



Public Service Commission

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

DATE: MAY 25, 2000

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

FROM: DIVISION OF LEGAL SERVICES (CLEMONS) *DMC RVE*
DIVISION OF AUDITING AND FINANCIAL ANALYSIS (MERTA) *SM*
DIVISION OF ELECTRIC AND GAS (BREMAN) *JS DM 198 JDJ*

RE: DOCKET NO. 991834-EI - PETITION FOR APPROVAL OF DEFERRED ACCOUNTING TREATMENT FOR THE GULF COAST OZONE STUDY PROGRAM BY GULF POWER COMPANY.

AGENDA: 06/6/00 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\LEG\WP\991834R2.RCM

CASE BACKGROUND

At the November 22, 1999 hearing, in Docket No. 990007-EI, the Commission deferred a decision on the inclusion of the costs for the Gulf Coast Ozone Study ("GCOS") Program in Gulf Power Company's ("Gulf" or "the Company") Environmental Cost Recovery Clause ("ECRC") factor for 2000. On December 3, 1999, Gulf filed a petition for approval of deferred accounting treatment for the costs associated with GCOS. On March 6, 2000, the Commission issued Order No. PSC-00-0476-PAA-EI, authorizing recovery of the GCOS costs through the ECRC and authorizing recovery of only those annual costs of the GCOS in excess of the \$178,000 already in base rates for environmental studies. On March 27, 2000, Gulf filed a Request for Clarification/Modification of Order No. PSC-00-0476-PAA-EI or in the Alternative Petition for a Formal Proceeding.

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DISCUSSION OF ISSUES

ISSUE 1: Should Gulf Power Company's request for clarification and/or modification of Order No. PSC-00-0476-PAA-EI or in the Alternative Petition for a Formal Proceeding be granted?

RECOMMENDATION: Yes. The Commission should grant Gulf Power Company's request for modification of Order No. PSC-00-0476-PAA-EI. Gulf should recover only those annual costs of the GCOS in excess of the amount included in the approved rate case test year budget reduced by the amount actually spent on environmental studies as an operating expense during the relevant ECRC recovery period. If the amount reflected in surveillance reports for expenditures on environmental studies during the relevant ECRC recovery period exceeds the amount included in the approved rate case test year budget, there should be no adjustment to the amount of expenses associated with GCOS for recovery through the ECRC. (CLEMONS, MERTA, BREMAN)

STAFF ANALYSIS: As stated previously, on March 27, 2000, Gulf filed a Request for Clarification/Modification of Order No. PSC-00-0476-PAA-EI or in the Alternative Petition for a Formal Proceeding.

A. Gulf's Request for Clarification/Modification of Order No. PSC-00-0476-PAA-EI

In its Request, Gulf states that at the February 15, 2000, Agenda Conference, the Commission voted to allow Gulf to recover its GCOS expenses through the ECRC, subject to an offset which took into account environmental studies costs already included in Gulf's rate case test year to the extent that Gulf was no longer incurring such costs. This so called "netting", Gulf states, was to take into account \$178,000 of identified expenditures for environmental studies contained in its test year budget for its last rate case, and the fact that it was no longer incurring such costs as a base rate item. Gulf asserts that the Commission's intent was that the amount of the base rate offset to be applied against total GCOS expenses would be the amount of Gulf's actual expenses for environmental studies undertaken through base rates. Notwithstanding, it argues, Order No. PSC-00-0476-PAA-EI, which memorializes the Commission's February 15, 2000, vote, contains language which fixes the offset at \$178,000. It is these portions of the Order, it states, that it seeks to have clarified or modified to be consistent with the Commission's stated intent.

