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Public Service Commission

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

DATE: June 2, 2011

TO: Office of Commission Clerk (Cole)

FROM: Division of Regulatory Analysis (Graves, Ma)
Division of Economic Regulation (Draper, D. Lee, Lester)
Office of the General Counsel (Robinson Evans)

RE: Docket No. 110041-EI – Petition for approval of Amendment No. 1 to generation services agreement with Gulf Power Company, by Florida Public Utilities Company.

AGENDA: 06/14/11 – Regular Agenda – Proposed Agency Action – Interested Persons May Participate

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: ~~Administrative~~ Brisé

CRITICAL DATES: Amendment conditioned upon receipt of final non-appealable order by July 31, 2011.

SPECIAL INSTRUCTIONS: The items for Florida Public Utilities Company should be considered together in the following order: Docket No.100459-EI, then Docket No. 110041-EI, and finally Docket No. 110001-EI.

FILE NAME AND LOCATION: S:\PSC\RAD\WP\110041.RCM.06-14-11.DOC

Case Background

Florida Public Utilities Company (FPUC) provides electric utility service to customers located in two sections of north Florida. The Northwest Division serves Jackson, Calhoun, and Liberty Counties. The Northeast Division is located in the Fernandina Beach area and serves Nassau County. FPUC does not generate any of the power it sells, but meets the needs of its

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customers through purchased power contracts. FPUC recovers its prudently incurred purchased power costs through the Fuel and Purchased Power Cost Recovery Clause (fuel clause).

On December 28, 2006, FPUC and Gulf Power Company (Gulf) executed a purchased power contract for generation service, which was effective January 1, 2008, for power supply to FPUC's Northwest Division over a ten-year period (Existing Agreement). Pursuant to Order No. PSC-07-0476-PAA-EI, the Commission approved the Existing Agreement.[1] On January 26, 2011, FPUC filed a petition requesting approval to amend its existing purchased power agreement (Amendment) with Gulf. The terms of the Amendment are expressly conditioned upon the receipt of a final, non-appealable order of the Amendment no later than July 31, 2011.

The Existing Agreement and the proposed Amendment are wholesale arrangements, therefore, jurisdiction of the terms and rates rest with the Federal Energy Regulatory Commission. The Commission has jurisdiction to determine the regulatory treatment of the costs and/or savings associated with implementing the Existing Agreement and the Amendment.

On February 11, 2011, the City of Marianna (City) which is located in Jackson County, filed a petition to intervene. On February 28, 2011, the Commission granted the City intervention in this docket.[2]

The Commission has jurisdiction over this subject matter pursuant to Section 366, Florida Statutes (F.S.).

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[1] See Order No. PSC-07-0476-PAA-EI, issued June 6, 2007, in Docket No. 070108-EI, In re: Petition for approval of agreement for generation services and related terms and conditions with Gulf Power Company for Northwest Division (Marianna) beginning 2008, by Florida Public Utilities Company.

[2] See Order No. PSC-11-0137-PCO-EI, issued February 28, 2011, in Docket No. 110041-EI, In re: Petition for approval of Amendment No. 1 to generation services agreement with Gulf Power Company, by Florida Public Utilities Company.

Discussion of Issues

Issue 1: Should the Commission approve Florida Public Utilities Company's petition for approval of amendment to the agreement for generation services between Gulf Power Company and Florida Public Utilities Company for purposes of fuel cost recovery calculations?

Recommendation: Yes. The proposed Amendment is projected to result in a savings of nearly $6 million through 2017 for FPUC and its customers. (Graves, Draper, Ma)

Staff Analysis: Currently, FPUC's bills are approximately 20 percent greater than any other Florida investor-owned utility, therefore, cost reductions in the near term are desirable. The Existing Agreement does not terminate until the end of 2017, therefore, absent an amendment to the Existing Agreement, any rate reduction would not be achievable until that time.

