BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into 1996 earnings of Florida Public Utilities Company - Marianna Division.	DOCKET NO. 971228-EI ORDER NO. PSC-97-1487-FOF-EI ISSUED: November 24, 1997

The following Commissioners participated in the disposition of this matter:

JULIA L. JOHNSON, Chairman
J. TERRY DEASON
SUSAN F. CLARK
DIANE K. KIESLING
JOE GARCIA

NOTICE OF PROPOSED AGENCY ACTION
ORDER DETERMINING AND DISPOSING
OF EXCESS EARNINGS

BY THE COMMISSION:

NOTICE is hereby given by the Florida Public Service Commission that the action discussed herein is preliminary in nature and will become final unless a person whose interests are substantially affected files a petition for a formal proceeding, pursuant to Rule 25-22.029, Florida Administrative Code.

By letter dated May 7, 1996, Florida Public Utilities Company-Marianna Division ("Marianna" or "Company") agreed to cap the earnings of the Marianna Division at 11.85% for calender year 1996. The disposition of any excess earnings was left to the discretion of this Commission. The Company did, however, reserve the right to request alternative dispositions, such as additional contributions to its storm damage reserve or the reduction of any depreciation reserve deficiencies.

Our continuing earnings surveillance program showed that the Company's earnings were within five basis points of its maximum authorized return on equity (ROE) of 11.85%. Accordingly, our staff conducted an earnings audit of the Company's books and records and issued an audit report on July 10, 1997. The Company's response to the audit was received on July 30, 1997.

By letter dated October 3, 1997, the Company agreed with our staff's calculation of 1996 excess earnings of $36,143, plus interest of $1,005. The Company requested that the total amount of $37,148 in excess earnings be contributed to the Storm Damage Reserve in Marianna.

Rate Base

In its December 1996 Earnings Surveillance Report, the Company reported a total "FPSC Adjusted" rate base of $12,389,266. This amount should be adjusted as shown in Attachment 1 to yield the Company's appropriate rate base for determining its 1996 excess earnings.

The Company did not overearn in 1995 but estimated that it would overearn by $49,000 in 1996. The Company reduced revenues $49,000 to cover the estimated 1996 overearnings. (An adjustment for this item is addressed below.) The 13-month average of this amount, or $3,769, was included by the Company in working capital. In order to accurately determine 1996 overearnings, the $3,769 should be removed from working capital, which results in an increase in working capital. Based on this adjustment, the Company's appropriate rate base for determining its 1996 excess earnings is $12,393,035.

Rate of Return

For purposes of measuring excess earnings, the appropriate overall rate of return for the Company is 8.67%. This rate is based on the Company's return on equity (ROE) cap of 11.85% and accounts for its 13-month average capital structure of $3,769 for the period ending December 31, 1996.

The 13-month average capital structure of $3,769 is appropriately treated as deferred revenue in the capital structure. This amount represents excess earnings for 1996. (The treatment of excess earnings as an item in the capital structure is consistent with the treatment of deferred revenue in the recent earnings review of Tampa Electric Company. See Order No. PSC-97-0436-FOF-EI, issued April 17, 1997.) Pursuant to Rule 25-6.109, Florida Administrative Code, the cost rate on deferred revenue is the 30 day commercial paper rate, which in this case is 5.70%.

In Order No. PSC-94-0170-FOF-EI, issued February 10, 1994, the Commission established the return on common equity for Marianna as 10.85%, with a range of 9.85% to 11.85%. Using the 11.85% cap, the weighted average cost of capital should be 8.67%, as shown in Attachment 2. This is the appropriate rate of return to measure excess earnings.

We note that, in its earnings surveillance report, the Company removed its investment in Flo-Gas entirely from common equity in a manner consistent with previous cases. The Company specifically identified deferred taxes, investment tax credits, and customer deposits.

Net Operating Income

In its December 1996 Earnings Surveillance Report, the Company reported an "FPSC Adjusted" net operating income of $1,068,684. This amount should be adjusted as shown in Attachment 1 to yield the Company's appropriate net operating income for determining its 1996 excess earnings.

First, the Company made an error of $11,880 in the allocation of medical self insurance expenses between the Marianna Division and Flo-Gas. Flo-Gas is a wholly-owned unregulated subsidiary of Florida Public Utilities Company. This error caused expenses for Marianna to appear lower than they actually were. To reflect the proper charges for Marianna, expenses should be increased by $11,880.

Second, the Company included interest earning cash in working capital but did not include the related interest income of $1,506 in revenues. In Order No. PSC-94-0170-FOF-EI, we determined that interest income should be included in revenues if the interest bearing cash is included in working capital. Therefore, operating revenues should be increased by $1,506.

