State of Florida

Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

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

RECEIVED-FPSC
98 NOV 19 AM 11:05
RECORDS AND REPORTING

DATE: NOVEMBER 19, 1998

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

FROM: DIVISION OF AUDITING AND FINANCIAL ANALYSIS (SLEMKEWICZ) DM
DIVISION OF ELECTRIC AND GAS (KUMMER)
DIVISION OF LEGAL SERVICES (C. KEATING) WCK RVE

RE: DOCKET NO. 981635-EI - REQUEST FOR AUTHORITY TO ESTABLISH A REGULATORY LIABILITY TO DEFER 1998 EARNINGS FOR DISPOSITION IN 1999 BY FLORIDA POWER CORPORATION

AGENDA: 12/01/98 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: ATTACHMENT IS NOT AVAILABLE

FILE NAME AND LOCATION: S:\PSC\LEG\WP\981635.RCM

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve Florida Power Corporation's (FPC) request to establish a regulatory liability to defer 1998 earnings for disposition in 1999?

RECOMMENDATION: Yes. The Commission should approve FPC's request to establish a regulatory liability to defer 1998 earnings for disposition in 1999. (SLEMKEWICZ)

STAFF ANALYSIS: Pursuant to Order No. PSC-97-0652-S-EQ, issued June 9, 1997, the Commission approved a stipulation concerning the disputed issues and the accounting treatment related to FPC's purchase of the Tiger Bay Limited Partnership (Tiger Bay) cogeneration facility and the termination of the related purchased power contracts (contracts). As a result, a regulatory asset of approximately $370 million was created related to the termination of the contracts. The regulatory asset is being amortized by using the savings realized from the early termination of the contracts. It is expected that the regulatory asset will be fully amortized by 2008 using this methodology. As part of the stipulation, however, FPC has the discretion to accelerate the amortization if and when earnings permit. FPC's ratepayers will not receive any of the savings associated with termination of the contracts until the entire Tiger Bay regulatory asset is fully amortized.

At the current time, FPC estimates that its 1998 earnings level will be sufficient to allow it to increase the amount of the Tiger Bay regulatory asset amortization. As an alternative, however, FPC states that it is considering several possible unidentified rate initiatives that might allow its ratepayers to receive the benefit of 1998 earnings sooner than if additional amortization is booked. (See Attachment) In order to accomplish this, FPC is requesting that it be allowed to defer an unspecified amount of 1998 earnings. This deferral would create a regulatory liability to be disposed of in the future. FPC has agreed that interest will be accrued on the deferred earnings.

Since no proposal for the disposition of the deferred 1998 earnings has been presented, Staff cannot presently determine whether the deferral will, in fact, result in a more immediate benefit to FPC's ratepayers. However, Staff believes it is not in the best interests of FPC's ratepayers to preclude FPC from offering any plan or proposal that might accomplish this end. Given FPC's assurances that the deferred 1998 earnings, plus interest, will be applied against the Tiger Bay regulatory asset if a proposal is either not filed or is not approved by the Commission, the Staff recommends that FPC's request be approved.

ISSUE 2: How should FPC's 1998 deferred earnings, if any, be treated in the capital structure for earnings surveillance reporting purposes?

RECOMMENDATION: For earnings surveillance reporting purposes, any 1998 deferred earnings should be included in the capital structure as a separate line item using the actual interest rate applied to the deferred earnings. (SLEMKEWICZ)

STAFF ANALYSIS: When working capital is computed, interest-bearing liabilities are excluded from the calculation. FPC's deferred earnings regulatory liability is interest bearing. In reconciling the rate base and the capital structure, the adjustment to exclude interest-bearing liabilities increases the total amount of capital. The capital structure can be increased on a pro rata basis over all sources of capital or on a specific basis over one or more sources of capital. If the reconciliation is made pro rata, the Company will earn its overall cost of capital on the balance of the deferred earnings. However, the Company would only be accruing interest at the commercial paper rate which is less than its overall cost of capital.

Staff believes that FPC's deferred earnings should be included in the capital structure as a separate line item using the actual interest rate applied to calculate the interest. This treatment is consistent with the treatment in a number of other Commission cases. In Order No. 22367 involving Quincy Telephone (Docket Nos. 890292-TL and 891237-TL), deferred revenues from 1987, 1988, 1989, and the first six months of 1990 were included in the capital structure and allowed to accrue interest at the thirty day commercial paper rate. In Order No. PSC-94-0172-FOF-TL involving Southern Bell (Docket No. 920260-TL), the accrued refund for Florida ratepayers was included in the capital structure as a specific adjustment to short-term debt and allowed to accrue interest at the thirty day commercial paper rate. In Order No. PSC-97-0135-FOF-EI involving Florida Public Utilities Company (Docket No. 961542-EI), deferred revenues associated with over earnings were included in the capital structure as a specific adjustment to short-term debt and allowed to accrue interest at the thirty day commercial paper rate. Finally, in Order No. 97-0436-FOF-EI involving Tampa Electric Company (Docket No. 950379-EI), deferred revenues were included in the capital structure as a separate line item at the commercial paper rate.

ISSUE 3: Should the Commission direct FPC to file a proposal for the disposition of the 1998 deferred earnings by a date certain?

