Florida Power
CORPORATION

James P. Fama
SENIOR COUNSEL

November 13, 1992

Mr. Steve Tribble, Director
Division of Records and Reporting
Florida Public Service Commission
101 East Gaines Street
Tallahassee, Florida 32399-0850

Re: Docket No. 920949-EU
Our File No. 9200264

Dear Mr. Tribble:

Enclosed please find an original and fifteen copies of Prehearing Memorandum of Florida Power Corporation.

Please acknowledge receipt of filing by returning the enclosed copy of this cover letter.

Sincerely yours,

James P. Fama

JPF:mkv
Enclosure

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BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In re: Joint Petition of Florida Power Corporation and Sebring Utilities Commission for Approval of Certain Matters in Connection with Sale of Assets by Sebring Utilities Commission to Florida Power Corporation	)	Docket No. 920949-EU Filed: November 16, 1992

PREHEARING MEMORANDUM OF FLORIDA POWER CORPORATION

Pursuant to the Commission's Case Assignment and Scheduling Record in this case, Florida Power Corporation (FPC) hereby submits its Prehearing Memorandum.

Sebring Utilities Commission (Sebring) and FPC have entered into an Agreement For Purchase And Sale of Electric System, the provisions of which govern the relief requested in this case. The parties have asked the Commission to approve (1) an amendment to their territorial agreement, (2) the depreciated net book value of $ 17.8 million, (3) any additional amount to be allocated for going concern value deemed to be a prudent investment, (4) the imposition of the Sebring rider rate and the methodology for changing that rate, (5) inclusion of the SR-1 rate schedule as part of FPC's rate schedules, (6) the assignment by Sebring of the Glades territorial agreement, (7) the purchase by FPC of the rate base assets as a prudent investment, and (8) FPC's recovery of certain capacity costs related to a purchase power

Statement of Organization of Political Committee — Page 2

6. List by Name, Address, Office Sought, and Party Affiliation each Candidate or Other Individual that this Committee is Supporting.

Full Name	Mailing Address	Office Sought	Party
NO CANDIDATES NOR	OFFICES SOUGHT AT THIS TIME.	NO PARTY AFFILIATION.	

7. List Any Issues the Committee is Supporting: EQUITABLE SOLUTION FOR RATE PAYERS AND TAX PAYERS IN SEBRING UTILITIES COMMISSION FINANCIAL SITUATION ACTIONS.

List Any Issues this Committee is Opposing: SEBRING CITY COUNCIL'S BLIND OPPOSITION TO ANY SOLUTION OR ACTION OF SUC. (MORE ISSUES TO FOLLOW IN THE FUTURE)

8. If this Committee is Supporting the Entire Ticket of a Party, Give Name of Party:
NO TICKET AND NO PARTY INVOLVED AT PRESENT.

9. In the Event of Dissolution, What Disposition Will Be Made of Residual Funds?
AFTER ALL DEBTS ARE PAID RESIDUAL FUNDS WILL BE RETURNED PRO RATA TO CONTRIBUTORS.

10. List all Banks, Safety Deposit Boxes, or other Depositories used for Committee Funds:
FIRST UNION NATIONAL BANK OF SEBRING

Name of Bank or Depository and Account Number	Mailing Address
FIRST UNION NATIONAL BANK ACCOUNT NO. 18957101170	228 N. RIDGEWOOD DR., SEBRING, FL. 33870

11. List all Reports Required to be Filed by this Committee with Federal Officials and the Names, Address, and Positions of Such Officials, if any?

Report Title	Dates Required To Be Filed	Name and Position of Official	Mailing Address
NO FEDERAL REPORTS ARE REQUIRED.			

State of FLORIDA HIGHLANDS County

I, ROBERT G. POLLARD, being duly sworn, depose (affirm) and say that the information in this Statement of Organization is complete, true, and correct.

(seal)

Robert G. Pollard
(Signature of Chairman of Political Committee)

Subscribed and sworn to (affirmed) before me this 20TH day of JUNE, A.D., 1991.

Notary Public

My Commission Expires Jan 4 1993

S.O.E.

agreement. The parties seek approval of these items in their totality, as these items taken together constitute the bargain struck by the parties.

Approval is warranted because this sale will allow Sebring to retire its existing bonds and pay other debts and expenses. It also will end one of the longest-running episodes of territorial conflict before the Commission. Sebring customers will have the benefit of increased quality of service, superior customer service programs, and participation in many energy conservation programs. Sebring customers will also benefit from lower rates and from lower operating costs. FPC will realize the benefits of filling a geographic gap in its system in such a way that service and territory conflicts will no longer be at issue and burdensome recordkeeping and accounting will be eliminated. FPC will also realize the benefits of deferred or foregone construction of facilities and other efficiencies which are gained through consolidation of resources.

ISSUES

ISSUE 1 Does the proposed Sebring Rider unduly discriminate against Sebring customers?

FPC Position: No. The cost of serving Sebring customers includes the cost of retiring Sebring's debt, while the cost of serving FPC's current customers does not. These two classes of customers are in dissimilar situations, which justifies their paying different rates.

There is nothing unlawful about rate discrimination, so long as it is justified by factual differences between rate classes. Discrimination becomes unlawful only when it is undue--that is, when it entails a rate differential not justified by factual differences

between customers. Thus, rate discrimination questions turn on the facts of each case.

