

FLORIDA PUBLIC SERVICE COMMISSION  
Capital Circle Office Center • 2540 Shumard Oak Boulevard  
Tallahassee, Florida 32399-0850

MEMORANDUM

September 26, 1996

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

FROM: DIVISION OF APPEALS (BELLAR) *RB bx DS*  
DIVISION OF RESEARCH & REGULATORY REVIEW (KEWITT) *CA om*  
DIVISION OF AUDITING & FINANCIAL ANALYSIS (REVELL) *JS*  
DIVISION OF ELECTRIC & GAS (R. BASS) *Feb* *RT*

RE: DOCKET NO. ~~96335-BI~~ - PROPOSED REVISIONS TO RULE 25-6.0141, F.A.C., ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION (AFUDC)

AGENDA: 10/8/96 - REGULAR AGENDA - RULE ADOPTION - PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF (SEE ISSUE 1)

SPECIAL INSTRUCTIONS: I:\PSC\AFA\WP\5

CASE BACKGROUND

As a result of a process which included meeting with the companies and other parties on several occasions, Staff recommended certain amendments to Rule 25-6.0141, Allowance for Funds Used During Construction (AFUDC). The purpose of the amendments is to increase the threshold of project qualification in order to limit AFUDC accrual treatment to projects with a significant financial impact on the company.

The original proposed rule revision was discussed at the February 6, 1996 Agenda Conference. On the basis of company comments and questions raised by several Commissioners, this matter was deferred to a later agenda in order that these concerns and questions could be addressed. Staff made revisions to the rule in the form of a Primary and Alternate version of the rule.

This matter was again discussed at the June 11 Agenda Conference. After discussions with representatives of Gulf Power Company, Tampa Electric Company and Florida Power & Light Company, the Commission proposed the adoption of the Primary version of the rule. The companies were given the opportunity to respond with written comments. Florida Power & Light Company and Florida Power Corporation again verbally supported the proposed rule revision,

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while Tampa Electric Company and Gulf Power Company filed written comments. Both Companies continue to believe that a fixed dollar floor rather than a percentage of rate base method is the only appropriate method for the accrual of AFUDC.

No Company requested a hearing, but Tampa Electric Company and Gulf Power Company requested to address the Commission at the Agenda Conference prior to formal adoption of the rule. Neither company responded with any significantly different arguments against the adoption of the percentage method for calculating AFUDC than were previously presented.

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**DISCUSSION OF ISSUES**

**ISSUE 1:** Should Gulf Power Company's and Tampa Electric Company's requests to speak on this rule prior to adoption be granted?

**RECOMMENDATION:** No.

**STAFF ANALYSIS:** Gulf Power Company and Tampa Electric Company filed written comments and have requested to speak at Agenda in lieu of a hearing. Staff believes this is contrary to Commission procedures and Rule 25-22.017, F.A.C. However, the rule would allow Commissioners to ask questions of other persons as part of these deliberations.

**ISSUE 2:** Should the Commission adopt the proposed amendments to Rule 25-6.0141, F.A.C. included in the attachment?

**RECOMMENDATION:** Yes. The Commission should adopt the amendments to Rule 25-6.0141 included in the attachment. At the suggestion of the Joint Administrative Procedures Committee, Staff is proposing a minor modification to Section (1)(g).

**STAFF ANALYSIS:** Staff has reviewed the comments received from Tampa Electric Company and Gulf Power Company and both companies presented the same arguments in their written comments as they did at the Agenda Conference on June 11, 1996.

Both companies urge the Commission to reject the adoption of this rule revision which uses a percentage of rate base to calculate the amount of CWIP eligible for AFUDC. The companies believe that the adoption of the method will result in a disparity in accounting treatment among the companies.

Several points in Gulf Power's response, dated July 25, 1996 do need to be addressed however:

(1) Gulf makes the statement that "Gulf has not uncovered any evidence to support the notion that other public service commissions are "waiting in the wings" in preparation to act in a fashion similar to the proposed changes..."

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Staff can find no suggestion in the recommendation dated April 18, 1996 and discussed at the June 11, 1996 Agenda Conference, or in the transcript of the conference, that it stated that any other regulatory bodies were ready to propose similar changes to their AFUDC rules. Staff replied that when there was in fact full competition, and everyone is following generally accepted accounting principles, it is unlikely that anyone will be using a flat amount upon which to accrue AFUDC.

(2) In its response, Gulf states that Staff failed to take into account potential competitive disparity between utilities or other generators of electricity. Gulf's statement said "Staff's perception on this issue is confusing since all four of the major investor owned electric utilities stated competitive concerns as the basis for their positions". This phrasing by Gulf Power needs clarification.

