BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for authority to increase annual storm fund accrual commencing January 1, 1997, to $35 million by Florida Power & Light Company.	DOCKET NO. 971237-EI ORDER NO. PSC-98-0953-FOF-EI ISSUED: July 14, 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 MAINTAINING ANNUAL STORM DAMAGE ACCRUAL AT CURRENT LEVEL
AND REQUIRING STUDIES

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.

I. CASE BACKGROUND

By Order No. 24728, issued July 1, 1991, in Docket No. 910257-EI, the Commission approved Florida Power & Light Company's ("FPL" or "the Company") request to discontinue the annual accrual to its storm damage reserve. FPL asserted, and the Commission found, that given the level of insurance coverage in place for FPL's transmission and distribution (T&D) facilities, the balance in the reserve was sufficient.

In August of 1992, Hurricane Andrew severely damaged FPL's T&D system. While the damage claims related to Hurricane Andrew were paid, FPL's insurers canceled the coverage, effective May 31, 1993.

DOCUMENT NUMBER-DATE
07394 JUL 14 8

On April 19, 1993, FPL filed a petition to implement a self-insurance mechanism for storm damage to its T&D system and to resume and increase the annual contribution to its storm and property insurance reserve fund to $7.1 million. The amount of $7.1 million represented $3 million embedded in rates for the storm fund accrual and an additional $4.1 million for the traditional T&D insurance that was also embedded in rates. The $7.1 million was not based upon a risk study that indicated the appropriate amount that should be accrued to the fund, given the expected exposure. Because of the expiration of FPL's T&D insurance on May 31, 1993, FPL requested consideration of its request on an emergency basis. A hearing on FPL's petition was held on May 17, 1993.

By Order No. PSC-93-0918-FOF-EI, issued June 17, 1993, in Docket No. 930405-EI, we authorized the Company to implement a self-insurance approach or plan for the costs of repairing and restoring its T&D system in the event of hurricane, storm damage or other natural disaster. FPL also was granted the discretion to establish a line of credit for storm damage liquidity. In addition, FPL was required to submit a study detailing what it believed to be the appropriate amount that should be accrued annually to the reserve and what costs it intended to charge to the storm fund. Until the appropriate amount was determined, an annual accrual of $7.1 million, net-of-tax, to the storm fund was set effective June 1, 1993. We denied FPL's request to "pre-approve" a surcharge on customer bills for damages in the event the reserve balance was inadequate. We indicated that in the event of a shortfall in the reserve, FPL could file a petition seeking appropriate action.

FPL filed the required study in October of 1993. FPL's 1993 study suggested that an annual accrual of $20.3 million would allow for storm fund growth, decrease reliance on the customer bill surcharge mechanism and provide an adequate level of insurance. The study also indicated that in order to achieve minimal storm fund growth, a $9 million annual accrual combined with a provision for emergency relief was required.

By Order No. PSC-95-0264-FOF-EI, issued February 27, 1995, in Docket No. 930405-EI, we found the storm damage study to be adequate. Based upon the study, we authorized FPL to increase its annual storm damage accrual to $10.1 million, effective January 1, 1994. The storm fund was to continue to be funded on a net-of-tax basis.

On September 28, 1995, FPL filed a petition to, among other things, increase its annual storm fund accrual to $20.3 million commencing January 1, 1995; and to add approximately $51.3 million of recoveries for damage due to Hurricane Andrew and the March 1993 Storm to the storm reserve and contribute the after tax amount to the storm fund. By letter dated November 14, 1995, the Company expanded its explanation of why it was appropriate to increase the annual accrual at that time. When the $10.1 million annual accrual was approved, FPL stated it had anticipated that the availability of insurance would improve. Instead, the potential for commercial or other insurance was less than before. FPL asserted that since the only cost effective measure available at that time was self-insurance, an increase in the annual accrual was needed to provide an adequate level of insurance to FPL and its customers.

By Order No. PSC-95-1588-FOF-EI, issued December 27, 1995, in Docket No. 951167-EI, we approved FPL's petition to increase the accrual to $20.3 million, funded on a net-of-tax basis. As of December 31, 1997, the balance in the reserve was $251.3 million.

On September 23, 1997, FPL filed a petition seeking authorization to increase its storm fund accrual to $35 million, effective January 1, 1997. This Order addresses FPL's petition.

