

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:** November 22, 2016

**TO:** Office of Commission Clerk (Stauffer)

**FROM:** Division of Economics (Rome, Guffey, Draper)  
Division of Accounting and Finance (D. Buys)  
Office of the General Counsel (Leathers)

*Handwritten initials: CAR, SKG, ESD, DAB, ALM, and others.*

**RE:** Docket No. 160175-GU – Petition for review and determination on the project construction and gas transportation agreement between NUI Utilities, Inc. d/b/a City Gas Company of Florida and Florida Crystals Corporation, and approval of an interim service arrangement.

**AGENDA:** 12/06/16 – Regular Agenda – Interested Persons May Participate

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** Patronis

**CRITICAL DATES:** None

**SPECIAL INSTRUCTIONS:** None

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## Case Background

On July 22, 2016, Florida City Gas (FCG or City Gas) filed a Petition for Review and Determination on the “Project Construction and Gas Transportation Agreement (GTA) between NUI Utilities, Inc. d/b/a City Gas Company of Florida and Florida Crystals Corporation dated April 24, 2001” and Approval of an Interim Service Arrangement. City Gas is an investor-owned natural gas utility subject to the Commission’s jurisdiction per Section 366.02(1), Florida Statutes, (F.S.). Florida Crystals Corporation (Florida Crystals or Crystals) is a national sugar manufacturer.

The GTA was executed by City Gas and Florida Crystals on April 24, 2001, and has a 30-year term. However, City Gas never submitted the GTA for Commission review and approval. The

purpose of the GTA was for City Gas to construct, own, and operate a lateral pipeline from its transmission network to the Okeelanta Plant of Florida Crystals and provide natural gas transportation service to Florida Crystals. Florida Crystals began taking transportation service pursuant to the GTA in January 2002 and both parties have abided by the terms and negotiated rates of the GTA since its execution. The GTA contains a Primary Term, a Make-Up Period, and an Extended Term. The rates of the Extended Term differ from the rates applicable during the prior two terms. City Gas states that the Extended Term of the GTA will commence in January 2017 and its analysis shows that for the next 15 years of the Extended Term the cost to serve Florida Crystals will substantially exceed projected revenues, and therefore the revenue shortfall to City Gas will be very significant.

City Gas in its petition is requesting that the Commission take the following actions: (1) determine that the GTA is not a legally effective and enforceable special contract under Florida law because the GTA was never submitted to the Commission for its review or approval and the terms of the Extended Term do not meet the Commission's rules and City Gas's tariff requirements for a special contract, (2) approve an interim service arrangement until the Commission approves a new agreement that complies with Florida law, and (3) take no further action with respect to City Gas's past performance under the GTA unless the Commission determines that such action is required, but in no event is a fine or other penalty appropriate.

City Gas further asserts in its petition that in the absence of an approved special contract, beginning January 1, 2017, City Gas, as required by law, will have to charge Crystals the applicable tariff rate (GS-1,250k rate schedule), which is much higher than the negotiated GTA rate. Therefore, FCG is requesting an interim service arrangement as presented in the petition which should remain in effect until the Commission approves a successor GTA. v

On August 5, 2016, Florida Crystals filed a Motion to be Designated a Party, or in the alternative, a Motion to Intervene. This motion is addressed in Issue 1.

On August 29, 2016, Crystals filed a Motion to Dismiss City Gas's petition. The reasons asserted by Crystals are: (1) the GTA is a valid contract and did not require filing because it was covered by and complied with City Gas's applicable tariffs, specifically the KTS rate schedule, (2) City Gas informed the Commission of the GTA in its 2003 rate case and stated in expert testimony that the negotiated rate with Crystals recovers its costs to provide service, (3) any attempt to reverse the Commission's approval of the GTA rates as supported by City Gas's expert witness is barred by the administrative finality, (4) GTA provides for rates that are fully compliant with City Gas's tariff, specifically with the KDS rate schedule (the successor to the KTS rate schedule), (5) only Florida courts can determine the validity of a contract and the Commission lacks the jurisdiction to grant City Gas's requested relief of determining that the GTA is not legally effective, (6) City Gas violated its own tariff and Rule 25-9.034, Florida Administrative Code (F.A.C.), and then asks the Commission to allow City Gas's own failures to enable City Gas to escape its contractual obligation, and (7) City Gas's claim that its other customers could be harmed if City Gas does not recover higher amounts from Crystals is not an issue in this proceeding as City Gas has not pleaded that it requires relief to earn an adequate return. The Motion to Dismiss is addressed in Issue 3.

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On August 29, 2016, Florida Crystals requested oral argument on its Motion to Dismiss City Gas's petition. Crystals' request for oral argument is addressed in Issue 2.

