



Public Service Commission

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DATE: SEPTEMBER 14, 2000

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYÓ)

FROM: DIVISION OF SAFETY AND ELECTRIC RELIABILITY (LEE, BREMAN, MCNULTY) *WBM*
 DIVISION OF LEGAL SERVICES (STERN) *MKS RUE EDD*
 DIVISION OF ECONOMIC REGULATION (E. DRAPER, D. DRAPER, LEE, MAUREY, SWAIN) *rs*

RE: *psf* DOCKET NO. 000808-EI - PETITION FOR APPROVAL OF CONSUMPTIVE WATER USE MONITORING ACTIVITY AND SMITH WETLANDS MITIGATION PLAN AS NEW PROGRAMS FOR COST RECOVERY THROUGH THE ENVIRONMENTAL COST RECOVERY CLAUSE BY GULF POWER COMPANY.

AGENDA: 09/26/00 - REGULAR AGENDA - INTERESTED PERSONS MAY PARTICIPATE - PROPOSED AGENCY ACTION

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\SER\WP\000808.RCM

CASE BACKGROUND

On June 30, 2000, Gulf Power Company ("Gulf" or "Company") petitioned this Commission for approval of the Company's Consumptive Water Use Monitoring Activity and Smith Unit 3 Wetlands Mitigation Plan as new programs for cost recovery through the Environmental Cost Recovery Clause ("statute" or "ECRC").

Section 366.8255, Florida Statutes, the ECRC, gives the Commission the authority to review and decide whether a utility's environmental compliance costs are recoverable through the ECRC. The Commission has established, by its own Orders, guidelines for environmental cost recovery through the ECRC. Order No. PSC-94-1207-FOF-EI, issued October 3, 1994, in Docket No. 940042-EI,

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states in part, "...a utility's petition for cost recovery must describe proposed activities and projected costs, not costs that have already been incurred." (emphasis in original, p. 5.) Thus, utilities are expected to petition the Commission for approval of new projects in advance of the project costs being incurred.

Furthermore, Order No. PSC-94-0044-FOF-EI, issued January 12, 1994 in Docket No. 930613-EI, established three criteria for costs to be recovered through the ECRC. According to the Order, costs may be recovered through the ECRC if:

- (1) such costs were prudently incurred after April 13, 1993;
- (2) the activity is legally required to comply with a governmentally imposed environmental regulation enacted, became effective, or whose effect was triggered after the company's last test year upon which rates are based; and,
- (3) such costs are not recovered through some other cost recovery mechanism or through base rates. (p. 6-7)

Staff's review of the petition is based on the statute and these prior Commission Orders implementing the statute.

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve Gulf's petition for the Consumptive Water Use Monitoring Activity as a new program appropriate for recovery through the ECRC?

RECOMMENDATION: Yes. (Lee, Breman, Stern)

STAFF ANALYSIS: The Consumptive Water Use Monitoring Activity is legally required to comply with a governmentally imposed environmental regulation. Gulf is required to install and maintain in-line totaling water flow meters on all existing and future water supply wells at Gulf's Crist and Smith electric generating plants. This requirement is a part of the Consumptive Use and Individual Water Use permits issued by the Northwest Florida Water Management District ("NWFWM"). The relevant permits and the associated requirements for Plant Crist and Plant Smith were issued on November 30, 1999 and August 26, 1999, respectively. Gulf's Smith Plant meters must be installed by August 31, 2000, and Gulf's Crist Plant meters must be installed by December 31, 2000. The new

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requirement is also expected to be a condition of the permit renewal for Plant Scholz in 2005. Rule 40A-2.381, Florida Administrative Code, provides the specific basis for the NFWFMD's authority to impose a condition on any permit issued by the NFWFMD. Gulf has attested that there are no in-line totaling water flow meters currently installed on any of Gulf's existing water supply wells.