There is no question in this case about the fact that the cost of doing business in the Sebring territory includes the cost of servicing or retiring the Sebring debt. This debt was incurred in order to serve Sebring customers. It is not a part of the cost of serving FPC customers.

Florida law is quite clear that resolution of a discrimination issue requires comparison of the cost of serving the two customer classes in question. In one of the earliest cases on point, the court found that discrimination issues surrounding service to customers in different locations should involve a comparison of the cost of production and delivery to the two customer classes. Cooper, et al. v. Tampa Electric Co., 17 So. 2d 785, 787 (1944). Currently, Sebring's cost of producing power and delivering it to Sebring customers includes the costs of the debt Sebring has incurred. Acquisition of Sebring does not break the link between Sebring customers and the debt incurred for their benefit.

In a more recent case building on Cooper, the court considered the facts surrounding the differing costs of serving customers in different locations. Clay Utility Co. v. City of Jacksonville, 227 So. 2d 516 (1969). The case turned not on the issue of location per se, but on the issue of cost of service: "Based upon the evidence hereinabove summarized, the trial court found that there existed a true and substantial difference in the cost of supplying electricity through larger lines over longer distances to customers outside of the old city limits." Id. at 519. Again, FPC is not seeking to

charge Sebring customers the Rider because they are in a different location, but because they cost more to serve than FPC customers who have not incurred such a debt. Importantly, the court found that the burden rests upon those seeking to establish unlawful discrimination. The proponent must show that the difference in rates cannot be justified on the basis of the cost of furnishing electricity to two different classes of customers. Id. at 518. Likewise, those challenging the Rider as discriminatory should bear the burden in this case.

Later cases reiterate the principles established in the Cooper and Clay cases. Again dealing with different rates based upon the differing cost of serving customers in two locations, the Florida Supreme Court has found no unlawful discrimination, even though "the exact additional cost of delivery of utility services to those outside the municipal limits cannot be assessed with mathematical certainty, although it is obvious that such additional costs exist...." Mohme v. City of Cocoa, 328 So. 2d 422,425 (1976). FPC submits that even though exact cost of retiring Sebring's debt cannot be calculated at this time, it is no less obvious a distinct cost of acquiring and serving the Sebring customers than the costs described in the Mohme case. See also, City of Miami Beach v. Millpin, Inc., 389 So. 2d 283, 286 (1980).

Just as it is undue discrimination to charge different rates to similarly situated customers, it is unduly discriminatory to charge the same rates to customers who are not similarly situated. In a very recent articulation of the principle, the Commission endorsed rates which were "designed to more accurately reflect the costs associated with each service and to place the burden of payment on the person who causes the

cost to be incurred rather than on the entire body of ratepayers." Order No. 24817, p. 21 (July 15, 1991). Applying the lesson of Order No. 24817 to the case at hand, the imposition of the Sebring Rider is the most accurate reflection of the cost of serving customers in Sebring's territory. Stated another way, it is plain that the Sebring ratepayers should bear the cost of retiring Sebring's debt, because they, not the entire body of FPC's ratepayers, caused its incurrence.

ISSUE 2 Is the method used to calculate the rate of the Sebring Rider, and any changes thereto, appropriate?

FPC Position: Yes. The method is fair, verifiable, consistent with other formula rates, and in accordance with the Agreement For Purchase And Sale Of Electric System.

As presented in Mr. Nixon's testimony and in Exhibit 1, page 43, the Sebring Rider is a formula rate. Formula rates, such as the Fuel Cost Recovery factor, Energy Conservation Cost Recovery factor, the Capacity Cost Recovery factor and the Oil Backout factor, are routinely reviewed and approved. The Sebring Rider is designed to recover:

(1) the capital which allows Sebring to retire its debt and cease operations; plus

(2) the interest and other expenses incurred by FPC associated with the capital to be recovered by the Sebring Rider; plus

(3) other revenue related taxes.

The amount of capital to be recovered by the Sebring Rider is the difference between:

(1) the purchase price; and

(2) the depreciated net book value of the Rate Base Assets *plus* any going concern value determined by the Commission to be a prudent FPC investment.

Several elements of the transaction will not be known until after the closing and a final audit. Various factors influencing these elements are Sebring's sales revenues and operating expenses, plant additions, and going concern value. The final costs will be incorporated in subsequent Sebring Rider adjustments. The amount used in the initial Sebring Rider is $38,134,631.00, without the consideration of any going concern value. The Commission has approved transactions based on estimated costs, such as the petition of Florida Power & Light Company for the inclusion of the Scherer Unit No. 4 purchase, FPSC Order No. 24165, (January 26, 1991).

The costs to be recovered under this Rider will be recovered on a kWh energy basis over a 15-year period. The rate will be periodically reviewed and adjusted if necessary. While most of the variables will become known shortly after the closing, such as the interest rates and depreciated net book value, the assumption of kWh sales over the 15-year period remains subject to actual sales and changes in the forecast for the balance of the fifteen year period. If the growth in the area exceeds the medium forecast of 2.09% annually, the Sebring Rider will be lowered; if growth does not meet the projected annual rate, the Sebring Rider will be increased.