Third, the Company booked a $49,000 provision for Rate Refund in December 1996, thereby reducing the reported operating revenues for 1996. As discussed in Issue 1, this amount should be reversed to determine the total amount of excess earnings for 1996.

Fourth, in its earnings surveillance report, the Company showed a negative cash position for the 13 months ending December 31, 1996. The Company therefore made an adjustment to reduce its revenues by an allocated amount of $6,795. The Company's rationale was that if it had to add interest income to revenues for any interest earned on a positive cash position, it could impute negative interest earned on a negative balance of cash and make a corresponding reduction to revenues. The Company stated that the interest income adjustment was properly reported pursuant to Order No. PSC-94-0170-FOF-EI.

We disagree with the Company's adjustment. The Company did not pay any interest on the negative balance of cash and should not make reductions to revenue to take advantage of this fact. Order No. PSC-94-0170-FOF-EI simply states that interest earned on interest bearing cash allowed in working capital is to be included in revenues; the Order does not address Company adjustments to revenue for imputed negative interest. We note that many companies routinely carry negative balances of cash due to aggressive cash management policies; a negative balance of cash does not necessarily indicate cash flow or other financial problems. Therefore, $6,795 should be added back to operating revenues.

Finally, based on a reconciliation of the Company's rate base and capital structure, made necessary by the adjustment to the Company's rate base, above, income taxes should be decreased by $130.

As a result of these adjustments, the Company's appropriate net operating income for 1996, for purposes of determining 1996 excess earnings, is $1,097,132.

Excess Earnings

Based on our findings above, we find that the Company's 1996 excess earnings are $36,143, plus interest of $1,005, as shown in Attachment 3. This represents an earned ROE of 12.38%, which exceeds the maximum authorized ROE of 11.85%.

Disposition of Excess Earnings

As of December 1996, the total Storm Damage Reserve for Marianna amounted to $201,527. The approved level of this reserve was addressed in Order No. PSC-94-0170-FOF-EI in Marianna's last rate case. In that Order, we authorized a storm damage reserve of $1 million, with an annual accrual of $100,000. The total amount in this reserve is presently inadequate and will continue to be for the next several years. Therefore, the $37,148 of excess earnings should be included in Marianna's Storm Damage Reserve.

Since these excess earnings occurred during 1996 and interest has only been calculated for that year, the increase in this reserve should be made effective January 1, 1997, for all regulatory purposes. This treatment will eliminate the need for the calculation of any additional amounts of interest and will include the increased reserve in the determination of earnings for 1997.

Based on the foregoing, it is

ORDERED by the Florida Public Service Commission that Florida Public Utilities Company - Marianna Division's 1996 excess earnings are appropriately calculated to total $37,148 and shall be contributed to the Division's Storm Damage Reserve effective January 1, 1997, for regulatory purposes. It is further

ORDERED that the provisions of this Order, issued as proposed agency action, shall become final and effective unless an appropriate petition, in the form provided by Rule 25-22.036, Florida Administrative Code, is received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on the date set forth in the "Notice of Further Proceedings or Judicial Review" attached hereto. It is further

ORDERED that in the event this Order becomes final, this Docket shall be closed.

By ORDER of the Florida Public Service Commission this 24th day of November, 1997.

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BLANCA S. BAYÓ, Director
Division of Records and Reporting

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NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.569(1), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Mediation may be available on a case-by-case basis. If mediation is conducted, it does not affect a substantially interested person's right to a hearing.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25-22.029(4), Florida Administrative Code, in the form provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 2540 Shumard Oak Boulevard, Tallahassee, Florida 32399-0850, by the close of business on December 15, 1997.

In the absence of such a petition, this order shall become effective on the day subsequent to the above date as provided by Rule 25-22.029(6), Florida Administrative Code.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days of the effective date of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

