State of Florida

Public Service Commission

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TALLAHASSEE, FLORIDA 32399-0850

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

DATE: March 25, 2004

TO: Director, Division of the Commission Clerk & Administrative Services (Bayó)

FROM: Division of Economic Regulation (Bohrmann, Draper, Matlock, Lingo)
Office of the General Counsel (Brubaker)

RE: Docket No. 031135 – EI: Petition for Approval to Implement Consolidated Fuel Adjustment Surcharge by Florida Public Utilities Company

AGENDA: 04/06/2004 – Regular Agenda – Proposed Agency Action -- Interested Persons May Participate

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\031135EI.RCM.DOC

Case Background

In Docket No. 030438-EI, Florida Public Utilities Company (FPUC or utility) filed a petition for an increase in its rates and charges, and requested that the Commission consolidate the two divisions into a single entity for ratemaking purposes. FPUC provides retail electric service to approximately 27,000 ratepayers in its Northwest division (formerly known as the Marianna division, serving all or parts of Jackson, Calhoun, and Liberty counties) and its Northeast division (formerly known as the Fernandina Beach division, serving part of Nassau county). The Commission approved the parties' stipulation to consolidate FPUC's electric rates at the March 16, 2004, agenda conference.

The petition in Docket No. 030438-EI applied only to base rate charges. On September 26, 2003, FPUC filed a petition to consolidate its factors for the energy conservation recovery clause. The Commission approved this request by Order No. PSC-03-1375-FOF-EG, in Docket No. 030002-EG, issued December 4, 2003. Moreover, by Order No. PSC-03-1461-FOF-EI, in

Docket No. 030001-EI, issued December 22, 2003, the Commission ruled that FPUC should submit a separate petition to address consolidation of FPUC's fuel and purchased power cost recovery factors (fuel adjustment surcharge, fuel rates, or fuel factors) for its two electric divisions, concurrent with revisions to FPUC's base rates at the conclusion of Docket No. 030438-EI. On December 31, 2003, FPUC filed its petition with the Commission to consolidate its fuel rates to be effective concurrent with the consolidated base rates' effective date, which is discussed below.

The Commission has jurisdiction over this subject matter pursuant to the provisions of Chapter 366, Florida Statutes, including Sections 366.04, 366.05, 366.06, Florida Statutes.

Discussion of Issues

Issue 1: Should the Commission approve Florida Public Utilities Company's (FPUC) petition to implement a consolidated fuel adjustment surcharge?

Recommendation: No. The Commission should deny Florida Public Utilities Company's petition to implement a consolidated fuel adjustment surcharge. FPUC's proposal results in significant cost shifting with minimal benefits. Also, FPUC Northeast division's ratepayers oppose FPUC consolidating its rates and charges. (BOHRMANN, LINGO, DRAPER)

Staff Analysis: Although FPUC considers its Northwest (Marianna) and Northeast (Fernandina Beach) divisions as one entity within its corporate structure, the Commission has historically treated each division separately for regulatory purposes. Prior to the parties' stipulation in Docket No. 030438-EI, each division had its own rate base, capital structure, rate structure, and other regulatory elements. In addition, FPUC has historically filed separate monthly and annual fuel schedules for both divisions.

By Order No. PSC-03-1461-FOF-EI, for FPUC's Northwest division, the Commission established a levelized fuel rate at 2.430¢/kwh to recover approximately $11,706,000 in projected 2004 fuel expenses and prior years' under-recovery balance. For FPUC's Northeast division, the Commission established a levelized fuel rate at 1.569¢/kwh to recover approximately $13,835,000 in projected 2004 fuel expenses and prior years' over-recovery balance.

FPUC does not generate any electrical energy for sale to its retail electric ratepayers, but purchases wholesale capacity and associated electrical energy from three wholesale providers: Jacksonville Electric Authority; Jefferson Smurfit Corporation; and Gulf Power Company (wholesale providers). FPUC then re-sells this capacity and energy to its retail ratepayers. FPUC does not transmit any power between the two divisions. In other words, FPUC's contracts with Jacksonville Electric Authority and Jefferson Smurfit Corporation exclusively serve the electricity needs of FPUC's Northeast division's retail ratepayers. Likewise, FPUC's contract with Gulf Power exclusively serves the electricity needs of FPUC's Northwest division's retail ratepayers. The purchased power costs from these wholesale suppliers have historically been significantly different.