The proposed Amendment contains two significant changes to the current Agreement: (1) an immediate reduction in FPUC's monthly capacity payment; and (2) a two-year extension of the term of the Existing Agreement. In its petition to intervene, the City stated that the Commission should deny approval of the Amendment for cost recovery. The City believes the rates to be charged under the Amendment in years 2018 and 2019 are excessive and will result in FPUC's rate being unfair, unjust, and unreasonable. The City also believes the structure of the demand and energy charges are inappropriate.

The Existing Agreement contains a ratchet provision based on historic peak demand values. If actual demand requirements are reduced in the future through conservation, or load control measures such as time-of-use and interruptible rates, there is no corresponding reduction in the capacity payments to Gulf. The current minimum capacity purchase quantity (97,944 kW) was set beginning in 2008, and was established considering FPUC's peak demand during the period 2004 through 2007. Weather conditions and relatively favorable rates resulted in elevated capacity demand levels during the 2004 through 2007 time period. FPUC's actual peak demand since 2007 has declined, however, the ratchet provision contained in the Existing Agreement has maintained the capacity purchase quantity at 97,944 kW since 2008. Absent the ratchet provision, FPUC's purchase amount in 2009 and 2010 would have been 89,807 kW and 87,797 kW, respectively.

The proposed Amendment eliminates the ratchet provision and reduces the minimum capacity purchase quantity from the current level of 97,944 kW to 91,000 kW. Therefore, the capacity purchase quantity can rise above the minimum in any particular year, however, if the capacity purchase quantity subsequently reverts back to 91,000 kW or lower, FPUC will again be billed for 91,000 kW. Based on current projections, the proposed reduction in the capacity purchase quantity would result in a savings of nearly $6 million for FPUC and its customers through 2017. Table 1 below, summarizes the projected savings that would result from the Amendment and the impact on a residential customer's bill.

Table 1: Savings Associated with the Proposed Amendment[3]

Year	Projected Annual Savings ($)	Projected Residential Bill Reduction ($/1,000 kWh)	Projected Residential Bill Reduction ($/1,200 kWh)
2011	724,954	2.59	3.10
2012	749,952	2.67	3.21
2013	791,616	2.82	3.38
2014	837,446	2.99	3.59
2015	879,110	3.13	3.75
2016	929,107	3.32	3.99
2017	974,938	3.49	4.19
Total	**5,887,123**	-	-

As described, the Amendment extends Gulf's services to FPUC an additional two years. The capacity rates for 2018 and 2019 are escalated at a rate comparable to the escalation rates for the years contained in the Existing Agreement. FPUC explained that the companies discussed numerous options, but ultimately, near term reductions were only achievable through an extension of the Existing Agreement. Recognizing that Gulf had little, if any, incentive to agree to any changes that would result in lowering its revenues from the Existing Agreement, staff believes the proposed two-year extension is reasonable and necessary to provide the benefits articulated above.

Regarding the City's concerns, staff would note that the Existing Agreement was approved based on the evaluation and outcome of a bid process. Given that the Existing Agreement does not terminate until the end of 2017, it is not reasonable to conclude that a similar process several years into the future would yield results that would out-weigh the projected savings of the proposed Amendment. Furthermore, the City identified the ratchet provision as a feature that is contributing to high rates and the Amendment eliminates that feature.

Conclusion

Staff believes near-term rate reductions for FPUC are desirable. As discussed above, the proposed Amendment is projected to result in a savings of nearly $6 million through 2017 for FPUC and its customers. Moreover, staff believes that the modifications to the capacity purchase quantity provides the pricing flexibility necessary to develop conservation, or load control measures such as time-of-use and interruptible rates.

[3] In Order No. PSC-11-0112-TRF-EI, issued February 11, 2011, in Docket No. 100459-EI, the Commission approved FPUC's proposal to allocate up to 55 percent of the projected annual savings to time-of-use and interruptible rates. Therefore, the actual reduction in a residential customer's bills may be less.

Issue 2: Should this docket be closed?

Recommendation: Yes. If no person whose substantial interests are affected by the proposed agency action files a protest within 21 days of the issuance of the Order, this docket should be closed upon the issuance of a Consummating Order. (Robinson Evans)

Staff Analysis: At the conclusion of the protest period, if no protest is filed this docket should be closed upon the issuance of a Consummating Order.