On August 31, 2016, City Gas filed a Motion for Approval of a Temporary Interim Service Arrangement, including the rates presented in Confidential Exhibit No. 3. Such temporary interim service arrangement would remain in effect until the Commission issues a final order in this docket, or the Commission issues a successor transportation arrangement. If the Commission does not approve the interim service arrangement or approve a successor program, City Gas, as required by law would charge Crystals the applicable tariff rate (rate schedule GS 1,250k) effective January 1, 2017. The proposed Temporary Interim Service Arrangement is addressed in Issue 5.

On September 19, 2016, Crystals filed a Request for Oral Argument on its response in opposition to the Motion for Approval of a Temporary Interim Service Arrangement. Crystals' request for oral argument is addressed in Issue 4.

On September 19, 2016, City Gas filed a response in opposition to Crystals' Motion to Dismiss City Gas's petition. City Gas requested the Commission deny Crystals' Motion to Dismiss the petition because: (1) the GTA is a non-binding agreement because it was not approved by the Commission, (2) the petition is well pled, and (3) states a cause of action upon which the Commission may grant relief to Crystals.

On September 19, 2016, Crystals filed a response in opposition to the motion for approval of a temporary interim service arrangement. Crystals states that City Gas's entire case is predicated on the basis that the GTA is invalid, City Gas is trying to extract more money from Crystals which has paid in excess of the cost to serve, and that City Gas is evading its obligations pursuant to the GTA.

On October 10, 2016, staff issued its First Data Request to City Gas and to Crystals. City Gas provided partial, non-confidential responses on October 28, 2016. Staff received complete responses from both parties on November 1, 2016.

On October 18, 2016, staff issued a Notice of Apparent Violation to City Gas. City Gas responded on November 1, 2016 and Florida Crystals filed Comments concerning City Gas's Response to Notice of Apparent Violation on November 17, 2016.

On November 4, 2016, after review of City Gas's newly filed, revised, confidential data, staff issued an informal meeting notice. On November 15, 2016, staff held a noticed meeting with City Gas and Crystals to discuss the discovery responses. The Commission has jurisdiction over this matter pursuant to Sections 366.04, 366.05, and 366.06, F.S.

### Discussion of Issues

**Issue 1:** Should the Commission grant Florida Crystals' Motion to be Designated a Party or in the Alternative Motion to Intervene?

**Recommendation:** No. The Commission should deny Florida Crystals' Motion to be Designated a Party or in the Alternative Motion to Intervene because intervention is premature and unnecessary at this time. (Leathers)

**Staff Analysis:** On July 22, 2016, FCG filed its Petition for Review and Determination and Approval of an Interim Service Arrangement (Petition) asking the Commission to find that the GTA is not legally effective or enforceable because its terms do not meet the Commission's rules and statutes or FCG's tariff requirements for a special contract. FCG also requested that the Commission approve FCG's proposed interim service arrangement set forth in the Petition until the Commission approves a new service agreement as successor to the GTA. On August 5, 2016, Florida Crystals' filed its Motion to be Designated a Party or in the Alternative Motion to Intervene, pursuant to Chapters 120 and 366, F.S., and Rules 25-22.036, 25-22.039, 28-106.201, and 28-106.205, F.A.C. Florida Crystals states that as FCG's counterparty to the GTA and as the customer for whom FCG is attempting to establish an interim service arrangement for future gas transportation services, Florida Crystals is a necessary, indispensable party and its substantial interests will be directly affected by the issues raised in this docket. Florida Crystals requests party or intervenor status so that it may file responsive pleadings and otherwise fully participate in Docket No. 160175-GU.

Section 120.57, F.S., sets forth the provisions applicable to hearings involving disputed issues of material fact. Determinations as to intervention or party status are appropriate for proceedings conducted pursuant to Section 120.57, F.S. However, subsection (5) of the statute does not apply to agency investigations preliminary to agency action. This is precisely the posture this docket is currently in: a proceeding preliminary to Commission action, for which intervention or determinations as to party status are premature. Interested persons may participate at the Agenda Conference on Issue 5, pursuant to Rule 25-22.0021(2), F.A.C. The Commission invites broad participation in preliminary proceedings in order to better inform itself of the scope and implications of its decisions.<sup>1</sup> Florida Crystals may participate fully in this proceeding, including filing its motion to dismiss and other responses and having them considered by the Commission, without intervening in this proceeding.

Further, substantially affected persons will have the opportunity to request a hearing pursuant to Sections 120.569 and 120.57, F.S., once the Commission's order is issued. For the reasons explained above, formal intervention by Florida Crystals, pursuant to Chapter 120, F.S., is premature and unnecessary at this time. Staff therefore recommends that the Commission deny Florida Crystals' Motion to be Designated a Party or in the Alternative Motion to Intervene.

