State of Florida

Public Service Commission

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

DATE: AUGUST 24, 2000

TO: DIRECTOR, DIVISION OF RECORDS AND REPORTING (BAYÓ)

FROM: DIVISION OF SAFETY AND ELECTRIC RELIABILITY (BREMAN, LEE, MCNULTY)
DIVISION OF LEGAL SERVICES (STERN)
DIVISION OF ECONOMIC REGULATION (D. DRAPER, E. DRAPER, LEE, MAUREY, SWAIN)

RE: DOCKET NO. 000685-EI - PETITION OF TAMPA ELECTRIC COMPANY FOR APPROVAL OF A NEW ENVIRONMENTAL PROGRAM FOR COST RECOVERY THROUGH THE ENVIRONMENTAL COST RECOVERY CLAUSE.

AGENDA: 09/05/00 - REGULAR AGENDA - PROPOSED AGENCY ACTION - INTERESTED PERSONS MAY PARTICIPATE

CRITICAL DATES: NONE

SPECIAL INSTRUCTIONS: NONE

FILE NAME AND LOCATION: S:\PSC\SER\WP\000685.RCM

CASE BACKGROUND

On May 31, 1996, Tampa Electric Company (TECO) petitioned for Environmental Cost Recovery Clause treatment of the Big Bend Unit 3 Flue Gas Desulfurization Integration project, Docket No. 960688-EI. The project was necessary to reduce sulfur dioxide (SO_2) emission reductions as required by the Acid Rain section of the Clean Air Act. The Commission approved the Big Bend Unit 3 Flue Gas Desulfurization Integration project for recovery through the Environmental Cost Recovery Clause by Order No. (PSC-96-1048-FOF-EI, issued August 14, 1996)

On December 3, 1998, in Docket No. 980693-EI, the Commission approved TECO's petition for cost recovery of the Big Bend Units 1 and 2 Scrubber project through the Environmental Cost Recovery Clause. The project was necessary because Phase II of the Acid

Rain section of the Clean Air Act required additional SO_2 emission reductions. TECO argued that a flue gas desulfurization (FGD) unit serving both Big Bend Units 1 and 2 was the most cost-effective option to achieve the air emissions reduction. The Commission considered various key assumptions and analyses in reaching its decision such as alternatives to the single scrubber, fuel price forecasts, and projected environmental compliance costs for air, water and land pollutants. (PSC-99-0075-FOF-EI, issued January 11, 1999)

The United States Department of Justice, on behalf of the United States Environmental Protection Agency (EPA), filed a law suit against TECO, on November 3, 1999, alleging TECO violated the Prevention of Significant Deterioration (PSD) requirements at Part C of the Clean Air Act, 42 U.S.C. §§ 7470-7492. The EPA alleged that TECO was required to obtain a PSD permit and apply best available control technology (BACT) before proceeding with various power plant modifications which TECO completed between 1991 and 1996. The power plant modifications in question were replacements of boiler equipment such as steam drum internals, high temperature reheater, water wall, cyclone, and furnace floor.

The Florida Department of Environmental Protection (DEP) filed a lawsuit against TECO on December 7, 1999, which mirrored the EPA lawsuit. Shortly after DEP filed its lawsuit, TECO and DEP settled the suit by entering a Consent Final Judgment (CFJ). The CFJ became effective on December 16, 1999. The CFJ requires TECO to:

- Optimize the scrubber on Big Bend Station Units 1&2 to achieve 95% sulfur removal efficiency beginning year 2000.
- Maximize the availability of both scrubbers at Big Bend Station beginning in year 2000.
- Repower Gannon Station with natural gas by December 31, 2004.
- Install Selective Catalytic Reduction technology on the repowered Gannon units to achieve a emission rate for nitrogen oxides (NO_X) of 3.5 parts per million by December 31, 2004.
- Install retrofit NO_X controls, repower or shut down Big Bend Units 1&2 by the year 2007.
- Install retrofit NO_X controls, repower or shut down Big Bend Units 3&4 by the year 2010.
- Spend up to $8 million to control NO_X emissions with non-ammonia control technology or other combustion controls by December 31, 2004.
- Perform Best Available Control Technology analysis and optimization of the Big Bend Station electro-static precipitators by the year 2003.

