State of Florida

Public Service Commission

CAPITAL CIRCLE OFFICE CENTER • 2540 SHUMARD OAK BOULEVARD
TALLAHASSEE, FLORIDA 32399-0850

-M-E-M-O-R-A-N-D-U-M-

DATE: November 17, 2009

TO: Office of Commission Clerk (Cole)

FROM: Division of Economic Regulation (Chase, Devlin, Kummer, Slemkewicz)
Division of Regulatory Analysis (Ballinger, S. Brown, Ellis)
Office of the General Counsel (Young, M. Brown)

RE: Docket No. 090368-EI – Review of the continuing need and costs associated with Tampa Electric Company's five Combustion Turbines and Big Bend Rail Facility.

AGENDA: 12/01/09 – Regular Agenda – Tariff Filing - Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Klement

CRITICAL DATES: 12/12/09 (60-Day Suspension Date)

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\090368.RCM.DOC

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Case Background

On October 12, 2009, Tampa Electric Company (TECO or Company) filed a Petition for a step increase in rates pursuant to Order No. PSC-09-0283-FOF-EI (Final Order), issued April 30, 2009, and confirmed on reconsideration in Order No. 09-0571-FOF-EI (Order on Reconsideration), issued August 21, 2009.[1]

The Final Order granted TECO an increase in rates and charges with a step increase in rates to generate a maximum of $33.5 million of additional revenue effective January 1, 2010. This amount was increased to $34,077,079 by the Order on Reconsideration to reflect an

[1] Docket No. 080317-EI, In re: Petition for rate increase by Tampa Electric Company.

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adjustment of the weighted average cost of capital. The step increase is designed to address the additional costs incurred by TECO to construct five combustion turbines (CTs) during 2009 and a new rail unloading facility at Big Bend Station (Rail Facility) to be placed in service toward the end of 2009.

The Final Order contained certain conditions TECO must meet to recover the deferred cost for the five CTs, including that these investments are completed and in commercial operation by December 31, 2009, and that the units must be needed for load generation. The Final Order specifically states:

> The decision to complete any or all of these projects by year end, considering changed circumstances such as, but not limited to, decreased electricity consumption, shall be subject to our staff's review and approval. There is testimony in the record that TECO may not stay on schedule with the CTs because of the downturn in the economy. TECO shall only move forward with the units if the capacity is needed. This condition will help ensure that TECO will only move forward with its plans for the CTs if it is justified in terms of load requirements.

Final Order, p. 6.

With regard to the rail facility, the Final Order conditioned the recovery of the step increase on completion of the project by December 31, 2009. Final Order, p. 9.

The Intervenors in the rate case jointly filed a Motion for Reconsideration contesting the Commission's decision to grant the step increase. The Order on Reconsideration confirmed the step increase and provided "that a new docket will be opened to evaluate whether there continues to be a load generation need for the CTs, including whether there has been a change in circumstances to warrant the Company not completing the CTs, and to verify and evaluate the reasonableness of the cost associated with these projects." The Order on Reconsideration also clarified that the Final Order did not grant staff the authority to approve the step increase. The Order on Reconsideration provided that "(b)efore TECO recovers the costs for the CTs through base rates, our staff will prepare a recommendation for our consideration. Staff's recommendation will be limited to whether the conditions established in the Final Order have been met." Order on Reconsideration, p. 12

On September 14, 2009, the Intervenors in Docket No. 080317-EI (TECO's rate case proceeding) filed with the Florida Supreme Court a Joint Notice of Administrative Appeal of the Final Order and the Order on Reconsideration, appealing the decision of the Commission to grant the step increase.

The purpose of this memorandum is to present the results of staff's review of the TECO petition in this docket and staff's recommendation on the implementation of the step increase authorized by the Final Order and confirmed by the Order on Reconsideration. The Commission has jurisdiction pursuant to Sections 366.05 and 366.06, Florida Statutes (F.S.)

Discussion of Issues

Issue 1: What action should the Commission take with respect to the step increase designed to recover the costs of the five combustion turbine units (CTs) and the rail facilities for unloading coal at Big Bend Station (Rail Facilities)?

