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MEMORANDUM

FEBRUARY 24, 1998

TO: DIVISION OF RECORDS AND REPORTING

FROM: DIVISION OF LEGAL SERVICES (C. KEATING) RVE WCK

RE: DOCKET NO. 971310-GU - INVESTIGATION INTO 1996 EARNINGS OF PEOPLES GAS SYSTEM, INC.

98-0329-FOF-GU

Attached is a NOTICE OF PROPOSED AGENCY ACTION ORDER DETERMINING AND DISPOSING OF EXCESS EARNINGS, with attachments, to be issued in the above referenced docket. (Number of pages in Order - 16)

WCK/js
Attachment
cc: Division of Electric and Gas (Makin)
Division of Auditing and Financial Analysis (L. Romig, C. Romig, Draper, Lester)
I:971310or.wck

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into 1996 earnings of Peoples Gas System, Inc.	DOCKET NO. 971310-GU ORDER NO. PSC-98-0329-FOF-GU ISSUED: February 24, 1998

The following Commissioners participated in the disposition of this matter:

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

NOTICE OF PROPOSED AGENCY ACTION
ORDER DETERMINING AND DISPOSING
OF EXCESS EARNINGS

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.

By letter dated July 11, 1996, Peoples Gas System, Inc., ("Peoples Gas" or "Company") stated that any revenues contributing to a return on equity in excess of 12.25% for the calendar year 1996 would be held subject to this Commission's jurisdiction and disposition. The Company stated that it anticipated its earnings would remain within the authorized range for the remainder of the 1996 calendar year. In the event that its earnings were above the authorized range, the Company urged us to defer the excess earnings to a later period. According to Peoples Gas, the deferral would provide a longer period of stable rates benefitting its customers. However, the Company's earnings prediction proved inaccurate; its December 31, 1996 Earnings Surveillance Report (ESR) showed approximately $600,000 of excess revenues based on its 12.25% ROE ceiling.

Rate Base

In its December 1996 ESR, the Company reported a total "FPSC Adjusted" rate base of $253,138,000. Based on the following adjustments, however, we find that the Company's appropriate rate base for 1996 is $249,983,000. Our adjustments and calculations appear on Attachment A to this Order.

First, by Order No. 16313, issued July 8, 1986, in Docket No. 850811-GU, we authorized Peoples Gas to amortize $1.2 million in estimated and projected environmental clean-up costs associated with its manufactured gas production plants over a five year period. The effective date of the new base rates was July 18, 1986. The Company began its amortization in October 1986, which coincided with the first month of its fiscal year. We find, however, that the Company should have begun the amortization in August 1986, the first full month in which the new rates were in effect, in order to have a proper matching of revenues and expenses. Accordingly, we find that Deferred Environmental Costs should be reduced $40,000, and working capital should similarly be reduced $40,000.

By Order No. 23858, issued December 11, 1990, in Docket No. 891353-GU, we authorized the Company to increase its amortization of environmental clean-up costs from $240,000 to $1,248,000 annually, effective November 1, 1990. In the Company's last rate case (Docket No. 911150-GU), our auditors determined that the Company made an error in calculating the amortization for the fiscal year ended September 1991 by using the wrong monthly amortization amount for 11 months of the historical test year. We find that the Company, as a result of this error, understated 1991 expenses and overstated 1996 deferred costs by $220,000.

To correct the errors cited above, we find that Peoples Gas should record additional amortization of $260,000 for years prior to 1996. In addition, the Company should reduce 1996 working capital by $260,000.

Second, the Company made adjustments to remove conservation and fuel overrecoveries from working capital, thereby increasing working capital by $1,935,000 and $960,000, respectively. Peoples contends that its accounting for these overrecoveries is consistent with the method used in its last rate case and that no adjustment should be made to its accounting. Upon review of the Company's last rate case, it appears that we inadvertently failed to make a similar adjustment for overearnings. This Commission's long standing practice, however, has been to include recovery clause overrecoveries as reductions to working capital.

