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DECEMBER 4,1997

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

FROM: DIVISION OF ELECTRIC & GAS (HARLOW, BOHRMANN)
DIVISION OF LEGAL SERVICES (PAUGH)

RE: DOCKET NO. 970001-EI - FUEL AND PURCHASED POWER COST RECOVERY CLAUSE AND GENERATING PERFORMANCE INCENTIVE FACTOR

AGENDA: DECEMBER 16, 1997 - REGULAR AGENDA - POST HEARING DECISION - PARTICIPATION IS LIMITED TO COMMISSIONERS AND STAFF

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: S:\PSC\EAG\WP\970001.RCM

CASE BACKGROUND

The Federal Energy Regulatory Commission's (FERC) Order 888, issued April 24, 1996, requires investor owned electric utilities to unbundle transmission and ancillary charges from economy energy sales. The primary purpose of FERC's unbundling requirement is to remove or reduce the competitive advantage that a transmission owner has in favor of its own power sales. Florida Power and Light Company (FPL), Florida Power Corporation (FPC), Gulf Power Company (Gulf) and Tampa Electric Company (TECO) filed amendments to their existing economy coordination tariffs on January 1, 1997, at FERC. FERC has not yet ruled on these tariffs. Each of the utilities implemented the tariffs on an interim basis, subject to refund, as of January 1, 1997. Prior to FERC Order 888, the utilities used a consistent pricing and cost recovery methodology for broker sales. However, each of the four utilities has implemented a different method of pricing and/or cost recovery for broker transactions subsequent to the FERC Order.

Staff raised four issues concerning the pricing and cost recovery of broker sales at the Prehearing Conference in this Docket on February 5, 1997. The issues were deferred pursuant to Order No. PSC-97-0180-PHO-EI to the August 14-15, 1997, hearing in this Docket. Staff raised an additional issue concerning the

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appropriateness of the 20 percent stockholder incentive in staff's preliminary list of issues and positions on July 22, 1997. The stockholder incentive issue was withdrawn at the hearing. The Florida Industrial Power Users Group (FIPUG) and the Office of Public Council (OPC) were granted leave to intervene in this proceeding. FPL, FPC, Gulf, TECO, FIPUG and OPC participated in the hearing and filed post hearing briefs.

DISCUSSION OF ISSUES

This recommendation is limited to issues 9 through 12 in this docket. Issues 1 through 8 and 14 through 24A were decided in Order No. PSC-97-1045-FOF-EI, issued September 5, 1997. Issue 13 was withdrawn during the August 14-15, 1997, hearing.

ISSUE 9: How should the transmission costs be accounted for when determining the transaction price of an economy, Schedule C, broker transaction between two directly interconnected utilities?

RECOMMENDATION: The transaction price should be based on the incremental system production cost, just as before FERC Order 888. Any transmission charge required by FERC Order 888 should not influence the gain on a broker sale. As outlined in Gulf's proposal, any FERC required transmission costs should be added after the broker has matched a buyer and seller. This method preserves the intent of the broker system. [HARLOW, BOHRMANN]

POSITION OF PARTIES

FPL: The broker incorporates these costs by adjusting the buyer's costs where there is a separate additional charge just like is done for transactions between non-directly interconnected utilities.

FPC: For economy sales made pursuant to agreements executed prior to July 9, 1996, FERC requires the transaction cost to be unbundled into generation and transmission components, with no increase in the total transaction cost. For sales made pursuant to new agreements executed after that date, a separate transmission charge should be added to the transaction price.

GULF: The selling utility's transmission cost should be added to the production cost component of an economy sale.

TECO: The transmission charges should be accounted for from the seller's share of the transaction savings as contemplated in FERC Orders Nos. 888 and 888-A for split-the-savings transactions.

FIPUG: The buyer's price should be adjusted for transmission if there is a separate charge for it. If there is no separate charge, there should be no adjustment.

OPC: The relevant purpose of FERC Order 888 is to level the economic playing field so that a transmission owner has no undue competitive advantage in favor of its own power sales. The main purpose of the broker transactions is to assure that the least

expensive fuel available is burned at any given time. Unfortunately, none of the alternatives advanced by the parties attain both goals in all circumstances. The Citizens recommend the Commission or its staff continue to examine the issue. In the meantime, however, the Citizens believe the best alternative is that submitted by FP&L: (1) the transmission charge (whether wheeling or "self-wheeling") should be billed separately to the buyer; (2) the wheeling charge should be subtracted from the buyers decremental fuel cost; and (3) that remainder should be averaged with the seller's incremental fuel costs to calculate the transaction price for an economy, Schedule C, broker transaction.

