BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Investigation into earnings for 1994, 1995 and 1996 of St. Joe Natural Gas Company, Inc.	DOCKET NO. 960930-GU ORDER NO. PSC-96-1188-FOF-GU ISSUED: SEPTEMBER 23, 1996

The following Commissioners participated in the disposition of this matter:

SUSAN F. CLARK, Chairman
J. TERRY DEASON
JOE GARCIA
JULIA L. JOHNSON
DIANE K. KIESLING

NOTICE OF PROPOSED AGENCY ACTION
ORDER REGARDING DISPOSITION OF OVEREARNINGS

BY THE COMMISSION:

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

CASE BACKGROUND

St. Joe Natural Gas Company, Inc. (St. Joe or the Company) is a local gas distributor that serves approximately 3,090 residential, commercial, and industrial customers in Port St. Joe, Mexico Beach, and the unincorporated areas of Gulf County. St. Joe has one very large industrial customer, Stone Container Company (formerly St. Joe Paper Company), that takes approximately 66 percent of St. Joe's volume equating to a 75 percent contribution to revenues. St. Joe's residential and commercial rates are significantly lower than those charged by any other local distribution company in Florida.

As a result of the Commission's ongoing earnings surveillance program, we were made aware of the high level of St. Joe's earnings, based on the June 30, 1994 report. Accordingly, our Staff and the Company worked to resolve the matter concerning any potential overearnings. St. Joe agreed to a 12.00% ROE earnings deferred and commingled with 1995 earnings before the Commission determines the appropriate disposition of any excess earnings. By Order No. PSC-95-0017-FOF-GU dated January 5, 1995, we approved a 12.00% ROE earnings cap for St. Joe for 1994 and 1995. In addition, we ordered that the overearnings for 1994 and 1995 be commingled before determination of disposition by the Commission.

After meetings between the Company and Staff to find a resolution of this matter, St. Joe hand-delivered its proposal for disposition of the overearnings for 1994 and 1995 on August 8, 1996.

DECISION

RATE BASE

To make an appropriate determination as to the disposition of overearnings it is necessary to first determine precisely the amount of those overearnings. The process begins with determining the appropriate rate base. After a review of the books of St. Joe, the following adjustments were made.

Cash:

The Company made an adjustment to its cash balance in working capital to add $107,452 in 1994 and $101,132 in 1995. The unadjusted amounts on the books tie to the bank statements. St. Joe assumed incorrectly that the interest expense on debt is "non-utility," and incorrectly added back amounts to cash that consisted primarily of interest expense that was paid. The Company's adjustments need to be reversed to reflect the correct treatment of cash that was used to pay interest. Therefore, we approve a reduction in cash by $107,452 for 1994 and by $101,132 for 1995.

Accrued Interest:

The Company made adjustments to remove $5,394 in accrued interest in 1994 and $5,285 in 1995. Commission practice is to include accrued interest in working capital. Therefore, we approve a reduction in working capital by $5,394 in 1994 and $5,285 in 1995.

Accrued Taxes:

The Company made adjustments to increase its regulated accrued taxes by $44,606 and $39,141 for 1994 and 1995, respectively. These adjustments were based on its incorrect assumption that the interest expense on debt is "non-utility." As discussed below, we decreased income tax expense by $66,046 for 1994 and by $63,038 for 1995, to reflect the correct treatment of the interest and the reconciliation adjustment and to reflect other adjustments to revenues and expenses. To indicate the accrued tax effect of the foregoing, we have increased accrued taxes by $33,023 for 1994 and by $31,519 for 1995. These rate base/working capital increases represent the simple average of our decreases for income tax.

In summary, we find that the rate base shall be reduced by $79,823 for 1994 and by $74,898 for 1995. Attachments 1 and 3 show the rate bases and adjustments for 1994 and 1995, respectively. Based on the foregoing adjustments, we find the appropriate rate base is $3,988,277 for 1994 and $4,149,535 for 1995.

COST OF CAPITAL

To measure overearnings it is also necessary to determine the overall rates of return for 1994 and 1995 and to make appropriate adjustments to particular accounts.