In Order No. 13537, Docket No. 830465-EI, we reaffirmed our practice in this area by stating:

> In Order No. 9273, Docket No. 74680-CI, we determined that interest should be applied to over/under recoveries in order to counter any incentive to bias projections in either direction. If the ratepayer has to provide the interest on both over/under recoveries, the Company will have no incentive to make its projections as accurate as possible.
>
> In FPL's last rate case and in subsequent rate cases involving other electric utilities, we have consistently determined that adjustment clause over recoveries should be included as a reduction to working capital.

In Order No. PSC-93-0165-FOF-EI, Docket No. 920324-EI, we stated:

> By stipulation, [Tampa Electric Company] has agreed that the Commission's policy of including net over recoveries in working capital and excluding net under recoveries is the appropriate treatment. Net under recoveries, which are assets, are excluded from working capital, and net over recoveries, which are liabilities, are included. We accept and approve the stipulation. In its filing, the Company incorrectly removed both over recoveries and under recoveries.

Further, in Order No. PSC-94-0452-FOF-GU, Docket No. 930091-GU, the Commission stated:

> This would result in the ratepayers providing the interest that [West Florida Natural Gas Company] would return to them. By the same token, unrecovered costs should be excluded from working capital. To include those costs would allow the Company to earn a return on the under recovery plus recover the interest through the recovery clause.

Most recently, in Order No. PSC-97-0136-FOF-GU, Docket No. 970023-GU, involving Chesapeake Utilities Corporation, the Commission stated:

> It has been our policy that these over recoveries should be treated as cost-free liabilities which are used to reduce a utility's working capital allowance. See Docket No. 830012-A (Tampa Electric Company) and Docket No. 960502-GU (City Gas Company). If over recoveries are not recognized in Working Capital, Rate Base is increased and the utility earns a return on the over recovery. In other words, the ratepayer provides the interest on the over recovery. By including over recoveries as a reduction to Working Capital, a Company will have an incentive to make its projections for the cost recovery clause as accurate as possible and avoid large over recoveries.

As we stated in the above orders, the rationale for including overrecoveries as a reduction to working capital is (1) to provide an incentive to utilities to make their projections as accurate as possible, and (2) to protect the ratepayer from paying interest on the overrecovery.

Ratepayers pay interest to the Company on underrecoveries and the Company pays interest to ratepayers on overrecoveries at the commercial paper rate. If an overrecovery is not included in working capital, then the ratepayer is paid the commercial paper rate by the Company, but, at the same time, the Company is allowed to earn the overall rate of return on the increased rate base. This gives the Company a bonus instead of a penalty when cost overrecoveries occur because the overall cost of capital is higher than the commercial paper rate; Peoples' overall rate of return for 1996 was 9.27%, while the average commercial paper rate for 1996 was 5.70%.

If we allow the Company to remove these overrecoveries from working capital, it would earn approximately $432,000 on a higher rate base and pay the customer $165,000 at the commercial paper rate. If we do not allow the Company to remove these overrecoveries from working capital, however, its rate base is reduced and the Company must pay interest to the ratepayer at the commercial paper rate. Only in the latter case is there a penalty to the Company. Thus, we find that Peoples Gas should reduce working capital by $1,935,000 and $960,000 to include conservation and fuel overrecoveries, respectively. Further, we find that future surveillance reports should include fuel overrecoveries in working capital but, for the sole purpose of providing flexibility in reporting, need not include conservation overrecoveries in working capital unless and until we order otherwise. By this finding, we do not change our current policy of requiring conservation overrecoveries to be included in working capital for purposes of determining earnings.

Weighted Average Cost of Capital

Rate base is the utility's investment in plant and working capital and is primarily derived from the assets side of the balance sheet. Total capital represents the sources of capital for the Company and is primarily derived from the liabilities and common equity side of the balance sheet. In reconciling capital structure and rate base, the Company is showing its investment in rate base and how it financed that investment.

Utilities file ESRs with the capital structure reconciled to rate base. Typically, sources of funds cannot be traced to uses of funds. Funds are fungible, i.e., interchangeable. Therefore, we usually reconcile differences between capital structure and rate base with pro rata adjustments over total capital. However, under certain circumstances it is appropriate to make specific adjustments to capital structure components. In these cases, specific adjustments are necessary to more accurately reflect the true cost of providing service. After all specific adjustments have been made, any additional adjustment necessary to reconcile capital structure and rate base will be made on a pro rata basis. From the reconciled capital structure, the overall rate of return is calculated and applied to rate base to calculate the allowed net operating income.