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<sup>1</sup> Order No. PSC-12-0139-PCO-WS, issued on March 26, 2012, Docket No. 110264-WS, *In re: Application for increase in water and wastewater rates in Pasco County by Labrador Utilities, Inc.*, (Order Denying Motion to Intervene in PAA Proceeding); Order No. PSC-14-0311-PCO-EM, issued on June 13, 2014, in Docket No. 140059-EM, *In re: Notice of new municipal electric service provider and petition for waiver of Rule 25-9.044(2), F.A.C.*, by *Babcock Ranch Community Independent School District*.

**Issue 2:** Should the Commission grant Florida Crystals' Request for Oral Argument on its Motion to Dismiss Petition?

**Recommendation:** Yes. The Commission should grant Florida Crystals' Request for Oral Argument on its Motion to Dismiss Petition. Staff recommends allowing each side 10 minutes to address this matter. (Leathers)

**Staff Analysis:** Rule 25-22.0022(7)(a), F.A.C., provides that oral argument at an Agenda Conference will only be entertained for recommended orders and dispositive motions (such as a motion to dismiss). A request for oral argument must be filed concurrently with the motion on which argument is requested, as has been done here. Rule 25-22.0022(1), F.A.C. In its Response in Opposition to Florida Crystals' Motion to Dismiss Petition, FCG stated that it did not object to the request if the Commission finds that oral argument will assist with the Commission's understanding and evaluation of the issues related to the Motion to Dismiss Petition.

Rule 25-22.0022(3), F.A.C., provides that granting or denying a request for oral argument is within the sole discretion of the Commission. The Commission has traditionally granted oral argument upon a finding that oral argument would aid the Commission in its understanding and disposition of the underlying motion. Furthermore, the Commission invites broad participation in PAA or preliminary proceedings in order to better inform itself of the scope and implications of its decisions.<sup>2</sup> Staff believes that the Commissioners would benefit from oral argument on Florida Crystals' Motion to Dismiss the Petition. Accordingly, staff recommends that the Commission grant Florida Crystals' Request for Oral Argument with respect to the Motion to Dismiss addressed in Issue 3. Staff further recommends that if the Commission decides to hear oral argument, Florida Crystals and FCG should each be allowed 10 minutes to address the Commission on this matter.

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<sup>2</sup> Order No. PSC-12-0139-PCO-WS; Order No. PSC-14-0311-PCO-EM.

**Issue 3:** Should the Commission grant Florida Crystals' Motion to Dismiss Petition?

**Recommendation:** No. The Commission should deny Florida Crystals' Motion to Dismiss Petition because the Petition states a cause of action upon which relief may be granted. (Leathers)

**Staff Analysis:**

**Standard of Review**

A motion to dismiss challenges the legal sufficiency of the facts alleged in a petition to state a cause of action.<sup>3</sup> In order to sustain a motion to dismiss, the moving party must show that, accepting all allegations as true, the petition fails to state a cause of action for which relief may be granted.<sup>4</sup> The moving party must specify the grounds for the motion to dismiss, and all material allegations must be construed against the moving party in determining if the petitioner has stated the necessary allegations.<sup>5</sup> A sufficiency determination should be confined to the petition and documents incorporated therein, and the grounds asserted in the motion to dismiss.<sup>6</sup> Thus, "the trial court may not look beyond the four corners of the complaint, consider any affirmative defenses raised by the defendant, nor consider any evidence likely to be produced by either side."<sup>7</sup> Finally, all allegations in the petition must be viewed as true and in the light most favorable to the petitioner in order to determine whether there is a cause of action upon which relief may be granted.<sup>8</sup>

**FCG's Petition**

On July 22, 2016, FCG filed a petition with the Commission requesting the review and determination of the legal effectiveness and enforceability of the GTA, along with approval of an interim service arrangement. FCG alleges that the GTA was negotiated and signed by prior management and that key elements of the development and implementation of the GTA remain unknown because the employees involved in the transaction are no longer with the company. FCG acknowledges that the GTA was never submitted to the Commission for approval, pursuant to Rule 25-9.034, F.A.C., but that FCG and Florida Crystals have apparently followed the terms of the GTA for nearly 15 years.

While FCG asserts that its management first became aware of the GTA in 2010-2011 during the course of Docket No. 090539-GU (Miami-Dade docket), it did not fully understand when the Extended Term of the GTA would begin until Florida Crystals exceeded its transportation volume cap in 2015. As a result of the subsequent legal, regulatory, and financial analyses and the lack of Commission approval, FCG petitioned the Commission to determine that the GTA is

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<sup>3</sup> *Meyers v. City of Jacksonville*, 754 So. 2d 198, 202 (Fla. 1st DCA 2000); *Varnes v. Dawkins*, 624 So. 2d 349, 350 (Fla. 1st DCA 1993).

