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: AUGUST 5, 1999

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYÓ)

FROM: DIVISION OF ELECTRIC AND GAS (BOHRMANN, WHEELER)
DIVISION OF AUDITING AND FINANCIAL ANALYSIS (REVELL)
DIVISION OF LEGAL SERVICES (C. KEATING)

RE: DOCKET NO. 990771-EI - PETITION OF FLORIDA POWER CORPORATION FOR APPROVAL OF REGULATORY TREATMENT ASSOCIATED WITH THE SALE OF REPLACEMENT CAPACITY AND ENERGY TO THE CITY OF TALLAHASSEE

AGENDA: 08/17/99 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\EAG\WP\990771.RCM

CASE BACKGROUND

The City of Tallahassee (City) currently owns a 1.3333 percent undivided interest in Crystal River Unit 3[1] (CR-3) as a tenant in common with Florida Power Corporation (Florida Power), Seminole Electric Cooperative, and eight other municipal-owned utilities. As a party to the CR-3 Participation Agreement, the City currently receives 1.3333 percent of CR-3's actual output. However, on December 9, 1998, Florida Power agreed to acquire the City's interest (approximately 11.4 MW) in CR-3 for a nominal cost and assume responsibility for all associated future costs, including decommissioning costs ("Agreement to Acquire the City of Tallahassee's Interest in the Crystal River Nuclear Plant").

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[1] Crystal River Unit 3 is a 859 MW nuclear steam electric generating unit located in Citrus County, Florida.

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Concurrently, Florida Power agreed to replace the same amount of capacity that the City previously received from its CR-3 share ("Power Sale Agreement By and Between Florida Power Corporation and the City of Tallahassee").

DISCUSSION OF ISSUES

ISSUE 1: Should the Commission approve Florida Power's proposed regulatory treatment associated with the sale of replacement capacity and associated energy to the City of Tallahassee?

RECOMMENDATION: Yes. Staff believes that Florida Power's proposed regulatory treatment would benefit its retail ratepayers; thus, Florida Power has met the Commission's standard set forth by Order No. PSC-97-0262-FOF-EI.

STAFF ANALYSIS: For regulatory purposes, Florida Power proposes that the Commission treat the sale of capacity and associated energy to the City as a unit power sale. Thus, Florida Power would assign all costs of the "unit" (i.e., 1.3333 percent of CR-3) to the wholesale jurisdiction. Also, when the unit does not operate at a 100 percent capacity factor, Florida Power would assign all costs of providing supplemental capacity and associated energy to the wholesale jurisdiction.

The Commission restated its criteria for separated wholesale sales in Order No. PSC-97-0262-FOF-EI, issued March 11, 1997, in Docket No. 970001-EI (Order No. 97-0262). As stated in that order, the Commission has traditionally required a utility to separate a wholesale sale if it is a long-term firm sale (greater than one year) that commits production capacity to a wholesale customer. The Commission separates a wholesale sale in order to remove the production plant and associated operating expenses from the retail jurisdiction. The Commission uses average embedded costs for production plant and operating expenses to assign costs to both jurisdictions and has required the utility to credit its fuel clause with its average system fuel cost. This treatment is intended to avoid any cross-subsidies between the wholesale and retail jurisdictions.

On behalf of Florida Power in Docket 960001-EI, Mr. Karl Wieland testified[2]:

> ...Florida Power believes that any sale, either retail or wholesale, should be priced at the average cost of the generation resources used to make the sale. In other words, sales from the utility's system should be based on system average fuel costs, and sales from a single generating unit (e.g., a Unit Power Sales arrangement) or from a combination of units (e.g., a "stratified" sales arrangement) should be based on the average cost of the particular unit or units involved with the sale. Following this approach will ensure that retail customers do not subsidize wholesale sales...

As noted in Order No. 97-0262, a utility can propose a deviation from this policy, if the utility proves, on a case-by-case basis, that each new sale provides overall benefits to its retail ratepayers. Florida Power seeks approval of its proposed regulatory treatment because the treatment is a deviation from the Commission's policy as stated in Order No. 97-0262. The Commission's approval of the proposed regulatory treatment is necessary for Florida Power and the City to complete the aforementioned agreements. Staff recommends approval because the proposed regulatory treatment provides a nominally positive benefit to Florida Power's retail ratepayers.

