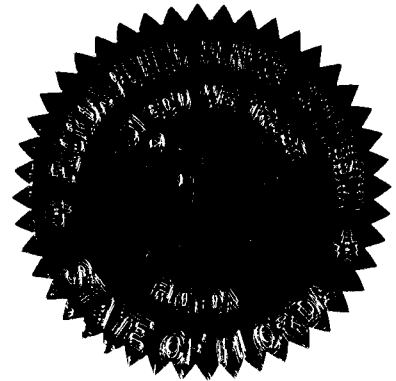


BEFORE THE  
FLORIDA PUBLIC SERVICE COMMISSION

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In the Matter of : DOCKET NO. 990250-EI  
Investigation into the :  
earnings and authorized :  
return on equity of Gulf :  
Power Company. :

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In the Matter of : DOCKET NO. 990244-EI  
Petition of Gulf Power :  
Company for approval of :  
proposed plan for an :  
incentive revenue-sharing :  
mechanism that addresses :  
certain regulatory issues :  
including a reduction to :  
the company's authorized :  
return on equity. :



PROCEEDINGS: AGENDA CONFERENCE  
ITEM NO. 10

BEFORE: CHAIRMAN JOE GARCIA  
COMMISSIONER J. TERRY DEASON  
COMMISSIONER SUSAN F. CLARK  
COMMISSIONER JULIA L. JOHNSON  
COMMISSIONER E. LEON JACOBS, JR.

DATE: April 20, 1999

TIME: Commenced at 9:30 a.m.

PLACE: Betty Easley Conference Center  
Room 148  
4075 Esplanade Way  
Tallahassee, Florida

REPORTED BY: KIMBERLY BERENS, CSR, RPR  
FPSC Commission Reporter

DOCUMENT NUMBER-DATE

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FPSC-RECORDS/REPORTING

1 **PARTICIPATING:**

2 **DALE MAILHOT and PETE LESTER**, FPSC Division  
3 of Auditing & Financial.

4 **BOB ELIAS**, FPSC Division of Legal Services.

5 **JOE JENKINS**, FPSC Division of Electric &  
6 Gas.

7 **JEFF STONE**, representing Gulf Power Company.

8 **JOHN McWHIRTER**, representing Florida Industrial  
9 Power Users Group, (FIPUG).

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**P R O C E E D I N G S**

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2           **CHAIRMAN GARCIA:** Mr. Mailhot, you want to  
3 tee up Item 10?

4           **MR. MAILHOT:** Sure. At the March 16th  
5 agenda, Staff brought a recommendation concerning a  
6 petition by Gulf Power Company for an incentive plan,  
7 and in addition, at that agenda, Staff had its own  
8 incentive plan. The Commission directed the Staff and  
9 the company and any interested persons to meet and try  
10 to resolve any differences. We met a couple of times  
11 and from those meetings, although we didn't resolve  
12 all our differences, we have a revised proposal from  
13 the company and a revised proposal from Staff. And  
14 the company's proposal is considered in Issue 1 and  
15 the Staff's proposal is in Issue 2. And I believe the  
16 company would like to speak.

17           **CHAIRMAN GARCIA:** Mr. Stone.

18           **MR. STONE:** Thank you, Mr. Chairman. I am  
19 Jeff Stone of the law firm of Beggs and Lane. I'm  
20 here today on behalf of Gulf Power Company. And I  
21 would like to go through our proposal and the  
22 revisions we made since we were here on March 16th.

23           In order to facilitate your review and our  
24 discussion, I have some handouts that I think will be  
25 helpful. One is a copy of our March 2nd filing that

1 has the consecutive number sequence in the lower right  
2 hand corner from Page 1 through Page 27. That's the  
3 same thing that was handed out on March 16th.

4 The other document that's being handed out  
5 to you now is our April 6th filing. It consists of a  
6 letter in the first two pages, and then the next  
7 attachment to the letter is the red line strike out  
8 version of our revised Attachment A to our petition.  
9 It sets out our revised proposal. And I'd like to  
10 just walk you through that just briefly. You'll see  
11 the shading indicates additions and they're strike out  
12 to show the deletions from our original Attachment A  
13 which set out our proposal.

14 In Paragraph 2, you'll see that we have --  
15 we have lowered our proposed ROE even further. Our  
16 currently existing ROE -- approved ROE is 12% midpoint  
17 and we have proposed to lower that 40 basis points to  
18 11.6. There is some discussion in laying out all of  
19 that in Paragraph 2 of our revised Attachment A.

20 Paragraph 3 talks about an incremental  
21 increase to the property insurance reserve of \$1  
22 million dollars. And that would bring the total  
23 annual accrual to the property insurance reserve  
24 before sharing to \$4.5 million on an annual basis for  
25 the three years covered by this plan.

1           In Paragraph -- new Paragraph 4, you'll see  
2           in the handout that we've given you is a discussion of  
3           a credit that we'd be providing to our retail  
4           customers for calendar year 1999. And that credit is  
5           a \$3.7 million credit to customers and it would be  
6           issued under our proposal on a per kilowatt basis on  
7           the July bill to our customers. If there was any  
8           difference in the projections, that would be taken  
9           care of in a true-up mechanism that is provided there.

10           Paragraph 4 goes on on page -- the  
11           consecutive sequence there, Page 4, to talk about what  
12           would be done in the calendar year 2000. Again it's a  
13           \$3.7 million credit. And, in this instance, we're  
14           talking about reducing the fuel and purchase power  
15           cost recovery factor. Since we don't have that  
16           information, we flow it into the determination of our  
17           factor come November.

18           And then for 2001, we have a little bit of a  
19           different twist on that \$3.7 million credit. We have  
20           some concerns about the company's earnings in that  
21           last year of the three year plan and so what we're  
22           proposing is that we would recredit to customers in a  
23           fashion similar to what we proposed for the 1999  
24           credit up to \$3.7 million and that would be the first  
25           \$3.7 million of revenues that contribute to earnings

1 above the 12.2% earnings set point that we've been  
2 identified in Paragraph 2.

3 So basically the \$3.7 million we talked  
4 about, it's automatic for years 1999 and 2000. But  
5 it's subject to earnings being available to support it  
6 for 2001.

7 The next area of change in our proposal is  
8 in Paragraph 6 and that's where we -- on our  
9 merchandizing program, we've talked about using a  
10 proxy as an alternative for the determination of how  
11 to remove our merchandizing operation for capital  
12 structure. And I'll go more into that later in my  
13 presentation.

14 But essentially what we're trying to  
15 identify is the type of operation that Gulf's  
16 merchandizing operation is, which is basically a  
17 financing operation.

18 Paragraph 7 is the sharing mechanism itself.  
19 Of course, it recognizes the reduction in our proposed  
20 ROE. The top of the range is where we start our  
21 sharing under our proposal and since we've lowered it  
22 more -- lowered it further than we had when we gave  
23 you our original proposal on March 2nd, you'll see  
24 that as a red line strike out there. And it makes  
25 reference to the incremental accrual to the property

1 insurance reserve down there in the text on Page 5 of  
2 this red line strike out version.

3 The other changes noted are on Page 6,  
4 Paragraph 9, when we were trying to conform to what we  
5 understood Staff's concerns were about the reporting  
6 cycle. And then finally on Paragraph 10, which is on  
7 Page 7 of the red line strike out version of the  
8 April 6th filing, we talk about the company's going to  
9 commission an updated study to come up with the  
10 wholesale retail separation factors for use and  
11 surveillance report. And I just wanted to track you  
12 through our revision that was filed on April 6th.

13 The company formulated its original sharing  
14 proposal in order to address Staff's stated concerns  
15 regarding the level -- the current level of Gulf's  
16 authorized return on equity and the outstanding  
17 balance of certain regulatory assets. And our revised  
18 proposal continues to address the stated concerns in  
19 what the company believes is a reasonable manner and  
20 at the same time we have developed a mechanism that  
21 provides opportunities for significant benefits to  
22 customers and shareholders alike. I touched on it  
23 briefly, the significant change in our proposal where  
24 we talk about the \$3.7 million credit to customers.

25 As I indicated, for 1999 that would be

1 passed to customers' bills in July. For Gulf's  
2 residential customers, based on the projected average  
3 residential energy use billing in July 1999, that  
4 would amount to 16 -- 16,019 kilowatt hours in that  
5 month and so the average credit would be about \$5.94  
6 in July.

7 As I go into my presentation, I want to  
8 point out that we have several people here from the  
9 company that when I get to a breaking point, they'll  
10 be available to answer questions if the Commission has  
11 any. And my comments right now will focus on four  
12 outline points.

13 I want to provide an overview, including a  
14 description of the plan; talk about our proposed ROE  
15 adjustment and the basis for our sharing percentage;  
16 and finally, our proposed treatment of the  
17 merchandizing operation.

18 As I mentioned, on the 16th of March, the  
19 foundation for the company's proposal is Gulf's  
20 sustained performance on three key indicators: Rates,  
21 reliability and the level of customer complaints. We believe  
22 our proposal properly takes into account significant  
23 differences between Gulf and other Florida electric utilities  
24 in regard to five years of data on these key indicators  
25 related to electricity prices, reliability of electric service



1 and the number of justified customer complaints to this  
2 Commission. The data on these key indicators is shown in our  
3 petition on Attachment B, that's pages 11 to 12 of the  
4 March 2nd filing. And it shows superior performance by Gulf  
5 on a sustained basis with regard to prices to residential  
6 customers, regards to the number of minutes of interruption  
7 per customer per year, and regards to the incidents of  
8 customer complaints to the Commission.

9 Gulf's customers presently benefit from the fact  
10 that Gulf Power has the lowest electric rates in Florida among  
11 major utilities and among the lowest in the nation. Gulf's  
12 customers also benefit from the company's high reliability.  
13 And for the four major investor-owned utilities in Florida,  
14 Gulf has the lowest annual rate of justified customer  
15 complaints per thousand customers. Gulf's performance in  
16 these key areas reflects the company's long-term focus on  
17 issues related to customer satisfaction and value.

18 Gulf is highly ranked among leading electric  
19 utilities across the country in regards to customer  
20 satisfaction. As we stated on March 16th, we pointed your  
21 attention to Page 17 of our original petition which contained  
22 a table outlining the results of a recent benchmark study  
23 survey. Gulf's low rates, high reliability and high customer  
24 satisfaction clearly reflect management's focus on these key  
25 areas.

1           Again, Attachment C to our original  
2 petition, Pages 13 through 19, summarizes fuel cost  
3 initiatives, reduction initiatives, reliability and  
4 customer satisfaction initiatives undertaken by the  
5 company as part of this management focus.

6           These initiatives demonstrate that such  
7 outstanding results as shown in Attachment B did not  
8 occur by accident but instead are an indication that  
9 management's focus is working. As we pointed out on  
10 March 16th, despite combined effects of customer  
11 growth, inflation and several hurricanes since base  
12 rates were last set, Gulf's management has been able  
13 to find ways to consistently meet the expectations and  
14 needs of its customers through low rates, high  
15 reliability and high customer satisfaction. And at  
16 the same time, still satisfy its shareholders by  
17 achieving earnings near the top of the authorized  
18 range. And all of this is done with no increase in  
19 the company's base rates.

20           Our revised sharing plan starts from this  
21 positive starting point and builds towards something  
22 better in the future. It is important to note that  
23 Gulf's proposed plan incorporates a reduction to the  
24 company's authorized midpoint ROE of 40 basis points  
25 and this is retroactive to the first of the year. The

1 reduction would change the midpoint from 12% to 11.6%  
2 and has a corresponding shift in the authorized range  
3 so that it would now be -- if approved, it would  
4 extend from 10.6% to 12.6% instead of the current 11%  
5 to 13%. And all of this is shown on page 3 of our  
6 April 6th filing in Paragraph 2.