STAFF ANALYSIS: The Florida Energy Broker Network was designed to replicate an economic dispatch for hourly non-firm economy sales. (Tr. 79) Prior to FERC Order 888, buy and sell quotes were based on incremental system costs and any applicable variable O&M costs. (Tr. 79, 267) Transmission costs were not included in broker quotes.(Tr. 79) Matches were made on the broker system by maximizing savings between the buyer's decremental production cost and the seller's incremental production cost. A transaction price was then determined by averaging the buyer's and seller's quotes. (Tr. 267) For example, the transaction price for a sale between a buyer with a quote of $30 and a seller with a quote of $20 would be $25. This resulted in maximizing the statewide savings for participants.(Tr. 79)

There is disagreement among the four utilities as to whether the FERC unbundling requirement for existing agreements allows an additional charge for transmission for broker transactions involving two adjoining utilities. FPC and TECO stated that for existing agreements, FERC will not allow an additional transmission charge to be added to the existing transaction price when a 'split-the-savings' pricing approach is used. (Tr. 90, 224) Both FPL and Gulf believe that an additional charge is allowed. FPL's witness Villar stated that FERC's position on whether an additional transmission charge can be added is unclear and will be settled through litigation before FERC.(Tr. 155)

The following table summarizes the pricing methodology proposed by each utility when there are only two utilities involved, a buyer and a seller. The proposed cost recovery methodologies are discussed in Issue 10.

	FPC	TECO	FPL	GULF
Sell Quote	$20	$20	$20	$20
Buy Quote	$30	$30	$27	$30
Transaction Price	$25	$25	$23.50	$25
Seller's Margin	$5	$5	$3.50	$5
Buyer Billed For Transmission	$0	$0	$3	$3
Buyer's Total Cost	$25	$25	$26.50	$28

Under the pricing methodologies of FPC and TECO, matches are made based on the incremental system production cost, just as before FERC Order 888. For example, the transaction price for a sale between a seller with incremental system costs of $20 and a buyer with decremental system costs of $30 would remain $25. Both FPC and TECO unbundled a transmission charge from the existing transaction price, resulting in a total cost to the buyer of $25. (Tr. 78, 281) FPC includes a separate charge for transmission for economy sales made pursuant to new agreements executed after July 9, 1996. However, FPC stated that these economy sales are not made on the broker system. (Tr. 64)

Gulf only makes economy sales as a part of Southern Company. (Tr. 192) As in FPC's and TECO's methodology, under Gulf's methodology, matches are made based on the incremental production cost. The transaction price remains $25, just as before FERC Order 888. However, the buyer is billed separately for the $3 transmission charge, resulting in a total cost for the buyer of $28. (Tr. 193)

Staff agrees with the positions of FPC, TECO and Gulf. Matches should be made based on the incremental system production cost, just as before FERC Order 888. This will maintain the original purpose of the broker to maximize statewide incremental system cost savings for participants. Consistent with Gulf's methodology, any transmission charge required by the FERC Order should not influence the matches made on the broker and the gains associated with broker sales. Staff believes this is appropriate because the transmission charge is not an incremental production

cost associated with the sale, but a contribution to fixed costs. (Tr. 84)

In contrast to FPC, TECO and Gulf, under FPL's methodology the transmission charge affects the transaction price of a broker sale. FPL proposes to subtract the transmission charge from the buyer's quote before determining the transaction price. (Tr. 168) For example, if FPL were the seller with a quote of $20, the buyer's quote of $30 would be reduced by FPL's transmission charge ($3) to $27. According to FPL's witness, Villar, FPL's quote of $20 and the buyer's adjusted quote of $27 are then averaged by the broker system to obtain a transaction price of $23.50. The resulting gain is then $3.50. FPL would then bill the buyer separately for the $3 transmission charge, resulting in a total cost to the buyer of $26.50. (Tr. 129)

