

State of Florida



Public Service Commission
CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850
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COMMISSION
CLERK

DATE: DECEMBER 23, 2003

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

FROM: DIVISION OF COMPETITIVE MARKETS & ENFORCEMENT (MAKIN, MARSHALL, BULECZA-BANKS) *you*
DIVISION OF ECONOMIC REGULATION (SLEMKEWICZ, MAUREY) *JS*
OFFICE OF THE GENERAL COUNSEL (VINGING, HELTON) *next* *tax* *ALM*

RE: DOCKET NO. 030923-GU - PETITION FOR APPROVAL OF REVISIONS TO TARIFF PROVISIONS GOVERNING EXTENSION OF MAINS AND SERVICES TO PROVIDE GAS SERVICE FACILITIES TO NEW CUSTOMERS, BY PEOPLES GAS SYSTEM.

AGENDA: 01/06/04 - REGULAR AGENDA - TARIFF FILING - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: 60-DAY SUSPENSION DATE: 11/20/03 - COMPANY WAIVED THE 60-DAY SUSPENSION DATE TO THE 01/06/04 AGENDA

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\CMP\WP\030923.RCM

CASE BACKGROUND

Peoples Gas System (Peoples or Company) presently extends its facilities to provide service in accordance with the provisions of Rule 25-7.054, Florida Administrative Code. The rule requires that natural gas utilities maintain a standard policy governing the amount of main service extension that will be made at no cost to a new customer. Free extensions are required when the capital investment necessary to extend the facilities in order to provide service is equal to or less than the maximum allowable construction cost (MACC). Rule 25-7.054, Florida Administrative Code, defines the MACC as an amount equal to four times the estimated annual gas revenues to be derived from the facilities, less the cost of gas. If a utility and a consumer are unable to agree in regard to an

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extension, either party may appeal to the Commission for review, pursuant to Rule 25-7.054, Florida Administrative Code; however, the Company has the discretion to develop an extension policy more favorable to its customers as long as no discrimination is practiced between customers. In the event the required capital investment exceeds the MACC, the company may require the customer to make a non-interest bearing deposit in aid of the construction cost.

Peoples current main and service extensions policy provides that the MACC shall equal five times the estimated annual revenue to be derived from the facilities, less the cost of gas.

On September 22, 2003, Peoples filed a petition for approval of a modification to its tariff provisions governing extension of mains and services reducing the MACC to four times the estimated annual revenue to be derived from the facilities, less the cost of gas. This recommendation addresses People's petition.

Jurisdiction over this matter is vested in the Commission pursuant to Chapter 366, Florida Statutes, including Sections 366.04, 366.05, and 366.06, Florida Statutes.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve the modification to tariff provisions governing Mains and Service Extensions requested by Peoples Gas System?

PRIMARY STAFF RECOMMENDATION: No. The Commission should not approve the modifications to tariff provisions governing Mains and Service Extensions requested by Peoples Gas System because there are special circumstances here that warrant deviation from the minimum requirements of Rule 25-7.054, Florida Administrative Code. (MAKIN, MARSHALL, BULECZA-BANKS, HELTON)

ALTERNATE STAFF RECOMMENDATION: Yes. The Commission should approve the modifications to tariff provisions governing Mains and Service Extensions requested by Peoples Gas System, because the tariff modification meets the minimum requirements of Rule 25-7.054, Florida Administrative Code. (VINING, MAKIN, MARSHALL, BULECZA-BANKS)

STAFF ANALYSIS: Peoples has proposed modification of its existing tariff rules and regulation governing Main and Service Extensions. The most recent tariff provisions governing Mains and Service Extensions were approved by Order No. PSC-94-1341-FOF-GU, issued October 31, 1994, Docket No. 940960-GU, In Re: Petition for approval of modifications to tariffs governing main and service extensions by Peoples Gas System, Inc. According to this Order, Peoples' tariff defines the MACC to be five times the estimated annual revenue to be derived from the extended facilities, less the cost of gas, and requires a deposit from the customer for the amount by which the estimated construction cost for an extension exceeds the MACC. In this petition, Peoples is proposing to reduce the MACC to four times the estimated annual revenue, less the cost of gas.

