

Marguerite McLean

090125-GU

From: beth.keating@akerman.com
Sent: Friday, October 09, 2009 1:51 PM
To: Filings@psc.state.fl.us
Subject: Docket No. 090125-GU - Petition for Increase in Rates by Florida Division of Chesapeake Utilities Corporation
Attachments: 2009100913495 1277.pdf

Attached for electronic filing in the referenced Docket, on behalf of the Florida Division of Chesapeake Utilities Corporation, please find the Company's Responses to Staff's 7th Set of Data Requests (Nos. 211-215).

If you have any questions, please do not hesitate to contact me.

Sincerely,
Beth Keating
Akerman Senterfitt
(850) 224-9634
(850) 521-8002 (direct)
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A. Beth Keating

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B. Docket No. 090125-GU - Petition for Increase in Rates of Florida Division of Chesapeake Utilities Corporation

C. Filed on behalf of the Florida Division of Chesapeake Utilities Corporation

D. Number of Pages: 8

E. Responses to PSC Staff's 7th Set of Data Requests (Nos. 211-215).

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October 9, 2009

VIA Electronic Filing

Ann Cole
Commission Clerk
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Re: Docket No. 090125-GU - Petition for increase in rates by Florida Division of Chesapeake Utilities Corporation.

Dear Ms. Cole:

Please accept for electronic filing the Florida Division of Chesapeake Utilities Corporation's responses to the PSC Staff's 7th Data Requests in this Docket (Nos. 211 - 215).

Thank you for your assistance with this filing. Should you have any questions whatsoever, please do not hesitate to contact me.

A handwritten signature in cursive script that reads "Beth Keating".

Beth Keating
AKERMAN SENTERFITT
106 East College Avenue, Suite 1200
Tallahassee, FL 32302-1877
Phone: (850) 224-9634
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Attorneys for the Florida Division of Chesapeake Utilities Corporation

cc: Patty Christensen
Erik Sayler

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The Florida Division of Chesapeake Utilities Corporation
Re: Docket No. 090125- GU: Petition for Increase in Rates by Florida
Division of Chesapeake Utilities Corporation

Responses to Staff's Seventh Set of Data Requests (Nos. 211 – 215)

The Florida Division of Chesapeake Utilities Corporation ("Company" of "Chesapeake") provides the following responses to Staff's Sixth Data Requests (Nos. 211 – 215).

211. Please refer to Commission decisions in Order No. PSC-04-1110-PAA-GU, issued November 8, 2008, in Docket No. 040216-GU, In re: Application for rate increase by Florida Public Utilities Company, and Order No. PSC-07-0913-PAA-GU, issued November 13, 2007, in Docket No. 060657-GU, In re: Petition for approval of acquisition adjustment and recognition of regulatory asset to reflect purchase of Florida City Gas by AGL Resources, Inc. Please explain in detail why Chesapeake is not amortizing the acquisition adjustment and expense the transaction and transitions costs starting the day after the closing of the merger transaction consistent with these Commission decisions.

Company Response: The Company's proposed amortization of its acquisition premium and transaction and transition costs in no way affects the revenue requirement or proposed rates in the Company's current rate case. To be clear, the proposed amortization treatment will NOT result in rates that in any way recover or collect merger-related costs in this rate case. This case was prepared and filed as a "stand alone" case, with no merger-related assumptions included in the derivation of the proposed rates. Furthermore, the merger has not occurred as of the date of this response, therefore, the Company has not incurred any acquisition adjustment or transition costs. At this time, absent a Commission order to the contrary, the Company is expensing transaction costs in accordance with Generally Accepted Account Principles (GAAP). The Company, again absent any Commission order to the contrary, would follow GAAP and expense transition costs when incurred, after the merger is consummated. GAAP also prescribes, as noted on page 55 of my testimony, that the acquisition adjustment premium would be recorded as an asset ("goodwill") on the Company's books. The "goodwill" premium, unless the Company is otherwise directed by the Commission, would not be amortized but would instead be subject to periodic impairment assessments.

In 2001, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("FAS 142"). FAS 142 addresses the subsequent accounting treatment for recorded

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goodwill (it does not address how to calculate goodwill but provides direction on how to account for goodwill once recorded). FAS 142 was effective for all goodwill resulting from business combinations after June 30, 2001 and all other goodwill in 2002. Prior to FAS 142, Accounting Principles Board Opinion No. 17, "Intangible Assets" ("APB 17") provided the accounting treatment for goodwill. Under APB 17, goodwill was considered to have a useful life and amortized over that life. However, under FAS 142, this is no longer the case; goodwill is not amortized. Rather, goodwill is assessed for impairment at least annually. FAS 142 provides specific guidance on how to perform goodwill impairment testing. Once an impairment loss is recorded it cannot be reversed in future years.

