

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition by Tampa
Electric Company d/b/a Peoples
Gas System for approval of a
methodology for accounting for
environmental expense accrual
and reserve account and
disposition of West Florida
Division's environmental reserve
account.

DOCKET NO. 980434-GU
ORDER NO. PSC-98-0739-FOF-GU
ISSUED: May 28, 1998

The following Commissioners participated in the disposition of
this matter:

JULIA L. JOHNSON, Chairman
J. TERRY DEASON
SUSAN F. CLARK
JOE GARCIA
E. LEON JACOBS, JR.

NOTICE OF PROPOSED AGENCY ACTION
ORDER CONCERNING APPROPRIATE ACCOUNTING TREATMENT
FOR ENVIRONMENTAL COSTS AND REQUIRING REFUND AND REPORT

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service
Commission that the action discussed herein is preliminary in
nature and will become final unless a person whose interests are
substantially affected files a petition for a formal proceeding,
pursuant to Rule 25-22.029, Florida Administrative Code.

I. CASE BACKGROUND

By Order No. PSC-92-0924-FOF-GU, issued September 3, 1992, we
authorized Peoples Gas System ("Peoples" or "the Company") to
amortize \$1,248,000 in environmental costs annually based on a 5-
year amortization period beginning November 1, 1990. By Order No.
PSC-93-1773-FOF-GU, issued December 10, 1993, we required Peoples
to fully amortize \$2,496,000 in environmental clean-up costs by
September 30, 1994.

Since September 30, 1994, Peoples has been deferring all
environmental costs instead of expensing them. By Order No. PSC-

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FPSC RECORDS/REPORTING

98-0329-FOF-GU, issued February 24, 1998, we ordered Peoples to write-off, against 1996 over earnings, its deferred environmental costs as of December 31, 1996. We also ordered the Company to expense all environmental costs as incurred, effective January 1, 1997, until the Company formally requested and received our authority to account for these costs using reserve or other accounting treatment.

On June 30, 1997, West Florida Natural Gas ("West Florida") was merged into Peoples Gas System. Prior to the merger, we authorized West Florida to accrue \$198,312 annually for environmental costs in Order No. PSC-92-0580-FOF-GU, issued June 29, 1992. By Order No. PSC-94-0452-FOF-GU, issued April 14, 1994, we ordered that at June 30, 1997, during West Florida's next rate case, or at the discretion of the Commission, any accruals in excess of actual expenses would be reviewed and subject to refund with interest, or other disposition, independent of West Florida's earnings. Also, the same order required West Florida to apply \$515,622 of 1993 overearnings towards its environmental clean-up costs. As of June 30, 1997, West Florida had accrued \$475,306 in excess of actual costs. By December 31, 1997, this balance reached \$546,464. The balance at March 31, 1998, further increased to \$595,052.

As a result of Order No. PSC-98-0329-FOF-GU, Peoples filed a petition on March 25, 1998, for approval to implement reserve accounting treatment for its environmental costs, with an annual base accrual of \$640,000 that may be adjusted based on expected reserve balances. In its petition, Peoples also requests approval to suspend the annual environmental cost accrual for its West Florida divisions and dispose of West Florida's environmental reserve account by writing it off against a portion of the current balance of unamortized debt costs related to the West Florida divisions.

II. RESERVE ACCOUNTING FOR ENVIRONMENTAL COSTS

A. RESERVE ACCOUNTING TREATMENT

In its petition, Peoples requests approval to implement reserve accounting for environmental costs as provided for in the Uniform System of Accounts for Natural Gas Utilities. As stated in Peoples' petition, the purpose for using reserve accounting is to ". . . mitigate the earnings impact from fluctuations which occur in environmental costs . . ." Peoples provided historical, pre-

merger environmental cost data for Peoples and West Florida, which show such cost fluctuations. From 1985 to 1997, Peoples' environmental costs ranged from (\$766,231) to \$2,478,538. From 1993 to 1997, West Florida's environmental costs ranged from \$7,662 to \$69,786.

Based on the wide fluctuations in environmental costs historically experienced by Peoples and its West Florida divisions, we find that the Company's request for reserve accounting should be approved. Reserve accounting treatment should levelize environmental expenses and mitigate their impact on the Company's earnings.

B. ANNUAL ACCRUAL AMOUNT

In its petition, Peoples requests authorization to accrue, beginning in 1998, a base amount of \$640,000 annually to this reserve account for environmental costs. The Company bases this amount on the historical environmental costs cited above.