Recommendation: For the reasons discussed below, this matter should be set directly for hearing on the Commission's own motion. However, TECO should be authorized to implement a revised step rate increase of $26,735,801 on January 1, 2010, subject to refund with interest, during the pendency of the proceeding.

Staff Analysis: As noted in the background, TECO filed a Petition on October 12, 2009, for approval of rate schedules that implement a step increase to recover costs for its five 60 megawatts (MW) aero-derivative CTs scheduled to go in service in 2009 and the rail facilities for unloading coal at Big Bend Station. The total amount of the step increase authorized in the rate case Final Order was $33,561,370. This amount was adjusted in the Order on Reconsideration to $34,077,079 for a change in the weighted average cost of capital. The step increase includes a maximum increase of $26,938,806 for the five CTs and $7,138,274 for the Rail Facility.

The Final Order and the Order on Reconsideration established conditions that must be met before the step increase could be implemented. Those conditions include:

(1) The Rail Facility is completed and in commercial operation by December 31, 2009;

(2) The five CTs are actually in service during 2009; and

(2) The five CTs continue to be needed for load generation.

Staff discusses the status of each condition separately, below:

Condition 1: The Rail Facility is completed and in commercial operation by December 31, 2009:

In its Petition, TECO states that the Rail Facility is substantially complete and is on schedule to begin receiving coal deliveries by December 1, 2009. A staff engineer from the Commission's Tampa District Office conducted an on site inspection of the Rail Facility on October 23, 2009. He found that nearly all of the railroad track's inside perimeter has been completed and that much of the work remaining involves service road crossings. He also observed the conveyor belt system and found that most of it is completed. Some of the remaining sections are being assembled on the ground and will be lifted into place. Thus, it appears that the Rail Facility will be completed by December 31, 2009.

While there is no reason to believe the Rail Facility will not be completed as scheduled, it is not in service as of the writing of this recommendation, and may not be in service at the time of the Commission vote. For this reason, and in order to verify the actual cost of the project, staff recommends that this item be included in the topics to be covered in the hearing we are recommending be held in this docket. In the interim, staff recommends that the step increase of

$7,138,274 for the Rail Facility be approved on a temporary basis, subject to refund, pending the outcome of the hearing. In this way, the Company is allowed to collect its authorized rates during the pendency of the hearing, and the customers are protected in case the step increase is ultimately denied or reduced.

Condition 2: The five CTs are actually in service during 2009:

Along with its Petition, TECO provided documentation that each of the five CTs has been placed in commercial operation on the dates indicated below:

Unit	In Service Date
Bayside CT 5	April 27, 2009
Bayside CT 6	April 20, 2009
Bayside CT 3	July 13, 2009
Bayside CT 4	July 13, 2009
Big Bend CT 4	August 26, 2009

Staff verified the in-service dates of all five CTs by reviewing the Commercial Operation Memorandum for each CT attached to the Petition, as well as TECO's responses to staff's data requests in this docket and the May, July and August A-Schedules filed by TECO with the Commission in the Fuel Docket. In addition, field staff from the Tampa District Office conducted a site visit and verified that all five CTs are fully completed and appear to be functional. Therefore, staff concludes that TECO met the condition of the Final order that all five CTs are actually in service during 2009.

Condition 3: The five CTs continue to be needed for load generation:

The Final Order also required that the five CTs continue to be needed for load generation. In the Final Order, the Commission recognized the need for the five CTs but also noted that Company witness Black testified that not all of the five CTs may be needed in 2009. The Final Order provides that the decision to complete any or all of these projects by year end, considering changed circumstances such as, but not limited to, decreased electricity consumption, shall be subject to staff's review and Commission approval. Final Order, p. 5-6, and Order on Reconsideration, p. 12.