FPC will establish and maintain a balance account which nets the revenues from the Sebring Rider against the payments for principal, interest and other expenses. Any monies refunded from the former Sebring operations, such as insurance premium refunds, or partial refund of the additional purchase price, will be credited to this

balance, to the benefit of the Sebring ratepayer. Interest will accrue on the balance at a rate approved by the Commission.

ISSUE 3 Is the forecast of customers and usage used to develop the rate of the Sebring Rider appropriate?

FPC Position: Yes. It is appropriate to rely initially on RMI's forecast. New forecasts will be prepared by FPC at least every four years.

An energy and demand forecast has been prepared specifically for the Sebring area by Resource Management International ("RMI"). The forecast was prepared in late 1991 for the Sebring Utilities Commission for the years 1991 - 2022. For the period, 1993 through 2007, the Medium Forecast produces a total kWh sales of 3,164,633,000 kWh. This represents an average annual energy growth rate of 2.09%. This forecast is appropriate for use in developing the initial rate of the Sebring Rider. The Sebring Rider will be subject to review and revision at least once every four years during the 15-year period. A new forecast will be prepared by FPC for the remaining term of the 15-year period. Future forecasts will incorporate use characteristics of customers subject to the Sebring Rider.

The RMI's forecast results from an econometric model using assumptions similar to those used by FPC in its long term forecast. RMI's forecast additionally includes specific assumptions with respect to Highlands County and Sebring, such as the employment in retail trade and services in Highlands County and the load from the Lakeshore Mall which opened in February, 1992.

For Fiscal Year 1992, the RMI forecast was within 0.3% of actual Sebring energy sales (167,511,000 kWh versus 167,055,013 kwh respectively). The RMI energy forecast for Sebring does not consider the impact of FPC's Load Management Programs or FPC's other energy conservation programs. Two FPC districts adjacent to Sebring have 40% of their residential customers participating in FPC's Load Management program. They receive, on average, a monthly credit of about $9.00. Because the majority of FPC's Load Management programs are directed at reducing demand rather than energy consumption, the impact of Load Management on the sales forecast is not material. Conversely, there is potential for increased usage. The average use by today's Sebring residential customer is 667 kWh per month. FPC's Ridge Division residential customers use an average of 882 kWh per month.

ISSUE 4 Is the method used to identify customers who will be subject to the Sebring Rider appropriate?

FPC Position: Yes. The method is appropriately based on three criteria: (1) whether a customer receives service through a Sebring meter at the time of closing, (2) whether a customer is located in Sebring's territory, and (3) whether a customer is located in the airport area.

The Sebring Rider, as stated in Exhibit 1, Rate Schedule SR-1, page 156, will be applicable to:

1) all customers currently receiving retail electric service through a Sebring meter at the time of closing (and successors to such customers) at any

location within Sebring's territory, or within FPC's territory in, and near the City of Sebring, Florida; and

2) all retail electric service meters at new locations within the Sebring territory at any time after the closing, *except* for meters in the separate Sebring retail service area in and around the Sebring Airport.

Those customers with Sebring meters at the time of closing who have always been Sebring customers should bear the financial responsibility for the Sebring System debt and pay the rider. Additionally, those customers who move into what was formerly Sebring territory will help maintain the customer base in which to spread the Sebring Rider. The Sebring airport is in the Sebring territory but has always been served by FPC, not Sebring, which was confirmed in FPSC Order No. 23823 (December 4, 1990.)

ISSUE 5 Is the proposed 15-year period to collect the Sebring Rider appropriate?

FPC Position: Yes. It results in the Rider being established at a reasonable level and being collected over a reasonable number of years.

Collecting the Sebring Rider over 15 years results in an initial rate which will offer immediate rate relief to Sebring ratepayers. This period also provides a reasonable margin against the risk of negative amortization wherein revenues might not be sufficient to cover the interest expense.

The 15 years coincides with the Amendment to Territorial Agreement and Termination of Settlement Agreement which gives the exclusive right, as between

Sebring and FPC, to operate an electric distribution system in the service territory allocated to Sebring Utilities by the Territorial Agreement.

ISSUE 6 Is the proposed regulatory treatment of the Sebring Rider financing appropriate?

FPC Position: Yes. It is appropriate to tie the Sebring Rider to 100% debt financing.

Using the actual financing associated with the Sebring Rider is more appropriate than the application of FPC's average weighted cost of capital. The financing of the Sebring Rider is a non-recurring requirement with the funds being strictly accounted for from the placement of the rates through the collection of the Sebring Rider revenues to the payment of the debt.

The Sebring Rider will be 100% debt financed through Florida Power Corporation Medium Term Notes, Series B. Separate notes from this series are planned to be issued by FPC at the date of closing or shortly thereafter based on market conditions. These notes will mature beginning approximately the twelfth month after the date of closing through the fifteenth year of the rider. The principal of each note is determined by the revenues received from the Sebring Rider after interest expense and revenue related taxes. The Medium Term Notes provide for the least cost with a fixed interest rate.

ISSUE 7 Should the Commission approve the SR-1 Rate Schedule as a part of FPC's rate schedules?

