State of Florida

Public Service Commission

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

DATE: October 12, 2006

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

FROM: Division of Economic Regulation (VonFossen)
Office of the General Counsel (Brown)

RE: Docket No. 060583-EI – Petition for approval of new environmental program for cost recovery through Environmental Cost Recovery Clause, by Tampa Electric Company.

AGENDA: 10/24/06 – Proposed Agency Action – Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Deason

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\ECR\WP\060583.RCM.DOC

Case Background

On August 30, 2006, Tampa Electric Company (TECO or the company) filed its petition for approval of a new environmental compliance program, the Clean Air Mercury Rule (CAMR) for cost recovery through the Environmental Cost Recovery Clause (ECRC).

CAMR was promulgated by the Environmental Protection Agency (EPA) on May 18, 2005, and became effective on July 18, 2005. It imposes nation-wide standards for mercury (Hg) emissions from existing and new coal-fired electric utility steam generating units. CAMR will cap and reduce mercury emissions in two phases: the Phase I cap is 38 tons per year with a compliance date of 2010 and the Phase II cap is 15 tons per year with a compliance date of 2018. CAMR also requires that continuous emissions monitoring systems (CEMS) be installed on all

coal fired units by January 1, 2009, one year prior to implementation of the Phase I caps. The Florida Department of Environmental Protection will administer CAMR as delineated in Chapters 62-204, 62-210 and 62-296, Florida Administrative Code. DEP's new rules implementing CAMR were certified on August 17, 2006.

Section 366.8255, Florida Statutes, authorizes the Commission to review and decide whether a utility's environmental compliance costs are recoverable through an environmental cost recovery factor. Section 366.8255(1)(d) provides that:

> 'Environmental compliance costs' includes all costs or expenses incurred by an electric utility in complying with environmental laws or regulations. . . .

Section 366.8255(1)(c) provides that:

> 'Environmental laws or regulations' includes all federal, state, or local statutes, administrative regulations, orders, ordinances, resolutions, or other requirements that apply to electric utilities and are designed to protect the environment.

Section 366.8255(2) provides that:

> An electric utility may submit to the commission a petition describing the utility's proposed environmental compliance activities and projected environmental compliance costs in addition to any Clean Air Act compliance activities and costs shown in a utility's filing under s. 366.825. If approved, the commission shall allow recovery of the utility's prudently incurred environmental compliance costs, including the costs incurred in compliance with the Clean Air Act, and any amendments thereto or any change in the application or enforcement thereof, through an environmental compliance cost-recovery factor that is separate and apart from the utility's base rates. An adjustment for the level of costs currently being recovered through base rates or other rate-adjustment clauses must be included in the filing.

Discussion of Issues

Issue 1: Should the Commission approve Tampa Electric Company's petition for implementing its Clean Air Mercury Rule Phase I compliance program as a new activity for cost recovery through the Environmental Cost Recovery Clause?

Recommendation: Yes, Tampa Electric Company's Clean Air Mercury Rule Phase I emission monitoring compliance program is eligible for cost recovery through the ECRC. The projected and actual costs of the program will be considered in the Commission's ECRC proceedings. (Von Fossen, Brown)

Staff Analysis:

The Company's Petition/Project

Based upon the Clean Air Mercury Rule, Tampa Electric Company must install continuous emission monitoring systems (CEMS) or sorbent trap monitoring systems at its Big Bend Units 1 through 4 and Polk Unit 1 to sample mercury levels in the flue gas by January 1, 2009. These requirements are contained in Rule 62-296.480 (3)(g), Florida Administrative Code which references the Environmental Protection Agency Rule (40 CFR 60, subparts 60.4170 through 60.4176).

Prior to installing CEMS and sorbent trap monitoring systems, TECO will perform baseline testing to measure actual mercury emissions at each affected plant. Baseline testing will allow the Company to measure mercury emissions and gather data to ensure that the new monitoring instruments are designed for the proper monitoring range. Further, Section 40 CFR 75.81(b) provides that units which annually emit less than 464 ounces will be allowed to use periodic instead of continuous monitoring for mercury emissions. TECO anticipates being able to use sorbent trap systems on two units based upon the results of baseline testing.

TECO will begin incurring expenses for baseline testing in late 2006 and incur mercury monitoring costs through 2010. Through this monitoring, TECO can certify to EPA accurate emission levels which will determine if additional compliance activities will be needed to comply with Phase I of CAMR. Based upon discussions with staff, TECO has modified its original cost projections. Within its application, the company had referenced baseline testing costs that would be incurred in 2006, however Exhibit C attached to the petition did not include these costs. TECO has provided its estimated costs for 2006 and also modified years 2009 and 2010 to properly state costs after the January 1, 2009, compliance deadline as operation and maintenance costs instead of capital costs. The costs in the table below are preliminary estimates. Staff will audit actual costs to true-up original projections and to verify the prudence of the individual cost components included for recovery. TECO has stated it will seek cost recovery of the 2006 baseline testing costs in its 2006 true-up filing. Costs for 2007 are included for recovery purposes in TECO's projection filing in Docket No. 060007-EI.