II. APPROPRIATE ANNUAL STORM DAMAGE ACCRUAL

FPL attached to its petition two reports prepared by EQE International, Inc. (EQE) as support for increasing the accrual. The first is a Hurricane Loss Estimation Study for Transmission and Distribution Assets. This study is a probabilistic analysis of FPL's potential T&D replacement costs due to hurricane events. No nuclear expenses or events were included in this study. The analysis addresses different storm tracks, various storm intensities, storm frequencies, the geographic location of existing T&D facilities, as well as FPL's experiences with storm damages to T&D facilities. EQE concluded that FPL's annual accrual for funding T&D hurricane restoration should be $42.3 million because this figure is representative of FPL's expected annual damage estimate. EQE also indicated that FPL's highest reasonable risk in any single year within the next 50 years is approximately $559 million. These results are indexed to achieving sufficient coverage for all the damage caused by 98% of all storm events over a 50 year period. Appendix E of the study shows that distribution facilities comprise 80% or $35 million of the expected annual damage.

FPL seeks to increase the annual accrual to $35 million to a storm fund which will be used for transmission restorations, distribution restorations and possibly certain nuclear events not covered by other insurance. We agree with FPL to the extent that a 98% coverage level for all events over a 50 year period is excessive. We are not persuaded that any harm will result to FPL's ratepayers if the annual contribution remains at its current level as long as the fund is used primarily for T&D restorations due to significant weather events.

The second report FPL attached to its petition is titled Storm Reserve Solvency Analysis. This report addresses policy considerations for capping the fund as well as the reasonableness of certain funding levels assuming an annual damage level of $42.3 million. While this report is informative, it provides no specific conclusions on the fund cap amount nor on the appropriate funding level for regulatory purposes because it assumes an annual damage amount which we do not believe is appropriate for regulatory purposes.

In its Petition, FPL stated that "a funding level sufficient to protect against another 'Andrew type' event is appropriate." An Andrew type event is defined by FPL in its Petition at page 2, as $350 million, which reflects inflation and system growth since 1992. However, FPL stated that the $350 million covers T&D only and an additional $20 million is necessary for property deductibles under the traditional insurance coverage which it currently holds. Rule 25-6.0143(1)(a), Florida Administrative Code, provides, among other things, that insurance deductibles may be charged against the reserve account. Therefore, we believe the reserve level should include this amount for insurance deductibles, and that a reasonable level for the reserve is $370 million in 1997 dollars.

The requested $35 million accrual would allow the reserve to reach Andrew level in approximately three years, while the current $20.3 million accrual will attain this level in approximately four years, assuming minimal future charges to the reserve. This calculation includes a reduction to the reserve of $14.5 million in charges associated with the 1998 "Groundhog Day" storm. In either scenario, any charges against the reserve will lengthen the amount of time needed to reach the $370 million.

FPL has two lines of credit totaling $900 million. $300 million is specifically designated for storm damage. FPL also has approximately $152 million, net-of-tax, in a funded reserve. It

should be noted that the after tax amount in the fund equates to approximately $247 million in storm costs. This is true because the amounts contributed to the fund are not tax deductible until actual storm costs are incurred, i.e., the difference between the $152 million and $247 million is the tax benefit realized when FPL takes a deduction for the expenses. FPL's financial resources from the lines of credit and the fund appear to be sufficient to cover most storm emergencies. However, the costs of storm damage incurred over and above the balance in the reserve and the costs of the use of the lines of credit would still have to be recovered from the ratepayers.

In the event FPL experiences catastrophic losses, it is not unreasonable or unanticipated that the reserve could reach a negative balance. Rule 25-6.0143(4)(b), Florida Administrative Code, recognizes that charges to a reserve may exceed the reserve balance resulting in a negative balance, as was the case of Gulf Power Company in Order No. PSC-96-0023-FOF-EI, issued January 8, 1996, in Docket No. 951533-EI. According to FPL's Response to Interrogatories 1 and 2, it has never experienced a negative reserve balance since the reserve's inception in 1946. The December 1997 balance of $251.3 million, is, we believe, sufficient to protect against most emergencies. In cases of catastrophic loss, FPL continues to be able to petition the Commission for emergency relief, as reflected in Order No. PSC-95-1588-FOF-EI.

Therefore, we find that FPL shall continue the current $20.3 million annual accrual. Further, FPL shall file a study addressing the reasonableness of the level of the reserve and accrual by no later than December 31, 2002. If there are no significant charges to the reserve, the fund balance should reach the target level about that time.

Given our decision to maintain the annual accrual at $20.3 million, FPL's request to implement the increase effective January 1, 1997 is moot.