It appears that OPC has also adopted FPL's methodology as an interim method. Staff disagrees with FPL's pricing methodology because the transaction price should not be affected by the transmission charge, which is not an incremental cost of the sale. Staff further disagrees with FPL's pricing methodology being couched as "just like it is done for transactions between non-directly interconnected utilities." (Tr. 100-101) It is clear from the record that for non-directly interconnected utilities, a separate wheeling charge is added to the transaction price, resulting in the buyer paying the full transmission charge. (Exh. 4) For a wheeled sale, the buyer would pay a $3 wheeling fee in addition to the $25 transaction price, resulting in an effective price of $28, just as in Gulf's methodology. In contrast, FPL's pricing methodology results in a cost of $26.50 for the buyer and has the effect of splitting the transmission charge between the buyer and the seller. (Exh. 6)

FIPUG did not provide an opinion on the appropriate pricing methodology in this issue. Instead, FIPUG focused on the appropriate recovery method. This is discussed in Issue 10.

ISSUE 10: If the cost of transmission is used to determine the transaction price of an economy, Schedule C, broker transaction between two directly interconnected utilities, how should the costs of this transmission be recovered?

STAFF RECOMMENDATION: The gains from broker sales should be, to the extent possible, the same before and after FERC Order 888. Because broker sales are non-separated sales, any additional transmission revenues should be credited and separated according to the normal procedure within the fuel adjustment clause of the selling utility. For the purchaser, all actual costs should continue to be recovered through the fuel clause. The fuel clause should be adjusted to reflect the Commission's decision effective January 1, 1997, for all broker transactions. Each utility should reflect the impact of the Commission's decision in its projection testimony and filing in Docket No. 980001-EI. [HARLOW, BOHRMANN]

POSITION OF THE PARTIES

FPL: The additional revenue, if any, should be flowed through the fuel clause.

FPC: For sales under pre-existing (pre-July 1996) agreements, where there is no separately added transmission charge, appropriate jurisdictional transmission revenues should continue to be credited to the fuel clause. For sales under new agreements, where a transmission charge is added, transmission revenues should be treated as above-the-line base rate revenue, as are all other transmission revenues. For purchases, the total transaction cost, including transmission charges, should continue to be recovered through the fuel clause.

GULF: For the seller, the transmission component of the economy sale is reflected in base rates and the fuel cost component of the economy sale is credited to the customer through the fuel clause. For the buyer, the full cost of the economy purchase is recovered through the fuel clause.

TECO: The transmission charges associated with an economy sale should be treated as operating income above the line.

FIPUG: It should be treated as part of the fuel cost to the purchasing utility and part of the fuel revenue of the selling utility (to be passed through the fuel adjustment clause). Retail ratepayers are supporting the transmission system and should receive the benefit of it.

OPC: It should be treated as part of the fuel cost to the purchasing utility and as part of the fuel revenue to the selling utility (to be passed through the fuel adjustment clause).

STAFF ANALYSIS: The appropriate treatment of the costs and revenues, including transmission charges, is discussed separately for the seller and purchaser involved in a broker transaction.

A. **RECOVERY FOR THE SELLER**

Commission policy on the treatment of the costs of economy sales was established in 1977. Selling utilities were allowed to recover the fuel component of economy energy sales through the Fuel and Purchased Power Cost Recovery clause (fuel clause). The profit margin, or gain, on economy sales was included in base rates.

Order No. 12923, issued January 24, 1984, in Docket No. 830001-EU-B, removed economy energy sales profits from base rates and required that these gains be credited to the fuel clause. The Order further stated that the economy energy gains are to be divided between ratepayers and stockholders on an 80%-20% basis. Staff's recommendation is that FERC Order 888 should have no effect, to the extent possible, on these gains. Because economy sales are non-separated sales, retail ratepayers support all the investment used to make the sale. Therefore, staff recommends that additional transmission revenues should be credited through the selling utility's fuel adjustment clause.

As a result of the FERC unbundling requirement, each of the four utilities is following a different cost recovery method for economy sales. Based on a hypothetical $20 sell, $30 buy, and $3 transmission quote, the following table summarizes the utilities' methods as well as the effect of staff's recommendation on each utility:

Before 888			After 888							
All IOUs			FPC	Staff Rec	FPL	Staff Rec	Gulf	Staff Rec	TECO	Staff Rec
A	Transaction price	$25.0	$25.0	$25.0	$23.5	$23.5	$25.0	$25.0	$25.0	$25.0
B	Additional trans-mission charge	$0.0	$0.0	$0.0	$3.0	$3.0	$3.0	$3.0	$0.0	$0.0
C	Buyer's cost (A+B)	$25.0	$25.0	$25.0	$26.5	$26.5	$28.0	$28.0	$25.0	$25.0
D	Less incremental fuel cost	$20.0	$20.0	$20.0	$20.0	$20.0	$20.0	$20.0	$20.0	$20.0
E	Less credit to oper. revenue (trans. revenue)	$0.0	$0.0	$0.0	$0.0	$0.0	$3.0	$0.0	$3.0	$0.0
F	Less credit to fuel clause (trans. revenue)	$0.0	$0.75 ($0.00 retail)	$0.0	$3.0	$3.0	$0.0	$3.0	$0.0	$0.0
G	Net gain (C-D-E-F)	$5.0	$4.25 ($4.15 retail)	$5.0	$3.5	$3.5	$5.0	$5.0	$2.0	$5.0
H	Credit to fuel clause (.80 * G)	$4.0	$3.32 (retail)	$4.0	$2.8	$2.8	$4.0	$4.0	$1.6	$4.0
I	Below the line (.20 * G)	$1.0	$0.83	$1.0	$0.7	$0.7	$1.0	$1.0	$0.4	$1.0

Prior to FERC Order 888, the transaction price on the example sale above would be $25, with a $5 gain for the seller. The gain would be split 80%-20% between ratepayers ($4) and stockholders ($1). (See rows H and I in Table above) As a result of the FERC Order, the utilities proposed four different cost recovery methods. This ultimately affects the gains from economy sales and therefore the credit to the seller's ratepayers through the fuel clause. (Exh. 13)

Each utility has interpreted the FERC order to best suit its needs. For example, TECO is usually a net seller and FPL is usually a net buyer on the Florida broker system. TECO proposed a methodology that results in the lowest transaction price but would increase retail operating revenue enuring to stockholders and

reduce the fuel credit to retail customers. FPL proposed a methodology that reduces the total cost of the transaction by splitting the transmission charge.

Staff's recommendation attempts to maintain the level of gains the same as before FERC Order 888. This will hold ratepayers harmless to the FERC Order, which has imposed no additional costs. (Tr. 84) Staff defines the gain on each sale as the total revenue net of incremental system costs and any transmission charge which is separately billed to the buyer. Under staff's proposal, the gain for FPC, Gulf and TECO is $5 (See row G in Table above). This is split 80%-20% between ratepayers ($4) and shareholders ($1), the same as before FERC Order 888. Staff disagrees with the cost recovery method proposed by FPC because of the separations method applied. Staff also disagrees with TECO's cost recovery method because TECO is crediting the portion of the original gain the company has 'earmarked' for transmission to operating revenues. These issues will be discussed further below.

As displayed in the table above, staff's recommendation does not result in the same gain for FPL as before FERC Order 888. FPL is the only utility for which the transaction price changed subsequent to the FERC Order. Maintaining the same gain for FPL would require imputing revenues and recreating hourly broker matches. However, staff believes that to the extent possible, stockholders and ratepayers should not be harmed by the FERC Order. Staff's recommendation for FPL is consistent with FPL's position.

Credit of Transmission Revenues:

Economy sales have traditionally been treated as non-separated sales by this Commission. In Order No. PSC-97-0262-FOF-EI, issued March 11, 1997, in Docket No. 970001-EI, the Commission reconfirmed its policy of crediting all revenues resulting from non-separated sales through the fuel and capacity cost recovery clauses. The Order states:

> Because non-separated sales are sporadic, a utility does not commit long-term capacity to the wholesale customer. Non-separable sales are not assigned cost responsibility through a separation process, therefore the retail ratepayer supports all of the investment that is used to make the sale. In exchange for supporting the investment, the retail ratepayer receives all of the revenues, both fuel and non-fuel, that the sale generates through a credit in the fuel and capacity cost recovery

> clauses. For Broker sales, the utility's shareholders receive 20 percent of the profit associated with the sale. (Pg. 2)