In the Petition filed in this docket, TECO states that when the decision to approve construction of these five units was made, each unit was required in order to meet the Company's 20 percent reserve margin obligation in 2009. TECO acknowledges that it has experienced lower than expected sales and, as a result, with the addition of the CTs, the Company's reserve margin exceeds the minimum 20 percent criteria. The Company asserts that because of the advanced state of construction when evidence of reduced demand and energy became a reality, the Company had no cost-effective option to cease construction of any of the CT units in 2009. According to TECO's petition, by January 15, 2009, over 70 percent of the funds for all contracts involving the five CT projects were irrevocably committed and would have represented sunk costs providing no benefits if construction had been stopped. TECO claims that because construction of Bayside CTs 5 and 6 was in the final stages during the rate case hearings and complete when the Commission issued the Final Order on April 30, 2009, these units were never candidates for postponement. With regard to the other three CTs, TECO maintains that postponement was not a cost-effective option since the majority of funds for contracts were committed and substantial construction had been completed at the time of the rate case hearings.

Additionally, in its Petition, TECO maintains that these units have produced significant amounts of energy in 2009 which benefited its customers while providing additional reliability. According to TECO's Petition, all of the new CTs provide black start[2] and quick start[3] capability, which significantly enhances the operational flexibility and reliability of the system, and provides a more economical option to meet the Company's operating reserve obligation than through the use of spinning reserves. In addition, TECO asserts that the quick start capability of the five CTs will provide fuel savings over the life of the assets. The 2009 fuel savings resulting from the operation of the five CTs were factored into TECO's most recent fuel adjustment mid-course correction that reduced the fuel adjustment factor effective May 8, 2009. The lower fuel cost resulting from the CTs is also reflected in TECO's 2010 fuel factors. TECO states that the five CTs will produce an estimated 2009 and 2010 fuel savings of $4.0 million through the displacement of less efficient units or more expensive power purchases.

Staff from the Division of Regulatory Analysis (RAD) reviewed the Petition and other data submitted by TECO in order to analyze the continuing need for the five CTs. As part of discovery, staff asked for information of monthly reserve margins under TECO's 2007 through 2009 Ten Year Site Plans. In its analysis, staff did multiple calculations based on TECO's response in which one or more of the CTs were removed from the planned installed capacity. This analysis also looked at the effect on the reserve margins of scheduled maintenance of other plants. Staff's analysis indicates that if one or more of the new CTs were not on line, the reserve margin would fall below 20 percent in several months during 2010 taking into account scheduled maintenance of other plants. However, staff notes that since scheduled maintenance is not something that occurs regularly, it could be possible that other options may exist to maintain reliability, such as short-term Purchase Power Agreements (PPA) to cover the temporary shortage. Staff also notes there are several months in which the reserve margin is well over the 20 percent reserve margin criteria. RAD staff prepared a memorandum describing its analysis, which has been filed in this docket file. In its memorandum, RAD staff concluded that there is a need for the five CTs based on the immediate fuel cost savings and the long term system reliability benefits.

Staff believes questions remain regarding whether all of the five CTs were needed for load generation as required by the Final order in the rate case and confirmed by the Order on Reconsideration. TECO acknowledges that its reserve margin exceeds the minimum 20 percent

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[2] Black start capability is the ability to start the unit independent of an energized connection to the bulk electric system, such as in a blackout condition. This capability allows for faster restoration of electric service to customers following hurricanes or other major system disturbances.
[3] Quick start capability enables these units to go from off-line to full load within 10 minutes.

criteria with the addition of the five CTs. This was confirmed by the analysis conducted by RAD staff. However, the addition of the five CTs does offer additional system flexibility and enhanced long-term reliability as well as fuel savings. Staff recommends that this matter be set directly for hearing to examine whether the new CTs are needed to satisfy the load requirements on the TECO system, and if not, if they provide other benefits which justify their inclusion in rates.