Peoples states that the reduction of the multiplier from five to four will help ensure that the Company is not required to make extensions of mains and services to the detriment of its existing customers. Most of the facilities extensions are needed to serve potential new commercial customers. As indicated by Exhibits A and B of the Company's petition, which are included as Attachment A to this recommendation, Peoples maintains that extensions using a five-year multiplier results in a return on equity (ROE) below the Company's currently authorized mid-point of 11.25%, while those using a four-year multiplier would produce an ROE at or slightly above 11.25%.

PRIMARY STAFF ANALYSIS: Rule 25-7.054, Florida Administrative Code, provides that, unless special circumstances prevent, the Commission will be guided by the general principle that MACC is equal to four times the estimated annual gas revenue to be derived from the facilities less the cost of gas. In this instance, staff believes there are special circumstances that warrant deviation from the minimum requirements of Rule 25-7.054, Florida Administrative Code, and that the Commission should deny the proposed modification to Peoples' tariff provisions governing Mains and Service Extensions.

In Docket No. 020384-GU, In Re: Petition for rate increase by Peoples Gas System, the Company proposed to change the MACC multiplier from five to four. In that docket, staff asked Peoples, in Staff's Interrogatory 87, to provide a full explanation of the purpose and impact of Peoples' proposed change to the definition of MACC contained in proposed Second Revised Tariff Sheet No. 5.601.

In response, the Company stated that the proposed change would theoretically make it more difficult for single appliance customers to meet the new MACC hurdle. In the final rate order in that proceeding, Order No. PSC-03-0038-FOF-GU, issued January 6, 2003, the Commission approved a stipulation between staff and the Company which stated that the proposed change from five to four to the definition of Maximum Allowable Construction Cost is not appropriate. In its petition in this proceeding, Peoples did not indicate what has changed since the rate proceeding to warrant the Commission deviating from its previous decision.

Staff issued a data request to the Company in this proceeding asking for the number of residential and commercial customers that would have had to make a Contribution in Aid of Construction (CIAC) if the MACC would have been four years instead of five. The Company responded that had the MACC been four for the past two years, 475 residential customers and 192 commercial customers would have been required to make a CIAC. As Peoples' current customer base is 264,375, the number of customers that would have been required to make a contribution is less than one percent. The small number of customers affected does not support the Company's argument that the change will help ensure that Peoples is not required to make extensions of mains and services to the detriment of its existing customers.

Exhibit B of Attachment A demonstrates that using a four-year multiplier for commercial extensions will cause those customers requesting service under the proposed MACC to contribute to the Company's ROE in excess of the midpoint. In fact, customers in four of the five commercial classes shown in Exhibit B would contribute in excess of the high point of the authorized ROE range. Staff does not believe that the Company should be allowed to modify a tariff in such a fashion that the individual transactions would exceed its authorized rate of return.

As a result, pursuant to Rule 25-7.054, Florida Administrative Code, staff believes there are special circumstances here that warrant the Commission deviating from the minimum requirements of Rule 25-7.054, Florida Administrative Code. Therefore, staff recommends that the Commission should not approve the modification to tariff provisions governing Mains and Service Extensions requested by Peoples Gas System.

ALTERNATE STAFF ANALYSIS: Rule 25-7.054, Florida Administrative Code, requires the utility to develop a standard policy governing the amount of main and service extension that will be provided to connect a new customer without requiring compensation from the customer. The rule, which is included as Attachment B to this recommendation, provides that if a utility and a consumer cannot agree in regard to an extension, either party may appeal to the Commission for a review, wherein the Commission will be guided by the general principles laid out in the rule. One of these general principles says that the MACC "shall equal four times the estimated annual gas revenue to be derived from the facilities less the cost of gas."

Paragraph (3)(c) of Rule 25-7.054, Florida Administrative Code, provides that a utility has the discretion to develop an extension policy more favorable to its customers as long as no discrimination is practiced between customers. As a result, a utility could have a multiplier of ten for MACC if it chooses to do so, as St. Joe Natural Gas has, but the minimum required by the rule is four. Peoples currently defines the MACC to be five times the estimated annual revenue to be derived from the extended facilities, less the cost of gas. In its petition, the Company is requesting that the MACC be changed to a multiplier of four. The proposed tariff governing main and service extensions meets the minimum requirements of the rule. Accordingly, Peoples' requested modification to tariff provisions governing Mains and Service Extensions should be approved.

ISSUE 2: Should this docket be closed?

