charges (for demand-metered classes) or non-fuel energy charges (for non-demand-metered classes). In keeping with its precedents, the Commission should reject the minimum distribution system approach to classifying and allocating distribution costs. On this point, see Mr. O'Sheasy's direct testimony at T. 1822-1823, wherein he explains that he did not use the Minimum Distribution System concept "[i]n order to conform with Commission policy" as enunciated in Order No. 11498 in Docket No. 820150-EU.

ISSUE 117: How should uncollectible expenses be allocated?

OPC Position: Uncollectible expense should be allocated to all rate classes based on revenues.

DISCUSSION: The Citizens agree with Staff that uncollectible expenses should be allocated on the basis of revenues. As Citizens' Mr. Wright testified on cross-examination, it is his opinion that it would "be more equitable to allocate the uncollectibles between and within classes on revenues and classify [them] as revenue-related." [T. 2141]. He went on to cite an example where a large customer of another utility had entered bankruptcy, leaving the utility with an uncollectible debt in excess of $1 million [T. 2141].

ISSUE 118: How should fuel stocks be classified?

OPC Position: The level of fuel inventory allowed in rate base has been based on a calculated number of days burn which is a function of number of KWH to be generated. Therefore, fuel stock should be classified as energy-related.

ISSUE 119: Are Gulf's separation of amounts for wholesale and retail jurisdictions appropriate?

OPC Position: The appropriate separation factors are those in the cost of service study requested in Staff's Interrogatory No. 209.

ISSUE 120: Is the method employed by the company to develop its estimates by class of the 12-monthly coincident peaks hour demands and the class non coincident peak hours demand appropriate?

OPC Position: No. The 12 CP and class (NCP) demands have been underestimated for LP/LPT and PX/PXT customers taking service on the Supplemental Energy Rider because all KWH forecast to be used during Supplemental Energy Periods have been excluded in the development of the demands. The assumptions for recreational lighting customers have underestimated at least their estimated class (NCP) demand.

ISSUE 121: If a revenue increase is granted, how should it be allocated among customer classes?

OPC Position: Any increase should be allocated among rate classes so as to bring class rate of return indices closer to parity as indicated by the cost of service study approved by the Commission in this case, subject to the transition rules usually followed by the Commission. It should be noted, however, that in determining parity, the Commission should recognize any risk differentials that exist between classes.

DISCUSSION: The Citizens' position on this issue is generally consistent with the Commission's established practice of attempting to move classes closer to parity subject to considerations of rate continuity. To the extent possible, increases should be limited to 1.5 times the percentage increase in total retail system revenues. In this case, the Citizens particularly endorse the parties' stipulation to set Gulf's GS rates equal to its RS rates, as advocated by Mr. Wright [T. 2087].

In attempting to move the customer classes toward parity, the Commission must be careful to recognize that risk (and therefore the cost of equity) to provide services is not the same for all customer classes. As Mr. Rothschild points out:

> It is well recognized that serving industrial customers entails a higher degree of risk than serving residential or commercial customers. As will be explained later in this testimony, it is estimated that the cost of equity to be applied to industrial customers should be about 0.4% higher than the cost level to apply to residential or commercial customers. The returns allowed to each

1875

class should be weighted so that the overall effective allowed return is 11.75%.

[T. 2720]

The Commission should allow for this phenomenon when it undertakes to move the various customer classes toward parity.

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*STIPULATED ISSUE 122: If an increase in revenues is approved, unbilled revenue will increase. Is the method used by the utility for calculating the increase in unbilled revenues by rate class appropriate?

OPC Position: Agree with Staff's position as stated in Order No. 23025.

*STIPULATED ISSUE 123: Should the increase in unbilled revenues be subtracted from the increase in revenue from sales of electricity use to calculate rates by class?

OPC Position: Agree with Staff's position as stated in Order No. 23025.

ISSUE 124: What are the appropriate customer charges?

OPC Position: Customer charges should be set as close as reasonably practicable to the customer unit costs indicated by the Commission-approved cost of service study.