In its December 1996 ESR Summary, Peoples Gas reconciled capital structure and rate base with specific and pro rata adjustments. The pro rata adjustments were made over all sources of capital. Unusually, these pro rata adjustments were positive, meaning the beginning balance of total capital was increased to match rate base. This occurred because the Company prorated an intercompany payable, amounting to $7,724,000, over all sources of capital. This adjustment is consistent with the treatment we allowed in Order No. 23858, issued December 11, 1990, in Docket No. 891353-GU (an earlier Peoples Gas rate case). For the Company's last rate case, capital structure and rate base were reconciled with pro rata adjustments over investor sources of capital and customer deposits.

As discussed in Order No. 23858, the intercompany payable is an interest-bearing account and is the sum of all transactions that occur between Peoples Gas and any of its non-utility affiliates. The Company did not include this amount as a liability in the calculation of working capital, thus increasing working capital. The Company reconciled this amount to the capital structure as a pro rata increase to all sources of capital.

The rationale for the treatment allowed in Order No. 23858 was that the Company used the intercompany payable to balance the balance sheet for the projected test year, and the pro rata increase in capital was analogous to the pro rata decrease in capital that results when temporary cash investments are removed from working capital. Further, because the intercompany payable was a balancing amount, we believed at that time that the payable might not actually exist during the projected test year.

The Company believes the pro rata treatment of the intercompany payable should continue. In a letter, the Company asserted that this Commission has historically removed from rate base all intercompany accounts, whether payables or receivables. Further, the Company asserted that in every rate case in the Company's history, this adjustment has been made on a pro rata basis over all sources of capital. Finally, the Company noted that specifically identifying the intercompany payable as a source of capital is completely inconsistent with the treatment prescribed in Peoples Gas' last rate case or any previous case.

We believe it is important to distinguish between an earnings review and a rate case. Although each company must file ESRs consistent with Commission adjustments in its last rate case, further adjustments are necessary to accurately measure earnings. For example, a company's last rate case is usually based on a projected test year, but the subsequent surveillance reports are always historical. Also, a rate case may contain amortization of an item that is appropriately expensed entirely during the historical surveillance period.

We find that the intercompany payable should be included in Peoples Gas' capital structure as short-term debt for the following reasons. First, during 1996, the intercompany payable existed as an interest-bearing amount; this is a historical fact. Unlike the rate case in Docket No. 891353-GU, the intercompany payable is not a balancing entry for projection purposes. Second, the intercompany payable is tied to a specific interest expense. By including the intercompany payable as short-term debt in the capital structure, we will allow the Company to recover its appropriate interest expense. If the intercompany payable is prorated over all sources of capital, it will earn the overall rate of return, which is higher than its interest rate. Finally, as stated above, the payable was interest bearing. In this respect, it is like any other debt instrument in the Company's capital structure; the intercompany payable supplied funds to the Company that otherwise would be supplied by investors. Therefore, we find that Peoples' Gas should include the intercompany payable as short-term debt in its capital structure.

To reflect our finding, above, concerning the adjustment to expense environmental costs, we find it appropriate to reduce common equity and deferred taxes by $754,000 and $455,000, respectively. By Order No. PSC-93-1773-FOF-GU, issued December 10, 1993, in Docket No. 931101-GU, we set the Company's return on equity at 11.25%, with a range of plus or minus 100 basis points. Using the top of that range, 12.25%, for measuring excess earnings, we find that the appropriate weighted average cost of capital for Peoples Gas, for the period ending December 31, 1996, is 9.27%. Our calculations appear on Attachment B to this Order.

Net Operating Income

In its December 1996 ESR, the Company reported a "FPSC Adjusted" net operating income (NOI) of $24,051,000. Based on the following adjustments, however, we find that the Company's appropriate net operating income for 1996 is $23,752,098. Our adjustments and calculations appear on Attachment A to this Order.

First, in May 1996, the Company accrued $250,000 to expenses for a study being performed by IBM. According to the Company, the actual cost of the study was $188,600. In March 1997, the Company credited expenses $61,400 to reflect the actual cost. Therefore, we find that Peoples Gas should reduce 1996 expenses by $61,400.