RECOMMENDATION: Yes. If the Commission approves the alternate staff recommendation in Issue 1, and a protest is filed within 21 days of the issuance of an Order, the tariff should remain in effect with any increase held subject to refund pending resolution of the protest; however, if no timely protest is filed, this docket should be closed upon the issuance of a Consummating Order. If the Commission approves the primary staff recommendation in Issue 1, and no timely protest is filed, this docket should be closed upon the issuance of a Consummating Order. (VINING)

DOCKET NO. 030923-GU
DATE: DECEMBER 23, 2003

STAFF ANALYSIS: If the Commission approves the alternate staff recommendation in Issue 1, and a protest is filed within 21 days of the issuance of an Order, the tariff should remain in effect with any increase held subject to refund pending resolution of the protest; however, if no timely protest is filed, this docket should be closed upon the issuance of a Consummating Order. If the Commission approves the primary staff recommendation in Issue 1, and no timely protest is filed, this docket should be closed upon the issuance of a Consummating Order.

**Peoples Gas System
Main & Service Extension
Feasibility Analysis**

EXHIBIT A

Project Payback Years

5	5	5	5	5
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Assumption:

Adding 1 Commercial Customer - Annual Therms Rate Class	10,000 GS-1	35,000 GS-2	175,000 GS-3	350,000 GS-4	650,000 GS-5
Customer Charge	\$ 30.00	\$ 35.00	\$ 45.00	\$ 85.00	\$ 150.00
Base Rate	\$0.23045	\$0.22267	\$0.19533	\$0.17828	\$0.10041
Annual revenue	\$ 2,665	\$ 8,213	\$ 34,723	\$ 63,418	\$ 67,067

Maximum Allowable Construction Cost (MACC)

\$ 13,323	\$ 41,067	\$ 173,614	\$ 317,090	\$ 335,333
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Capital Structure:

	Ratio	Cost Rate (1)	Amount	Amount	Amount	Amount	Amount
Shareholders' Equity	51.68%		\$ 6,885	\$ 21,224	\$ 89,724	\$ 163,872	\$ 173,300
Long Term Debt	34.90%	7.73%	4,650	14,332	60,591	110,664	117,031
Short Term Debt	1.64%	3.40%	218	674	2,847	5,200	5,499
Customer Deposits	6.11%	6.76%	814	2,509	10,608	19,374	20,489
Tax Credits	5.67%		755	2,329	9,844	17,979	19,013
	100.00%		\$ 13,323	\$ 41,067	\$ 173,614	\$ 317,090	\$ 335,333

Income Statement:

Net Revenue			\$ 2,665	\$ 8,213	\$ 34,723	\$ 63,418	\$ 67,067
Less: O&M Expense		(2)	474	1,313	2,999	9,414	13,515
Depreciation Expense	@	4.59% (3)	612	1,885	7,969	14,554	15,392
Taxes Other (Property)	@	1.80% (4)	240	739	3,125	5,708	6,036
Taxes Other (Revenue)	@	0.50% (5)	67	205	868	1,585	1,677
Income Tax	@	38.58%	328	1,069	5,502	8,531	7,649
Net Operating Income			944	3,002	14,259	23,625	22,798
Interest Expense			422	1,300	5,498	10,041	10,619
Net Income			\$ 523	\$ 1,702	\$ 8,762	\$ 13,584	\$ 12,180

Implicit Return on Equity	7.59%	8.02%	9.77%	8.29%	7.03%
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- (1) Actual Capital Structure and Cost Rates at June 30, 2003
(2) Based on Cost of Service Study in last Rate Case
(3) Overall effective depreciation rate based in plant at 12/31/02
(4) Actual effective rate for 2002
(5) Regulatory Assessment Fee

**Peoples Gas System
Main & Service Extension
Feasibility Analysis**

EXHIBIT B

Project Payback Years

4	4	4	4	4
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Assumption:

Adding 1 Commercial Customer - Annual Therms	10,000	35,000	175,000	350,000	650,000
Rate Class	GS-1	GS-2	GS-3	GS-4	GS-5
Customer Charge	\$ 30.00	\$ 35.00	\$ 45.00	\$ 85.00	\$ 150.00
Base Rate	\$0.23045	\$0.22267	\$0.19533	\$0.17828	\$0.10041
Annual revenue	\$ 2,665	\$ 8,213	\$ 34,723	\$ 63,418	\$ 67,067

Maximum Allowable Construction Cost (MACC)

\$ 10,658	\$ 32,854	\$ 138,891	\$ 253,672	\$ 268,266
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Capital Structure:

	Ratio	Cost Rate (1)	Amount	Amount	Amount	Amount	Amount
Shareholders' Equity	51.68%		\$ 5,508	\$ 16,979	\$ 71,779	\$ 131,098	\$ 138,640
Long Term Debt	34.90%	7.73%	3,720	11,466	48,473	88,532	93,625
Short Term Debt	1.64%	3.40%	175	539	2,278	4,160	4,400
Customer Deposits	6.11%	6.76%	651	2,007	8,486	15,499	16,391
Tax Credits	5.67%		604	1,863	7,875	14,383	15,211
	100.00%		\$ 10,658	\$ 32,854	\$ 138,891	\$ 253,672	\$ 268,266

Income Statement:

Net Revenue			\$ 2,665	\$ 8,213	\$ 34,723	\$ 63,418	\$ 67,067
Less: O&M Expense		(2)	474	1,313	2,999	9,414	13,515
Depreciation Expense	@	4.59% (3)	489	1,508	6,375	11,644	12,313
Taxes Other (Property)	@	1.80% (4)	192	591	2,500	4,566	4,829
Taxes Other (Revenue)	@	0.50% (5)	53	164	694	1,268	1,341
Income Tax	@	38.58%	432	1,387	6,849	10,991	10,250
Net Operating Income			1,025	3,249	15,305	25,535	24,817
Interest Expense			337	1,040	4,398	8,033	8,495
Net Income			\$ 687	\$ 2,209	\$ 10,907	\$ 17,502	\$ 16,322

Implicit Return on Equity	12.47%	13.01%	15.19%	13.35%	11.77%
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- (1) Actual Capital Structure and Cost Rates at June 30, 2003
- (2) Based on Cost of Service Study in last Rate Case
- (3) Overall effective depreciation rate based in plant at 12/31/02
- (4) Actual effective rate for 2002
- (5) Regulatory Assessment Fee

(2) Each utility shall test the gas in such manner and with such frequency as is necessary to insure compliance with this rule.

Specific Authority: 366.05(1), F.S.

Law Implemented: 366.05(1), F.S.

History: Repromulgated 1/8/75, 5/4/75, formerly 25-7.53.

25-7.054 Extension of Facilities.

(1) Each utility shall develop a standard policy governing the amount of main and/or service extension which will be made free to connect a new customer. The amount of free extension made should be related to the investment that can prudently be made for the anticipated revenue to be received.

(2) A detailed statement of its standard main extension policy shall be filed by each utility as part of its rules and regulations. This policy shall have uniform application and shall be non-discriminatory between consumers whose service requirements are similar.

(3) If a utility and consumer shall be unable to agree in regard to an extension, either party may appeal to the Commission for a review. The Commission, unless special circumstances prevent, will be guided by the following general principles:

(a) Free extensions. The maximum capital investment to be made by the utility for main and service facilities without cost to the customer shall be defined as the maximum allowable construction cost. The maximum allowable construction cost shall equal four times the estimated annual gas revenue to be derived from the facilities less the cost of gas.

(b) Extensions above free limit. When the cost of the extension required to provide service is greater than the free limit specified in (a) above, the utility may require a non-interest bearing advance in aid of construction of the cost in excess of such free limit provided that:

1. At the end of the first year the utility shall refund to the person paying the advance in aid of construction or his assigns an amount equal to the excess, if any, of the maximum allowable construction cost calculated using actual gas revenues, less the actual cost of gas, over the maximum allowable construction cost used to determine the amount of the advance in aid of construction.

2. For each additional customer taking service at any point on the extension within a period of five (5) years from date of construction, the utility shall refund to the person paying the advance in aid of construction or his assigns an amount by which the maximum allowable construction cost for the new customer exceeds the cost of connecting the customer, provided that an additional main extension shall have not been necessary to serve the additional customer.

3. The aggregate refund to any customer made through the provisions of 1. and 2. above shall at no time exceed the original advance in aid of construction of such customer.

4. The extension shall at all times be the property of the utility and any unrefunded portion of the advance in aid of construction at the end of five (5) years shall be credited to the plant account of the utility.

(c) Nothing in this section (3) shall be construed as prohibiting any utility from establishing extension policies more favorable to consumers so long as no discrimination is practiced between consumers.

(4) The customer may be required to install or to pay in full or in part for the service line from the property line to the customer's piping in accordance with