Staff Audit:

On July 15, 2009, the staff initiated an audit to, among other things, verify the capital costs for the five CTs and provide a comparison to amounts used in the Commission's rate case order. The audit was completed on August 31, 2009. Audit Finding No. 4 indicates that total cost to date for the five CTs is about \$50 million less than what was projected in the rate case. Even though the CTs are now in commercial operation, there will probably be some additional charges that have yet to be accounted for. The Rail Facility is not complete and TECO expects the final costs to be about \$13 million in excess of what was originally projected and used in the rate case. TECO expects the final costs for the Rail Facility to be \$60 million whereas the original projection was \$46.9 million. Staff believes that this information regarding the updated capital costs for the CTs should be considered in determining the level of the step increase. Accordingly, staff recommends that the step increase be reduced from \$34,077,080 to \$26,735,801, a reduction of \$8,334,871. (See Schedule 1)

Conclusion:

Staff recommends that this matter be set directly for hearing in order to determine whether TECO has satisfied the three conditions for the step increase set forth in the rate case Final Order and confirmed in the Order on Reconsideration. Staff believes it is unlikely that a PAA order would not be protested, regardless of the outcome of the Commission's decision. Therefore, in the interest of administrative efficiency, this matter should be set directly for hearing. In the hearing, the Commission can determine whether the Rail Facility was completed and in commercial operation by December 31, 2009, as required by the Final Order. Further, the Commission can explore the benefits of the five new CTs, determine whether there is a continuing need for each of the units, and ascertain the actual costs of the CTs and the Rail Facility. A hearing would also afford the parties to this proceeding an opportunity to conduct their evaluation of the cost of, and need for, the five CTs.

Staff further recommends that TECO be allowed to implement a revised step increase effective January 1, 2010, of \$26,735,801, consistent with the findings in the Staff Audit. This step increase should be approved on a temporary basis, subject to refund, with interest, pending the outcome of the hearing.

Issue 2: Should the Commission approve TECO's proposed tariffs filed with its petition in this docket, reflecting the costs for the five CT unit additions and the new rail facility at the Big Bend Station?

Recommendation: No. The Commission should deny the tariffs as filed. If the Commission approves Issue 1, the Commission should order TECO to file tariffs using the revised revenue requirement discussed in Issue 1, no later than December 11, 2009. The revised tariffs should be effective beginning with bills rendered on or after January 1, 2010, with all additional revenues collected under the new tariffs held subject to refund, pending final disposition of this matter by the Commission. Staff should be given authority to administratively approve the new tariffs as long as they are consistent with the Commission vote. (Kummer)

Staff Analysis: TECO filed revised tariff sheets to adjust base rates to collect the $34,077,079 maximum amount contained in the Order on Reconsideration. Staff is recommending in Issue 1 that that amount be reduced to $26,735,801. This increase represents approximately a 2.8 percent increase on a Company total basis. If the Commission approves staff's recommendation in Issue 1, the Commission should deny the tariffs as filed, and order TECO to refile tariffs consistent with the recommendation in Issue 1. The revised tariffs should be effective for bills rendered on or after January 1, 2010, consistent with the language in Order No. PSC-09-0283-FOF-EI, the Final Order.

Staff is also requesting authority to administratively approve the revised tariffs to be filed on or before December 11, 2009. The Final Order clearly specified that such costs associated with any step increase shall be allocated to rate classes consistent with the approved cost of service methodology, so there is no dispute on how the dollars will be allocated to rate classes. In its petition, TECO proposes a fixed percentage increase in the demand and energy charges for all rate classes to accomplish the increase. Staff agrees that is the appropriate way to adjust rates to reflect any approved increase. The proposed administrative review is to make sure TECO has allocated the appropriate dollars in total, used the factors approved in the rate case, and properly applied the increase to rate classes. These are all mathematical calculations and involve no discretionary decisions by staff.

In addition, staff is recommending that all additional revenues collected under the new tariffs be held subject to refund, with interest, pending final disposition of this matter by the Commission. This protects customers from any discrepancies between any rates implemented in January 2010 and final rates adopted by the Commission in its final decision on the matter.

However, if the Commission wishes to review the revised tariff sheets, staff recommends that the effective date be delayed beyond January 1, 2010. Recommendations for the December 15 Agenda Conference are due December 3, 2009, two days following the Commission's decision based on this recommendation. Staff does not believe there is sufficient time for TECO to file the new sheets and for staff to review them and write a recommendation for the December 15, 2009 Agenda Conference.

Issue 3: Should this docket be closed?

