

State of Florida



Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

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

DATE: April 25, 2024

TO: Office of Commission Clerk (Teitzman)

FROM: Division of Accounting and Finance (Ferrer, D. Buys) *ALM*
Office of the General Counsel (M. Thompson) *JSC*

RE: Docket No. 20240035-GU – Petition for approval of change in rate used to capitalize allowance for funds used during construction from 6.00% to 7.08%, effective January 1, 2024, by Peoples Gas System, Inc.

AGENDA: 05/07/24 – Regular Agenda – Proposed Agency Action – Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Administrative

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

Case Background

Peoples Gas System, Inc. (PGS or Company) current Allowance for Funds Used During Construction (AFUDC) rate of 6.00 percent was approved by Order No. PSC-2021-0170-PAA-GU, issued May 14, 2021.¹ On February 16, 2024, PGS filed a petition for approval to change its AFUDC rate from 6.00 percent to 7.08 percent, effective January 1, 2024. As required by Rule 25-7.0141(5), Florida Administrative Code (F.A.C.), PGS filed with its petition Schedules A, B, and C identifying the capital structure, capital structure adjustments, and the methodology used to calculate the monthly AFUDC rate. The Commission has jurisdiction over this matter pursuant to Chapter 366, Florida Statutes (F.S.), including Sections 366.04, 366.05, and 366.06, F.S.

¹Order No. PSC-2021-0170-PAA-GU, issued May 14, 2021, in Docket No. 20210040-GU, *In re: Request for approval of change in rate used to capitalize allowance for funds used during construction (AFUDC) from 5.97% to 6.00%, effective 1/1/21, by Peoples Gas System.*

Discussion of Issues

Issue 1: Should the Commission approve PGS's request to change its AFUDC rate from 6.00 percent to 7.08 percent?

Recommendation: Yes. The appropriate AFUDC rate for PGS is 7.08 percent based on a 13-month average capital structure for the period ended December 31, 2023. (Ferrer)

Staff Analysis: PGS requested an increase in its AFUDC rate from 6.00 percent to 7.08 percent. Rule 25-7.0141(3), F.A.C., Allowance for Funds Used During Construction, provides the following guidance:

(3) The applicable AFUDC rate will be determined as follows:

(a) The most recent 13-month average embedded cost of capital, except as noted below, must be derived using all sources of capital and adjusted using adjustments consistent with those used by the Commission in the Company's last rate case.

(b) The cost rates for the components in the capital structure will be the midpoint of the last allowed return on common equity, the most recent 13-month average cost of short-term debt and customer deposits and a zero cost rate for deferred taxes and all investment tax credits. The cost of long-term debt and preferred stock will be based on end of period cost. The annual percentage rate will be calculated to two decimal places.

In support of its requested AFUDC rate of 6.00 percent, PGS provided its calculations and capital structure in Schedules A and B attached to its request. Staff reviewed the schedules and determined that the proposed rate was calculated in accordance with Rule 25-7.0141(3), F.A.C. The requested increase in the AFUDC rate is due to an increase of 27 basis points in the weighted cost of long-term debt, an increase of 57 basis points in the weighted cost of short-term debt, and an increase of 26 basis points in the weighted cost of common equity, offset by a 2 basis point decrease in the weighted cost of customer deposits. PGS's cost rate for short-term debt increased from 1.16 percent in 2020 to 5.84 percent in 2023. Over the same period, PGS's cost rate for long-term debt increased from 4.69 percent to 5.68 percent. The debt cost rate increases were primarily due to market conditions and the Federal Open Market Committee raising interest rates. In its calculation, the Company appropriately used the mid-point return on equity of 10.15 percent, which was approved by Order No. PSC-2023-0388-FOF-GU.²

Based on its review, staff believes that the requested increase in the AFUDC rate from 6.00 percent to 7.08 percent is appropriate, consistent with Rule 25-7.0141, F.A.C., and recommends it be approved.