ISSUE 125: What are the appropriate demand charges?

OPC Position: Basically agree with Staff position as stated in Order No. 23025.

ISSUE 126: The company presently has seasonal rates for the RS and GS rate classes. Should seasonal rates be retained for RS and GS? If so, should they be required for GSD/GSDT, LP/LPT and PX/PXT?

OPC Position: If the Commission determines that seasonal rates are cost-based and therefore should be retained for Gulf's RS and GS classes, then seasonal rate should also be implemented for Gulf's other rate classes. If the Commission determines that seasonal rates are not cost-based, then they should be eliminated for all rate classes.

DISCUSSION: The record contains little evidence on the seasonal rates issue. In his rebuttal testimony, Gulf's Mr. Haskins stated that the Company was not proposing to implement seasonal rates for its demand-metered rate classes because it "simply did not want to introduce the additional complexity of seasonal rates for those classes in this filing." [T. 3359]. Common sense dictates that if seasonal rates are appropriately cost-based, then they should apply equally to all classes of service. Additionally, if seasonal rates are appropriate at all, it is obviously unduly discriminatory to impose them on the RS and GS classes without also imposing them on Gulf's other classes. That Gulf "simply did not want" to do so is grossly insufficient justification for such disparate treatment.

Finally, the Citizens note that the Company's cost of service study sponsored by Mr. O'Sheasy does not identify seasonal cost variations. Although the Company's summer peaks in 1987 and 1988 were higher than its winter peaks in those years, in other years, including 1989, this relationship was reversed [See Exhibit 365].

ISSUE 127: If seasonal rates are continued, how should they be designed?

OPC Position: If continued, seasonal rates should probably differ from non-seasonal rates by having greater amounts of demand-related production and transmission costs incorporated into the demand charges (for demand-metered customers) or non-fuel energy charges (for non-demand-metered customers) applicable during the months of the defined peak season or seasons, and by seasonally-differentiated fuel charges.

DISCUSSION: The Citizens' position on this issue is based on the common-sense idea that the significant cost differentials (other than fuel) that could come into play in justifying seasonally differentiated rates would primarily be attributable to differences in peak demands between seasons. Generally, on a system basis, these would be expected to comprise primarily, if not entirely, peak-demand-related production and transmission costs. One reasonable approach to allocating these demand-related production and transmission costs to identified peak seasonal months and non-peak months would be to do so according to aggregate reliability index values in the peak and non-peak months. The allocation of energy-related production costs, and the non-fuel energy charges based on these costs, should not vary seasonally, with a possible exception for seasonal variations in non-fuel variable O&M costs, if identifiable. (Fuel charges are already seasonally differentiated under present Commission practices). Local facilities charges should not vary from season to season, nor should customer charges.

ISSUE 128: How should time-of-use rates be designed?

OPC Position: Agree with Staff's position as stated in Order No. 23025.

ISSUE 130: The company currently gives transformer ownership discounts of $.25 per KW for customers taking service at primary voltage and $.70 per KW for customers taking service at transmission levels. Is the current level of discounts appropriate?

OPC Position: Agree with Staff's position as stated in Order No. 23025.

ISSUE 131: All general service demand rate schedules (GSD, GSDT, LP, LPT, PX and PXT) except Standby Service (SS) and Interruptible STandby Service (ISS) provide for transformer ownership and metering discounts. The company has proposed providing metering discounts only for standby service rate schedules. Should the SS and ISS rate schedules have provisions for both transformer ownership and metering voltage discounts? If so, should the level of the transformer ownership discount and metering voltage discount for SS and ISS be set equal to the otherwise applicable rate schedule?

OPC Position: Yes as to providing transformer ownership credits to standby customers; no as to setting them equal to those of the otherwise applicable full requirements rate schedules.