FPUC's Reasons for Consolidation

In response to staff discovery in Docket Nos. 030438-EI and 031135-EI, FPUC provides the following rationale for consolidating its fuel rates: minimizing rate shock and minimizing regulatory administrative costs.

FPUC agrees that temporary rate differences exist which benefit one division and creates subsidies for the other division. However, FPUC believes that the long-term impact of consolidated fuel rates should be equal and beneficial to all ratepayers. FPUC attributes the difference in the fuel rates between the two divisions, beyond the impact of the true-up from prior years, to timing issues associated with the negotiations of fuel contracts and fuel purchases between the wholesale providers and their fuel suppliers. Through consolidation, FPUC believes that spreading such timing risks over a larger group of ratepayers would yield a smaller per-ratepayer impact, and prevent rate shock.

FPUC also estimates an annual cost savings of $2,750 due to the reduced workload from making one filing with the Commission, instead of two filings. FPUC also surmises that the parties and staff to Docket No. 040001-EI and subsequent fuel dockets may experience a reduction of 25 to 50 percent in their workload regarding FPUC's filings.

Staff Analysis of FPUC's Reasons for Consolidation

Staff believes that FPUC has made a corporate decision to consolidate its two electric operating divisions as evidenced in Docket No. 030438-EI and Docket No 030002-EG. In those dockets, the Commission approved stipulations regarding the consolidation of base rates and the environmental cost recovery clause because of the similarity in costs incurred by the two divisions. Based on the perceived corporate philosophy of the utility, it would be consistent with the decision in those dockets to grant the utility's petition in this docket. However, staff does not believe the facts are the same in this docket to justify the same consolidation approved in those dockets.

In its analysis of FPUC's petition, staff draws the following conclusions. First, consolidated fuel rates would be unduly discriminatory. Second, any regulatory administrative cost savings would be minimal. Third, FPUC Northeast division's ratepayers oppose such consolidation.

Subsidies, and, therefore, rate discrimination, are inherent in any rate design. Staff determined whether the utility's request to consolidate its fuel costs for its Northwest and Northeast divisions would result in subsidies and rates that are unduly discriminatory. Staff performed a subsidy analysis, shown on Schedule 1, to determine the level of subsidies, if any, that would arise from the approval of the utility's consolidation request. Staff believes that, based on its analysis of subsidies using FPUC-estimated 2004 values, the resulting consolidated rates would be unduly discriminatory.

Through their elected city commission, FPUC's Northeast division ratepayers expressed their opposition to the Commission consolidating FPUC's base rates and charges in Docket No. 030438-EI. The commission of the city of Fernandina Beach, Florida passed a resolution on December 2, 2003, which expressed this opposition. Although the resolution only addresses FPUC's proposal to consolidate its base rates and charges, staff believes this resolution has general applicability regarding consolidation of any component of a Northeast division ratepayer's total bill.

The Commission has consistently encouraged its jurisdictional utilities to minimize its regulatory administrative costs. However, such cost minimization efforts should not create an unreasonable subsidy among ratepayers. Moreover, the cost savings on a per-ratepayer basis are minimal (i.e., approximately 10.2¢ per ratepayer per year). In addition, FPUC's base rates support these costs; therefore, its shareholders would benefit from these cost savings. Finally, both staff and the Office of Public Counsel (OPC) expect that annual cost savings for the

Commission and OPC to be minimal, because consolidating FPUC's fuel rates would not change the amount of data that the Commission and OPC would analyze and audit.

Conclusion

In summary, the Commission should deny FPUC's instant petition, without prejudice, for the following reasons. First, consolidated fuel rates would be unduly discriminatory. Second, any regulatory administrative cost savings would be minimal. Third, FPUC Northeast division's ratepayers oppose such consolidation.

Issue 2: What is the appropriate regulatory treatment for the true-up balances that exist for FPUC's Northeast and Northwest divisions on the day prior to the effective date of a consolidated fuel cost recovery factor?