As stated above, Peoples' environmental costs have varied widely from year to year and could impact earnings accordingly. We note that from 1985 to 1997, Peoples' average annual environmental costs were \$607,435, and from 1993 to 1997, West Florida's average annual environmental costs were \$39,634. Combined, the companies' average annual environmental costs totaled \$647,069, an amount roughly equivalent to the \$640,000 annual accrual requested by the Company. In addition, we believe that a \$640,000 annual accrual will levelize the Company's environmental expenses and mitigate their impact on the Company's earnings. Further, we believe that this amount will not have a significant impact on the Company's earnings. The \$640,000 annual accrual less the requested discontinuance of West Florida's \$198,312 annual accrual, discussed below, will result in a net increase to expense of \$441,411. Increasing 1997 expenses by \$441,411 would cause the Company's earned Return on Equity to decrease from 10.88% to 10.68%, within an authorized range of 10.25% to 12.25%. Based on the Company's budget, the ROE for 1998 would decrease from 11.72% to 11.52%.

Based on the foregoing, we find that the requested annual accrual of \$640,000 is reasonable. Further, because the Company uses a calendar year fiscal year, this accrual should be effective as of January 1, 1998.

C. EXPENSING MECHANISM TO ADJUST ANNUAL ACCRUAL AMOUNT

Through its petition, Peoples also seeks authorization to use an expensing mechanism that would allow the Company to adjust the \$640,000 annual accrual amount based on expected reserve balances. Peoples describes this expensing mechanism on pages 4 and 5 of its petition:

(1) . . . Peoples also requests authority to adjust the expense based on the Company's budgeted surveillance report if the expected reserve balance reaches certain levels after applying the normal \$640,000 expense amount in a given year. The following adjusted annual expense amounts would apply under the circumstances listed below:

<u>Forecasted Reserve Balance</u>	<u>Adjusted Annual Expense</u>
Asset more than \$2 million	\$1,280,000
Asset more than \$1 million (but less than \$2 million)	\$ 960,000
Asset less than \$1 million	\$ 640,000
Liability less than \$1 million	\$ 640,000
Liability more than \$1 million (but less than \$2 million)	\$ 320,000
Liability more than \$2 million	\$ -0-

(2) Peoples submits that the \$640,000 annual expense amount, adjusted as set forth above, would avoid repeated petitions to the Commission for adjustment of the annual expense amount, while ensuring that the balance in the reserve is limited over time. The amount of the expense would be established at the beginning of each year and the computation thereof would be included in the Company's forecasted earnings surveillance report filing with the Commission.

We note first that this Commission has recognized the possibility that actual costs incurred may exceed accumulated accruals in accumulated provision accounts. Rule 25-6.0143, Florida Administrative Code, provides, in pertinent part, that "charges shall be made to accumulated provision accounts regardless of the balance in those accounts." We recognize that this rule is intended to govern electric utilities and is not per se applicable to natural gas utilities. However, the rule is instructive in this instance due to similarities between the types of accounts

discussed in the rule and natural gas utility accounts under the Uniform System of Accounts for Natural Gas Utilities.

We also note, based on the historical environmental cost data provided by Peoples, that actual costs incurred are not likely to greatly exceed the \$640,000 annual accrual amount. As stated above, Peoples' average annual environmental cost from 1985 to 1997 was \$607,435, and West Florida's average annual environmental cost from 1993 to 1997 was \$39,634. The total of these average annual costs formed the basis for the \$640,000 annual accrual amount. The historical cost data for Peoples shows that its \$607,435 average annual environmental cost exceeded actual costs incurred in nine of the last thirteen years. The historical data for West Florida shows that its \$39,634 average annual environmental cost exceeded actual costs incurred in two out of the last five years. In addition, the historical data shows that if the Company had accrued \$640,000 each year for the last thirteen years, the reserve balance would have never have been over-accrued or under-accrued by the \$2 million threshold established in Peoples' request.

Further, we note that the Company's proposed expensing mechanism may result in a yearly fluctuation in expenses. Based on the historical cost data provided by Peoples, it appears that annual expenses may vary from \$320,000 to \$1,280,000. We believe that this result would defeat one of the main purposes of reserve accounting treatment, which is levelizing expenses. We also note that total expenses for the last thirteen years would have been approximately \$600,000 higher using the Company's proposed expensing mechanism rather than a fixed annual accrual of \$640,000 for each year. Thus, we believe that a fixed accrual based on historical experience will result in a reasonable reserve balance over time.

