State of Florida

Public Service Commission

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

DATE: June 17, 2004

TO: Director, Division of the Commission Clerk & Administrative Services (Bayó)

FROM: Division of Economic Regulation (Floyd, Matlock, Windham, Maurey, McNulty, VonFossen)
Division of Auditing & Safety (Vandiver)
Office of the General Counsel (C. Keating, Rodan)

RE: Docket No. 031057-EI – Review of Progress Energy Florida, Inc.'s Benchmark for Waterborne Transportation Transactions with Progress Fuels.

AGENDA: 06/29/04 – Regular Agenda – Recommendation on Stipulation and Settlement – Parties May Participate

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\031057.RCM.DOC

Case Background

At its November 12-14, 2003, hearing in Docket No. 030001-EI, the Commission voted to defer consideration of issues related to Progress Energy Florida, Inc.'s (PEF) waterborne transportation transactions with Progress Fuels Corporation (PFC) to a separate proceeding. PFC is the coal procurement affiliate of PEF that arranges all coal purchases and coal transportation for the utility. The Commission also voted to eliminate the domestic and foreign waterborne coal transportation price proxies paid by PEF to PFC as established in Order No. PSC-93-1331-FOF-EI and Order No. PSC-94-0390-FOF-EI, respectively, beginning January 1, 2004. The Commission directed the staff to open a new docket for the purpose of establishing a new system for determining the just, reasonable, and compensatory rate for PEF's waterborne coal transportation service for 2004 and beyond.

The parties in this docket filed a Joint Notice of Settlement and Motion to Abate Proceeding on April 28, 2004. On April 29, 2004, the parties filed their Joint Motion for

Approval of Stipulation and Settlement (Joint Motion). Attachment 1 to this recommendation is the Joint Motion with a redacted copy of the Stipulation and Settlement. On April 30, 2004, the Prehearing Officer issued Order No. PSC-04-0451-PCO-EIO granting the Joint Motion to Abate Proceedings. All controlling dates in the docket are held in abeyance pending the Commission's consideration of the settlement agreement.

On May 7, 2004, staff sent the parties a list of questions seeking clarification of certain terms of the Stipulation and Settlement. On June 1, 2004, the parties submitted a joint response to staff's questions.

This recommendation addresses the Joint Motion for Approval of Stipulation and Settlement. The Commission has jurisdiction over this matter 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 Stipulation and Settlement?

Recommendation: Yes. The Stipulation and Settlement, as clarified by the parties' joint response to staff's questions, represents a fair and reasonable resolution of all issues in this docket. (FLOYD, McNULTY, WINDHAM, MAUREY, MATLOCK, VONFOSSEN)

Staff Analysis: The Stipulation and Settlement addresses the amount PEF will be permitted to recover from ratepayers for waterborne coal transportation services (WCTS) in 2004 and the manner in which PEF will obtain WCTS from January 1, 2005, going forward. The following analysis deals with both aspects of the Stipulation and Settlement as well as the clarifications that were provided in response to staff's questions.

Recoverable Costs for WCTS for 2004

The Stipulation and Settlement calls for a 26.4% reduction in the transportation cost per ton for domestic purchases of coal during 2004 compared to the cost that would have been incurred using the 2003 domestic market price proxy. Also, the transportation cost for foreign purchases of coal during 2004 would be reduced by 26.5% compared to the cost that would have been incurred using the 2003 foreign market price proxy. Staff estimates that these reductions would result in savings between $13.3 million and $15.6 million for calendar year 2004, depending on the amounts of foreign and domestic coal that will be purchased.

In its questions concerning this portion of the Stipulation and Settlement, staff first requested clarification regarding what is meant by the term "FOB Gulf terminal" as referenced in Paragraph 4 of the Stipulation and Settlement. The parties responded that the term refers to coal purchases for which PFC takes title at the terminal before the coal is unloaded or transloaded. In addition, while the term "FOB Gulf terminal" is intended to apply to shipments received at any Gulf terminal from Texas to Florida, the parties anticipate that Gulf terminal purchases will be made primarily at Davant, Louisiana (International Marine Terminal or IMT) or at Mobile, Alabama (State Dock).

Second, staff requested clarification as to whether the proposed 2004 rate for cross-Gulf waterborne transportation of foreign coal purchases or coal purchased FOB Gulf terminal, appearing in Paragraph 4 of the Stipulation and Settlement, includes the costs associated with Gulf terminalling. In response, the parties stated that normal, pre-arranged purchases at the Gulf terminal, and any other purchases where PFC has the option, will be made before terminalling charges have been included in the commodity price. This is an important clarification because it means that Gulf terminalling costs will not normally be included in the commodity price for such coal purchases. Thus, the proposed stipulated rate for cross-Gulf waterborne transportation of foreign coal purchases or coal purchased FOB Gulf terminal includes not only cross-Gulf shipping costs, but also the Gulf terminalling costs as well. The parties specified that transactions where terminalling may be included in the commodity price will be made only if the total price is less than the price of any other regular (without terminalling charges) Gulf terminal purchases with comparable BTU and sulfur content made within the preceding 60 days.

