BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

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| In the matter of:<br><br>Investigation into earnings for 1995 and 1996 of Tampa Electric Company | DOCKET NO. 950379-EI |

VOLUME 1

Pages 1 through 146

PROCEEDINGS: HEARING

BEFORE: CHAIRMAN JULIA L. JOHNSON
COMMISSIONER J. TERRY DEASON
COMMISSIONER SUSAN F. CLARK
COMMISSIONER JOE GARCIA
COMMISSIONER E. LEON JACOBS, JR.

DATE: Monday, December 7, 1998

TIME: Commenced at 9:25 a.m.

PLACE: Betty Easley Conference Center
Room 148
4075 Esplanade Way
Tallahassee, Florida

REPORTED BY: MARY ALLEN NEEL, RPR

APPEARANCES:

LEE L. WILLIS and KENNETH R. HART, Ausley & McMullen, Post Office Box 391, Tallahassee, Florida 32303, on behalf of Tampa Electric Company.

VICKI GORDON KAUFMAN, McWhirter, Reeves, McGlothlin, Davidson, Decker, Kaufman, Arnold & Steen, 117 South Gadsden Street, Tallahassee, Florida 32301, on behalf of Florida Industrial Power Users Group.

JOHN ROGER HOWE, Office of Public Counsel, c/o The Florida Legislature, 111 West Madison Street, Room 812, Tallahassee, Florida 32399, on behalf of the Citizens of the State of Florida.

WILLIAM COCHRAN KEATING IV and ROBERT V. ELIAS, Florida Public Service Commission, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, on behalf of the Commission Staff.

# I N D E X

## WITNESSES - VOLUME 1

EXHIBITS - VOLUME 1

P R O C E E D I N G S

CHAIRMAN JOHNSON: We're going to go on the record. Counsel, could you please read the notice.

MR. KEATING: Pursuant to notice issued October 28, 1998, this time and place have been set for a hearing in Docket No. 950379-EI, investigation into earnings for 1995 and 1996 of Tampa Electric Company.

CHAIRMAN JOHNSON: Take appearances.

MR. WILLIS: I'm Lee L. Willis, appearing together with Kenneth R. Hart of Ausley & McMullen, P.O. Box 391, Tallahassee, Florida 32302, appearing on behalf of Tampa Electric Company.

MS. KAUFMAN: Vicki Gordon Kaufman of the McWhirter Reeves law firm, 117 South Gadsden Street, Tallahassee, 32301. I'm appearing on behalf of the Florida Industrial Power Users Group.

MR. HOWE: Commissioners, I'm Roger Howe with the Public Counsel's Office, appearing on behalf of the Citizens of the State of Florida. The address is as shown in the Prehearing Order.

MR. HOWE: Cochran Keating and Bob Elias appearing on behalf of the Commission Staff.

CHAIRMAN JOHNSON: Are there any preliminary matters?

MR. KEATING: There is one. On Issue 3, I believe we can stipulate that issue. Staff has prepared an exhibit, and I believe the parties --

CHAIRMAN JOHNSON: For some reason I can't hear you very well. You may just need to get close to the microphone.

MR. KEATING: Is this picking up?

COMMISSIONER GARCIA: No. Try again.

MR. KEATING: Is this picking up any better?

COMMISSIONER GARCIA: Are you picking him up?

CHAIRMAN JOHNSON: She is, but we aren't.

COMMISSIONER GARCIA: Just speak louder.

CHAIRMAN JOHNSON: You're going to have to just scream. And, Bob, maybe turn on both and then turn them towards him.

COMMISSIONER GARCIA: You know what it is, Madam Chairman? I just don't think it's broadcasting, but she's picking it up. She's hearing everything we're seeing.

CHAIRMAN JOHNSON: Go ahead.

MR. KEATING: Okay. On Issue 3, I believe we can show that issue stipulated. Staff has prepared an exhibit that's being handed out right now. The parties have agreed to stipulate this exhibit into the record, and these numbers on the exhibit address the issue that's being stipulated.

CHAIRMAN JOHNSON: This document, does it need to be identified?

MR. KEATING: Yes, it does. I'm sorry.

CHAIRMAN JOHNSON: Okay. We'll identify it as Exhibit 1. What's a good short title for it?

MR. KEATING: Impact of separation factors on adjustments and on components of rate base and NOI.

CHAIRMAN JOHNSON: It will be identified as stated.

(Exhibit 1 was marked for identification.)

MR. KEATING: Staff would also -- now it's on.

CHAIRMAN JOHNSON: It wasn't on. Okay. Thank you.

MR. KEATING: Staff would also like to add -- we believe that the calculation of future deferred revenues should include the impact of these adjustments as of December 1, 1996, if that's acceptable to the parties.

CHAIRMAN JOHNSON: Is that acceptable to the parties?

MS. KAUFMAN: Madam Chairman, we do not have an objection to the exhibit, and we are prepared to accept Staff's calculation. But when I checked with my expert, we did not have the work papers in order to check the calculation in detail. It looks like it's going in the right direction, and we don't object.

However, we would just like the record to reflect that this calculation will not be precedential for future proceedings involving overearnings.

CHAIRMAN JOHNSON: Any other comments? Mr. Willis?

MR. WILLIS: Well, the calculation is whatever it is. We have done it correctly for this proceeding, I think, based on this exhibit, and it will have whatever effect it has.

MR. HOWE: Chairman Johnson, I would support Ms. Kaufman's comments. I would point out to you, for 1996, this separation only affects I believe the last two weeks of the year. For 1997, the FMPA and Lakeland sales will be in there perhaps for a full year, and I think that's why we're a little bit concerned. But as it reflects 1996 data, we accept this document.

CHAIRMAN JOHNSON: Okay. And could you again tell me what language are you looking for?

MS. KAUFMAN: Chairman Johnson, in the

Prehearing Statement, under Issue 3, FIPUG has submitted language that would be acceptable to us. And it simply says that our position will not be viewed as precedent in this issue, and it's without prejudice for any party to take any position in a future proceeding regarding the separation issue.

CHAIRMAN JOHNSON: Okay. And do you object to that language?

MR. WILLIS: Well, I think that can be her position going forward, and we all can take whatever position we take in the future. But this exhibit settles this matter for this hearing.

CHAIRMAN JOHNSON: Well, I understand, and maybe I'm overreading what you're saying, but I understand that in order for this to be a stipulated kind of exhibit, she needed that comfort language. Otherwise, it's not going to be stipulated to.

MS. KAUFMAN: Right. We agree with Mr. Willis. For purposes of 1995, we are prepared to accept this calculation. However -- I mean 1996. Excuse me. However, as Mr. Howe pointed out, this will be a much more significant issue in years going forward, and we want our position to be without prejudice to take any position on the future calculation.

COMMISSIONER CLARK: I don't see what's wrong with that.

CHAIRMAN JOHNSON: I don't either. Do you have a problem with that? And the only reason I'm hesitating is, this is supposed to be something you all are stipulating, and I need to have some agreement.

MR. WILLIS: We have no objection.

CHAIRMAN JOHNSON: Thank you. Anything else?

MS. KAUFMAN: Chairman Johnson, just one more thing. We would like the order to so reflect. Would that be all right?

CHAIRMAN JOHNSON: And I think that's understood.

MR. HART: Madam Chairman, we have one more preliminary matter.

CHAIRMAN JOHNSON: Yes, sir.

MR. HART: There's a package of orders that the Prehearing Officer has ruled are to be officially noticed for purposes of this proceeding, and we would like those marked as an exhibit.

CHAIRMAN JOHNSON: Okay. We'll mark them as Composite Exhibit 2, and it will be short titled TECO's orders to be officially -- or orders that TECO has requested official recognition.

MR. HART: Yes.

(Exhibit 2 was marked for identification.)

CHAIRMAN JOHNSON: Okay.

MR. KEATING: I'm not aware of any other preliminary matters.

CHAIRMAN JOHNSON: Now, do we need to then -- do we need to go to Issue 3, and would the Commissioners vote at this time on Issue 3?

MR. KEATING: I don't think that that's necessary.

CHAIRMAN JOHNSON: Okay.

COMMISSIONER DEASON: Let me ask a question about Exhibit No. 1. Contrast -- someone explain to me what the information at the top of the page is in relation to the information at the bottom of the page. It's both rate base and income statement information, but obviously it pertains to two different matters, and I'm trying to understand what's what.

MS. MERTA: Yes, Commissioner. When the separation factors change, two things are impacted. One of them is -- and if you can picture the earnings surveillance report, the first thing that's impacted is the -- actually is at the bottom of the page, the components of rate base and NOI, and that happens between the system number and the retail number. So that affects every component of rate base.

Then the second thing that's affected by the separation factor is the amount to be --

COMMISSIONER DEASON: Slow down for a second. Where is the system numbers, and where is the retail number?

MS. MERTA: On the earnings surveillance report?

COMMISSIONER DEASON: No. I'm trying to understand your -- the title of these columns have something to do with the data request, and adjustments were made subsequent, and there's a difference.

MS. MERTA: Oh, I see.

COMMISSIONER DEASON: What is just the basis of this exhibit? What does it purport to represent?

MS. MERTA: This is just the incremental adjustment to rate base and NOI of the 15 additional days in December. Data Request No. 15 was the prior response from the Company that gave us the figures for the prior months. And the Company in that calculation only gave us 15 days of December, and they -- subsequently in testimony the Company agreed that there should be a full month of December separated instead of just the 15 days.

So the second column reflects the additional 15 days impact of the separations. So we compare the 15 additional days with the original response, and then we get the incremental adjustment to NOI and rate base.

COMMISSIONER DEASON: For the additional 15 days?

MS. MERTA: Pardon me?

COMMISSIONER DEASON: For the additional 15 days?

MS. MERTA: Yes, sir.

COMMISSIONER DEASON: Okay. Now, what do you do with that after you have that?

MS. MERTA: Well, we make an adjustment to -- we'll make an adjustment to our calculation for deferred revenues in '96.

COMMISSIONER DEASON: Okay. Now, what is the difference between the information at the top of the page and the information at the bottom of the page?

MS. MERTA: The information at the top of the page is the impact on the adjustments to rate base and NOI that the Company made in the earnings surveillance report. That's just the adjustments that they made. The bottom of the page reflects the difference in the components of rate base. In other words, the separation factors, when they change, they affect every component of rate base and NOI, and that's what the bottom part of the page calculates.

COMMISSIONER DEASON: Thank you.

CHAIRMAN JOHNSON: Any other questions, Commissioners?

COMMISSIONER JACOBS: So we're looking at an overall reduction in rate base; correct?

MS. MERTA: Actually, Commissioner, in the separation factors that affect the adjustments, we're going to have an increase to rate base of 16,777. Then the impact of the components of rate base, we do have a decrease of 812,797.

COMMISSIONER JACOBS: Okay. Will there be impacts to retail rates from that, or is that so low that it wouldn't have a meaningful impact?

MS. MERTA: I'm sorry. I didn't hear you.

COMMISSIONER JACOBS: Is that amount large enough to have any legible impact to retail rates?

MS. MERTA: It won't affect rates. It will affect the amount of the deferred revenues.

COMMISSIONER JACOBS: Oh, that's right.

Okay.

CHAIRMAN JOHNSON: Is that it? Does Staff have any other preliminaries?

MR. KEATING: Not that I'm aware of.

CHAIRMAN JOHNSON: Then I guess we're prepared to swear in the witnesses.

(Witnesses collectively sworn.)

CHAIRMAN JOHNSON: Thank you. You may both be seated.

TECO?

MR. WILLIS: We call Ms. Bacon.

COMMISSIONER CLARK: Has any testimony been stipulated into the record? Where is Mr. Pollock?

MS. KAUFMAN: Mr. Pollock hopefully is en route, Commissioner Clark.

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DELAINE M. BACON

assumed the stand as a witness on behalf of Tampa Electric Company and, having been previously sworn, testified as follows:

DIRECT EXAMINATION

BY MR. HART:

Q Ms. Bacon, would you please state your name, your business address, and your position with Tampa Electric?

A Yes. My name is Delaine M. Bacon. My business is Tampa Electric Company. The address is 702 North Franklin Street, and I'm Director of Utility Financial Analysis.

Q Did you prepare a document entitled "Direct Testimony of Delaine M. Bacon" and cause it to be filed in this proceeding?

A Yes, I did.

Q Do you have any corrections to your testimony?

A No, I do not.

Q Ms. Bacon, if I were to ask you the questions in your prepared testimony, would your answers be the same?

A Yes, they would.

MR. HART: I would ask that Ms. Bacon's testimony be inserted into the record as though read.

CHAIRMAN JOHNSON: It will be so inserted.

TAMPA ELECTRIC COMPANY
DOCKET NO. 950379-EI
SUBMITTED FOR FILING 09/28/98

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DIRECT TESTIMONY

OF

DELAINE M. BACON

Q. Please state your name, business address and position with Tampa Electric Company.

A. My name is Delaine M. Bacon. My business address is 702 North Franklin Street, Tampa, Florida, 33602. I joined Tampa Electric Company ("Tampa Electric" or "company") in October 1984 and have held various positions within the Regulatory Affairs department. Currently, I am the Director of Utility Financial Analysis - Regulatory Affairs for TECO Energy, Tampa Electric Company's parent. I am responsible for financial-related regulatory issues before the Florida Public Service Commission ("Commission") for Tampa Electric, as well as developing the company's long-term financial forecasts.

Q. Please state your educational background and qualifications.

A. I have a Bachelor of Science in Accounting from St. Leo College and a Masters of Business Administration from the University of Tampa. I am a Certified Public Accountant and a member of the Florida Institute of Certified Public Accountants.

Q. What is the subject of your direct testimony?

A. I address the Commission's orders which determined the interest rate to be applied to deferred revenues in Tampa Electric's regulatory capital structure for 1996, and relevant Commission precedent for this treatment. I also address the appropriate regulatory accounting separation in 1996 for Tampa Electric's City of Lakeland ("Lakeland") and Florida Municipal Power Agency ("FMPA") wholesale sales contracts.

**Interest on Deferred Revenues**

Q. Please identify the Commission orders that are applicable to this proceeding.

A. In the Stipulation Agreements between the Office of Public Counsel ("OPC"), the Florida Industrial Power Users Group ("FIPUG") and Tampa Electric, the parties agreed to an interest rate equal to the 30-day commercial paper rate on the balance of revenues deferred from 1995 and 1996. In the company's 1995 earnings review (Order No. PSC-97-0436-FOF-EI), the Commission included the deferred revenue balance as a specific item in the company's regulatory capital structure, concluding that these deferred revenues were a source of funds for Tampa Electric.

Because the parties had stipulated that the deferred revenues balance should accrue interest at the 30-day commercial paper rate, the Commission also made a decision in Order No. PSC-97-0436-FOF-EI to apply a 30-day commercial paper rate to this source of funds in the capital structure. The Commission explained in its decision that this treatment was consistent with prior Commission decisions.

In Tampa Electric's 1996 earnings review (Order No. PSC-98-0802-FOF-EI), the Commission again determined that the 30-day commercial paper rate should be applied to the deferred revenues specifically identified in the capital structure. In June of this year, the OPC and FIPUG protested the Commission's decision contending that a zero cost rate should be applied to the deferred revenues in the capital structure.