7           Although important, the proposed ROE  
8 reduction is just one part of Gulf's overall sharing  
9 plan. Adoption of Gulf's sharing plan sends a proper  
10 signal to management and the company's shareholders.  
11 This incentive is designed to achieve good financial  
12 results while maintaining a high level of performance  
13 on the key customer service indicators of rates,  
14 reliability and customer satisfaction.

15           Briefly, the plan elements are, it's for  
16 three calendar years, 1999, 2000, and 2001 and that's  
17 in Paragraph 1 on Page 3 of our April 6th filing. It  
18 addresses two regulatory concepts established in  
19 Gulf's last rate case -- readdresses them. The third  
20 for deferred return and the effect of merchandizing  
21 operations on the company's capital structure. You'll  
22 find that treatment on Page 4 of the April 6th filing,  
23 Paragraphs 5 and 6.

24           And finally, the third plan element that  
25 we're focusing on is the sharing mechanism which

1 allows earnings above the newly established top of the  
2 authorized range to operate to the benefit of  
3 customers and shareholders alike, both in the short  
4 term through the 40% credit to customers and the 40%  
5 credit to shareholders, and in the long-term, by using  
6 the remaining 20% to accelerate the amortization of  
7 three identified regulatory assets to lower base rates  
8 for the future and provide needed support to the  
9 property insurance reserve. That mechanism is  
10 detailed on Pages 5 and 6 of our April 6th filing in  
11 Paragraph 7.

12 We did meet since March 16th and we made an  
13 effort to come to an agreement, and you will note that  
14 the company has provided a significant credit to its  
15 customers in the form of \$3.7 million to bring our  
16 projected earnings down to the revenue set point of  
17 12.2%. But there are three major areas of  
18 disagreement between the company and the Staff. And  
19 these areas are of critical concern to Gulf's  
20 management and they're set forth in the company's  
21 revised proposal.

22 They are the ROE level, the sharing  
23 percentage and the treatment of Gulf's investment in  
24 its merchandizing operation.

25 Gulf's proposed ROE adjustment from 12.0%

1 midpoint to 11.6% midpoint is important. That is a  
2 significant reduction but it recognizes that ROE  
3 should not be set in a cookie cutter fashion. One  
4 size clearly does not fit all.

5 A hasty or ill-advised decision now, when  
6 capital needs for new generating capacity and other  
7 property additions are just around the corner, could  
8 cost Gulf's customers in the long run if rating  
9 agencies downgrade our credit worthiness out of  
10 concern about the regulatory environment created by  
11 FPSC actions.

12 It also -- a hasty or ill-advised decision,  
13 or dramatic decision and change in the ROE could send  
14 the wrong signal on opportunities for return on equity  
15 from this Commission, and could have far-reaching  
16 impacts on decisions regarding choices of where to  
17 invest equity capital.

18 **COMMISSIONER CLARK:** Let me just ask a  
19 question right on that point. How are you listed in  
20 the stock market? Are you Southern Company or are you  
21 Gulf?

22 **MR. STONE:** As far as Gulf's --

23 **COMMISSIONER CLARK:** Who raises capital? I  
24 guess that's a better way to put it.

25 **MR. STONE:** Common equity is provided to

1 Gulf from our parent, Southern Company.

2 **COMMISSIONER CLARK:** Okay. So Southern  
3 Company is the one that's traded, right?

4 **MR. STONE:** It's the one that's listed on  
5 the exchange, yes. Gulf is rated with regard to its  
6 debt individually. So we have our own credit rating.

7 **COMMISSIONER CLARK:** Okay. Thank you.

8 **MR. STONE:** In Attachment D to our petition,  
9 Pages 20 through 27, there is a detailed discussion of  
10 the basis for the ROE component of Gulf's proposal.  
11 And we discuss key points of difference between Gulf  
12 Power and other Florida electric utilities in terms of  
13 leverage, electric rates, reliability, customer  
14 complaints and business risk. I'd like to touch on  
15 some elements of that discussion for you today.

16 Relative differences in leverage between  
17 utilities justify relative differences in authorized  
18 ROE. I have a chart that we'd like to hand out that  
19 illustrates the dramatic difference in equity ratio  
20 that has developed between Gulf Power and FP&L over  
21 the past four years.

22 Although intuition leads us to the  
23 conclusion that differences in equity ratio reflect  
24 relative differences in risk, two separate studies  
25 conducted nearly 12 years apart establish this concept

1 empirically for electric utilities. The two studies  
2 have been summarized in Attachment D to our original  
3 petition, on Pages 20 to 21. And they reach similar  
4 conclusions regarding the quantification of this  
5 difference. In Gulf's case, based on expert testimony  
6 before you by affidavit, the quantified difference is  
7 at least 47 basis points above the midpoint recently  
8 established for FP&L.

9 We also discussed trends and the comparative  
10 costs for kilowatt hour for Florida's electric --  
11 Florida's electric utilities. We talk about the data  
12 of comparative reliability and we provide information  
13 regarding the customer complaints or satisfaction  
14 index and those are all on Page 21 of our original  
15 petition. And we submit to you that the data on these  
16 pages provide further grounds for appropriately  
17 exercising the Commission's discretion in setting  
18 Gulf's ROE at a higher level.

19 Although the ROE effects of the differences  
20 in these three areas are not specifically quantified  
21 in our proposal, the dramatic differences in  
22 performance between Gulf and other utilities, when  
23 combined with the 47 basis point difference associated  
24 with the difference in leverage, clearly justifies  
25 setting the midpoint for Gulf Power for the three

1 years covered by the company's proposal at the level  
2 proposed by Gulf, 11.6%.

3 On March 16th I recited the basis for  
4 exercising discretion in this manner. It is found in  
5 the applicable statute and case law. Summaries of  
6 those matters are on Page 3 of our March 2nd filing.

7 I will not belabor the point further at this  
8 time except to say that the Commission clearly has the  
9 discretion to approve the ROE midpoint proposed by  
10 Gulf as an appropriate incentive reward for its  
11 outstanding achievement in the areas of customer  
12 rates, reliability of electric service and the low  
13 rate of justified customer complaints.

14 We submit to you that Gulf's sustained  
15 performance on these three key indicators are of  
16 sufficient magnitude that they should be recognized  
17 explicitly when establishing Gulf's authorized ROE.  
18 The differences between Gulf and other Florida  
19 electric utilities warrant the exercise of the  
20 Commission's discretion to establish a different  
21 higher midpoint than 11.0%.

22 The discussion in Attachment D also  
23 addresses differences in relative business risk faced  
24 by Gulf as compared to other Florida electric  
25 utilities.



1           As we mentioned on March 16th, Gulf faces  
2 more business risk than other electric utilities, in  
3 part due to our greater reliance on sales to the  
4 industrial sector and the dominant role of the U.S.  
5 military on the economy of the area in which we serve.  
6 These and other differences in relative business risk  
7 should also be reflected as differences in authorized  
8 ROE.

9           As we pointed out on March 16th, in order to  
10 evaluate the reasonableness of our proposed midpoint  
11 as a compromise settlement, Gulf examined recent  
12 trends in returns authorized for electric utilities  
13 across the nation. As part of Attachment D to our  
14 petition, Pages 22 to 23, using the consecutive  
15 numbering at the lower right-hand corner, we have  
16 included data from a January 1999 report. It's  
17 entitled, Major Rate Case Decisions, January 1990 to  
18 December 1998. It was produced by the Regulatory  
19 Research Associates or RRA.

20           And according to this report, equity returns  
21 authorized for electric utilities across the nation  
22 averaged approximately 11.7% in 1998 compared to 11.4%  
23 in '96 and '97. The ROE decision summarized in the  
24 RRA report during the fourth quarter of '98 averaged  
25 12.03%. In fact, in nine of the cases for 1998

1 contained in the RRA report, the authorized ROE was  
2 established at or above 12.0%. Remember that's our  
3 current authorized midpoint.

4           When measured against these trends, our  
5 settlement proposal of 11.6%, a reduction from the  
6 12.0% currently authorized and a further reduction  
7 from the 11.8% proposed on March 2nd, our 11.6% is  
8 clearly reasonable. This is especially so when you  
9 take into account that the proposal submitted by the  
10 company would operate retroactively.

11           The trend in ROEs recently authorized for  
12 electric utilities across the country on a going  
13 forward basis, suggests that the cost of equity  
14 capital for electric utilities is trending up.  
15 Forecasts show that rates for A-rated utility bonds  
16 and T-bills are expected to rise over the period  
17 covered by Gulf's proposal.

18           In fact, we'd like to hand out a chart that  
19 shows out selected financial information from 1990 to  
20 present including the T-bill rates, historical and  
21 projected, as well as the rates for A-rated utility  
22 bonds.

23           As you can see, based on the trends, now is  
24 not the time for a dramatic change in ROE for Gulf  
25 Power. The company's offered reduction of 40 basis

1 points, as contained in Gulf's proposal and as part of  
2 the overall sharing plan, should be accepted as  
3 reasonable.

4           Turning now to the sharing plan itself. As  
5 we pointed out before, the existing regulatory  
6 framework provides a limited incentive for management  
7 to seek out and achieve efficiencies in operations.  
8 This limited incentive is provided by allowing  
9 shareholders to keep the increment in earnings above  
10 the authorized midpoint ROE up to the top of the  
11 authorized range. But our proposal builds on that and  
12 goes beyond by providing an appropriate incentive to  
13 seek out and achieve even greater efficiencies in  
14 order to grow shareholder value by entering into what  
15 we've labeled the sharing range above the top of the  
16 traditional zone.

17           We believe we struck an appropriate balance  
18 of customer and shareholder interest in our proposed  
19 sharing mechanism that allows both constituencies to  
20 receive and retain benefits resulting from added  
21 efficiencies.

22           Gulf's proposed allocation to shareholders  
23 under the sharing plan is important to the overall  
24 success of the plan and it's way it's contained in our  
25 proposal as an important element.

1           This share, 40%, is significant enough to  
2 get the attention of the company's shareholders and  
3 maintain their support of managements efforts to  
4 achieve further efficiencies without sacrificing the  
5 efforts that have led to outstanding accomplishments  
6 with regard to customer rates, reliability, and  
7 customer satisfaction as shown by the low incidents of  
8 justified customer complaints.

9           Furthermore, setting the shareholders  
10 allocation of the shared revenues at 40% is consistent  
11 with the Commission's established precedent. The  
12 Commission has approved a sharing mechanism for  
13 Southern Bell and TECO that provided 40% sharing to  
14 the shareholders.

15           As we've indicated, the allocation to  
16 shareholders must be large enough that it's not viewed  
17 by the shareholders as a mere token, but rather  
18 justifies their support of continuing management  
19 efforts. At the same time, we recognize that it has  
20 to be balanced with what the customers receive. We  
21 believe by striking the balance at 40% for both of  
22 these constituencies we have reached the proper  
23 balance point.

24           To build on the existing foundation it is  
25 important to add to whatever incentives exist within

1 the traditional top of the zone framework. Gulf's  
2 proposal does this by adding an appropriate level of  
3 incentive based sharing opportunity that encourages  
4 efforts that may result in earnings above the top of  
5 the zone that can be appropriately shared, earnings  
6 that are essentially discouraged under the existing  
7 framework.

8           The third key point of difference that I  
9 wanted to describe for you is the merchandizing  
10 operation. The manner in which Gulf has been  
11 treated -- has been required to treat the capital  
12 structure of its merchandizing operation for  
13 surveillance purposes is not reasonable under the  
14 actual circumstances faced by Gulf. The company uses  
15 the -- Gulf's overall capital structure to support  
16 both utility and nonutility operations.

17           By taking the merchandizing operation out of  
18 the company's capital structure, based on 100% equity,  
19 we're unfairly penalizing the shareholders for this  
20 investment by forcing them to subsidize the retail  
21 jurisdiction. There simply is no empirical evidence  
22 to support the notion that Gulf's investment in its  
23 nonutility merchandizing operation has any impact on  
24 the company's overall cost of capital.

