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RECORDS AND REPORTING

State of Florida

Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: JULY 9, 1998

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

FROM: DIVISION OF ELECTRIC AND GAS (TRAPP, KUMMER, DRAPER)
DIVISION OF AUDITING AND FINANCIAL ANALYSIS (REVELL)
DIVISION OF LEGAL SERVICES (CRUZ-BUSTILLO)

RE: DOCKET NO. 980706-EI - PETITION FOR APPROVAL OF COMMERCIAL/INDUSTRIAL SERVICE RIDER TARIFF BY TAMPA ELECTRIC COMPANY

AGENDA: 07/21/98 - REGULAR AGENDA - TARIFF FILING - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: 60-DAY SUSPENSION DATE: AUGUST 1, 1998

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\EAG\WP\980706.RCM

CASE BACKGROUND

On August 24, 1995, Tampa Electric Company (TECO) filed a proposed Commercial/Industrial Service Rider (CISR) tariff in Docket No. 951002-EI. A hearing was scheduled to consider TECO's petition and also a similar petition filed by Gulf Power Company (Gulf) in Docket No. 951161-EI. On December 7, 1995, TECO withdrew its petition. Gulf's petition was denied after an evidentiary hearing on March 7-8, 1996. Order No. PSC-96-0845-FOF-EI, issued July 2, 1996. On June 28, 1996, Gulf refiled a modified CISR tariff and Docket No. 960789-EI was opened. At the July 30, 1996, Agenda Conference, Gulf voluntarily withdrew its proposed tariff. On August 20, 1996, Gulf submitted two alternative example CISR tariffs and implementation plans for the Commission's consideration. The Commission approved one of the tariffs and implementation plans at the August 22 Agenda Conference. Order No. PSC-96-1219-FOF-EI, issued September 24, 1996.

On June 2, 1998, TECO petitioned for Approval of a Commercial/Industrial Service Rider tariff (CISR or Rider) and Pilot Study Implementation Plan. If approved, the proposed Rider allows TECO to negotiate a discount on the base energy and/or base demand charges with commercial/industrial customers who can show that they have viable alternatives to taking electric service from TECO (at-risk load). The effective date of the tariff is January 1, 2000. The Commission approved a stipulation entered into by TECO, the Office of Public Counsel, and the Florida Industrial Power Users Group in Order No. PSC-96-1300-S-EI, issued October 24, 1996. The stipulation represents a settlement covering TECO's base rates and rate of return for the period January 1, 1999 through December 31, 1999.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve Tampa Electric Company's Commercial Industrial Service Rider tariff and Pilot Study Implementation plan?

PRIMARY RECOMMENDATION: Yes. TECO's petition is essentially the same as Gulf's currently approved CISR tariff. (JENKINS, DRAPER)

ALTERNATIVE RECOMMENDATION: No. The Commission should deny the proposed tariff because TECO has not provided sufficient evidence to show that the general body of ratepayers will not be harmed by the proposal. At a minimum, the matter should be set for hearing to obtain the necessary information to make an informed decision on the issues. (TRAPP, KUMMER)

PRIMARY STAFF ANALYSIS:

Description of proposed tariff

The proposed tariff is available to new customers (new load) or to existing customers (retained load). Specifically, non-residential customers currently taking firm service or qualified to take firm service under rate schedules GSD, GSDT, GSLD or GSLDT qualify. New customers must have at least 1,000 kW of connected demand. For existing customers, two minimum levels of demand are required: (1) For customers whose highest demand in the past 12 months was less than 10,000 kW, the minimum qualifying load is 500 kW; (2) for customers whose highest demand in the past 12 months was greater than or equal to 10,000 kW, the minimum qualifying load is 2,000 kW. The Rider can be applicable to all, or a portion of the customer's existing or projected load.

The negotiated discount will only apply to base energy and/or base demand charges. The customer will pay all otherwise applicable adjustment clauses. To ensure that the other ratepayers are not being harmed through the adjustment clauses, TECO proposes to allocate all revenues received from CISR customers first to all applicable cost recovery clauses at the rate which the customer would have been charged in the absence of the CISR. The CISR customer will also pay the otherwise applicable customer charge and an additional $250 customer charge. The additional customer charge is intended to cover incremental CISR customer-related costs.

Customers must make a written request to TECO for service under the CISR and provide the following documentation. First, a legal attestation or affidavit stating that, but for the application of the Rider, the load would not be served by TECO. Second, documentation demonstrating that the applicant has a viable lower cost alternative to taking service from TECO. Third, an existing customer must provide TECO with the results of a recent energy audit or request that TECO conduct such audit. The audit will provide information on potential energy efficiency improvements which could reduce the customer's cost in addition to the lower CISR rate. All CISR applications will be reviewed and approved by TECO's standing committee. The standing committee is comprised of TECO's President and four Vice Presidents.