Deferred Credit:

St. Joe Forest Products Company (SJFP) guarantees a note for St. Joe. SJFP also agreed to purchase a minimum of $91,947 of gas each month. SJFP makes the monthly note payments of $39,396, which offset payments for gas. The terms of the note state that if the cost of gas used by SJFP falls below the required note payment, the amount by which the note payment exceeds the cost of gas will be applied to prepaid gas and will be offset by future gas purchases after the final note payment. Interest on this prepaid gas accrues annually at the prime rate.

St. Joe recorded the balance of prepaid gas as a deferred credit and included it in common equity. We believe that the deferred credit is similar to long-term debt because interest is paid on it and the terms of the agreement indicate it is debt. Therefore, the deferred credit shall be removed from common equity and included as a separate line item in the capital structure for 1994 and 1995. The interest rate attributable to the deferred credit shall be calculated by dividing accrued interest by the average balance of the deferred credit.

Non-utility working capital:

St. Joe removed an amount for non-utility working capital specifically from equity in reconciling capital structure and rate base. Our practice is to remove non-utility investment specifically from equity in reconciling capital structure and rate base because non-utility investment, such as investment in a non-regulated subsidiary, typically would be more risky than an investment in the utility. However, this is not so with non-utility working capital. Therefore, we find it appropriate to reverse the Company's equity adjustment for 1994 and 1995 working capital and spread the capital structure adjustment pro rata over all sources of capital except accumulated deferred income taxes, which are specifically identified.

Capital Structure:

St. Joe's average capital structures for 1994 and 1995 are reported in its earnings surveillance reports. In 1995, the Company made an adjustment to remove $52,569 of unrecovered gas cost from working capital. However, the Company neglected to remove this amount from its capital structure, which resulted in its capital structure not reconciling to its rate base. To correct this error, we find it appropriate to make a pro rata adjustment of $52,569 over all sources of capital except accumulated deferred income taxes.

Return on Equity:

By Order No. PSC-95-0017-FOF-GU, dated January 5, 1995, the Commission ordered an earnings cap of 12.0% ROE for St. Joe for 1994 and 1995. An adjustment was made to reflect this order.

With these adjustments, the overall rates of return for 1994 and 1995 for measuring overearnings are 10.77% and 10.63%, respectively. Attachments 2 and 4 show the capital structures for 1994 and 1995, respectively.

NET OPERATING INCOME

Similarly, to determine the appropriate amount of Net Operating Income for 1994 and 1995, we find it necessary to make certain adjustments to specific accounts.

Director Fees:

The Company expensed $28,800 for director fees in 1994 and 1995, or $7,200 each for its four directors. One of the four directors, the company President, is also paid a salary.

In Order No. PSC-95-0964-FOF-GU, issued August 8, 1995, we denied West Florida Natural Gas the allowance of directors' fees for those directors who are already compensated through the payment of salaries. Therefore, we find it appropriate to reduce expenses by $7,200 for 1994 and 1995 to adjust for the employee twice compensated.

Rent Revenues:

St. Joe's non-utility operation paid St. Joe $2,520 in 1994 and 1995 for rent, in lieu of allocating office space. The rental income was recorded below-the-line. All plant, including the corresponding non-utility plant, is recorded above-the-line. For this reason, we find that the revenue from the rent should be recorded above-the-line. Therefore, revenue shall be increased by $2,520 in 1994 and 1995.

Interest on Cash:

The Company earns interest on its cash account, which is recorded below-the-line. When an interest-bearing account is included in working capital, the Commission has either ordered the interest recorded above-the-line or has removed the cash from working capital and left the interest below-the-line. In Order No. PSC-95-0518-FOF-GU, we directed Florida Public Utilities Gas Division to record above-the-line the interest earned on cash included in rate base. Therefore, we find it appropriate for St. Joe to record above-the-line the interest earned on cash included in rate base and that revenue be increased by $7,854 in 1994 and by $5,189 in 1995.

House Piping Expense:

St. Joe recorded $20,974 and $22,661 in below-the-line expenses for 1994 and 1995 respectively for house piping and venting. The Commission has allowed other companies, City Gas and West Florida Natural Gas, to record this type of expense above-the-line for recovery in base rates or through the conservation cost recovery mechanism. Therefore, we find it is appropriate to accord St. Joe comparable treatment for these costs and recommend increasing operating expenses by $20,974 and $22,661 for 1994 and 1995, respectively.