Based on the foregoing, we find that Peoples' proposed expensing mechanism should be denied. We believe that this finding is consistent with our findings above because a fixed annual accrual amount will better levelize expenses and mitigate their impact on earnings while maintaining a reasonable reserve balance. We do recognize that the Company's actual costs may exceed its reserve balance. If, over time, the reserve balance does not appear representative of costs actually incurred, the Company may file a petition for different treatment.

III. SUSPENSION OF ACCRUAL FOR WEST FLORIDA DIVISIONS

As stated above, Peoples acquired West Florida by merger in June, 1997. The Company's West Florida divisions currently use reserve accounting for environmental costs and are accruing \$198,312 annually to the reserve. In its petition, Peoples requests that this \$198,312 annual accrual be suspended and replaced by its proposed annual accrual of \$640,000 for Peoples' and its West Florida divisions combined. Thus, in the future, all environmental costs associated with the Company's combined operations would be applied against the new environmental reserve accrual.

Based on the historical environmental cost data discussed above, we find Peoples' request reasonable. Further, this accounting treatment should be effective as of January 1, 1998, to correspond with the implementation of the new environmental reserve accrual.

IV. DISPOSITION OF WEST FLORIDA'S ENVIRONMENTAL RESERVE ACCOUNT

By the end of 1997, Peoples' had \$637,521 in costs associated with West Florida's debt. Of this total, \$270,641 related to unamortized debt issuance costs, and the difference related to prepayment premiums of West Florida debt retired by Peoples at the time of the merger. Peoples considers the entire amount to be a regulatory asset and treats this amount as a regulatory asset in its surveillance report. In its petition, the Company states that the debt was retired because there was a net present value savings notwithstanding the prepayment premium.

Peoples explains, in its petition, why these debt-related costs are treated as a regulatory asset on its surveillance report. Peoples states that the generally accepted accounting principles (GAAP) provide that when an unregulated company extinguishes its debt, the gain or loss must be adjusted for issuance costs and for unamortized premiums or discounts. Peoples notes that it has been amortizing the West Florida debt costs in conformity with the Uniform System of Accounts. Peoples states that a regulatory asset is an amount that has been given regulatory treatment different from the GAAP that an unregulated company must follow. Thus, according to Peoples, the balance of debt-related costs is reported as a regulatory asset.

Given this background, Peoples, in its petition, requests authorization to dispose of the June 30, 1997, balance of \$475,306 in West Florida's environmental cost reserve account by writing it off against the December 31, 1997, balance of \$637,521 in unamortized debt costs related to West Florida. Peoples states that this write-off will benefit both ratepayers and the Company. Peoples contends that the ratepayers will benefit because they will not have to support a return on the regulatory asset as part of the rate base, and the Company will benefit by having a more competitive balance sheet. In addition, Peoples states that the proposal will dispose of the West Florida environmental clean-up reserve related to its environmental cost accruals. For the following reasons, we find that Peoples' request should be denied.

By Order No. PSC-94-0452-FOF-GU, we ordered West Florida to apply \$515,622 of its 1993 overearnings to its environmental clean-up reserve. The remainder of its 1993 overearnings were refunded to its customers. In addition, we authorized West Florida to accrue \$198,312 annually for environmental clean-up costs. Specifically, this Commission stated:

Because of the continued uncertainty of the potential liability associated with the clean-up, [West Florida] requested that it be allowed to continue its annual accrual of \$198,312. As a concession for continuing the accrual, [West Florida] proposed that it would refund any accruals in excess of actual expenses, plus interest. We believe that [West Florida's] proposal is reasonable, since it will protect [West Florida] against future liabilities and the customer in the event [West Florida] does not incur anticipated expenses.

Further, we stated that at June 30, 1997, during West Florida's next rate case, or at the discretion of the Commission, any accruals in excess of actual expenses would be reviewed and subject to refund with interest or other disposition, independent of West Florida's earnings.

As of June 30, 1997, West Florida's environmental reserve balance was \$475,306. Peoples informed us that the balance in West Florida's reserve account had increased to \$546,464 at December 31, 1997, and had further increased to \$595,052 at March 31, 1998. We believe that the 1993 overearnings applied to West Florida's environmental reserve are the main factor contributing to the \$546,464 reserve balance at December 31, 1997. Thus, we find that

West Florida's customers provided funds for environmental clean-up costs that were not incurred and should receive a refund in accordance with Order No. PSC-94-0452-FOF-GU.

We believe that West Florida's ratepayers should not be denied a refund of amounts paid prior to the merger simply because of the merger. Although Peoples carries the unamortized debt costs related to West Florida as a regulatory asset on its books, those costs do not represent regulatory assets on West Florida's books. The portion of unamortized debt costs related to prepayment premiums arose only as a result of the merger. Thus, we find that these costs were not a regulatory asset to West Florida. The remaining portion related to West Florida's unamortized debt issuance costs. The regulatory treatment of these costs on West Florida's books was no different than the treatment provided for under GAAP. Thus, we find that the unamortized debt issuance costs did not represent a regulatory asset on West Florida's books.

We note that, based on our findings above, the \$198,312 annual environmental cost accrual formerly applicable to West Florida will be decreased by nearly \$160,000 to approximately \$40,000 annually. This \$160,000 decrease will more than offset the annual amortization of the refinancing costs incurred by Peoples.

We do not agree that Peoples' requested disposition will create the benefits suggested by Peoples. We believe that the requested disposition will have an immaterial impact on Peoples' balance sheet. In addition, we note that the Company's proposal would benefit current Peoples' customers who did not provide these funds, by reducing the amount of interest expense embedded in the capital structure.

In conclusion, we find that the Company's proposed disposition of West Florida's June 30, 1997, environmental cost reserve balance of \$475,306 should be denied. We find instead that the December 31, 1997, reserve balance of \$546,464, plus interest of \$79,870 through July 31, 1998, should be refunded to West Florida's customers on a cents per therm basis, based on actual therm sales for the month of July, 1998. The total refund amount, divided by July, 1998 actual therm sales, shall be refunded to customers in August, 1998. Any dollars remaining after the refund, shall be credited to fuel expense for the following month. Within 60 days of the refund, Peoples shall file a complete report with this Commission indicating the total amount of the refund, total amount of interest, and total amount remaining, if any.

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Our findings in this matter do not represent a retreat from our desire to have regulatory assets written off when earnings permit. We believe that West Florida's merger into Peoples creates a unique situation that requires the action described above.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that Tampa Electric Company d/b/a Peoples Gas System's request to implement reserve accounting for environmental costs is approved. It is further

ORDERED that Tampa Electric Company d/b/a Peoples Gas System shall accrue \$640,000 annually to the environmental cost reserve account, effective January 1, 1998. It is further

ORDERED that Tampa Electric Company d/b/a Peoples Gas System's request to establish an expensing mechanism to adjust the amount annually accrued to its environmental cost reserve account based on expected reserve balances is denied. It is further

ORDERED that Tampa Electric Company d/b/a Peoples Gas System's request to suspend the former West Florida Natural Gas Company's annual environmental cost accrual of \$198,312 is approved. It is further

ORDERED that Tampa Electric Company d/b/a Peoples Gas System's request to dispose of the former West Florida Natural Gas Company's environmental cost reserve account balance by writing it off against a portion of the current balance of unamortized debt costs related to West Florida is denied. It is further

ORDERED that Tampa Electric Company d/b/a Peoples Gas System shall refund \$626,334, consisting of the former West Florida Natural Gas Company's environmental cost reserve account balance plus interest through July, 31, 1998, to West Florida's customers on a cents per therm basis, based on actual therm sales for the month of July, 1998. The total refund amount, divided by July, 1998 actual therm sales, shall be refunded to customers in August, 1998. Any dollars remaining after the refund, shall be credited to fuel expense for the following month. It is further

ORDERED that Tampa Electric Company d/b/a Peoples Gas System, within 60 days of providing the refund, shall file a complete report with this Commission indicating the total amount refunded,

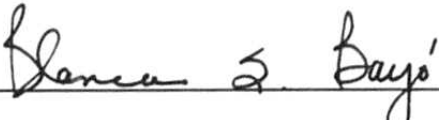
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the total amount of interest refunded, and total amount remaining, if any. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective unless an appropriate petition, in the form provided by Rule 25-22.036, Florida Administrative Code, is received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings or Judicial Review" attached hereto. It is further

ORDERED that in the event this Order becomes final, this Docket shall be closed.

By ORDER of the Florida Public Service Commission this 28th day of May, 1998.



BLANCA S. BAYÓ, Director
Division of Records and Reporting

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

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Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on June 18, 1998.

In the absence of such a petition, this order shall become effective on the day subsequent to the above date as provided by Rule 25-22.029(6), Florida Administrative Code.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days of the effective date of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.