<sup>4</sup> *Varnes v. Dawkins*, 624 So. 2d at 350.

<sup>5</sup> *Matthews v. Matthews*, 122 So. 2d 571 (Fla. 2nd DCA 1960).

<sup>6</sup> *Barbado v. Green and Murphy, P.A.*, 758 So. 2d 1173 (Fla. 4th DCA 2000); *Varnes v. Dawkins*, 624 So. 2d at 350; Rule 1.130 Florida Rules of Civil Procedure.

<sup>7</sup> *Varnes v. Dawkins*, 624 So. 2d at 350.

<sup>8</sup> See e.g., *Ralph v. City of Daytona Beach*, 471 So. 2d 1, 2 (Fla. 1983); *Orlando Sports Stadium, Inc. v. State ex rel Powell*, 262 So. 2d 881, 883 (Fla. 1972); *Kest v. Nathanson*, 216 So. 2d 233, 235 (Fla. 4th DCA 1968); *Ocala Loan Co. v. Smith*, 155 So. 2d 711, 715 (Fla. 1st DCA 1963).

not a legally effective or enforceable special contract and approve FCG's proposed interim service arrangement for Florida Crystals in lieu of the Extended Term of the GTA until the issuance of a final order by the Commission or the parties negotiate an appropriate special contract to be submitted for Commission approval. FCG supported its Petition by stating that the Extended Term of the GTA consists of a rate that is substantially below FCG's cost to serve, thereby making it impossible to serve Florida Crystals under the GTA rates. Accordingly, FCG maintains that the Commission has not only the authority, but the responsibility to step in and prevent the Extended Term rates from going into effect.

FCG further appears to assert that the GTA should have been submitted to the Commission for approval, pursuant to Rule 25-9.034, F.A.C., prior to its execution. FCG cited the Commission's finding in the Miami-Dade docket stated that: "[the Commission has] exclusive, superior authority over the rates and charges of FCG, a regulated public utility. Pursuant to Rule 25-9.034(1), F.A.C., all special contracts and agreements entered into by a public utility that are not specifically covered by its filed tariff must be approved by this Commission."<sup>9</sup> Furthermore, FCG averred that, "another fundamental tenant of Florida law establishes that utility contracts remain subject to PSC oversight throughout their tenure and that the PSC has the authority to later terminate or amend a contract that is no longer compliant with the law."<sup>10</sup>

FCG stated that its general body of ratepayers has not been adversely impacted by service to Florida Crystals and that FCG management has acted in good faith to remedy this situation in a manner that will not adversely impact its general body of ratepayers or Florida Crystals.

### **Florida Crystals' Motion to Dismiss Petition**

On August 29, 2016, Florida Crystals filed its Motion to Dismiss Petition. Florida Crystals argues that FCG's Petition should be dismissed because:

- No basis in law or fact exists for the relief requested by FCG, as the rates set forth in the GTA were covered by and consistent with FCG's Rate Schedule KTS at the time the GTA was negotiated and, therefore, FCG was not required to obtain Commission approval of the GTA pursuant to Rule 25-9.034(1), F.A.C.;
- FCG expressly represented to Florida Crystals that the Commission's approval was not required and that FCG communicated that it would effectively waive regulatory approvals;
- The Commission approved the rates paid by Florida Crystals in FCG's 2003 rate case when FCG induced the Commission to approve its Rate Schedule KDS as the successor to Rate Schedule KTS and averred in expert testimony that "[t]he Company's negotiated

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<sup>9</sup> Quoting Order No. PSC-10-0671-PCO-GU, issued on November 5, 2010, in Docket No. 090539-GU, *In re: Petition for approval of Special Gas Transportation Service agreement with Florida City Gas by Miami-Dade County through Miami-Dade Water and Sewer Department.*

<sup>10</sup> *Miller & Sons, Inc. v. Hawkins*, 373 So. 2d 913 (Fla. 1979).

rate contract with Florida Crystals establishes a rate that recovers its costs to provide service”;<sup>11</sup>

- The doctrine of administrative finality bars FCG from overturning the Commission’s approval of its rates in its 2003 rate case;
- FCG’s assertion that the GTA is inconsistent with its tariff is false because it is impossible for Florida Crystals to ever pay a rate less than 1 cent per therm for transportation service as the average rate paid for the service under the GTA can never be less than 1.2 cents per therm;
- FCG fails to state a claim upon which relief can be granted because the Commission lacks the jurisdiction to grant its request as jurisdiction to interpret contracts between parties rests exclusively with the judicial courts of Florida;
- The Commission cannot allow FCG to “bootstrap” its admitted violations of Commission rules to escape the consequences of FCG’s prior representations to the Commission or deprive Florida Crystals the benefit of its bargain;
- FCG’s suggestion that its other customers will be harmed if the Commission does not allow it to charge Florida Crystals a higher rate is not at issue in this proceeding and any claims to an entitlement to a rate increase would have to be established in an appropriate general rate case proceeding.