Q. Please provide the background and purpose of the deferred revenues.

A. Tampa Electric made substantial reductions in its level of operating expenses beginning in 1994 in order to offset the anticipated increase in revenue requirements associated with the company's Polk Power Station ("Polk"), which was to be placed into service in late 1996. In 1995 and 1996, the Commission approved a regulatory accounting treatment in which Tampa Electric would defer earnings in excess of its allowed return on equity in 1995 and 1996 to be included as a part of Tampa Electric's earnings in 1997 and 1998 to offset the additional revenue requirements of Polk.

This regulatory accounting treatment was agreed upon in settlements between the OPC, the FIPUG and Tampa Electric. Rather than have Tampa Electric refund overearnings and file a petition for a rate increase at the same time, the parties agreed that rate stability for customers was important, and they agreed to a regulatory treatment(the Stipulations) that would defer revenues into years where the return on equity would be adversely affected by the new unit.

In addition to the agreement to defer revenues into 1997 and 1998 to offset Polk revenue requirements, the company agreed to refund or return $50 million to customers over the October 1996 to December 1998 time period. This equates to over half of the revenues deferred from 1995 and 1996, and is equivalent to a 2.5 percent reduction in the average residential base rate over a 27-month period. The company also agreed to freeze base rates through 1999, absorb $12 million of new annual base rate revenue requirements previously recovered through the Oil Backout Clause, share equity returns on a 60/40 basis with customers even as the company earned within its allowed return on equity range, and potentially refund additional earnings to customers in 1999 and 2000.

Q. Please summarize the Commission's decision in Order No. PSC-97-0436-FOF-EI related to the treatment of deferred revenues in the capital structure and the Commission's stated reasons in that decision.

A. In the 1995 earnings surveillance report, deferred revenues were included in the capital structure on a pro-rata basis across all sources of capital, consistent with the treatment in the company's tax savings docket. As explained earlier, the Commission made a decision in Order No. PSC-97-0436-FOF-EI to treat deferred revenues in the capital structure as a separate item, and applied a cost rate at the 30-day commercial paper rate as specified in Rule 25-6.109, F.A.C.

The transcript of the March 18, 1997 agenda conference for the 1995 earnings review, which resulted in Order No. PSC-97-0436-FOF-EI, shows that the following factors were considered when the Commission made its decision: it was patently fair to include the same rate in the capital structure as utilized for refund purposes; the Commission's rule called for a commercial paper rate to be applied for refund purposes, and therefore the commercial paper rate was the cost of capital and should be utilized in the capital structure; the Stipulation was silent on the proper treatment, and therefore the Commission was free to utilize what it concluded was appropriate accounting; and, the Commission should not apply one cost for capital structure purposes and another cost for refund purposes.

Q. What precedent did the Commission reference in Order No. PSC-97-0436-FOF-EI in making its decision to include deferred revenues in the capital structure at the 30-day commercial paper rate?

A. Page 5 of Order No. PSC-97-0436-FOF-EI states that the Commission's method for applying interest to the deferred revenues is consistent with prior cases involving Quincy Telephone, Order No. 22367 (Docket No. 890292 & 891237), Southern Bell, Order No. 94-0172-FOF-TL (Docket No. 920260) and Florida Public Utilities Company - Fernandina (FPUC - Fernandina), Order No. 97-0135-FOF-EI (Docket No. 961542-EI).

Q. Please provide more detail of these orders referenced by the Commission.

A. In the Quincy Telephone docket, the Commission ordered the company to set aside surplus revenues from 1987, 1988, 1989 and the first six months of 1990. This revenue of $504,000 was to accrue interest at the 30-day commercial paper rate and then be returned to the company beginning January 1, 1991. The annual credit was $200,000 until the full amount was exhausted. The Commission stated in its Order No. 97-0436-FOF-EI that these deferred revenues "were included in the capital structure and allowed to accrue interest at the thirty-day commercial paper rate." This scenario is comparable to Tampa Electric's deferred revenue agreement.

In the Southern Bell case (Docket No. 920260), revenues from 1994, 1995 and 1996 were deferred for eventual refund to customers. These deferred revenues were included in the capital structure as a specific adjustment to short-term debt and allowed to accrue interest at the 30-day commercial paper rate. This case, likewise, is relevant precedent to Tampa Electric's case.

FPUC - Fernandina earned above its allowed return on equity in 1995. The Commission made a decision in Order No. 97-0135-FOF-EI to defer these overearnings into 1996 to be booked to FPUC - Fernandina's storm damage reserve. For its 1995 surveillance report, the overearnings were specifically included as short-term debt in the capital structure with an effective interest rate of 5.97 percent. The short-term or 30-day commercial paper rate was correspondingly used in calculating the interest to be added to the 1995 excess earnings. This capital structure treatment is identical to what the Commission ordered in Tampa Electric's 1995 and 1996 earnings reviews.

Q. Please explain the effect of using a zero cost in the capital structure for deferred revenues as proposed by OPC and FIPUG.

A. Using a zero cost rate for deferred revenues in the capital structure goes against financial and regulatory theory and against Commission precedent. It has the effect of treating the interest expense being accrued by the company as though it is not a legitimate cost of providing service and, therefore, leaves the cost to be absorbed by the utility's shareholders "below the line." The company would not be afforded an opportunity to achieve the return on equity disclosed in its surveillance report because the interest expense being incurred would effectively be disallowed.

Since the company is obligated to accrue this interest pursuant to Commission order, it is clearly reasonable to include it in the determination of regulatory earnings. It should not be treated in a manner that, in effect, represents a disallowance of an expense ordered by the Commission.

Q. The protest from the FIPUG states that the Stipulations called for interest to come from "below the line," not "above the line." Did the Stipulations discuss or state that interest on the deferred revenues was to come from "below the line?"

A. No. There is no discussion in the Stipulations calling for interest expense to be paid by shareholders. The reference to interest on deferred revenues in Paragraph 9 of Order No. PSC-96-0670-S-EI states:

> "The revenues held subject to refund and the deferred revenues provided for herein shall accrue interest at the 30-day commercial paper rate as specified in Rule 25-6.109, Florida Administrative Code."

The reference to interest on deferred revenues in Paragraph 6 of Order No. PSC-96-1300-S-EI states:

> "The revenues held subject to refund shall accrue interest calculated at the thirty-day commercial paper rate as specified in Rule 25-6.109, Florida Administrative Code."

These statements in no way indicate that the company's shareholders should pay for the interest to be applied to deferred revenues. There also was no indication by the parties during negotiations that these costs, that are required by the Stipulations, would be disallowed in the calculation of the company's returns on equity. Absent any language in the Stipulations to the contrary, the Commission should treat the interest on deferred revenues as a legitimate cost of providing service.

Q. In its protest of Order No. PSC-98-0802-FOF-EI, the OPC alleges that Tampa Electric's customers are harmed by the Commission's decision in Order No. PSC-98-0802-FOF-EI not to assign a zero cost to deferred revenues in Tampa Electric's capital structure for purposes of calculating the company's allowed rate of return for 1996. Please address this concern.

A. Customers are not harmed by this order because it does not treat them unfairly. In 1996, the company applied an interest rate to deferred revenues in the capital structure that corresponded to the rate being applied to the deferred revenue balance. The alternative proposed by the OPC and FIPUG to use a zero cost rate for deferred revenues in the capital structure could only be considered fair to customers and the company if interest was not being accrued on the deferred revenue balance.

In addition, as explained earlier, Commission precedent clearly establishes the principle that when the cost rate is applied consistently to the deferred revenue balance and to the deferred revenues in the capital structure, customers as well as the company are treated properly.

Q. Are there any situations similar to deferred revenue interest in which the expense is included in the calculation of earnings?

A. Yes. Interest accrued on customer deposits is similar to interest for deferred revenues. In both cases, the Commission has approved an accounting method for funds collected from customers in which the ultimate disposition of those funds is not certain.

In the case of customer deposits, amounts are collected as security on the customer's account and interest is accrued on these amounts. Later, the deposit plus accrued interest is returned to the customer or the company retains the amount plus any accrued and unpaid interest for application to unpaid bills.

The deferred revenues situation is similar. Interest is accrued on deferred revenues because such revenues are initially deemed to represent overearnings, with customers entitled to the benefit of interest on any such amounts. The deferred amounts plus the accrued interest are designed for return to customers in the form of refunds, subject to a prior claim by the company, as is the case of customer deposits. In the customer deposits case, the claim is based on a failure by the customer to pay for services, while in the deferred revenues case, the claim is based on the company's failure to achieve the return on equity previously determined by the Commission to be proper.

Q. Is the treatment of deferred revenues and customer deposits unusual?

A. No. It is consistent with the manner in which other sources of funds are treated in Tampa Electric and other utilities' capital structures for purposes of determining base rates.

**Separation of the Lakeland and FMPA Sales in 1996**

Q. Please describe the FPSC decision regarding the treatment of the FMPA and Lakeland contracts in Order No. PSC-97-1273-FOF-EI.

A. The Commission ordered Tampa Electric to separate capital and O&M costs associated with the wholesale sales made to FMPA and Lakeland in accordance with the procedure approved in the company's last rate case.

> "We find that the Stipulation approved pursuant to Order No. PSC-96-1300-S-EI requires TECO to separate capital, and operation and maintenance (O&M) costs associated with the FMPA and Lakeland wholesale sales.

Specifically, 5F of the order states, "The separation procedure to be used to separate capital and O&M which was approved in the Company's last rate case, Docket No. 920324-EI, shall continue to be used to separate any current and future wholesale sales from the retail jurisdiction."

Q. Please describe the separation methodology approved in the company's last rate case, Docket No. 920324-EI.

A. The approved method of separation in the company's last rate case was based upon the 12 coincident peak methodology. This methodology calls for a separation of costs to the wholesale jurisdiction that is based on the actual amount of resources used to serve the wholesale customer at the time of the company's monthly coincident peak.

Q. Please describe the calculation used by the company to comply with the FPSC order to separate FMPA and Lakeland in 1996.

A. The process used by the company to separate the FMPA and Lakeland contracts in 1996 is consistent with the methodology used by the company since the last rate case. In that process, separation factors are adjusted in its surveillance report based on any new wholesale sales being served from Tampa Electric's resources.

For the FMPA and Lakeland contracts, the separation factors were adjusted for the load served out of the resources used in the month of December 1996. Because the sale to FMPA did not begin until December 16, the separation for FMPA was adjusted only to reflect the time during the month the contract was in effect.

In retrospect, the company realizes that the proration of a month is not explicit in the 12 month coincident peak method and agrees to separate the full amount for December 1996. The company will make an accounting entry in 1998 to reflect this change which should increase the deferred revenue balance.

Q. Does this conclude your testimony?

A. Yes, it does.

BY MR. HART:

Q Ms. Bacon, would you please summarize your testimony?

A Yes, sir.

Good morning, Commissioners. We are here today as a result of protests by OPC and FIPUG of your order approving Tampa Electric's earnings for 1996. In this order, you specifically identified deferred revenues in Tampa Electric's capital structure for 1996 and assigned a cost rate equal to the 30-day commercial paper rate, which is also being used to calculate the interest accrual applied to the deferred revenue balance. This is the same treatment that you approved in several other dockets before this Commission and in your order approving Tampa Electric's earnings for 1995.

Commissioners, OPC and FIPUG argue that this cost rate for deferred revenues in the capital structure should be zero. However, the deferred revenues were the source of funds used during 1996 to fund the Company's operations, and therefore, any cost associated with these funds should be recoverable as a prudent and reasonable cost of providing service to its customers. For this expense to bear a zero rate in the capital structure can only mean that the

Company has been disallowed a prudent cost.

When this Commission disallows a cost, it is because the cost is unrelated to regulated utility service or was imprudently incurred. The interest on the deferred revenues does not meet this criteria. The interest accrual is required by the stipulations, it was adopted by the parties and the Commission, and the interest expense associated with this accrual is being properly booked.

Commissioners, we believe that the accounting treatment that you affirmed in your PAA order for the interest on deferred revenues is appropriate for both ratepayers and the Company. When the Company included a replacement source of funds in its 1995 deferred revenue filing equal to the overall cost of capital, you decided that the cost rate to apply to the deferred revenues in the capital structure should be equal to the rate utilized to accrue the interest on the deferred revenues. Your currently approved symmetrical treatment of deferred revenue interest is the proper method.

In addition, this Commission's precedent on this topic is very clear on the proper capital structure treatment and has been cited in your orders for Tampa Electric's '95 and 1996 earnings reviews.

The Quincy Telephone, Florida Public Utilities, and Southern Bell cases fully represent this appropriate capital structure treatment of deferred customer supplied dollars.

Finally, Commissioners, Tampa Electric would not have agreed to a disallowance without it being very clearly defined and stated in the stipulations. The language in the stipulations certainly does not specify that the interest would be absorbed by the shareholders. The language is clear that all reasonable and prudent expenses should be included in the calculation of deferred revenues. Your current treatment corresponds with the requirement of the stipulation in regards to both the interest provision and recovering prudent costs. Any other interpretation is inappropriate and inconsistent with the stipulations and current Commission practice.

Thank you.

Q Ms. Bacon, does that conclude your summary?

A Yes, it does.

MR. HART: We would tender the witness for cross examination.

CROSS EXAMINATION

BY MR. HOWE:

Q Good morning, Ms. Bacon.

A Good morning.

Q I have found for my own purposes to understand the issues in this, it's best for me to kind of follow through chronologically from 1995 into 1996. And I believe you stated, did you not, that the Commission's treatment of the deferred revenues for 1996 was consistent with its treatment for 1995?

A Yes, it is.

Q Could you please refer to Order No. PSC-95-0580? Commissioners, that's in one of the tabbed orders.

A Okay.

Q Ms. Bacon, are you familiar with this order?

A Yes, I am.

Q And would you agree that this order defines the manner in which deferred revenues are to be calculated and treated for 1995?

A Yes, it does.

Q Would you refer to the last page of that order, please. This attachment is Tampa Electric Company's proposal which was accepted by the Commission in Order No. 95-0580, is it not?

A Yes, hold on just a second. I don't know what page you're referring to. I don't happen to see it in this particular --

Q Do you have the compilation of orders that the Company distributed?

A No, I do not.

Now I do.

Okay. Now, you're referring to the last page of the written portion of the order?

Q The last page of the order itself, which is an attachment. It's page 5.

A I don't see this.

MR. WILLIS: Could you give us the order number again?

MR. HOWE: Order No. PSC-95-0580.

WITNESS BACON: 95.

MR. HOWE: Dash 0580. It's dated May 10, 1995.

WITNESS BACON: Okay. Now I have it.

BY MR. HOWE:

Q All right. Maybe we need to revisit those earlier questions.

A I see the last page. It is Tampa Electric's proposal.

Q All right. Now, in the second paragraph of the proposal, Tampa Electric agreed to defer a revenue amount of $15 million, did it not?

A Yes, it did.

Q And that $15 million was not tied to any earnings level, was it?

A That's correct.

Q Did Tampa Electric actually make that deferral?

A Yes, it did.

Q All right. And would you agree that pursuant to Paragraph 3, that if Tampa Electric had earnings or revenues above 11.75% return on equity after accounting for the $15 million, that they would then go into the sharing arrangement in Paragraph 3?

A That's correct.

Q And in Paragraph 3, it provides that the sharing arrangement will be based on Tampa Electric's December 1995 earnings surveillance report; is that correct?

A Yes, sir.

Q And it would be based on a surveillance report consistent with surveillance reports generally filed, right, with adjustments consistent with the Company's last rate case?

A That's correct.

Q Did the Company's last rate case have any adjustments in its surveillance report for deferred revenues?