Gulf's most recent cost estimate for the Consumptive Use Monitoring Activity is \$205,000 for calendar year 2000. Gulf does not expect to incur any maintenance expenses in the first five years after installation of the flow meters. After that period, additional O&M expenses, currently estimated at a 5-year cycle cost of \$9,000, may be required for the flow meters to be re-calibrated. Costs related to the Plant Scholz flow meters, to be determined when the permit is renewed in 2005, are also expected to be incurred in this program. Gulf uses a combination of bidding and past experience to develop the cost estimates. The costs presented in the petition were projected costs rather than costs that had already been incurred.

Based on Gulf's representation of their actions taken to date, staff believes Gulf has been prudent with respect to the proposed program. The environmental authority (NFWFMD) has set forth the specific compliance requirement for Gulf, and thus no alternative compliance approaches are relevant. Staff will continue to monitor and evaluate the prudence matter in the regular ECRC docket as Gulf's actual costs and other relevant information become available. To insure that the most cost effective compliance action is taken, the Company should continue to monitor costs, trends, technology, and other relevant factors.

Staff believes that Gulf's Consumptive Water Use Monitoring Activity Program qualifies for recovery through the ECRC based on the guidelines established in Order No. PSC-94-1207-FOF-EI and Order No. PSC-94-0044-FOF-EI. The actual expenditures/expenses will be addressed in an up-coming true-up cycle and will be subject to audit. Issues that will determine the specific amount recoverable through the ECRC, such as whether specific costs were prudently incurred and whether they have already been recovered in other mechanisms, will be further examined and resolved in the regular ECRC docket. Gulf is not requesting a change in the ECRC factors that have been approved for 2000. Based on the information currently available, it appears that there is no potential for a significant rate impact. Therefore, the review of Gulf's expenses should be addressed at the November 2000 ECRC hearing.

ISSUE 2: Should the Commission approve Gulf's petition for recovery through the ECRC of the wetland mitigation plan required in order to construct the new Smith Unit 3 plant?

RECOMMENDATION: No. The Commission should deny Gulf's petition for recovery of costs for wetland mitigation through the ECRC for both legal and policy reasons. (Stern, Lee, Breman)

STAFF ANALYSIS: The Smith Unit 3 Wetlands Mitigation Plan ("Smith Plan") is the second activity for which Gulf seeks recovery through the ECRC. This environmental requirement is associated with the planned construction of the new Smith Unit 3 in Bay County. The Commission has never had to decide whether environmental costs associated with construction of new power plants should be recoverable through the ECRC.

The new Unit 3 will result in the unavoidable loss of wetlands that are regulated by the Florida Department of Environmental Protection (FDEP) and the United States Army Corps of Engineers (USACE). To offset the loss of wetlands, the FDEP and the USACE required that existing wetlands near the site be enhanced. Gulf is required to enhance 130 acres of wet pine plantation within a 232-acre parcel of land. The 130 acres will be preserved in perpetuity through a conservation easement or transferred to a resource agency. Various tree species will be planted and monitored for five years. Reporting requirements are also a part of the Smith Plan. This new program will be initiated after the Company's last test year upon which its current base rates were established. The Smith Plan is required by the final order issued in DOAH Case No. 99-2641EPP. This final order meets the definition of "environmental laws or regulations" in Section 366.8255(1)(c) of the ECRC. Staff concurs that the Smith Plan is legally required to comply with a governmentally-imposed environmental regulation.

In its petition, Gulf projected \$1,270,000 in costs related to the Smith Plan for calendar year 2000. Gulf's most recent cost estimates for the Smith Plan are \$360,000 for calendar year 2000 and a total of \$870,000 through calendar year 2005. These expenditures include land purchase and site preparation (\$360,000), tree planting (\$340,000), and monitoring and reports to FDEP (\$170,000). The reduced cost estimates are due to a combination of factors, including the timing of tree planting and the availability of trees that can achieve the same mitigation objective at a lower cost. These types of costs are normally recorded as part of the in-service costs of new power plants.