Gulf maintains that it should not be required to reduce the level of costs for GCOS that can be recovered through ECRC by \$178,000 because it is actually incurring expenses outside of the

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ECRC for environmental studies as it was in the rate case test year. Thus, it argues, the amount of the base rate offset should be reduced from the cap of \$178,000 by an amount equal to the amount actually spent by Gulf on environmental studies outside of the ECRC during the relevant recovery period. According to Gulf, it has four non-ECRC activities planned for the year 2000 and beyond, which fall into the environmental studies category, including studies for Advanced Energy Systems, Regional Air Quality Issues, the Southern Oxidant Study, and the Cooperative Tree Planting Program. Gulf states that its total expected expenses in 2000 for these four activities is more than \$300,000, all of which are outside of ECRC, and is, therefore, being addressed in base rates.¹

In addition, Gulf argues that in Order No. PSC-94-0044-FOF-EI, by which the Commission first established the ECRC for Gulf, the Commission specifically rejected the kind of offset for base rate expenditures that is proposed in Order No. PSC-00-0476-PAA-EI. It further asserts that in Order No. PSC-94-0044-FOF-EI, the Commission favored a policy that limited ECRC recovery to new activities since the last rate case test year and existing activities that have increased in scope due to changes in regulatory requirements since the last rate case proceeding. The Order states, at page 20:

The last nine O&M categories are disallowed because all activities included in each of the following categories are being recovered in base rates. The fact that Gulf's current cost projections is different today from the same activities addressed in the last rate case is not an increase in compliance requirements but an adjustment to reflect changes in projections.

According to Gulf, with over six years of implementing Order No. PSC-94-0044-FOF-EI, the Commission has now changed its policy "so that an offset to an ECRC recoverable activity for base rate items is required."

Gulf maintains that such a change in policy is not warranted under the circumstances of the GCOS. First, it states, the GCOS is a new activity that did not exist in the rate case test year. Second, Gulf continues, the required offset is tied to activities in the rate case test year which have been identified as

¹ Staff notes that Gulf disclosed these four activities for the first time in its Request for Clarification/Modification of Order No. PSC-00-0476-PAA-EI.

environmental studies which were essentially research and development (R&D) activities, and as such, are not eligible for ECRC recovery under the Commission's established policy. Third, Gulf argues, it continues to incur expenses for these types of environmental studies outside of ECRC well above the \$178,000 identified for such activities in the rate case test year budget.

Therefore, Gulf requests that the Commission clarify or modify Order No. PSC-00-0476-PAA-EI so that it may either: 1) reduce the amount of the base rate offset by the amounts it incurs in connection with environmental studies outside of the ECRC; or 2) remove the offset requirement altogether. In either case, it states, it would be allowed to fully recover its GCOS expenses consistent with the intent of the Commission as expressed at the February 15, 2000, Agenda Conference. Alternatively, if the Commission declines to clarify or modify Order No. PSC-00-0476-PAA-EI, Gulf requests a formal hearing pursuant to Sections 120.569 and 120.57(1), Florida Statutes.

B. Staff Analysis

At the February 15, 2000, Agenda Conference, Gulf raised similar arguments to the ones in its Request. It stated that in Order No. PSC-94-0044-FOF-EI, the Commission set a policy that only new activities would be recoverable through the ECRC. (Tr. at 25-25). Gulf maintained that "[i]f you stick with your new activity standard, which is what you imposed back in the 1994 Order, then we can implement that without going into an earnings test." (Tr. at 28). However, it argued, "if there is concern that there's \$178,000 embedded in our base rate structure that is causing the company to overearn because it's no longer being incurred, then it's a base rate proceeding that deals with that." (Tr. at 31). Therefore, the company asserted, "that's why I say to you that you cannot answer the question about whether it's embedded in base rates without dealing with the earnings question in this context. And that's why I submit to you that it is -- it does represent a major policy shift." (Tr. at 32).

A Commissioner agreed with Gulf that the policy set forth in Order No. PSC-94-0044-FOF-EI did indeed require that only new activities would be recoverable through the ECRC, but clarified that the Order did not state that the new activity could not be offset by costs included in base rates which were no longer being incurred. (Tr. at 26). The Commissioner explained that the Legislature did not want companies to recover dollars both in base rates and in a cost recovery clause. (Tr. at 27). He further stated:

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We have some costs right now that were in the previous rate case which were for environmental studies. Obviously, they weren't for an ozone study. But they were for environmental studies. Those costs are no longer being incurred specific, but there is an allowance in base rates. I think it's contemplated within the statute, and it is fair to recognize that and to offset that given that we've got a new mechanism.

(Tr. at 49-50).

