

ORIGINAL

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into Earnings
for 1995 and 1996 of Tampa
Electric Company

DOCKET NO. 950379-EI
ORDER NO. PSC-98-1619-PHO-EI
FILED: January 14, 1999

**TAMPA ELECTRIC COMPANY'S
POST-HEARING BRIEF**

I. Procedural Background

On June 9, 1998, the Florida Public Service Commission (the "Commission") issued Proposed Agency Action Order No. PSC-98-0802-FOF-EI (the "Proposed Order"), which established the amount of deferred revenues that Tampa Electric Company ("Tampa Electric" or the "Company") would be deferring for 1996, pursuant to stipulations approved by Order No. PSC-96-0670-S-EI, issued May 20, 1996, and Order No. PSC-96-1300-S-EI, issued October 24, 1996 (the orders and stipulations collectively referred to as "the Stipulations"). Thereafter, the Florida Industrial Power Users Group ("FIPUG") and the Office of Public Counsel ("OPC") filed protests of the Proposed Order.

Tampa Electric submitted both the direct and rebuttal testimony of its witness Delaine M. Bacon, and FIPUG and OPC submitted direct testimony of its witnesses, Jeffry Pollock and Hugh Larkin, Jr., respectively. On December 7, 1998, a hearing on this matter was held before the full Commission.

II. Introduction and Summary of Arguments

The issues presented to the Commission in this docket arise out of the Stipulations that were approved by the Commission in 1996. The Stipulations require Tampa Electric Company to freeze rates until December 31, 1999, absorb \$12 million of new annual base rate revenue

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requirements previously recovered through the oil backout clause, refund \$50 million to ratepayers, share sixty percent of its equity returns with ratepayers even within its permitted range of return on equity (“ROE”), and potentially refund additional earnings to ratepayers in 1999 and 2000 (TR 20,21). The Stipulations further require the Company to accrue interest at the thirty day commercial paper rate specified in Rule 25-6.109, F.A.C. on the deferred revenues. Consistent with the language of the Stipulations, proper utility accounting procedures and regulatory practices, and this Commission’s recent regulatory precedent, the Company includes the deferred revenue accrual in the regulatory capital structure and assigns a cost rate equal to the thirty day commercial paper rate. In June 1998, the Commission issued a Proposed Order approving the Company’s regulatory and accounting treatment of those deferred revenues in excess of its ROE for 1996. FIPUG and OPC protested the Proposed Order.

As a basis for their protest, both FIPUG and OPC have asserted that Tampa Electric’s regulatory and accounting treatment of the interest accrual on the deferred revenues is inconsistent with the intent of the Stipulations (TR 173-174, 188-189, 202). More specifically, FIPUG and OPC argue that the Company improperly included the cost of the interest accrual on the deferred revenues in its capital structure at its actual cost and, instead, should have assigned a zero cost rate to the interest accrual in its capital structure (TR 166).

The Company opposes the positions advocated by FIPUG and OPC and relies on the language of the Stipulations, utility accounting practices and regulatory procedures, and this Commission’s prior regulatory precedent to support its inclusion of the interest accrual in its capital structure at the thirty day commercial paper rate. The Stipulations require the Company to accrue interest on the deferred revenues at the thirty day commercial rate. They also state that all reasonable and prudent expenses and investment shall be allowed in the [ROE] calculation. Moreover, the Commission’s treatment of the deferred revenues and its interest component is consistent with generally accepted utility accounting procedures and regulatory practices. Both utility accounting procedures and regulatory practices permit recovery of all prudent costs incurred in providing utility services. Using a zero cost rate for deferred revenues would result

in disallowance of a prudent expense related to providing utility service and prevent the Company from achieving the ROE defined in the Stipulations.

Finally, the Company's treatment of deferred revenues is consistent with the most recent orders adopted by this Commission on this issue. In the Quincy Telephone, Southern Bell, FPUC - Fernandina Beach and FPUC - Marianna dockets, the Commission determined that the interest on deferred revenue should be included as a line item in the capital structure at its actual cost. Most recently, the Commission affirmed this view in the Florida Power Company Docket No. 98-1635-EI (Order No. PSC-98-1750-FOF-EI).

Accordingly, the Company believes that the Proposed Order accurately reflects the language of the Stipulations, utility accounting practices and regulatory practices, and this Commission's regulatory precedents. In further support of its position, Tampa Electric hereby submits its Post-Hearing Brief.

III. The Thirty Day Commercial Rate is the Appropriate Cost Rate to Apply to the Deferred Revenues in the Capital Structure.