25           The company's merchandizing investment of

1 \$14 million, the overwhelming majority of which is  
2 accounts receivable, simply pales in significance when  
3 compared to the \$1.3 billion invested in the company  
4 overall. The merchandizing investment is such a small  
5 piece of the total that it is lost in the rounding.  
6 It, therefore, has no impact on the company's cost of  
7 capital. It is a mere fiction to act as though the  
8 merchandizing investment materially alters the  
9 company's risk profile. There simply is no evidence  
10 to suggest that Gulf's merchandizing investment has  
11 had any adverse impact on the cost to Gulf's retail  
12 electric customers.

13 **COMMISSIONER CLARK:** Mr. Stone, is that the  
14 test we've used in the past that it have no adverse  
15 impact?

16 **MR. STONE:** Commissioner, the way --

17 **COMMISSIONER CLARK:** Let me ask the question  
18 another -- what makes it different than what we  
19 decided in the last rate case?

20 **MR. STONE:** It was assumed in the last rate  
21 case that because it is perceived that the  
22 merchandizing operation has increased risk, that it  
23 must have some impact. But there was no evidence of  
24 that impact. In fact, the only evidence that was  
25 provided, was provided by Gulf and showed that there

1 was no adverse impact.

2 **COMMISSIONER CLARK:** So you're saying we  
3 were wrong in the last case and we should change that  
4 now, not that the circumstances are different?

5 **MR. STONE:** Commissioner, that is correct.  
6 But I also point out that that's essentially what the  
7 Staff's concluded with regard to the third floor. And  
8 so, if we're revisiting the third floor decision,  
9 it -- we're basically asking the same type of  
10 re-review take place with regard to the merchandizing  
11 operation.

12 **COMMISSIONER DEASON:** Is Staff saying we  
13 were wrong on the third floor, that the opportunity is  
14 now present to cease accruing a regulatory asset and,  
15 in fact, try to reverse that accrual and get it off  
16 the books as rapidly as possible?

17 **MR. STONE:** They've not actually used the  
18 words that we're wrong, but certainly that is the  
19 effect of what we're doing.

20 This is a suitable breaking point in our  
21 presentation. As I mentioned at the beginning, we do  
22 have a number of people here from the company that are  
23 available to answer any questions you may have and  
24 certainly I will try to answer them as well. After we  
25 hear from other individuals, I would like an

1 opportunity to make some further remarks in closing.

2           **MR. McWHIRTER:** Mr. Chairman and  
3 Commissioners, my name is John McWhirter and I'm here  
4 representing an industrial consumers group. Our group  
5 has not participated in these discussions from day  
6 one. We didn't know they were going on until Gulf  
7 filed its plan in March. After that time we were  
8 invited to participate and have participated.

9           At the outset, I'd like to pass on to you  
10 what Mr. Cresse told me and that is that Gulf is a  
11 very good utility company. It's very reliable. Its  
12 rates to the industrial consumer are less than the  
13 interruptible rates -- firm industrial consumer are  
14 less than the interruptible rates in other parts of  
15 the state. So why would we be here objecting and  
16 looking a gift horse in the mouth so to speak? Well,  
17 it's a matter of economics and it's a matter of money  
18 and it's a matter of proper regulatory philosophy.

19           Gulf has given you a plan and the Staff has  
20 given you a plan. The Gulf is Attachment A. The  
21 Staff's plan is Attachment B. I would like to proffer  
22 to you the FIPUG plan as Attachment C. And Gulf's  
23 plan is an 11 point plan. Staff has an eight point  
24 response with several subparts, and the FIPUG response  
25 is a simple six point plan.



1           First item would be that we would reduce  
2 base rates by \$7 million a year. Item No. 2, Gulf has  
3 proposed that its ROE be 11.6%. Staff says it ought  
4 to be 11.2% or lower. I would suggest that the  
5 Commission adopt the return on equity that Florida  
6 Power & Light and the Public Counsel agreed upon in  
7 its recent rate confrontation at 11%.

8           The third item would be that all revenues  
9 that are 100 basis points in excess of the authorized  
10 11.7 -- 11% return be refunded to customers.

11           The Commission has what it calls the range  
12 of reasonableness. You set a rate and you said the  
13 proper rate is 12% for this utility, but there's a  
14 range of reasonableness and you'll let it go up to 13%  
15 before you do anything about it. And the reason this  
16 case got started was, Gulf's 1998 revenues were over  
17 13% when you take into consideration some things that  
18 were omitted from the Gulf presentation, which I'll go  
19 into in a minute.

20           So the third point is, that between 11 and  
21 12, Gulf keeps the money. When it gets over 12, give  
22 it back to the customers. They're the ones that  
23 provided it.

24           Third -- the fourth point -- I combined with  
25 my -- oh, yeah. The fourth point is that as to this

1 revenue between 11% and 12%, it would be retained by  
2 Gulf but it be retained as a fund entitled  
3 contribution and aide of construction against future  
4 anticipated storm damage.

5 Right now, you allow a storm damage reserve  
6 of 36 -- up to \$36 million. We don't know exactly how  
7 that works and that needs some study, but I think if  
8 you treated these excess revenues in that fashion  
9 people would be properly accounted for.

10 **COMMISSIONER CLARK:** Mr. McWhirter, what is  
11 the point at which you start counting the revenues as  
12 excess? 12%?

13 **MR. McWHIRTER:** You talking about  
14 regulatory -- repeat the question. You know I'm hard  
15 of hearing.

16 **COMMISSIONER CLARK:** I guess your view that  
17 it should be retained for storm -- revenues be  
18 retained for storm damage --

19 **MR. McWHIRTER:** Future anticipated storm  
20 damage.

21 **COMMISSIONER CLARK:** And what revenues was  
22 that? Above what percent?

23 **MR. McWHIRTER:** That's between 11 and 12.

24 **COMMISSIONER CLARK:** So we --

25 **MR. McWHIRTER:** Earnings over 11% go to the

1 first -- the first 1% goes to that storm reserve.  
2 Over 12%, which is 100 basis points over your  
3 authorized return, that would go to the customers.

4 **COMMISSIONER CLARK:** So you would eliminate  
5 the range of return?

6 **MR. McWHIRTER:** Beg your pardon?

7 **COMMISSIONER CLARK:** You would eliminate the  
8 range of return? You would set it at 11% and  
9 anything --

10 **MR. McWHIRTER:** Well, the range of return is  
11 merely used for surveillance purposes so that you know  
12 when something should be done. Revenues are volatile.  
13 They follow the weather and they follow other things.  
14 And as long as the revenues are within a range, you  
15 say, that's okay. And the revenues here are not  
16 within your authorized range. So what should you do?

17 Now, what we're doing here, the Staff and  
18 Gulf recommend that we freeze everything in stone for  
19 three years and so for the next three years we'll  
20 control. I'm suggesting that under a revenue cap  
21 procedure like we have, Gulf will be assured of  
22 getting its 11%, but over 11% it will get to keep the  
23 money and send it on to Southern Company like it does  
24 now, and over 12% the customers get some relief.

25 **COMMISSIONER CLARK:** Mr. McWhirter, I didn't

1 understand your presentation as saying that. If  
2 you're saying the revenues over 11% have to be  
3 accredited to the storm reserve, then essentially I  
4 think what you're saying is, the top of the range is  
5 11%.

6 **MR. McWHIRTER:** That's the authorized  
7 return.

8 **COMMISSIONER CLARK:** Yes.

9 **MR. McWHIRTER:** What do you do with money  
10 when it's more than you've authorized it to keep?

11 **COMMISSIONER CLARK:** But the point is,  
12 you're saying they can keep everything up to 11%.  
13 Above 11% -- above 11 to 12, they have to credit it to  
14 a specific account.

15 **MR. McWHIRTER:** It keeps that money, but  
16 that money is tagged.

17 **COMMISSIONER CLARK:** Okay.

18 **MR. McWHIRTER:** And it keeps the money. It  
19 can use it anyway it wants to, but it's tagged. If we  
20 have storm damage and they replace that storm damaged  
21 equipment, at that point in time the money they use  
22 that should have been in this reserve fund will be  
23 considered a contribution in aide of construction.

24 **COMMISSIONER CLARK:** So their earnings  
25 are --

1           **MR. McWHIRTER:** Similar to what you do in  
2 water and sewer companies. Yes.

3           **COMMISSIONER CLARK:** So their earnings --  
4 what they're allowed to keep and have the discretion  
5 to do with as they please is 11%?

6           **MR. McWHIRTER:** Yes. Yes.

7           **COMMISSIONER CLARK:** Okay.

8           **COMMISSIONER DEASON:** Mr. McWhirter.

9           **MR. McWHIRTER:** Now --

10          **COMMISSIONER DEASON:** Mr. McWhirter.

11          **MR. McWHIRTER:** Yes, sir. I'm with you. I  
12 apologize.

13          **COMMISSIONER DEASON:** That's okay. I  
14 believe you indicated maybe in your presentation or  
15 response to a question that the company was guaranteed  
16 11%?

17          **MR. McWHIRTER:** Yes.

18          **COMMISSIONER DEASON:** How is it in your  
19 proposal the company would be guaranteed 11%?

20          **MR. McWHIRTER:** I don't have any problem  
21 with giving it the same kind of guarantee that you do  
22 with environmental cost and the same kind of guarantee  
23 that you do with conservation investments. If it  
24 falls below 11%, go ahead and give them the guaranteed  
25 revenue. As you know, right now, 38% of all the

1 revenues received by utilities are guaranteed  
2 revenues. It's not an opportunity to earn a return.  
3 And I won't go into that because you don't have time  
4 for it.

5 **COMMISSIONER DEASON:** Let me -- I want to  
6 clarify what you're proposing. If the company files a  
7 report with the Commission indicating that they earned  
8 10% return on equity, then you think the company  
9 should be allowed to collect revenue through fuel  
10 adjustment or whatever mechanism, enough so that they  
11 would earn 11% on equity?

12 **MR. McWHIRTER:** I think if -- you need to  
13 address it the way you think appropriate to address  
14 it. But if we're restricting the company to the 11%,  
15 then I don't see any real problem with letting them  
16 earn 11%, provided that the investments are prudent  
17 and that you actually supervise the investments to  
18 ensure that they're --

19 **COMMISSIONER DEASON:** What happens -- there  
20 is no incentive to do anything to improve operations  
21 or be innovative or to be efficient, to cut costs or  
22 to try to increase sales because you're saying they're  
23 guaranteed 11 no matter what they do, but they're not  
24 going to get anything above 11 because if it goes  
25 above 11 we're going to take the first million -- I'm

1 sorry -- the first 100 basis points and treat it as  
2 storm damage accrual and anything over 12 we're going  
3 to refund to customers.

4 **MR. McWHIRTER:** One of the benefits of being  
5 a monopoly and the only company that can provide  
6 service to customers is that you get an authorized  
7 return on your investment. That's one -- if you want  
8 the franchise and you want to have the monopoly  
9 rights, then you submit your operations to this  
10 regulatory body and this regulatory body doesn't need  
11 to give this kind of incentives that flow in a  
12 competitive industry to an industry that has  
13 essentially a guaranteed return, and here we're giving  
14 them a guaranteed 11% return. If they don't like this  
15 proposal, just as if they don't like the Staff's  
16 proposal, then they can ask for a hearing and we can  
17 deal with it at a hearing and the logic of the  
18 circumstances.

19 But we're in very serious times, as you well  
20 realize, far better than I do. And right now you're  
21 suggesting that we chisel something in stone for three  
22 years. If we're going to chisel it in stone, you need  
23 to truly evaluate and enunciate what your policies are  
24 with respect to what's going to happen the next three  
25 years. And I'm suggesting to you, and I will suggest

1 it a little -- I want to hurry along because I know  
2 you have a crowded agenda. But I think this is a very  
3 interesting and a very extremely important topic.  
4 It's one of your best utilities without a doubt, but  
5 you're talking about regulatory philosophy.