Second, we find that the Company should reduce 1996 expenses to exclude $4,000 in directors' fees paid in 1996 to directors who were also employees of the Company. By Order No. PSC-95-0964-FOF-

GU, issued August 8, 1995, and Order No. PSC-96-1188-FOF-GU, issued September 23, 1996, we denied West Florida Natural Gas and St. Joe Natural Gas, respectively, the allowance of directors' fees for those directors who were already compensated through the payment of salaries. We found it appropriate to reduce expenses for director fees in each of those overearnings dockets. We note that similar adjustments were not made in prior rate cases or other earnings dockets for these companies.

The Company believes that no adjustment should be made based on the disclosure because (1) the expenses are paid to the employees in recognition of the services performed as directors in addition to their regular duties and (2) no adjustment was made for these expenses in the Company's last rate case.

We believe it is appropriate to distinguish between an earnings review and a rate case. Although the companies must file ESRs consistent with Commission adjustments made in their last rate case, further adjustments may be appropriate to accurately measure earnings and reflect current Commission policy. For example, a Company's last rate case is usually based on a projected test year, but the earnings reports are based on historical data. Accordingly, we find that the Company's 1996 expenses should be reduced by $4,000.

Third, we find that the Company's 1996 expenses should be reduced by $24,807 to exclude charitable contributions of $18, 767 and Chamber of Commerce dues of $6,040. During our audit of Peoples Gas' 1996 ESR, a sample of the transactions recorded in the managers' working funds was reviewed for the proper treatment of employee activities or civic/social club dues. The above expenses for charitable contributions and Chamber of Commere dues were noted. Since similar adjustments were made in the Company's last rate case, we find it appropriate to reduce expenses by the above amounts.

Fourth, based on our review of the tax returns and property tax assessments paid by the Company, we find that Taxes Other Than Income is understated by $11,784. This amount is based on two adjustments. First, property taxes should be increased by $8,893 to the amount that was paid in 1996. This amount is net of maximum discounts available. Second, Regulatory Assessment Fees should be increased by $2,891 for a credit adjustment relating to November 1995 taxes that was not booked until January 1996. Because the adjustment was not booked until 1996, the Regulatory Assessment

Fees reflected in the general ledger and in the ESR were understated for the calendar year 1996.

Fifth, subsequent to the filing of Peoples Gas' ESR, it was determined that the Company, through its interest reconciliation adjustment, had eliminated consideration in its ESR of the recovery of $264,000 of interest it had paid in 1996 for tax deficiencies of prior years. Following a series of discussions with the Company, the Company requested that this amount be "reclassified" as an above-the-line O&M expense. Subsequent to its request, the Company provided our staff with the following information about the deficiencies: copies of the check requests prepared by the Company, with supporting documentation for the tax and interest; several cost/benefit analyses demonstrating that the ratepayers received more benefit than the $264,000 of interest paid out; and the Internal Revenue Code and Treasury Regulation Sections (Internal Revenue Code Section 450 and Treasury Regulations Section 1-451-5) that the Company relied on when it took its position on Customer Advances that eventually led to the majority of the $264,000 interest on the deficiencies.

The interest Peoples Gas paid in 1996 for tax deficiencies was a result of an Internal Revenue Service (IRS) audit of tax years 1988 through 1990. The final settlement of the audit resulted in a net deficiency of tax. The interest was computed on the tax deficiency from the due date of the original tax returns to the date the final settlement was reached and paid. No interest was accrued in anticipation of the outcome of the audit. Therefore, the earliest any part of the interest or the tax liability could have been recorded on the books was in January 1996, when the final settlement was reached and the Company prepared a check request for payment to the IRS.

Peoples Gas states that:

> The final settlement with the Appeals Division of the IRS included some adjustments of taxable income arising in these years and some adjustments that carried over from previous examinations. The carryover items were primarily depreciation related and resulted in additional deductions in these years. The amount of these net adjustments was an increase to taxable income of $888,144.

The primary issue that was raised in these years related to the timing of income recognition. This item accounted for $783,092 of the $888,144 increase to taxable income. PGS was recognizing advances in advances in aid of construction as taxable income after the end of the second year following the year of receipt if the advance had not been refunded by then. The company believed there was authority for this position in the tax code. The IRS argues that the contribution should be included in taxable income when received, and in the context of an overall settlement that is how the issue was decided.