Recommendation: If the Commission approves staff's recommendation in Issue 1, this issue is moot and no decision is necessary. If the Commission decides in Issue 1 to consolidate the fuel rates for FPUC's two division, FPUC should continue to refund 0.38363¢ per kilowatt-hour (kwh) to its Northeast (Fernandina Beach) division ratepayers and collect 0.11373¢ per kilowatt-hour from its Northwest (Marianna) division ratepayers for the remainder of 2004 as directed by Order No. PSC-03-1461-FOF-EI. In addition, FPUC should refund (collect) any over- (under-) recovery balance accrued from July 2003, through the day prior to the effective date of the consolidated fuel cost recovery factor on an energy basis during calendar year 2005. (BOHRMANN)

Staff Analysis: Based on actual data through June 2003, and re-estimated data for the remainder of 2003, FPUC's Northeast division reported an over-recovery balance of $1,302,700 in its August 12, 2003, filing in Docket No. 030001-EI. In the same filing, FPUC's Northwest division reported an under-recovery balance of $343,777 for 2003. The Commission approved these balances as reasonable by Order No. PSC-03-1461-FOF-EI. By this same Order, the Commission also directed FPUC to refund 0.38363¢ per kwh to its Northeast division ratepayers and collect 0.11373¢ per kwh from its Northwest division ratepayers during 2004 to refund the over-recovery balance for the Northeast division and collect the under-recovery balance for the Northwest division.

In this petition, FPUC initially proposed combining the Northeast division's over-recovery balance with the Northwest division's under-recovery balance for a consolidated over-recovery balance of $958,923. FPUC would refund 0.1494¢ per kwh to all of its electric ratepayers from the effective date of the petition to the last billing cycle for 2004. This proposal would increase the typical Northeast division residential ratepayer's monthly bill (1,000 kwh) by approximately $2.34, and decrease the typical Northwest division residential ratepayer's monthly bill (1,000 kwh) by approximately $2.63. Staff believes this proposal is neither equitable to FPUC's Northeast division's ratepayers nor consistent with Commission policy.

Once FPUC filed actual data for the remainder of 2003 in Docket No. 040001-EI, both the over-recovery balance for the Northeast division and the under-recovery balance for the Northwest division were larger than once expected. FPUC's Northeast division experienced an additional over-recovery of $535,273 compared with the August 12, 2003, filing. Conversely, FPUC's Northwest division experienced an additional under-recovery of $624,352 compared with the August 12, 2003, filing. Until the Commission authorizes FPUC to consolidate its fuel factors for its Northeast and Northwest divisions, these divisions will continue to accumulate their distinct true-up balances. Through February, the Northeast division has accumulated an under-recovery balance of $103,680 for 2004, and the Northwest division has accumulated an additional $60,141 under-recovery.

In the interest of fairness, the Commission should direct FPUC to refund (collect) any over- (under-)recovery balances that accumulate for the separate divisions prior to consolidation of the fuel factors to those ratepayers as if the two division still existed until those balances are completely trued-up. In response to staff discovery in this docket, FPUC expressed a willingness to adopt this concept regarding true-up balances which had accumulated prior to the effective date of the consolidated fuel factors.

In summary, if the Commission approves staff's recommendation in Issue 1, this issue is moot and no decision is necessary. Otherwise, FPUC should refund 0.38363¢ per kwh to its Northeast division ratepayers and collect 0.11373¢ per kwh from its Northwest division ratepayers for the remainder of 2004 as directed by Order No. PSC-03-1461-FOF-EI. In addition, FPUC should refund (collect) any over- (under-) recovery balance accumulated from July 2003, through the day prior to the effective date of the consolidated fuel cost recovery factor on an energy basis during 2005.

Issue 3: If the Commission approves FPUC's petition, in whole or in part, to consolidate its two divisions' fuel cost recovery factors, what should be the effective date of the consolidation?

Recommendation: If the Commission approves staff's recommendation in Issue 1, this issue is moot and no decision is necessary. If the Commission decides in Issue 1 to consolidate the fuel rates for FPUC's two division for costs incurred for wholesale energy purchases on a going-forward basis, the Commission should set the effective date to consolidate FPUC's two divisions' fuel cost recovery factors as the first billing cycle for May 2004 (i.e., April 29, 2004). (BOHRMANN, DRAPER, BRUBAKER)

Staff Analysis: The Commission typically considers two factors when determining the effective date of a change in a utility's fuel rates. First, can the Commission provide sufficient notice to the utility's ratepayers of its decision to allow the ratepayers an opportunity to change their electric consumption patterns? Second, can the Commission set the effective date of the change in the fuel rates at the beginning of the utility's billing cycle to ascertain that all ratepayers pay the same factor for an equal number of billing periods?

FPUC has requested an effective date that coincides with the effective date of consolidated base rates which is scheduled for April 15, 2004. This day is only nine days after the Commission's scheduled agenda conference on this recommendation. Also, this day is in the middle of FPUC's billing cycle for April 2004. Therefore, FPUC would charge some ratepayers the new factor for nine months until the end of 2004, and some ratepayers only eight months.

The Commission has typically not required a 30-day notice period prior to implementing new fuel cost recovery factors after a mid-course correction. See, e.g., Order No. PSC-03-0381-PCO-EI, in Docket No. 030001-EI, issued March 19, 2003. However, the Commission did require a 30-day notice in Order No. PSC-00-1081-PCO-EI, in Docket No. 000001-EI, issued June 5, 2000, which granted FPL's, Florida Power Corporation's, and Tampa Electric Company's petitions for mid-course corrections in 2000. The Commission delayed the implementation of the new factors for approximately two weeks to allow ratepayers the opportunity to adjust their usage in light of the new factors.

The Commission has typically required that a utility implement any change to its fuel factor at the beginning of its monthly billing cycle. A change to a utility's fuel factor at the beginning of its monthly billing cycle will ensure that all ratepayers pay the old and new factors for the same number of months during the year. See, e.g., Order No. PSC-03-0381-PCO-EI, in Docket No. 030001-EI, issued March 19, 2003. However, as stated above, by Order No. PSC-00-1081-PCO-EI, the Commission did authorize a change in Florida Power's, FPL's, and Tampa Electric's fuel factors in the middle of their respective billing cycles to allow their ratepayers 30 days notice to allow their ratepayers an opportunity to change their electric consumption behavior.

Staff believes that an effective date of April 29, 2004, will provide FPUC's ratepayers sufficient notice to change their electric consumption patterns, if necessary. More importantly, this effective date will ensure that all ratepayers pay the consolidated fuel rate for the same number of billing periods in 2004.

FPUC should notify its ratepayers in writing of the Commission approved fuel rates. FPUC should mail the notice to its ratepayers as soon as possible after the Commission's decision. Such information should include: the impact on the typical ratepayer's monthly bill; and the effective date of the consolidated fuel factors. Through communication with FPUC, staff will verify that FPUC provided its ratepayers with adequate and timely notice.

Issue 4: Should this docket be closed?

Recommendation: Yes. If no timely protest is received from a substantially affected person within 21 days of the date of the Proposed Agency Action (PAA) Order, the PAA Order will become final upon the issuance of a Consummating Order. (BRUBAKER)

Staff Analysis: If no timely protest is received from a substantially affected person within 21 days of the date of the Proposed Agency Action (PAA) Order, upon expiration of the protest period, the PAA Order will become final upon the issuance of a Consummating Order.

FLORIDA PUBLIC UTILITIES COMPANY
DOCKET NO. 031135-EI **Schedule 1**
PETITION FOR CONSOLIDATED FUEL ADJUSTMENT **Page 1**

SUBSIDY ANALYSIS: BASED ON FPUC'S ESTIMATES

NORTHWEST DIVISION

Line No.	Description	Total Period (6)
(A)	**Energy Cost + Adj Demand Cost Recovery**	**$0.0394060**
(1)	KWH Sold to Residential Customers	141,466,583
(2)	Number of Residential Customers	9,885
(3) = (1) / [(2)*12]	Average KWH per Bill per Residential Customer	1,193
(4) = (3) * (A)	Average KWH $ per Residential Customer	$47.00