Company concerns about competition were considered in development of the rule changes. One of the questions in a survey sent to all five IOU's in September 1995, asked if the proposed rule revisions would impact the company's ability to compete in the market. Florida Power & Light Company stated that it would help them compete in the future. Florida Power Corporation stated that there wouldn't be any significant effect on the Company by making these changes. In its second response to our request for comments, FPC stated that it might in fact be at a competitive disadvantage if a specific dollar threshold was adopted. FPL and FPC support the attached rule.

Gulf Power and Tampa Electric maintain that there should be a dollar threshold, rather than a percentage threshold. The dollar amounts preferred by Gulf and Tampa Electric of \$10,000,000 and \$15,000,000, respectively, are approximately equal to 1/2 of 1% of rate base for these companies, which is the percentage Staff is recommending for adoption for all companies. In addition, Tampa Electric's first response in comments dated October 20, 1995, on the ability to compete with other companies stated, "Tampa Electric does not expect the proposed rule revisions to have any significant effect on the ability of our company to compete against other companies in the market." Also on October 20, 1995, Gulf Power also stated that the rule was not expected to have any significant impact on its ability to compete. The rule revision at that time proposed a threshold of 1% of rate base, twice as high as the present proposal. Since that time, both Tampa Electric Company and Gulf Power Company have changed positions on this point, but clearly it was not an overriding concern when this rule was first proposed by staff over a year ago.

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Staff believes that the competitive concerns are alleviated by the waiver provision found in Section (f) of the rule. In addition, a utility may unilaterally choose not to accrue AFUDC and not include the CWIP in rate base.

This rule revision was sent to the Joint Administrative Procedures Committee for review. The staff attorney that reviewed the revisions believes the phrase "in the best interests of the ratepayers" in paragraph (1)(g) is too vague. This phrase has been changed to read "...the Commission, upon its own motion, may determine that the potential impact on rates may require the exclusion of an amount of CWIP from a utility's rate base...". This language change more directly states that the Commission may make a determination based on whether and how rates are affected, rather than the somewhat ambiguous phrase of "best interests of the ratepayers".

Staff believes that neither Gulf Power Company nor Tampa Electric Company has presented any new arguments in their responses. Staff, therefore, recommends that the version of the rule revision which the Commission proposed on June 11, 1996 should be adopted with the minor modification noted previously.

ISSUE 3: Should this docket be closed?

RECOMMENDATION: Yes.

**25-6.0141 Allowance For Funds Used During Construction.**

(1) Construction work in progress (CWIP) or nuclear fuel in process (NFIP) not under a lease agreement that is not included in rate base may accrue allowance for funds used during construction (AFUDC), under the following conditions:

(a) Eligible projects. The following projects may be included in CWIP or NFIP and accrue AFUDC:

1. Projects that involve gross additions to plant in excess of 0.5 percent of the sum of the total balance in Account 101 - Electric Plant in Service, and Account 106, Completed Construction not Classified, at the time the project commences \$25,000 and
  - a. are expected to be completed in excess of one year after commencement of construction, or
  - b. were originally expected to be completed in one year or less and are suspended for six months or more, or are not ready for service after one year.

(b) Ineligible projects. The following projects may be included in CWIP or NFIP, but may not accrue AFUDC:

1. Projects, or portions thereof, that do not exceed the level of CWIP or NFIP included in rate base in the utility's company's last rate case.
2. Projects where gross additions to plant are less than 0.5 percent of the sum of the total balance in Account 101 - Electric Plant in Service, and Account 106 - Completed Construction not Classified, at the time the project commences \$25,000 or less.
3. Projects expected to be completed in less than one year after commencement of construction.
4. Property that has been classified as Property Held for Future Use.

(c) Unless otherwise authorized by the Commission, the following projects may not be included in CWIP or NFIP, nor accrue AFUDC:

1. Projects that are reimbursable by another party.
2. Projects that have been cancelled.
3. Purchases of assets which are ready for service when acquired.
4. Portions of projects providing service during the construction period.

(d) Other conditions. Accrual of AFUDC is subject to the following conditions:

1. Accrual of AFUDC is not to be reversed when a project originally expected to be completed in

- excess of one year is completed in one year or less;
2. AFUDC may not be accrued retroactively if a project expected to be completed in one year or less is subsequently suspended for six months, or is not ready for service after one year;
  3. When a project is completed and ready for service, it shall be immediately transferred to the appropriate plant account(s) or Account 106, Completed Construction Not Classified, and may no longer accrue AFUDC;
  4. Where a work order covers the construction of more than one property unit, the AFUDC accrual shall cease on the costs related to each unit when that unit reaches an in-service status;
  5. When the construction activities for an ongoing project are expected to be suspended for a period exceeding six (6) months, the utility shall notify the Commission of the suspension and the reason(s) for the suspension, and shall submit a proposed accounting treatment for the suspended project; and
  6. When the construction activities for a suspended project are resumed, the previously accumulated costs of the project may not accrue AFUDC if such costs have been included in rate base for ratemaking purposes. However, the accrual of AFUDC may be resumed when the previously accumulated costs are no longer included in rate base for ratemaking purposes.