A. The Stipulations require inclusion of the interest expense at the thirty day commercial rate in the capital structure.

An examination of the *language* of the Stipulations affirmatively demonstrates that Tampa Electric is required to accrue interest on the deferred revenues at the thirty day commercial paper rate and include the balance in its capital structure at its actual cost. In the Orders adopting the Stipulations, it directs Tampa Electric to accrue interest on the deferred revenues at the thirty day commercial paper rate. In addition, in Order No. PSC-96-0670-S-EI, it states: "**All reasonable and prudent expenses and investment shall be allowed in the [ROE] calculation and no annualized or proforma adjustments will be made.**" (emphasis added). This view is again affirmed in Order No. PSC-96-1300-S-EI, which states: "All reasonable and prudent expenses and investment are to be included in the calculation of the actual ROE for 1999." Excluding the interest accrual from the capital structure is tantamount to determining that

a cost that Tampa Electric was required to incur was imprudent.¹ Clearly, the requirement to accrue interest at the 30 day commercial paper rate demonstrates that the interest accrual is a real and prudently incurred expense related to providing electric service. The additional requirement that all reasonable and prudent expenses are to be included in the calculation of the ROE further justifies Tampa Electric's above-the-line treatment of the deferred revenue interest expense.

The language of the Stipulations further supports inclusion of the interest accrual in the capital structure at the thirty day commercial paper rate. In the Order adopting the Stipulations, the Commission affirmed its desire to apply a fair and balanced approach that would be beneficial to **both ratepayers and the Company** (emphasis added). (TR 233). This fair and balanced approach adopted by the Commission reflects, in part, its desire for the Company to have use of the deferred revenues to fund its operations while, at the same time, provide the ratepayers with a \$50 million refund, the possibility of future refunds in 1999 and 2000, and a rate freeze until December 31, 1999. Treating the interest expense as an above-the-line expense is consistent with the balanced approach because it is fair to both the Company and ratepayers.

Both Witnesses Larkin and Pollock ignore the actual language of the Stipulations and instead rely upon the "intent" of the Stipulations. During the December 7th hearing, both Witness Larkin and Witness Pollock stated that the parties "intended" for the cost of interest accrual to be treated as below-the-line. This untenable position is undermined by the language of the Stipulations. Pointedly, when the Stipulations and related orders intended for a cost to be treated as a below-the-line expense, they explicitly stated so. On page 3 of the October 24, 1996 Order adopting the second Stipulation, the Commission states that the entire investment of the Port Manatee site shall be treated as below-the-line. Clearly, the Stipulations do not define the interest accrual as a below-the-line expense. Therefore, it is clear that the Stipulations

¹ During the direct testimony of the Company's witness, Delaine Bacon, she discussed the prudence of including the interest as a line item in the capital structure: "I think that by including those two amounts [deferred revenues and interest] in the capital structure, it reflects the actual cost of providing service in 1996. Tampa Electric could not have provided service in 1996 without that \$77 million worth of funds. And to the extent that that was a source of funds for the Company, I believe that it's proper to include that cost in the capital structure." (TR 71).

recognized the interest accrual as an actual expense that was prudently incurred by the Company.

2

Both FIPUG and OPC also argue that the correct cost rate to assign to the deferred revenues in the capital structure is zero. As a basis for this position, FIPUG has asserted that any other treatment would be “at odds with the intent of the Stipulations.” In support of this position, FIPUG’s witness Jeffry Pollock stated in his direct testimony: “The Stipulation clearly contemplated a refund. Logic and common sense suggest that at least two of the three Stipulating Parties - OPC and FIPUG- would not have agreed to receive less than a full refund of excess revenues, including compensation for the time value of money.” (TR 159) Witness Larkin also echoed a similar belief when cross examined at the December 7th hearing: “..... but my background and experience would indicate that nobody would enter into a stipulation that required the ratepayers to pay their interest, their own interest.” (TR 209).

However, during Witness Pollock’s cross examination at the December 7th hearing, he admitted that he, in fact, did not have first hand knowledge of the parties intent and that he had not participated in the 1996 negotiations. (TR 174). Witness Larkin similarly admitted he too had no first hand knowledge of the intent of the Stipulations and was not involved in the negotiations in 1996.

Q: “So your discussions regarding the intent of this Stipulation are based solely upon your reading of the stipulation”?

A: “That’s correct.” (TR 208,211).