PROJECTED CAMR PHASE I MONITORING COSTS

COMPONENTS	2006	2007	2008	2009	2010	TOTALS
CEMs/Sorbent Trap Systems			$850,000			$850,000
Baseline Testing	$46,000	$100,000	$50,000			$196,000
Monitoring Site		$300,000				$300,000
Monitoring Equipment		$110,000	$280,000			$390,000
Vendor Consultation		$50,000	$50,000	$25,000		$125,000
Total Capital	$46,000	$560,000	$1,230,000	$25,000		$1,861,000
Operation and Maintenance			$75,000	$355,000	305,000	$735,000
Total Estimated Project Cost	$46,000	$560,000	$1,305,000	$380,000	$305,000	$2,596,000

Eligibility For Cost Recovery Through The ECRC

As stated above, Section 366.8255, Florida Statutes, authorizes the Commission to review and decide whether a utility's environmental compliance costs are recoverable through an environmental cost recovery factor. Environmental compliance costs include ". . . all costs or expenses incurred by an electric utility in complying with environmental laws or regulations. . ." Section 366.8255(1)(d), Florida Statutes. Environmental laws or regulations include "all federal, state, or local statutes, administrative regulations, orders, ordinances, resolutions, or other requirements that apply to electric utilities and are designed to protect the environment." Section 366.8255(1)(c), Florida Statutes. Only prudently incurred environmental compliance costs may be recovered through the clause.

In Order No. PSC-94-0044-FOF-EI, issued January 12, 1994, in Docket No. 930613-EI, In Re: Petition to establish an environmental cost recovery clause pursuant to Section 36.8255, Florida Statutes by Gulf Power Company, the Commission identified three criteria for eligibility for cost recovery through the ECRC: 1) the costs must have been incurred after April 13, 1993;

2) the activity is legally required to comply with a governmentally imposed environmental regulation which was enacted, or became effective, or whose effect was triggered after the company's last test year upon which rates are based, and; 3) the costs are not recovered through some other cost recovery mechanism or through base rates.

Staff believes TECO's Phase I compliance program meets the eligibility criteria stated above. As previously stated CAMR requires mercury monitoring systems to be in place by January 1, 2009. These requirements are contained in Rule 62-296.480 (3)(g), Florida Administrative Code, which references the EPA rule (40 CFR 60, subparts 60.4170 through 60.4176). Therefore, TECO is undertaking this project to comply with environmental rules and regulations finalized in August 2006. Thus, costs to comply with this new rule will be incurred after 1993.

TECO's current base rates were established by Order No. PSC-93-0758-FOF-EI, issued May 19, 1993, in Docket No. 920324-EI, In Re: Application for a rate increase by Tampa Electric Company. Since CAMR was promulgated in 2005, costs associated with mercury monitoring are not included in base rates or any other cost recovery clause.

Other cost recovery matters

Staff notes that CAIR and CAMR are established pursuant to the Clean Air Act. Commission policy regarding how to allocate costs to the rate classes due to Clean Air Act compliance activities was established by Order No. PSC-94-0044-FOF-EI, issued January 12, 1994, In that docket, the Commission ordered that costs associated with compliance with the Clean Air Act Amendments of 1990 ("CAAA") be allocated to the rate classes in the ECRC on an energy basis, due to the strong nexus between the level of emissions which the CAAA seeks to reduce and the number of kilowatt-hours generated. In every subsequent order approving recovery of CAAA costs through the ECRC, other than decisions affected by stipulations, the Commission has required that the costs be allocated to the rate classes on an energy basis. Because the costs for which TECO is seeking recovery in this docket are also related to Clean Air Act compliance, staff believes an energy allocation is appropriate.

The depreciation rates used to calculate the depreciation expense for the proposed plant additions should be the rates that are in effect during the period the capital investment is in service.

Conclusion

Staff concludes that TECO must comply with the CAMR monitoring requirements, the costs will be incurred after, 1993 and the monitoring costs are not being recovered through base rates or another cost recovery clause. Therefore, staff recommends that the CAMR Phase I mercury monitoring program is eligible for cost recovery through the ECRC. Additionally, we recommend that TECO's request to recover costs on an energy basis be approved.

Issue 2: Should this docket be closed?

Recommendation: Yes, this docket should be closed upon issuance of a consummating order unless a person whose substantial interests are affected by the Commission's decision files a protest within 21 days of the issuance of the proposed agency action. (Brown)

Staff Analysis: If no timely protest to the proposed agency action is filed within 21 days, this docket should be closed upon issuance of the consummating order.