(e) Subaccounts. Account 107, Construction Work in Progress, and Account 120.1, Nuclear Fuel in Process of Refinement, Conversion, Enrichment and Fabrication, shall be subdivided so as to segregate the cost of construction projects that are eligible for AFUDC from the cost of construction projects that are ineligible for AFUDC.

(f) Prior to the commencement of construction on a project, a utility may file a petition to seek approval to include an individual project in rate base that would otherwise qualify for AFUDC treatment per Section (1)(a).

(g) On a prospective basis, the Commission, upon its own motion, may determine that the potential impact on rates may require the exclusion of an amount of CWIP from a utility's rate base that does not qualify for AFUDC treatment per Section (1)(a) and to allow the utility to accrue AFUDC on that excluded amount.

(2) The applicable AFUDC rate shall be determined as follows:

(a) The most recent 13-month average embedded cost of capital, except as noted below, shall be derived using all sources

of capital and adjusted using adjustments consistent with those used by the Commission in the utility's Company's last rate case.

(b) The cost rates for the components in the capital structure shall be the midpoint of the last allowed return on common equity, the most recent 13-month average cost of short term debt and customer deposits and a zero cost rate for deferred taxes and all investment tax credits. The cost of long term debt and preferred stock shall be based on end of period cost. The annual percentage rate shall be calculated to two decimal places.

~~(c) The treatment by the Commission of all investment tax credits at a zero cost rate shall be contingent upon a ruling from the Internal Revenue Service that such treatment will not, for companies elected to be treated under s. 46(f) (2) of the Internal Revenue Code, result in the forfeiture of the tax credits. Pending receipt of such a ruling, each utility shall continue to use the weighted overall cost of capital calculated in a manner consistent with the final IRS Regulation Section 1.46-6 published May 22, 1986, as the cost of the utility's 4% and 10% investment tax credits.~~

~~(d) Any such ruling request must be submitted to the Commission by December 15, 1987. The AFUDC cost rate for the investment tax credit for any company which fails to submit its own letter ruling request to the IRS shall be governed by the first letter ruling issued by the IRS in response to a request submitted pursuant to subsection 2(c) of this rule.~~

(3) Discounted monthly AFUDC rate. A discounted monthly AFUDC rate, calculated to six decimal places, shall be employed to insure that the annual AFUDC charged does not exceed authorized levels.

(a) The formula used to discount the annual AFUDC rate to reflect monthly compounding is as follows:

$$M = [(1 + \frac{A}{100})^{1/12} - 1] \times 100$$

Where:

M = discounted monthly AFUDC rate

A = Annual AFUDC rate

(b) The monthly AFUDC rate, carried out to six decimal places, shall be applied to the average monthly balance of eligible CWIP and NFIP that is not included in rate base.

(4) The following schedules shall be filed with each petition for a change in AFUDC rate:

(a) Schedule A. A schedule showing the capital structure, cost rates and weighted average cost of capital that are the basis for the AFUDC rate in subsection (2).

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(b) Schedule B. A schedule showing capital structure adjustments including the unadjusted capital structure, reconciling adjustments and adjusted capital structure that are the basis for the AFUDC rate in subsection (2).

(c) Schedule C. A schedule showing the calculation of the monthly AFUDC rate using the methodology set out in this Rule.

(5) No utility may charge or change its AFUDC rate without prior Commission approval. The new AFUDC rate shall be effective the month following the end of the 12-month period used to establish that rate and may not be retroactively applied to a previous fiscal year unless authorized by the Commission.

(6) Each utility charging AFUDC shall include in its ~~June and December Earnings Rate-of-Return Surveillance Reports~~ to the Commission Schedules A and B identified in subsection (4) of this Rule, as well as disclosure of the AFUDC rate it is currently charging.

(7) The Commission may, on its own motion, initiate a proceeding to revise a utility's AFUDC rate.

(8) Each utility shall include in its Forecasted Surveillance Report a schedule of individual projects that commence during that forecasted period and that are estimated to equal or exceed a gross cost of \$10,000,000. The schedule shall include the following minimum information:

(a) Description of the project.

(b) Estimated total cost of the project.

(c) Estimated construction commencement date.

(d) Estimated in-service date.

(9)-(8) The provisions of this rule are effective January 1, 1996 and shall be implemented by all electric utilities no later than January 1, 1999, or the utility's next rate proceeding, whichever occurs first. Paragraphs (a) and (b) of subsection (i) shall not be effective for any utility until it implements final rates in a general rate case initiated after the effective date of this Rule. The foregoing notwithstanding, those provisions will become effective for all utilities no later than January 1, 1989.

Specific Authority: 350.127(2), 366.05(1), P.S.

Law Implemented: 350.115, 366.04(2)(a), 366.06(1), P.S.

History: New 8/11/86, Amended 11/13/86, 12/7/87.