There is no compelling reason to deviate from this Commission policy. The transmission charge required by the FERC Order is a contribution to fixed transmission costs, not an incremental cost associated with the sale. (Tr. 84) Since fixed transmission expenses are included in retail base rates and fully supported by retail customers for non-separated sales, retail ratepayers should benefit fully from the transmission revenues generated by economy sales. Staff disagrees with TECO's witness, Branick, that crediting these revenues to operating revenues will allow retail customers to benefit fully from transmission related revenues. (Tr. 270) If this revenue is credited to operating revenues, as suggested by TECO and Gulf, retail ratepayers will only benefit by a base rate type of proceeding, such as a rate case or an overearning stipulation, which is not applicable to all utilities. (Tr. 210) In contrast, if transmission revenues are credited to the fuel clause, as suggested by FPL, FIPUG, OPC and FPC, retail ratepayers will be fully compensated for their investment in the facilities used to make the sale. FPC also stated that to the extent the company collects additional revenues for transmission, the additional revenue should be credited to operating revenues. However, under FPC's methodology, additional transmission revenue is only collected for economy sales made outside the broker system.(Tr. 68)

Further, transmission revenues from economy sales between directly interconnected utilities were not anticipated as a credit to operating revenues when base rates were set. It follows that base rates are higher than they would have otherwise been for the seller.(Tr. 147-148) Crediting operating revenues with these transmission revenues, without a downward adjustment to base rates would result in a windfall for the seller.

Finally, staff does not find Gulf's and TECO's argument that FERC requires non-firm transmission revenues to be treated as a 'revenue credit' a compelling reason to credit the seller's transmission revenues from broker sales to operating revenues. According to TECO's witness Kordecki, in Order .888A, FERC "explained that revenue from non-firm transmission services should continue to be reflected as a revenue credit in the derivation of firm transmission tariffs." (Tr. 235) Gulf's witness, Howell, uses this FERC requirement to argue that if these revenues were credited to the fuel clause, the utility would be required to credit the revenue twice, resulting in an underrecovery for the selling utility. No additional supporting evidence beyond the testimony of

witnesses Kordecki and Howell was supplied by Gulf or TECO explaining this FERC requirement. It also appears that the testimony of TECO's witness Branick conflicts with the testimony provided by TECO's witness Kordecki. Branick states that TECO's treatment of these transmission revenues is consistent with this Commission's policy of crediting third party transmission revenues to operating revenues for retail ratemaking purposes, rather than crediting to wholesale customers in the establishment of firm transmission rates. (Tr. 270) It is also interesting to note that FPL and FPC did not express concern about this issue.

Separation Factor for Transmission Revenues:

Currently, both the fuel costs and gain from economy sales are separated between retail and wholesale customers based on energy. This separation occurs automatically for all revenues and expenses flowing through the fuel clause. (Tr. 84) For simplicity, all parties in the docket, except FPC, ignored jurisdictional separations factors in their example transactions. (Tr. 214)

FPC believes that the seller's transmission revenues should be separated by a transmission-related separations factor before any gains on economy sales are calculated. For FPC, "Jurisdictional responsibility for retail customers is approximately 95% for generation-related and 75% for transmission-related," expenses. (Tr. 60) According to FPC's calculations, applying the transmission-related separations factor to this revenue results in a reduced credit to retail customers through the fuel clause for sales under existing economy agreements. (Tr. 87)

Staff does not agree with FPC. The transmission-related separations factor FPC is referring to is the result of the separations, or cost of service, study applied in the establishment of base rates. This separation factor allocates a portion of transmission costs to separated wholesale sales. As noted above, economy sales are non-separated sales. In a sense, FPC is asking that these non-separated sales be treated as separated sales. Staff sees no compelling reason for applying a base rate separations factor to non-separated sales. The Commission has clearly stated that revenues from non-separated sales should be credited to retail customers to compensate them for supporting the investment used in making these sales.

B. RECOVERY FOR THE PURCHASER

All costs for economy purchases are currently recovered through the fuel clause for the purchaser. (Tr. 92) There is agreement among all the parties participating in the docket that

the full cost of economy purchases between directly interconnected utilities, including any new transmission charges resulting from the FERC Order, should continue to be recovered through the fuel clause.

Staff agrees that the total cost of an economy purchase should be recovered through the fuel clause. The purchaser of economy energy has a choice between purchasing or generating the power. If the purchaser were to generate the power, the associated incremental system costs would be recovered through the fuel clause. The full costs of an economy purchase should be recovered in the same manner to avoid false incentives in favor of generation or purchase alternatives with relatively low transmission charges. If the transmission charge is recovered through base rates rather than the fuel clause, there is no guarantee that the purchaser will choose the least cost alternative. (Tr. 87)

C. EFFECTIVE DATE

The fuel clause should be adjusted to reflect the Commission's decision effective January 1, 1997, for all broker transactions. This is the date the utilities began pricing broker transactions according to their FERC filings. Each utility should reflect the impact of the Commission's decision in its projection testimony and filing in Docket No. 980001-EI.