However, contingent on the merger being consummated, the Company has, in my testimony, proposed what it considers to be a more appropriate disposition of the acquisition adjustment, transaction and transition costs than occurred in the referenced cases, and which the Company believes is more consistent with FAS 142. Simply stated, the Company is seeking a Commission order that would: 1) authorize the deferral of any acquisition adjustment amortization; 2) authorize the reversal of any expensed transaction costs; 3) establish all transaction and transition costs as Regulatory Assets (instead of being expensed when incurred); and 4) defer the final disposition of these issues until the proposed "come-back" filing.

As stated on pages 48 and 49 of my testimony, in the AGL Resources Inc (AGL), case referred to above, the Commission stated that "[a]cquisition adjustments have been allowed in extraordinary circumstances if a company could demonstrate that customers will derive certain benefits attributable to the acquisition." The Commission goes on to state that "[s]uch an adjustment provides an incentive for stronger companies to purchase weak or troubled companies." The Company agrees with these statements and, assuming the merger is consummated, will be prepared to meet the Commission's five factor test in the proposed "come-back" filing. The five factors are:

- 1) Increased quality of service;
- 2) Lower operating costs;
- 3) Increased ability to attract capital for improvements;
- 4) Lower overall cost of capital; and
- 5) More professional and experienced managerial, financial, technical and operational resources.

A closer inspection of these factors seems to indicate that the test is not related to the historic Plant Assets purchased in the transaction, but rather are prospective in nature such that the benefits of the merger will positively impact future service and operation of the combined company. The Company also believes that the five factor test could be used to determine if the positive acquisition adjustment is "impaired" (the cost is greater than the benefits obtained), consistent with FAS 142. If the positive acquisition adjustment is

determined to be impaired, then the Company would not be authorized to recover this asset through approved rates. If it is determined that it is not impaired, then the Company would be authorized to recover this asset (and earn on this asset) through approved rates and "match" the costs (amortization) against the benefits (lower operating costs). Therefore, it is the Company's position that the positive acquisition adjustment amortization should be deferred until the "impairment" (five factor) test can be best performed in the "come-back" filing. **(Response by Mr. Geoffroy)**

212. Please refer to witness Geoffroy's testimony, page 49, lines 12-21. Witness Geoffroy states that the Code of Federal Regulation (Code) does not prescribe when the amortization period should begin. He also states, "the Company believes that the acquisition adjustment should begin when 'the benefit will be realized.'" Please explain why the amortization should be tied to "the benefit will be realized" versus "to the life of the asset"?

Company Response: As explained on pages 49 and 50 of my testimony, the Code of Federal Regulations (Code) requires that the purchase price be recorded on the Company's books in two (2) distinct pieces: 1) record the plant assets of the acquired company at book value in the appropriate Plant Accounts; and 2) record the premium as an acquisition adjustment in a separate account.

The Company receives benefits from the acquired plant assets through the revenues derived from the approved rates established to recover the cost of service, including the return component, related to the plant assets (rate base). These benefits begin immediately upon the closing of the merger.

However, the Company does not receive any benefit from the revenues derived from the approved rates for the acquisition premium. The acquisition premium asset was not part of the rate base upon which the current approved rates have been set. The Company expects to receive benefits from the premium paid (and is the reason why the Company is willing to pay a premium) through future operating cost savings in an amount that is at least equal to the total cost of the acquisition adjustment – the second factor of the Commission test (amortization of the acquisition adjustment over a reasonable time and the return on the acquisition adjustment asset). The language contained in the Code appears to recognize that the acquiring company cannot match the benefits of paying a premium with the benefits derived from the transaction (lower operating costs) if the company were *required* to begin the amortization of the acquisition adjustment at the closing date. In fact, if the Company were required to begin amortizing the acquisition adjustment immediately upon closing, the Company would be irreparably harmed and it would appear to be inconsistent with the Commission's statements noted in the Company's response to Data Request 211 above. **(Response by Mr. Geoffroy)**

213. Please refer to witness Geoffroy's testimony, page 50, lines 15 through 17. Witness Geoffroy states "In the Company's view, the definition of 'amortization' in the Code and the 'matching principle' of Generally Accepted Accounting Principles [GAAP], would defer the amortization of the acquisition adjustment until the lower operating costs (benefits) are realized." Please explain or describe how "amortization" in the Code and "matching principle" in GAAP "would defer the amortization of the acquisition adjustment until the lower operating costs (benefits) are realized"?