FPC Position: Yes. The SR-1 Rate Schedule meets the requirements of Florida Statutes Chapter 366 and the Commission's rules and should be approved so that it may be collected upon the closing of the Sebring transaction.

The recovery of the capital, interest and other related expenses associated with the retirement of Sebring's debt can be accomplished only through an approved Commission rate schedule. The evidence presented in this case meets the burden of Chapter 366 of the Florida Statutes and the Commission's rules and procedures. The SR-1 rate schedule incorporates the necessary provisions of a rate schedule as stated in Commission Rule 25-9.031 as it contains provisions covering Availability, Applicability, Rate per Month, Term of Service and Miscellaneous.

ISSUE 8 Should the Commission approve the Sebring Rider and retain jurisdiction of it in accordance with the terms of the Joint Petition?

FPC Position: Yes. The Florida Public Service Commission maintains jurisdiction over the Sebring Rider just as it would maintain jurisdiction over any other rate.

The terms of the Joint Petition are consistent with the Commission's procedures. The terms of the Joint Petition, referring to Exhibit 1, page 44, provide "It is understood and agreed that the Transition Rate will be reviewed periodically by the FPSC along with the review of Buyer's other rates and it is anticipated that this review and resetting of rates will occur no less frequently than every four (4) years." This is consistent with Florida Statutes § 366.06(3)(a) which provides that electric utilities must file with the commission every 4 years, or 4 years from the public

utility's most recent completed rate case, a report consisting of, at a minimum, the modified minimum filing requirements then required by the commission, by rule, for rate proceedings held pursuant to this section in order to allow interested persons to periodically obtain the necessary information to reasonably ascertain whether the rates and charges of a public utility are just, reasonable, and not unjustly discriminatory.

ISSUE 9 Is the cost study performed by RMI to value Sebring's distribution system, transmission system and other tangible assets reasonable and appropriate?

FPC Position: Depreciated net book value is a reasonable method for the valuation of Sebring's distribution system, transmission system and other tangible assets. The RMI study is supported by Sebring witnesses in this case.

Although FPC participated in an organized physical inventory that was utilized by RMI, FPC has not computed or verified the calculations set forth in RMI's study. However, in FPC's opinion, the depreciated net book value approach, is a reasonable method to value tangible assets of the type described therein. Sebring witnesses, Mr. Rumolo, of RMI, and Ms. Holloway, of Sebring have sponsored testimony in support of the net book value of $17.8 million. The portion of the purchase price that is allocable to the Rate Base Assets, is the depreciated net book value thereof as of the closing date. See Exhibit 1, Agreement for Purchase and Sale, Sections 2.2 and 3.16. As discussed by Sebring witness Ms. Holloway, Sebring's auditors have prepared a schedule of the depreciated net book value of Rate Base Assets as of September 30, 1991, totalling $17,813,753.00. This amount, which was derived, in part, from

RMI's study, will be adjusted to the date of closing based on a post-closing audit. See Exhibit 1, Agreement for Purchase and Sale, Sections 2.2 and 3.16.

ISSUE 10 Is the proposed regulatory treatment of the Sebring system acquisition financing appropriate?

FPC Position: Yes. The proposed regulatory treatment is the standard for normal capital expenditures.

FPC proposes to incorporate the Sebring system into its existing capital structure, which is the normal way to treat such an acquisition.

ISSUE 11 Is the methodology used to arrive at the valuation of Sebring's rate base assets appropriate?

FPC Position: Yes. The value of Sebring's rate base assets as of September 30, 1991, has been determined in accordance with generally accepted accounting principles. It is appropriate to continue the accounting practices and treatment employed as of September 30, 1991 through the date of closing. The value of Sebring's rate base assets is supported by Sebring witnesses in this case.

The accounting treatment and practices used in determining the depreciated net book value of the rate base assets as of September 30, 1991, should continue through the date of closing. The 1991 Sebring financial statement has been audited by an independent CPA, and supported by Sebring witness Frank L. Williams.

ISSUE 12 Should the Commission approve the depreciated net book value of Sebring's Electric System assets, as of September 30, 1991, in the amount of $17,813,753.00?

FPC Position: Depreciated net book value is a generally recognized method of calculating electric system assets. Support for the $17 million amount is provided by Sebring witnesses in this case.

Depreciated net book value is a generally recognized method of calculating electric system assets. Sebring witnesses Mr. Rumolo and Ms. Holloway address this issue, and supports the calculation of $17,813,753.00.

ISSUE 13 What are the tax consequences associated with FPC acquisition of the Sebring system?

FPC Position: FPC will take amortization deductions, for federal income tax purposes, with respect to a number of intangible assets that FPC is purchasing, including, without limitation, the exclusive right to operate in Sebring's service area. These amortization deductions are extremely important to FPC, and the Commission's order should be consistent with FPC's intent, as expressed in the discussion of Issue 13 below.

The federal income tax consequences of FPC's purchase of Sebring's system are as follows: The "Acquired Assets", as defined in Section 1.1 of the Agreement for Purchase and Sale of Electric System (the "Agreement"), include both tangible and intangible assets. FPC will obtain a basis (i.e., tax cost) in the Acquired Assets, for federal income tax purposes, equivalent to the total purchase price. Section 1012, Internal Revenue Code of 1986, as amended ("IRC"). The basis of an asset for federal income tax purposes is the beginning reference point for determining depreciation or amortization deductions (with respect to assets that qualify for depreciation or amortization deductions) and the gain (i.e., tax profit) or loss, for federal income tax purposes, on the sale or exchange of such asset.

In a purchase of multiple assets, as is the case under the Agreement, the seller and buyer are each required to allocate the purchase price among the assets. IRC §1060. An agreement in writing between the seller and buyer as to the allocation will, generally speaking, be binding on both parties unless the Internal Revenue Service determines that such allocation is not appropriate IRC § 1060(a).

Under Section 2.2 of the Agreement, Sebring and FPC have allocated the purchase price among the assets being sold and purchased. Thus, approximately, $17.8 million, before adjustment for the period October 1, 1991 to closing, will be allocated among the Rate Base Assets, as defined in Section 3.16 of the Agreement, plus any "going concern" value determined by the Commission to be allocable to the Rate Base Assets and a prudent investment by FPC. The balance of the purchase price will be allocated among certain intangible assets described in Section 1.1(a), (g) (except (g)(1)), (h), (i) and (j) (collectively, the "Specified Intangibles"), in such manner as FPC may determine in its sole discretion. The asset described in Section 1.1(a) is the exclusive right, as between Sebring and FPC, to operate an electrical distribution system in Sebring's service area for a period of approximately 15 years (the "Exclusive Right").

If for example, the purchase price is $55 million and the Commission determines that $22.6 million is a prudent amount for FPC to pay for the Rate Base Assets, including any "going concern" value allocable thereto, the $22.6 million will be allocated among the Rate Base Assets. The remaining purchase price of

$33 million will be allocated among the Specified Intangibles, including the Exclusive Right, in such manner as FPC shall determine in its sole discretion.

Generally speaking, tangible property that is used in a trade or business and that has a finite useful life in the business, qualifies for depreciation deductions for federal income tax purposes. IRC §§ 167 and 168. Intangible assets used in a trade or business that have a finite useful life in the business are subject to amortization deductions, for federal income tax purposes over their useful lives or otherwise required under federal income tax law. In concept, depreciation and amortization deductions are very similar. FPC will take depreciation and amortization deductions with respect to those purchased assets that qualify for such deductions.

In the example set forth above, FPC would determine how it will allocate the remaining $33 million of the Purchase Price among the Specified Intangibles, including the Exclusive Right, and will amortize that portion of the purchase price according to the useful lives of those assets. Thus, FPC may elect to amortize the amount allocated by it to the Exclusive Right over the period of 25 years - the period permitted under IRC § 1253(d)(3). In Tele-Communications, Inc. and Subsidiaries v. Commissioner of Internal Revenue, 95 T.C. 495 (1990), the United States Tax Court permitted the amortization under IRC § 1253 of a cable television franchise granted by a governmental body. Alternatively, the amount allocated by FPC to the Exclusive Right could be amortized, similar to a payment for a covenant not to compete, during the 15-year period that Sebring has agreed to engage in the business of distributing electricity in its service area.

ISSUE 14 Should the Commission approve at this time the prudence of the proposed acquisition of Sebring's electric system assets for recovery from FPC's general body of ratepayers?

FPC Position: In order to allow the Sebring acquisition to go forward, the Commission should at this time approve for recovery in a future FPC rate case, an amount for the Rate Base Assets which the Commission determines to be a prudent FPC investment. The sum of the depreciated net book value of the Rate Base Assets and an amount that Sebring has determined as a going concern value, approximately $23 million as of September 30, 1991, would be a prudent investment by FPC.

FPC recognizes that a determination of prudence for the purpose of placing items in rate base is typically done within the context of a rate case. However, there are good policy reasons, as well as precedent, for granting such approval outside of a rate case, as FPC requests in this case.

The Commission has articulated a policy of encouraging large utilities "to look for and acquire small, troubled systems." FPSC Order No. 25729 (February 17, 1992). In considering proposed acquisition adjustments, it is the Commission's policy to examine whether the customers of the acquired utility derive the following benefits:

1. increased quality of service;
2. lowered operating costs;
3. increased ability to attract capital for improvements;
4. a lower overall cost of capital; and
5. more professional and experienced managerial, financial, technical and operational resources.

FPSC Order No. 23376, p. 2 (August 21, 1990). See also FPSC Order No. 23858, pps. 4-7 (December 11, 1990). It is also the Commission's policy to examine these five factors when considering whether to rate base an acquisition adjustment. FPSC Order No. 24013, p. 13 (January 23, 1991). Thus, these five criteria equally are

applicable in this circumstance where FPC seeks to earn a return on the Rate Base Assets. The testimony of FPC's three witnesses amply demonstrates that FPC brings to Sebring's customers all of the benefits enumerated in these five criteria.

The Commission has the authority, under Florida Statutes §366.06(1), to determine the legitimate costs of the property of each utility company, actually used and useful in the public service, and honestly and prudently invested by the public utility company, including any going-concern value actually paid with respect thereto.

One of the conditions precedent to the obligations of Sebring and FPC to close the sale is that the Commission grant the approvals contained in the Joint Petition, including, without limitation, the Commission's approval of not less than $17,813,753.00 as the depreciated net book value of the Rate Base Assets, as of September 30, 1991, and the Commission's approval of the prudence of FPC's purchase of the Rate Base Assets and any "going-concern" value that the Commission may determine is allocable thereto and a prudent FPC investment. FPC is not willing to take the risk of expending such a substantial sum of money for the Rate Base Assets without obtaining, in advance, the Commission's approval of the prudence of its purchase of the Rate Base Assets and any "going-concern" value that the Commission may determine is allocable thereto. This is simply the nature of a merger and acquisition undertaking. As a matter of good public policy, the Commission should grant such approval in order to foster its stated goal of encouraging large utilities "to look for and acquire small, troubled systems." FPSC Order 25729 (February 17, 1992)

There is Commission precedent for approval of large acquisitions outside of the context of a rate case. For example, the Commission approved outside of a rate case, the rate basing of the acquisition of the Scherer plant by Florida Power & Light Company. FPSC Order No. 24165 (January 26, 1991). That case involved the acquisition of the 76 percent share of a coal-fired plant, for a price $616 million, which exceeded the depreciated book value of the portion of the unit by $111 million. These figures dwarf the rate base recovery of approximately $23 million sought by FPC in the instant case.

The purchase by FPC of the Rate Base Assets, including any "going concern" value that the Commission may determine, would be a prudent investment by FPC. The amount of $22,663,753.00 would be prudent considering the depreciated net book value of the Rate Base Assets and the benefits to FPC and its customers from the purchase of the Sebring electric system, including the long-term benefits as discussed in Mr. Dagastino's and Mr. Southwick's testimony.

The book value will be adjusted to reflect the actual depreciated net book value at the time of closing, and the other numbers discussed above will change accordingly.

ISSUE 15 Should the Commission approve at this time the prudence of any proposed going concern value of the Sebring system for recovery from FPC general body of ratepayers, and in what amount?

FPC Position: The sum of the net book value of Sebring's electric system and the going concern value proposed by Sebring is approximately $23 million. An investment of this approximate amount would be prudent for FPC, and the Commission should render such a determination at this time to allow the Sebring acquisition to go forward.

For all of the policy and precedential reasons discussed in Issue 14 above, the Commission should at this time approve the prudence of an FPC investment in acquiring Sebring, which is the sum of depreciated net book value of the Sebring electric system assets and the going concern value proposed by Sebring (approximately $23 million).

ISSUE 16 Should the Commission approve at this time the prudence of FPC's proposed assumption of Sebring's purchased power contract with Tampa Electric Company?

FPC Position: Yes. The Commission should grant approval at this time of FPC's assumption of Sebring's purchased power contract with Tampa Electric Company (TECO). This contract is legally binding on Sebring's successors and assigns. It has features which will benefit FPC.

Section 8 of the Agreement For Full Requirements Electric Service between TECO and Sebring provides that the Agreement shall be binding upon the successors of Sebring. Any party who acquires Sebring would be legally bound to abide by this contract. The assumption of outstanding contract obligations of the acquired party is simply one of the necessary components of accomplishing a merger or acquisition. Exhibit 1 (page 103 to 106) contains a list of twenty other contracts being assigned to FPC as a part of this transaction.

Contract assignments involve not only the assumption of obligations, but the realization of the benefits of the bargain. In this case, there are many benefits which will flow to FPC under the contract. The TECO contract represents an attractive opportunity to add a reasonably-priced block of highly reliable capacity to FPC's resource mix at this time.

Utility reserve margins typically vary in part due to the fact that additions of blocks of capacity do not coincide with the addition of loads, which tend to grow slowly, rather than in blocks. However, in this case, inclusion of the TECO purchase at the same time that FPC assumes the Sebring load will assure that the transaction has no adverse impact on FPC's projected reserve margins or loss-of-load probability.

Another benefit of the TECO contract is the fact that it is based on the embedded cost of the TECO system, which is primarily coal-based capacity. The contract includes a capacity charge which is guaranteed to remain fixed for the first five years of the contract term. Furthermore, the electricity purchased under the contract has a virtually 100 percent reliability. This is a firm purchase with a priority equal to TECO's native load from a system which currently has a winter reserve margin of 28%. Moreover, it will be delivered over the many points of interconnection that FPC has with the TECO system. Hence, the TECO purchase is much more reliable than a purchase made from a QF or other sole source of generation.

Another benefit of the TECO contract is that it is projected to save FPC's retail customers over $2 million annually in fuel expenses. Assumption of this agreement

is expected to increase the diversity of FPC's fuel mix. The contract also is expected to have a lower cost than many comparable contracts with qualifying facilities.

Because the TECO purchase will be a system-based, partial requirements contract, it will benefit, and hence will be charged to, FPC's general body of ratepayers. While the amount of capacity and energy to be purchased under the contract is based on the pattern and growth of the Sebring load, the capacity and energy purchased will not be dedicated to serve Sebring's load. The TECO purchase will be blended into FPC's resource mix and dispatched in the most economical manner practicable.

FPC seeks approval of the TECO contract for the same reasons that the Commission approves in advance the need for construction of new generation, the execution of qualifying facility purchase contracts or large capacity purchases such as FP&L's purchase of a portion of Scherer Unit #4. Just as the financial risks of building utility generating plants and developing QF projects cannot reasonably proceed without regulatory approval in advance, the acquisition of Sebring cannot proceed without the prudency determination that FPC seeks in this case.

The assumption of the TECO power purchase agreement, as it stands currently, is a condition of FPC's purchase of the Sebring electric distribution system. FPC currently is exploring with TECO certain modifications designed to simplify and better tailor the contract to the needs of FPC and TECO. However, the TECO contract may not be revised during the pendency of this case, or revised at all. The contract is acceptable and desirable to FPC and its customers in its present form.

FPC proposes to address and resolve any and all concerns which the Commission may identify with the current TECO contract within the current proceeding. The company believes that the most appropriate, fair and efficient manner to review and approve the prudence of the contract is in conjunction with the review and approval of the prudence of the entire Sebring transaction, including all of the 20 issues raised in this case. We do not propose to leave any issues to future capacity and fuel adjustment proceedings other than contract administration issues.

FPC asks that the Commission's order in this case explicitly state that the determination of the prudency of the TECO contract reviewed here, not be revisited in a fuel adjustment or capacity cost recovery proceeding in the future. We also ask that the Commission's order explicitly state that in the event that the contract reviewed and approved in this case is later modified, there is no need to revisit the determination of its prudency so long as the modified terms are equivalent or more favorable than the terms of the original contract. FPC seeks a prudence determination which will remain in effect continuously over the life of the contract, as it may be modified for the benefit of FPC and its ratepayers. We believe that FPC is entitled to a reasonable assurance that the determination of prudence granted in this proceeding will continue in force, subject to the same ongoing review and oversight by the Commission as any other prudently incurred purchased power obligation.

ISSUE 17 Should the Commission approve FPC's recovery of the fuel costs associated with the Tampa Electric Company purchased power contract through the fuel cost recovery clause from its general body of ratepayers with no special allocation of costs to Sebring's ratepayers?

FPC Position: Yes. The TECO purchase is a system purchase which will be combined with FPC's other generation, rather than be dedicated to serve Sebring's load.

After making a determination that the TECO power purchase contract is a prudent commitment by FPC, it is expected that the Commission will treat the fuel costs associated with this contract in the same manner as any other approved contract and in accordance with Commission fuel adjustment rules and orders. It is expected that this contract will be subject to the same periodic review as all other prudently incurred fuel expenses.

The TECO contract benefits the entire FPC system and the costs associated with this contract should be recovered from FPC's general body of ratepayers on a system basis, with no special allocation of costs to those customers subject to the Sebring Rider. The FPC customers who will be subject to the Sebring Rider will be customers on an equal footing with all other retail customers of FPC with regard to the generation resources required to meet capacity and energy requirements. They will be served along with all other FPC customers from the system-wide resources of the Company. As a result, any special allocation of fuel costs to these customers would be unreasonable and unsupportable.

ISSUE 18 Should the Commission approve FPC Corporation's recovery of the capacity costs associated with the Tampa Electric Company purchase power contract through the capacity cost recovery clause from its general body of ratepayers with no special allocation of costs to Sebring's ratepayers?

FPC Position: Yes. The TECO purchase is a system purchase which will be combined with FPC's other generation, rather than be dedicated to serve Sebring's load.

As discussed in Issue 17 above, after making a determination that the TECO power purchase contract is a prudent commitment by FPC, it is expected that the Commission will treat the capacity costs along with the fuel costs associated with this contract in the same manner as any other approved contract and in accordance with Commission fuel adjustment rules and orders. Also as discussed above, the TECO contract benefits the entire FPC system and the costs associated with this contract should be recovered from FPC's general body of ratepayers on a system basis with no special allocation of costs to those customers subject to the Sebring Rider. Therefore, a special allocation of capacity costs to Sebring customers is unwarranted.

ISSUE 19 Should the Commission approve the proposed Amendment to the Territorial Agreement and Termination of Settlement Agreement?

FPC Position: Yes. Approval is in the best interests of FPC and Sebring ratepayers.

Under the proposed Amendment to the Territorial Agreement and Termination of Settlement Agreement, Sebring would relinquish, and FPC would obtain, for the balance of the term of the Territorial Agreement, the exclusive right to serve all

customers in the former Sebring area. Obviously, this Amendment is necessary to allow the entire transaction to go forward.

The Territorial Agreement would continue in effect, because the boundaries established in that agreement are needed to determine which former Sebring customers will be charged the Sebring Rider. The Settlement Agreement entered into in 1990, however, will be terminated, saving Sebring and FPC the time and expense of administering the exchange of kilowatthours and customers over the remaining term of that 15 year agreement.

Thus, this transaction will eliminate territorial conflicts, duplication of facilities, and needless expenditures that have prevailed for many years. Customer confusion with respect to their service provider will be eliminated. Both Sebring and FPC will be relieved of difficulties maintaining confusing customer accounting of records in overlapping territories. This consolidation will afford customers with better service. Additionally, disputes regarding duplication of power lines and other overlapping facilities will be put to rest with the proposed transaction.

An issue arose during the course of depositions in this case as to whether amount of monies allocated by FPC to the Exclusive Right will, together with FPC's franchise payments to the City of Sebring (the "City"), constitute a double payment for a franchise. In order to understand why this is not the case, it must be kept in mind that FPC will not purchase the Electric System without the assurance that FPC will have the exclusive right, as between Sebring and FPC, to operate an electric distribution system in Sebring's service area for a period of approximately fifteen

years. At the same time, Sebring has an interest in retiring all of its outstanding bond debt.

The Agreement accomplishes both parties' objectives. Section 1.1(a) gives FPC the exclusive right, as between Sebring and FPC, to operate an electric distribution system in Sebring's service area for a period of approximately 15 years (the "Exclusive Right"). The purchase price for the Electric System, including the portion of the purchase price allocated to the Exclusive Right, together with the proceeds from the sale of Sebring's water system to the City will provide Sebring with sufficient funds to pay in full its outstanding bond debt.

The purchase price to be paid by FPC will be allocated among the assets of the Electric System as set forth in Section 2.2 of the Agreement. Specifically, approximately $17.8 million, before adjustment for the period October 1, 1991 to the closing, plus any "going-concern" value determined by the Commission to be a prudent FPC investment, will be allocated to the Rate Base Assets, as defined in Section 3.16 of the Agreement. The balance of the purchase price will be allocated to certain intangible assets, including the Exclusive Right, in such manner as FPC will determine in its sole discretion.

The agreement between Sebring and FPC with respect to the Exclusive Right is akin to a territorial agreement between two utilities, which is subject to Commission approval, as is the Exclusive Right. Absent Sebring's agreement not to operate an electric distribution system in its entire territory during a fifteen year period, and the Commission's approval thereof, FPC would not be willing to purchase the Electric

System, and Sebring, and FPC would continue operating overlapping facilitates, subject to the existing territorial and settlement agreements.

Furthermore, only 40% of Sebring's customer base is within the City of Sebring. Sebring and the City are separate legal entities, Sebring having been created as a body corporate and politic by special act of the Legislature (Laws of Florida, 1945, Chapter 23535, as amended). Sebring has been granted by its special acts" . . . the exclusive general supervision, charge, operation and management of the City of Sebring public municipal electric, gas and water utilities. . ." and " . . . the full power and exclusive authority to fix rates and charges for electricity, gas and water furnished by [Sebring] . . .." (Special Act, Sections 7 and 9).

FPC wishes to purchase not only Sebring's electrical facilities, but also its entire electric customer base. Effectively, this can be accomplished only by Sebring's agreement that it will not operate an electrical distribution system in its current service area, which includes customers both within and outside the City limits, for a substantial period of time (i.e., fifteen years).

Finally, under the proposed franchise agreement with the City, FPC's franchise payments are required by the City in return for the City's granting to FPC (1) a franchise to operate and maintain within the City limits electric utility facilities required by FPC to furnish electric service to the City, its residents and places of businesses, and (2) the right to utilize the City's rights of way in furnishing such electric service. In the State of Florida franchise fees are typically required by municipalities from utilities that desire to furnish electricity within the city limits.

ISSUE 20 Should the Commission approve the assignment of the Glades Electric Cooperative Territorial Agreement to FPC Corporation?

FPC Position: Yes.

The Assignment of the Glades Electric Cooperative Territorial Agreement will grant to FPC Sebring's entire right, title, and interest under the Glades Agreement dated February 19, 1987, between Sebring and Glades Electric Cooperative, Inc.. As provided in the Joint Petition, FPC seeks approval of the Glades Territorial Agreement assignment as an integral part of the entire transaction which is the subject of this proceeding. The Glades Territorial Agreement evolved out of the resolution of territorial disputes between Glades and Sebring which the Commission approved in FPSC Order No. 18028, (August 24, 1987) and finalized in FPSC Order No. 18161 (effective September 12, 1987). The Agreement specifically remedies overlapping service areas and duplication of facilities in the same territory. It further addresses the problems which arose as a result of the respective areas of service being contiguous and overlapping in some areas, and the parties wanting to avoid duplication of facilities, and to otherwise realize the benefits of defined retail service areas. See Exhibit 1, Schedule 1.6, Exhibit F.

Since the Commission reviewed this matter fairly recently with the Order approving the Glades Agreement, effective September 12, 1987, this issue has already been before the Commission and there is no need to revisit an approved agreement. Additionally, FPC is ready, able and willing to step into Sebring's role and

to perform those requirements under the Agreement of selling electric distribution in the territory.

With the proposed assignment, the purpose and goals of that Agreement would continue to be achieved and further strengthened by FPC's service. Additionally, with FPC's expanded territory to include customers in the Sebring area, FPC believes the Commission should approve the assignment of the Glades Electric Cooperative Territory Agreement to FPC in support of the entire transaction and because the public interest would be best served by the transfer of these rights for consolidation of service.

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H:\SEBRING\PREHEAR.MEM

BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In Re: Joint Petition of Florida Power Corporation and Sebring Utilities Commission for Approval of Certain Matters in Connection with the Sale of Assets by Sebring Utilities Commission to Florida Power Corporation	)	Docket No. 920949-EU Filed: November 16, 1992

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of Florida Power Corporation's Prehearing Memorandum has been served by U. S. Mail, Postage Prepaid to the following parties this 16th day of November, 1992.

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