Because the language of the Stipulations is clear and unambiguous, there is no reason to ascertain the “intent” of the parties. Neither FIPUG or OPC offered *any* testimony that was

2 Adoption of FIPUG’s and OPC’s below-the-line approach requires this Commission to suspend its common sense and believe that it ordered Tampa Electric to accrue interest on the deferred revenues for the express purpose of later determining that the expense associated with the accrual was “imprudent”. Clearly, below-the-line treatment of the interest accrual is contrary to the dictates of the Stipulations, utility accounting procedures and regulatory practices, and past regulatory precedent.

probative of the parties intent at the time the Stipulations were negotiated nor produced any witnesses who participated in the negotiations. The testimony offered by FIPUG and OPC is merely argumentative and without any factual support.

Witness Pollock's and Witness Larkin's argument that the parties to the Stipulation "intended" for the interest accrual on the deferred revenues to be included in the capital structure at zero cost is also without merit. As can be seen from the language of the Stipulations, the parties to the Stipulations *never* intended for the interest cost to be treated below-the-line as a shareholder expense.³ Moreover, neither FIPUG or OPC produced any evidence or any calculations that support a below-the-line treatment. The language of the Stipulations irrefutably supports treating the interest accrual above-the-line.

Witness Larkin argues that the Company's treatment of the interest on the deferred revenues, as approved by this Commission, will cause "less to be deferred than if there had been zero interest." Witness Bacon, however, demonstrates that Tampa Electric's method is at least neutral to the deferred revenue balance and potentially more beneficial when compared with Witness Larkin's method.

The neutral impact of Tampa Electric's method is shown in Schedules A (Tampa Electric's method) and B (Larkin's method) of Witness Bacon's rebuttal testimony. Both Schedules assume that the Company's level of earnings require it to refund 100 percent of accumulated deferred revenues and demonstrate that assigning no interest to the deferred revenues results in the same amount of deferred revenues as the method used by Tampa Electric.⁴ (TR 249,259)

³ During the cross-examination of Witness Pollock at the December 7th hearing, he admitted that the treatment of the deferred revenues advocated by FIPUG would result in treating the interest accrual as a below-the-line expense. (TR 170). Witness Larkin also admitted during his cross examination that it was also his position that the interest, "ought to be paid by the shareholder". (TR 213).

⁴ Witness Bacon further demonstrates in Schedule C that adoption of FIPUG's and OPC's method, i.e. accrual of the interest but failure to include it in the capital structure, is patently unfair. As shown in Schedule C, failure to assign a cost in the capital structure results in different regulatory and market returns on equity and precludes the Company from *ever* achieving the ROE permitted by the Stipulations. (TR 249, 259)

The potential benefits of Tampa Electric's current approved method, in contrast to the "zero cost" method discussed by Witness Larkin, are demonstrated in two ways. (TR 247). In those years where the Company's ROE is in the 60/40 percent sharing range, interest accrued to the deferred revenue balance will be offset by only 60 percent, representing the impact of including the interest expense in the company's earnings. The remaining forty percent of the accrued interest results in more deferred revenues than if there were no interest provision. This higher deferred revenue balance increases the potential for refunds to customers.

The second potential benefit to ratepayers occurs after the Stipulation period because interest will continue to accrue on the balance that it is going to be refunded to ratepayers, resulting in more deferred revenues over the Stipulation period than if no interest had been accrued. Each of these examples demonstrate that Tampa Electric's current approved method results in equal or more deferred revenues than if no interest was accrued. (TR 247).

B. Utility accounting procedures and regulatory practices require inclusion of the interest expense at the thirty day commercial rate in the capital structure

Generally accepted utility accounting procedures also compel recognition of the interest accrual on the deferred revenues as an expense in the capital structure. As required by the Stipulations, Tampa Electric has accrued interest on the deferred revenues at the thirty day commercial paper rate and recorded the interest expense on its financial records as both an expense and liability. Tampa Electric's financial reporting has been consistent with Generally Accepted Accounting Procedures (GAAP). The Stipulations require the Company to accrue interest at the thirty day commercial paper rate; therefore, the Company is required to account for this cost in its capital structure and recognize the expense on its income statement. If Tampa Electric were to adopt the approach advocated by FIPUG and OPC, it would accrue interest at the thirty day commercial rate but ignore the cost of this accrual in its capital structure and fail to recognize the expense. FIPUG's and OPC's approach is not only inconsistent with GAAP, but it ignores the basic regulatory principles regarding the cost of capital.

