BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into Affiliated Cost-Plus Fuel Supply Relationships of Florida Power Corporation - Phase II.	)	DOCKET NO. 860001-EI-G ORDER NO. 22402 ISSUED: 1-10-90

The following Commissioners participated in the disposition of this matter:

MICHAEL McK. WILSON, Chairman
THOMAS M. BEARD
BETTY EASLEY
GERALD L. GUNTER
JOHN T. HERNDON

ORDER DENYING CITIZENS' MOTION FOR RECONSIDERATION

BY THE COMMISSION:

CASE BACKGROUND

In February, 1986, we opened Docket No. 860001-EI-G for the purpose of investigating the affiliated cost-plus fuel supply relationships between Florida Power Corporation (FPC) and Tampa Electric Company (TECO) and their respective affiliated fuel supply corporations. Also, in February, 1986, we established Docket No. 860001-EI-F in Order No. 15895 for the purpose of determining why FPC's cost to transport coal by its affiliated waterborne system exceeded its costs to transport coal by non-affiliated rail. In September, 1987, we issued Order No. 18122, which removed TECO from Docket 860001-EI-G, established Docket No. 870001-EI-A for hearing the TECO issues, consolidated the two FPC issues for hearing in Docket No. 860001-EI-G and closed Docket No. 860001-EI-F.

By Order No. 18982, issued on March 11, 1988, we decided to bifurcate the hearings in this docket as follows: (1) the policy issue of whether a market price standard should be imposed on the recovery of costs for goods and services purchased from affiliated companies and (2) the separate issue

of whether any of the monies FPC had recovered through its fuel and purchased power cost recovery clause for goods and services purchased from affiliates from 1984 to date had been imprudently or unreasonably incurred and should, therefore, be refunded to its customers. Hearings on the policy issues in this docket were held on May 11-13, 1988. Hearings on the prudence issues in this docket were held December 14-16, 1988 and April 19, 1989. Order No. 21847, containing our decisions on the prudency issues, was issued September 7, 1989. Office of the Public Counsel (OPC, Public Counsel) filed a motion for reconsideration on September 22, 1989. This order addresses that motion.

DISCUSSION

First, we find that we did not overlook or otherwise misapprehend the adjustment necessary to disallow additional costs incurred to ship Kentucky May coal by a rail/water mode when direct rail shipment was cheaper. Public Counsel maintains that our decision regarding the price of Kentucky May coal considered only the reasonableness of the F.O.B. mine price. Public Counsel's witness, Mr. Jaron, did not contest the reasonableness of the F.O.B. mine price of the Kentucky May coal. In fact, Witness Jaron testified that the Kentucky May price was reasonable. However, Witness Jaron did conclude that Electric Fuels Corporation (EFC) was imprudent by shipping most of the Kentucky May coal by water when rail delivery was cheaper. It is not contested that water transportation of Kentucky May coal is more costly than rail. EFC's witness, Mr. Carter, agreed to this fact. No determination of the reasonableness of the transportation cost of Kentucky May purchases was included in this issue. To do so would have been incorrect. In Issue Nos. 9, 10, 11 and 12, we addressed transportation charges. We determined that was reasonable for EFC to use the capacity of three barges to ship coal to Crystal River through 1986 and four barges thereafter. We further determined that EFC did transport more coal by water than was reasonable and an adjustment was made to disallow transportation costs associated with excess barge usage. Since EFC had a responsibility to move a certain volume of coal by water, it does not matter whether the waterborne coal came from Kentucky May or other mines. An adjustment for the transportation charges associated with the Kentucky May purchases would be either inappropriate or double counting.

We further find that we did not overlook or otherwise fail to consider that FPC paid more for Powell Mountain Joint Venture (PMJV) coal than EFC charges other electric utilities for such coal. Public Counsel maintains that it is neither prudent for EFC to make sales of compliance coal to third parties from PMJV reserves which might not contain adequate economically recoverable compliance coal reserves, nor for EFC to sell spot compliance coal from Powell Mountain to third parties at a price lower than the contract price charged to FPC. Further, it is argued, it is not prudent to purchase spot coal for FPC as replacement coal and charge FPC an amount in excess of the spot price. Finally, Public Counsel argues that the policy of replacing high priced contract coal with lower priced spot coal is imprudent.