A No, it did not, but that's because the deferred revenues did not exist during the Company's last rate case.

But I do believe, though, Mr. Howe, that in the Company's last rate case, there were adjustments that were very much consistent with the adjustments that were made for deferred revenues, in that typically liabilities that have other return provided are removed from rate base and treated differently. And to the extent that deferred revenues do have a separate interest cost associated with them, we book the adjustments in the surveillance report consistent with that.

Q I see. So in your December surveillance report then for 1995, did the Company make those adjustments actually made in the last rate case as well as adjustments for deferred revenues?

A That's correct.

Q Now, if you look at Paragraph 4, it states that the 1995 revenues will be deferred until 1997. Do you see that?

A Yes, sir.

Q Would you agree it states that the revenues will be deferred until 1997, but nowhere in the

Company's proposal does it state that those revenues will be included in the capital structure or will be used to fund the Commission's operations during 1995?

A I think what causes the Company to utilize those sources of funds does not exactly need to be described here. I think that's a natural outcome of the Company having those funds available to it and utilizing those funds as a source of capital.

Q Well --

A I think the adjustments that the Company has made to recognize that or to reflect that are consistent with prior Commission practices.

Q With prior Commission practices; is that correct?

A Yes.

Q Then did the Company just assume that the funds that were deferred should be recognized as a source of funds to support operations in 1995?

A I'm sorry. Can you repeat that again?

Q I'll try. Did Tampa Electric assume that the revenues deferred in 1995 would be available to the Company as a source of funds to support operations in 1995?

A Yes, we did make adjustments to reflect that they were a source of funds.

Q And if that was the adjustment the Company made, then in what sense were these same revenues from 1995 available for booking in 1997 as revenues?

A Well, if I understand your question, I believe that the fact that we recognize that they were a source of funds in 1995 should not have any impact on the fact that they were available to 1997.

As we're all aware, eventually we ended up signing additional stipulations that were -- that, you know, took the deferred revenues and added to those in 1996 and then took those deferred revenues into 1997 and 1998. And I believe that those funds have been out there for all of those years as a source of funds.

Q Do you mean as a source of funds that supported the Company's operations in 1995 and later in 1996?

A Yes.

Q My question remains then, in what sense were those funds -- if you have committed them to support operations in 1995 and 1996, in what sense were those funds available to be recorded as revenues in 1997 pursuant to Paragraph 4?

A All right. I think I understand what your question is better now.

I think that it's a difference between

whether the cash is available as a source of funds as opposed to whether or not the earnings are available to reverse as revenues to the Company in the future. In 1995 and 1996, we did have these funds, and they were cash to the Company, and we used those funds to offset the cost of other funds or sources of other funds. To the extent that those revenues were set aside as earnings, we were able to reverse those earnings back to the Company in the future for 1997 to offset cost of service. I don't believe those are contradictive. I believe that you can accomplish both of those under, you know, regular accounting practice.

Q I am not an accountant, so my questions are not as precise perhaps as they should be. But I guess what I'm really trying to find out is, if the Company committed revenues that were deferred in 1995 to support operations of the Company in '95 and '96 --

A The cash.

Q The cash. Then in 1997, if the cash, the revenue, for example, is reversed and reflected as revenue in 1997, what is the source of that revenue? Where is the cash coming from? Did the Company have to go out and raise capital to support the revenue that was recognized in 1997 which originated in 1995?

A To the extent that the Company had the cash coming from 1995 and 1996, I believe that the -- in 1997, the Company still had the use of that cash to the extent we had not given it back as refunds as yet. But to the extent that the Company was recognizing the revenues on its income statement, those were noncash revenues. So to the extent that we had to go out and find additional funds if we needed to in 1997 and 1998, yes, we did have to do that.

Q Could the Company have satisfied the provisions in Paragraph 4 on page 5 of Order No. 95-0580 by just setting the deferred revenues aside for use in 1997?

A Well, we did do that for the revenue side.

Again, I think we are confusing revenues versus cash. The revenues were set aside in a liability account and will be reversed to the Company as revenues to offset cost of service in 1997 and 1998. But to the extent that the Company had the cash associated with those revenues, we utilized that cash to offset the other sources of capital that the Company would have had to have gone out and gotten had it not been for the deferred revenues.

But I don't think that just because we utilized the deferred revenues or the cash associated with that to offset the funds, I don't believe that

that meant that the dollars still were not available to reverse as earnings to the Company in '97 and '98.

MR. HOWE: Chairman Johnson, if I could have an exhibit number, Mr. Larkin is distributing a copy of Tampa Electric's December 1995 surveillance report. Would that be Exhibit 3?

CHAIRMAN JOHNSON: Show it marked as 3, please. What's a short title?

MR. HOWE: Tampa Electric's December 1995 surveillance report.

CHAIRMAN JOHNSON: It will be identified as stated.

(Exhibit 3 was marked for identification.)

BY MR. HOWE:

Q Ms. Bacon, do you recognize this document as Tampa Electric's 1995 surveillance report?

A Yes, I do.

Q Are you generally familiar with the Company's surveillance reports?

A Yes, I am.

Q Do you participate in their preparation?

A I review them. They're actually prepared by the accounting department. I work in the regulatory department, but I do review them on a monthly basis.

Q Now, if you would refer, please, to the cover sheet, the first page, that shows, does it not, that the Company originally estimated that the deferred revenues for 1995 would be $50.8 million?

A That is how much we accrued during the year of 1995.

Q And that was consistent with your original estimates on a month-to-month basis, was it not, of what the appropriate amount was?

A If I understand your question, yes, it is.

Q And then at the end of the year when you trued things up, still looking at that first page, in the Company's estimation, deferred revenues for 1995 should in fact have been 48,832,000; is that correct?

A That's correct.

Q And you made an appropriate adjustment to reflect that; is that true?

A Yes, we did. Not in 1995, however.

Q And when did you make that adjustment?

A I would imagine in 1996 after the deferred revenue amounts were approved.

Q All right. And if you would, just turn the page. Let's see. I want to go to the third page in Exhibit 3, the 1995 surveillance report. It's Attachment 2. Do you see that?

A Yes.

Q Now, this is titled as a deferred revenue interest calculation. Are you familiar with this document?

A Yes.

Q And could you tell me what is shown here?

A This is the calculation of the deferred revenue interest that the Company must accrue according to the stipulations. It takes the total accrual for the year, the 48,832,000, and assumes that those deferred revenue amounts were booked evenly throughout the year, which is also a provision within the stipulation that requires us to do that, and then carries those numbers across times the commercial paper rate to calculate the monthly interest amounts.

Q Is this approach used only for the calculation of interest?

A Yes.

Q Now, am I correct that in 1995, the Company did not actually accrue deferred revenues and interest in this fashion on its books and records?

A The interest was accrued exactly in this fashion. The accrual of the deferred revenues themselves we book according to a different procedure that recognizes the liability according to GAAP. In other words, for like financial reporting purposes, we have to recognize the liability as we incur it, so we're not allowed to spread it evenly over the 12 months, because obviously, the Company's earnings are not generated as such. But for interest purposes, the stipulation required us to assume that the deferred revenues would be evenly over the year.

Q If I might ask you, please, to backtrack a moment to Order No. 95-0580, and the second page.

A That's the same order that we were on before?

Q Yes, ma'am.

A Okay.

Q On the second page. And do you see that paragraph with the heading underlined, "Treatment of Deferred Revenues"?

A Yes.

Q Could you read that, please?

A It says, "For regulatory purposes, such as determining earnings and calculating interest, any revenue deferred until 1997 will be treated as if it were earned evenly throughout 1995, or one-twelfth per month."

Q So for purposes of calculating the Company's earnings in 1995, not the interest calculation, but the earnings in 1995, did Tampa Electric assume that those deferred revenues occurred equally at the rate of one-twelfth per month?

A Well, when the Company originally filed its surveillance report, which is this particular filing right here, the deferred revenues had been removed from rate base on a total amount. So anything the Company had accrued according to its GAAP method had been totally removed from rate base. Then the adjustment to the capital structure was across all sources on a pro rata basis to reflect that as a source of capital.

I think that the Company indicated to the Staff later on what the amounts were that it had booked, and it was actually Staff who later on set the deferred revenues up in the capital structure equal to that accrual. So the answer to your question, I guess, is, I think the Company utilized the numbers that were on its books and records to do its calculations.

Q Why did it use that? And I would point out that the order is dated May 10, 1995, and your December surveillance report is dated February 14, 1996. Why did the Company not calculate its earnings for 1995 on the assumption that deferred revenues had been received equally throughout the year?

A I think the Company has to file its original surveillance report as if it were -- as if we booked it. I mean, we have to, you know, put what's on the Company's records in the surveillance report.

To the extent that down road when the Staff does its calculations, that interest amount or that deferred revenue amount could have been trued up to the amount that would have been evenly over the year. But I would imagine, Mr. Howe, that you would probably not like the answer to that, because what would happen is, the deferred revenue amount in the capital structure would have actually been a lower number, and the deferred revenues would have been lower than what they would have otherwise.

Q The statement on the second page of the Order No. 95-0580 that this assumed even treatment, one-twelfth per month throughout the year, should be for regulatory purposes, Tampa Electric did not perceive that that applied to its surveillance reports; is that correct?

A That was a provision that was included in the '95 agreement that was suggested by Staff. I'm not exactly even sure the Commission had a full understanding at the time as to exactly what determining earnings exactly meant. I think that we did -- all of our conversations that we had with Staff regarding this issue really surrounded the calculation of the interest, and it was very clear that that's the way we calculated our interest throughout the year. I'm not exactly even sure if when I read that original provision that the Company even understood that, you know, we were to do something differently with the accrual in the surveillance report filings.

Q Would the provision in the order that it would be done evenly throughout the year at the rate of one-twelfth per month suggest that the Commission's intent was that it would be an after-the-fact calculation, calculate the earnings at the end of the year, the earnings above 11.75, and then go back and restate the Company's books and records to show that they were assumed to accrue evenly?

A Again, I'm not exactly sure that you would like that particular answer of that calculation, because I think it would only tend to decrease the amount of deferred revenues that the Company booked. I mean, it can work both ways, I think is what we've seen so far. In 1995, I think that you would have ended up perhaps maybe having a slightly higher amount of deferred revenues, but in 1996, you would probably have a slightly -- an amount of lower deferred revenues. So I think it can work in both directions.

I think the Staff approved and the Commission finally approved that using the actual accrual on the Company's books was the appropriate method for the capital structure.

Q Now, if we could kind of jump -- I said I was going to go chronologically. I find the way the questions and answers are going, I'm going to need to jump a little bit ahead to April 17, 1997. Do you have a copy before you of Order No. PSC-97-0436?

A Yes, I do.

Q And if you would turn, please, to the ordering paragraphs. Let's see, the first, second, third, the fourth ordering paragraph. Would you agree that in this order, the Commission found that the appropriate amount of deferred revenues for 1995 was $50,517,063 plus interest?

A Yes, I would.

Q Now, how much interest is to be added to that?

A I think again, according to the stipulations -- I mean, I don't know the exact number. I would imagine that you would take the 50 million and divide it by 12 evenly over the year and then calculate the interest on that amount.

Q Well, wouldn't you need to have already done that, because that would be your starting point at the end of '95 to start 1996, so the amount that is already accrued from 1995 would be increased by interest, and then it would earn interest again, additional interest in 1996? Necessarily, wouldn't that calculation already have been done?

A The Company trues up these amounts in its books and records as the Commission makes the decisions on the levels of the deferred revenues. So any impact on this particular amount would have already been reflected in the Company's books.

Q Ms. Bacon, my question is, to begin 1996, wouldn't the Company begin accruing interest on 1995's deferred revenues, plus interest for 1995?

A And the effect of that I think has already been trued up.

MR. HOWE: All right. Commissioners --

COMMISSIONER CLARK: Ms. Bacon, I still don't know if that's a yes or no.

WITNESS BACON: Oh, I'm sorry. I think it is a yes, that the Company has already reflected the impact on the 1996 amounts related to any changes in 1995.

What we do is, when the Commission makes a decision on one year, we flow that effect and true it up on our books for all of the years, to the extent that it affects the interest that would roll into '96 and roll into '97. So any effects on the amounts -- subsequent interest amounts would be included in that true-up. It might not have been in the original filing that the Company made, because at that point in time we did not have the '96, or we did not have the decision for the 1995. But once we received this order, we went back and corrected all of our books. And I believe Staff has looked at those calculations, and they have approved of our methodology of truing up the deferred revenue amounts.

COMMISSIONER CLARK: Okay.

MR. HOWE: Chairman Johnson, could I have an exhibit number for an exhibit that has just been distributed? It's entitled "Tampa Electric's Answer to Informal Data Request No. 21."

CHAIRMAN JOHNSON: It will be marked 4 and identified as you just stated.

(Exhibit 4 was marked for identification.)

BY MR. HOWE:

Q Ms. Bacon, are you familiar with this document?

A Yes, I am.

Q Now, I'll need for you to refer to a couple of different things at the same time. First off, looking at the third page of Exhibit No. 4, which is -- it's marked as page 2 of 2 of the actual response to the data request.

A Okay.

Q Now, if you'll look in the far lower right-hand corner, you see that amount, the 13-month average amount of $77,670,075?

A Yes.

Q Now, if I could ask you also now to refer to the order that we protested, the order in which the Commission first issued its proposed agency action approving Tampa Electric's deferred revenue calculation for 1996, and that's Order No. PSC-98-0802.

A Okay.

Q And then if you would go to the back of that order, the third page from the end, which would be Attachment B.

A Yes, I have that.

Q Now, what the Commission included in the capital structure on an average test year basis for deferred revenue is exactly this amount, is it not,

$77,670,075?

A Yes, it is.

Q All right. Now, I'll refer you back, please, to what has been marked as Exhibit 4, the Response to the Informal Data Request No. 21.

This spreadsheet, I'll call it, provides the basis upon which the Company calculated the $77 million figure, does it not?

A Yes, it represents the original accrual on the Company's books of the deferred revenues.

Q The original accrual?

A The accrual, the only accrual.

Q So, for example, for 1995, the Company accrued $50,800,000 of deferred revenues, is that correct, in 1995?

A Correct.

Q Did the Company go back and restate the deferrals for 1995 to match the Commission order approving the deferral for 1995, which was that $50,500,000 figure plus interest reflected in that other order we referred to?

A Like I said before, all of the adjustments were trued up. All of the liabilities and the associated expense was trued up eventually for the 1995 decisions.

Q But it was not trued up in the calculation of the amount of deferred revenues that's going to be carried forward and shown in the capital structure for '96; is that correct?

A That's correct.

Q So for 1995, if we might focus on that first -- and here I'm looking at page 2 of Exhibit No. 4. The Company did not accrue any interest in the months of January, February, or March of 1995; is that correct?

A Where are you looking at?

Q I'm looking at Exhibit 4, which is Tampa Electric Company's Answer to Informal Data Request No. 21.

A Yes, that's correct, because that was before the '95 agreement was signed. The Company already started recognizing an amount over 12.75 on our books in 1995 even before the 1995 deferred revenue agreement was signed. Once it was signed, then the interest provision was present, and we began accruing the interest.

Q So you did not accrue interest in the months of January, February, and March; is that correct?

A Again, we would have went back and trued it up as if we had. In other words, the total balance still will represent the correct amount of interest at the end of the year. We just did not have the interest provision at the time in January, February, and March when we closed the books.