ISSUE 11: How should the transmission costs be accounted for when determining the transaction price of an economy, Schedule C, broker transaction that requires wheeling between two non-directly interconnected utilities?

STAFF RECOMMENDATION: Transmission wheeling costs should continue to be added to the broker transaction price after a match is made to determine the purchaser's total price. [HARLOW, BOHRMANN]

POSITION OF THE PARTIES

FPL: FPL is proposing no change in the manner in which transmission costs are accounted for by the Broker for transactions between two non-directly interconnected utilities. In these transactions, the Broker adjusts the buyer's quote to recognize the transmission cost.

FPC: Third-party transmission costs should continue to be added to the broker transaction price to determine the purchaser's total price.

GULF: The selling utility's transmission cost and the third party's transmission wheeling cost are added to the production cost component.

TECO: The transmission cost of the third party providing wheeling service should be billed to the buyer.

FIPUG: It should be included in the buyer's costs.

OPC: The relevant purpose of FERC Order 888 is to level the economic playing field so that a transmission owner has no undue competitive advantage in favor of its own power sales. The main purpose of the broker transactions is to assure that the least expensive fuel available is burned at any given time. Unfortunately, none of the alternatives advanced by the parties attain both goals in all circumstances. The Citizens recommend the Commission or its staff continue to examine the issue. In the meantime, however, the Citizens believe the best alternative is that submitted by FP&L: (1) the transmission charge (whether wheeling or "self-wheeling") should be billed separately to the buyer; (2) the wheeling charge should be subtracted from the buyers decremental fuel cost; and (3) that remainder should be averaged with the seller's incremental fuel costs to calculate the transaction price for an economy, Schedule C, broker transaction.

STAFF ANALYSIS: This issue addresses broker sales between a buyer and seller which must be wheeled by a third party. The seller's transmission charge was addressed in issue 9. This issue will discuss how the wheeling charge of the third party affects the broker price.

The FERC unbundling requirement has not affected the pricing methodology for wheeled sales on the broker system. (Tr. 67) The broker match for a wheeled sale is still made based on maximizing incremental system cost savings. (Tr. 91) The wheeling fee is then added to the buyer's cost and billed separately to the buyer. (Tr. 71) Staff believes this is appropriate and should not change due to FERC's requirement that the seller unbundle transmission costs. FPC, TECO, Gulf and FIPUG share this position.

OPC appears to adopt the pricing methodology proposed by FPL for sales between directly interconnected utilities as an interim methodology for wheeled sales. Staff disagrees that FPL's pricing methodology is "just like it is done for transactions between non-directly interconnected utilities." (Tr. 100-101) It is clear from the record that for non-directly interconnected utilities, a separate wheeling charge is added to the transaction price, resulting in the buyer paying the full transmission charge. (Exh. 4) For a wheeled sale, the buyer would pay a $3 wheeling fee in addition to the $25 transaction price, resulting in an effective price of $28.

ISSUE 12: If the cost of transmission is used to determine the transaction price of an economy, Schedule C, broker transaction between two non-directly interconnected utilities, how should the costs of this transaction be recovered?

PRIMARY STAFF RECOMMENDATION: Third party wheeling revenues should continue to be treated as a credit to operating revenues for the wheeling utility. Wheeling costs should continue to be recovered through the fuel clause for the purchaser. [HARLOW]

ALTERNATIVE STAFF RECOMMENDATION: Third party wheeling revenues should be credited to the fuel clause of the wheeling utility. In addition, the Commission should commence a proceeding to remove wheeling revenues' concomitant effect upon each utility's base rates and credit all future wheeling revenue for each type of non-separated wholesale sale through the wheeling utility's fuel cost recovery clause. [BOHRMANN]

POSITION OF THE PARTIES

FPL: FPL is proposing no change in the current regulatory treatment of these costs. Transmission costs paid to intervening utilities are part of the total cost of Schedule C transactions and should continue to be recovered through the Fuel Clause.

FPC: The total transaction cost (including the seller's and any third party's transmission costs) paid by the purchaser should continue to be recovered through the fuel clause. Transmission revenues received by the third-party utility should continue to be credited as an above-the-line base rate revenue.