Public Counsel's concern about the sufficiency of the Powell Mountain compliance coal reserves was addressed in Issue No. 16. This issue addressed whether sufficient reserves of compliance coal exist at Powell Mountain which can be mined economically to meet the EFC/PMJV contract provisions. The record indicates that there are sufficient reserves of compliance coal at Powell Mountain to satisfy the tonnage requirements of the EFC/PMJV contract. The issue becomes whether the reserves can be mined economically. We made no finding on this issue because of the "economically mined" qualifying phrase. However, it is academic whether the Powell Mountain reserves are economic since Powell Mountain has a contract commitment to supply certain tonnages to EFC and since we have decided to evaluate the Powell Mountain coal price using a market standard.

Public Counsel also stated that it was not prudent for EFC to sell spot coal from Powell Mountain to third parties at a price lower than the contract price charged to FPC. First, Powell Mountain has not sold any compliance coal to third parties without first offering the coal to EFC. Second, Powell Mountain has a contract with EFC and we have decided to evaluate the contract price using a market methodology. Third, any sales of Powell Mountain compliance coal to third parties by EFC were made to lower the price of coal to FPC by replacing the high priced contract coal with lower priced spot coal.

Public Counsel does not approve of replacing high priced contract coal with lower priced spot coal to reduce coal cost

to FPC. On several occasions, EFC has sold high priced contract coal intended for use at Crystal River to third parties on the spot market. The spot price to third parties is generally much less than the contract price of the coal originally purchased for FPC. Florida Power Corporation is obligated to pay the full contract price, and is responsible for the differential between the full contract price and the spot price charged to the third party. EFC then purchases replacement coal on the spot market at a price less than the price charged to the third party. FPC is responsible for this spot price. The difference between the price of spot coal to third parties and the price of spot replacement coal represents a savings. A portion of this savings is retained by Progress Trading, an EFC affiliate, and a portion of the savings is realized by FPC's ratepayers. Progress Trading acts as a broker and is the corporate entity which arranges for the third party spot coal sales and the replacement coal spot purchases. Witness Carter testified that such a transaction which replaced Columbian coal reduced the price of coal to FPC's ratepayers by $984,128.

We find that it is prudent for EFC to sell coal on the spot market at a price less than the PMJV price to FPC if the coal is replaced at a price which results in a savings to FPC's ratepayers. We further find that we correctly rejected all three of the following proposed findings of fact:

2. FPC's ratepayers have underwritten EFC's participation in the PMJV and should have first claim to any coal from that source.

3. FPC's ratepayers have been harmed to the extent that PMJV reserves are depleted by sales to other utilities.

4. If PMJV coal can be sold to other utilities at spot prices below PMJV contract prices, it can be sold to FPC on the same basis.

Specifically, with respect to the first finding, the record does not support the conclusion FPC's ratepayers should have first claim to any coal from PMJV. Rather, the record indicates that PMJV has a contractual obligation to supply

coal to EFC through the year 2002 and that there are sufficient reserves to satisfy this contractual obligation. With respect to Public Counsel's proposed finding regarding the PMJV reserves, the record indicates that there are sufficient reserves to satisfy the EFC contract. Therefore, we properly rejected this proposed finding of fact.

Finally, the record does not support the finding that if PMJV coal can be sold to other utilities at spot prices, it can be sold to FPC on the same basis. The record indicates that PMJV has not sold any compliance coal to third parties without first offering the coal to EFC. However, the price of coal to FPC is governed by contract. The record further indicates that any sales of Powell Mountain compliance coal to third parties by EFC were made to lower the price of coal to FPC by replacing the higher priced contract coal with lower cost spot coal.

We further find that we were not mistaken in our analysis which concluded that Dixie tow number 3 was needed to ship coal in the 1984-1987 time frame. Public Counsel maintains that EFC could have shipped all coal to FPC using the original two ocean barges and rail deliveries. The capacity of two ocean barges is 1.2 million tons of coal per year. All other coal would have to be shipped to FPC by rail. Assuming Dixie operated a two barge fleet, FPC would have received 2.9 million tons by rail in 1984, 3.7 million tons by rail in 1985, 4.2 million tons by rail in 1986 and 4.7 million tons by rail in 1987.