6 The fifth item in our report is that the  
7 third floor, way back when, when you had a rate case,  
8 there was a determination that the \$3.8 million that  
9 was spent to put in the third floor was excessive at  
10 the time, but sometime in the future it would be okay.

11 Well, since that time you've been booking a  
12 return on that. And that item now is a \$3.8 million  
13 investment plus the \$2.9 million or 47% interest on  
14 that initial investment. And I'm suggesting that  
15 that, instead of amortizing that investment over a  
16 three year period, that you put the \$5.7 million in  
17 rate base and amortize it over the remaining useful  
18 life of that building.

19 Now, a few years ago the company spent  
20 \$18.9 million to get better interest rates. They were  
21 able to refinance their debt. The company calls that  
22 a loss on refinanced debt. But, actually, over the  
23 length of the -- I'm sure they wouldn't have done it  
24 if they hadn't done a net present value study and  
25 concluded that over the term of the loan that



1 \$18.9 million would be more than returned many times.

2 So the question is, should today's customers  
3 pay that in the next three years or so, or should the  
4 company amortize that over the remaining life of the  
5 indebtedness which you normally do with a mortgage  
6 with the Internal Revenue Service require you to do?

7 And I'm suggesting, as my last point, that  
8 this 8.9% spent to get a lower interest rate flow to  
9 the people who are going to benefit from the lower  
10 interest rate. Right now you're asking the customers  
11 to pay for it, but you're not giving the customers any  
12 benefit from the lower interest rate. So it doesn't  
13 make much sense. Let the people who benefit, pay for  
14 it.

15 Now, one of the problems with the man in the  
16 street and me, people that have fourth grade  
17 understanding like I do, is when you talk in  
18 percentages and mix percentages and dollars, you get  
19 kind of confused and you don't know what's going on.

20 So what I've done for you is I've taken the  
21 company's year-end surveillance report that was filed  
22 on February 15th, and it's the report that the Staff  
23 used to get its analyses. And I've translated the  
24 percentages that we're talking about here into dollars  
25 and I think -- what I'd like to do in the next three

1 minutes is to analyze for you the dollar impact of the  
2 three proposals.

3           The first proposal is that the current  
4 authorized return, when we're doing our analysis,  
5 based upon Gulf Power's equity component, is  
6 \$350 million in round numbers and it's entitled to a  
7 12% return on that. That results in \$42 million a  
8 year is what you authorized Gulf Power to earn.

9           Staff, Plan B, agrees with that and FIPUG  
10 agrees with that. So we're all in agreement that the  
11 current authorized return translated in dollars as  
12 though we were looking at a moment in time,  
13 December 31, 1998, the authorized return is  
14 \$42 million.

15           Gulf says, here's what the return should be.  
16 Gulf says the return should be \$44 million in cash.  
17 Staff says it should be \$39 million because it's using  
18 a return of 11.2%.

19           (End of Tape 1, Side B.)

20           **MR. McWHIRTER:** What really happened was  
21 that instead of earning \$42 million according to Gulf  
22 it earned \$45 million. According to the Staff, Gulf  
23 earned \$49.5 million plus. So it earned some seven  
24 and a half million dollars more than the authorized  
25 return. The difference is that in 1998 the Staff

1 gives Gulf credit for \$3.5 million going to the  
2 insurance reserve and Gulf took \$6.5 million. FIPUG  
3 agrees with the Staff that the real earnings were  
4 \$49.5 plus. So Gulf has got this money in its packet.  
5 Never recoverable from the customers. Okay.

6           What should we do about the excess in the  
7 future? Gulf says let's take \$3.7 million of that  
8 \$49 million and reduce rates. Staff says, take  
9 \$7 million of that \$49 million -- 49 and a half  
10 million dollars, which would bring Gulf back to \$42  
11 million, and reduce rates by that amount. FIPUG  
12 agrees with the Staff. We think \$7 million rate  
13 reduction today is an appropriate amount under a  
14 settlement proposition. We think the amount is lower  
15 than that but what would happen is that would occur  
16 after a rate case and if you had a full rate case it  
17 would be a year before we would get any relief. So  
18 \$7 million is appropriate in the short run.

19           So the next step is, what do we do with the  
20 money in excess of the amount that comes about with  
21 the new returns allowed? Gulf says it gets to keep  
22 the first \$44 million, which is \$2 million more.  
23 Staff says Gulf gets to keep \$42.6 million. FIPUG  
24 says, Gulf can keep \$41.9 million. Now, this is a 12%  
25 return on -- strike that. An 11% return on the equity

1 component of the rate base.

2 Now, here's where we differ substantially  
3 with the Staff. Gulf says between \$44 million and \$51  
4 million, customers will get 40% of the difference. So  
5 if it earns up to 14.2%, customers could get as much  
6 as \$2.8 million more. So, Gulf would be earning  
7 \$51 million and you would reduce that back to the 3.7  
8 plus the 2.8 and it would get back, you know,  
9 somewhere in the mid 40's. Still far above the  
10 current authorized return.

11 What does the Staff say? The Staff says  
12 Gulf keeps the difference between \$42 million --  
13 \$42.6 million and \$49.6 million. Gets to keep it all.  
14 FIPUG, under its proposal, would say that anything  
15 over \$40.19 million would go first to the insurance  
16 reserve and the balance to customers.

17 **COMMISSIONER JACOBS:** That's your 12%,  
18 Mr. McWhirter?

19 **MR. McWHIRTER:** Beg your pardon?

20 **COMMISSIONER JACOBS:** That's your 12%?.  
21 That number represents your 12%?

22 **MR. McWHIRTER:** Yes. Yes, sir. So that's a  
23 very simplistic approach which I've taken for you and  
24 put it in terms of dollars rather than mysterious --  
25 not mysterious. But put it in percentage returns and

1 then you have to go back and find some numbers and  
2 apply the percentages to them to see what's really  
3 happening. I tried to point out for you what's really  
4 happening. What makes sense. 11% return makes sense.

5 I was intrigued by the last handout that  
6 Gulf gave you and they justify -- they justify keeping  
7 the return high, based on what's going to happen in  
8 the bond market.

9 Now, the high point where it goes way up to  
10 6.8% on the 30 year treasuries, that happens in the  
11 year 2001 so this is a projection. If you want to see  
12 where we are today, and you're making rates today, not  
13 in 2001, it's down here at the very lowest point on  
14 their exhibits.

15 Who is it that makes this projection? Well,  
16 it's Regional Financial Associates Inc. They may be a  
17 very fine firm. I'm not familiar with Regional  
18 Financial Associates Incorporated. But those are the  
19 kind of things that you would have if you had a  
20 hearing on what the appropriate return on equity would  
21 be. People like Regional Financial would come in and  
22 show what the projections are.

23 I'm suggesting to you that you do what is  
24 fair. What I propose to you, I think, is fair. If  
25 Gulf doesn't think it's fair, then it can come in and

1 ask for a hearing. I think that's essentially the  
2 same thing that Staff has done. Staff has made a  
3 proposal to you. If Gulf doesn't think it's fair,  
4 then you don't implement it. Gulf comes in and asks  
5 for a hearing.

6 But what we've done is we have taken a  
7 moment in time in which some action will be taken and  
8 the action you take is -- the most important thing to  
9 FIPUG is your treatment of regulatory assets. And we  
10 think the regulatory asset treatment that has been  
11 given by Gulf and Staff is not rational in today's  
12 times. This money is extra money the utility gets and  
13 there's no evidence that this extra money is doing  
14 anything to benefit Florida ratepayers. It's going to  
15 flow up to Southern Company and Southern Company can  
16 invest it internationally with no protection for  
17 Florida ratepayers.

18 **CHAIRMAN GARCIA:** Thank you.

19 **COMMISSIONER DEASON:** I have one question.  
20 Mr. McWhirter, what was your sixth point? Number six?  
21 Was it concerning refinancing costs?

22 **MR. McWHIRTER:** \$18.9 million was spent in  
23 order to get a lower interest rate. They call that  
24 loss on refinancing. I would suggest to you that  
25 18.9% is an expenditure that was made in order to

1 achieve a lower return over a longer period of time,  
2 and probably the net present value of that amount of  
3 money is far less than you're asking current  
4 ratepayers to pay. So I'm suggesting to you that you  
5 don't treat that as a regulatory asset, but that you  
6 just use your normal practice of plowing that into the  
7 debt component as an additional part of the debt.

8 **COMMISSIONER DEASON:** Thank you.

9 Mr. Mailhot, how are we treating that currently?

10 **MR. MAILHOT:** How are we treating the loss  
11 on reacquired debt?

12 **COMMISSIONER DEASON:** Yes. Loss on  
13 reacquired debt.

14 **MR. MAILHOT:** Under Staff's proposal or --

15 **COMMISSIONER DEASON:** How is the company  
16 currently accounting for it and then how does Staff  
17 address it?

18 **MR. MAILHOT:** Okay. I believe the company  
19 amortizes it over the remaining life of the retired  
20 debt.

21 **COMMISSIONER DEASON:** So the company is  
22 currently doing what Mr. McWhirter says should be  
23 done?

24 **MR. MAILHOT:** That's correct.

25 **COMMISSIONER DEASON:** Okay. And does Staff

1 address it at all in its proposal?

2 **MR. MAILHOT:** Yes. In Staff's proposal, if  
3 the company moves into the sharing range, a portion of  
4 that sharing would go to write off this loss more  
5 quickly.

6 **COMMISSIONER DEASON:** But only if the  
7 sharing range is reached?

8 **MR. MAILHOT:** That's correct.

9 **COMMISSIONER DEASON:** Okay. Thank you.

10 **COMMISSIONER CLARK:** Mr. McWhirter, you  
11 indicated that you thought that ROE should be the same  
12 as FP&L. And as I understood, I think what Staff was  
13 recommending, there ought to be some recognition of  
14 the fact that they carry less equity than FP&L. Do  
15 you have any response to that?

16 **MR. McWHIRTER:** Staff says that it should be  
17 11.2 or lower. They selected 11.2 because it was a  
18 number that would move towards settlement. I don't  
19 think there's any magic in that number. They thought  
20 it should be lower as I understand their memorandum.

21 **COMMISSIONER CLARK:** Well, let me ask you  
22 this question. Do you think any adjustments should be  
23 made to recognize the fact that they carry lower  
24 equity?

25 **MR. McWHIRTER:** Yes. I agree that there is



1 some differential in risk. I think the 11% that was  
2 chosen for Florida Power & Light was a settlement  
3 number that's higher than the current cost of debt.  
4 And I think this exhibit, if you cut it off at current  
5 times rather than projecting it to the future -- and  
6 what you do when you set rates is you look at  
7 historical plus a short projection to the future --  
8 you'll see that the cost of debt have gone down, down,  
9 down, and it's now 5.5% on 30 year treasury.

10 **COMMISSIONER CLARK:** Then your position is  
11 that because some time has passed since we made a  
12 decision in FP&L -- I don't know how long that is. A  
13 month?

14 **MR. McWHIRTER:** I don't think you ought to  
15 look at FP&L. I think you need to look -- this whole  
16 thing --

17 **COMMISSIONER CLARK:** Let me ask you a  
18 question. You suggested that the ROE be the same as  
19 what we set for FP&L. I thought I heard you say that.

20 **MR. McWHIRTER:** Yes. That's a settlement  
21 number, yes. I'm not suggesting that's the right  
22 number, but I suggest to you that if you had a rate  
23 case it would be a lower number on current conditions  
24 and, therefore, that's a good settlement number. I  
25 think Gulf will buy off on it.