Under current regulatory practices, a company is entitled to recover all prudent costs related to the cost of service as above-the-line costs; those costs that are not prudent and do not relate to a utility's cost of service are treated as below-the-line costs that are absorbed by a company's shareholders. The deferred revenues constitute a source of capital that the Company has been able to use for its operating expenses that it otherwise would have to obtain from outside funding. In other words, because outside funding would also have an associated cost, Tampa Electric would have incurred a cost regardless of the source of funds. The placement of the interest accrual in Tampa Electric's capital structure at the thirty day commercial rate recognizes this cost. If the Commission were to adopt the approach advocated by FIPUG and OPC and require the interest accrual but ignore its cost in the capital structure, Tampa Electric would be disallowed recovery of a prudent cost which has been legitimately incurred by the Company.

The treatment of the deferred revenues and its interest component should be similar to the regulatory treatment afforded customer deposits. In the case of customer deposits, amounts are collected as security on the customer's account and interest is accrued on these amounts. Later, the deposit plus accrued interest is returned to the customer or the company retains the amount plus accrued and unpaid interest for application to delinquent bills. The interest expense related to customer deposits is recovered "above-the-line".

Deferred revenues are similar. Interest is accrued on deferred revenues because the Stipulations require the interest to be accrued. Both the deferred revenues and accrued interest are potentially subject to customer refund, unless the company has a prior claim. In the case of customer deposits, the prior claim is based upon failure to pay a bill, while in the case of deferred revenues, the prior claim is based upon a company's failure to achieve its target ROE. The Commission's treatment of the deferred revenues in this matter should be consistent with its prior regulatory practice regarding customer deposits⁵

⁵Throughout this proceeding, OPC and FIPUG have compared deferred revenues to deferred taxes, bank deposits, and fuel under-and-over-recoveries. In each instance, the analogies are flawed. In the case of

C. Regulatory precedent requires inclusion of the interest expense at the thirty day commercial rate in the capital structure

Regulatory precedent also supports including the deferred revenue interest in the capital structure at its actual cost. In the Quincy Telephone, Southern Bell, FPUC - Fernandina Beach and FPUC - Marianna dockets, the Commission determined that it was appropriate to recognize deferred revenues in the capital structure as well as the interest accrued on the balance at the thirty day commercial paper rate. This methodology adopted by the Commission was independent of whether or not the deferred revenues were intended for refund to customers or were to be used by the company.

In the Quincy Telephone Order, Order No. 22367 (Docket No. 890292), the Commission ordered Quincy to defer surplus revenues for years 1987, 1988, 1989 and the first six months of 1990. The Commission further ordered Quincy to accrue interest at the thirty day commercial paper rate. The revenue and interest were to be annually credited to Quincy in an amount of \$200,000 until exhausted. In that Order, the Commission expressly stated that the deferred revenues and interest at the thirty day commercial paper rate were to be included in the company's capital structure. This approach is consistent with the method used by Tampa Electric.

Similarly, in the Southern Bell Order No. 94-0172-FOF-TL (Docket No. 920260), the Commission ordered the company to defer 1994, 1995 and 1996 revenues for eventual refund to the customers. For each of these years, the company included the deferred revenues in the

deferred taxes, interest is not accrued and, therefore, there is no interest component. Similarly, the analogy to bank deposits was misused because a bank customer **does** pay for his own interest in those cases where the bank depositor is also a bank customer through customer fees, interest on loan obligations and other customary bank fees. Finally, the Commission's treatment of fuel under-and-over recovery is inapplicable to deferred revenues because this treatment is guided by the Commission's desire to keep fuel under and over recoveries as low as possible. With respect to the treatment of deferred revenues, the Commission by definition is not implementing a policy to deny a company the opportunity to earn a fair and equitable ROE. In fact, the Commission stated in Order No. PSC-960670-EI approving the first stipulation, "This settlement provides an incentive for TECO to be more cost efficient since it can retain a significant portion of any increased earnings."

capital structure as a specific adjustment of short-term debt and the interest accrual at the thirty day commercial paper rate. The Commission approved this treatment.

In the Florida Public Utilities Company ("FPUC") - Fernandina Order No. 97-0135 (Docket No. 961542-EI), the Commission again permitted interest on deferred revenues to be included in capital structure at the short-term or thirty day commercial paper rate. In that matter, Fernandina earned above its allowed ROE in 1995 and was ordered to defer those over-earnings into its 1996 storm damage reserve. The capital structure treatment in that docket is consistent with the method used by Tampa Electric and the treatment previously approved by the Commission in Order No. PSC-97-0436-FOF-EI.⁶

To support its position, OPC cites the FPUC - Fernandina Beach case. However, this case is consistent with the other precedents cited above because the deferred revenues were included in the capital structure at the commercial paper rate. The reason that the Commission decreased the investor resources of capital by a like amount was because the company's initial accrual in 1995 and its subsequent filing did not recognize enough deferred revenues. In other words, FPUC did not offset the other sources of capital in the correct amount. Therefore, the Commission made the adjustment to investor sources of capital.