For customers meeting the eligibility criteria described above, TECO seeks approval to offer a negotiated rate with the incremental cost plus a contribution to fixed costs to serve the customer as the price floor. Incremental costs are the additional costs TECO incurs to serve the CISR load. The rate offered may also take the form of a rate guarantee for a specific time period. If TECO and the customer are able to agree on the price and other terms and conditions the customer will be required to execute a Contract Service Agreement (CSA). By signing the CSA, the customer commits to taking electric service from TECO for the negotiated term. TECO has requested that the CSA be treated as a confidential document.

In addition to the CISR tariff sheets, TECO submitted a Pilot Study Implementation Plan (implementation plan) which is attached as Attachment A. The implementation plan sets out additional conditions of the tariff, which are described below.

TECO proposes to offer the CISR to eligible customers until one of three conditions has occurred: (1) total capacity subject to all CSAs reaches 300 megawatts of connected load; (2) the company has executed 25 CSAs or; (3) 48 months have passed from the tariff's effective date. In addition, the implementation plan states that TECO will not use the CISR to shift existing load currently served by another Florida electric utility to TECO's service territory.

TECO's proposal does not require that the Commission approve each CSA. TECO proposes, however, to include in its monthly surveillance reports the difference between the revenues which would have been received under the otherwise applicable tariff rate and the CISR rate and to file quarterly reports. In addition, the Commission can fully review each executed CSA to evaluate its prudence. The implementation plan sets forth three conditions which would trigger a review of the contracts by the Commission: (1) a request by TECO for a base rate increase; (2) if the difference in revenues resulting from the CSAs causes TECO's achieved jurisdictional return on equity to exceed the top of the Company's authorized range, the Commission will review all executed CSAs which have not yet been reviewed; (3) TECO may on its motion request a prudence review subsequent to signing a CSA. TECO has not yet established a set of circumstances under which it might request a prudence review. However, nothing precludes the Commission to initiate a prudence review at any time on its own motion.

TECO states that it will have the burden of proof that the company's decision to enter into a particular CSA was made in the interest of the general body of ratepayers. TECO proposes that if the Commission finds that a particular CSA was not a prudent decision, then the revenue difference between the standard rate and the CISR rate will be imputed. If the review results in the CSA being found prudent, then TECO proposes to no longer report the revenue shortfall in its monthly surveillance reports.

<u>Analysis of proposed tariff</u>

The Commission has recognized that rate discounts can be appropriate for investor-owned electric utilities. The Commission approved in 1996 Gulf's CISR and more recently, Florida Power and Light Company's (FPL) Economic Development rate. Order No. PSC-98-0603-FOF-EI, issued April 28, 1998. TECO's proposed CISR tariff and implementation plan are essentially the same as Gulf's CISR tariff and implementation plan with only a few minor modifications as discussed below.

In TECO's proposal a Commission prudence review may be requested by the company subsequent to entering into a CSA. Gulf's CISR does not contain this provision, however, the absence of this language does not preclude Gulf from requesting a prudence review. Also, TECO's implementation plan contains language that if the review results in the CSA being found prudent, then TECO will no longer report the associated revenue shortfall on the monthly surveillance report. Gulf's implementation plan does not contain this language. Finally, Gulf's CISR is available for 12 customers or a total load of 200 megawatts, while TECO's CISR is available for 25 customers or a total load of 300 megawatts. TECO states that this increase is due to TECO being a larger company than Gulf.

Alternative staff notes that this filing is premature since the effective date of the tariff is January 1, 2000. TECO argues in its petition that time will be necessary for negotiations and agreements to be reached with customers and that such "a lead time reflects commercial reality." (Petition, page 5) Primary staff believes that TECO's petition to have a decision now to negotiate with customers is reasonable and notes that almost a year passed before Gulf signed its first CSA.

TECO classifies the proposed CISR as "experimental." In response to staff's informal questions, TECO states that the success or failure of this experiment will be determined based on the experience of CSAs offered, accepted or rejected during the four years of the pilot study period. TECO expects to report to the Commission at the end of the pilot study regarding the failure or success of the CISR and at that time recommend that the CISR end or be renewed. Primary staff believes that, given the uncertainty of the electric industry's future, limiting the tariff to a four-year pilot is reasonable.