Q I guess my question is, in your capital structure the Commission approved for 1996, which apparently is the $77 million supported by this schedule in Exhibit No. 4, you don't have those true-ups in that calculation, do you?

A Well, I think you would for that one, particularly because any of the true-ups would have been booked in 1995, and the 77,670,000 reflects a 13-month average number for 1996. So any true-ups that were booked in 1995 would be reflected in that number.

Q Well, where would they be reflected? This spreadsheet in Exhibit 4 shows the 1995 deferred revenue, how it was treated in '95 and how it was treated in '96, and then it shows the deferred revenue for '96, and the addition of those two is what gets you the 77 million on a 13-month average basis at the end of '96.

A Well, the 77 million just simply represents the 13-month average of the outstanding balance that was out there for 1996. So to the extent that the December 1995 balance had been restated to be correct, automatically the 13-month balances that are out there for 1996 will include that correction.

Q Where would that have been restated on here?

A It would have been restated during the months of April through December of 1995, such that that 52,329,000 number that's out there for December of 1995 million reflects the correct amount of interest and deferral. And that just automatically flows into 1996, and so therefore the 77 million includes all of the impacts of the correction.

Q My question is, the Commission order approving the deferred revenues for 1995 did not use the $50,800,000 figure. It used a different number.

A That's a different issue, I believe, Mr. Howe, than the one I think you were asking me about. You were asking me about the true-up of the interest amounts that were -- you know, the fact that we did not accrue any interest originally for January through March and the effects of that on the 77,670,000.

Q All right. Let me see if I can understand.

A It's rather complex.
Q Does this spreadsheet, I'll call it, on page 2 of 2 of Exhibit No. 4, does this show the -- and I'll refer to the question that was asked in the informal data request. Does this show the actual monthly data as booked concerning the amount of revenue deferred and associated interest segregated between 1995 and 1996 revenues?
A Yes, it does.
Q And this is what's actually on the books of the Company; is that correct?
A Yes, it is, for those years.
Q Would you agree that the Company's books, for example, for 1995 don't match exactly with what the Commission approved for 1995?
A To the extent that subsequent adjustments were made by the Commission as they approved the '95 deferred revenues, there would be additional amounts on top of these, yes.
Q And where would those additional amounts be shown? Are they shown on this schedule?
A They are not shown on this schedule.
Q All right. So the additional adjustments ordered by the Commission would effect the $77 million, would it not, that the Company has included

in its capital structure and that the Commission used in the order approving the 1996 deferred revenues?

A I think the Commission precedent on other cases where I've seen where they had subsequent years deferred revenue agreements that were back to back, they did not go back and try to adjust subsequent adjustments back into those years. So I don't believe that that's something the Commission has ever done for any of the other, you know, subsequent year adjustments or deferred revenue years for different companies.

Q If I might ask, again returning to the question of the interest accrual for January, February, and March of 1995, which is not shown on this spreadsheet of Exhibit 4, could I ask you to please return to Exhibit 3, which is the calculation of interest for 1995, which you show on Attachment 2?

A Yes.

Q Now, in that calculation you show interest for every month in 1995, do you not?

A Yes.

Q Where is the calculation on Attachment 2 of Exhibit 3 ever used by the Company?

A We use it every single month when we go to accrue the interest amount. See, what you're seeing here, this original page 2 of 2 exhibit that has the zeros for the interest amounts for January, February, and March is how much the Company actually recorded for the interest amounts for every single month in 1995. And to the extent that the deferred revenue agreement had not been assigned and approved by the Commission until after March and the interest provision did not even exist, the Company had not physically recorded any interest on its books for those three months.

Subsequent to that, though, the interest provision was approved, and the interest provision provided that the accrual should be spread evenly throughout the 12 months. At that point in time, the Company would have taken whatever accrual that it estimated and went back and assumed that it would have been spread evenly, which is what Attachment No. 2 does, and then trued up any interest amounts on its books to be reflective of that provision of the stipulations. So even though you see zeros for January, February, and March, the total interest amount for the year reflects the provision in the stipulation that requires us to spread it evenly over the 12 months.

Q But those trued-up numbers were not then used to derive the $77 million figure that was included by the Commission in the capital structure; is that correct?

A For the particular case of us not accruing January, February, and March, yes, they are. The changes are in there, because we booked them in 1995.

Again, there are two separate issues here. One, I think you're asking about the January, February, and March issue, the fact that the Company did not initially accrue interest for those three months. That was trued up in 1995 as soon as we received the provision that told us to do the calculation a certain way.

Now, the other issue regarding subsequent decisions by the Commission after the '95 and '96 books had been closed, I would agree, they would not be reflected in the 77 million.

Q When you say things are trued up, does that change the books and records of the Company?

A Not for 1995 and 1996. Once the Company closes its books and records, these are the amounts that were recorded.

Q All right. And please realize you're dealing with a non-accountant here.

For example, we look at Attachment 2 of

Exhibit 3. You show a monthly accrual. Let's just look at January of 1995, a monthly accrual of $4,069,333. Do you see that?

A Yes.

Q And you show an interest calculation for that same month. Is it $10,275?

A Yes.

Q Are these numbers on the Company's books and records anywhere?

A Not -- this is a worksheet that we utilize to true up the interest amount, such that -- the provision says that regardless of how you accrue the deferred revenues on the books, you have to assume as if the deferred revenues were spread evenly over the 12 months. That's what this particular work paper does. So it should not have the actual amounts that were really accrued, because the stipulation tells us to do differently. Then we take the total amount of the interest, and we go back to the books and we true up the interest amount such that we will accrue that.

Q All right. So then --

A It might not look exactly like this. In other words, you won't be able to go to January and see 10,275 or so forth. But the effects of the total interest have been included in the 1995 books.

Q When you say included in the books, do you mean on the books for 1995 that were closed by the Company?

A Yes.

Q All right. Now, I must then return. You said it was for the interest calculation. But in Order 0580 for 1995 which established the approach, it was supposed to be done evenly for both earnings and interest, was it not?

A That's correct.

Q Now, again referring to Exhibit No. 4, page 2 of 2, the last page, this shows the Company starting 1996 with deferred revenues from 1995 of $50,800,000, does it not?

A Yes, it does.

Q Why does it not start with deferred revenues plus interest from 1995, which will then accrue interest in 1996?

A I believe -- well, I know that the interest is included in the calculation for purposes of calculating interest in 1996. I'm not exactly sure if I can point to you on this particular page how that works. But any interest that was accrued in 1996, that 1,773,563 that's in January, it should be including interest on top of the interest that was in

1995.

Q Well, if you would note, for example, December of 1995 interest was $343,220; is that correct?

A Say that number again.

Q $343,220 for December of 1995.

A Yes.

Q And then that's carried over and showed as an accumulated balance of $1,529,186; is that correct?

A Correct.

Q Now, the total amount there for December, the total accumulated balance of $52,329,186, that is the total amount of deferred revenue plus interest that the Company started with in January of 1996, is it not?

A That's correct.

Q And is it your testimony that that is reflected on this schedule?

A Absolutely. The interest that's calculated in 1996 is reflective of both the original 50,800,000, plus the additional interest that was booked in 1995 of 1,529,186. The interest is compounded on top of the interest, is the way the calculation works.

Q Then is there a column missing for 1996 then such that we need to see the deferred revenue balance and interest on that, then the interest carried forward from 1995, and the interest in 1996 on that interest? I mean, are we missing a column of data here?

A Actually, the interest accrual amounts, once you get out into 1996 and '97, are somewhat more complicated than the pages that we have here before us. There is another page similar to Attachment 2 that they continue to take the 50,800,000 and the associated interest for '95 deferred revenue and continue to calculate the interest out through time for that, and then they have another separate calculation of the interest for '96. And even when you got into the '97 deferred revenue amount, there would be even a separate page.

So I think that there are several pages here that we don't have before us. But I can tell you that that's the way I understand it works, is that the interest is compounded.

MR. HOWE: Could you keep -- we're distributing a document right now, Chairman Johnson. And Ms. Bacon and Commissioners and others, I would ask that you keep Exhibit 4 open to that schedule on page 2 of 2.

Chairman Johnson, we're distributing a copy of Tampa Electric's 1996 surveillance report. Could I have that marked for identification?

CHAIRMAN JOHNSON: It will be marked as 5 and identified as you stated.

(Exhibit 5 was marked for identification.)

BY MR. HOWE:

Q Ms. Bacon, do you recognize this document as Tampa Electric's 1996 surveillance report?

A Yes.

Q And are you familiar with this document?

A Yes, I am.

Q Now, Ms. Bacon, if you would, turn, please, to the very last page, which is Attachment 4 of the 1996 surveillance report. Now, this shows the calculation of interest on deferred revenues in a manner consistent with the calculation that was done in the 1995 surveillance report, does it not?

A Correct.

Q And would it be correct to state that the Company calculated total interest for 1996 of 668,475?

A Yes, but that is not the amount that was actually booked during 1996, I think it's important to point out.

Q Is this the amount that the customers would eventually receive under the stipulation if the

Company did not have to use the funds to support operations in 1997 and 1998?

A If the Commission had --

COMMISSIONER GARCIA: Could you repeat that question?

MR. HOWE: Yes.

BY MR. HOWE:

Q My question is, is this the amount of interest the customers would actually receive for deferred revenues associated with 1996 if the Company did not use them to support operations for '97 and '98?

A It would have been the amount for the 1996 accrual itself, just for the '96 deferral. So it does not include any interest on the 50 million that was coming from 1995. And it also would have only been the amount to the extent that the 31,507,000 was subsequently approved by the Commission, because this was what the Company had filed. To the extent the Commission did any additional adjustments, then all of this gets trued up by the Company.

Q Now, if I could ask you to return, if you would, to Exhibit No. 4, the last page.

A Yes.

Q And in that middle set of data for 1996, does that show that the Company actually accrued $924,337 of interest in 1996 for 1996 operations?

A Yes, it does, I believe.

Q Would it be correct then to state that the way the Company has calculated its capital structure and derived this $77 million figure, that the Company is using -- assuming the customers should bear the cost of $924,000 of interest, but that they would be expected to receive something on the order of $668,000 of interest?

A No, that is not how these schedules work, Mr. Howe. The original accrual that the Company placed on its books for the deferred revenue amount for 1996 was $34,200,000.

Q Where does that number -- okay. That's what you originally accrued for 1996 based on your estimates; is that correct?

A Correct. And this over here was -- once we closed the books and we went back to look, it said that we only should have accrued 31,507,000. So what the Company filed the 668,475 amount for was if the Company -- regardless of what the Company accrued as an estimate, if you went back and calculated what the Company ended up with, what would the amount have been. And we were saying it should have been

31,507,000, plus associated interest of 668,000. Now, what the Company accrued was 34,200,000, plus interest of 924,000.

But neither one of these amounts really matter in the end, because what will matter in the end was the final Commission approved amount, and then we would go back and update all our numbers to reflect the Commission approved amount of deferred revenues and associated interest.

Q Well, I think in part I agree with you, because the Commission approved amount would be the most important. But the way the Company has calculated or has used deferred revenues plus interest in its capital structure calculation, hasn't the Company included $924,337 worth of interest for 1996 upon which it asks the customers to then support that interest at the 30-day commercial paper rate in the capital structure number of 77 million?

A Well, to the extent that the interest is included in the calculation of the capital structure, I think that is the issue that we're here today about. And on that note, I think it's important to point out that I believe that that's appropriate, considering that these deferred revenues were a source of funds for the Company during that year. But as to the amount of the interest that was included in the capital structure, again, once the Commission reapproved or approved a different number, I believe Staff in their work papers would update all of those numbers, including the associated interest in the capital structure, to reflect that new amount.

Q Would you agree, though, that as the Commission issued its order approving the Company's 1996 deferred revenues, it included in the Company's capital structure 77,670,075 at the 30-day commercial paper rate?

A What was that number again?

Q $77,670,075.

A Yes, that's correct.

Q And so the way the Commission approved the capital structure for Tampa Electric for 1996 in this case, the customers are being asked to support and pay the 30-day commercial paper rate on the principal as shown in the third from last column on page 2 of 2 of Exhibit 4, the $74,383,303, as well as $3,286,772 of interest; is that correct?

A The total amount that's included in the capital structure is the 77,670,000, because that represents the total amount that was deferred from the Company. But earlier on, you pointed out about the requirement to represent the number evenly throughout the year, and I think I pointed out that if you trued up to that, you might not exactly like the answer that it would give you.

If we put that number in the capital structure as if it was earned evenly throughout the year, the amount would have been 69 million, so the effect of that would have been to increase other sources of capital within the capital structure, and I believe that would result in a lower deferred revenue amount. So I believe what the Company put into the capital structure was a fair amount. Or actually Staff included the 77 million in their calculations.

Q And would you agree that the Commission's approach in its proposed agency action order and the Company's data as filed would require the customers to pay interest on $74.3 million of principal for deferred revenue on a 13-month average basis, and on $3.3 million of interest on a 13-month average basis?

A I think that's appropriate to the extent that the interest is compounded. I mean, the interest goes into the deferred revenue balance and generates additional interest amount. So the only proper way to include the total effect of the interest in the capital structure is to put both the original accrual of the deferred revenues in the capital structure plus the amount of the interest on top of that. So I believe that the total interest accrual should be the effects of both of those.

Q And the effect of both of those then reduces the amount of revenues deferred for 1996 for the customers' benefit, does it not?

A I believe that by including those two amounts in the capital structure, it reflects the actual cost of providing service in 1996. Tampa Electric could not have provided service in 1996 without that $77 million worth of funds. And to the extent that that was a source of funds for the Company and it offset other sources of funds for the Company, I believe that it's proper to include that cost in the capital structure.

Probably the best way to evidence that it is not a double counting of the interest, as Mr. Larkin pointed out in his testimony, is to consider the Company's cash balances in 1996. In 1996 Tampa Electric had less than $5 million of total cash on a 13-month average basis. And if you look in 1995 and 1997, you will also see very small amounts, and that's cash and cash equivalents. And by looking at those, it's very evident that Tampa Electric does not retain additional sources of cash or excess cash on its books. It used the sources of the cash from the deferred revenues and paid down those other sources of capital, and those savings are reflected back in the capital structure already. So to include this interest is appropriate, in that this does represent the actual source of funds that was used by the Company.

Q If I might pose a hypothetical, let's address 1996 in isolation, and if we might, ignore 1995. In other words, just assume that we're dealing with deferred revenues for 1996 in isolation without consideration of whether there's any deferred revenues for 1995.

Now, am I correct that the Company's approach is that any earnings that the Company has above 11.75 are a source of funds at the 30-day commercial paper rate which customers must support?

A Any revenues above what number?

Q 11.75, given that that's the trigger point for the sharing.

A I think it's 60% of those dollars above 11.75.

Q Now, let's assume if we can for purposes of this hypothetical that the Company's revenues are sufficient in 1996 to allow it to earn exactly 11.75. All right? Let's take that as a starting point. Would you agree that if we take that as a starting point that there are no deferred revenues in the Company's capital structure for 1996?

A I would agree with that argument, or understanding.

Q Now, if the Company has additional revenues such that they cause the Company's earnings to go above 11.75, does that trigger the inclusion of deferred revenues in the Company's capital structure?

A Yes, it does.

Q Now, if I might ask you to compare those two scenarios, the Company earns exactly 11.75, and the Company earns above 11.756. Under the second scenario, does it take more revenues to achieve a return of 11.75 than it does under the first scenario?

A Under the second scenario, does it --

Q Yes, ma'am.

A I don't believe so.