1                   **COMMISSIONER DEASON:** But you referred us to  
2 one of Gulf's handouts. I assume you also received  
3 the handout entitled Equity Ratio Analysis?

4                   **MR. McWHIRTER:** Yes.

5                   **COMMISSIONER DEASON:** And according to this,  
6 Gulf is making the argument that their difference in  
7 equity ratio should justify a 47 basis point increase  
8 above whatever is appropriate for Florida  
9 Power & Light. Do you agree or disagree with this?

10                  **MR. McWHIRTER:** Well, no. I don't.

11                  **COMMISSIONER DEASON:** Don't agree.

12                  **MR. McWHIRTER:** Well, the 6.75 is merely --  
13 they subtracted 49% ratio from 55% ratio and then they  
14 multiplied it by 7. I don't know if that's some holy  
15 mystery number or if that is a number that is  
16 calculated based on what they think overall returns  
17 should be. Actually, it might be greater if you use  
18 7.4.

19                         But, all this stuff is fiction. The thing  
20 that is important to stockholders and investors is  
21 what's happening at Southern Company. And Southern  
22 Company is where the money comes in from investors.  
23 They're paying 8.32% for preferred stock. Well, those  
24 people are investors. Maybe there ought to be some  
25 kind of revision of that. Maybe they ought to borrow

1 money at 6.6 and pay off the preferred stock if they  
2 can. That's imprudent in today's market, I'm pretty  
3 sure.

4 **COMMISSIONER DEASON:** Mr. Stone, let me ask  
5 you, and you may want to refer this to one of your  
6 experts. The factor of 7, which is applied to the  
7 6.75 percent differential in equity ratio, how is that  
8 factor determined?

9 **MR. STONE:** I'll touch on that briefly, but  
10 I believe Mr. Scarbrough can elaborate on it. It was  
11 calculated -- the first time it was calculated was by  
12 Dr. Gene Briggum approximately 12 years ago. And he  
13 did it based on an empirical analysis of other  
14 utilities and their returns and examined the betas  
15 involved. Dr. Vander Wiede, as shown in his  
16 affidavit, has updated and done another study --  
17 empirical study and he came up with that quantified  
18 difference based on empirical analysis in the  
19 marketplace. Not sure if Mr. Scarbrough has anything  
20 else he wants to add to that.

21 **MR. SCARBROUGH:** Mr. Stone, is exactly  
22 right. There was a study done by Dr. Gene Briggum  
23 through the Public Utility Research Center, University  
24 of Florida, and I understand it was at the request of  
25 this Commission. I haven't verified that, but that

1 was 12 years ago. And then Dr. Vander Wiede, in  
2 recent testimony has -- has done a new empirical study  
3 on the same issue and that whole purpose was, what  
4 does the impact of leverage have on the cost of  
5 equity.

6 They both arrived at the same conclusion,  
7 that for every 1% increase in the leverage for  
8 electric utility, that the cost of equity should be  
9 increased by 7 basis points.

10 **COMMISSIONER DEASON:** What is Staff's  
11 viewpoint on that?

12 **MR. LESTER:** We constructed a leverage  
13 formula using our models. Same manner that we used --  
14 for the water and wastewater leverage formula. And  
15 our conclusion to reach 11.2 midpoint is we basically  
16 are looking at the 11% for Florida Power & Light and  
17 then adding 20 basis points, which is appropriate  
18 given that leverage formula we used. I think  
19 Dr. Vander Wiede's 7 point proposal, that's just a  
20 conclusion that he reached in his study. I simply  
21 disagree. We're doing -- going with our leverage  
22 formula.

23 **COMMISSIONER DEASON:** So under our leverage  
24 formula there's basically about 20 points can be  
25 justified -- 20 basis points can be justified for the

1 difference in equity ratio?

2 **MR. LESTER:** Yes, sir.

3 **COMMISSIONER DEASON:** Between Florida  
4 Power & Light and Gulf?

5 **MR. LESTER:** Yes, sir.

6 **COMMISSIONER DEASON:** Let me ask you this.  
7 What equity ratio did you use in your analysis? Was  
8 it as reported in financials or was it as adjusted by  
9 the PSC for eliminating the nonutility investment 100%  
10 from equity?

11 **MR. LESTER:** I'm using the 49% which is not  
12 adjusted for the nonutility investment.

13 **COMMISSIONER DEASON:** And it would be  
14 approximately 48% after that adjustment?

15 **MR. LESTER:** Yes, sir.

16 **COMMISSIONER DEASON:** Okay.

17 **MR. LESTER:** I believe it only makes a 4  
18 basis point difference if you go down to the 48.

19 **COMMISSIONER DEASON:** In your leverage  
20 formula?

21 **MR. LESTER:** Yes, sir.

22 **COMMISSIONER DEASON:** If you assume the 7  
23 was correct, then it would be -- it would be something  
24 greater than that? It would be about 7 basis points  
25 or how much would it be?

1           **MR. LESTER:** I believe only 3 or 4 basis  
2 points higher if you use the 48% equity ratio.

3           **COMMISSIONER DEASON:** Yeah, but what I'm  
4 saying is -- let me ask Gulf Power. Your analysis  
5 that you're using, your equity ratio analysis, I  
6 assume you're using your as reported equity ratio  
7 since you oppose the adjustment to remove it 100% from  
8 equity. So you're 49.8% does not reflect any  
9 adjustments to your equity ratio as a result of the  
10 nonutility investment?

11           **MR. SCARBROUGH:** No. That's the actual  
12 ratio.

13           **COMMISSIONER DEASON:** All the presentations  
14 are concluded; is that correct?

15           **CHAIRMAN GARCIA:** I believe so.

16           **COMMISSIONER DEASON:** Did Staff want to  
17 respond to anything Mr. McWhirter said or --

18           **MR. MAILHOT:** Yes. We have just one or two  
19 brief comments. In our initial recommendation and  
20 proposal that was presented at the March 16th agenda  
21 conference, Staff had crafted a plan based primarily  
22 on the Commission's prior decision in BellSouth with  
23 some modification to recognize what had been done in  
24 the Georgia Power case. And when we did that, we  
25 crafted what we thought was an appropriate plan at the

1 time.

2 **COMMISSIONER CLARK:** Some recognition of  
3 what happened in the Georgia Power case.

4 **MR. MAILHOT:** Yes.

5 **COMMISSIONER CLARK:** Okay.

6 **MR. MAILHOT:** In terms of a couple of the  
7 components of the plan. So, primarily what was  
8 presented at that conference was a combination of the  
9 two plans. It was probably 90% Southern Bell and 10%  
10 Georgia Power.

11 And we thought that the plan we presented  
12 was reasonable in terms of setting up a three year  
13 plan and I think at the time, one of the most critical  
14 components of starting a plan is where you set the  
15 company's earnings to begin with, and in that  
16 recommendation we set the company's earnings at 11.2%  
17 return on equity.

18 **COMMISSIONER CLARK:** Can I interrupt you a  
19 minute?

20 **MR. MAILHOT:** Yes.

21 **COMMISSIONER CLARK:** Just what exactly --  
22 did I miss it in the Staff's write-up about what part  
23 you sort of developed in light of the Georgia Power  
24 decision?

25 **MR. MAILHOT:** Well, essentially, it was one

1 component of the plan that had to do with productivity  
2 factors. In BellSouth's plan, the way the plan worked  
3 was the productivity factors were assumed for the  
4 next -- each of the next multiple years in the plan.  
5 BellSouth was required to reduce rates, for example,  
6 in years two and three of the plan regardless of  
7 earnings, you know, whether earnings improved or, you  
8 know, went down hill. No matter what, they had to  
9 reduce rates in the subsequent years of the plan.

10 In Georgia Power's case, what happened was,  
11 the company only had to -- the productivity factor  
12 only kicked in if the company's earnings hit a certain  
13 level. Okay. And the way that worked was in Georgia  
14 Power's plan, if the company earned 12.5% return on  
15 equity in years two and three --

16 **COMMISSIONER CLARK:** Go slower. Go slower.  
17 Say that again.

18 **MR. MAILHOT:** Okay. In years two and three  
19 of the Georgia Power plan, if the company's earnings  
20 got to 12.5% return on equity, the first \$50 million  
21 above that 12.5% had to go -- was not shared. It  
22 essentially went 100% towards writing off regulatory  
23 assets.

24 What that does, essentially, is that the  
25 company doesn't start sharing until they actually



1 improve earnings above the sharing point.

2 **COMMISSIONER CLARK:** All right. So the  
3 assumption being that that would be a productivity  
4 factor.

5 **MR. MAILHOT:** Essentially that's the way it  
6 works. Okay. And that, in a sense, is more  
7 conservative because if the company didn't earn 12.5  
8 then they wouldn't have to put anything towards  
9 regulatory assets, any additional money. As opposed  
10 to like in the BellSouth case --

11 **COMMISSIONER CLARK:** Where no earnings is  
12 taken out.

13 **MR. MAILHOT:** Right. Even if earnings went  
14 down they still had to reduce rates.

15 **COMMISSIONER CLARK:** Okay.

16 **MR. MAILHOT:** So that was kind of one of the  
17 features that we incorporated from the Georgia plan.

18 **COMMISSIONER CLARK:** And that's -- is that  
19 what we incorporated in our plan?

20 **MR. MAILHOT:** Yes, we did. It's not  
21 specified as a productivity factor, but it's part of  
22 the plan. It's part of our plan.

23 **COMMISSIONER CLARK:** And that is the  
24 reference to -- I'm looking at the chart somebody  
25 developed.

1           **MR. MAILHOT:** Yes. On Item 5.

2           **COMMISSIONER CLARK:** Item 5. That means --  
3 what does that mean?

4           **MR. MAILHOT:** Okay. Staff's plan, in our  
5 revised proposal, in the current recommendation,  
6 there's a productivity factor included where,  
7 essentially, if the company earns 12.2% then the first  
8 \$2 million above that level goes into the storm damage  
9 reserve.

10           **COMMISSIONER DEASON:** Before any sharing  
11 begins?

12           **MR. MAILHOT:** Before any sharing begins.  
13 But if the company doesn't reach 12.2%, then they  
14 don't have to do anything.

15           Anyway, our revised plan, Staff has moved  
16 essentially from targeting earnings at 11.2% return on  
17 equity, which we thought was appropriate, you know,  
18 based on the Commission's prior decisions, to  
19 targeting earnings at 11.8%. Now, this is 60 basis  
20 points above where we think earnings should be  
21 targeted. And you can ascribe that 60 basis points,  
22 you know, to a number of reasons. I mean, you can say  
23 it's for compromise. You can say it's for, you know,  
24 the company's -- you know, all the reasons the  
25 company's pointed out they should be rewarded. I

1 mean, for whatever reason, you know, we are setting or  
2 targeting earnings above what we think, you know,  
3 would actually be appropriate in our proposal.

4           The only other thing I'd like to say is, you  
5 know, you already brought up is, the productivity  
6 factor. In the plans that have been approved in the  
7 past productivity factor is an integral part of the  
8 plan. And the company hasn't proposed anything in  
9 that area. They don't even mention it as, you know,  
10 any kind of a difference between Staff and the  
11 company. We think it's important to include a  
12 productivity factor in any plan.

13           One other thing the company mentioned is the  
14 treatment of nonutility and the third floor. The  
15 company's indicated that those two things, you know,  
16 that we're just revisiting both of them and that there  
17 is no difference between them.

18           Staff would say that, you know, since the  
19 last rate case the treatment of the third floor was  
20 determined I think at that time to be essentially  
21 nonused and useful. Staff this year reviewed the use  
22 of the third floor. Sent an auditor over there to  
23 physically inspect the third floor. And although it  
24 may be questionable as to whether it's 100% used and  
25 useful at this point in time, Staff believes that it

1 is being used in large part, and so we think that  
2 there is a change in circumstances since the time of  
3 the last rate case involving the third floor.