DISCUSSION: The standby rate local facilities charges are based on the distribution unit cost for the otherwise applicable rate schedule. These charges therefore include transformer costs. The transformer ownership credit was not addressed in the Commission's generic standby rates docket, but because the standby local facilities charge includes transformer costs, standby customers who own their own transformation equipment or facilities should also receive appropriate transformation ownership credits. The level of the transformer ownership discount should be calculated based on 100 percent ratcheted billing demand in order to match the calculation of the local facilities demand charge applicable to standby service. Paying the same credits as applicable under full requirements rate schedules may provide too great a credit because these are calculated on the sum of annual billing demand, which is smaller than 100 percent ratcheted billing demand (i.e., the sum of each customer's maximum demand during the year times 12).

*<u>STIPULATED ISSUE 132</u>: Should Gulf's proposed revision of the statement of the customer service on the standby service rate schedules (SS and ISS) be approved?

<u>OPC Position</u>: Agree with Staff's position as stated in Order No. 23025.

*<u>STIPULATED ISSUE 133</u>: Should Gulf's proposed change in the definition of the capacity used to determine the applicable local facilities and fuel charges on the standby service rate schedules (SS and ISS) be approved?

<u>OPC Position</u>: Agree with Staff's position as stated in Order No. 23025.

<u>ISSUE 135</u>: Should the Interruptible Standby Service (ISS) Rate Schedules's sections on the Applicability and Determination of Standby Service (KW) Rendered be replaced by the language approved for the firm Standby Service (SS) in Docket No. 801304-EI?

<u>OPC Position</u>: Agree with Staff's position as stated in Order No. 23025.

<u>ISSUE 136</u>: The present standby rates are based on system and class unit costs from Docket No. 840086-LEI. Should the standby rate schedules (SS and ISS) charges be adjusted to reflect unit costs from the approved cost of service study (a compliance rerun) in this docket and the 1989 IIC capacity charge rates?

<u>OPC Position</u>: Yes.

ISSUE 137: Order No. 17568, Docket No. 850102-EI approved the experimental Supplemental Energy (SE) (Optional) Rider as a permanent rate schedule on the condition that it become a separate rate class in the company's next rate case. Has Gulf complied with Order No. 17568, and should the SE be a separate rate class?

OPC Position: Agree with Staff's position as stated in Order No. 23025.

DISCUSSION: Consistent with Order No. 17568, the SE customers should be placed into a separate rate class. The reasons for this were explained by Mr. Wright as follows:

> [T]he rate should be redesigned based on considerations of local facilities costs, and also based on considerations of potential differences between the peak demand kW characteristics and the billing demand kW characteristics of SE customers, as opposed to those in the general LP and PX rate classes.
>
> [T. 2146]

ISSUE 138: How should rates for the separate Supplemental Energy Rate Schedule be designed?

OPC Position: The Supplemental Energy rate should have a maximum demand charge designed to recover distribution systems costs, an on-peak demand charge to recover demand-related production and transmission costs, a non-fuel energy charge equal to the class energy unit cost, and a cost-based customer charge. The maximum demand charge should be the distribution unit cost for the SE rate class calculated using 100 percent ratcheted billing demand and assessed on maximum demand registered by the customer during an appropriate ratchet period defined in the tariff. The ratchet period should be the same as the ratchet period applied to local facilities charges for Gulf's standby customers.

ISSUE 139: The applicability clause of the three demand classes (GSD, LP and PX) is stated in terms of the amount of KW demand for which the customer contracts. Is this an appropriate basis for determining applicability?

OPC Position: Agree with Staff's position as stated in Order No. 23025.

ISSUE 140: The current GSD/GSDT and GSLD/GSLDT (LP/LPT) rate schedules have minimum charges equal to the customer charge plus the demand charge for the minimum KW to take service on the rate schedule for customer opting for the rate schedule. Is this minimum charge provision appropriate?

OPC Position: Agree with Staff's position as stated in Order No. 23025.

ISSUE 141: What is the appropriate method for calculating the minimum bill demand charge for the PX rate case?

