

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for Rate Increase by)
Peoples Gas System)
_____)

Docket No. 080318-GS

Filed: February 13, 2009

**PREHEARING STATEMENT
OF THE OFFICE OF PUBLIC COUNSEL**

The Citizens of the State of Florida, through the Office of Public Counsel (“OPC”), pursuant to the Order Establishing Procedure (Order PSC-08-0555-GU, issued August 21, 2008), hereby submit this Prehearing Statement in this Petition for a Rate Increase by Peoples Gas System (“PGS”).

1. APPEARANCES:

CHARLES J. REHWINKEL
Office of Public Counsel
c/o The Florida Legislature
111 West Madison Street, Room 812
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On behalf of the Citizens of the State of Florida.

2. WITNESSES:

Citizens prefiled testimony by the following witness:

Helmuth W. Schultz, III. In his testimony, Mr. Schultz recommends numerous accounting adjustments to the PGS rate filing.

Dr. J. Randall Woolridge. In his testimony, Dr. Woolridge recommends the appropriate cost of equity.

3. EXHIBITS:

Witness for Citizens prefiled the following exhibits:

Helmuth W. Schultz, III.

Appendix – Qualifications of Helmuth W. Schultz, III

(HWS-1) – Adjustments

Dr. J. Randall Woolridge

Appendix – Qualifications of Dr. J. Randall Woolridge

(JRW -1) -- Weighted Average Cost of Capital

(JRW -2) -- Interest Rates

(JRW -3) -- Summary Financial Statistics for Gas Proxy Group

(JRW -4) -- Capital Structure Ratios and Debt Cost Rate

(JRW -5) -- S & P 500 Price CV / Bear Stearns Bond Price Index CV

(JRW -6) -- The Relationship Between Estimated ROE and Market-To-Book-Ratios

(JRW -7) -- Public Utility Capital Cost Indicators

(JRW -8) -- Industry Average Betas

(JRW -9) -- Three Stage DCF Model

(JRW -10) -- DCF Study

(JRW -11) -- CAPM Study

(JRW -12) -- Summary of Dr. Murry's Results

(JRW -13) -- Analyst's Long term Forecasted EPS Growth Rates

(JRW -14) -- Value Line 3-5 year Growth Rate Forecasts

(JRW -15) -- Historical Risk Premium Evaluation

(JRW -16) -- CFO's Equity Risk Premium

4. STATEMENT OF BASIC POSITION

Peoples Gas has substantially overstated its projected revenue requirements. The Commission should not allow revenues to increase by more than \$5,673,535 nor allow a return on common equity of greater than 9.5%

5. STATEMENT OF FACTUAL ISSUES AND POSITIONS

TEST PERIOD

ISSUE 1: Are the historical base year ended December 31, 2007, and the projected test year ending December 31, 2009, the appropriate test years to be utilized in this docket?

OPC: No Position.

ISSUE 2: Are the projected bills and therms for the test year ending December 31, 2009, appropriate for use in this case?

OPC: No Position.

QUALITY OF SERVICE

ISSUE 3: Is the quality of gas service provided by PGS adequate?

OPC: No Position.

RATE BASE

ISSUE 4: What are the appropriate unit costs for projected plant additions?

OPC: Pending further discovery, it is the OPC's position that PGS has not provided sufficient information to determine whether PGS has used reasonable prudent unit costs in projecting the costs of plant additions for mains and services. At this time an adjustment to reduce plant appears to be warranted. (Schultz)

ISSUE 5: Should any adjustments be made to Projected Plant, Accumulated Depreciation, and Depreciation Expense?

OPC: Yes. Distribution Plant should be reduced \$15,277,686, Accumulated Depreciation should be reduced \$369,404 and Depreciation Expense should be reduced \$404,900. (Schultz)

ISSUE 6: Should any adjustments be made to remove a portion of the cost of the main running east to west across the Florida Turnpike on SW Martin Highway from the projected test year rate base?

OPC: Yes. Pending further discovery, the amount is unknown.