Company Response: See the above responses. (Response by Mr. Geoffroy)

214. Please refer to witness Geoffroy's testimony on page 51, lines 10-14. Witness Geoffroy states "If approved by the Commission, the amortization of the acquisition adjustment would be suspended until the final disposition of the 'come back' filing, unless the operating savings subsequent to closing place the combined company in an overearnings situation." (emphasis added)
- a. Does this statement mean that if there are operating saving subsequent to the closing of the merger and before the final disposition of the "come back case," Chesapeake is proposing to amortize the acquisition adjustment until the excess revenues (overearnings) are reduced to allow a return on equity that will be at the top of the Company's authorized range of return?

Company Response: Yes.

- b. Does the Company anticipate this situation to cause an "overearnings situation"? Please explain.

Company Response: The Company does not know whether this situation could cause an overearnings situation. However, the Company believes that the proposal would provide benefits and protection to ratepayers. Any amortization amount would reduce the remaining acquisition adjustment premium, thus IF the Commission ultimately approves recovery of the acquisition adjustment, the amortization amount would be lower and the return on the acquisition adjustment asset would also be lower (benefit). If the Commission does NOT approve recovery, then the Commission could recognize the overearnings and dispose of it however the Commission deems appropriate (protection).

- c. What authorized range of return would be used if there was an overearnings situation?

Company Response: The Company believes that the authorized range of return approved in the Company's instant case would be used to determine if an overearnings situation occurs.

(Response by Mr. Geoffroy)

215. Please refer to witness Geoffroy's testimony, page 53, lines 18-22, where he states "the Florida Division is not seeking 'approval' of the positive acquisition adjustment or transaction and transition costs at this time, only that these items be established as Utility Plant and Regulatory Assets, respectively, and that the amortization of these items be suspended until the 'come back' filing, anticipated to be filed in 2011." Please respond to the following:

- a. Please explain how the establishment of requested Utility Plant (positive acquisition adjustment) and Regulatory Assets (transaction and transition costs) will not be seen by the ratepayers as a foregone conclusion of the recovery of these costs and expenses by Chesapeake?

Company Response: The Company has indicated in my testimony that if the Commission accepts the Company's proposal, that it should in its order clearly state that these items are being deferred for final disposition in the "come-back" filing and that the burden is on the Company to demonstrate why the Commission should approve the recovery of these items. The Commission would simply be deferring action on the potential recovery of these items until sufficient information is available in order to make an informed decision. The Company believes that all parties would want to clearly understand the full benefits of the acquisition and how they will be shared between the ratepayers and the Company. If the Commission were to order the proposed deferral treatment, the Company does not see how ratepayers could perceive the ultimate recovery of these costs as a "foregone conclusion."

- b. Based upon an anticipated "come back" filing in 2011, please explain how the utility will address the potential positive acquisition and regulatory assets if they are not approved in the "comeback case"?

Company Response: The Company would certainly abide by the actions ordered by the Commission in the "come-back" filing. The Company would, however, welcome the opportunity to work with Commission Staff and Public Counsel to find alternative, mutually acceptable, accounting methods to make sure that both the Company and its ratepayers receive all available benefits of these regulatory assets.

- c. Based upon an anticipated "come back" filing in 2011, please explain how the utility will address potential positive acquisition and regulatory assets if the merger is not consummated?

Company Response: If the merger is not consummated, then there would not be any positive acquisition or transition costs and any transaction costs would be expensed.

(Response by Mr. Geoffroy)

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for increase in rates by)
Florida Division of Chesapeake Utilities)
Corporation)

Docket No. 090125-GU

AFFIDAVIT

State of Florida
County of Polk

I, Thomas A. Geoffroy, having been duly sworn, depose and say that:

1. I am the Vice President of Chesapeake Utilities Corporation; and
2. On October 9, 2009 under my direction and supervision, the attached responses (211-215) to Staff's Seventh Data Request Nos. 211-215 were prepared and submitted and are true and correct to the best of my knowledge.


Thomas A. Geoffroy

Sworn to and subscribed before me this 9th day of October, 2009, by Thomas A. Geoffroy.


NOTARY PUBLIC
State of Florida

Personally known or Produced Identification
Type of identification produced _____

My commission expires:

