

FLORIDA PUBLIC SERVICE COMMISSION
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M E M O R A N D U M

September 26, 1996

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYO)

FROM: DIVISION OF ELECTRIC & GAS (R.BASS, BREMAN) *Rue*
DIVISION OF AUDITING & FINANCIAL ANALYSIS (J.BASS, *AM*)
L.ROMIG, MAUREY) *ALM*
DIVISION OF LEGAL SERVICES (ERSTLING) *JDJ*

RE: DOCKET NO. 951433-EI - GULF POWER COMPANY - PETITION
FOR APPROVAL OF SPECIAL ACCOUNTING TREATMENT OF
EXPENDITURES RELATED TO HURRICANE ERIN AND HURRICANE OPAL
BY GULF POWER COMPANY

AGENDA: 10/8/96 - REGULAR AGENDA - PROPOSED AGENCY ACTION -
INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: S:\PSC\EAG\WP\951433EI.BCM

CASE BACKGROUND

On November 17, 1995, Gulf Power Company (GULF or the Company) filed a petition to increase the annual accrual for storm damage from \$1.2 million to \$3.5 million beginning in 1996; and to amortize approximately \$9 million of hurricane-related expenditures to the accumulated provision account over the five-year period of 1996-2000. Additionally, the Company requested that it be allowed to apply any earnings over a 12.75% return on equity (ROE) for calendar year 1995, to the accumulated provision account. GULF also requested that the Commission rule on its petition on or before December 19, 1995, before the closing of its books for 1995.

The Commission resolved all issues except for the annual accrual amount for storm damage. The Commission found there was no basis for determining the reasonableness of the proposed \$3.5 million accrual amount. Instead, the Commission ordered GULF to prepare and submit for review a storm damage study. However, pending Commission receipt and review of the study, GULF was allowed their proposed annual accrual amount of \$3.5 million.

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The Commission required GULF's study to address the impact of random storm events, and their intensities and paths on the accumulated provision account balance as part of determining the appropriate annual accrual amount. GULF filed the study June 13, 1996.

DISCUSSION OF ISSUES

ISSUE 1: Does GULF's study "Transmission and Distribution Study for Hurricanes" adequately address the appropriate accumulated provision account balance and the annual accrual amount as required in Order No. PSC-96-0023-FOF-EI?

RECOMMENDATION: Yes. GULF's study "Transmission and Distribution Study for Hurricanes" adequately addresses the appropriate accumulated provision account balance and the annual accrual amount as required in Order No. PSC-96-0023-FOF-EI. (J.BASS, R.BASS, BREMAN, L.ROMIG, MAUREY)

STAFF ANALYSIS: GULF's analysis of the annual accrual amount is based on a report by independent consultants, M&M Protection Consultants (M&M). M&M used a probabilistic model to estimate a range of possible damage to transmission and distribution (T&D) facilities with three different tests. The first test was an estimate of damage costs to current T&D facilities due to the strongest hurricane on record that affected GULF's service area. The next test was an estimate of T&D damage costs due to a worst case scenario. The third test was an estimate of the average annual damage costs to T&D facilities. All test results presented by M&M are based on a 90 percent probability that the estimated damages will not be exceeded. M&M estimates that GULF can expect \$25.1 million in T&D damages due to a recurrence of the strongest storm on record and \$106.9 million due to a worst case scenario. They project the long term average T&D damage to be \$1.3 million annually.

Key criteria such as location of facilities, current replacement costs, design standards, storm paths, and a 120-year history of tropical storms were incorporated into the probabilistic model. While staff does not necessarily agree with all of the assumptions, the study provides sufficient insight into GULF's exposure to T&D storm damage losses for determining the reasonableness of GULF's annual accrual amount and the appropriate accumulated provision account balance.

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ISSUE 2: Should the Commission change the annual accrual amount from \$3.5 million?

RECOMMENDATION: No. The Commission should not change the annual accrual amount from \$3.5 million. (J.BASS, R.BASS, BREMAN, L.ROMIG, MAUREY)

STAFF ANALYSIS: GULF is not requesting an increase in the annual accrual of \$0.4 million as recommended by M&M Protection Consultants. Staff agrees with GULF's proposal to leave the annual accrual at the \$3.5 million level. Staff believes that an adjustment of this small magnitude infers a degree of accuracy in predicting weather that does not yet exist.

The primary concern is that the accrual amount is sufficient to cover annual damages and promote growth in the Accumulated Provision for Property Insurance account balance. If GULF's estimate of \$1.3 million in annual losses is accurate, then an annual accrual amount of \$3.5 million will be adequate to cover those losses and provide for reasonable increases to the Accumulated Provision for Property Insurance account balance.

The study also recommends the Accumulated Provision for Property Insurance account have a balance between \$20.1 and \$28.8 million and that the balance could be achieved over 10 years with a \$3.9 million annual accrual. However, the target account balance was based on assuming only 80 percent of the actual damages were charged to the account with the remaining 20 percent capitalized. Staff believes this assumption is not appropriate for purposes of determining a target balance level. Instead, all damages should be assumed to be charged to the Accumulated Provision for Property Insurance account. Therefore, based on GULF's study, the appropriate target level for the Accumulated Provision for Property Insurance account is between \$25.1 and \$36 million. The only impact this change has is to increase the number of years required to achieve the target account balance by approximately three to seven years. Thus, staff does not believe this is a material change. The study should not be used as the basis for determining the specific charges to the Accumulated Provision for Property Insurance account. Because of the unpredictable nature of any given storm, deciding the prudence of any particular future charge against the Accumulated Provision for Property Insurance account is premature. If there is a storm, GULF should bear the burden of showing that specific charges against the Accumulated Provision for Property Insurance account are prudent and reasonable.

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ISSUE 3: Should this docket be closed?

RECOMMENDATION: Yes. If no substantially affected person timely files a protest to the Commission's proposed agency action then this docket should be closed. (BREMAN, ERSTLING)

STAFF ANALYSIS: This docket should be closed if no substantially affected person timely files a protest to the Commission's proposed agency action.