ISSUE 7: Should any adjustments be made to reduce Plant, Accumulated Depreciation, Depreciation Expense, and other expenses to reflect non-utility operations?

OPC: No position at this time.

ISSUE 8: What is the appropriate amount of Construction Work in Progress (CWIP) for the 2009 projected test year?

OPC: Pending further discovery and the resolution of issues related to Issue 4, the OPC has no position at this time. (Schultz)

ISSUE 9: What is the appropriate 2009 projected test year Total Plant?

OPC: The appropriate 2009 projected test year Total Plant is \$994,096,604. (Schultz)

ISSUE 10: What is the appropriate 2009 projected test year Depreciation Reserve?

OPC: The appropriate 2009 projected test year Depreciation Reserve is \$425,994,955. (Schultz)

ISSUE 11: Should conservation over recoveries be included in the calculation of working capital?

OPC: Yes. To the extent included consistent with Commission practices, these liabilities, if excluded, would increase working capital. Such an adjustment makes the customers pay interest that the company will return to them in clause proceedings.

ISSUE 12: What is the appropriate 2009 projected test year Working Capital Allowance?

OPC: Projected test year working capital allowance is (\$11,503,321). (Schultz)
Adjustments are necessary to reflect the appropriate amount of deferred rate case expense and any other adjustments related to Issue II.

ISSUE 13: What is the appropriate projected test year Rate Base?

OPC: The test year rate base is subject to the resolution of other issues but should not exceed \$548,682,201. (Schultz)

COST OF CAPITAL

ISSUE 14: What is the appropriate return on common equity for the projected test year?

OPC: The appropriate return on common equity for the 2009 projected test year is 9.25%, as of December 18, 2008.

ISSUE 15: What is the appropriate capital structure for the projected test year?

OPC: The PGS capital structure as filed is not inappropriate so long as recognition is given that its level of equity is higher than the proxy group used for purposes of determining an appropriate cost Common equity. (Woolridge)

ISSUE 16: What is the appropriate cost rate of long-term debt for the projected test year?

OPC: The appropriate cost rate of long term debt for the test year is 7.20%. (Woolridge)

ISSUE 17: What is the appropriate cost rate of short-term debt for the projected test year?

OPC: The appropriate cost rate of short term debt for the test year is 1.76%. (Woolridge)

ISSUE 18: What is the appropriate amount of accumulated deferred taxes to be included in the capital structure for the projected test year?

OPC: No position at this time.

ISSUE 19: What is the appropriate amount and cost rate of the unamortized investment tax credits to include in the capital structure for the projected test year?

OPC: No position at this time.

ISSUE 20: What is the appropriate weighted average cost of capital for the projected test year?

OPC: The appropriate weighted average cost of capital for the projected test year is subject to the resolution of other issues but should be no greater than 7.77%. (Woolridge)

REVENUES

ISSUE 21: Has PGS made the appropriate test year adjustments to remove revenues and expenses recoverable through the Purchased Gas Adjustment Clause?

OPC: No position at this time.

ISSUE 22: Has PGS made the appropriate test year adjustments to remove conservation revenues and conservation expenses recoverable through the Conservation Cost Recovery Clause?

OPC: No position at this time.

ISSUE 23: What amount, if any, of Off-System Sales revenues should be included in the projected test year?

OPC: Off-system sales should be increased by \$1,500,000. (Schultz)

ISSUE 24: What is the appropriate amount of projected test year total Operating Revenues?

OPC: The appropriate amount of projected test year total operating revenues is \$171,406,126. (Schultz)

EXPENSES

ISSUE 25: Are the trend rates used by PGS to calculate projected O&M expenses appropriate?

OPC: No. The 2008 average CPI has dropped considerably from the 2.90% requested by the company to 0.1%. The projected 2009 CPI should also be reduced accordingly.

ISSUE 26: Should the projected test year O&M expense be adjusted for the effect of any changes to the trend factors?

OPC: Yes as addressed in Issue 25.

ISSUE 27: Should any adjustments be made to the 2007 O&M expenses for staff Audit Finding Nos. 1 and 2, to address out-of-period expenses, reclassifications, and non-utility expenditures?