WCTS Beginning January 1, 2005

The Stipulation and Settlement proposes that, beginning January 1, 2005, waterborne transportation costs that are allowed to be recovered from ratepayers by PEF through the fuel cost recovery clause will be based on the results of competitive bidding. In the event that competitive bidding does not result in a valid market price, PEF will propose a market price proxy for Commission approval. The main elements of the Stipulation and Settlement for the period beginning January 1, 2005, are summarized as follows:

● PFC will conduct a competitive bidding process for all WCTS.

● PFC will maintain sufficient documentation to allow the Commission and affected parties to fairly evaluate the bidding process and the selection decision. This documentation will be made available no later than 45 days after the execution of any WCTS contract resulting from the competitive bidding process.

● For any competitive bidding proposal and RFP procedure for cross-Gulf WCTS, PEF and PFC will meet with staff and affected parties at least 30 days prior to issuing the proposal and will give due consideration to the input of the meeting participants.

● If the Commission determines that the bidding process did not produce competitive bids or did not result in a valid market price for the component of WCTS addressed by the process, or if the bidding process did not result in a WCTS contract, PEF will petition the Commission for approval of a market price proxy for that component.

● Contracts entered into by PFC for WCTS provided to PEF will be subject to competitive bidding procedures. Each such contract, and the competitive bidding process from which the contract results, will be presented to the Commission for review and approval or denial.

● If the initial contract or market price proxy for a WCTS component has not been approved or established by the Commission on or before January 1, 2005, the portion of the recoverable costs attributable to such component will remain in effect until a new contract or market price proxy is subsequently approved by the Commission. The respective portions attributable to each WCTS component are as follows: Upriver – 25%; River Barge – 40%; Gulf Terminal – 10%; and Cross-Gulf – 25%.

In response to staff's questions, the parties stated that terms of the Stipulation and Settlement with respect to 2005 and beyond do not address the recovery of costs incurred by PFC to integrate, coordinate, and schedule WCTS. These are costs other than WCTS contract costs or WCTS market proxy costs related to WCTS for which PEF may request cost recovery through the Fuel and Purchase Power Cost Recovery Clause. Other parties to the Stipulation and Settlement may take any position regarding such requests.

The Stipulation and Settlement indicates that if the initial contract or market price proxy for a WCTS component has not been approved or established by the Commission on or before the effective date of January 1, 2005, the portion of the FOB Mine deliveries specified in Paragraph 4 attributable to such WCTS component shall remain in effect on an interim basis, subject to true-up. For all such deliveries, the costs derived from the contract or market proxy subsequently approved by the Commission will then be used to true-up the component's interim costs as of January 1, 2005, according to the clarification provided by the parties.

In addition, staff sought clarification regarding the identity of the components of PEF's waterborne coal transportation service. The Parties responded that the components will initially include upriver, river barge, Gulf terminal, and cross-Gulf components. Depending upon the source of future coal purchases, new or reconfigured components may arise, and the Parties intend that contracts or market price proxies would be entered into or established for these components as well.

Finally, the parties clarified that PEF will file documentation supporting any new contract in the form of a petition to the Commission for review and approval or denial. In the event the Commission determines that the competitive bid process and any resulting WCTS contract did not result in a valid market price for a specified WCTS component, or if the competitive bid process does not result in a WCTS contract, PEF will petition the Commission for approval of a market price proxy for that WCTS component.

Conclusion

With the clarifications provided by the parties, staff recommends the Commission determine the Stipulation and Settlement is in the public interest and approve it as a reasonable means of resolving the issues in this docket. While the recovery of costs to integrate, coordinate, and schedule waterborne coal transportation costs charged by PFC to PEF are not addressed by the Stipulation and Settlement, staff believes these costs are relatively small compared to the contractual costs incurred by PFC to provide WCTS, and the recovery of such costs may be resolved by the Commission's review of any such cost recovery requests by PEF.

Issue 2: Should Docket No. 031057-EI be closed?

Recommendation: Yes. If there is no appeal of the Commission's order on this matter, this docket should be closed after the time for filing an appeal of the Commission's order has run. (C. Keating)

Staff Analysis: Yes. If there is no appeal of the Commission's order on this matter. This docket should be closed after the time for filing an appeal of the Commission's order has run.