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The difference between the Smith Plan and prior ECRC petitions is that the Smith Plan is associated with construction of a new power plant, not modifications of an existing power plant. Gulf acknowledges this fact. Gulf believes all environmental compliance costs associated with new power plant construction are appropriate for cost recovery through the ECRC.

Gulf argues that approval of the Smith Plan for recovery through the ECRC is consistent with the ECRC and subsequent Commission orders implementing the statute. Gulf points out that costs associated with new facilities meet the definition of "environmental compliance cost" in Section 366.8255(1)(d) the ECRC. That term is defined as "all costs or expenses incurred by an electric utility in complying with environmental laws or regulations." Section 366.8255(1)(d), Florida Statutes. Furthermore, Gulf contends that its petition is consistent with the Commission's criteria for recovery in Order Nos. PSC-94-1207-FOF-EI and PSC-94-0044-FOF-EI implementing the ECRC. (Those criteria are stated in Issue 1 of this recommendation.) Therefore, Gulf maintains that the Smith Plan should be approved regardless of whether it is associated with new power plant construction.

Staff believes Gulf's petition for cost recovery of the Smith Plan through the ECRC should be denied. Neither the ECRC nor previous orders require the petition to be granted. Furthermore, additional factors such as legislative intent and policy implications should be considered. First, it is the Commission's policy to review ECRC petitions on a case by case basis. See Order No. PSC-93-1304-FOF-EI, issued September 8, 1993, in Docket No. 930169-EI. The Commission has never been presented with a petition for environmental costs associated with construction of new power plants, so there is no guiding precedent. Furthermore, when establishing the criteria in Order Nos. PSC-94-1207-FOF-EI and PSC-94-0044-FOF-EI, which addressed existing power plants, there is no indication that the Commission was considering the applicability of the criteria to new power plants.

Second, staff believes the statute allows the Commission some discretion in deciding which prudently incurred environmental costs can be approved. Section 366.8255(2) states:

An electric utility may submit to the commission a petition describing the utility's proposed environmental compliance activities and projected environmental compliance costs in addition to any Clean Air Act compliance activities and costs shown in a utility's filing under Section 366.825. If approved, the

commission shall allow recovery of the utility's prudently incurred environmental compliance costs. (Emphasis added.)

The ECRC falls short of expressly requiring that all prudently incurred environmental costs be approved for recovery. While the statute grants the Commission discretion, that discretion must be exercised fairly and in accordance with the legislative intent. As will be discussed in more detail later, the legislative history indicates that environmental costs associated with new power plants were not to be recovered through the ECRC. Given the discretion provided in Section 366.8255(2), and the legislative history, staff believes the Commission should deny that part of Gulf's petition pertaining to recovery for the Smith Plan through the ECRC.

Section 366.01, Florida Statutes, states that the provisions of Chapter 366 are to be liberally construed to protect the public welfare. The authority to construe a statute liberally allows the Commission to look beyond the letter of the law to the spirit of the law. Words may be omitted or added by implication to effectuate legislative intent. See 73 Am. Jur. 2d, Statutes § 272; 49 Fla. Jur., Statutes § 187.

The legislative history of the ECRC indicates that environmental costs associated with new power plants were not intended to be recoverable through the clause. Representative Tobin, the sponsor of the legislation in the House, is reported in the *Journal of the Florida House of Representatives* as stating:

The intent is not to authorize recovery through this procedure of new plant construction costs. The intent is to allow the recovery of modifications to existing plants in order to bring them into compliance with environmental standards. 95th Reg. Sess., Mar. 24, 1993, p. 672.

It should be noted that comments made in the House Journal are typically not considered to be the best indicator of legislative intent. See *The Search for Intent: Aids to Statutory Construction in Florida - An Update*, 13 Fla. St. U.L. Rev. 485, 505-6 (1985). In this case, however, the committee reports from the Senate offer no real analysis of the legislation. See Fla. S. Comm. On Com., SB 584, Staff Analysis (Feb. 20, 1993); Fla. S. Comm. On Com., CS/SBs 582 & 584 Staff Analysis (Feb. 23, 1993). In the House, the ECRC was added to HB 2129 as an amendment on the floor and then voted on so committee reports do not address it. Fla. H.R. Comm. on Bus. & Prof. Reg., HB 2129 (Apr. 19, 1993). Representative Tobin's remarks were not opposed or questioned when he made them.

Of the various cost recovery clauses associated with the electric industry, only the ECRC is embodied in statute. The other similar clauses - fuel, conservation and capacity - were created by Commission Order. Given the limited legislative history on the ECRC, it is informative to consider the rationale for creating the other clauses.

It appears the intent behind the clauses is to address costs that may fluctuate significantly and unpredictably from year to year. In such cases, the costs included in a test year would not adequately capture future costs. The fuel clause, which was the first to be created, is a good example. The docket that created the current version of clause, Docket No. 74680-CI, was opened in response to the dramatic rise in fuel costs in the mid-1970s. See Order No. 6357, Nov. 26, 1974. At that time, the cost of fuel was a significant and volatile part of the utilities' expenses. The clause provided a method for ensuring that utilities could recover fluctuating costs quickly. See *id.*; Order No. 13452, issued in Docket No. 820001-EU-A, on June 22, 1984.

Construction of a new plant can not be characterized as an unpredictable event. It is a predictable event, as evidenced by inclusion of new plants in the utilities' ten-year site plans, submitted annually, and the requirement to solicit bids for construction of new plants in Rule 25-22.082, Florida Administrative Code. Because the event of construction is predictable, the utility is able to anticipate when it will incur costs. Furthermore, much of the planning process is under the control of the utility, unlike costs of fuel or changing environmental regulations for existing plants which increase the costs on which base rates are set. Thus, the rationale behind the clauses does not apply in the case of planned construction of a new power plant.

In addition to the text of Chapter 366, legislative intent, and the Commission's intent as expressed in orders for other similar clauses, policy considerations warrant against recovery of environmental costs for new power plants through the ECRC. If Gulf's petition is approved the door will open for recovery of a class of expenses that are quite large. Because many of the components of a new plant must meet environmental requirements, a substantial percentage of the cost of a new plant could be recovered through the ECRC. For example, the cost of selective catalytic reduction and the cost of the Gannon repowering project (required by FDEP and EPA orders) could be recovered through the ECRC if this door is opened. In fact, it could be difficult to

determine which costs would not be eligible for recovery through the ECRC.

Denial of Gulf's petition to recover costs for the Smith Plan through the ECRC does not mean the costs will not be recovered. Gulf can include the costs in its monthly earnings surveillance reports and recover the costs through base rates. This is the method that has always been used to recover costs associated with construction of new power plants.

In summary, staff believes Gulf's petition to recover costs for the Smith Plan through the ECRC should be denied for the following reasons: 1) the legislative history of the ECRC indicates that environmental costs associated with new power plants were not intended to be recoverable through the clause; 2) the other clauses implemented by the Commission have been adopted, in part, to respond to unpredictable costs, and the costs associated with construction of new power plants does not rise to the same level of unpredictability; 3) allowing recovery of environmental compliance costs associated with new power plant construction may substantially increase the amount of costs recovered through the clause because many components of a new plant must meet environmental requirements; and 4) the ECRC and prior orders allow the Commission the discretion to deny recovery through the clause of environmental compliance costs associated with construction of new power plants.

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ISSUE 3: Should this docket be closed?

RECOMMENDATION: Yes, this docket should be closed upon issuance of a Consummating Order unless a person whose substantial interests are affected by the Commission's decision files a protest within 21 days of the issuance of the proposed agency action. (STERN)

STAFF ANALYSIS: If no timely protest to the proposed agency action is filed within 21 days of the date of issuance of the Consummating Order, this docket should be closed upon the issuance of the Consummating Order.