OPC: No position at this time.

ISSUE 28: Should any adjustments be made to Account 920, Administrative and General Salaries, or any other accounts related to employee compensation?

OPC: Yes. Payroll expense should be reduced \$210,199 to account for the slowdown in customer growth. Incentive compensation should be reduced by \$2,714,400 to account for their excessive amount relative to any benefits produced for ratepayers. Adjustments should also be made to reflect the zero percent executive base pay raises implemented in February 2009. (Schultz)

ISSUE 29: What is the appropriate amount of rate case expense and what is the appropriate amortization period for that expense?

OPC: Rate case expense should not exceed \$684,500 and should be amortized over no less than 5 years consistent with historical spacing of rate case filings. (Schultz).

ISSUE 30: Is PGS's proposed recovery of the gas cost portion of bad debt expense through the Purchased Gas Adjustment Clause appropriate?

OPC: No. Uncollectible expense recovery is properly a matter for base rate treatment. Recovery through the PGA Clause will reduce scrutiny and company incentive to pursue collection. (Schultz).

ISSUE 31: Should any adjustments be made to bad debt expense?

OPC: Yes. Consistent with Commission practice, bad debt expense should be based on a 5-year historical average.

ISSUE 32: Should any adjustments be made to Account 926, Employee Pensions and Benefits?

OPC: Yes. Employee welfare/activity expense should be reduced \$172,881 to match these expenses to the appropriate trending and inflation factors. Also, \$569,500 of expense related to restricted stock grants and stock options should be reduced due to the excessive nature of this type of expense. (Schultz)

ISSUE 33: What is the appropriate amount of pipeline integrity expense, if any, to be included in the projected test year?

OPC: Projected test year pipeline integrity expense should be reduced by \$250,000 to \$501,500. (Schultz)

ISSUE 34: Should the Commission allow PGS to establish a storm damage reserve, and if so, what is the appropriate amount of annual storm expense accrual?

OPC: No. The need for an unfunded reserve of \$1 million and \$100,000 annual accrual appears overstated based on experience. (Schultz)

ISSUE 35: Should any adjustments be made to Account 912, Demonstrating and Selling expenses?

OPC: Yes. Projected demonstrating and selling expenses should be reduced \$2,000,530 due to the ineffectiveness of this service that is provided by an affiliate. (Schultz)

ISSUE 36: Should the costs to fund Directors and Officers Liability Insurance be included in the projected test year?

OPC: No. The entire projected DOL insurance expense should be eliminated since the insurance benefits primary shareholder defending lawsuits from shareholders. (Schultz)

ISSUE 37: Should any adjustments be made to costs allocated by TECO to PGS?

OPC: Yes. \$1,262,437 of allocated incentive and bonus compensation and DOL expense should be removed. (Schultz)

ISSUE 38: What is the appropriate amount of Taxes Other Than Income Taxes?

OPC: \$10,823,933.

ISSUE 39: Is it appropriate to make a parent debt adjustment as per Rule 25-14.004, Florida Administrative Code?

OPC: Yes. (Schultz)

ISSUE 40: What is the appropriate Income Tax Expense, including current and deferred income taxes, ITC amortization, and interest synchronization?

OPC: The appropriate income tax expense amounts are reflected in Exhibit HWS-1, Schedule C-1, per the testimony of Helmuth W. Schultz. (Schultz)

ISSUE 41: What is the appropriate amount of projected test year O&M Expense?

OPC: \$65,598,432. (Schultz)

ISSUE 42: What is the appropriate amount of projected test year Depreciation and Amortization Expense?

OPC: \$42,759,833. (Schultz)

ISSUE 43: What is the appropriate level of Total Operating Expenses for the 2009 projected test year?

OPC: \$132,210,478. (Schultz)

ISSUE 44: What is the appropriate amount of projected test year Net Operating Income?

OPC: \$39,195,648. (Schultz)

REVENUE REQUIREMENTS

ISSUE 45: What is the appropriate projected test year revenue expansion factor to be used in calculating the revenue deficiency?