Recommendation: No. This docket should be held open to conduct the hearing recommended by staff. (Young, M. Brown)

Staff Analysis: This docket should be held open to conduct the hearing recommended by staff in Issue 1.

SCHEDULE 1

TAMPA ELECTRIC COMPANY
DOCKET NO. 090368-EI
CALCULATION OF JANUARY 1, 2010 STEP INCREASE
STAFF ADJUSTED FOR REVISED ESTIMATES FOR TOTAL PROJECTED COSTS OF CTs

Step Increase Base Rate Increase

	APPROVED[0]	ADJUSTMENT	**REVISED**
Big Bend Rail Facility	7,138,274	0[1]	**7,138,274**
May 2009 CTs	8,030,533	(496,796)	**8,527,329**
September 2009 CTs	18,908,273	(7,838,075)	**11,070,198**
Total Step Increase	34,077,080	(8,334,871)	**26,735,801**

MAY 2009 CTs (2 Units)

Line No.		Jurisdictional Approved Total Revenue Requirement[2]	Jurisdictional Revised Total Revenue Requirement[3]	Jurisdictional Difference
1	Net Plant in Service	94,758,291	92,068,272	(2,690,019)
2	Rate Of Return*	8.29%	8.29%	8.29%
3	Required Return (2x3)	7,855,462	7,632,460	(223,003)
4	O&M Expenses	636,000	636,000	0
5	Depreciation	4,173,000	4,055,020	(117,980)
6	Taxes Other Than Income	2,226,000	2,159,621	(66,379)
7	Income Taxes (4+5+6)x-.38575	(2,713,751)	(2,642,635)	71,116
8	Income Tax Effect of Interest* [(1) x 3.12% x -.38575]	(1,140,469)	(1,108,093)	32,376
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9	Total NOI Requirement (3+4+5+6+7+8)	11,036,242	10,732,373	(303,869)
10	NOI Multiplier*	1.6349	1.6349	1.6349
11	Revenue Requirement (9x10)	18,043,153	17,546,357	(496,796)

SEPTEMBER 2009 CTs (3 Units)

Line No.		Jurisdictional Approved Total Revenue Requirement[2]	Jurisdictional Revised Total Revenue Requirement[3]	Jurisdictional Difference
1	Net Plant in Service	137,373,373	96,110,153	(41,263,220)
2	Rate Of Return*	8.29%	8.29%	8.29%
3	Required Return (2x3)	11,388,253	7,967,532	(3,420,721)
4	O&M Expenses	987,000	987,000	0
5	Depreciation	6,051,000	4,142,195	(1,908,805)
6	Taxes Other Than Income	3,348,000	2,212,234	(1,135,766)
7	Income Taxes (4+5+6)x-.38575	(4,006,400)	(2,831,956)	1,174,443
8	Income Tax Effect of Interest* [(1) x 3.12% x -.38575]	(1,653,365)	(1,156,739)	496,626
		------	------	------
9	Total NOI Requirement (3+4+5+6+7+8)	16,114,488	11,320,265	(4,794,223)
10	NOI Multiplier*	1.6349	1.6349	1.6349
11	Revenue Requirement (9x10)	26,345,577	18,507,502	(7,838,075)

	Amount	Ratio	Cost Rate	Weighted Cost
Common Equity	1,632,611,907	53.96%	N/A	N/A
Long Term Debt	1,384,998,776	45.78%	6.80%	3.11%
Short Term Debt	7,904,810	0.26%	2.75%	0.01%
Total	3,025,515,493	100.00%		3.12%

NOTES:

[0] Per Reconsideration Order - Order No. PSC-09-0571-FOF-EI in Docket No. 080317-EI

[1] The actual and projected total costs exceed the cap. Therefore, no adjustment is required.

[2] Approved Total Revenue Requirement is based on the combined total annualized costs included in both base rates and the step increase for the CTs. (Order No. PSC-09-0283-FOF-EI and Order No. PSC-09-0571-FOF-EI in Docket No. 080317-EI)

[3] Revised Total Revenue Requirement is based on the revised "Total Projected Costs per Company" included in Audit Finding No. 4 in staff's audit (Audit Control No. 09-197-2-1)