4 So, we see that item as being significantly  
5 different than the treatment of the nonutility.  
6 There -- I don't think we believe there is any real  
7 change in circumstances since the last rate case. And  
8 I think that's all. Do you have anything else?

9 **MR. LESTER:** If I could just respond briefly  
10 to the ROE concerns. The company raised the concern  
11 of business risk and in the last utility credit report  
12 that Standard Reports issued for Gulf, which would be  
13 in November of '97, they said that Gulf Power's heavy  
14 concentration on the residential class mitigates  
15 concerns regarding the company's dependence on  
16 military and cyclical demand. Also regarding --

17 **COMMISSIONER CLARK:** I'm sorry. Would you  
18 read that again and who is it from?

19 **MR. LESTER:** This is from Standard Reports  
20 from the utility credit report. The sentence is,  
21 "Gulf Power's heavy concentration on the residential  
22 class mitigates concerns regarding the company's  
23 dependence on military and cyclical industry related  
24 demand." It goes on to say, "the presence of the  
25 contracts with military customers, as well as

1 projected growth in the military employment and load  
2 through the year 2001, also offsets those concerns."

3           You can go through these reports and pick  
4 out, you know, anything you want to favor sometimes.  
5 But I think what it's trying to say is that the  
6 company has enough of a residential base to offset any  
7 concerns regarding, you know, Gulf's having the  
8 military base as its customers.

9           **COMMISSIONER CLARK:** Do we know what portion  
10 of their revenues come from the military base or --

11           **MR. LESTER:** I believe it's about 15% from  
12 military and industrial.

13           **COMMISSIONER CLARK:** And what -- what  
14 additional residential percentages is somewhat  
15 dependent on the 15%?

16           **MR. LESTER:** It would be somewhat  
17 interrelated, yes. But they're also forecasting a  
18 growth in military employment, in a sense.

19           **MR. STONE:** Commissioner Clark, with regard  
20 to the reliance on the industry and military, at  
21 Page 22 of our filing on March 2nd, there is some  
22 discussion of that. And it talks in some detail about  
23 the numbers. It may not be precisely the number that  
24 you were looking for as an answer, but it does give  
25 some numbers about percentage of our sales. It's

1 interesting to note that Gulf's reliance is far  
2 different than the other utilities in Florida on the  
3 military and on industrial sales. And that was the  
4 difference we were trying to point out with regard to  
5 the differences in relative business risk.

6 **COMMISSIONER DEASON:** Mr. Stone, though, you  
7 have no nuclear generation, correct?

8 **MR. STONE:** This is true.

9 **COMMISSIONER DEASON:** Let me ask Staff a  
10 question, and here once again, I'm referring to the  
11 side-by-side comparison which Staff prepared. And  
12 it's Item 3 which looks at the means of getting the  
13 earnings down to a targeted level. And, of course,  
14 Staff's target is 11.8 and the company's target is  
15 12.2. So I realize there is a difference there.

16 But Staff's is recommending that regulatory  
17 assets be written off at \$2.26 million a year. And  
18 that includes, according to the information that I  
19 have, the inclusion of the third floor and rate base  
20 and the depreciation and amortization of that. Also,  
21 accelerated recovery of the regulatory asset  
22 associated with that, and FAS 109 cost, for a total of  
23 \$2.26 million, is that correct?

24 **MR. MAILHOT:** Yes.

25 **COMMISSIONER DEASON:** Okay. The -- describe

1 for me the FAS 109 cost and why that needs to be  
2 included in a rapid recovery?

3 **MR. MAILHOT:** What that is, is essentially  
4 before -- I'm not a tax expert. But before we went to  
5 full normalization, certain tax items were flowed  
6 through to the benefit of the customers and when we  
7 went to full normalization, those flow through of  
8 prior benefits now must be collected from current  
9 customers, so it's essentially -- this is one of those  
10 cases where prior customers benefitted years ago and  
11 the way it's being recovered currently is, over the  
12 remaining life of property, and it has anywhere from  
13 probably a 10 to 15 years future recovery period.

14 This item in particular, the Commission  
15 approved for accelerated recovery for FP&L. As an  
16 item -- essentially it's a past cost that's currently  
17 being collected from ratepayers.

18 So we think it's appropriate since there is  
19 no -- since it's a past cost it should be recovered as  
20 quick as possible.

21 **COMMISSIONER DEASON:** Do these amounts  
22 appear as a debit balance, deferred taxes?

23 **MR. MAILHOT:** The regulatory asset does.

24 **COMMISSIONER DEASON:** Yes. So by writing  
25 these off, you remove that which, in essence, has the

1 net effect of reducing the company's rate base in the  
2 long run?

3 **MR. MAILHOT:** Right.

4 **COMMISSIONER DEASON:** Okay. Now, describe  
5 to me why you've chosen to accelerate the recovery of  
6 the regulatory asset associated with the third floor  
7 up front and delay recovery of the loss on reacquired  
8 debt until there are earnings available to do that?  
9 You had to draw the line somewhere?

10 **MR. MAILHOT:** Yes. And these were small  
11 items that, you know, seem to have a long life. I  
12 mean, if you were to use the remaining life of the  
13 third floor it would be spread out over probably 25  
14 years as the remaining life. The same thing with the  
15 tax item. It has, you know, a 10 to 15 year remaining  
16 life and it's, you know, like I said, that's  
17 definitely a past cost.

18 So, I mean, these are small items that, you  
19 know, we thought were appropriate to deal with as  
20 quick as possible.

21 **COMMISSIONER DEASON:** How much is the loss  
22 on reacquired debt? I think Mr. McWhirter quoted  
23 \$18.9 million?

24 **MR. MAILHOT:** It's approximately that at the  
25 end of last year.



1                   **COMMISSIONER DEASON:** And right now that's  
2 being recovered over the life of the debt issued?

3                   **MR. MAILHOT:** I believe it's the life of the  
4 old debt, the debt retire.

5                   **COMMISSIONER DEASON:** The debt that was  
6 retired?

7                   **MR. MAILHOT:** Yes.

8                   **COMMISSIONER DEASON:** And how many years is  
9 that doing that?

10                  **MR. MAILHOT:** I would say on average that's  
11 probably in the neighborhood of 12 to 15 years.

12                  **COMMISSIONER JACOBS:** Going to the question  
13 Mr. McWhirter raised on the ceiling, we have  
14 historically had a 13 as a ceiling for them, right?  
15 And the proposal here is that that be 14.2; is that  
16 correct?

17                  **MR. MAILHOT:** Yes.

18                  **COMMISSIONER JACOBS:** With the caveat of the  
19 sharing after 12.2?

20                  **MR. MAILHOT:** Right. That's correct.

21                  **COMMISSIONER JACOBS:** And essentially what  
22 we do when we give them the target of 11.8 is we give  
23 them kind of a jump start on that, don't we? We kind  
24 of say, you know, you're earnings are going to be able  
25 to start off at a point larger than we think the

1 midpoint is, is that correct?

2 **MR. MAILHOT:** That's correct. That's about  
3 60 basis points above where we think rates should be  
4 targeted.

5 **COMMISSIONER JACOBS:** Okay.

6 **MR. MAILHOT:** Or at least in our previous  
7 recommendation.

8 **COMMISSIONER JACOBS:** Now, there was some  
9 statistics cited here which would indicate that -- I  
10 think the number that was 11 -- I think the point was  
11 going to the midpoint. I may be mistaken, but I think  
12 that there was some data which was presented and I'm  
13 trying to -- the chart. That's what it was. Which  
14 would indicate that companies were having midpoints --  
15 I'm sorry. It was in the file. That's what it was.  
16 It was at Page 23. 23 of the filing. What's your  
17 response to this data in comparison to what your  
18 recommendations are?

19 **MR. LESTER:** I think I just disagree. I  
20 looked at my chart, which would be on Page 11, I  
21 believe.

22 **COMMISSIONER JACOBS:** Right.

23 **MR. LESTER:** And, I mean, we've assembled  
24 the returns using a reporting service and then we've  
25 added the top two based on news reports. Those are

1 the reports that we're finding in terms of around the  
2 country. I'm not sure of their source of data. Now  
3 we, obviously, conflict.

4 **COMMISSIONER JACOBS:** Okay.

5 **COMMISSIONER CLARK:** I just want to be  
6 clear. On your chart, which shows your revised plan  
7 and Gulf's revised plan, with respect to, you set the  
8 rates at 11.8%, would that be correct? Or do the  
9 rates get left where they are?

10 **MR. MAILHOT:** In Staff's plan, earnings get  
11 targeted at 11.8%.

12 **COMMISSIONER CLARK:** Okay. So the rates  
13 stay where they are?

14 **MR. MAILHOT:** It's partly through just a  
15 credit on the bill and partly through write-offs.

16 **COMMISSIONER CLARK:** Okay. And as I  
17 understand it, under 3(A) and (B), those things get  
18 done regardless of where the earnings are?

19 **MR. MAILHOT:** In Staff's plan?

20 **COMMISSIONER CLARK:** Yes.

21 **MR. MAILHOT:** Yes.

22 **COMMISSIONER CLARK:** And the same is true  
23 for Gulf, except when you get down to the year 2001.  
24 Then it has an earnings test.

25 **MR. MAILHOT:** Right.

1                   **COMMISSIONER CLARK:** Okay.

2                   **COMMISSIONER DEASON:** Commissioners, I think  
3 that we've got to answer a basic question. And that  
4 is, do we want to try to come out with a proposal.  
5 We've got Staff's proposal. We've got the company's  
6 proposal. We've got Mr. McWhirter's proposal.  
7 They're all different. Some things are alike. Some  
8 things are different.

9                   I guess the question is, do we want to come  
10 out with our own proposal, in effect. Issue that as  
11 PAA and basically test the waters with it and see if  
12 anybody wants to protest it. Obviously, if it's  
13 protested, it goes away. And, I assume at that point  
14 then, we could either litigate that PAA or simply just  
15 decide to go to a rate case. That would be our  
16 options, Mr. Elias?

17                   **MR. ELIAS:** Yes.

18                   **COMMISSIONER DEASON:** Okay. I'm of the  
19 opinion that we should try our own proposal, issue it  
20 as a PAA and see what the reaction is. It may be  
21 protested, and that's fine if it is. It may be that  
22 nobody is happy with it but everybody can live with it  
23 and say, we can go forward from this. And that's what  
24 I'd like to attempt to do.

25                   And it seems to me that if we're willing to

1 do that, one of the -- the key factors we've got to  
2 decide before we decide any of the other  
3 particulars -- and there are a number of things that  
4 we need to address. But the key factor we need to  
5 decide up front is the targeted rate of return we're  
6 going to use. We need to set a floor and a midpoint.  
7 We also need to set a target earnings level to  
8 currently set at this time.

9           And also if we think that there should be  
10 some type of sharing, which I think there is, I think  
11 it provides the correct incentives, what that sharing  
12 point is going to be. And I think that we've got to  
13 agree on that before we even get to all of the  
14 particulars because if we can't agree on that, there  
15 is no need even talking about all of the particulars.

16           So, just for trying to throw something out  
17 and see if we can reach any type of consensus on this,  
18 I'd be willing to suggest, and open it up to  
19 discussion, but my suggestion would be that we would  
20 establish a floor of 10.5%, a midpoint of 11.5%. We  
21 would target our rates or to set earnings at 12.0%.  
22 We would initiate sharing at 12.5%. And that sharing  
23 would cease at 14% at which time any earnings in  
24 excess of that would be determined by the Commission  
25 in the future, but it would be utilized by the

1 Commission either as refunds or as write-off of  
2 regulatory assets. But we could -- if we find  
3 ourselves in that position, which I think would be a  
4 fortunate position to find ourselves in, we can deal  
5 with that at that time.