OPC Position: The minimum bill for PX customers should include at least the customer charge plus a local facilities charge equal to the class distribution unit cost calculated using 100 percent ratcheted billing demand and applied to the customer's highest demand in the two years ending with the current billing month. Basically agree with Staff's approach as to the other cost components of the PX minimum bill.

ISSUE 142: What is the appropriate method for calculating the minimum bill demand charge for the PXT rate class?

OPC Position: The minimum bill for PXT customers should include at least the customer charge plus a local facilities charge equal to the class distribution unit cost calculated using 100 percent ratcheted billing demand and applied to the customer's highest demand in the two years ending with the current billing month. Basically agree with Staff's approach as to the other cost components of the PXT minimum bill.

*<u>STIPULATED ISSUE 143</u>: The proposed change in the application of the minimum bill provision allows a customer who has less than a 75 percent load factor in a given month to not be billed pursuant to the minimum bill provision as long as his annual load factor for the current and most recent 11 months is at least 75 percent. Is this appropriate?

<u>OPC Position</u>: Agree with Staff's position as stated in Order NO. 23025.

ISSUE 144: The company has proposed the implementation of a local facilities demand charge for LP/LPT and PX/PXT customers, which would be applied when the customer's actual demand does not reach at least 80 percent of the Capacity Required to be Maintained (CRM) specified in the Contract for Electric Power. Is this local facilities charge appropriate? If so, to what customer class should it apply?

OPC Position: No. The Commission should require Gulf to implement local facilities demand charges for all of its demand-metered classes calculated and applied in the same way as the local facilities charges prescribed by the Commission for standby customers.

DISCUSSION: Mr. Wright testified that Gulf should implement a local facilities for its LP/LPT and PX/PXT classes calculated in the same way as the cost-based local facilities charges that apply to standby service [T. 2089]. Even granting that Gulf plans to administer its proposal so as to avoid the potential anti-conservation properties identified in Mr. Wright's direct testimony [T. 2088-2089], there is no "justification for continuing to treat stand-by customers any differently than full requirement[s] customers when it comes to rate design and cost recovery for local distribution facilities." [T. 2098]. Maintaining this separate treatment may even unduly discriminate against cogenerators and other self-generating customers. The Commission recognized the sound cost basis of the local facilities charge for standby service in Docket No. 850673-EU; it applies equally well to full requirements service.

ISSUE 150: Should LP customers who have demands in excess of 7500 KW but annual load factor of less than 75 percent be allowed to opt for the PXT rate?

OPC Position: No.

DISCUSSION: Allowing customers to opt up based on size, rather than on usage characteristics, would reduce the homogeneity of the PXT class, resulting in potential underrecovery of costs from the customers thus opting up and in potential intra-class cross-subsidization.

ISSUE 151: Should Gulf's proposal to decrease the PXT on-peak energy charge and increase the off-peak energy charge be approved?

OPC Position: No.

DISCUSSION: Although the Company's proposed changes are in the right directions, the non-fuel energy charges for both on-peak kWh consumption and off-peak kWh consumption should be set equal to the class energy unit cost, unless evidence is presented to establish that variable O&M costs differ between the on-peak and off-peak periods, in which case a slight on-peak/off-peak differential based on such variable O&M cost differences would be justified [T. 2085]. Gulf's cost of service study does not identify or analyze costs by time period, i.e., for on-peak and off-peak periods, so there is no analytical cost basis for differentiating the energy charges for demand-metered classes by time period. The goal of sending appropriate price signals for on-peak and off-peak use is sound, and in this regard it makes perfect sense that peak-demand-related costs are appropriately recovered through on-peak charges. However, it is not clear that energy-related costs, other than fuel, vary measurably between on-peak and off-peak periods; accordingly, the Citizens support Mr. Wright's proposal to set both the on-peak and off-peak energy charges at the class energy unit cost, subject to adjustments to reflect measured differences in variable O&M costs between periods.

ISSUE 152: Should scheduled maintenance outages of a self-generating customer that are fully coordinated in advance with Gulf Power be subject to the ratchet provision of the SS rate?

