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December 21, 2016

Ms. Carlotta S. Stauffer
Commission Clerk
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Re: Docket No. 160060-EC: Complaint and Petition of the City of Cape Coral, Florida For An Investigation Into The Rate Structure Of Lee County Electric Cooperative, Inc. (LCEC)

Dear Ms. Stauffer:

The City Council of the City of Cape Coral has requested by the above-referenced Complaint and Petition that the Public Service Commission take such steps as are necessary to ensure that residents and businesses in Cape Coral are not subsidizing the electric rates of LCEC's other customers. To this end, Cape Coral respectfully requests that the Commission order LCEC to conduct and file a cost of service study within ninety (90) days and modify LCEC's rate structure to remove any subsidies identified by such study.

In this regard, it is important to understand that when Florida Power & Light had a customer base like LCEC's current customer base, consisting of a large city (Miami), a few smaller cities, and customers in predominantly rural areas, FPL recognized the different cost of serving each group of customers. This recognition was reflected in FPL's rate structure: the rate structure grouped customers by whether they were located in a large city, small city or a rural area. Customers in a large city were charged less than a customer in a rural area to reflect FPL's lower cost of serving them.

LCEC's current customer base consists of Florida's 10th largest city, Cape Coral, a few smaller cities and customers in predominantly rural areas. Cape Coral requests that LCEC be ordered to investigate the adoption of a rate structure charging lower rates for service in Cape Coral to reflect LCEC's lower cost of service in the City, just as FPL did when it served similar customer groups. Failure to modify LCEC's rate structure in this way would result in the continued application of discriminatory rates to Cape Coral residents and businesses and the continuation of unlawful subsidies by Cape Coral of other LCEC customers in violation of constitution-based ratemaking principles.

Facts not in dispute. LCEC does not deny that its costs to serve in Cape Coral are lower. LCEC does not deny that the composition of its customer base (large city/smaller cities/rural areas) is similar to FPL's former customer base.

LCEC does not deny that a cost of service study is the tried and true mechanism for determining fair rates and eliminating unreasonable subsidies which benefit one group of customers to the detriment of

the residents and businesses of Cape Coral. The City of Cape Coral, responsible for \$185 million every year of LCEC revenues, requests that LCEC perform a cost of service study to identify the true cost of providing service in the City.

LCEC suggests that Cape Coral's request is somehow revolutionary in its premise. LCEC is mistaken. What Cape Coral is requesting is that LCEC rates and rate structure be established based upon cost of service principles. When the cost of serving one group of customers is different than other groups, the rates should be different.

The evolution of FPL's rate structure from the predominant days of Miami requiring a large city/smaller city/ rural area rate structure, to today, when FPL serves 12 of Florida's 20 largest cities with similar costs to serve each should be instructive in this regard. LCEC's customer base has gone in the opposite direction; from serving exclusively rural areas to serving Florida's 10th largest city, Cape Coral, with a population exceeding 175,000, as well as a few smaller cities and other more costly, predominantly rural areas. LCEC's rate structure should reflect this new reality.

A cost of service study could save Cape Coral residents and businesses many millions, every year, if rates are premised upon cost of service. LCEC has informed Cape Coral that LCEC service in the City represents approximately 45% of its annual revenue of \$425 million, or \$185 million every year.

To provide a glimpse into the materiality of the rate issue which Cape Coral wishes to be investigated, consider that approximately 70% of the \$185 million LCEC receives from serving the City every year represents power costs paid to FPL. The balance is approximately \$55 million. Even a 10% differential in LCEC's cost of serving within the City compared to serving other areas, if reflected in City specific rates, represents more than a \$5 million savings to customers in Cape Coral, every year. A 20% differential, if recognized in LCEC's rate structure, would result in annual savings of more than \$10 million, or more than \$100 million every 10 years. This savings is significant. If the cost differential is not recognized in LCEC's rate structure, LCEC customers in the City are subsidizing LCEC's other customers by these same amounts, which would be unreasonable.

LCEC suggests to the Commission that it would cost more than \$2 million to have the requested cost of service study performed. Cape Coral points out that even this exaggerated, one-time cost of \$2 million represents only 1% of the revenue LCEC takes from Cape Coral residents and businesses every year; and less than half of one year's savings in Cape Coral if even a 10% cost of service differential exists and rates are reduced accordingly.

LCEC cost projection is exaggerated. LCEC has informed the City (and the public) that it would cost LCEC only \$50,000 to identify its assets in the City and their depreciated, net book value. The net book value of assets to be included in rates is perhaps the most important factor in rate-setting. It is very difficult to give credence to a suggestion that it would cost more than \$2 million more to complete the remainder of a cost of service study.

LCEC is a distribution only rural electric cooperative. LCEC owns no generation assets. LCEC sold its transmission assets to FPL. LCEC buys 100% of its power from FPL, which power is re-sold to LCEC customers.

LCEC contracts with third parties for a myriad of services and maintains work orders for work they perform, including the location of such service. Direct attribution of such costs appears possible.

There are a number of accepted practices for allocating common costs like LCEC's other expenses, such as administrative and general, customer service and billing, management salaries and other compensation, and other expenses.

Cape Coral requests that the Commission order LCEC to conduct a cost of service study after appropriate bidding of the work. Based upon the costs which city utilities have paid for cost of service studies, it can be expected that the bids will be far lower than LCEC projects, but the only way to know is if bids for the work are solicited by LCEC.

LCEC's current rates are premised upon out-dated cost of service information. LCEC admits that it has not performed a cost of service study since 2007. Since Cape Coral began its investigation of LCEC rates and policies in 2014, LCEC has felt comfortable reducing rates four times. To implement so many rate decreases without the benefit (or support) of an updated cost of service study reveals that LCEC has been well aware that its rates provide a significant cushion of profit. As the Commission well knows, an investor-owned utility subject to Commission jurisdiction is not permitted to change its rates absent filing of a cost of service study for Commission review and validation. Cape Coral requests no less from LCEC so that a non-discriminatory rate structure reflecting fair rates and eliminating unreasonable and unlawful subsidies is established.

To conclude, the City of Cape Coral very much appreciates the speedy response of Commission staff to several document requests initiated by the City in the past few months. It is now clear that the Commission has no record of ever reviewing LCEC's rate structure or rates to determine whether unreasonable, discriminatory subsidies exist. Cape Coral would very much appreciate the Commission remedying this lapse by ordering a cost of service analysis be submitted to the Commission by LCEC within ninety (90) days and modifying LCEC's rate structure to remove unlawful and discriminatory subsidies should such study reveal their existence.

Respectfully submitted,



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Counsel for the City of Cape Coral

Cc: Parties of Record

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been furnished by electronic delivery to the following (unless otherwise noted below) on the 21st day of December, 2016:

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