6 **COMMISSIONER CLARK:** Second.

7 **CHAIRMAN GARCIA:** If there is no discussion,  
8 we have a motion and a second. All those in favor  
9 signify by saying aye.

10 **COMMISSIONER JACOBS:** The midpoint again  
11 was?

12 **CHAIRMAN GARCIA:** Midpoint was --

13 **COMMISSIONER DEASON:** Midpoint was 11.5 but  
14 we would target earnings. I want to make it clear.  
15 We would target earnings at 12% which is above the  
16 midpoint. It's halfway between the midpoint and the  
17 high end. And the reason that I'm suggesting that is,  
18 first of all, as Staff has indicated and I think some  
19 of the parties, we're here in an attempt to reach an  
20 agreement. And there's a little bit of negotiating  
21 factors involved. And while we don't negotiate, our  
22 Staff does and Mr. McWhirter is involved in those  
23 things.

24 I think that, given the performance of this  
25 company, the fact that their rates are low, customer

1 satisfaction is high, customer complaints are low,  
2 reliability is high, that -- and that this would, if  
3 it is issued and it is not protested, it would negate  
4 the need for a rate proceeding, which means that we  
5 would capture the benefits of this proposal  
6 retroactive to the beginning of the year. If we go to  
7 a rate proceeding, we're looking at least eight months  
8 or longer from now before we capture any benefits.

9           So there's kind of a sharing so to speak of  
10 the benefits. We also avoid a rate proceeding and the  
11 rate case expense associated with that. I think this  
12 company's rate case expense the last time they filed a  
13 rate case was somewhere in the neighborhood of  
14 \$1 million. So, it's just kind of a massage factor to  
15 recognize all of those things.

16           **COMMISSIONER JACOBS:** Can I ask a question  
17 real quickly? Basically to Staff. First of all, let  
18 me say this. I agree in concept of where you're  
19 going. I think there is an indication that this  
20 company has operated effectively. My concern is that  
21 we're essentially giving them a productivity incentive  
22 that is not real quantified, not very well quantified.

23           And my thought is, and the question I have  
24 for Staff is, how does this relate to the idea of  
25 giving them -- versus the 11.2, giving them the 11.5?

1 How -- is there any correlation to that, to whether or  
2 not there is a productivity factor or not? Are they  
3 different concepts or do they play into one another or  
4 not?

5 **MR. LESTER:** The idea of a productivity  
6 factor is really separate from, you know, where you  
7 set rates or what your authorized ROE is. They're  
8 somewhat related, but they're separate too.

9 **COMMISSIONER JACOBS:** Okay. So, there is  
10 no -- we wouldn't do anything if we were to do one  
11 versus the other? They're totally different --  
12 different atmospheres. And the reason I'm thinking  
13 that is at least there you have something that you can  
14 begin to say, we're giving this company this addition  
15 because we -- of this factor. That's the only thing  
16 I'm searching for.

17 **COMMISSIONER CLARK:** I think, if understood  
18 the motion from, and the explanation from Commissioner  
19 Deason is, we're recognizing some -- the positives  
20 things of that company; low rates, low customer  
21 complaints. And, in my view, recognizing the  
22 relatively lower amount of equity. What was the third  
23 thing?

24 **COMMISSIONER DEASON:** Low customer  
25 complaints, high reliability and low rates.



1           **COMMISSIONER CLARK:** That was it. High  
2 reliability.

3           **COMMISSIONER DEASON:** Lower equity ratio.

4           **COMMISSIONER CLARK:** I think those factors  
5 indicate setting the midpoint at a higher level. And  
6 I would point out that we have been quick to penalize  
7 this company when they don't live up to those  
8 productivity issues.

9           **COMMISSIONER DEASON:** Let me also indicate  
10 that if we were in a rate proceeding and if by just  
11 some chance we were to determine that 11.5 is the  
12 correct amount, we would set rates at 11.5, but we  
13 also would put a whole -- 100 basis points on the  
14 upper end of that and we would allow the company to  
15 earn up to 12.5 and would not say anything to the  
16 contrary. We'd say those are still reasonable  
17 earnings.

18           Under this proposal, we would be setting  
19 rates at 12.0 and allowing the company to earn up to  
20 12.5, which is only a half a percentage point or 50  
21 basis points. Whereas, when we normally set rates, if  
22 we were in a rate proceeding, it would be 100 basis  
23 points on that end. So, here again, it's kind of --

24           **COMMISSIONER CLARK:** You mean where sharing  
25 begins.

1           **COMMISSIONER DEASON:** Yes. Sharing begins  
2 at 12.5. They can still have bottom line earnings  
3 above 12.5 because there is a sharing percentage which  
4 we will address later on. But I would also point out  
5 that that only begins if there are efficiencies or  
6 enhanced revenues or reduced costs or something  
7 happens and there are going to be additional benefits  
8 for customers too, and that that's what incentives are  
9 all about is to provide an incentive to management,  
10 hopefully customers are made better off by those  
11 incentives.

12           **COMMISSIONER JACOBS:** And that's exactly the  
13 point. I was persuaded by Mr. McWhirter's point that  
14 if there are going to be efficiencies gained then they  
15 ought to flow through. I don't want to belabor it, if  
16 that's not a way of doing this. I agree in concept  
17 with the idea that there are things here that the  
18 company can be regarded on. I'm searching for a way  
19 to make that a bit more quantified. But if we can't  
20 do that then I'm --

21           **CHAIRMAN GARCIA:** All right. We have a  
22 motion and a second.

23           **COMMISSIONER CLARK:** Well, let me -- you  
24 made a motion on the ROE and that's not really a  
25 motion on any of the issues, so do we need to wait or

1 are you moving that --

2 **COMMISSIONER DEASON:** You know, we may want  
3 to look at this as a package. If we can all kind of  
4 agree that at least that's a framework that we can  
5 look at. Because to me that's the key, is to  
6 determine an ROE before you start looking at any  
7 particulars. And I'm willing to do it either way.

8 **COMMISSIONER CLARK:** Well, I guess I'm  
9 willing to second a motion that uses those parameters  
10 with respect to the ROE and sharing and then moving  
11 Staff's recommendations on the write-off of the  
12 assets, the credits to the customers, with the  
13 understanding that it gets adjusted by the new sharing  
14 points.

15 **COMMISSIONER DEASON:** Okay. So are you  
16 moving now to Item 3 on the side-by-side comparison?

17 **COMMISSIONER CLARK:** I guess what I'm  
18 suggesting is -- yeah, I guess I am moving to Item 3.

19 **COMMISSIONER JACOBS:** And the number that  
20 we're going to set them at is what again?

21 **COMMISSIONER CLARK:** I'm okay with Staff's  
22 recommendations with respect to 3, 4, 5 and 6, but  
23 with the new proposals on the ROE.

24 **MR. MAILHOT:** We need a little bit of  
25 clarification because --

1           **COMMISSIONER DEASON:** The numbers are going  
2 to change because you get a new target point.

3           **COMMISSIONER CLARK:** Yes. The actual  
4 figures will change as a result of the different ROEs.

5           **COMMISSIONER DEASON:** And I guess that was  
6 going to be my next question as to, if we target  
7 earnings at 12% as opposed to the Staff's recommended  
8 11.8, obviously, you cannot do everything Staff is  
9 recommending in Items 3(A) and 3(B). There's got to  
10 be something that's got to be reduced to make up that  
11 20 basis points differential.

12           And I guess my question to Staff is, is  
13 there still adequate earnings available to achieve the  
14 \$2.26 million and the \$3.5 million first year accrual  
15 to storm damage reserve, which is your Part A? Is  
16 there sufficient earnings to do that before we look at  
17 credit on the bills?

18           **MR. MAILHOT:** Yes. The difference, if I  
19 understand your proposal, is to target earnings at  
20 12%?

21           **COMMISSIONER DEASON:** Correct.

22           **MR. MAILHOT:** Okay. This analysis here is  
23 based on targeting earnings at 11.8%. The dollar  
24 difference between those two is \$1.2 million.

25           **COMMISSIONER DEASON:** \$1.2 million per year.

1           **MR. MAILHOT:** Per year. So, for example, I  
2 mean on this schedule, if you wanted to --

3           **COMMISSIONER DEASON:** So the \$7 million, in  
4 essence, would become what, \$5.8 million as opposed to  
5 7?

6           **MR. MAILHOT:** That's correct.

7           **COMMISSIONER DEASON:** And under your  
8 rational then that the first year accrual to the storm  
9 damage would be half of the 5.8 which would --

10          **MR. MAILHOT:** You could do it that way.  
11 That's a way to do it.

12          **COMMISSIONER CLARK:** Wait a minute. I'm  
13 misunderstanding. I thought there was also going to  
14 be a credit on the customer's bill and what I  
15 understand is in 1999 the credit would -- recognizing  
16 the fact that it's \$1.2 million less, it would be --  
17 is it \$2.3 million?

18          **COMMISSIONER DEASON:** What happens there --  
19 what Staff has done is they've done their regulatory  
20 asset write-off of \$2.26 million. Then they've taken  
21 what is left over and put that as customer credits.  
22 But they recognize that the 1999 customer credit will  
23 only be for a half of a year. So they've taken the  
24 other half of the year and recommended that it be  
25 recognized as an accrual to the property insurance

1 reserve.

2 **COMMISSIONER CLARK:** Okay.

3 **COMMISSIONER DEASON:** And if you reduce the  
4 \$7 million per year by \$1.2 million you're down to  
5 5.8.

6 (End of Tape 2, Side A.)

7 (Beginning Tape 2, Side B.)

8 **MR. MAILHOT:** That would be consistent with  
9 the current recommendation.

10 **COMMISSIONER JACOBS:** Do we -- is it  
11 possible to keep that customer credit close to the  
12 existing number? I'm thinking rather than having the  
13 credit, you'd keep that at three maybe and then do the  
14 other to the --

15 **COMMISSIONER DEASON:** Well, to achieve that  
16 you would have to basically reduce your \$2.26 million  
17 write-off of regulatory assets, and that basically  
18 consists of three things, which is the inclusion of  
19 the third floor and rate base and the associated  
20 depreciation and amortization of that; the accelerated  
21 amortization of the regulatory asset associated with  
22 the third floor; and the FAS 109 write-off.

23 **CHAIRMAN GARCIA:** With the motion, where is  
24 that credit now under your motion?

25 **COMMISSIONER DEASON:** Under my motion the

1 credit would be \$5.8 million a year. Well, I guess I  
2 haven't really made a motion. I'm trying to clarify.  
3 But following Staff's rationale, if you make the  
4 assumption you still want \$2.26 million a year in  
5 regulatory asset write-offs, then the only other  
6 alternative would be to reduce the customer credit  
7 from \$7 million to \$5.8 million.

8 **MR. MAILHOT:** That's correct for 2000 and  
9 2001. Staff's assumption here is that the credit is a  
10 monthly credit. But I mean, you could make it a once  
11 a year credit which was the company's proposal. I  
12 mean, in the sense of, I think they were planning on  
13 crediting the customer's bill all in one month of the  
14 year and if you do it that way, then you can just pick  
15 a dollar amount for 1999.

16 **COMMISSIONER DEASON:** But then you forego  
17 any accrual to the property insurance reserve.

18 **MR. MAILHOT:** Yes. That's the trade-off in  
19 1999, would be between the property insurance reserve  
20 and the credit.

21 **COMMISSIONER DEASON:** And I think it's  
22 important -- I know the company is proposing \$1  
23 million a year for three years or a total of  
24 \$3 million up-front increase in the property insurance  
25 reserve. Our Staff's recommending \$3.5 million but,

1 of course, that was with an 11.8% targeted earnings  
2 level.

3 I would hate to forego -- I think that  
4 that's something that we need to do up front so -- you  
5 know, if we want to modify this some, I guess, we can  
6 tinker with it, but I think it's important to have an  
7 accrual somewhere in the neighborhood of \$3 million  
8 over this period of time to the property insurance  
9 reserve.