ATTACHMENT 1
F_ORIDA PUBLIC UTILITIES COMPANY
MARIANNA ELECTRIC DIVISION
DOCKET NO. 971228-EI
REVIEW OF 1996 EARNINGS

	As Filed FPSC Adjusted Basis	Underalloc. Medical Self Insurance [X4]	Include Interest Income on Bank Bal. [AD 2]	Provision for Rate Refund	Reverse Imputed Interest Income	Interest Reconciliation	Total Adjustments	Total Adjusted Rate Base
RATE BASE								
Plant in Service	$20,128,766						0	$20,128,766
Accumulated Depreciation	7,469,061						0	7,469,061
Net Plant in Service	12,659,705	0	0	0	0	0	0	12,659,705
Property Held for Future Use	0						0	0
Construction Work in Progress	145,999						0	145,999
Net Utility Plant	12,805,704	0	0	0	0	0	0	12,805,704
Working Capital	(416,438)			3,769			3,769	(412,669)
Total Rate Base	$12,389,266	$0	$0	$3,769	$0	$0	$3,769	$12,393,035
INCOME STATEMENT								
Operating Revenues	$5,483,425		$1,506	$49,000	$6,795		$57,301	$5,540,726
Operating Expenses:							0	0
Operation & Maintenance - Fuel	(2)						0	(2)
Operation & Maintenance - Other	2,226,439	11,880					11,880	2,238,319
Depreciation & Amortization	757,785						0	757,785
Taxes Other Than Income	1,145,172						0	1,145,172
Income Taxes - Current	194,705	(4,470)	567		2,557	(130)	(1,477)	193,228
Deferred Income Taxes (Net)	114,627			18,450			18,450	133,077
Investment Tax Credit (Net)	(23,985)						0	(23,985)
(Gain)/Loss on Disposition	0						0	0
Total Operating Expenses	4,414,741	7,410	567	18,450	2,557	(130)	28,853	4,443,594
Net Operating Income	$1,068,684	($7,410)	$939	$30,550	$4,238	$130	$28,448	$1,097,132
EQUITY RATIO	43.52%						0.00%	43.52%
OVERALL RATE OF RETURN	8.63%						0.23%	8.85%
RETURN ON EQUITY	11.80%						0.58%	12.38%

ATTACHMENT 2
FLORIDA PUBLIC UTILITIES COMPANY
MARIANNA ELECTRIC DIVISION
DOCKET NO. 971228-EI
REVIEW OF 1996 EARNINGS

CAPITAL STRUCTURE

AS FILED - FPSC ADJUSTED	Amount	Ratio	Cost Rate	Weighted Cost
Long Term Debt	$4,362,060	35.21%	9.97%	3.51%
Short Term Debt	1,069,402	8.63%	6.19%	0.53%
Preferred Stock	114,894	0.93%	4.75%	0.04%
Customer Deposits	568,107	4.59%	6.30%	0.29%
Common Equity	4,273,679	34.50%	11.85%	4.09%
Deferred Income Taxes	1,754,691	14.16%	0.00%	0.00%
Tax Credits - Zero Cost	1,082	0.01%	0.00%	0.00%
Tax Credits - Weighted Cost	245,351	1.98%	10.32%	0.20%
Total	$12,389,266	100.00%		8.67%

ADJUSTED	Amount	Adjustments: Specific	Adjustments: Pro Rata	Adjusted Total	Ratio	Cost Rate	Weighted Cost
Long Term Debt	$4,362,060			$4,362,060	35.20%	9.97%	3.51%
Short Term Debt	1,069,402			1,069,402	8.63%	6.19%	0.53%
Preferred Stock	114,894			114,894	0.93%	4.75%	0.04%
Customers Deposits	568,107			568,107	4.58%	6.30%	0.29%
1996 Deferred Revenue	0	3,769		3,769	0.03%	5.70%	0.00%
Common Equity	4,273,679			4,273,679	34.48%	11.85%	4.09%
Deferred Income Taxes	1,754,691			1,754,691	14.16%	0.00%	0.00%
Tax Credits - Zero Cost	1,082			1,082	0.01%	0.00%	0.00%
Tax Credits - Weighted Cost	245,351			245,351	1.98%	10.32%	0.20%
Total	$12,389,266	$3,769	$0	$12,393,035	100.00%		8.67%

INTEREST RECONCILIATION

	Amount	Cost Rate	Interest Exp.	Tax Rate	Effect on Income Tax
Long Term Debt	4,362,060	9.97%	434,897		
Short Term Debt	1,069,402	6.19%	66,196		
Customer Deposits	568,107	6.30%	35,791		
1996 Deferred Revenue	3,769	5.70%	215		
Tax Credits - Weighted Cost	245,351	5.10%	12,513		
Staff Interest Expense			549,612		
Company Interest Expense			549,267		
Staff Adjustment			(345)	37.63%	(130)

ATTACHMENT 3

FLORIDA PUBLIC UTILITIES COMPANY
MARIANNA ELECTRIC DIVISION
DOCKET NO. 971228-EI
REVIEW OF 1996 EARNINGS

Adjusted Rate Base			$12,393,035
Achieved Rate of Return	8.85%		
Maximum Rate of Return	8.67%		
Excess Rate of Return		X	0.18%
Excess Net Operating Income			22,307
Revenue Expansion Factor		X	1.6202
Excess Revenues			$36,143