Tampa Electric, in contrast, has not failed to recognize the proper amount of deferred revenues. The amount of revenues deferred from 1995 and 1996 by the Company will be very similar to the Commission's final calculation of deferred revenues. Accordingly, the 1995 over earnings docket for FPUC - Fernandina does not represent an alternative to the other precedents.

Most recently, the Commission affirmed its belief that the interest accrual on deferred revenues should be included in the capital structure at its actual cost in Florida Power Company Docket No. 98-1635-EI (Order No. PSC-98-1750-FOF-EI). In this proceeding, the Commission

⁶ This Commission in 1997 (Order No. PSC-97-0436-FOF-EI) approved Tampa Electric's inclusion of the interest accrual on the deferred revenues in the capital structure at the thirty day commercial paper rate. In transcript of the March 18, 1997 agenda conference for the Company's 1995 earnings review, the Commission concluded it was patently fair to include the thirty day commercial paper rate in the capital structure for refund purposes since it was unfair to apply one cost for capital structure purposes and another for refund purposes.

decided whether FPC's deferred over earnings should be included in its capital structure as a separate line item using the actual interest rate applied to deferred earnings. The Commission concluded that this approach was appropriate.⁷

Those precedents set forth above address issues similar to the one presently before this Commission and support Tampa Electric's current treatment. The precedents, therefore, should be followed by the Commission.

IV. The Methodology Used by the Company to Separate Lakeland and FMPA Sales Is Consistent with Methodology Adopted in the Company's Last Rate Case

In Order No. PSC-97-1273-FOF-EI, the Commission required the Company to "separate capital, and operation and maintenance (O&M) costs associated with the FMPA and Lakeland wholesale sales." The Order further stated that the Company should use the separation methodology approved in its last rate case, Docket No. 920324-EI.

In 1996, the Company used the methodology approved in its last rate case, the "12 coincident peak methodology." Using that methodology, separation factors are adjusted in the Company's surveillance report based upon the inclusion of new wholesale contracts being served by Tampa Electric resources. For the FMPA and Lakeland contracts, separation factors were adjusted for the load served out of Tampa Electric's retail resources used in the month of December 1996. Because the sale to FMPA did not occur until December 16, 1996, the separation for FMPA was adjusted to reflect the time during the month the contract was in effect. Because this adjustment is not explicitly permitted by the 12 month coincident peak method, the Company has agreed to make an accounting entry to reflect the change. Both FIPUG and OPC have agreed that this adjustment satisfactorily resolves this issue and have no further objection.

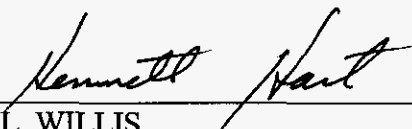
⁷ In the Staff's recommendation of this Order, it expressly stated this treatment was appropriate because it was "consistent with the treatment in a number of other Commission cases", including "**Order No. 97-0436-FOF-EI involving Tampa Electric Company (Docket No. 95-0379-EI).**" (emphasis added).

V. Conclusion

Based upon the language of the Stipulations, accepted utility accounting procedures and regulatory practices, and regulatory precedent, the Company believes that the Commission's approved treatment of the deferred revenues and its interest component in its Proposed Order is appropriate and should be affirmed by the Commission. Any other approach would fail to fully recognize the prudently incurred cost associated with the interest on deferred revenues, and would deny the Company the opportunity to earn the ROE defined in the Stipulations. Accordingly, Tampa Electric Company respectfully requests this Commission to adopt the deferred interest treatment in Proposed Order No. PSC-98-0802-FOF-EI.

DATED this 14th day of January, 1999.

Respectfully submitted,



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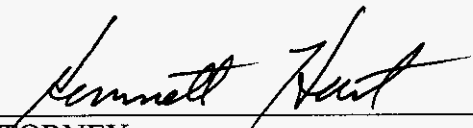
I HEREBY CERTIFY that a true copy of Tampa Electric Company's Post-Hearing Brief has been furnished by U. S. Mail or hand delivery (*) on this 14th day of January, 1999 to the following:

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