GULF: The seller's transmission component of the economy sale and the third party's transmission wheeling cost are reflected in base rates. The fuel cost component of the transaction is credited to the customer through the fuel clause. The buyer recovers the full cost of the economy purchase through the fuel clause.

TECO: The cost of third party transmission for purchases should be dealt with as part of the overall fuel cost.

FIPUG: It should be treated as part of the fuel cost to the purchasing utility and part of the fuel revenue of the selling utility (to be passed through the fuel adjustment clause). Retail ratepayers are supporting the transmission system and should receive the benefit of it.

OPC: The equities inherent in this issue are identical to those in Issue 10. Utilities charged a wheeling fee should charge it

through the fuel adjustment clause. Fundamental fairness dictates the same treatment when a transmission owner collects wheeling charges. The revenues collected for wheeling should be credited to the transmission owner's customers through the fuel adjustment clause.

PRIMARY STAFF ANALYSIS: Commission policy is consistent regarding the treatment of third party wheeling revenues. For non-broker sales, either short-term firm or non-firm, wheeling revenues are credited to operating revenues by the wheeler. (Tr. 109) Likewise, third party wheeling revenues associated with broker sales are currently credited to operating revenues by the wheeler. (Tr. 116)

Unlike transmission revenues for the seller, transmission revenues for the wheeler of an economy sale were included in the determination of base rates during the last rate case for each of the utilities. (Tr. 116) Base rates are therefore lower than they would have been if these revenue credits were not considered. Requiring that wheeling revenues be credited to the fuel clause without an upward adjustment to base rates could result in an underrecovery for the wheeling utility. Staff therefore agrees with FPL, FPC, Gulf and TECO that wheeling revenues should continue to be credited to operating revenues.

Staff disagrees with FIPUG's and OPC's position that third party wheeling revenues from broker sales should be credited to the fuel clause. Staff sees no compelling reason at this time for treating third party wheeling revenues from economy sales differently than that for other wheeled sales as a result of the FERC Order. However, if the Commission determines that the alternative staff recommendation to credit wheeling revenues from economy sales to the fuel clause is appropriate, base rates should be adjusted to prevent underrecovery by the wheeling utility. It should be noted that such a change in the treatment of wheeling revenues from broker sales as a result of this docket could have implications for the treatment of wheeling revenues from other types of sales. There is no evidence in the record concerning the appropriate treatment for wheeling revenues from other types of sales or the dollar impact in base rates if regulatory treatment is changed.

As discussed in Issue 10, staff agrees with the parties that all costs for the purchaser, including any third party wheeling fees, should continue to be recovered through the fuel clause.

ALTERNATIVE STAFF ANALYSIS: Alternative staff believes that for consistency and fairness, wheeling utilities should credit these transmission revenues to their fuel cost recovery clauses.

Prior to 1984, utilities estimated wheeling revenues and gains on economy energy sales to set base rates. These revenues were treated as other operating revenue and served to reduce revenue requirements. This approach was reasonable when utilities had base rate adjustments every few years. The mismatch between these revenues and the amount included in base rates could be corrected on a fairly regular basis. However, the volatility of economy energy transactions was recognized in 1984 and the Commission decided to remove gains on economy energy sales from base rates. Orders No. 12923 and 13092 established the policy of crediting 80 percent of the gains on such sales through the fuel cost recovery clause and allowing the utility to keep the remaining 20 percent for the utility's shareholders. If an adjustment to base rates is not made to remove wheeling revenues, alternative staff believes that the reduced likelihood of rate cases significantly decreases the ability of ratepayers to ever benefit from increased wheeling revenues unless these revenues are returned through a recovery clause.

When an economy transaction occurs between two non-directly interconnected utilities, there are at least three parties involved: the purchasing utility; the selling utility; and one or more wheeling utilities. The Commission has historically treated economy sales as non-separated sales in which the selling utility does not separate the part of its system rate base that was used to complete the sale from its retail rate base. Through their base rates, the retail ratepayers support the investment in transmission facilities used to complete broker transactions. Thus, the Commission has stated that all fuel and non-fuel revenues received by the selling utility from non-separated wholesale sales should be credited to the retail ratepayers through the fuel and capacity cost recovery clauses. The Commission has recently restated its policy for the regulatory treatment of non-separated wholesale sales in Order No. PSC-97-0262-FOF-EI. The wheeling utility's retail ratepayers also support through base rates the transmission investment used to complete the broker transaction just as ratepayers of the selling utilities do. Therefore, alternative staff believes that the retail ratepayers should receive the benefit of these wheeling revenues as a credit to the fuel cost recovery clause.