Staff notes that Chapter 120, Florida Statutes, generally requires an agency to adopt as rules any agency statement of general applicability that prescribes law or policy. However, Section 120.80(13)(a), Florida Statutes, specifically exempts from this requirement agency statements relating to cost recovery clauses and mechanisms implemented pursuant to Chapter 366, Florida Statutes. Order No. 97-0262 was issued as part of the Commission's fuel and purchased power cost recovery clause. Thus, although the Order contains an agency statement of general applicability that prescribes policy, this agency statement is exempt from the rulemaking requirements of Chapter 120, Florida Statutes.

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[2] Direct testimony of Karl H. Wieland in Docket No. 960001-EI, filed June 24, 1996, page 12

Provisions of "Power Sale Agreement By and Between Florida Power Corporation and the City of Tallahassee"

Florida Power will sell capacity and associated energy to the City until the expiration of CR-3's operating license (i.e., December 3, 2016). Details of the power sales agreement between Florida Power and the City are as follows:

> 1) Florida Power will deliver 11.4 MW of firm capacity to the City at a 100 percent capacity factor;
>
> 2) The City will pay Florida Power an all-inclusive $42 per MWH (includes energy, capacity, and transmission charges) until December 31, 2007. Then, the amount will increase annually by the rate of change in the Consumer Price Index until December 3, 2016;
>
> 3) Florida Power shall provide the capacity and associated energy to the City at a priority level equivalent to Florida Power's firm native load[3]; and
>
> 4) Pursuant to Florida Power's Open Access Transmission Tariff, the City will maintain a valid, binding, and enforceable agreement for firm transmission and related ancillary services.

Proposed Regulatory Treatment

With respect to acquiring the City's interest in CR-3, Florida Power's proposed treatment would affect its jurisdictional cost separations and surveillance reporting as follows:

> 1) Capital cost: In accordance with the Uniform System of Accounts, the City's gross investment and accumulated depreciation in its

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[3] To the extent that Florida Power eliminates bundled service for its native load, the capacity and associated energy will be provided at a priority equal to Florida Power's highest service obligation of its generation division.

share of CR-3 would be recorded on Florida Power's records. The difference between the acquisition price and the net book value of this share would be recorded as a credit to "Electric Plant Acquisition Adjustments", because the net book value is greater than the purchase price. The Uniform System of Accounts requires that any company that intends to record credit amounts to this account must receive Commission approval to do so. The credit would then be amortized to "Amortization of Electric Plant Acquisition Adjustments" over the remaining life of the investment. This would result in no increase to retail ratebase nor any increase in depreciation expense. No cost separation is therefore necessary;

2) Decommissioning costs: Florida Power would assign the continued funding of decommissioning costs for the newly acquired share to the wholesale jurisdiction;

3) O&M costs: Florida Power would assign 1.3333 percent of the costs to operate and maintain CR-3, as well as all other costs of the unit, such as insurance and property taxes, to the wholesale jurisdiction on an average cost basis; and

4) Capital Additions: Florida Power would assign 1.3333 percent of capital additions related to CR-3's existing capacity to the wholesale jurisdiction. However, the retail ratepayers would bear the associated costs of a capacity increase because capital additions to increase the unit's capacity would not increase the capacity sold to the City.

Florida Power proposes that all transactions related to the purchase, including the acquisition adjustment, be assigned to the wholesale jurisdiction. Staff believes that the proposed accounting treatment to amortize the acquisition adjustment over the remaining life of CR-3 is proper and will not impact retail

ratepayers. Therefore, staff recommends that Florida Power's proposed accounting treatment be approved.