Q Well, if I might address it, the first scenario is the Company's earnings are exactly 11.75. The second scenario is that the Company is earning above 11.75, which triggers the inclusion of deferred revenues in the capital structure. Correct?

A Correct.

Q The capital structure is larger under the second scenario, is it not?

A I don't believe so, no.

Q In total dollars it would have to be, wouldn't it, because you're using deferred revenues as a source of funds to support operations?

A The rate base and the capital structure must balance out, just similar to the balance sheet, where assets and liabilities balance out. So I don't believe overall the Company is going to have any more or less total assets and/or funds to earn on. It's just that there will be an additional amount that will be supported by the deferred revenues and will be recognized as being supported by the deferred revenues, and that would tend to offset other sources of capital which would already be reflected in our capital structure.

Q But under the Company's approach and the Commission's approach, the Company's capital structure is larger by $77 million, is it not, to recognize the 13-month average of deferred revenues?

A No, I would disagree with that. I think to the extent that that 77 million has already offset other sources of capital, I would think that it's the same as it would have been.

Q Is it your testimony then that if the Company has deferred revenues in a particular year, that those deferred revenues do not both increase the Company's rate base and capital structure?

A I think that if the Company recognizes deferred revenues -- I think I can answer yes to that. That is my testimony.

Q Yes. And it increases --

A If I understand the way you put it. If you accrue -- you're taking a situation where you have deferred revenues and where you do not have deferred revenues?

Q Yes.

A And to the extent that you recognize this liability on the Company's books with the deferred revenues, then all you're doing is taking that out of rate base, and you're going to put the rate base back to where it was prior to the recognition of the deferred revenues. And the same thing with the capital structure: To the extent that you would have had to have supported those assets with other sources of capital, all you're doing is replacing the deferred revenues as the source of capital. So I believe the net effect to the rate base and the capital structure would be the same both with and without the deferred revenues.

Q Well, now, if -- let's assume that the Company collects deferred revenues, and let's say they keep it as cash. It would increase the rate base, if only in the working capital calculation, would it not, for assets --

A We do not keep the cash.

Q Well, I understand, but I'm just saying as a first step, a simplified step, if it's in cash, you've got a larger rate base. If you take the cash and you invest it in plant, you've still got a larger rate base. The rate base increases because of the deferred revenues, does it not?

A Well, the rate base -- the plant increases has nothing to do with the level of deferred revenues that we have on the Company. The plant increases based upon the level of construction needs that the Company has to recognize.

Q Yes, ma'am. I guess I'm asking in very simple terms, as a first step, you get additional revenue and you treat it as deferred revenue. If you're going to use it as a source of funds to support the operations, it's going to be -- at least it can be, in a simplified step, in cash, can it not, in working capital?

A No, it cannot, because the Company does not keep additional sources of cash on our books. As a matter of fact, this Commission has provided utilities incentives to avoid large amounts of temporary cash investments. I do not believe our company has ever kept large amounts of cash on its books.

Q I'm not questioning your cash retention policy. I'm just saying in simplified first step --

A I'm just saying that that simplified first step I don't believe would occur, given the policy of Tampa Electric.

Q How does the Company -- what asset and liability accounts are affected by deferred revenues when you first book them, you know, in a month or for the year?

A Well, to the extent the revenues come in, you know, we would record them as revenues, and then we would have a debit to the cash act. And to the extent that the Company ran through its internally generated funds and its cash requirements, it would take that cash and then pay down probably short-term debt or some other source of capital.

Q All right. That's what I'm trying to address, just that first step, because I'm trying to be simple for my own edification. But that first step of cash, what you find is, if you did a working capital calculation right then, you would find working capital had increased by that cash; correct? And since working capital is a component of rate base, rate base would increase by the amount of the deferred revenue, would it not?

A Well, the deferred revenues also will be recognized as a liability on the books and would only tend to just reduce the working capital right back down.

Q And where would it be recorded as a liability? As a short-term liability?

A In the liability section of the balance sheet.

Q A short-term liability carrying its own cost rate; am I correct?

A Yes.

Q Would it be included in working capital?

A It would be removed from working capital.

Q So the net effect would be, your rate base would increase by the cash in working capital; is that not true?

A No, that's not true. The cash would then be taken and used to pay down short-term debt.

Q All right. So we can't address it, in your view, in that first step, the effect on cash in working capital?

A That's true.

Q All right. Would you agree that what the Company is doing is, the Company's approach is to use deferred revenue and include it in the capital structure and assign a cost rate; is that correct?

A I think that that has been the Commission's precedent for many years in regards to this type of calculation as well.

Q I see. So getting back to my earlier scenario one, scenario two -- I hate to make this so difficult, but if now the Company has deferred revenue in scenario two which it did not have in scenario one, it's now going to take more revenue to get up to 11.75 than it was before you had the deferred revenue, is it not?

A I would say just the opposite. I would say it would probably take less, because what you're doing is recognizing the fact that the deferred revenues are a cheaper -- probably a cheaper source of capital than what would have been out there before you recognized it. The deferred revenues have a commercial paper rate which is probably about 6%. To the extent that the other sources of capital that it displaced had any costs that were greater than 6%, I would think it would take additional revenues to get to 11.75 in your first scenario.

Q Okay. I think I understand your answer. So your point is -- or is your point that the deferred revenues provide a source of funds to support the Company's operations?

A Yes.

Q If the Commission instead of deferring revenues had said, "Lower rates for '95, lower rates for '96, and if you need a rate increase in '97, we'll give it to you," would the Company need -- would the Company need additional capital in its capital structure in an amount equal to the revenues from the rate reduction?

A Yes, I believe so.

Q So Basically, if the Company has money available to it and uses it to support operations, no matter what its level, in your view, that's money it needs; is that correct?

A The Company needs what it needs to fund its operations, if I understand your question.

Q I see. So the Company's capital structure would not have been any smaller if the Commission instead of deferring revenues had just reduced rates? Is that your testimony?

A I think I agree with that.

Q Now, you've made quite a frequent reference to Commission precedent, and you also referred to the fact that in 1996 you used a similar -- interest should be calculated evenly throughout the -- based on the assumption that deferred revenues were collected evenly throughout the year. Where is that in the stipulation for 1996? Can you tell me?

A Yes, I believe I can.

This is in Docket PSC-96-1300-S-I. Actually, that's the order number. It's Docket No. 960409-EI. And I'm looking at the attached stipulation itself under Attachment 1, and I think it's page 6 of the stipulation itself.

I'm sorry. It's actually page 8 of the stipulation itself. Under general provisions, Paragraph 6, it says, "The revenues held subject to refund shall accrue interest calculated at the 30-day commercial paper rate. For purposes of the calculation, these revenues shall be treated as if collected evenly throughout the year."

Q I'm sorry. Which stipulation are you referring to? The second one?

A This should be the one that was approved October 24, 1996.

Actually, I'm sorry. That was the Polk stipulation.

Q That was the Polk stipulation, was it not?

A Let me back up. I can give you the same reference on the second stipulation, I believe.

Q Would you agree that 1996 is controlled by the first stipulation?

A Yes, I would agree with that.

Q And for that, I assume you would be referring to Order No. PSC-96-0670?

A Correct, and that's in Docket 950379.

Q Yes, ma'am.

A And again I'm looking at the stipulation that's attached. There's not a page. It's page 14 of the entire order number. It's under General Provisions, Paragraph 9. It says, "The revenues held subject to refund and the deferred revenues provided for herein shall accrue interest at the 30-day commercial paper rate. These revenues shall be treated as if collected evenly throughout the year."

Q Yes. Now, in this stipulation, it refers to revenues. It does not refer to interest, does it?

A But it's -- I think it's referring to the fact that the revenues should be treated as if collected evenly throughout the year when calculating the interest.

Q So are you reading those words into it, when calculating the interest?

A Absolutely. It's all within one paragraph. I think that's exactly the intent of that line, that sentence.

Q I see. But in the 199 -- in the Polk stipulation, it actually says for purposes of calculating interest, it shall be assumed that they're collected evenly -- the revenues were collected evenly throughout the year.

A To the extent that the wording might have changed slightly, that is probably because I think Staff did not have quite as much of a hand in this stipulation. Probably the exact wording might have gotten shortened a little by the Company when we included this part in the stipulation. I think we understood that the Staff would probably not support the stipulation to the extent that we did not have this provision in the stipulation.

Q But --

COMMISSIONER CLARK: Let me ask a question. Why else would you treat the revenues as accumulated evenly throughout? For what other purpose would you do it?

WITNESS BACON: Again, I'm not exactly sure what was mean by for earnings purposes, but that would be the only other reason why I would -- I would know of.

BY MR. HOWE:

Q And you could assume it to be collected evenly throughout the year for purposes of the earnings calculation, could you not?

A But the fact that it's included in the same paragraph that refers to the calculation of the interest, I think it was -- it was our understanding, the Company's understanding that it was in here for the purposes of calculating the interest.

Q All right. And how much interest did you defer for 1996? How much interest did you add to the deferred revenues for 1996 pursuant to this stipulation?

A I can calculate that for you. I don't know if I have the exact number.

Q I'm just curious. What did you put on the books?

A I believe that the amount is 3 million -- oh, yeah, I do have this number. I just remembered that I had calculated it. $3,837,000.

Q That's the 13-month average, is it not?

A No. The 13-month average was 3,286,000.

Q What are you referring to for that number, if I might ask?

A If you look on that same Informal Data Request No. 21 -- I think it's Exhibit 4.

Q Yes, ma'am.

A Page 2 of 2. If you look over on the far right side under the interest column, and if you take the total balance that was out there as of December 1996 of 5,366,718 --

Q Yes, ma'am.

A -- and subtract the balance that was out there at the end of 1995 of 1,529,186 that's shown right above that.

Q I'm sorry. You lost me on that --

A December of 1995's balance of 1,529,186.

Q Yes, ma'am.

A If you net those two amounts together, I believe you should get about 3,837,000, and that's how much the Company recognized during 1996 for the total deferred revenue pot, just not the amount for '96, but the amount that was coming from 1995 as well.

Q And how much did you recognize for 1996 then?

A Out of that amount, it would be the 924,337.

Q And the amount that the customers would receive, would it be calculated pursuant to this assumed equal amortization or 668,000?

A Again, that amount only would have been trued up to by the Company for 1996 alone, to the extent that the Commission subsequently or ultimately approved the Company's proposed $31,500,000 of deferred revenue. To the extent that the Commission decided on a different amount from that, that's what the Company would have ultimately trued up to.

Q If I might refer you to the stipulation itself, which is -- as you mentioned, it's appended to Order No. 96-0670.

A Which one was that again?

Q It's the first stipulation, or the stipulation that affects '96.

A Correct.

Q Now, if you would look at the second page of the stipulation at the very top of the page, it says Tampa Electric will refund $25 million plus interest.

A What page are you on?

Q I'm on the second page of the stipulation that is appended to Order No. 96-0670.

A Okay.

Q All right. Did Tampa Electric refund $25 million plus interest?

A Yes, we did.

Q And pursuant to the stipulation, the actual refund came from two sources, did it not?

A Yes, it did.

Q And what were those two sources?

A I want to make sure I don't get them backwards. I believe out of 19 -- I can check on this, but subject to check, I think it was $10 million out of 1995 and $15 million out of the 1996 deferred revenue balance.

Q All right. For 1996, did the Company actually refund $15 million plus interest?

A Yes, it did.

Q Was the $15 million reduced by the Company for the interest the customers received?

A Was the $15 million reduced by the Company?

Q My question basically is, did the customers of Tampa Electric receive pursuant to this stipulation $15 million plus interest on $15 million calculated at the 30-day commercial paper rate?

A Absolutely.

Q So the interest that the Company was obligated to pay for that $15 million refund was not used to reduce the amount of refund, was it?

A Could you repeat that? I'm trying to follow --

Q The simple question, Ms. Bacon, is, the customers were not responsible for their own interest on that $15 million, were they?

A To the extent that the Company had use of the deferred revenues and/or the $25 million that had yet to be refunded to customers, and that deferred revenue amount represented a source of funds to the Company, we included that deferred revenue amount in the capital structure with the associated interest as a cost of funds for Tampa Electric.

Q I don't believe that was the answer to my question. My question is, on the $15 million, did the customers receive the full $15 million plus interest at the 30-day commercial paper rate?

A Yes, they did.

Q And if you'll refer to page 3 of the stipulation, it provides that that 30-day commercial paper rate would be as specified in Rule 25-6.109, does it not?

A Yes, it does.

Q But in the case of $15 million refund for 1996, the Company paid that total amount to the customers, and that amount is not in deferred revenues, is it?

A I can only tell you what I believe the Company did. I'm still having a hard time following your question along these lines. But what the Company did was, to the extent the $15 million was set aside and was being refunded to customers ultimately, the Company continued to accrue the interest on the $15 million. Those dollars were given back to customers in the form of cash. And to the extent that those funds were still on the Company's books, they were also included in the capital structure with the associated interest on those dollars.

Q Would the effect of that have been then, on the one hand, to give the customer $15 million plus accrued interest, but on the other hand, to reduce the amount of deferred revenues for 1996 because of the interest they were receiving?

A I think to the extent that those dollars represented a source of funds -- I don't think it changes the distinction here just because the Company was holding those dollars in order to refund them to customers than if they were going to be reversed as earnings to the Company in the future. Either way, while they were being held by the Company, they represented the source of funds. So I think the correct amount of overearnings or deferral for 1996 was including the cost of providing service. And to the extent that those funds were available before they were refunded, if they had a cost, they should be included in the capital structure.

Q Why didn't the Company reduce the $15 million by the interest, given that, because otherwise the Company was the source of the interest on the 15 million, were they not?

A Who was?

Q The Company.

A Was the source of the interest?

Q Yes, ma'am.

A I think that the -- again, the interest was included in the calculation of the deferred revenues for 1996, and it was a part of our cost of doing business, just as if any other particular cost was out there, you know, interest on long-term debt, or interest on short-term debt, or depreciation expense. To the extent that that interest was on our books, it represented a cost that was included in the calculation of the deferred revenues.

Q Could you refer back again, please, to Exhibit No. 4, the last page, page 2 of 2? That's the response to the Informal Data Request.

A Yes.

Q Now, if I understand this math correctly, what you show is that refunds are coming out of both '95 and '96 beginning in October. Do you see that, Ms. Bacon?

A Yes.

Q And if I'm eyeballing this correctly, what the Company probably did was, they prorated $10 million over 12 months for 1995 and prorated 15 million over 12 months for '96, in other words, so that each month's -- the refund in October was made up of basically two-fifths out of '95 and three-fifths out of '96; is that correct? In other words, I'm looking at this refund amount for October. You show 853,240.

A Right. I would believe that those amounts, the way that they are calculated is, if the Company originally took $25 million and estimated a dollar per megawatt-hour that should be credited on the customers' bills, and then to the extent that whatever the sales were for that particular month, multiplied that times that credit, then this would represent the effect of that. Now, how they split it between '95 and 1996 I'm not exactly sure, but I would imagine it was according to the $10 million/$15 million relationship.

Q And for example, for 1995, the refund of $853,240, and for 1996, the 1,279,861, the customers actually received through this proration the full 25 million plus the full interest on the 25 million; is that correct?

A That's correct.

Q Now, you've at various times in answering questions, Ms. Bacon, you've referred to the Commission precedent and so forth. Could you point me to anywhere in the stipulation where the parties agreed to incorporate any past Commission precedent?