III. APPROPRIATE USES OF STORM DAMAGE RESERVE

FPL's study did not include any analysis of the appropriate reserve balance necessary to cover the possibility of retrospective assessments associated with FPL's insurance of its nuclear facilities. The best information available suggests that the probability of such an assessment is low. This Commission has ongoing regulatory authority to review and determine the prudence

of charges to this reserve and fund. It is not disputed that this reserve and fund is available to cover uninsured losses to FPL's transmission and distribution system, as well as insurance deductibles. We take this opportunity to make it clear that, consistent with Rule 25-6.0143, Florida Administrative Code, this reserve and fund is also available to cover retrospective assessments incident to FPL's property insurance for its nuclear facilities.

IV. SEPARATION OF TRANSMISSION, DISTRIBUTION, AND OTHER AMOUNTS

FPL does not separate transmission, distribution, and other amounts for purposes of the reserve, fund and expense. It should be stressed that this is not a physical separation, but merely an accounting allocation that should not affect the fund investments or any insurance risk. FPL was asked to develop a separations methodology for T&D, Nuclear, and Other. The Company responded:

> Florida Power & Light (FPL) believes it is inappropriate to allocate the reserve and fund to transmission, distribution, nuclear and other and is not aware of any methodology that could be used to appropriately allocate the Storm Reserve and Fund between functions. Previous insurance coverage for storm damage to Transmission and Distribution property was not separable. If by dividing the current Storm Reserve and Fund balances into discrete portions, FPL would be required to insure Transmission and Distribution property separately, any hope of future insurability would be virtually eliminated, resulting in higher costs and less flexible risk management. It would be counter productive to create an artificial separation of funds when any real storm will have a mixture of Transmission and Distribution damages which will differ from the hypothetical separation. A separation may not be in the best interests of ratepayers, until and unless changes in regulation make such separation appropriate. In addition, any separation of the Funds between functions resulting in the liquidation or retirement of certain investments could result in losses accruing to the Storm Fund.

Without reaching the conclusion that such a separation is appropriate, we believe a reasonable methodology could be developed by the Company. FPL's storm damage study based its separation of T&D on the replacement value of the T&D assets. FPL has agreed to

perform the requested study. Therefore, we find that FPL shall file a methodology for separating T&D and Other by December 31, 1998.

V. ESTABLISHMENT OF A TRUST FUND FOR STORM DAMAGE RESERVE

Currently, the storm fund is not a trust fund. The Commission does not have sufficient information to determine whether or not FPL should establish a trust fund. One advantage of a trust fund is that the funds could only be released by the trustee for the intended purpose as defined in the trust agreement. This would assure that the storm fund accrual, recovered through the company's rates, is used only for its intended purpose. Many allowances, such as nuclear decommissioning accruals and pension expense, are subject to trust funds. However, the tax consequences of having a trust fund, as opposed to not having one, have not been fully examined. Given the significant amount of money in this funded reserve, it is appropriate to examine the issue in greater detail. FPL has agreed to perform the study. Therefore, we find that FPL shall file a study addressing the feasibility of establishing a trust fund for the storm damage reserve fund by December 31, 1998.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that FPL shall continue the current $20.3 million annual accrual. It is further

ORDERED that FPL shall file a study addressing the reasonableness of the level of the reserve and annual accrual by no later than December 31, 2002. It is further

ORDERED that, consistent with Rule 25-6.0143, Florida Administrative Code, this reserve and fund is available to cover retrospective assessments incident to FPL's property insurance for its nuclear facilities. It is further

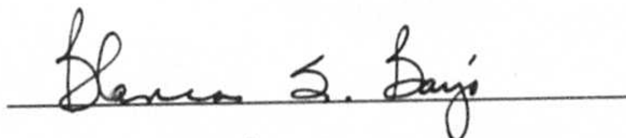
ORDERED that FPL shall file a methodology for separating Transmission, Distribution and Other assets covered by this reserve and fund no later than December 31, 1998. It is further

ORDERED that FPL shall file a study addressing the feasibility of establishing a trust fund for the storm damage reserve and fund no later than December 31, 1998. 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 14th day of July, 1998.



BLANCA S. BAYÓ, Director
Division of Records and Reporting

(S E A L)

RVE

Commissioners Clark and Garcia dissent from the decisions to maintain the annual accrual at the current level and to require the studies concerning an accounting separation and the feasibility of establishing a trust fund.

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 August 4, 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.