OPC: 1.6436. (Schultz)

ISSUE 46: What is the appropriate projected test year operating revenue increase, if any?

OPC: \$5,673,535. (Schultz)

RATES

ISSUE 47: Are PGS's estimated revenues by rate class at present rates for the projected test year appropriate?

OPC: No position.

ISSUE 48: What is the appropriate cost of service methodology to be used in allocating costs to the rate classes?

OPC: No position.

ISSUE 49: What are the appropriate customer charges?

OPC: No position.

ISSUE 50: What are the appropriate per therm Distribution Charges?

OPC: No position.

ISSUE 51: What are the appropriate Miscellaneous Service Charges?

OPC: No position.

ISSUE 52: Is PGS's proposal to stratify its current single residential service class into three individual classes appropriate?

OPC: No position.

ISSUE 53: Is PGS's proposal to reclassify certain customers appropriate?

OPC: No position.

ISSUE 54: Should the Commission approve PGS’s proposed “Gas System Reliability Rider,” which would permit recovery of revenue requirements associated with eligible infrastructure system replacements (e.g., replacements for existing facilities, relining projects to extend useful life of existing facilities, road relocation projects) and incremental O&M expenses, if any, incurred to comply with mandatory pipeline safety regulations? If approved as proposed by PGS, such recovery would continue until the effective date of revised base rates established in the Company’s next base rate proceeding. The rider would also provide for the refund of O&M expenses, if any, incurred to comply with mandatory pipeline safety regulations, in excess of such expenses included in the Company’s most recent base rate proceeding.

OPC: No. The company has not demonstrated that regulatory oversight of these costs should be removed from base rates review. The type of costs here are not sufficiently large or volatile as to warrant recovery in a “clause” mechanism, nor has PGS proposed any downward ROE adjustment in the event the rider is adopted. (Schultz)

ISSUE 55: Should the Commission approve PGS’s proposed “Carbon Reduction Rider,” which would permit recovery of revenue requirements associated with incremental capital expenditures, if any, for installation of supply mains (as defined in the rider) to serve primarily residential developments? If approved as proposed by PGS, such recovery would continue until the earlier of (i) the end of a five-year recovery period, or (ii) the effective date of revised base rates established in the Company’s next base rate proceeding.

OPC: No. The company has not demonstrated that regulatory oversight of these costs should be removed from base rates review. The type of costs here are not sufficiently large or volatile as to warrant recovery in a “clause” mechanism, nor has PGS proposed any downward ROE adjustment in the event the rider is adopted. (Schultz)

ISSUE 56: What is the appropriate effective date for PGS’s revised rates and charges?

OPC: No position.

ISSUE 57: Should any of the \$2,380,000 interim rate increase granted by Order No. PSC-08-0696-PCO-GU be refunded to the ratepayers?

OPC: No position at this time.

ISSUE 58: Should PGS be required to file, within 90 days after the date of the final order in this docket, a description of all entries or adjustments to its annual report, earnings surveillance reports, and books and records which will be required as a result of the Commission's findings in this docket?

OPC: Yes.

ISSUE 59: Should this docket be closed?

OPC: No position at this time.

6. PENDING MOTIONS:

None.

7. STATEMENT OF PARTY'S PENDING REQUESTS OR CLAIMS FOR CONFIDENTIALITY:

None.

8. OBJECTIONS TO QUALIFICATION OF WITNESSES AS AN EXPERT:

None at this time.

9. STATEMENT OF COMPLIANCE WITH ORDER ESTABLISHING PROCEDURE:

There are no requirements of the Order Establishing Procedure with which the Office of Public Counsel cannot comply.

Dated this 13th day of February, 2009.

Respectfully submitted,

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DOCKET NO. 080318 -GS
CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of the foregoing **PREHEARING STATEMENT OF THE OFFICE OF PUBLIC COUNSEL** has been furnished by U.S. Mail and electronic mail to the following parties on this 13th day of February, 2009.

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