Florida Crystals attached Exhibits A, B, and C in support of its Motion to Dismiss Petition. Staff believes that Exhibit C is evidentiary in nature because it provides facts not included in FCG’s Petition and disputes FCG’s statements. Therefore, Florida Crystals’ Exhibit C is not discussed or considered in staff’s analysis in this recommendation.<sup>12</sup>

### **FCG’s Response in Opposition to Florida Crystals’ Motion to Dismiss Petition**

On September 19, 2016, FCG filed a response to Florida Crystals’ Motion to Dismiss Petition. In its response, FCG asserts that its Petition properly states a cause of action upon which relief may be granted and that Florida Crystals’ Motion to Dismiss Petition should be denied as its arguments consist of affirmative defenses not pleading deficiencies. Specifically, FCG maintains that Florida Crystals’ motion should be denied because:

- Florida Crystals’ argument that the rates set forth in the GTA were covered by and consistent with FCG’s Rate Schedule KTS at the time the GTA was negotiated reflects disputed issues of fact and law and is, therefore, an affirmative defense. Further, that FCG is obligated to request the Commission’s review of the GTA as each of the respective rate periods are not consistent with Rate Schedule KDS;
- Florida Crystals’ Exhibit C does not meet the standards for a motion to dismiss and that “no public utility has the unilateral power to waive its tariff, Rule 25-9.034, or this Commission’s authority under Chapter 366”;

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<sup>11</sup> Quoting Direct Testimony of Jeff Householder, August 15, 2003, page 77, Docket No. 030569-GU, *In re: Application for rate increase by City Gas Company of Florida*. (Document No. 07495-03)

<sup>12</sup> See *Varnes v. Dawkins*, 624 So. 2d at 350.



- Florida Crystals' argument that the GTA is not a special contract requiring Commission approval pursuant to Rule 25-9.034(1), F.A.C., is an affirmative defense contrary to the language of the rule and the Commission's underlying statutory authority over public utility rates;
- Florida Crystals' argument that FCG obtained the Commission's approval of the GTA rates through FCG's 2003 rate case is an affirmative defense, not a demonstration that the Petition fails to state a cause of action, noting that nothing in that rate case directly or indirectly meets the requirements of Rule 25-9.034(1), F.A.C., as the GTA was never filed, reviewed, or approved, and that Florida Crystals cannot point to any part of that order that contains any of the GTA rates. Further, that Florida Crystals' submission of testimony and evidence from the 2003 rate case looks outside the four corners of FCG's Petition;
- Florida Crystals' argument that the doctrine of administrative finality bars FCG from overturning the Commission's approval of its rates in its 2003 rate case fails because there has been no final order on the GTA rates, the doctrine of administrative finality permits an agency to revisit a prior decision when there is a demonstration of changed facts and circumstances, and it is an affirmative defense that reaches beyond the four corners of the Petition;
- Florida Crystals' argument that the GTA is subject to general contract law and not the Commission's authority is an affirmative defense and does not meet the requirements for dismissal;
- The failure to previously obtain approval of the GTA does not bar FCG's Petition and that the statements made in the 2003 rate case, or at any other prior time, were based upon whatever the company's then management thought appropriate are irrelevant and are perhaps affirmative defenses;
- Florida Crystals' argument that FCG should file a general rate case in order to change its rates is not a basis for dismissal as the instant issue is whether the GTA recovers its cost per the rule, not whether FCG is meeting its revenue requirements.

### **Analysis**

When viewed within the "four corners of the complaint" exclusive of all affirmative defenses/responses, assuming all alleged facts are true, and in the light most favorable to FCG, staff believes that the Petition states a cause of action that would invoke the Commission's jurisdiction or permit the Commission to grant the relief requested. Specifically, the Petition contains sufficient allegations to allow the Commission to review the GTA and determine whether it is subject to the Commission's approval as prescribed by Rule 25-9.034(1), F.A.C. For these reasons, staff recommends that the Commission deny Florida Crystals' Motion to Dismiss Petition.

**Issue 4:** Should the Commission grant Florida Crystals' Request for Oral Argument on its Response in Opposition to Motion for Approval of a Temporary Interim Service Arrangement?