By virtue of the company taking this position, its customers had the benefit of higher deferred tax balances from the time the tax returns were filed until the deficiency was paid in 1996.

According to the Company, the net deficiency of $888,144 is comprised as follows:

Year	Tax Settlement Deficiencies/("Overpayments")	Deferred Taxes
1988	$ 285,000	$ 107,245
1990	$ 761,000	$ 286,365
	$1,046,000	$ 393,610
1989	(159,000)	
	$ 887,000 (a)	

(a) Rounded from $888,144.

We have reviewed the information provided by Peoples Gas, paying particular attention to the Company's cost/benefit analyses. The Company's analyses show customer benefits ranging from $203,335 to $297,149. However, without further research and study, we could not support the Company's methods that include inflation factors and/or opportunity cost. Nevertheless, we performed our own simple, conservative cost/benefit analysis. We used the final capital structure schedule from the Company's last rate case, as memorialized in Order No. PSC-92-0924-FOF-GU, as a basis for analysis and estimated the interest paid per year.

According to the Company, the deferred tax balance in the capital structure from Order No. PSC-92-0924-FOF-GU was $394,000 higher because of the Company's position on Customer Advances and other issues. The NOI requirement from Order No. PSC-92-0924-FOF-GU is $21,539,695. In our analysis, we reduced the deferred tax balance by the $394,000, thereby reflecting that the Company had paid the income taxes on the Customers Advances and other issues, and spread this amount proportionately to equity and long-term debt. The resulting NOI requirement was $21,583,695, or $44,184 more than that reflected in Order No. PSC-92-0924-FOF-GU. Grossing up the $44,184 by the revenue tax factor approved in Order No. PSC-92-0924-FOF-GU resulted in a revenue requirement that is $71,229 greater than the revenue requirement that was approved in that Order. For comparative purposes and to reflect four years of interest, we allocated the $264,000 interest between pre-1992 years and the four-year period it was examining. Therefore, for simplicity, we used a simple average of the amount of interest paid per year times the number of years under examination. The result is $176,000 of interest paid for the four years ($264,000/6 years x 4 years). Assuming that this savings was realized from 1992 through 1996, our staff calculated the savings to the ratepayers to be $108,916 (($71,229*4)-$176,000).

We believe that this method of analyzing the benefits is an appropriate, conservative approach. The use of this method results in savings to Peoples' customers. Accordingly, we believe that above-the-line O&M treatment is appropriate.

We note that above-the-line treatment for Peoples Gas is based solely upon the merits of our cost/benefit results; above-the-line treatment of interest on subsequent tax deficiencies will not be assumed to be appropriate. The appropriate accounting and recovery should be decided on a case by case basis, following a careful examination of the unique circumstances of each underlying position taken by the Company that gave rise to the interest.

Sixth, we find that the tax effect of our adjustments to net operating income results in a reduction to income taxes of $71,586.

Seventh, the Company made an adjustment of $43,000 to reduce income taxes. The Company intended this $43,000 adjustment to adjust the interest included in the Company's calculation of the per books income tax expense to that interest that is inherent in the Company's adjusted capital structure, i.e., the capital structure that has been reconciled to its rate base. However, upon review and based on our inclusion of the intercompany payable in capital structure, we believe that the Company's interest reconciliation adjustment as filed is incorrect. Based on its ESR, the Company included interest of $9,763,000 in its per books tax expense. Then, in its calculation of the interest reconciliation adjustment, it reduced the per books interest expense by the interest on the intercompany payable ($466,000) and the amortization of the debt issuance costs ($87,000), or by $553,000 in total. Adding back the $553,000 in interest, including the intercompany payable in capital structure and reflecting our other adjustments to the Company's ESR, results in a calculated interest reconciliation adjustment of $141,911, increasing income tax expense. Consequently, the adjustment that is required to reflect our interest reconciliation adjustment and reverse the Company's interest reconciliation adjustment is $184,911 ($141,911 + $43,000).