With respect to the sale of replacement capacity and associated energy to the City, Florida Power's proposed treatment would affect its retail fuel and capacity cost recovery clauses as follows:

1) Nuclear fuel costs: Florida Power would credit 1.3333 percent of the average cost of nuclear fuel to the fuel clause;

2) Spent fuel disposal costs: Florida Power would credit $1.00 per MWH generated with the newly-acquired share of CR-3 to the fuel clause;

3) Nuclear decommissioning and dismantlement (D&D) charges: Florida Power would assign 1.3333 percent of CR-3's nuclear D&D charges to the wholesale jurisdiction; and

4) Supplemental power costs: Florida Power would calculate the cost of providing supplemental power during periods when CR-3 is operating at less than a 100 percent capacity factor under the pricing provisions of Florida Power's standard Schedule B interchange tariff approved by FERC. Florida Power uses Schedule B to sell capacity and associated energy to other utilities to replace the output of a unit on a forced or maintenance outage. Its pricing provisions consist of an incremental energy charge and a capacity charge:

a) Calculation of incremental energy costs - Florida Power proposes to utilize the hourly incremental cost used to price as-available energy payments to qualifying facilities as representative of incremental energy costs. Florida Power would multiply the hourly difference between the 11.4 MW sale to the City and 1.3333 percent of the actual output of CR-3 by the incremental energy cost for that hour. Then, Florida Power would credit the sum of these hourly amounts to the retail fuel clause; and

b) Calculation of capacity costs - Capacity costs are based on average embedded costs and are expressed on an energy basis for billing purposes. The capacity charge under the current Schedule B tariff is $5.53 per MWH. Florida Power would credit the product of this capacity charge and the amount of supplemental energy to the capacity cost recovery clause.

Effects Upon Florida Power's Retail Ratepayers

The proposed regulatory treatment would have a nominally positive effect on the retail customers for the following reasons. First, the retail customers would not bear any fixed costs, non-fuel variable costs, or fuel costs associated with the newly-acquired share of CR-3. Also, the retail customers would not bear any of Florida Power's costs to provide supplemental power to the City when CR-3 operates at less than a 100 percent capacity factor.

Second, when CR-3 operates at less than a 100 percent capacity factor, Florida Power would assign the revenue received ($5.53/MWH) from the City for supplemental capacity to the retail customers. In the absence of the Florida Power's agreement to sell replacement capacity and associated energy to the City, the retail customers would bear the costs of this capacity. However, because Florida Power would credit these revenues to the capacity cost recovery clause, the retail customers would benefit through a reduction in rates. For example, if CR-3 operates at a 75 percent capacity factor, capacity costs paid by retail customers would fall by approximately $138,000[4].

Third, under the proposed regulatory treatment, when CR-3 operates at a 100 percent capacity factor, there would be no change in the amount of electricity that the City receives from Florida Power. Under this scenario, the proposed regulatory treatment would create a transparent effect on its retail customers. However, when CR-3 operates at less than a 100 percent capacity factor, the City would continue to receive 11.4 MW from Florida Power. Under this scenario, Florida Power would credit the incremental energy costs to the fuel clause for the difference between 1.3333 percent of CR-3's actual output and 11.4 MW.

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[4] 11.4 MW x 24 hours/day x 365 days/year x (100% - 75%) x $5.53/MWH = $138,062

Staff believes that Florida Power's proposed regulatory treatment of its supplemental power costs is analogous to the regulatory treatment ordered by the Commission in Order No. PSC-97-1273-FOF-EU, issued October 15, 1997, in Docket No. 970171-EU. In that order, the Commission ordered Tampa Electric Company to credit its fuel clause with system incremental fuel cost associated with wholesale sales to FMPA and the City of Lakeland. In a similar fashion, when the capacity factor of CR-3 is less than 100 percent, Florida Power proposes to utilize the hourly incremental cost used to price as-available energy payments to qualifying facilities to represent incremental energy costs.

In summary, the Commission set forth a standard for deviating from the regulatory treatment prescribed by Order No. 97-0262. After reviewing the two aforementioned agreements between Florida Power and the City and the effects of each agreement on Florida Power's retail customers, staff believes that Florida Power's proposed regulatory treatment would provide a nominally positive benefit to its retail ratepayers. Thus, staff believes that Florida Power has met the Commission's standard set forth in Order No. 97-0262.

ISSUE 2: Should this docket be closed?

RECOMMENDATION: Yes. If no person whose substantial interests are affected by the Commission's proposed agency action files a protest within 21 days of the order, this docket should be closed.

STAFF ANALYSIS: If no person whose substantial interests are affected by the Commission's proposed agency action files a request for hearing within 21 days of the order, no further action will be required and this docket should be closed.