**Recommendation:** No. The Commission should not grant Florida Crystals' Request for Oral Argument on its Response in Opposition to Motion for Approval of a Temporary Interim Service Arrangement. However, staff recommends that the parties be permitted to participate informally on this issue. (Leathers)

**Staff Analysis:** Rule 25-22.0022(3), F.A.C., provides that granting or denying a request for oral argument is within the sole discretion of the Commission. Rule 25-22.0022(7)(a), F.A.C., provides that oral argument at an Agenda Conference will only be entertained for recommended orders and dispositive motions. Because Florida Crystals' Response in Opposition to Motion for Approval of a Temporary Service Arrangement does not comport with any of the provisions of Rule 25-22.0022(7)(a), F.A.C., staff believes that oral argument is inappropriate. However, the Commission invites broad participation in PAA or preliminary proceedings in order to better inform itself of the scope and implications of its decisions.<sup>13</sup> Therefore, pursuant to Rule 25-22.0021(2), F.A.C., staff believes Florida Crystals should be permitted to participate informally with respect to Issue 5 of this recommendation.

Accordingly, staff recommends that the Commission deny Florida Crystals' Request for Oral Argument with respect its Response in Opposition to Motion for Approval of a Temporary Interim Service Arrangement addressed in Issue 5. However, staff recommends that the parties be permitted to participate informally on this issue.

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<sup>13</sup> Order No. PSC-12-0139-PCO-WS; Order No. PSC-14-0311-PCO-EM

**Issue 5:** Should the Commission approve City Gas's Motion for Approval of the Temporary Interim Service Arrangement including the revised Interim Rates filed on November 1, 2016 in Confidential Exhibit 3A?

**Recommendation:** No. The Make-Up Period GTA rates should be in effect for a transition period beginning on the date of the Commission vote on this recommendation until a final Commission decision in this docket. If City Gas and Crystals are able to negotiate within the transition period a mutually agreeable operating agreement, it should be brought before the Commission for a decision. If City Gas and Crystals are unable to negotiate a mutually agreeable operating arrangement within the transition period, City Gas should be required to file a limited proceeding by July 31, 2017, for the purpose of determining the appropriate cost basis for contract rates. Revenues collected via the temporary rates during the transition period should be subject to refund with interest based on the Commission's final order in this docket. (Rome, Draper, D. Buys)

**Staff Analysis:** The following discussion is predicated on the assumption that the Commission adopts staff's recommendation on Crystals' Motion to Dismiss in Issue 3. If the Commission approves Crystals' Motion to Dismiss, this issue is moot.

### **Background**

As chronicled in the case background, the parties to the GTA have filed pleadings in which numerous assertions were made pertaining to factual circumstances and points of law regarding which the parties provided differing interpretations. Staff does not attempt to adjudicate each point of contention for purposes of this recommendation. As discussed below, staff believes that the overarching objective at this time is to recommend an interim solution under which the parties to the GTA can continue to operate and collaborate on a permanent solution.

The term of the GTA<sup>14</sup> is divided into three basic intervals: Primary Term, Make-Up Period, and Extended Term. City Gas represented that the Extended Term begins on January 1, 2017. Crystals provided documentation in its November 1, 2016 response to staff's first data request to support its representation of a November 15, 2016 start date for the GTA's Extended Term. Staff believes that the documentation provided by Crystals adequately supports the assertion regarding a November 15, 2016 start date for the Extended Term. The contract rates that Crystals would pay under the Extended Term differ from the contract rates applicable during the Primary Term and Make-Up Period. Staff's analysis in this issue focuses on whether the contract rates during the Extended Term would cover City Gas's cost to serve Crystals on a going-forward basis. The Extended Term has a 15-year term ending in 2032. Therefore, the determination of appropriate prospective contract rates is important due to the length of the remaining duration of the GTA.

### **Prospective Coverage of Cost of Service**

In conjunction with its petition filed on July 22, 2016, City Gas provided information to support its assertion that the Extended Term contract rates would not cover the cost to serve Crystals on a going-forward basis. In its August 31, 2016 Motion for Approval of a Temporary Interim Service Arrangement, City Gas provided temporary rates set forth in the Company's original petition in

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<sup>14</sup> City Gas requested confidential treatment of the GTA in its entirety on July 25, 2016; Document No. 05536-16.

which City Gas stated that based upon its recent experience, “transportation service for Florida Crystals can be net profitable at rates below the tariff rate.”<sup>15</sup>

However, in its November 1, 2016 response to staff’s first data request, City Gas provided revised information which indicated that from its inception in 2002, the GTA has not covered the cost to serve Crystals. City Gas also provided revisions to the proposed temporary interim rates that it avers would be necessary to cover the cost to serve (*i.e.*, superseding the rates in the proposed Temporary Interim Service Arrangement).

In its September 19, 2016 Response in Opposition to Motion for Approval of a Temporary Interim Service Arrangement, Crystals asserted that the Extended Term rates generate revenues that are significantly greater than City Gas’s true incremental costs to serve. Crystals suggested that the true incremental costs of serving the Okeelanta facility are at most City Gas’s operation and maintenance (O&M) costs. Crystals stated that comparing City Gas’s projected O&M costs to the revenues that City Gas expects to receive under the Extended Term GTA rates shows that the projected revenues exceed the true incremental costs of service.<sup>16</sup>

When staff evaluates whether or not special contract rates such as those contained in the GTA are sufficient to cover the cost of service, staff reviews the support provided for all the costs associated with serving the customer. These costs include the utility’s required return on investment (rate base times rate of return), O&M expense, depreciation expense, state income taxes, federal income taxes, and taxes other than income taxes (primarily property taxes). Staff disagrees with Crystals’ assertion that the consideration should be limited to the projected O&M costs.

At the noticed meeting with City Gas and Crystals on November 15, 2016, staff discussed the differences between City Gas’s November 1, 2016 representation that the GTA has never covered the cost to serve and the testimony of City Gas’s expert witness in City Gas’s 2003 rate case which stated that “The Company’s negotiated rate contract with Florida Crystals establishes a rate that recovers its cost to provide service.”<sup>17</sup> City Gas represented to staff that its current presentation on the cost to serve Crystals is based on the best available information.

While the above mentioned inconsistency in historical information is a concern to staff, staff focuses in this recommendation on whether or not the rates in the GTA will cover City Gas’s cost to serve Crystals on a going-forward basis. Based on the confidential information provided by City Gas, staff believes that City Gas has made a reasonable demonstration that the GTA contract rates under the Extended Term would not cover the cost to serve. Staff suggests that Commission action is appropriate at this time due to Crystals’ assertion that the Extended Term commences on November 15, 2016. Staff has developed four potential options for consideration; these options are discussed below.

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<sup>15</sup> City Gas’s July 22, 2016 petition; page 20.

<sup>16</sup> Crystals’ Response in Opposition to Motion for Approval of a Temporary Interim Service Arrangement; pp. 20-22.

<sup>17</sup> Direct Testimony of Jeff Householder, August 15, 2003, page 77, Docket No. 030569-GU, *In re: Application for rate increase by City Gas Company of Florida*. (Document No. 07495-03)

### **Discussion of Potential Courses of Action**

The four options discussed below are presented in the order of least preferred to recommended option. All options are predicated on the assumption that the Commission adopts staff's recommendation in Issue 3.

#### ***Option 1 – Tariff Rate***

If the Commission were to take no further action in this docket prior to January 1, 2017, City Gas stated that pursuant to Section 366.06(1), F.S., and Rule 25-9.034, F.A.C., it would be required to begin charging Crystals the applicable tariff rate as of January 1, 2017.<sup>18</sup> Staff does not recommend this option as it appears the applicable rate contained in the GS-1,250k rate schedule would cause a significant adverse financial impact to Crystals. City Gas also agreed that the application of the tariff would impose a significant hardship to Crystals and the tariff does not adequately address a customer like Crystals.<sup>19</sup> Therefore, staff does not recommend this option.

#### ***Option 2 – Revised Temporary Interim Rate (FCG Proposal)***

City Gas proposed interim rates in its Motion for Approval of a Temporary Interim Service Arrangement (Confidential Exhibit No. 3) and revised interim rates in its response to staff's first data request (Confidential Exhibit No. 3A). Based on the information in City Gas's data request response, staff believes that the proposed interim rates as revised would cover the cost to serve Crystals. However, staff also believes that City Gas potentially could recover its cost of service at rates that would be more favorable to Crystals. Staff further recognizes that it appears that the implementation of Option 2 would cause a significant adverse financial impact to Crystals; although, the impact would be less severe than the impact that would result from the implementation of Option 1. Furthermore, based on its preliminary analysis of the revised interim rates, staff does not agree with a key assumption regarding Crystals' therm usage used by City Gas in the calculation. Therefore, staff does not recommend this option.

#### ***Option 3 – Extended Term Contract Rate (Crystals Proposal)***

If the Commission were to deny City Gas's Motion for Approval of a Temporary Interim Service Arrangement including the revised interim rates, the Commission has the option to allow the Extended Term contract rates stated in the GTA to take effect. This option would enable Crystals to receive the Extended Term rates as set forth in the GTA. However, as stated above, staff believes that the Extended Term contract rates do not cover City Gas's cost to serve Crystals on a going-forward basis; therefore, staff does not recommend this option.

#### ***Option 4 – Make-up Period GTA Rate (Staff Recommended)***

If the Commission were to deny City Gas's Motion for Approval of a Temporary Interim Service Arrangement including the revised interim rates, the Commission has the option to leave the Make-Up Period GTA rates in effect beginning on the date of the Commission's vote on this recommendation until a final Commission decision on this matter. Although Crystals would not realize the benefits of the Extended Term rates during the transition period, it would continue to pay the same current Make-Up Period rates and avoid the adverse financial impacts that would occur under Options 1 and 2. Based on information provided by City Gas, staff believes that City

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<sup>18</sup> City Gas's Motion for Approval of a Temporary Interim Service Arrangement; p. 4.