Overearnings

Based on our findings above, we find that the Company's 1996 overearnings are $973,572. This amount is comprised of $947,236 in overearnings plus interest of $26,336. The $26,336 in interest was calculated for the year ended December 1996. Our calculation of these amounts appears on Attachment A to this Order.

Disposition of Overearnings

By Order No. PSC-92-0924-FOF-GU, we authorized Peoples Gas to amortize $1,248,000 in environmental costs annually based on a 5-year amortization period beginning November 1, 1990. We then opened Docket No. 931101-GU to investigate the appropriate equity return for Peoples Gas. By Order No. PSC-93-1773-FOF-GU, issued December 10, 1993, we reduced the Company's ROE from 12.00% to 11.25%, plus or minus 100 basis points, beginning January 1, 1994. In that same Order, we ordered Peoples Gas to fully amortize $2,496,000 in environmental clean-up costs by September 30, 1994.

Since that time, the Company has incurred approximately $2.5 million in environmental costs. For the year ended December 31, 1996, the Company incurred $1,629,373 in such costs. As of December 31, 1996, and December 31, 1997, the Company had deferred balances of $2,081,725 and $1,315,494, respectively. The decrease between 1996 and 1997 was a result of the Company receiving approximately $935,000 in insurance proceeds. The current balance should be further reduced $260,000 to reflect our finding, above, concerning the Company's deferred environmental costs.

According to the Company, environmental clean-up projects are expected to continue for several more years. Currently, at least eight sites have been determined to fall under regulatory oversight for possible clean-up of hazardous materials. No estimate of future clean-up costs has been provided.

In prior cases, we have disposed of overearnings by crediting the overearnings to the accumulated clean-up costs. Most recently, we ordered such a disposition in Order No. PSC-97-0136-FOF-GU, issued in Docket No. 970023-GU, involving Chesapeake Utilities. We find it appropriate to apply the $973,572 in overearnings determined in this Order to the accumulated clean-up costs effective December 31, 1996, for earnings surveillance purposes as a reduction to working capital.

Accounting for Environmental Costs

The Company has been deferring all environmental costs since September 30, 1994, instead of expensing them. According to Peoples Gas, its position since that time, supporting deferral accounting, is that environmental costs are outside the Company's control in both magnitude and timing and are so unpredictable and erratic from year to year that deferral accounting is the only appropriate accounting method with which to account for them. Peoples Gas also believes that its accounting for these costs is correct and consistent with the method used in its last rate case.

We find that the Company should be expensing these costs because it was allowed $1,248,000 in expenses in its last rate case and does not have our specific authority to defer these costs. A review of prior orders addressing Peoples Gas' environmental costs shows that the Commission has not authorized Peoples Gas to utilize deferral accounting on an ongoing basis.

We believe that the environmental costs constitute a regulatory asset as stated in the Uniform System of Accounts (USoA). Regulatory assets result from rate actions of regulatory agencies. Regulatory assets arise from specific revenues, expenses, gains, or losses that would have been included in net income determinations in one period under the general requirements of the USoA but for it being probable that such items will be included in different period(s) for developing the rates the utility is authorized to charge for its utility services.

Generally, for a utility to capitalize or defer costs that would otherwise be expensed under Generally Accepted Accounting Principles (GAAP), a specific finding by this Commission is required.

As stated above, the balance for deferred environmental costs as of December 1997 was $1,315,494. After adjusting this balance by $260,000, in accordance with our findings in this Order, and crediting the Company's overearnings of $973,572, the remaining balance is $81,922. We find that the Company should expense this amount in 1997 and continue expensing environmental costs as incurred, until it receives this Commission's authorization to account for these costs differently. Further, if the Company desires to defer these costs, it should request reserve accounting treatment or other treatment of future environmental costs and request a reasonable monthly accrual.

In summary, we find that Peoples Gas should expense $260,000 as a prior period correction and credit its 1996 overearnings of $973,572 to the deferred environmental account effective December 31, 1996, for earnings surveillance purposes. In addition, we find that the remaining balance of $81,922 should be expensed in 1997.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that Peoples Gas System, Inc.'s 1996 overearnings are appropriately calculated, as shown in the body of this Order, to total $973,572 and shall be credited to the Company's Deferred Environmental Costs account effective December 31, 1996, for regulatory purposes. It is further

ORDERED that Peoples Gas System, Inc., shall expense all environmental costs as they are incurred until it receives this Commission's approval to use any other accounting treatment for these costs. It is further

ORDERED that each and all of the specific findings herein are approved in every respect. 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 24th day of February, 1998.