We determined that FPC had the capacity to receive at least 3.6 million tons, and possibly as much as 4.0 million tons of coal by rail per year. Obviously, more than two ocean barges were needed in 1986 and 1987. The issue can now be restated as whether a third barge was needed in 1984 and 1985 and what facts should EFC have considered in 1981 when EFC authorized the construction of the third barge.

We determined that it was appropriate for EFC to transport 1.0 million tons of Massey coal by water in 1982. The record indicates that EFC could have planned to ship some Powell Mountain coal by water in 1982 and 1983. The record also indicates that the higher sulfur Amax and Consol midwestern coals would be phased out between 1982 and 1983 but does not indicate what volumes would be shipped in those years. It

would be reasonable for EFC to expect water deliveries to be in excess of 1.2 million tons in 1982 and 1983.

Public Counsel asserts that FPC should have known when the Amax and Consol contracts were signed that environmental restrictions would not allow the high sulfur coals to be burned once Crystal River Units 4 and 5 came on-line. Public Counsel is correct. Public Counsel also maintains that EFC should have executed low sulfur contracts which would have probably been more economical to deliver by rail. FPC points out that these two contracts were renegotiated and that the record indicates that the new Amax low sulfur contact is delivered by rail but that the new Consol low sulfur contract can only be delivered by water. Both contracts are for 500,000 tons of coal per year. The combined tonnage of the Massey and Consol contracts is 1.5 million tons per year. Given an ocean barge capacity of 600,000 tons per year, this equates to a need for 2.5 barges. We are of the opinion it was reasonable for EFC to maintain a fleet of three ocean barges in 1984, 1985 and 1986. This is consistent with our decision in Docket No. 850001-EI-A.

We find that we correctly determined that it was prudent for EFC to maintain a three barge fleet in order to reduce operational constraints, to enhance reliability and to increase EFC's negotiating leverage with the railroads. We further find that if we use a market price methodology to evaluate the price of Powell Mountain Joint Venture coal, any payments to the recoupable reserve fund should be considered to be a part of the PMJV coal price when payment occurs. Electric Fuels Corporation negotiated a "price cap" with PMJV in 1984 to constrain the escalating base price. Under this agreement, EFC was billed an F.O.B. mine price which was less than the full contract rate. The dollar difference between the invoiced amount using the price cap and the contract price accumulated in a "recoupable reserve" fund. Repayment of this fund can be triggered by certain market conditions. This price cap was in effect through 1988. Using a market price methodology to evaluate the price of Powell Mountain Joint Venture coal, any payments to the recoupable reserve fund should be considered to be a part of the PMJV coal price when payment occurs.

We further find that we neither failed to address the prudence of EFC's decision to expand the IMT commitment and

the effect of this decision on FPC's ratepayers, nor the IMT rate which EFC concedes is excessive. Public Counsel makes an argument that EFC has favored its waterborne affiliates to the detriment of FPC's ratepayers. In 1984, EFC increased its tonnage commitment to IMT from 1.2 million tons per year to 1.75 million tons per year. Public Counsel points out that this increased tonnage is not dedicated to FPC business and maintains that no economic analysis was performed prior to EFC's decision to increase the IMT tonnage commitment. EFC witnesses indicated that studies were done, but that they had been lost in several office moves and could not be provided.

We addressed the tonnage commitment to IMT when we considered the prudence of purchasing Dixie tows 3 and 4. The waterborne transportation system is a network extending from the coal mine to Crystal River. When we determined that it was reasonable for EFC to deliver up to 1.8 million tons of coal by water in the period 1984-1986 and up to 2.4 million tons of coal by water in 1987, we decided what volume of coal was reasonable on the waterborne network. When we disallowed certain costs for excess barge use it effectively disallowed costs for excess waterborne transportation system usage. The disallowance was calculated by considering the amount which total waterborne transportation cost from the mine to Crystal River exceeded rail costs from the mine to Crystal River. This disallowance considered any overuse of IMT.

Public Counsel also maintains that the IMT rate was excessive. Witness Carter conceded that the current contract rate charged by IMT exceeds the current market conditions. However, he indicated that the rate was reasonable when the contract was signed. We find that the IMT rate was also addressed in our decision concerning excess waterborne transportation usage and that the current rate is another example of why we should impose a more stringent review of prices charged by affiliates. We find, therefore, that we need not reconsider our decision on this issue.