FPL, FPC, TECO, and Gulf believe that the purchasing utility should recover the cost paid to wheel power across a wheeling utility's transmission lines through the fuel cost recovery clause.

That treatment of wheeling costs is consistent with Commission policy. Since the purchasing utility has rationally determined that the total transaction is less than the cost for the utility to generate the power with its own resources, it is fair to allow concurrent recovery of the costs of that transactions to be recovered from the customers receiving the benefit.

However, these four utilities also believe that the wheeling utility should credit the revenue from such transactions to base rates.(TR 67,109,196,269-271) Alternative staff agrees with FIPUG and the Citizens that the regulatory treatment of crediting wheeling revenues by the wheeling utility to base rates is not a fair application of Commission policy. FIPUG points out that the same transmission lines can be used for either transaction. Therefore, ratepayers are still responsible for the non-fuel costs of either transaction. Furthermore, Mr. Howell, Gulf's witness, stated there is no longer a meaningful distinction between transactions involving third party transmission costs and economy transmission costs between two directly interconnected utilities (Tr. 194). The utilities' proposal effectively allows for the immediate recovery from ratepayers of costs incurred to make the more cost effective transactions, but at best defers indefinitely benefits gained from third-party use of assets supported by their ratepayers. Alternative staff believes the Commission should not differentiate between the regulatory treatment of transmission revenues for a selling utility and transmission revenues for a wheeling utility.

TECO asserts that crediting the wheeling revenues to base rates would decrease future revenue requirements and postpone further rate adjustments. TECO further argues that its ROE sharing mechanism acts as an instant ratemaking mechanism in that each dollar credited to above the line operating revenue increases dollar for dollar the potential for revenue sharing and refunds (Tr. 269-271). However, as stated by the Citizens, "the potential for revenue sharing and refunds" does not occur until specified earnings levels are surpassed. Crediting wheeling revenues through the fuel cost recovery clause provides for full and immediate payment to the ratepayers for the proportionate benefit derived as the wheeling utility. Alternative staff believes this immediate benefit is far superior to the uncertainty of a refund at some future point.

Finally, TECO and Gulf assert that FERC Orders 888 and 888A require that revenue from non-firm transactions be reflected as a revenue credit in setting firm transmission rates under FERC's jurisdiction (Tr. 222-223). They maintain that under those orders, firm rates are reset annually to reflect the credit from

transmission revenues associated with non-firm transactions, and that crediting the same revenue through the fuel cost recovery clause would result in a "double-dipping" situation for the selling utility (Tr. 199-200, 205-206). Therefore, TECO and Gulf Power believe that wheeling revenues should be reflected as a credit to base rates on their respective earnings surveillance reports to the Commission.

Alternative staff agrees with FIPUG and the Citizens that the regulatory treatment of revenues derived from the Florida Broker System is a matter within this Commission's jurisdiction, not FERC's. Moreover, this Commission's responsibilities lie with protecting the utility's retail ratepayers, not the utility's wholesale customers. Also, alternative staff agrees with the Citizens that the selling utility would encounter a double-dipping situation whether the Commission credits the revenues to base rates or the fuel cost recovery clause. Neither TECO nor Gulf has raised any concerns about double dipping when revenues are credited to base rates.

In summary, alternative staff believes that recovering wheeling charges by the purchasing utility through the fuel cost recovery clause and crediting wheeling revenues by the wheeling utility to base rates is not an appropriate application of Commission policy. Also, alternative staff believes that the Commission should adopt a consistent regulatory treatment of transmission revenues received from the selling utility and the wheeling utility. Finally, alternative staff recommends that the Commission commence a proceeding to remove the effect upon each utility's base rates and credit all future wheeling revenue for each type of non-separated wholesale sales through the wheeling utility's fuel cost recovery clause.

ISSUE 25: Should this docket be closed?

RECOMMENDATION: No. This is an ongoing docket.

STAFF ANALYSIS: This is an ongoing docket. It should remain open to conduct regularly scheduled audits and other matters, as necessary.