Income Taxes:

In calculating its income tax expense, the Company neglected to include interest expense in its calculation. The "reconciled to rate base" interest is $172,114 for 1994 and $159,768 for 1995. The result of including the interest is a decrease to income taxes of $64,767 for 1994 and $60,121 for 1995. Further, other adjustments we made to NOI decrease NOI by $3,400 and $7,752 and decrease income tax expense by $1,279 and $2,917, for 1994 and 1995 respectively. Accordingly we find it appropriate to decrease tax expense for 1994 by $66,046 and to decrease tax expense for 1995 by $63,038.

In summary, we find it appropriate to increase St. Joe's achieved NOI by $62,646 for 1994 and by $55,286 for 1995. Attachments 1 and 3 show the NOI with adjustments for 1994 and 1995, respectively. Based on the adjustments discussed above, the appropriate net operating income is $541,908 for 1994 and $488,761 for 1995.

OVEREARNINGS

After making the appropriate adjustments shown above, we find that the Company's overearnings for 1994 and 1995 are $183,339 and $77,979, respectively, for a total of $261,318. The amount of overearnings has been accepted by the Company. The calculation of the overearnings for 1994 and 1995 are shown on Attachments 1 and 3, respectively.

The Company submitted its proposal to dispose of the above stated overearnings and potential overearnings for 1996. The proposal is attached hereto as Attachment 5. In summary, the Company proposes:

1. To amortize, off the books, over a 25-year period beginning January 1, 1997, $261,318 in excess earnings for 1994 and 1995;

2. If the Company files with the Commission, a petition to increase its rates, that has the effect of increasing revenues, then the Company agrees to refund over a 60-month period commencing with the new rate change, the remaining unamortized balance of excess earnings to be established at the conclusion of the rate proceeding, without interest;

3. The refund procedures will not apply where the Company petitions to restructure its rates such that the resulting rate changes have no effect on the Company's total revenues;

4. In the event the Company's earnings for the calendar year 1996 are determined by the Commission to be in excess of maximum authorized levels, the excess earnings will be administered in accordance with the procedures established for the 1994 and 1995 overearnings.

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We believe that St. Joe's circumstances are unique and that there is no ideal solution for this Company given its distinctive situation. Upon review of the Company's proposal, we find it is the best alternative for disposition of overearnings for 1994, 1995 and 1996, if any, for the reasons that follow.

1. St. Joe's situation is unique in that it has the lowest rates in the State of Florida for residential natural gas customers and its largest customers have negotiated contracts.

2. The Company has cash flow problems in view of its construction program.

3. In its proposal, the Company agrees to a cap on its 1996 earnings.

4. The proposal provides for a potential refund.

5. If overearnings were recorded as CIAC, rate base would be reduced thereby exacerbating overearnings.

6. The proposal provides an incentive not to file for a rate increase, thereby minimizing rate case costs being borne by its existing customers.

7. Even if St. Joe does succeed in justifying increased rates, the Company's proposal lessens the impact of a rate increase for a five-year period.

8. The proposal will not hinder the completion of the main line extension to the City of Wewahitchka and the Gulf Correctional Institute, outside of Wewahitchka.

Therefore, we approve the Company's proposal for its treatment of its 1994, 1995 and 1996 overearnings.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that St. Joe Natural Gas Company, Inc.'s proposal for disposition of its overearnings for the years 1994, 1995 and 1996 if any, are approved as discussed in the body of this order. It is further

ORDERED that accounti[illegible]justments be made as discussed herein. It is further

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

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

By ORDER of the Florida Public Service Commission, this 23rd day of September, 1996.

Blanca S. Bayó

BLANCA S. BAYÓ, Director
Division of Records and Reporting

(S E A L)

SLE

DISSENT

Commissioner Deason dissents.

NOTICE OF FURTHER PROCEEDINGS OR 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.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on October 14, 1996.

