State of Florida

Public Service Commission

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

DATE: JULY 25, 2002

TO: DIRECTOR, DIVISION OF THE COMMISSION CLERK & ADMINISTRATIVE SERVICES (BAYÓ)

FROM: DIVISION OF ECONOMIC REGULATION (SPRINGER)
OFFICE OF THE GENERAL COUNSEL (HOLLEY)

RE: DOCKET NO. 020537-EC - PETITION FOR APPROVAL OF MODIFICATION OF ELECTRIC RATE SCHEDULES BY CHOCTAWHATCHEE ELECTRIC COOP., INC.

AGENDA: 08/06/02 - REGULAR AGENDA - TARIFF FILING - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\ECR\WP\020537.RCM

CASE BACKGROUND

On February 18, 2002, Choctawhatchee Electric Cooperative, Inc. (CHELCO) filed a petition with supporting documentation to modify its rates. The proposed rates went into effect on April 1, 2002. CHELCO's proposed rates were designed using the Minimum Distribution System (MDS) classification methodology. The MDS classification methodology had not previously been used by CHELCO to design its rates. In conjunction with modifying its rates, CHELCO is updating its Wholesale Power Adjustment (WPA) to contain a true-up mechanism.

The Commission has rate structure jurisdiction over cooperatives pursuant to Section 366.04(2)(b), Florida Statutes. Cooperatives are required to file tariffs with the Commission in accordance with Rule 25-9.053(1), Florida Administrative Code. The Commission has delegated the authority to staff to administratively approve tariff filings by cooperatives as long as: (1) there is no

change in the rate structure previously approved for that utility; (2) the change results in the rate relationships moving closer to those approved for the investor-owned electric utilities; or (3) the proposal does not contain new pricing concepts. Because CHELCO's filing involves a new pricing concept, Commission approval is required. This recommendation addresses only the proposed rates that have been designed using the MDS classification methodology. The Commission has jurisdiction pursuant to Section 366.04(2)(b), Florida Statutes.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve CHELCO'S proposed rates based on the MDS classification methodology?

RECOMMENDATION: Yes. (Springer)

STAFF ANALYSIS: CHELCO is a member owned, not-for-profit cooperative that acquires and distributes electricity to its members/owners. CHELCO has proposed to modify its residential (RS), general service (GS), general service - demand (GSD), and large power (LP) rate classes. The present and proposed rates are contained in the table below:

Rate Schedule	Present Rates	Proposed Rates
Residential (RS)		
Customer Charge (per month)	$12.32	$18.00
Non-Fuel Energy Charge(cents per kWh)	6.407	7.046
General Service (GS)		
Customer Charge (per month)	$12.32	$18.00
Non-Fuel Energy Charge(cents per kWh)	6.615	6.459
General Service - Demand (GSD)		
Customer Charge (per month)	$12.32	$26.25
Demand Charge (per kW)	$4.94	$6.22
Non-Fuel Energy Charge(cents per kWh)	4.587	4.265
Large Power (LP)		
Customer Charge (per month)	$500.00	$30.00
Demand Charge (per kW)	$9.50	$4.91
Non-Fuel Energy Charge(cents per kWh)	2.970	4.265

The purpose of a cost of service study is to perform three activities. First, it functionalizes costs into production,

transmission, distribution, customer, and administrative/general categories. Second, these functionalized costs are separated into the three primary cost classifications: (1) demand costs that vary with the kilowatt (kW) demand imposed by the customer; (2) energy costs that vary with the energy or kilowatt hours (kWh) consumed; and (3) customer costs that are directly related to the number of customers served. Finally, after the costs have been functionalized and classified, the costs are allocated among the various customer classes.

In previously approved methodologies, the customer charge has been designed to recover the costs to provide the service drop and meter, meter reading, billing and collection, and customer information and service. Distribution equipment costs such as transformers, poles, and conductors have normally been classified as demand-related costs. These distribution equipment costs are classified as demand-related, based on the theory that peak load determines the size of this equipment, not the presence of the customer. The MDS method classifies a larger portion of these distribution costs as customer-related. CHELCO proposes to use the MDS classification methodology to justify increased customer charges.