NORTHEAST DIVISION

Line No.	Description	Total Period (6)
(A)	**Energy Cost + Adj Demand Cost Recovery**	**$0.0332693**
(1)	KWH Sold to Residential Customers	202,706,750
(2)	Number of Residential Customers	12,980
(3) = (1) / [(2)*12]	Average KWH per Bill per Residential Customer	1,301
(4) = (3) * (A)	Average KWH $ per Residential Customer	$43.30

CONSOLIDATED

Line No.	Description	Total Period (6)
(A)	**Energy Cost + Adj Demand Cost Recovery**	**$0.0358526**
(5) = NW (A) * NW (3)	Average KWH per Bill per Northwest Residential Cust	$42.76
(5) = NE (A) * NE (3)	Average KWH per Bill per Northeast Residential Cust	$46.66

(6): Energy cost + adj demand cost recovery expressed in $ per KWH.

Docket No. 031135-EI
Date: March 25, 2004

FLORIDA PUBLIC UTILITIES COMPANY
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PETITION FOR CONSOLIDATED FUEL ADJUSTMENT

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SUBSIDY ANALYSIS:
BASED ON FPUC'S ESTIMATES

NORTHWEST DIVISION

Line No.	Description	Total Period (6)	Consolidated Residential Bill	Northwest Pays (Recvs) Resid Subsidy
(A)	**Energy Cost + Adj Demand Cost Recovery**	**$0.0394060**		
(1)	KWH Sold to Residential Customers	141,466,583		
(2)	Number of Residential Customers	9,885		
(3) = (1) / [(2)*12]	Average KWH per Bill per Residential Customer	1,193		
(4) = (3) * (A)	Average KWH $ per Residential Customer	$47.00	$42.76	**($4.24)**

NORTHEAST DIVISION

Line No.		Total Period (6)	Consolidated Residential Bill	Northeast Pays (Recvs) Resid Subsidy
(A)	**Energy Cost + Adj Demand Cost Recovery**	**$0.0332693**		
(1)	KWH Sold to Residential Customers	202,706,750		
(2)	Number of Residential Customers	12,980		
(3) = (1) / [(2)*12]	Average KWH per Bill per Residential Customer	1,301		
(4) = (3) * (A)	Average KWH $ per Residential Customer	$43.30	$46.66	**$3.36**

(6): Energy cost + adj demand cost recovery expressed in $ per KWH.
Source: Florida Public Utilities Company, Docket No. 031335-EI, Petition; Docket No. 030001-EI, Exhibit 21; Docket No. 030438-EI, Schedule E-17 supplemental.

Explanation of Staff's Analysis from Schedule 1

Staff performed a subsidy analysis, shown on Schedule 1, to determine the level of subsidies, if any, that would arise from the approval of the utility's consolidation request. This analysis is based on the sum of the utility's 2004 estimates of energy cost plus the adjusted demand cost recovery, both expressed in terms of dollars per KWH. Page one of Schedule 1 shows the utility's estimated values of its cost per KWH for both the Northwest and Northeast divisions, as well as the utility's estimated consolidated cost per KWH. Figures corresponding to KWH sold, number of customers, average KWH per bill and average KWH dollars per bill are also shown for the residential class in each division. The actual subsidy calculations begin on page two of Schedule 1. As shown on page two, based on the utility's 2004 estimates, if the fuel cost per KWH for the two divisions were consolidated, the Northwest division's residential customers would receive a subsidy of approximately $4.24 per bill, while the Northeast division's residential customers would pay a subsidy of approximately $3.36 per bill.

Furthermore, a review of the historical fuel costs per KWH for the respective divisions indicates that the utility's 2004 estimated fuel costs may be conservative. For example, the five-year average energy charge per KWH component for the Northwest division was $.038 per KWH, while the corresponding five-year average for the Northeast division was $.025, or an average cost differential between divisions of approximately 50%. These historical averages are significantly above the utility's corresponding 2004 estimated differential between divisions of approximately 20%. Therefore, staff believes that the actual subsidies that would result from consolidation would be even greater than the results shown on Schedule 1.