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

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

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

ATTACHMENT 1

ST. JOE NATURAL GAS COMPANY
DOCKET NO. 960930-GU

ATTACHMENT 1
11-Sep-96

CALCULATION OF 1994 EXCESS REVENUE

Adj. No.			
	NET OPERATING INCOME PER ESR		$479,262
	Staff Adjustments:		
8	Director Fees	$7,200	
9	Rent Revenues	2,520	
10	Interest on Cash	7,854	
11	House Piping Expense	(20,974)	
12	Income Taxes	66,046	
	Total Adjustments		62,646
	Adjusted NOI		$541,908
	RATE BASE PER ESR		$4,068,100
	Staff Adjustments:		
1	Nonreg Cash	($107,452)	
2	Accrued Interest	(5,394)	
3	Accrued Taxes	33,023	
	Total Adjustments		(79,823)
	Adjusted Rate Base		$3,988,277
	ROR @ 12.00% ROE		x 10.77%
	Maximum allowed NOI		429,704
	Achieved NOI		541,908
	Excess NOI		112,204
	NOI Multiplier		x 1.6340
	1994 Excess Revenue		183,339
	Interest		0
	TOTAL 1994 EXCESS REVENUE		$183,339

ATTACHMENT 2
11-Sep-96

ST. JOE NATURAL GAS COMPANY
DOCKET NO. 960930-GU

1994 CAPITAL STRUCTURE

		ADJUSTMENTS							
	PER BOOKS	COMPANY SPECIFIC	STAFF SPECIFIC	TOTAL BEFORE PRO RATA	PRO RATA	STAFF ADJUSTED	RATIO (%)	COST RATE (%)	WEIGHTED COST (%)
LONG TERM DEBT	1,727,451			1,727,451	(20,679)	1,706,772	42.79%	9.85%	4.22%
SHORT TERM DEBT				0	0	0	0.00%	10.00%	0.00%
DEFERRED CREDIT			42,330	42,330	(507)	41,823	1.05%	4.27%	0.04%
CUSTOMER DEPOSITS	27,974			27,974	(335)	27,639	0.69%	8.00%	0.06%
COMMON EQUITY	2,214,919	32,294	(74,624)	2,172,589	(26,008)	2,146,581	53.82%	12.00%	6.46%
DEFERRED INCOME TAXES	65,462			65,462		65,462	1.64%		0.00%
TAX CREDITS-ZERO COST				0		0	0.00%		0.00%
TAX CREDITS-WEIGHTED COST				0		0	0.00%		0.00%
TOTAL	4,035,806	32,294	(32,294)	4,035,806	(47,529)	3,988,277	100.00%		10.77%

ATTACHMENT 2

ST. JOE NATURAL GAS COMPANY
DOCKET NO. 960930-GU

ATTACHMENT 3
11-Sep-96

CALCULATION OF 1995 EXCESS REVENUE

Adj. No.			
	NET OPERATING INCOME PER ESR		$433,475
	Staff Adjustments:		
8	Director Fees	$7,200	
9	Rent Revenues	2,520	
10	Interest on Cash	5,189	
11	House Piping Expense	(22,661)	
12	Income Taxes	63,038	
	Total Adjustments		55,286
	Adjusted NOI		$488,761
	RATE BASE PER ESR		$4,224,433
	Staff Adjustments:		
1	Nonreg Cash	($101,132)	
2	Accrued Interest	(5,285)	
3	Accrued Taxes	31,519	
	Total Adjustments		(74,898)
	Adjusted Rate Base		$4,149,535
	ROR @ 12.00% ROE		x 10.63%
	Maximum allowed NOI		441,037
	Achieved NOI		488,761
	Excess NOI		47,724
	NOI Multiplier		x 1.6340
	1995 Excess Revenue		77,979
	Interest		0
	TOTAL 1995 EXCESS REVENUE		$77,979