CHELCO's MDS classification methodology uses a Zero Intercept (ZI) method to determine how distribution transformers, poles, and conductors costs are separated between demand-related and customer-related costs. The ZI method develops a hypothetical distribution system to determine the cost of a distribution system that is not capable of carrying any load. The costs of this hypothetical system are classified as customer-related. All other distribution transformers, poles, and conductors costs are classified as demand-related. The MDS classification methodology increases the RS, GS and GSD customer costs by classifying a portion of the normally demand-related distribution equipment costs as customer-related.

The Commission has consistently rejected the use of the MDS classification methodology by investor-owned utilities for the last 20 years. (See Orders 9599, 9864, 10557, 11628, 11498, 23573) Most recently, MDS was rejected in the Gulf Power rate case. See Order No. PSC-02-0787-FOF-EI issued on June 10, 2002, in Docket No. 010949-EI. MDS was rejected because of inconsistencies in the methodology and because it does not always reflect the way a utility incurs costs. In this case, however, staff believes that

CHELCO has four unique characteristics that justify the use of the MDS classification methodology in its cost of service study.

First, CHELCO has a density of ten customers per mile, while most investor-owned utilities have a density of fifty-five customers per mile or greater. In a high-density service territory, several customers may be served by a single transformer, while in a sparsely populated rural area there is usually one transformer for each residential account. Thus, the significant costs of constructing and maintaining a mile of line in a rural service territory are spread to a significantly fewer number of customers.

Second, CHELCO's rural service territory is quite different from an urban investor-owned utility. Urban areas are normally occupied throughout the year, and customers usually consume a large amount of electricity that varies seasonally with their heating and cooling load. By contrast, CHELCO provides service to a significant number of barns, stock tanks, electric fences, hunting cabins, and vacation homes. These types of customers consume small amounts of electricity during the course of the year, and their usage is sporadic. A rate design with a relatively low customer charge and a high energy charge for these customers may not recover the costs of investment necessary to serve their load.

Third, CHELCO has many customers taking service under multiple accounts. Presently, it is relatively expensive to hire an electrician to extend a line from a customer's existing meter to a barn, well, stock tank, or electric fence. Customers typically find that it is cheaper to establish a separate account with CHELCO, which then incurs these costs. In April 2002, CHELCO had 34,246 active accounts, but only 27,871 cooperative memberships. The higher proposed customer charges based on the MDS methodology will provide a better price signal and reduce the subsidization of these multiple account customers.

Fourth, CHELCO has been experiencing financial hardships, and has not increased its base rates since 1992. Last year, CHELCO had an operating loss of $101,179. As of April 2002, CHELCO had realized an operating loss of $1,113,074. The proposed higher customer charges designed using MDS should stabilize CHELCO's revenues.

CHELCO's management and staff have spent a considerable amount of time and effort in educating its owners/members about the proposed rates. This was accomplished via the customer newsletter, a presentation by the General Manager at CHELCO's annual meeting, and presentations to various groups. Currently, there have been no customer complaints and minimal negative response to the proposed rates from CHELCO's customers. Additionally, the proposed rates will moderate the variability in both CHELCO's operating margins and in customer bills. Staff believes that CHELCO's proposed rate design is fair and reasonable based on the unique circumstances that confront the cooperative and its members/owners. For these reasons, staff recommends that the Commission approve CHELCO's proposed rates based on the MDS classification methodology.

ISSUE 2: Should this docket be closed?

RECOMMENDATION: Yes. If no person whose substantial interest are affected by the Commission's order in this docket files a protest within 21 days of the issuance of the order, this docket should be closed. If a protest is timely filed, the tariff should remain in effect, pending resolution of the protest. (HOLLEY)

STAFF ANALYSIS: If no person whose substantial interest are affected by the Commission's order in this docket files a protest within 21 days of the issuance of the order, this docket should be closed. If a protest is timely filed, the tariff should remain in effect, pending resolution of the protest.