State of Florida

Public Service Commission

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DATE: May 10, 2007

TO: Office of the Commission Clerk (Cole)

FROM: Division of Economic Regulation (Sickel, Windham)
Office of the General Counsel (Bennett)

RE: Docket No. 070108-EI – Petition for approval of agreement for generation services and related terms and conditions with Gulf Power Company for Northwest Division (Marianna) beginning 2008, by Florida Public Utilities Company.

AGENDA: 05/22/07 – Regular Agenda – Proposed Agency Action – Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: McMurrian

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\070108.RCM.DOC

Case Background

On February 8, 2007, Florida Public Utilities Company (FPUC) filed a petition with the Florida Public Service Commission (Commission) seeking approval of an agreement for the purchase of generation services from Gulf Power Corporation (Gulf). FPUC is seeking to recover, through its Capacity and Purchased Power Cost Recovery Clauses, the prudently incurred costs that it will incur under the agreement.

The Commission has jurisdiction over this matter pursuant to Sections 366.04 and 366.041 Florida Statutes.

Discussion of Issues

Issue 1: Should the Commission approve Florida Public Utilities Company's (FPUC) petition for approval of the agreement for generation services to be provided by Gulf Power Company (Gulf) for purposes of fuel cost recovery calculations?

Recommendation: Yes. By the terms of the agreement submitted in this petition, Florida Public Utilities Company (FPUC) will meet its power needs for a period of ten (10) years beginning January 1, 2008. (Sickel, Windham)

Staff Analysis: FPUC provides electric utility service to customers located in two sections of north Florida. The Northwest Division serves Jackson, Calhoun and Liberty Counties, and is commonly called the "Marianna Division." The Northeast Division is located in the Fernandina Beach area, and serves Nassau County. The Company does not generate any of the power it sells, but has met the needs of its customers through contracts for purchased power.

The purchased power contracts for both divisions were set to expire December 31, 2007. In the first quarter of 2005, FPUC began the work of obtaining replacement contracts for both divisions. FPUC hired the consulting firm of Christensen Associates to provide expertise and guidance over the entire process, from planning and releasing the request for proposals (RFP) to entering the final contract for the purchase of electricity.

The RFP was designed to hold a minimum level of constraints and impediments to serious potential bidders. Bidders were free to offer multiple packages and various bundles of services. Offers covering full requirements, partial requirements, and energy only services were invited. The RFP also offered flexible terms for proposed charges. Offers could be based on fixed charges, demand charges, energy charges, and could include indexed charges. Initially, the RFP sought offers for a five-year term, although shorter term offers were acceptable and ten-year options were encouraged. Thirty-five entities expressed interest initially, leading to seven formal offers.

During 2006, FPUC reached an agreement with JEA for the supply of purchased power to the Northeast Division beginning January 1, 2007. That agreement was presented for consideration by the Commission in the fuel adjustment Docket No. 060001-EI, In Re: Fuel and purchased power cost recovery clause with generating performance incentive factor. The Commission approved cost recovery for these purchased power costs by Order No. PSC-06-1057-FOF-EI, issued on December 22, 2006.

At issue here is FPUC's contract with Gulf to meet the needs of the Northwest Division. Based on analysis of offers and negotiations with service providers, FPUC selected Gulf for a ten-year power supply agreement to begin January 1, 2008. The contract for power supply was executed on December 28, 2006. FPUC seeks cost recovery approval for this agreement.

The expiring contract was negotiated a decade ago, in a time when costs relating to provision of electric energy were relatively stable. Consequently, that contract included firm prices for provision of electric service, with transmission service included in the firm price. The new contract includes market based costs, with environmental costs rolled into the energy costs.

The transmission costs are separately negotiated with the transmission services provider, which is Southern Company Services.

The process of selecting a supplier began with a request for power supply over a five-year period. Offers for a ten-year period were then negotiated and evaluated. The longer term provides more stability with regard to prices that are increasing and volatile.

The contract with Gulf is the best power supply alternative known by and available to FPUC. Staff has reviewed FPUC's confidential analysis of responses to the request for proposals. The projected costs associated with Gulf's offer are far below the costs associated with competing offers. FPUC describes Gulf as a good business partner, providing high service reliability and prompt response to technical issues that have developed.

Under the new agreement, FPUC will assume the position of a direct customer for transmission services. FPUC will have a transmission service agreement with Southern Company which will define the charges for monthly scheduling services, voltage control, and reactive power, plus a federal regulatory fee. Although the new agreement has FPUC paying for interconnection services, including metering and substation facilities, the charges are expected to be very similar to charges under the current contract.

The new agreement will result in an increase in the charges borne by customers. A residential customer using 1,000 KWH will pay $91.94 under the new contract, which is an increase of $21.80 over the charge for the same energy under the expiring contract. In addition, projected costs for transmission amount to approximately $3.50 per customer. During the 1997 - 2007 period of the current contract, customers have enjoyed relatively favorable rates. FPUC asserts that every available option would have resulted in a rate increase, and the agreement executed is the most prudent arrangement for continued purchased power.

FPUC is attempting to educate its body of ratepayers regarding the anticipated increase in charges. The utility has hired a public relations firm to direct the process of educating the community about the increase. Media releases have been used to advise of the expected increase, and suggest ways to conserve power. FPUC reports that a survey during May and June of 2006 included an inquiry whether customers would prefer to see the required increase gradually, or all at once. A detailed strategy for communicating information about the increase will be finalized after confirmation of the extent and timing of the rate changes.

Over a period of several months, staff has had an opportunity to observe the process used by FPUC to obtain a new contract for purchased power. Both the process and the results appear reasonable. Therefore, staff recommends that the reasonable and prudently incurred costs arising from exercise of the contract are appropriate for purposes of cost recovery under the fuel clause.

Issue 2: Should this docket be closed?

Recommendation: 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. (Bennett)

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.