We further find that we did not mistakenly reject certain proposed findings of fact and conclusions of law relating to the issue of whether FPC's efforts to control its fuel supply destiny through EFC and its affiliates resulted in additional risk and fuel cost to FPC's ratepayers. We properly rejected the following finding of fact as required by Chapter 120, Florida Statutes:

5. FPC's delegation of its fuel procurement responsibilities has caused ratepayers' interests to be subordinated to shareholder interests.

In Order No. 21847, we concluded that there is a conflict between the ratepayers' interest and the shareholders' interest because of FPC's decision to allow EFC to handle its fuel procurement activities. However, we do not believe nor does the record support the conclusion that this inherent conflict necessarily means that the ratepayers' interests are subordinate to the stockholders' interests.

The record of this proceeding contains testimony which indicates that EFC has engaged in specific activities which inured to the benefit of FPC's ratepayers. Witness Bass testified that 75% of EFC's share of the Dixie profits are used to reduce the price of coal to FPC. In addition, Witness Bass testified that with respect to IMT any profits received by EFC associated with FPC coal business is used to reduce the price of coal to FPC. We believe that these actions by EFC indicate that the ratepayers' interests are not subordinate to the interests of EFC's shareholders.

We further find that we properly rejected the following proposed conclusion of law:

5. Pursuant to the Commission's Fuel Procurement Policy, Order No. 12645, Appendix A, Paragraph I.C., FPC's management is solely responsible for procuring fuel in the most cost efficient manner possible. FPC's contracts with EFC and the authority granted to EFC pursuant to those contracts are not consistent with that policy.

The guidelines contained in the Commission's Fuel Procurement Policy, Order No. 12645, Appendix A, are designed to be broad and flexible enough to encompass all reasonable procurement decisions. (Order No. 12645, p. 5.) In fact Paragraph I.C. upon which Public Counsel relies also states that the utility should have the flexibility to employ any means to achieve the result of securing fuel in a most

cost-efficient manner. Clearly, our policy is broad enough to allow FPC to delegate its fuel procurement responsibilities to EFC. In addition, in Order No. 12645, we expressly stated that "the guidelines are applicable to affiliates and subsidiaries of utilities...engaged in the procurement of fuel or services for a utility."

We find that FPC's decision to delegate its fuel procurement responsibilities to EFC was not inconsistent with the Commission's Fuel Procurement Policy and we find, therefore, that Public Counsel's request for reconsideration of this proposed conclusion of law should be denied.

We also find that the following proposed conclusion of law was properly rejected:

> 6. Pursuant to Appendix A, Paragraph I.G. of Order No. 12645, FPC bears the burden of proof to document the reasonableness of its procurement practices and the resultant expenses from such practices. FPC has not met that burden with regard to expenses incurred pursuant to its contracts with EFC or EFC's contracts with affiliated entities.

Basically, Public Counsel argues that this proposed conclusion of law should not have been rejected because FPC did not meet its burden of proof regarding the reasonableness of its procurement practices and the resultant expenses from such practices. The record indicates that FPC entered into two fuel supply agreements with EFC which allow for the flow-through of costs incurred by EFC plus overhead and a profit component set at the midpoint of FPC's allowed return on equity. FPC's cost-plus arrangement with EFC was entered into prior to the adoption of the Commission's Fuel Procurement Policy contained in Order No. 12645.

We find that it is appropriate for EFC to present evidence regarding the prudence and reasonableness of its efforts to procure fuel on behalf of FPC. We expressly stated that the fuel procurement guidelines should be applied to affiliates and subsidiaries of utilities or utility holding companies engaged in the procurement of fuel or services for a utility.

(Order No. 12645, pgs. 5 and 6.) As was noted in Order No. 12645, Public Counsel agreed with this treatment of affiliated fuel supply transactions.

We further find that FPC has satisfied its burden regarding its fuel procurement practices and resultant expenses. As indicated in Order No. 21847, we determined that not all expenses incurred by EFC on behalf of FPC were prudent and ordered that a refund be made to FPC's ratepayers. We find, therefore, that Public Counsel's request that the we reconsider our finding regarding Public Counsel's proposed conclusion of law should be denied.