A I think that the stipulations do not contain specific language that refers to any past precedence, but I believe that the intent of the stipulations in regards to the treatment of the interest on deferred revenues can be found in two separate provisions in the stipulation, the first one, obviously, that the interest on deferred revenues -- or the interest should be accrued on the deferred revenues equal to the 30-day commercial paper rate.

The other provision that I think implies the intent of the stipulations in regards to this issue is the portion that refers to all prudent and reasonable costs should be included in the calculation of the deferred revenues.

And again, it's the Company's position that to the extent this represents the source of funds that were used during the provision of electric service, that that interest should be included in the prudent costs.

I think that the stipulations do not go in and detail out what all are reasonable costs. I mean, there are many, many reasonable costs, depreciation, interest on long-term debt, O&M costs. That's where I think it comes back to prior Commission precedent and Commission procedures and their reasoning to determine what is reasonable and prudent and what is not.

Q Then is it the Company's position, as you're testifying, that the stipulation necessarily includes prior precedent, that the parties could not have chosen to exclude that prior precedent from consideration, and instead chosen to be controlled from the date of the stipulation forward strictly by the terms of the stipulation?

A I believe that even though prior precedent was not directly specified in here, I believe that in determining -- I know that the Company's understanding of what would be used would be current Commission practice, which was to always recognize, always recognize that there was a source of funds included in the capital structure that represented the deferred revenues. And so that was -- that was our understanding when we signed the stipulations, that we would be allowed recovery of those costs.

Q With or without explicit wording to that effect?

A Absolutely. I think it's important, Mr. Howe, that the stipulations -- to point out that the stipulations do not have any explicit language that says that the deferred revenues, interest on the deferred revenues will be absorbed by shareholders below the line. So I think absent explicit statements of that nature, I think that it's only reasonable to assume that prior Commission precedent and practice would rule in this area.

Q Would it be reasonable for the Commission to view the stipulation and the effect of deferred revenues that the customer should be in the same position as if the customers were allowed to hold that revenue, basically have a rate reduction and invest it themselves at the 30-day commercial paper rate, so at the end of the year, 1995 or 1996, the customers' benefit would be either the rate reduction or the deferred revenues, but increased by interest at the 30-day commercial paper rate?

A I think if that were to occur, if we had actually given the money back to customers during those years, the obvious thing that would have happened for Tampa Electric is, we would have had to have replaced those source of funds, and there would have been probably even a higher cost on our books that would have been included in the calculation of its earnings.

Q I would like to go into another matter. I'm looking at page 11 of your prefiled direct testimony, and I'm looking at the answer that begins on line 5. You refer to interest on customer deposits as being similar to interest on deferred revenues, do you not?

A What page are you on? I'm sorry.

Q Page 11 of your prefiled direct testimony, line 5.

A Yes.

Q Now, would this analogy hold, for example, if Tampa Electric stipulated to increase the interest on customer deposits? Would your statement hold true that interest accrued on customer deposits is similar to interest on deferred revenues?

A Yes.

Q Well, wouldn't the customers then receive that increased interest on their deposit?

A I think that to the extent that the interest on the deferred revenues will ultimately go back to customers as well, either in form of refunds, cash refunds, or offsetting future cost of service, which without the deferred revenues would have been collected from the customers in the form of cash. So to the extent that the interest on deferred revenues ultimately benefits customers in the future, I think that the similarity holds up.

Q My question, though, was --

A The interest does go back to customers from the customer deposit on a different situation, a different scale, a different set of rules. I mean, the interest on the deferred revenues will only be returned to customers in the form of cash to the extent that the Company has certain return on equity levels in the future that pass the thresholds where we will then begin refunding dollars. But to the extent that -- if we do not reach those thresholds, the interest will be reversed as earnings to the Company, offsetting the cost of service that otherwise would have been passed on to customers.

Q I appreciate that you want to talk about the deferred revenues, but right now I just want to ask a couple of questions about interest on customer deposits. And my question is, if Tampa Electric agreed to increase interest on customer deposits, wouldn't the stockholders have to bear that increased interest cost?

A No, I do not believe so. I think that it's very important to realize what's the difference between the stockholders bearing a cost that's included in its regulated earnings when it doesn't affect like a particular year that a deferred revenue amount is being calculated, and stockholders bearing a cost below the line outside the regulatory calculation of earnings.

I mean, to the extent that if you're not in a deferred revenue year and you have higher customer deposits, yes, it's true, the interest on customer deposits will affect the earnings of the Company. But the important thing is, that interest would be included in the calculation of the Company's regulated earnings calculation. What I believe that you all are suggesting here is that stockholders would bear this cost below the line, which I think is a different situation.

Q All right. Are you saying then that if the Company stipulated or if the Commission just increased interest on customer deposits, it would not -- the increased deposit payments received by customers would not be borne by the stockholders below the line?

A If it was in a deferred revenue year?

Q No, just a general proposition. Increased interest on customer deposits. I'm not even addressing deferred revenue. Just as a general concept.

A Well, I think you get two different answers, and I guess that's why I think it's important.

Q Okay. What are those two answers?

A Well, I think the answer is, if you're not in a deferred revenue year, the increased interest on customer deposits would be included in the Company's regulated earnings and would affect the Company's earnings. But to the extent that if you are in a deferred revenue year, it would be passed along just as if it's a source of funds, just like any other source of funds, and it would affect the deferred revenues dollar for dollar.

But I think that it's very important not to consider that even if we're not in a deferred revenue year and it affects the shareholders, it's not a below-the-line item. It's included in the Company's regulated earnings.

Q All right. And if I might stay with my customer deposit question, if you were in a rate case and you had an increase in customer deposits, would the increased cost of the customer deposits be borne by the customers?

A Yes, it would, as part of the regulated earnings of the Company.

Q And it would be included in the capital structure, would it not?

A Yes, it would.

Q And that cost would then be passed on to the customers; am I correct?

A Yes, it would.

Q Now, to analogize to the situation we have here with the stipulation where we have a rate freeze, if Tampa Electric on the one hand agreed to a rate freeze and on the second agreed to increased customer deposits, would you agree that the customer deposits, the higher deposits would be paid to the customers, and it would not in any sense be recovered from those same customers? It would be precluded by the other component of the stipulation that there be a rate freeze?

A I believe -- if I understand your question, I believe if there were higher customer deposits during this time period of the deferred revenues --

Q I'm not speaking of deferred revenues. I'm speaking -- I'm just talking about a rate freeze and an agreement to increase customer deposits.

A Okay. I don't understand the analogy then, or the situation, because you're wanting to assume the rate freeze, but not assume the deferred revenue calculation, and I see that as a contradiction. I mean, I think if you -- if you assumed that there was a base rate freeze -- I mean, I'm making your assumption -- and there was no deferred revenue plan or no deferred revenue calculations, I still believe that what's important is that the customer deposits interest would be included in the Company's regulated earnings that we would report in our surveillance report.

Q I see. And in the non-deferred revenue situation, you just can't -- is it your testimony that you cannot address that, that it's --

A Well, I think I just did. I mean, I basically said I didn't agree with the analogy, but then I went on to answer your question. I think that in a year where you -- if you want to make the assumption, even though I disagree with it, that deferred revenues were nonexistent, yet you had a base rate freeze, I still don't believe that that would imply that the interest on deferred revenues should be placed below the line, because in the other instance, the interest on customer deposits is included in the Company's regulated earnings that we report in the surveillance reports that we report. It's a cost of providing service. It's recognized as a source of funds for the Company and included in the calculation of the Company's earnings for regulatory purposes.

Q Do you believe Tampa Electric could have found it in its own best interest to freeze base rates, defer revenue, and pay interest on those deferred revenues without expecting the customers to be the source of the interest?

A I would say that that is not what we did. I mean, I don't believe that that was ever our thought that that's what would happen, and I don't believe that that was ever discussed in the stipulation discussions or negotiations, and therefore, I don't believe it's a possibility.

COMMISSIONER CLARK: Ms. Bacon, if I understood your testimony, it was that if that had been the intended result, you would have expected to see that articulated in the stipulation.

WITNESS BACON: Absolutely. Another example of that is the Port Manatee site, where we did actually agree to place those dollars below the line, and it was very specifically stated in the stipulation that the Company would accept that.

BY MR. HOWE:

Q Ms. Bacon, did you participate in those negotiations?

A I was not directly present in each of the meetings for the negotiations, but I was involved at the Company throughout the entire deferred revenue planning from the inception of the thought about it all the way to the final stipulation, and am still involved in the deferred revenue calculations.

Q Ms. Bacon, do you feel that the methodology used by the Company and by the Commission is completely consistent in all aspects with the 1997, February 1997 decision in the Florida Public Utilities-Fernandina Beach case?

A There are some distinctions between these two cases, but I believe that the important aspect of the FPUC case is that the deferred revenues were included in the capital structure and that the cost rate was included in the capital structure with those deferred revenues.

Q But there were other aspects. For example, the Commission made adjustments to the income statement and to the rate base and to the dollars in the capital structure, did they not?

A Well, in this particular situation for Tampa Electric, adjustments were made to the rate base that were very similar to the FPUC case. The income statement -- the deferred revenues were not absolutely backed out or was not exactly backed out of the calculation of the income statement. And if you look at the original filings of the Company that we filed with the surveillance report, we did make adjustments to the income statement.

However, subsequent to that, I think that between Staff's calculations where they did not actually back out the income statement effect, we were comfortable that there was no impact to the calculation for them doing that. So even though adjustments were not made to the income statement, I believe that that was not, you know, a downside to the overall agreement of agreeing to the numbers. We could match their numbers even though the adjustments were not made. But the adjustments to the capital structure were different for the FPUC case, in that in the FPUC case they backed off of other sources of capital when they set deferred revenues up in the capital structure.

But I think it's very important to note that the situation for the Fernandina Beach case for FPUC is different than what it is here for Tampa Electric. I believe the reason why those adjustments were necessary was the fact that if you look at the rate base, FPUC only accrued $2,500 of deferred revenue on their books during the year, yet when they went to go calculate the amount, the Commission approved $30,000 of deferred revenues, over 10 to 15 times the amount of the original accrual. And I think in that magnitude of a case, it was very important for the Commission to go back and recognize that the Company did not recognize as much deferred revenues. In other words, they didn't offset those other sources of capital to the extent that they should have.

In Tampa Electric's case, the amounts of accruals that the Company booked were very, very similar to the final approved amounts that the

Commission subsequently approved, and therefore, that type of adjustment I don't believe was necessary.

Q Ms. Bacon, you said 10 to 15 times. I think the math was, was it not, in the Fernandina Beach case, it was exactly 13 times? It was a 13-month average.

A No, I don't believe that that was the -- that's not the difference. The $30,000 represents the 13-month average, so I was comparing two 13-month average numbers. In the FPUC case, they booked $2,500. The final deferral deferred itself was 60,000. The amount, the dollars of revenues of deferral was 60,000. The 13-month average of that 60,000 was like -- I think 29,000 and some change, and that number is the comparable number back to the 2,500.

Q Ms. Bacon, the Fernandina Beach case, will you accept subject to check that it was decided on February 10, 1997?

A Fine.

Q Do you remember attending a meeting on April 10, 1997, with the Commission Staff and myself present?

A I've attended several meetings. I'm not exactly sure which one that one might have been.

Q Mr. Elias had sent out a notice saying there would be a meeting, and the purpose of the meeting is to afford Tampa Electric Company the opportunity to advise the parties of certain computational errors in Staff's calculation of TECO's 1995 excess earnings. You had picked up a computational error, had you not?

A Yes. That is -- I'm recalling that, yes. I'm not sure if I recall all the specifics of what we found.

Q If it will help clarify your memory, my notes show that the meeting was on April 10th of '97, 9:45 a.m., Room 309, Commission Office Building, attended by Phil Barringer, Delaine Bacon, Bob Elias, John Slemkewicz, Connie Kummer, Vicki Kaufman, Andrew Mowrey, Sonya Jones, and myself.

A Yes.

Q And do you remember at that meeting, Staff distributed the sheets from the recommendation in the Fernandina Beach case? And wasn't the suggestion made by Staff that that's how they wanted you to calculate your '95 deferred revenues, consistent throughout, the income, rate base, and capital structure portions of the Fernandina Beach case?

A Well, I think that what they were referring to was setting up the deferred revenues in the capital structure at the single line item and applying the cost rate to it.

The other thing, like I was pointing out before, the Company had filed our income statement removing the deferred revenue. Staff wanted the work papers to look exactly like the FPUC case, and we were a little hesitant of that, because again, at that point in time, we really weren't sure that we would get to the same result by not backing out the revenues, because the sharing mechanism is rather complicated. But eventually we got comfortable that Staff's calculations were okay in that regard. But I do not believe that that implied that all of the calculations, certainly ones that do not apply to Tampa Electric's case, should be booked for the FPUC where the capital structure amounts were adjusted.

Q Just one last question, Ms. Bacon. Can you please tell us, what is the total amount of deferred revenues plus accrued interest under the stipulation for the years 1995 and 1996?

A As it has been approved?

Q Yes, ma'am.

A I do not have that number with me. I don't believe I have that number with me. I can certainly get it for you if you would like.

MR. HOWE: No further questions.

CHAIRMAN JOHNSON: We're going to take a ten-minute break.

(Short recess.)

CHAIRMAN JOHNSON: We're going to go back on the record.

Ms. Kaufman?

MS. KAUFMAN: Thank you, Chairman Johnson.

CROSS EXAMINATION

BY MS. KAUFMAN:

Q Ms. Bacon, will you turn to Order No. PSC-96-0670? That's the one that has the stipulation attached that we've been discussing.

A Yes.

Q Have you got that?

A Uh-huh.

Q Would you agree with me, Ms. Bacon, that in 1995, the Commission found that TECO was forecasting an ROE of about 14.28?

A Yes, that's the original projected ROE for 1995.

Q And this exceeded the top of TECO's range; right?

A Yes, it did.

Q And then in 1996, for 1996, TECO was forecasting about 13.81; is that correct?

A I think that's the number, yes.

Q And that also exceeded the top of the range, didn't it?

A Yes, it did.

Q Now, it's correct, isn't it, that due to this high level of forecasted earnings, the parties got together, and they met and they discussed entering into the stipulations that we're talking about in this proceeding?

A Yes, that's correct.

Q And the main reason that the parties met and discussed and entered into the stipulations was to address Tampa Electric's forecasted overearnings; right?

A Yes, that's correct, if I understood your question. Could you repeat it?

Q I'm just trying to get to the question of why it is the parties met and discussed and then entered into these stipulations, and my question was, the whole reason for that was to address Tampa Electric's overearnings. I mean, there would be no other reason for these parties to enter into these stipulations, would there?

A I think that the Company's intention from, you know, pretty much the beginning of time was to also find ways to mitigate the rate impacts in the future resulting from the potential increase related to the Polk Unit coming on line. But I agree, certainly the overearnings provided the opportunity for that to happen.

Q Would you agree with me that the term "overearnings" essentially represents money that the utility has collected in excess of what the Commission has determined is a fair rate of return?

A Yes, I could agree with that.

Q And would you also agree with me that in the absence of the stipulations that we've discussed today, after an appropriate proceeding, the Commission could have ordered those overearnings refunded to the customers immediately?

A Yes, they could have.

Q And if the Commission had done that, if the parties had not entered into these stipulations, it would be correct, wouldn't it, that the customers would have received and essentially had in their pockets the overearnings amounts that we've been discussing today?