ST. JOE NATURAL GAS COMPANY
DOCKET NO. 960930-GU

ATTACHMENT 4
11-Sep-96

1995 CAPITAL STRUCTURE

	PER BOOKS	ADJUSTMENTS COMPANY SPECIFIC	ADJUSTMENTS STAFF SPECIFIC	TOTAL BEFORE PRO RATA	PRO RATA	STAFF ADJUSTED	RATIO (%)	COST RATE (%)	WEIGHTED COST (%)
LONG TERM DEBT	1,412,820			1,412,820	(32,353)	1,380,467	33.27%	9.85%	3.28%
SHORT TERM DEBT	115,385			115,385	(2,642)	112,743	2.72%	10.00%	0.27%
DEFERRED CREDIT			174,762	174,762	(4,002)	170,760	4.12%	6.06%	0.25%
CUSTOMER DEPOSITS	27,755			27,755	(636)	27,119	0.65%	8.00%	0.05%
COMMON EQUITY	2,573,608	32,902	(207,664)	2,398,846	(54,933)	2,343,913	56.49%	12.00%	6.78%
DEFERRED INCOME TAXES	114,533			114,533		114,533	2.76%		0.00%
TAX CREDITS-ZERO COST				0		0	0.00%		0.00%
TAX CREDITS-WEIGHTED COST				0		0	0.00%		0.00%
TOTAL	4,244,101	32,902	(32,902)	4,244,101	(94,566)	4,149,535	100.00%		10.63%

Law Offices
HOLLAND & KNIGHT

A Partnership Including Professional Corporations

315 South Calhoun Street
Suite 600
P.O. Drawer 810 (ZIP 32302-0810)
Tallahassee, Florida 32301
904-224-7000
FAX 904-224-8832

Atlanta, Fort Lauderdale, Jacksonville, Lakeland, Miami, Orlando, St. Petersburg, Tampa, Washington, D.C., West Palm Beach

August 8, 1996

VIA HAND DELIVERY

Mr. Timothy J. Devlin, Director
Division of Auditing & Financial Analysis
Florida Public Service Commission
2540 Shumard Oak Boulevard
Gerald L. Gunter Building, Room 215J
Tallahassee, Florida 32399-0850

Re: Inquiry into the Level of Earnings of St. Joe Natural Gas Company, Inc.

Dear Mr. Devlin:

Based on our discussions earlier today, this letter modifies and supersedes our letter to you of August 7, 1996. As part of its earnings surveillance program, Commission staff has identified potential excess earnings relative to our client, St. Joe Natural Gas Company, Inc. (the "Company"), for the calendar years 1994 and 1995. This earnings review merits special analysis given the Company's unique operating and rate characteristics. As you are aware, the geographic location of the Company severely limits its expansion opportunities, yet the Company has been able to maintain the lowest residential gas rates in the state. In recognition of these unique characteristics and in order to expeditiously resolve this matter without resort to litigation, the Company proposes the following:

1. The Company agrees for purposes of settlement that there are $261,318.00 in excess earnings for the calendar years 1994 and 1995 ("Excess Earnings").

2. Excess Earnings identified in Paragraphs 1 and 4 shall be maintained off the books and amortized (i.e., reduced in equal monthly increments) over a 25 year period beginning January 1, 1997 (the "Amortization Period"). In the event the Company files with the Commission a petition to increase its rates that has the effect of increasing revenues ("Aggregate Rate Increase Proceeding"), the Company agrees to refund over a 60 month period, commencing with the new rate change, the remaining

Net Refund, if any, shall be without interest and established at the conclusion of the Aggregate Rate Increase Proceeding.

3. The Net Refund procedures will not apply where the Company petitions to restructure its rates such that the resulting rate changes have no effect on the Company's total revenues.

4. In the event that the Company's earnings for the calendar year 1996 are determined by the Commission to be in excess of maximum authorized levels, the Company will administer those excess earnings in accordance with the Net Refund procedures set forth herein.

5. This settlement proposal is contingent upon Commission approval without modification. If this proposal is not approved in its entirety by the Commission it shall be null, void and of no further binding effect.

6. Commission approval of this proposal will close out the Commission's review of the Company's earnings for the calendar years 1994 and 1995, and all prior periods. Calendar year 1996 remains subject to audit, review and adjustment.

The Company respectfully requests that the Staff prepare a recommendation to the Commission for approval of the foregoing proposal at the earliest practicable time. Please contact the undersigned should you have any questions.

Sincerely,

HOLLAND & KNIGHT

D. Bruce May

DBM/sms
cc: Public Counsel
Mr. Stuart Shoaf