As clarified by its response to staff's informal questions, TECO proposes to conduct specific analyses for each CISR customer to calculate the net benefits to the general body of ratepayers. TECO proposes to compare, on a cumulative net present value basis over the life of the CSA, the revenues received under the CISR to the incremental costs to serve the customer. As long as the revenues exceed the costs, TECO argues, the general body of ratepayers will benefit. TECO did not respond to staff's questions on system incremental costs, stating that <u>customer specific</u>

incremental costs are the relevant cost rather than <u>system</u> incremental costs.

Between rate cases, this proposal will not affect base rates or the various adjustment clauses since the CISR customers will pay the otherwise applicable adjustment clauses. This proposal does affect TECO's reported earnings and return on equity on the monthly surveillance report.

Whether TECO's reported earnings and return on equity on the monthly surveillance report will be higher or lower due to a CISR customer depends on whether the customer was truly at risk. If you assume that the customer would not have remained or become a TECO customer absent the lower electric rate and if revenues exceed incremental costs, then reported earnings will be higher than what they otherwise would have been. On the other hand, if you assume that the customer was not truly an "at-risk" customer, the reported earnings will be lower than they otherwise would be.

Primary staff recommends approval of TECO's petition. This tariff filing is essentially the same as Gulf's approved CISR tariff. Primary staff continues, however, to have some of the concerns that were raised during the Gulf CISR hearing. Like Gulf's CISR, TECO's CISR tariff puts the Commission in the position of having to determine whether the customer was truly at risk of leaving TECO's system or not entering TECO's service territory. This unanswerable question, however, will only arise during a prudence review. Likewise, the question of whether or not the CISR is unduly discriminatory will be reserved for a prudence review.

<u>ALTERNATIVE STAFF ANALYSIS</u>:

Alternative staff has several concerns with the proposed tariff and the fundamental concerns raised by staff in the analyses of Gulf's CISR tariff remain in TECO's proposal as well. The proposal does not define incremental cost in an objective manner and there are no criteria for determining whether a customer is truly "at-risk," or simply seeking a lower rate. Inherent in these concerns are questions about (1) the dangers of premature approval of a tariff where the potential exists for significant changes in the market prior to implementation date, (2) TECO's existing high residential and small commercial rates and the ability to use negotiated rates to potentially mask overearnings which could be used to lower rates to all customers, and (3) the ability for interruptible customers to "game the process" to obtain firm service at rates equal to or even less than they are currently paying for interruptible service.

Delayed effective date. TECO states in its petition that it requires time to negotiate contracts. Neither Gulf nor FPL sought such additional time prior to making their CISR or economic development tariffs available. The electric industry is changing daily and no one can predict what the regulatory or economic climate will be in two years. To approve a tariff today which will not even be available for 15 months seems premature at best. Approval at this point would tie the Commission's hands, no matter what might occur between now and January 1, 2000.

Earnings. In its petition, TECO was careful to point out that, by delaying the effective date of the tariff until the year 2000, there will be no issues related to the application of the stipulation (Docket No. 960409-EI, Order No. PSC-96-1300-S-EI) to this filing. It is true that delaying the effective date of the CISR tariff will cause the earnings cap and sharing mechanism not to be impacted. However, alternative staff believes the earnings issues addressed in the stipulation may exist beyond the termination of the stipulation. With TECO's deferral plan, TECO earned well within or at the top of its equity range for 1995, 1996, and 1997. TECO's earnings picture for the year 2000 is unclear. When staff asked for an estimate of earnings for the year 2000, TECO did not provide an answer, stating that "earnings projections for periods that are more than one year in the future are tentative at best due to the nature of Tampa Electric's business". (Response to Staff's Informal Questions No. 15)

Alternative staff believes that, given TECO's history of robust earnings, there is a possibility that TECO may have continued robust earnings after the year 2000. Under the CISR proposal, the benefit of higher earnings afforded by TECO's rates paid by all ratepayers would be flowed back only to a few large industrial customers who qualify for the CISR. On the other hand, if the customer was truly "at-risk" and incremental revenues exceed incremental costs, TECO's achieved earnings would be greater. However, the definition of "at-risk" is ill-defined and unquantifiable.

Gaming. A third issue concerns the ability of interruptible customers, who are currently not paying for the generating capacity serving them, to show that they are "at-risk" and to switch to firm CISR service and still pay little or nothing for the investment generating that power.