A Yes, that's true. They would have received dollars for 1995 and '96. But they also would not have had the $50 million refund that we gave back to customers, as well as they would have paid an additional $12 million a year related to the oil back-out clause that the Company agreed to collapse starting in 1996. So I think there would have been some dollars going both ways.

Q I think in your testimony when you were discussing Tampa Electric's position in regard to the accrual of interest, you at one point are referring to Paragraph 6, I believe, which is the paragraph that addresses the accrued interest. Actually, in the order we're looking at, it's Paragraph No. 9 on page 14?

A Yes.

Q And that's the language that you're relying on, isn't it, for Tampa Electric's position in the way that Tampa Electric has calculated the accrual of interest?

A That is not the only paragraph. I mean, I'm not exactly sure which issue you're exactly referring to. If you're talking about the overall issue of including the interest in the capital structure by the Commission, I think there are other paragraphs within the stipulation concerning the recovery of prudent costs that also apply. But to the extent of the -- assuming the spreading of the 12 months of the deferred revenue in calculating the interest, this would be the controlling provision.

Q Well, I'm also talking about the main issue in this case, which is whether or not Tampa Electric shareholders will be responsible for that interest or whether the customers will be responsible for it. And it's your position, isn't it, that Paragraph 9 is the controlling paragraph in that regard?

A Not just 9 alone. I think also Paragraph 11. If you don't mind, I'll read it.

Q I think I know where you are. That is the reasonable and prudent paragraph?

A Yes, it is.

Q Let's take a look at Paragraph 9 for a minute, if we can.

Would you agree with me that nowhere in the language of that paragraph does it explicitly state that ratepayers will be responsible for the payment of interest on the deferred revenues?

A That's true. It does not state explicitly that the shareholders in no way would bear that cost below the line.

Q Now, I think in your testimony, one of the things that Tampa Electric relies upon in support of its position is what the Commission did on this issue in 1995, is that right, in addressing the 1995 deferral?

A I think that this provision has been very similar throughout all three of the either agreements and/or stipulations. And I think that we were also pointing out that it's consistent with the Commission treatment that was afforded in 1995 as well.

Q Okay. If you'll turn to the bottom of page 2 of your testimony. I think it goes over to the top of page 3.

A Of the original direct testimony?

Q Yes, ma'am.

A Yes.

Q And in that passage beginning I guess on line 23, you're discussing what the Commission did in regard to Tampa Electric's 1995 earnings; correct?

A Correct. Yes.

Q It's true, isn't it, Ms. Bacon, that neither FIPUG nor the Office of Public Counsel pursuant to these stipulations was able to participate in the Commission's disposition of the 1995 earnings?

A That's true. And what that refers to, Commissioners, is the -- in the actual disposition of the calculation of the 1995 deferred revenues, there was a subsequent provision in I think the '96 deferred revenue that said that the FIPUG and OPC parties would not be allowed to participate in the actual outcome of the 1995 deferred revenue amounts.

Q So that pursuant to the stipulation, when the 1995 amount was discussed and the Commission's order was entered, there was no input from FIPUG or the Office of Public Counsel, because pursuant to the stipulation, they had agreed that they would not dispute the 1995 amount; correct?

A That is true. You all did not participate in that particular agenda and approval.

Q Ms. Bacon, do you agree that the stipulation that's attached to the May 20th order represents a very fine balance of benefits and burdens for all concerned?

A The stipulation that is the one that we were just referring to, the '96 stipulation?

Q Yes, ma'am.

A Yes.

Q And do you also agree, Ms. Bacon, that it was intended to comprise a comprehensive rate settlement among the three parties to the stipulation?

A A rate settlement? I'm not exactly sure of that exact wording that you're referring to there. I think it involved many aspects of the Company's earnings and rates for 1996, '97, and '98.

Q Okay. Would you look at page 8, which is actually the first page of the stipulation, the very first paragraph?

A Yes.

Q Do you now agree that this agreement was intended to represent a comprehensive rate settlement among the parties?

A That is the word. It also goes on to say covering Tampa Electric's base rates and rate of return. So I think it involves not just a base rate freeze. It also included, you know, calculations of earnings and allowed return on equity and other things that are outside I think of just the rate base --

Q You're --

A -- freeze.

Q I'm sorry. You're not disputing that this was intended to be a comprehensive rate settlement, are you?

A No. I guess that's the actual wording that's used in the stipulation, so I would agree.

Q Do you -- I guess you do have a copy in your booklet of the Quincy order that you've relied on

in your testimony. If you could turn to that.
A Yes. Hold on just a second.
Thank you. Yes, that's the same one. Okay. I have two copies now.
Q Yes, I do too. I didn't know we were going to be provided with this nice booklet.
Would you agree with me that this Quincy order does not involve any sort of settlement among parties that are affected by the disposition in that case?
A Yes, I would agree that this is not the result of a stipulation.
Q Do you also have the Southern Bell order that you cite and rely upon in your testimony?
A Yes, I do.
Q Can you point to any portion of that order that addresses the issues that we are here to discuss today? And for the record, that's Order No. PSC-94-0172-FOF-TL, which is the BellSouth rate settlement.
A Could you repeat your question?
Q Yes. I was just asking if you can point to any part of that order where it requires deferred revenues to be included in the capital structure or where it discusses the interest accrual that we've

been discussing this morning.

A One moment, please.

MS. KAUFMAN: Excuse me, Commissioners. I'm not sure who Ms. Bacon is consulting with, but I think I would object to that.

WITNESS BACON: Well, I just wanted to make sure if he could help me find something, but if that's -- I'll tell you what. I can answer it without talking to him.

BY MS. KAUFMAN:

Q Okay.

A I don't believe that in this particular order they have any reference to the capital structure treatment. However, what I was looking for was copies of the calculations of the Staff work papers that showed that the deferred revenues or the revenues that were subject to refund in the Southern Bell case were actually set into the capital structure as a single line item.

Q Well, take your time, Ms. Bacon, and look through this order, but I do not believe that there are any work papers or spreadsheets attached to it.

A I would agree with that. But I do believe that that was the treatment that was used in this case.

Q Just to be clear, in the order that you have in front of you that you've referred to in your testimony, there is no discussion of capital structrue or of the accrual on interest that we're discussing this morning? That's my question.

A I think I would agree with that. But I do believe still, though, that the calculation that was used by the Staff in the Southern Bell case -- in fact, the Commission quoted this themselves as a precedent for inclusion of the deferred revenues in the capital structure, so I would imagine that at least Staff would have known that that's what they have done in this particular case.

Q But it's not reflected in the order; right?

A That's correct.

Q Do you have a copy of the Prehearing Order in this case, Ms. Bacon?

A Yes, I do.

Q If you could turn to page 5, please. And this is Tampa Electric's basic position. And at the very bottom there, the -- I guess it's the third full paragraph, the first sentence, you say, or Tampa Electric says, "The purpose of accruing this interest is to recognize the time value of money associated with the deferred revenue as they're being used by the

Company during the stipulation period." Do you see that?

A Yes, I do.

Q Would you disagree, Ms. Bacon, however, that since the deferred revenues that we are discussing here are the ratepayers' revenues, that they are entitled to be compensated for the time value of their money?

A I believe that the interest accrual was to recognize that the deferred revenues were a source of funds, and we pay and accrue interest on other sources of funds similar to the deferred revenues. And I believe that that is what the interest provision in the stipulations was to account for. That was, I believe, Tampa Electric's understanding of reasons why the interest provision was included.

Q So I guess the answer to my question is that you would disagree that ratepayers are entitled to be compensated for the time value of their money?

A I think to the extent that a lot of our revenues are provided by our customers, and to the extent that this represented a source of revenues from customers, I think it was appropriate to accrue the interest on that. If that is to recognize the time value of money for those customer-provided revenues, then I think that that's what the Company has done.

Q Are you recognizing the value of that money to the ratepayers, or are you recognizing the value of that money to Tampa Electric?

A I think we're recognizing -- well, to the extent that deferred revenues ultimately end up being reversed as earnings to the Company to offset the cost of service, I think it might be a matter of both. I mean, you know, to the extent that those revenues were provided by customers, I think it certainly includes recognizing that those are customer-supplied dollars. They are a source of funds to the Company, and therefore, an interest provision on those deferred revenues is appropriate.

Q If you turn to the next page of the Prehearing Order, page 6, we're still on Tampa Electric's basic position. And I'm going to look at the second full paragraph, which is right above where FIPUG's position begins. Do you see where I am?

A Yes.

Q And if I understand what Tampa Electric is saying in that paragraph, it is that since in Tampa Electric's view, they have to accrue interest, to Tampa Electric it's clear that that amount ought to be included in regulatory earnings, and to do otherwise would amount to a disallowance of an expense that the Commission has approved. Is that a fair statement?

A Yes.

Q Would you agree with me, however, after looking at the stipulations and hearing the testimony, that the payment of this interest was an obligation that Tampa Electric's shareholders took on, and that amount of interest ought to be included below the line, and there would not be any disallowance of an approved regulatory expense?

A No. I still think -- I mean, it's certainly within the right of the Commission to take that decision if they feel appropriate, but I still believe that that would be a disallowance of the cost.

Q You think that if the Commission finds that this is a shareholder obligation that they undertook when they entered into this stipulation with FIPUG and Public Counsel that it would be a disallowance of an appropriate regulatory expense?

A If I understand your question, I think that you're asking me whether or not if the Commission disallows this cost, does that still not make it a disallowance of a regulatory -- I forget your exact words. A prudent regulatory expense. And I think that, yes, I mean, if I understand the question.

Q Maybe I wasn't clear. If this is an obligation the shareholders agreed to and it is to be reflected below the line, then it is not something that ought to be included when we are looking at regulatory earnings and expenses; correct?

A But I don't think anywhere does it ever say that's what was agreed by the parties.

Q I understand. That's an issue. We have a fundamental disagreement over that. I think that's clear.

A That's true. It would be our position that if the Commission so decided to put those dollars below the line, it would be through a disallowance of a prudent regulatory expense.

Q Even though it would be the Commission's determination that that had been an obligation the shareholders agreed to take on?

A I think that's the Company's position. The Commission can certainly decide what they feel is appropriate, but I believe that that would still be the Company's position.

Q I think I understand the Company's position.

Would you agree with me, Ms. Bacon, that Tampa Electric's proposed treatment of the interest essentially had the effect of decreasing any potential refund that customers would see when the stipulations come to an end?

A No, I do not. I believe that the inclusion of the interest in the capital structure only recognizes the actual cost of providing utility service to its customer in those years, and that the deferred revenues were the source of funds that were used by the Company. So I don't believe that -- I think it ends up calculating the appropriate level of deferred revenues. To exclude it would artificially inflate the deferred revenues at the expense of a disallowance of a cost below the line.

Q Okay. I think if you listen carefully to my question, we can move this along.

A Okay.

Q Would you agree that Tampa Electric's methodology of calculating the accrued interest has the effect of decreasing the amount of any potential refund that would be available at the termination of the stipulations?

A I still have to disagree with that. I think that whether or not including the interest on the deferred revenues in the capital structure as the source of funds or including some other type of replacement source of funds that represent that Tampa Electric had to have a source of funds to run its operations in that year results in a similar outcome by including the interest in the capital structure than by not including it.

In other words, I don't think that any -- if you go back, you know, several, you know, a couple of decades, I don't believe I ever recall any time where the Commission calculated overearnings for a company and did not recognize that those overearnings had a cost associated with them. In the past, what the Commission would do is, they would remove the liability from rate base, which would cause the rate base to go up. And then in the capital structure they would do what we call a pro rata, where you would spread that amount of deferred revenues across the capital structure. And by doing that, you included a cost equal to the overall cost of capital, but you still recognized by doing that that those source of funds had to be available to run the operations of the Company.

An easier way maybe to look at it is to look at it as a balance sheet, and you have assets and liabilities. And if you pull out the liabilities associated with the deferred revenues, something has to replace it. The Company could not have run its operations without that. And so I think the net effect of including the interest on the deferred revenue puts you back to where you would have been under the other method the Commission has used in the past.

Q Do you still have the Prehearing Order in front of you?

A Yes.

Q Okay. If you could turn to page 10, please, and if you would look at Issue No. 2 there.

A Yes.

Q And if you could read the first sentence of Tampa Electric's position, please?

A "The effect is to increase deferred revenues by $2.502 million."

I think that recognizes that if you assume you all's calculation where you zero out the interest rate, obviously the deferred revenues would increase. They would increase if you went in and reduced O&M expense by $10 million, but it's still removing a prudent cost and putting it below the line, and it's only by doing that that deferred revenues will increase. I mean, you know, we could get large amounts of deferred revenues to the extent that, you know, additional adjustments were made across all of the Company's costs. So, I mean, this to me was just a mechanical, that this would be the effect.

Q Right. And I just want it to be clear that understanding what Tampa Electric's position is, and understanding what FIPUG's position is, that the effect -- what we're talking about here is increasing the amount of deferred revenues by about $2-1/2 million. Do you agree? I mean, that is your position; correct?

A It is my position. I think that it's important to point out, though, that this is just the mechanics of disallowing an expense.

And so to your earlier point about -- I think you were trying a while ago to ask me a question regarding what would be the effect of including the interest, and I was saying that I think that it ends up resulting in an amount that's similar to the prior Commission practice of always including a source of funds in the capital structure.

In this particular instance, this sentence appears to disagree with my earlier position, and I think this is a different situation, in that all you're doing is going in and zeroing out the cost rate in the capital structure, and obviously, then the deferred revenue amount would increase.

Q And, you know, we may be making this more complicated and difficult than it is. The only thing I want to be clear about is that if the approach that is suggested by FIPUG and Public Counsel is followed by the Commission when they look at the stipulations and hear the evidence here, that the effect is going to be similar to what TECO has calculated in its position on Issue No. 2.

A That is the impact.

MS. KAUFMAN: Thank you. That's all I have.

CHAIRMAN JOHNSON: Staff?

CROSS EXAMINATION

BY MR. KEATING:

Q Ms. Bacon, I just have a few questions.

First, if a zero cost rate is assigned to deferred revenues in the capital structure, would you agree that interest reconciliation and income taxes would change?

MR. HOWE: Objection.

CHAIRMAN JOHNSON: Okay. Could you turn your mike on?

MR. HOWE: I think it is on. I'm just objecting on the basis that -- excuse me. I don't believe this is within the scope of her direct testimony.

CHAIRMAN JOHNSON: Staff?

MR. KEATING: I'll withdraw the question, and we'll address this in Ms. Bacon's rebuttal testimony.

CHAIRMAN JOHNSON: I'm sorry. You're going to address it in rebuttal?

MR. KEATING: Yes.

CHAIRMAN JOHNSON: Okay. Is that it?

MR. KEATING: I believe -- let me just ask a couple of questions.

CHAIRMAN JOHNSON: Sure.

BY MR. KEATING:

Q Turning to what was identified as Exhibit 4, I believe that exhibit shows that the 13-month average of deferred revenues in the capital structure, the 13-month average balance of deferred revenues in the capital structure was $77,670,075.

A Hold on just a second. I'm still looking for it.

Q I will.

A I seem to have misplaced it.

Oh, here it is. I found it.

Q Okay. I'll repeat the question. That

exhibit shows that the 13-month average balance of deferred revenues in the capital structure for '95 and '96 is $77,670,075; is that correct?

A Yes, it is.

Q And what portion of the balance consists of interest included for 1995?

A For 1995, on a 13-month average basis, it would be 2,977,754. It's shown on the left side at the bottom under 13-month average.