Blanca S. Bayó

BLANCA S. BAYÓ, Director
Division of Records and Reporting

(S E A L)

WCK

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

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

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

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on March 17, 1998.

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

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

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

PEOPLES GAS SYSTEM, INC
Docket No. 971310-GU

Schedule 1
15-Jan-98

CALCULATION OF 1996 EXCESS REVENUE

	NET OPERATING INCOME PER ESR		$24,051,000
Adj. No	Staff Adjustments:		
3	Overaccrual - IBM studies	61,400	
4	Director Fees	4,000	
5	Charitable Contributions	18,767	
5	Chamber of Commerce	6,040	
6	Taxes Other - Understated	(11,784)	
7	Interest on Tax Deficiencies	(264,000)	
8	Income Taxes	71,586	
9	Interest Reconciliation	(184,911)	
	Total Adjustments		(298,902)
	Adjusted NOI		$23,752,098

	RATE BASE PER ESR		$253,138,000
	Staff Adjustments:		
1	Unamortized Environmental Costs - Correct Errors	(260,000)	
2	Conservation Overrecovery	(1,935,000)	
2	Gas Overrecovery	(960,000)	
	Total Adjustments		(3,155 000)
	Adjusted Rate Base		$249,983 000

ROR @ 12.25% ROE	x	9 27%
Maximum allowed NOI		23,173 424
Achieved NOI		23 752 098
NOI in excess of authorized ROE		5[illegible]8 674
NOI Multiplier	x	1 6369
Revenue in excess of 12.25% ROE		$947,236
Interest 1/1/96 - 12/31/96		26 336
TOTAL EXCESS REVENUE		$973,572

PEOPLES GAS SYSTEM
DOCKET NO 971310-GU

Schedule 2
19-Jan-98

1998 CAPITAL STRUCTURE

	PER BOOKS	COMPANY ADJUSTMENTS SPECIFIC	COMPANY ADJUSTMENTS PRORATA	TOTAL COMPANY	STAFF ADJUSTMENTS REVERSE COMPANY PRO RATA	STAFF ADJUSTMENTS SPECIFIC	STAFF ADJUSTMENTS TOTAL PRIOR TO PRO RATA ADJUSTS	STAFF ADJUSTMENTS PRO RATA	STAFF ADJUSTMENTS ADJUSTED	RATIO (%)	COST RATE (%)	WEIGHTED COST (%)
LONG TERM DEBT	82 336 000	(829 000)	3 502 000	84 811 000	(3 502 000)	0	81 409 000	64 656	81 344 344	32 54%	6 97%	2 [illegible]
SHORT TERM DEBT	0	0	0	0	0	7 724 000	7 724,000	6 134	7 717 866	3 09%	6 00%	0 1[illegible]%
COMMERCIAL DEPOSITS	19,012,000	0	867 000	20 700,000	(867 000)	0	19,012 000	15,814	19 996 186	7 60%	7 00%	0 50%
RESIDENTIAL DEPOSITS	4,010,000	0	172,000	4 182,000	(172,000)	0	4 010 000	3,185	4 006 815	1 60%	6.00%	0 10%
INACTIVE DEPOSITS	36,000	0	2,000	37,000	(2,000)	0	36 000	0	36,000	0 01%	0.00%	0 00%
COMMON EQUITY	118,336,000	(5,840,000)	4,830,000	117 326,000	(4,830 000)	(150 706)	112,327,206	89,211	112,238,084	44 90%	12.29%	5 50%
DEFERRED INCOME TAXES	21 958,000	0	946,000	22,003 000	(946,000)	(100,206)	21,857 706	0	21,857,706	8 74%	0.00%	0 00%
TAX CREDITS-ZERO COST	0	2,887,000	124 000	3,011 000	(124,000)	0	2,887,000	0	2,887,000	1 15%	0.00%	0 00%
TAX CREDITS-WEIGHTED COST	0	0	0	0	0	0	0	0	0	0 00%	0 00%	0 00%
TOTAL	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]		[illegible]