OPC Position: Yes as to local facilities charges; no as to reservation charges, subject to certain conditions discussed below.

DISCUSSION: All demands registered during maintenance outages, even those fully coordinated in advance with Gulf should be subject to the ratchet provisions of the SS rate applicable to local facilities charges [T. 3087-3088].

Additionally, all kW demands registered during the monthly peaks that determine Gulf's payments or revenues pursuant to the Southern Company Intercompany Interchange Contract should be subject to the ratchet provision applicable to the Reservation Charge. If a self-generating customer can coordinate its maintenance power service with Gulf so as to avoid (1) any impact on Gulf's demand-based IIC payments or revenues or (2) any other adverse impacts on Gulf or its general body of ratepayers, then a fair case may be made for excusing demands registered during such periods from the ratchet provisions applicable to the Reservation Charge [T. 3087-3088].

ISSUE 153: Should the assumed 10% forced outage factor for self-generating customers that is built into the SS rate design be continued?

OPC Position: No, but there may be no practical alternative in this docket.

DISCUSSION: In the absence of sound, reliable data to support an alternative value for the forced outage rate used to set the reservation charge, it would be reasonable to use the 10% forced outage rate prescribed by the Commission in Order No. 17159, Docket No. 850673-EU.

However, Gulf Power has thus far failed to collect and report the data on standby usage required by the Commission per Order No. 17159. (On this point, see Mr. Haskins cross-examination at T. 1935-1937.) That Order, issued February 6, 1987, required each subject utility, including Gulf, to collect and report annually certain specified billing data, data on load factor and coincidence factor, and customer generation and availability. Order No. 17159 at 22. The Commission expressly recognized that these data were "necessary to assure, on a continuing basis, that the rates that we [the Commission] approve for these services are fair and cost-based." Id.

Allowing Gulf to continue to set the standby reservation charges on the basis of Order No. 17159, which was issued more than three years ago, when Gulf itself has failed to comply with that Order's requirements to collect and report these data, would unfairly give Gulf control over the rates: through its failure to collect the required data, Gulf can perpetuate the use of an assumed forced outage rate that may well result in unfairly high rates. Unfortunately, there appears to be no information upon which the Commission could act to remedy this problem. Therefore, the Citizens suggest that the Commission penalize Gulf for failing to comply with Order No. 17159 and revisit this issue <u>prior to</u> Gulf's next general rate case, hopefully when Gulf files the required data.

<u>ISSUE 155</u>: Which party to this proceeding should design the company's final rates?

<u>OPC Position</u>: The PSC Staff.

<u>ISSUE 156</u>: If the Commission decides to recognize migrations between the rate classes, how should the revenue shortfall, if any, be recovered?

<u>OPC Position</u>: Agree with Staff's position as stated in Order No. 23025.

__ISSUE 158__: **Should the SE rate be modified to allow additional opportunity sales to self-generating customers who have generating capacity which is available but less economic?**

__OPC Position__: **Generally agree with Staff's position as stated in Order No. 23025.**

__DISCUSSION__: As Mr. Wright testified, there is nothing conceptually wrong with allowing self-generating customers to take supplementary power or "economic back-up" power under terms and conditions similar to those on Gulf's SE rider [T. 3089]. The rate schedule or rider under which such service is taken must include a local facilities charge for the recovery of distribution costs. This local facilities charge should be applicable to the customer's maximum demand, regardless when it occurs, and should be designed in the same way that local facilities charges applicable to standby service are designed. The rate should also include a non-fuel energy charge, applicable to all KWH used by the customers, equal to the class energy unit cost [T. 3089].

The Citizens strongly oppose permitting self-generating customers to take service designated as supplementary power or "economic back-up" power during either forced outages or scheduled maintenance outages of the customer's generating facilities. As Mr. Wright testified, self-generating customers "should not be allowed to take supplemental energy when it's truly standby power." [T. 3119].

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by U.S. Mail or by *hand-delivery to the following parties on this 9th day of July, 1990.

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