²Order No. PSC-2023-0388-FOF-GU, issued December 27, 2023, in Docket No. 20230023-GU, *In re: Petition for rate increase by Peoples Gas System, Inc.*

Issue 2: What is the appropriate monthly compounding rate to achieve PGS's requested annual AFUDC of 7.08 percent?

Recommendation: The appropriate compounding rate to achieve an annual AFUDC rate of 7.08 percent is 0.005717. (Ferrer)

Staff Analysis: PGS requested a monthly compounding rate of 0.005717 to achieve an annual AFUDC rate of 7.08 percent. In support of the requested monthly compounding rate of 0.005717, the Company provided its calculations in Schedule C attached to its request. Rule 25-7.0141(4)(a), F.A.C., provides the following formula for discounting the annual AFUDC rate to reflect monthly compounding.

$$M = [(1 + A/100)^{1/12} - 1] \times 100$$

Where: M = discounted monthly AFUDC rate

A = annual AFUDC rate

The rule also requires that the monthly compounding rate be calculated to six decimal places.

Staff reviewed the Company's calculation and determined it was derived in accordance with Rule 25-7.0141(4), F.A.C., as presented in Attachment 2. Therefore, staff recommends that a monthly compounding AFUDC rate of 0.005717 be approved.

Date: April 25, 2024

Issue 3: Should the Commission approve PGS's requested effective date of January 1, 2024, for implementing the AFUDC rate?

Recommendation: Yes. The AFUDC rate should be effective January 1, 2024, for all purposes. (Ferrer)

Staff Analysis: PGS's requested AFUDC rate was calculated using the most recent 13-month average capital structure for the period ended December 31, 2023. Rule 25-7.0141(6), F.A.C., provides that:

No utility may charge or change its AFUDC rate without prior Commission approval. The new AFUDC rate will be effective the month following the end of the 12-month period used to establish that rate and may not be retroactively applied to a previous fiscal year unless authorized by the Commission.

The Company's requested effective date of January 1, 2024, complies with the requirement that the effective date does not precede the period used to calculate the rate, and therefore, should be approved.

Issue 4: 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. (M. Thompson)

Staff Analysis: 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.

PEOPLES GAS SYSTEM, INC.
CAPITAL STRUCTURE USED FOR THE REQUESTED AFUDC RATE
as of December 31, 2023

STAFF RECOMMENDED				
<u>CAPITAL COMPONENTS</u>	<u>JURISDICTIONAL AVERAGE</u>	<u>CAPITAL RATIO</u>	<u>COST OF CAPITAL</u>	<u>WEIGHTED COST OF CAPITAL</u>
COMMON EQUITY	\$942,550,797	47.40%	10.15%	4.81%
LONG-TERM DEBT	\$543,872,462	27.35%	5.68%	1.55%
SHORT-TERM DEBT	\$236,704,341	11.89%	5.84%*	0.69%
CUSTOMER DEPOSITS	\$28,387,477	1.43%	2.41%*	0.03%
DEFERRED INCOME TAXES	\$237,186,904	11.93%	0.00%	
TOTAL	\$1,988,701,981	100.00%		7.08%

* 13-MONTH AVERAGE

PEOPLES GAS SYSTEM, INC.
METHODOLOGY FOR MONTHLY COMPOUNDING AFUDC RATE
as of December 31, 2023

STAFF RECOMMENDED

<u>MONTHS</u>	<u>AFUDC BASE</u>	<u>MONTHLY AFUDC RATE</u>	<u>CUMULATIVE AFUDC RATE</u>
1	1.000000	0.005717	0.005717
2	1.005717	0.005749	0.011466
3	1.011466	0.005782	0.017249
4	1.017249	0.005815	0.023064
5	1.023064	0.005849	0.028913
6	1.028913	0.005882	0.034795
7	1.034795	0.005916	0.040710
8	1.040710	0.005950	0.046660
9	1.046660	0.005984	0.052643
10	1.052643	0.006018	0.058661
11	1.058661	0.006052	0.064713
12	1.064713	0.006087	0.070800

Annual Rate (R) = 0.0708

Monthly Rate = $((1+R)^{(1/12)})-1 = 0.005717$