The CISR tariff appears to preclude the possibility of applying the CISR to customers currently served under TECO's interruptible rates (IS). The applicability section of the CISR tariff limits its use to customers who are currently taking firm service or are qualified to take firm service under the company's demand rate schedules. Interruptible customers normally are required to give a 5-year notice or pay a penalty when transferring to firm service without giving the full 5-year notice. So it would appear that a current interruptible customer could not take service under a CISR contract until 2003 unless he pays a penalty. However, TECO's IS tariff allows TECO to waive the 5-year notice and the penalty if two conditions are present: (1) The customer has been on the IS rate for a minimum of five years, and (2) TECO has adequate capacity available such that the transfer would not adversely impact other firm customers. Most of TECO's interruptible customers have been on an interruptible rate for the minimum time period, so the only hurdle is the capacity.

According to reports submitted by TECO pursuant to Rule 25-6.018(3), <u>Records of Interruptions and Commission Notification of Threats to Bulk Power Supply Integrity or Major Interruptions of Service</u>, prior to last month TECO's IS customers have not been interrupted since March 1993. Capacity shortfalls were resolved by buying power pursuant to the buy-through clause in the tariff. Only last month's extreme temperatures statewide resulted in actual interruptions. Once this short term crisis is over, with the addition of the Polk Unit 1, it is likely that TECO could justify transferring an interruptible customer to firm service based on capacity availability.

Alternative staff believes that interruptible customers are unlikely to switch to the CISR tariff if the negotiated rate is not at a minimum equal to what they are currently paying for IS service. Since the rate they are currently paying does not include any cost for the capacity used to serve them, it is also unlikely that any negotiated rate would include any contribution to generation costs. Therefore, customers who have enjoyed a reduced rate with the risk of interruptions would be able to transfer to firm service at the same or an even lower rate, while the rest of the ratepayers continue to support the capital intensive costs of the generation units providing that firm service. This is especially troublesome when the cost of the recent Polk Unit is approximately $2000 per kW, and is being included in TECO, surveillance reports for earnings purposes. TECO has stated that it is not its intent to apply the CISR to at-risk interruptible customers, but added that the provisions of the tariff do not preclude it from doing so.

Summary. Alternative staff is quite concerned that TECO evaded direct answers to staff's questions about the impact of this proposed tariff. In its response to staff's data request, TECO stated that "because TECO has made no estimates of the number of Customers, load and revenues which will be served under the CISR, no estimates have been made of the impact of prospective CISR Customers on achieved return on equity (ROE) in the year 2000 when this rate would go into effect". (Response to Staff's Informal Question No. 3) TECO has also established no criteria for requesting a prudence review by this Commission, although they highlight this option in their petition. (Response to Staff's Informal Question No. 6)

TECO repeatedly refers to the Commission's acceptance of Gulf's CISR and the similarity of TECO's proposal to Gulf's. What TECO does not mention is that the Commission held a full evidentiary hearing on Gulf's proposal before approval. It is not unreasonable to subject TECO to similar scrutiny on their proposal. The companies are quite different in terms of markets, operating conditions, and costs. For example, unlike Gulf, whose rates remain some of the lowest in the State, TECO has the second highest residential rates of the investor-owned utilities.

Alternative staff contends that TECO has failed to show that this proposal is cost effective and beneficial for all of TECO's ratepayers. The responses to staff's data request were vague and provided no information on key issues such as the calculation of incremental cost. On that basis, alternative staff would recommend that the proposed tariff be denied. However, alternative staff recognizes the Commission's desire to move forward in the area of economic development. As an alternative to denial, alternative staff would recommend that the matter be set for an evidentiary hearing similar to the treatment the Commission required of Gulf's CISR offering.

ISSUE 2: Should this docket be closed?

RECOMMENDATION: Yes. If the Primary Recommendation for Issue 1 is approved, this tariff should become effective on January 1, 2000. If a protest is timely filed, the protest will be resolved before the scheduled effective date. Since the tariff will not be effective until after the protest is resolved, the issue of any revenues held subject to refund is moot. If no timely protest is filed, this docket should be closed. If the Alternative Recommendation for Issue 1 is approved, this docket should be closed.

STAFF ANALYSIS: If the Primary Recommendation for Issue 1 is approved, this tariff should become effective on January 1, 2000. If a protest is timely filed, the protest will be resolved before the scheduled effective date. Since the tariff will not be effective until after the protest is resolved, the issue of any revenues held subject to refund is moot. If no timely protest is filed, this docket should be closed. If the Alternative Recommendation for Issue 1 is approved, this docket should be closed.