<sup>19</sup> City Gas's July 22, 2016 petition; page 7.

Gas's under-recovery of the cost of service during the transition period under Option 4 would be less than the under-recovery that would occur under Option 3.

### **Possible Refunds**

Staff reviewed the financial condition of City Gas consistent with staff's recommendation that any revenues collected by City Gas from Florida Crystals during the transition period be held subject to refund pending a final Commission decision on the appropriate contract rates in the docket. To review City Gas's financial condition, staff performed an analysis similar to a corporate undertaking. The total corporate undertaking amount staff assumed in its analysis is the difference between City Gas's proposed Temporary Interim Service Arrangement Rate as revised and the Extended Term Contract Rate for one year. Staff notes that depending on the Commission vote on this issue (i.e., appropriate rates for transition period), the length of the transition period, and the final outcome and associated contract rates in the docket, the amount of a refund, if any, will likely vary.

City Gas is an operating division of Pivotal Utility Holdings, Inc., (Pivotal) which is a wholly-owned subsidiary of Southern Company Gas (formerly known as AGL Resources, Inc.) which is a wholly-owned direct subsidiary of Southern Company. Pivotal finances its on-going cash requirements through its participation in Southern Company Gas's Utility Money Pool currently in the amount of \$800 million. City Gas's available share of the Utility Money Pool is up to \$250 million.

The criteria for a corporate undertaking include sufficient liquidity, ownership equity, profitability, and interest coverage to guarantee any potential refund. Staff reviewed Pivotal's 2013, 2014, and 2015 financial statements to determine if the company can support a corporate undertaking in the amount required. In its 2013, 2014, and 2015 financial statements, Pivotal reported insufficient liquidity based on staff's criteria for a corporate undertaking. Pivotal reported negative working capital, a current ratio of less than one, and an interest coverage ratio less than two times. However, in the instant case, Pivotal's liquidity is not an issue due to its ability to access up to \$250 million from Southern Company Gas's Utility Money Pool to fund its on-going cash requirements. Further, Pivotal achieved a three-year average net income significantly greater the corporate undertaking amount indicating sufficient profitability. In addition, Pivotal reported adequate ownership equity over the entire 3-year review period.

Based on staff's review of Pivotal's financial statements, staff believes the company has adequate resources to guarantee any potential refund of revenues collected by FCG under interim conditions.

Further, in no instance should the maintenance and administrative costs associated with the potential refund be borne by Crystals. These costs are the responsibility of, and should be borne by City Gas. Irrespective of the form of security chosen by City Gas, an account of all monies received as a result of the temporary rates should be maintained by FCG. If a refund is ultimately required, it should be paid with interest calculated pursuant to Rule 25-7.091(4), F.A.C.

### **Conclusion**

Staff recommends Option 4 in an effort to provide a balanced temporary solution to allow City Gas and Crystals additional time to negotiate a mutually acceptable operating arrangement. If requested by the parties, Commission staff would be willing to facilitate any negotiations. Staff

encourages City Gas and Florida Crystals to negotiate a mutually acceptable operating arrangement. If the parties are not able to reach an agreement during the transition period, the Commission then would render a final decision on appropriate contract rates within the context of the limited proceeding.

To conclude, the Commission should deny City Gas's motion for Approval of a Temporary Interim Service Arrangement including the revised Interim Rates filed on November 1, 2016 in Confidential Exhibit 3A. The Make-Up Period GTA rates should be in effect for a transition period beginning on the date of the Commission's vote on this recommendation until a final Commission decision in this docket. If City Gas and Crystals are able to negotiate in the transition period a mutually agreeable operating agreement, it should be brought before the Commission for a decision. If City Gas and Crystals are unable to negotiate a mutually agreeable operating arrangement within the transition period, City Gas should be required to file a limited proceeding by July 31, 2017, for the purpose of determining the appropriate cost basis for contract rates. Revenues collected via the temporary rates during the transition period should be subject to refund with interest based on the Commission's final order in this docket.

**Issue 6:** Should this docket be closed?

**Recommendation:** No. This docket should remain open to allow City Gas and Crystals an opportunity to negotiate a mutually agreeable operating arrangement and until the Commission makes a final decision on the arrangement. If City Gas and Crystals are unable to negotiate an arrangement, this docket should continue to remain open until a limited proceeding to resolve the matter can be completed and a consummating order is issued. (Leathers)

**Staff Analysis:** This docket should remain open to allow City Gas and Crystals an opportunity to negotiate a mutually agreeable operating arrangement and until the Commission makes a final decision on the arrangement. If City Gas and Crystals are unable to negotiate an arrangement, this docket should continue to remain open until a limited proceeding to resolve the matter can be completed and a consummating order is issued.