Q Okay. And then the portion of the balance that consists of interest included for 1996 would be $309,018; is that correct?

A Yes, that's correct.

Q Is it correct that Tampa Electric recovered the 1995 interest in the capital structure by use of the commercial paper rate?

A Yes, that's correct.

Q So if a zero cost rate is assigned to 1996 deferred revenues in the capital structure, is it correct that Tampa Electric would not be able to recover the 1996 interest?

A That's correct.

Q So if a zero cost rate is assigned, do you believe that the 1996 accrued interest should be included as part of the deferred revenue balance?

MR. HOWE: Objection. Chairman Johnson, this is not an issue that has been addressed by the Company.

Basically what has happened is, the Company has said put it in -- put all deferred revenues plus accumulated interest in the capital structure at the 30-day commercial paper rate. We've said put it in the capital structure at a zero cost. We have not disputed the dollar amount of deferred revenues plus interest in the capital structure.

We believe the way the APA is written now, I believe it's 120.80(13)(b), which says a matter not in dispute will be deemed stipulated.

We only protested the cost rate in the capital structure, not the balance in the capital structure. We think it's perfectly proper under the Commission's interpretation of that statute that, for example, we can contest the cost rate on equity without contesting the dollar amount of equity. So we don't think this is an issue that has been raised. It hasn't been placed in dispute, and it's not appropriate to be addressed here.

Secondly, if anything, it's rebuttal. If Ms. Bacon had wanted to come back in her rebuttal testimony and say Tampa Electric disagrees with Public

Counsel's position, but if they are to use a zero cost in the capital structure, then you should change the balance in the capital structure. That has not been addressed in her rebuttal testimony, so this appears to be an attempt by Staff to get around the statute and/or to introduce rebuttal that the Company has chosen not to address.

CHAIRMAN JOHNSON: Staff, response?

MR. KEATING: Well, I would first point out that this was a matter that was brought up at the prehearing. Staff had raised a separate issue regarding the accrued interest and the cost rate that would apply. Commissioner Garcia as the Prehearing Officer determined that that separate issue -- well, let me step back. The issue would not be included in the Prehearing Order as a separate issue, but stated that Staff could address the issue within another issue in this proceeding.

Second, I believe from the cross examination of Ms. Bacon that the door is open for this type of question to address this issue.

CHAIRMAN JOHNSON: In the cross examination? Oh, you're saying during your cross examination, you believe that this particular cross examination --

MR. KEATING: No, ma'am.

CHAIRMAN JOHNSON: I didn't hear your last part.

MR. KEATING: Based on the cross examination questions asked by Public Counsel or FIPUG.

MR. HOWE: I don't believe I asked any questions dealing with the dollar amount of deferred revenues to be included in the capital structure. The total dollar amount, all I did is establish that the $77 million shown on this last page of Exhibit 4 is in fact the same $77 million that was included in the Commission's proposed agency action order.

MR. KEATING: If I could have just a minute.

(Pause in the proceedings.)

MR. KEATING: Staff will withdraw the question. We have no further questions at this point.

CHAIRMAN JOHNSON: Okay. Are these questions that we need to have answered?

MR. KEATING: Yes. It's Staff's opinion that this is something that needs to be addressed, and it was our understanding from the Prehearing Officer's order that this was an issue that we would be able to address.

CHAIRMAN JOHNSON: Could you state what the question was again?

MR. KEATING: The question was, if a zero cost rate is assigned, did Ms. Bacon believe that the 1996 accrued interest should be included as part of the deferred revenue balance.

CHAIRMAN JOHNSON: And Public Counsel objected --

MR. HOWE: The objection is --

CHAIRMAN JOHNSON: -- to the question as to outside of the scope, or is it --

MR. HOWE: It's two things. It's outside the scope of her direct, because her direct did not address the dollar balance in the capital structure.

Secondly, I believe what Staff is trying to do is address what they think is an inconsistency in FIPUG and Public Counsel's approach. In other words, we have challenged only the cost rate in the capital structure. Staff would like to introduce that Public Counsel has not gone far enough, that if you are to modify the cost rate, then you also should address the balance.

Under the APA provision, it's not a matter that has been put in dispute. It's not addressed in the Company's direct testimony, it's not addressed in FIPUG or Public Counsel's witnesses' testimony, and it's not addressed in the Company's rebuttal. So I think it's outside the scope of this proceeding. I think the Company, if they wanted to introduce it in rebuttal, then they could have done so, but they have chosen not to address it.

And I think the Commission needs to make a decision also, what does the APA provision mean when a matter is not placed in dispute? Can Staff introduce it at the hearing when the parties have chosen not to address it?

COMMISSIONER CLARK: Mr. Howe, let me ask you a question. What about the fact that Staff is obligated to flesh out the record for us and sort of act as our investigatory body? Would it help if we asked the question as opposed to Staff?

MR. HOWE: Well, no. Actually, I would object if you asked the question. And the reason is, if Staff is to be your investigative body, then essentially the Commission needs to say that they don't view that provision in the APA as having much force and effect, because whether the parties place the matter in dispute, and whether the statute says having not been placed in dispute, it's deemed stipulated, Staff can put it in contention, and the parties will have to address it.

COMMISSIONER CLARK: Well, I had understood Staff tried to put it in contention by asking that it be an issue. And I presume they were told by Commissioner Garcia that it was subsumed in another issue and that they could explore it.

MR. HOWE: Well, I think what he said was, his understanding is that Staff is going to explore it. I don't dispute that. For our position, you'll see the last three sentences of our position on this issue, which is --

COMMISSIONER DEASON: Mr. Howe, let me ask you a question.

MR. HOWE: -- Issue 1.

COMMISSIONER DEASON: Mr. Howe?

MR. HOWE: Yes, sir.

COMMISSIONER DEASON: I'm going to probably oversimplify this, but what I hear you saying is, if this Commission issued an order that said A plus B equals C, and the facts of this case is that 2 plus 2 equals 4, and somebody took issue with B and said B should not be 2, it should be zero, that we're obligated then to issue an order that says 2 plus zero equals 4.

MR. HOWE: I would characterize that as an oversimplification, yes. No, I think --

CHAIRMAN JOHNSON: And that was simple?

MR. HOWE: No. The difference is, if you issue an order that's saying the amount of equity in the capital structure is $10 million at a 12% cost rate, and I protest and say I think the appropriate cost rate is 9%, and nobody puts the dollar of equity at issue, then I think under the statute it's deemed stipulated.

The Staff wants to say, no, having addressed the cost rate, somebody needs to place the dollar balance in the capital structure at issue. And that just hasn't been done, either in our protest or in the testimony of any of these three witnesses.

COMMISSIONER CLARK: Commissioner Deason, I agree with --

COMMISSIONER DEASON: Well, I understand the -- I guess -- well, I don't understand the legalities, but it seems to me the issues just go hand in hand, and it's difficult to address one without the other.

MR. HOWE: Well, I guess in essence --

MR. HART: Madam Chairman, the --

MR. HOWE: -- I'm asking for some guidance on that very aspect of it, because we felt somewhat constrained by the Commission's order and the statute, and it seemed to limit our ability to introduce things that weren't covered in the order because of the way the statute is now written.

And it's our understanding, although I can't cite to any explicit decisions where the Commission has generally followed the approach that if it isn't protested and placed in dispute, that it's going to be deemed stipulated as it exists in the proposed agency action.

CHAIRMAN JOHNSON: Mr. Hart?

MR. HART: What happens when you have a method like this proposed by the Company and adopted in the PAA, if you introduce and object to the methodology and raise an issue like this, the zero cost of capital, there are mathematical calculations that result from doing it if you switch theories.

Mr. Howe seems to be arguing that you can intentionally calculate the wrong number or that you can calculate the impact on customers to be different than it actually is if somehow on some procedural ground you raise one issue and don't raise other issues that no one else would know was in the -- until you see the other person's proposal.

But more importantly, I think Commissioner Garcia's ruling -- this issue is discussed in the positions with regard to Issue 1 by everyone, or at least by OPC and the Company, and it's addressed in the last sentence of the Company's position, and it's addressed at length in Mr. Howe's position in the Prehearing Order.

So this issue was raised with the Hearing Officer. He ruled that this issue could be addressed in this case and that it would be subsumed as part of Issue No. 1. The parties have set forth their position on this issue. We believe it's a mathematical calculation that results from changing the theory of how you proceed with deferred revenues that results from the issue raised by the Office of Public Counsel, and this issue is addressed in the Prehearing Order.

CHAIRMAN JOHNSON: Thank you.

I understand that -- Staff, did you want to withdraw it or not? I'm assuming that you do not. And if you do, then one of the Commissioners will ask the question. Why don't you restate the -- I'm sorry, Mr. Elias.

MR. ELIAS: Two points. The first is that if we withdraw this question, it would be our intent to pursue it either on rebuttal or through one of the other witnesses, depending on the way the cross examination goes.

And the second thing is, on the question of the effect of Section 120.80(13)(b), Florida Statutes, dealing with the scope of the issues that can be addressed in a protest on proposed agency action, we do believe that this is a issue that is reasonably raised by Public Counsel's protest, and that if you're going to challenge the methodology, that the calculations that are reasonably associated with that methodology are at issue.

So I don't think that the question of the impact of the issue that's protested on other aspects of the Company's rate base, balance sheet, and capital structure are beyond the scope of what's in the protest.

CHAIRMAN JOHNSON: Thank you, Mr. Elias. And I didn't mean to put you all on the spot. Obviously, you're going to ask it then when she comes back? You think it's more appropriately addressed then?

MR. ELIAS: If it's --

CHAIRMAN JOHNSON: I just wanted to make sure that you all weren't just withdrawing it and you thought it should be addressed.

MR. HOWE: Chairman Johnson, could I --

CHAIRMAN JOHNSON: And at least now, Mr. Howe, you're on notice.

MR. HOWE: Could I offer a suggestion?

CHAIRMAN JOHNSON: Uh-huh.

MR. HOWE: If Staff really wants to address this, one of the things we're very concerned about is that the Company did not address it in its either direct or rebuttal. We're constrained by the prefiled testimony. I will not object to this witness being asked this question at this time if Staff will agree to ask our witnesses the same question.

MR. ELIAS: We would be glad to do that.

CHAIRMAN JOHNSON: Does that work better?

MR. HOWE: Then we can at least address it from both sides.

CHAIRMAN JOHNSON: Okay. Then let's start over with the question.

MR. KEATING: I'll repeat the question, because it has been a while.

BY MR. KEATING:

Q If a zero cost rate is assigned, do you believe that the 1996 accrued interest should be included as part of the deferred revenue balance?

A No, I do not. In other words, I believe that the interest amount should be removed from the deferred revenues.

And the reason why I believe that is that it would seem somewhat I guess hypocritical or contradictive, I guess is the appropriate word, you know, to not recognize that the interest cost exists when you zero out the cost rate, but then to leave the interest as if it were existing in the deferred revenue. It's either a cost or it's not. And so to the extent of removing it in one place and leaving it in the balance, it would seem to be contradictive in theory. So for that reason, I think it ought to be removed.

MR. KEATING: Commissioners, I had a couple other questions for Ms. Bacon that the Public Counsel had objected to before. Maybe now in light of the discussion that just occurred, if Public Counsel doesn't have the objection still, I could go ahead and ask those questions.

CHAIRMAN JOHNSON: And were they of the type that you would ask Public Counsel's witness?

MR. KEATING: I believe I have a similar question for Public Counsel's witness, yes.

CHAIRMAN JOHNSON: Go ahead and ask the

question.

BY MR. KEATING:

Q If a zero cost rate is assigned to deferred revenues in the capital structure, would you agree that interest reconciliation and income taxes would also change?

A Yes, it would.

Q Would you also agree that as a result, the achieved net operating income and achieved return on equity would also change?

A Yes, it would.

Q Would you agree that these changes would simply be a fallout of assigning a zero cost rate to deferred revenues in the capital structure?

A Absolutely. And if I could clarify that, I think by zeroing out the interest rate in the capital structure, the adjustments that he's referring to recognize that the income tax benefit that's included in the income statement would go away. I mean, to the extent that you zero out an interest cost, then everything else being equal, your income tax provision that's in your net operating income should increase. And what he's referring to is just a reflection of those adjustments throughout the other schedules.

MR. KEATING: That's all the questions I have. Thank you.

Commissioners?

Redirect?

MR. HART: No, we don't have any redirect questions.

CHAIRMAN JOHNSON: And there weren't any exhibits, so --

MR. HART: Yes, we do have --

CHAIRMAN JOHNSON: Oh, yes. I'm on the wrong page. There's nothing attached.

MR. HART: At this point we only have Exhibit No. 1.

CHAIRMAN JOHNSON: You had the request for official recognition. I didn't admit that before, but show that admitted without objection.

(Exhibit 2 was received in evidence.)

MR. HOWE: And that would be Exhibit 2?

CHAIRMAN JOHNSON: That would be Exhibit 2.

MR. HOWE: And I would move the admission of Exhibits 3, 4, and 5.

CHAIRMAN JOHNSON: Show those all admitted without objection.

(Exhibits 3, 4, and 5 were received in evidence.)

CHAIRMAN JOHNSON: And then Staff had --

MR. KEATING: Staff would move Exhibit 1.

CHAIRMAN JOHNSON: Show that admitted without objection.

(Exhibit 1 was received in evidence.)

CHAIRMAN JOHNSON: Thank you. You're excused for now.

Could we do kind of -- let me get an estimation of time for the witnesses that are left. I know -- do you pronounce it "Pollock" or "Pollack"?

MS. KAUFMAN: Mr. Pollock.

CHAIRMAN JOHNSON: Mr. Pollock. The summary, is it going to be short, long?

MS. KAUFMAN: It's going to be short.

CHAIRMAN JOHNSON: Okay. Let's say five minutes for that. Cross?

MR. HART: Hopefully it won't take more than 30 to 45 minutes.

CHAIRMAN JOHNSON: Forty-five minutes. Staff?

MR. KEATING: For Witness Pollock?

CHAIRMAN JOHNSON: Uh-huh.

MR. KEATING: I don't believe we have any questions for Witness Pollock.

CHAIRMAN JOHNSON: And your --

MR. HOWE: I have no questions for Mr. Pollock.

CHAIRMAN: Okay. Mr. Larkin, Jr., for cross?

MR. HART: It would be about the same. It's really hard to anticipate. It could be shorter than 30 minutes for both of them. Depending on their answers, it could be a little bit longer. It's hard to say.

CHAIRMAN JOHNSON: Thank you. His summary?

MR. HOWE: It will be fairly short.

CHAIRMAN JOHNSON: Ms. Kaufman?

MS. KAUFMAN: I may have a question or two for Mr. Larkin, about five minutes.

MR. KEATING: And Staff's will be fairly short.

CHAIRMAN JOHNSON: Ten minutes?

MR. KEATING: Ten minutes, yes.

CHAIRMAN JOHNSON: And the rebuttal? Don't you have some more for Bacon?

MR. KEATING: No, I asked all those questions.

CHAIRMAN JOHNSON: Oh, okay.

MR. HOWE: I will have about a half an hour of questions for Ms. Bacon on rebuttal.

MS. KAUFMAN: Maybe 15 minutes.

CHAIRMAN JOHNSON: Okay. We'll take a break until 1:00, a short lunch break.

(Proceedings recessed for lunch at 12:10 p.m., to resume at 1:00 p.m.)

(Transcript continues in sequence in Volume 2.)