10 **CHAIRMAN GARCIA:** Okay.

11 **COMMISSIONER DEASON:** So if we need a  
12 motion, -- I would move that we adopt Staff's  
13 recommendation for Item 3 in a side-by-side comparison  
14 except that the credits be reduced from \$7 million to  
15 \$5.8 million and that 1999 would be half of that as a  
16 customer credit and the other half of the \$5.8 million  
17 would be booked into the property insurance reserve.

18 **CHAIRMAN GARCIA:** Right. And then you --  
19 with the midpoint and the ROE that you -- with  
20 everything else that you stated.

21 **COMMISSIONER DEASON:** Right. That's  
22 correct.

23 **CHAIRMAN GARCIA:** So we understand the  
24 motion. Susan got a call from the Governor. He  
25 agrees also. So we've got a motion and a second. All



1 those in favor signify by saying aye. Aye.

2 **COMMISSIONER DEASON:** Aye.

3 **COMMISSIONER JOHNSON:** Aye.

4 **COMMISSIONER JACOBS:** Aye.

5 **COMMISSIONER CLARK:** I apologize.

6 **COMMISSIONER DEASON:** We also need to

7 address --

8 **COMMISSIONER CLARK:** What did we decide just

9 now?

10 **COMMISSIONER DEASON:** You voted for it. You

11 don't know?

12 **CHAIRMAN GARCIA:** You seconded it.

13 **COMMISSIONER CLARK:** I did not say aye,  
14 actually. Or if I side yes, I would be answering --

15 **CHAIRMAN GARCIA:** No. It was exactly what  
16 you had stated to tie in the Staff's proposal with  
17 Commissioner Deason's numbers.

18 **COMMISSIONER CLARK:** Okay. I just -- I  
19 think that's the correct thing to do. I just wanted  
20 to ask, where are we on the storm damage amount? Do  
21 we have in mind a figure that we think is appropriate  
22 to accrue to and how close are we?

23 **MR. MAILHOT:** Well, as far as I know, in the  
24 actual reserve, I think there is between \$1 million  
25 and \$2 million.

1                   **COMMISSIONER CLARK:** That's all that's  
2 there?

3                   **MR. MAILHOT:** Yes, as of the end of last  
4 year.

5                   **COMMISSIONER DEASON:** And we've targeted  
6 somewhere in the neighborhood of \$25 million to even  
7 perhaps \$30 million --

8                   **COMMISSIONER CLARK:** Okay.

9                   **MR. MAILHOT:** It's kind of controversial  
10 what the target is, but it's pretty large.

11                   **COMMISSIONER CLARK:** Okay.

12                   **CHAIRMAN GARCIA:** Okay. You wanted to make  
13 a second motion.

14                   **COMMISSIONER DEASON:** Well, we need to  
15 address the sharing percentages. There are some  
16 differences between our Staff and Mr. McWhirter and  
17 the company.

18                   I would simply suggest that we would just do  
19 it one-third, one-third, one-third, with the  
20 shareholders receiving one-third of any sharing,  
21 regulatory assets receive one-third, and then credits  
22 to customers would receive one-third. But -- and I'm  
23 open to negotiation.

24                   **COMMISSIONER CLARK:** Well, I guess the only  
25 thing that concerns me there is I think we need to get

1 the storm damage --

2           **COMMISSIONER DEASON:** Well, we're going to  
3 address that in the productivity factor to some  
4 extent, I think. Maybe we need to do those jointly  
5 because Staff's productivity factor takes \$2 million a  
6 year up front before sharing begins, in essence, and  
7 puts that into storm damage. I keep calling it storm  
8 damage reserve. I think it's property insurance  
9 reserve is the correct terminology, but we know what  
10 we're talking about.

11           **COMMISSIONER CLARK:** Okay. So what you're  
12 saying is that that is not included in the regulatory  
13 assets?

14           **COMMISSIONER DEASON:** Well, for the years  
15 2000 and 2001, that's correct. It's not part of  
16 regulatory assets. Well, it is too. Once we get  
17 sharing, Staff has identified the deficiency in the  
18 property insurance reserve as something that needs to  
19 be addressed with the sharing percentage that we  
20 determine when earnings exceed the 12.5%.

21           **COMMISSIONER CLARK:** Let me state it back to  
22 you. As I understand it, once we hit the sharing, an  
23 automatic \$2 million goes to the storm damage?

24           **MR. MAILHOT:** Right.

25           **COMMISSIONER CLARK:** And after that you

1 would go to the sharing of one-third, one-third,  
2 one-third.

3 **COMMISSIONER DEASON:** Well, Staff has  
4 identified a number of items that they think need to  
5 be addressed when we reach sharing. One of those is  
6 storm damage and another thing is the loss on  
7 reacquired debt, correct?

8 **MR. MAILHOT:** Yes.

9 **COMMISSIONER DEASON:** But you've got certain  
10 thresholds in there and you identify what triggers  
11 what and I don't really have a problem with what  
12 you're recommending, but we should remember though  
13 that Staff's recommendation on Item 5, the  
14 productivity factor, if we reach sharing, \$2 million  
15 per year would go into the storm damage reserve before  
16 you get your one-third, one-third, one-third or 40,  
17 30, 30, whatever you come up with.

18 **COMMISSIONER CLARK:** I guess I'm still not  
19 understanding it.

20 **COMMISSIONER DEASON:** Okay.

21 **COMMISSIONER CLARK:** The sharing -- when  
22 does the sharing start? When you hit --

23 **COMMISSIONER DEASON:** For 1999, it would --  
24 sharing would begin at 12.5%.

25 **COMMISSIONER CLARK:** All right. What about

1 2000 and 2001?

2 **MR. MAILHOT:** In 2000 and 2001, when  
3 earnings get to 12.5%, the next \$2 million of  
4 earnings --

5 **COMMISSIONER CLARK:** Okay.

6 **MR. MAILHOT:** -- goes to the storm damage  
7 reserve.

8 **COMMISSIONER CLARK:** All right.

9 **MR. MAILHOT:** As the productivity factor.

10 **COMMISSIONER CLARK:** And they the sharing  
11 begins?

12 **MR. MAILHOT:** Right.

13 **COMMISSIONER CLARK:** Then after that point  
14 it's one-third -- you're proposal is one-third,  
15 one-third -- okay.

16 **COMMISSIONER DEASON:** My proposal is  
17 one-third, one-third, one-third. But here again,  
18 that's --

19 **COMMISSIONER CLARK:** Regulatory assets back  
20 to customers and 33 to the company.

21 **MR. MAILHOT:** Correct.

22 **COMMISSIONER CLARK:** Okay. I'm okay with  
23 that.

24 **CHAIRMAN GARCIA:** That's a second.

25 **COMMISSIONER CLARK:** Yep.

1           **CHAIRMAN GARCIA:** We have a second. All  
2 those in favor signify by saying aye. Aye.

3           **COMMISSIONER DEASON:** Aye.

4           **COMMISSIONER CLARK:** Aye.

5           **COMMISSIONER JOHNSON:** Aye.

6           **COMMISSIONER JACOBS:** Aye.

7           **CHAIRMAN GARCIA:** Very good.

8           **COMMISSIONER DEASON:** I would move Staff on  
9 Item 5, productivity factor.

10          **COMMISSIONER CLARK:** Second.

11          **CHAIRMAN GARCIA:** There being no objection,  
12 show that approved.

13          **COMMISSIONER DEASON:** I would move Staff on  
14 Item 6.

15          **COMMISSIONER CLARK:** Second.

16          **CHAIRMAN GARCIA:** There being no objection,  
17 show that approved.

18          **COMMISSIONER CLARK:** So that for -- we would  
19 move Staff on Issue 1.

20          **MR. MAILHOT:** Okay.

21          **COMMISSIONER DEASON:** We would be denying  
22 Gulf's proposal.

23          **COMMISSIONER CLARK:** With respect to 2, we  
24 would move Staff as modified by those individual  
25 votes?

1           **COMMISSIONER DEASON:** Yes.

2           **CHAIRMAN GARCIA:** Correct. Do you want to  
3 show that like that, Mr. Elias, then? Show it moved  
4 and seconded --

5           **MR. ELIAS:** As modified.

6           **CHAIRMAN GARCIA:** No objection as modified.

7           **COMMISSIONER JACOBS:** Did it say what the  
8 floor was? Do we need to?

9           **MR. ELIAS:** There are other issues in this  
10 recommendation that need to be --

11           **CHAIRMAN GARCIA:** Okay.

12           **COMMISSIONER CLARK:** All right. And Issue 3  
13 and 4 are now moot.

14           **CHAIRMAN GARCIA:** Right.

15           **COMMISSIONER DEASON:** Until we determine if  
16 there is a protest or not.

17           **COMMISSIONER CLARK:** Right. Issues 3, 4 and  
18 5 actually.

19           **COMMISSIONER DEASON:** No, I think Issue 5 is  
20 an independent issue, I believe. At least my  
21 discussions with Staff they've indicated that's their  
22 belief.

23           **COMMISSIONER CLARK:** Okay. So we move Staff  
24 on --

25           **COMMISSIONER DEASON:** Move Staff on 5.

1           **CHAIRMAN GARCIA:** Is there a second?

2           **COMMISSIONER DEASON:** Well, Mr. Jenkins have  
3 something to say about that?

4           **MR. JENKINS:** Yes. I was sort of hoping  
5 that the outcome of this negotiation would be to  
6 resolve that docket with some of the agreements or  
7 some of the sharing. I can't give you the number  
8 because it's confidential, but it's not a large  
9 number.

10           **COMMISSIONER DEASON:** What is Gulf's  
11 position on Issue 5, the initiation of a review of the  
12 contract service arrangement?

13           **MR. STONE:** Commissioner, we are prepared to  
14 help the Commission in its review. We are confident  
15 we'll be able to justify that the actions taken in  
16 those contracts were prudent and within the concept  
17 approved by the Commission for our pilot program. We  
18 believe you will agree with that. We believe there  
19 will be no money subject to refund.

20           **CHAIRMAN GARCIA:** So let's keep it on that  
21 track, then.

22           **COMMISSIONER DEASON:** You're agreeing it  
23 should be done independent of whatever we do here?

24           **MR. STONE:** If that's the pleasure of the  
25 Commission, we're prepared to help with that.



1           **CHAIRMAN GARCIA:** Very good. We had a  
2 motion. I believe Susan moved it and Commissioner  
3 Deason seconded it. There being no objection, show  
4 Item 5 approved -- Issue 5 approved.

5           **COMMISSIONER CLARK:** I move Staff on Issue 6  
6 and 7.

7           **CHAIRMAN GARCIA:** Issue 6 and 7.

8           **COMMISSIONER DEASON:** Second.

9           **CHAIRMAN GARCIA:** Second. There being no  
10 objection, show those approved. Very good.

11           **COMMISSIONER DEASON:** Just ask the parties  
12 to look at the PAA order and I know nobody is going to  
13 be happy with that, but just weigh that against going  
14 to a rate case.

15           **CHAIRMAN GARCIA:** I want to thank the  
16 company and Staff for working through this as well as  
17 Mr. McWhirter. Thank you.

18           (Thereupon, the proceedings on Item 10 were  
19 concluded)

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STATE OF FLORIDA)  
:  
COUNTY OF LEON )

CERTIFICATE OF REPORTER

I, KIMBERLY K. BERENS, CSR, RPR, Official  
Commission Reporter,

Do hereby certify that I stenographically  
transcribed the said proceedings from tape recordings  
delivered to me by Commission Staff.

DATED this 22nd day of April, 1999.

*Kimberly K. Berens*  
KIMBERLY K. BERENS, CSR, RPR  
Official Commission Reporter  
(850) 413-6736

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