Upon this rationale, the same Commissioner moved to allow recovery of the GCOS expenses through the ECRC with the net amount, and the motion was carried. (Tr. at 52-53). Order No. PSC-00-0476-PAA-EI memorializes the Commission's February 15, 2000, vote, and states:

By approving the expenses of the GCOS for cost recovery, however, we do not believe that the entire amount requested is appropriate for cost recovery through the ECRC. Gulf continues to collect \$178,000 annually in base rates for environmental studies that it is no longer pursuing. Therefore, the estimated recoverable amount for the GCOS of \$250,000 for 2000 and \$250,000 for the next four years shall be reduced annually by the \$178,000 that is in base rates for environmental studies.

Gulf has requested that the Commission remove altogether the base rate offset requirement articulated in the foregoing language. However, staff believes that the Commission's decision is well reasoned, fairly balances the interests of the ratepayers and the shareholders, and is consistent with Section 366.8255, Florida Statutes, which provides that "[a]n adjustment for the level of costs currently being recovered through base rates or other rate-adjustment clauses must be included in the filing." Therefore, staff recommends that Gulf's request to clarify or modify Order No. PSC-00-0476-PAA-EI to remove altogether the base rate offset be denied.

By requiring a base rate offset, staff does not believe that the Commission has articulated a major policy shift as charged by Gulf, but has simply recognized the potential for double recovery. Staff further believes that a base rate offset is not inconsistent with the policy that if a project with the same function as a new project proposed for ECRC recovery was included in the last rate case test year, the company is only allowed to recover the incremental cost of the new project if there has been either a new environmental compliance requirement or a change in scope of an

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existing environmental compliance requirement which necessitated the new project for which recovery is being sought through the ECRC. As stated by the Commissioner at the February 15, 2000, Agenda Conference, Order No. PSC-94-0044-FOF-EI does not provide that the new activity cannot be offset by costs included in base rates which were no longer being incurred, and an offset is contemplated within the statute.

As previously discussed, the recoverable amount for the GCOS through the ECRC was reduced annually by the \$178,000 that is in base rates for environmental studies, but which staff believed Gulf was not currently incurring. Gulf originally identified \$178,000 of expenditures for environmental studies contained in the Company's test year budget for its last rate case. The belief that Gulf was no longer incurring costs for environmental studies as a base rate item was the result of incorrect information provided in response to a staff interrogatory. Gulf now states that it mistakenly overlooked four ongoing non-ECRC environmental activities for which the costs were included in Gulf's monthly surveillance report. For the period ending November 1999, the associated costs totaled \$242,049, and for 2000, the costs are expected to be more than \$300,000. According to Gulf, the error was only discovered after the February 15, 2000, Agenda Conference.

In light of the foregoing, staff recommends that page 2 of Order No. PSC-00-0476-PAA-EI be modified as follows, with recommended additions indicated by underline and recommended deletions indicated by strikethrough:

By approving the expenses of the GCOS for cost recovery, however, we do not believe that the entire amount requested is appropriate for cost recovery through the ECRC. ~~Gulf continues to collect \$178,000 annually in base rates for environmental studies that it no longer is pursuing.~~ Gulf shall recover only those annual costs of the GCOS in excess of the amount included in the approved rate case test year budget reduced by the amount actually spent on environmental studies as an operating expense during the relevant ECRC recovery period. If the amount reflected in surveillance reports for expenditures on environmental studies during the relevant ECRC recovery period exceeds the amount included in the approved rate case test year budget, there shall be no adjustment to the amount of expenses associated with GCOS for recovery through the ECRC. Therefore, the estimated recoverable amount for the GCOS of \$250,000 for 2000 and \$250,000 for the next four years shall be reduced annually by the \$178,000 that is in base rates for environmental studies.

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Since only the portion of Order No. PSC-00-0476-PAA-EI relating to the base rate offset as indicated above was protested by Gulf, the remainder of the Order should become final and effective upon the issuance of a Consummating Order.

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ISSUE 2: Should this docket be closed?

RECOMMENDATION: Yes. If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the order, this docket should be closed upon the issuance of a consummating order. (CLEMONS)

STAFF ANALYSIS: At the conclusion of the protest period, if no protest is filed, this docket should be closed upon the issuance of a consummating order.