RECOMMENDATION: Yes. The Commission should direct FPC to file a proposal for the disposition of the 1998 deferred earnings by May 1, 1999. If a proposal is not filed by that date, FPC should be directed to immediately apply any deferred 1998 earnings, plus interest, against the Tiger Bay regulatory asset. (SLEMKEWICZ)

STAFF ANALYSIS: In its request, FPC simply stated that it would file either a proposal, or a notification that no proposal would be filed, some time during 1999. Due to the unspecified nature of any proposal(s) that might be offered by FPC and the time required to adequately review any such proposals, Staff is concerned by the lack of a date certain for the filing of a proposal. Therefore, Staff recommends that FPC be directed to file any proposal that it intends to offer by May 1, 1999. This will allow FPC five months from the date of the Commission's vote on this recommendation to put any proposal together. Staff would then have sufficient time to evaluate the proposal, conduct any required discovery and prepare a recommendation for the Commission's consideration prior to the end of 1999. Staff further recommends that if a proposal is not filed by May 1, 1999, FPC be directed to immediately apply any 1998 deferred earnings, plus interest, to the Tiger Bay regulatory asset.

ISSUE 4: Should this docket be closed?

RECOMMENDATION: No. This docket should remain open pending the final disposition of any deferred 1998 earnings. (C. KEATING, SLEMKEWICZ)

STAFF ANALYSIS: This docket should remain open until a determination is made concerning the final disposition of any 1998 deferred earnings.

PUBLIC SERVICE COMMISSION

98 NOV 12 AM 10:28

AUDITING & FINANCIAL ANALYSIS

Florida Power
CORPORATION

JOHN SCARDINO, JR.
Vice President and Controller

November 12, 1998

Mr. Tim Devlin, Director
Division of Audits and Financial Analysis
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Re: Request for authority to establish a regulatory liability to defer 1998 earnings for disposition in 1999.

Dear Mr. Devlin:

As you know, under the stipulation approved by the Commission in Docket No. 970096-EQ regarding Florida Power's purchase of the Tiger Bay cogeneration facility, a regulatory asset of approximately $370 million was created based on the portion of the purchase price attributable to the termination of five high-cost purchase power agreements previously served from the facility. The Tiger Bay regulatory asset was expected to be fully amortized using the savings realized by terminating these agreements by 2008, at which time the savings would begin being passed through directly to Florida Power's customers. The stipulation also provided that Florida Power would have the discretion to accelerate the amortization of the regulatory asset through contributions from the Company's earnings when and to the extent those earnings permit, in which case customers would begin receiving the Tiger Bay savings sooner -- estimated to be as early as 2005 under the most favorable circumstances.

At this juncture, Florida Power believes 1998 system earnings may exceed the level estimated in its 1998 forecasted surveillance report submitted to the Commission last March, in large part due to the abnormal weather conditions experienced during the year. If this expectation proves to be correct, Florida Power

GENERAL OFFICE
3201 Thirty-fourth Street South • Post Office Box 14042 • St. Petersburg, Florida 33733-4042 • (727) 820-5722 • Fax: (727) 820-5985
A Florida Progress Company

Mr. Tim Devlin
Page 2

will be in a position to make an additional contribution to the amortization of the Tiger Bay regulatory asset commensurate with the amount of these additional earnings, as determined from the Company's 1998 books and records at year-end.

In addition, however, Florida Power is exploring several possible rate initiatives that have the potential of allowing customers to receive the benefit of the expected additional 1998 earnings much sooner than would be the case if these earnings were used to accelerate the amortization of the Tiger Bay regulatory asset. The difficulty with this, and the reason for this letter, is that these rate initiatives cannot be developed, submitted to the Commission and approved before the end of the year, when the Company's 1998 books and records must be closed. At that time, absent the grant of authority described below, Florida Power would use the additional 1998 earnings to write-down the Tiger Bay regulatory asset as authorized by the stipulation.

To avoid losing the opportunity to enhance the benefit of the additional 1998 earnings to its customers, Florida Power requests Staff's assistance in obtaining authority from the Commission, prior to the closing of the Company's 1998 books and records, to create a regulatory liability in the amount of the additional earnings, adjusted for income taxes.[1] Florida Power proposes that the order granting this authority would require the Company to file, in time for final Commission action in 1999, either (1) a rate proposal which utilizes the regulatory liability in a manner that provides a greater benefit to customers than accelerating the amortization of the Tiger Bay regulatory asset, or (2) a notification that such a rate proposal will not be filed. The order would further require that if such a rate proposal is either not filed by Florida Power or is filed but not approved by the Commission, the regulatory liability and accrued interest must be applied toward the Tiger Bay regulatory asset on Florida Power's 1999 books and records.

Florida Power believes the treatment of its additional 1998 earnings described above warrants Staff's support and the Commission's approval because it affords the opportunity to enhance the benefit to customers at no risk to the benefit currently available to them. In other words, this treatment will preserve the

---

[1] Consistent with the notification procedure for accelerated amortizations specified in the Tiger Bay stipulation, Florida Power will notify Staff of the amount of the regulatory liability when filing its December 1998 surveillance report.

Mr. Tim Devlin
Page 3

ability to use the additional earnings exactly as they can be used now, while, at the same time, providing an otherwise unavailable option to use the earnings in a way that may provide customers with a more immediate benefit. Your efforts to bring this request before the Commission at the earliest opportunity will be greatly appreciated.

I will be happy to meet with you and other interested Staff members at your convenience to discuss our request in greater detail and address any questions you may have. Thank you for your attention and consideration of this matter.

Very truly yours,

John Scardino Jr./sam

John Scardino, Jr.

JS/kf

cc: Mr. Jack Shreve, Public Counsel