Tampa Electric Company
Commercial/Industrial Service Rider
Pilot Study Implementation Plan

In order to give the Florida Public Service Commission ("FPSC") and Tampa Electric Company ("the Company") the opportunity to study the impacts of a trial implementation of the Company's proposed Commercial and Industrial Service Rider ("CISR") under "real world" conditions, the following conditions would be made part of the Pilot Study Implementation Plan:

Sunset Provision: The CISR would be scheduled to be closed to further subscription by eligible customers when one of three conditions has occurred: (1) the total capacity subject to executed Contract Service Arrangements ("CSAs") reaches 300 megawatts of connected load; (2) the Company has executed twentyfive CSAs with eligible customers under the CISR; or (3) forty-eight months has elapsed from the date upon which the CISR is made effective by the FPSC (the requested made effective date is January 1, 2000). The period defined by these conditions is the Pilot Study Period. This sunset provision can be removed or revised by the Commission at any time upon good cause having been shown by the Company based on data achieved during the Pilot Study Period.

Availability: In addition to other limitations on availability contained in the CISR, the Company would limit its use of the CISR so that a CSA will not be knowingly offered to a customer in order to shift existing load currently being served by a Florida electric utility away from that utility to service by Tampa Electric under the CISR.

Approval Level: Before any CISR can be executed by the Company, it must first be reviewed and approved by a standing committee of Tampa Electric officers. Prior to execution, each CSA must be shown to produce a positive contribution to the Company's fixed costs. The incremental costs on which each CSA is evaluated shall be determined in a manner consistent with the method for identification and quantification of such costs for use in both the Company's evaluation of conservation and demand side management programs for cost effectiveness and the Company's selection of cost-effective supply side resources.

Revenue Allocation: Any revenues received by the Company pursuant to a CSA shall be allocated first to the various applicable cost-specific recovery clauses so that the revenues associated with the respective cost recovery clauses for true-up purposes will be the same with the CSA as they would be without the CSA.

Required Reports: The Company will be required to file the following information with the PSC in accordance with the PSC's procedures for handling confidential information:

- the number of CSAs requested;
- the number of CSA prices quoted;
- the number of CSA requests which were canceled by a customer prior to price quotation;
- the number of CSA offers accepted;
- the number of CSA offers rejected;
- the number of CSA offers awaiting decision by customers;
- a brief description of all CSAs executed during the quarter, including the applicable rates, charges and contract period;
- for each CSA executed during the quarter, a summary of the justification for the offering; and
- on an annual basis, the cumulative total of revenues associated with all CSAs executed by the Company.

Regulatory Review: Each executed CSA shall be fully reviewed by the PSC under conditions that protect the confidentiality of proprietary information, either upon request of the Company or when either of two Triggering Events occur. One Triggering Event would be a request by the Company for a base rate increase. Another Triggering Event would be a review by the PSC resulting from the PSC's monthly surveillance reporting system discussed more fully in the following paragraph. This PSC review is to commence immediately following the request of the Company for review or the occurrence of a Triggering Event. The period for review shall be as long as necessary for the PSC's staff to conduct all reasonable discovery needed to evaluate the prudence of the Company execution of each CSA then in existence. For this review by the PSC, the Company will continue to have the burden of proof. At the conclusion of the regulatory review, if the Company has not demonstrated to the PSC's satisfaction that the Company's decision to enter into any particular CSA under review was a prudent choice made in the interests of the Company's general body of customers, then the difference between the revenues that would have been produced by the Company's standard tariff rates and the amount of the revenues that will be produced by the CSA which were deemed imprudent will be imputed to the Company as though this amount was actually received by the Company from the CSA customer and will be taken into account by the PSC with regards to any adjustment in the Company's base rates, whether in a rate case or in an over-earnings review as noted below. If the review results in the CSA being found prudent by the PSC, then no imputation will be made during the course of the period of the CSA and that CSA will no longer be reflected in the separate Surveillance reporting mechanism described below.

Upon execution of a CSA, the PSC's monthly surveillance reporting system will be enhanced to include a requirement that the Company shall identify and report, for all executed CSAs not yet reviewed and found to be prudent by the PSC, the difference between the revenues that would have been produced by the Company's standard tariff rates and the revenues that are produced by each executed CSA. This additional information will be set forth on a separate page so that the information can be filed subject to the Commission's procedures for handling confidential and proprietary information.. If the difference so reported, when added to the Company's actual revenues, would cause the Company's achieved jurisdictional return on equity ("ROE") to exceed the top of the Company's authorized range, the review by the Commission discussed above of the as yet unreviewed CSA's will be triggered. The amount of such identified difference that would cause the Company's achieved jurisdictional ROE to exceed the top of the Company's authorized range will be held subject to refund as possible over-earnings pending completion of the Commission's review.