We further find that we properly rejected the following proposed conclusion of law:

> 11. Pursuant to Appendix A, Paragraph II.T. of Order No. 12645, FPC has the full burden of proof to demonstrate that its transactions with EFC have been in the best interest of the ratepayer. FPC has not met its burden of proof in this docket on the issues placed in contention.

Public Counsel suggests that we improperly rejected this conclusion of law since FPC failed to establish by a preponderance of the evidence that its cost-plus contracts with EFC were in the best interests of its ratepayers. The record indicates that the costs incurred by FPC consisted of EFC's actual costs to supply fuel to FPC plus overhead and a profit component. In order to evaluate the reasonableness of these charges as well as the prudency of incurring those costs, we find that it was inappropriate to consider the evidence presented by EFC. In addition, to the extent the costs charged to FPC and recovered from its ratepayers resulted from imprudent actions, we find that the monies associated with these actions should be returned to FPC's ratepayers.

EFC was given the responsibility by FPC for the procurement of its fuel supply. This decision was made prior to the adoption of the Commission's Fuel Procurement Policy in Order No. 12645. Both FPC and EFC offered witnesses in this proceeding and we find that it is appropriate for us to hear

from any witness who has relevant material evidence to present regarding the issues in controversy. We find that the evidence presented was evaluated by the appropriate standard and that FPC, to the extent it was required, met its burden of proof. We find, therefore, that Public Counsel's request for reconsideration of our decision to reject Public Counsel's proposed conclusion of law should be denied.

We further find that we properly rejected the following proposed conclusions of law:

12. FPC's failure to comply with the Commission's Fuel Procurement Policy has resulted in excessive fuel and fuel-related charges from EFC being borne by FPC's ratepayers.

13. FPC's delegation of its coal procurement responsibilities to EFC and its affiliates resulted in excess risk and fuel cost to FPC's ratepayers.

The Commission's Fuel Procurement Policy was adopted in Order No. 12645 which was issued November 3, 1983. In general, most of the transactions at issue in this proceeding occurred prior to the adoption of the Commission's Fuel Procurement Policy and we find it appropriate that we acknowledged that fact. In addition, we would point out that Order No. 12645 clearly states that compliance with the central guidelines is not a prerequisite to recovery of fuel expenses. The underlying theme of the Commission's Fuel Procurement Policy is to allow the utility's management to run the utility and to review the decisions and resulting expenses based upon whether the decisions were reasonable in light of the information available at the time of the decision. Where a determination is made that a decision was imprudent, then the costs associated with that decision should be disallowed.

We further find that FPC's decision to delegate its coal procurement responsibilities is consistent with the broad guidelines established in Order No. 12645. However, we do not believe FPC's ratepayers are exposed to excess risk and fuel cost because we, with the statutory responsibility to protect the ratepayers, exercise the same level of scrutiny regarding these affiliated transactions as we would exercise over any

other utility transactions. As Public Counsel correctly states, we have determined that the decision to add the fourth tow/barge prior to 1987 was imprudent. FPC's decision regarding that barge was made during the 1981-82 time frame clearly before the implementation of the Fuel Procurement Policy. We find, therefore, that it is inappropriate to suggest that because certain imprudent decisions were made prior to the adoption of our Fuel Procurement Policy that FPC's failure to comply with that policy resulted in excessive fuel and fuel-related charges being borne by FPC's ratepayers as a matter of law. We find that we should deny Public Counsel's request that we reconsider our decision to reject Public Counsel's proposed conclusions of law.

It should be noted that we determined that it would not be appropriate to make a finding of this issue at the August 3, 1989 Special Agenda Conference, opting instead to make a determination of excess risk and/or excess fuel costs on a case by case basis. (Order No. 21847, pg. 19)

In consideration of the foregoing, it is

ORDERED that the motion for reconsideration filed by the Office of Public Counsel on September 22, 1989 is hereby denied as discussed in the body of this order.

ORDERED that this docket be closed after the time has run in which to file a petition for reconsideration or notice of appeal if such action is not taken.

By ORDER of the Florida Public Service Commission, this 10th day of JANUARY, 1990.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

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by: Kay Flynn
Chief, Bureau of Records

NOTICE OF JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.