- Install continuous emission measuring equipment for particulate matter on one Big Bend stack by May 1, 2003.
- Pay $2 million into the Tampa Bay Estuary (BRACE) program by year end 2002.
- Prohibit sale of NO_x emission allowances if such allowances are established by state or federal law.

On December 23, 1999, TECO filed a petition for Commission approval of its plan to comply with the Clean Air Act (Docket No. 992014-EI). TECO's proposed Clean Air Act compliance plan outlined the implementation requirements and timetables of the CFJ.

However, the EPA lawsuit remained unresolved even though TECO and DEP had reached settlement. TECO continued independent negotiations with the EPA to resolve the EPA's concerns. On February 29, 2000, TECO and the EPA signed a settlement agreement (Consent Decree). The Consent Decree was filed with the U.S. District Court in Tampa on February 29, 2000. The notice of lodging of the Consent Decree was published in the Federal Register on March 20, 2000, Volume 65, No.54.

The Consent Decree, includes the requirements of the CFJ, but modifies some of the CFJ compliance dates, provides more explicit instructions than the CFJ and goes beyond the CFJ in three areas. The three additional requirements of the Consent Decree are: a)TECO is prohibited from banking or selling SO_2 emission allowances; b)TECO is required to pay a one-time civil penalty of $3.5 million; and, c)TECO is required to spend up to $9 million on innovative or other combustion controls to reduce NO_x emissions at the Big Bend Station.

After entering the Consent Decree with the EPA, TECO filed with the Commission a Voluntary Dismissal and Withdrawal of the petition in Docket No. 992014-EI on March 1, 2000. The Commission closed Docket 992014-EI by Order PSC-000-0817-PAA-EI, issued April 25, 2000 without addressing TECO's proposed plan to implement the CFJ.

On June 2, 2000, TECO petitioned for approval of cost recovery of the Big Bend Units 1, 2, and 3 Flue Gas Desulfurization System Optimization and Utilization Program (FGD Plan) through the Environmental Cost Recovery Clause. TECO also seeks to include the actual year 2000 expenditures in their 2000 true-up amounts in the Environmental Cost Recovery Clause. TECO states that the FGD Plan costs will be allocated to rate classes on an energy basis because the program is a Clean Air Act compliance activity.

Jurisdiction over the subject mater of this petition is vested in the Commission by Section 366.8255, Florida Statues. Order No. PSC-94-0044-FOF-EI, issued January 12, 1994 in Docket No. 930613-EI, sets forth the criteria the Commission uses to administer Section 366.8255, Florida Statutes. Under the Commission's interpretation of the statute as expressed in Order No. PSC-94-044-FOF-EI, the Commission must first determine whether the project is eligible for recovery through the Environmental Cost Recovery Clause before cost recovery occurs. Therefore, pursuant to Order No. PSC-94-0044-FOF-EI and Section 366.8255, Florida Statutes, the instant docket was opened to address the eligibility of TECO's project for recovery through the Environmental Cost Recovery Clause.

DISCUSSION OF ISSUES

ISSUE 1: Is Tampa Electric Company's Big Bend 1,2, and 3 Flue Gas Desulfurization System Optimization and Utilization Program eligible for cost recovery through the Environmental Cost Recovery Clause?

RECOMMENDATION: Yes. (BREMAN, LEE, STERN)

STAFF ANALYSIS: The criteria used by the Commission in its administration of an Environmental Cost Recovery Clause (ECRC) petition is addressed in Order No. PSC-94-0044-FOF-EI, which states in part:

> 1. such costs were prudently incurred after April 13, 1993;
> 2. the activity is legally required to comply with a governmentally imposed environmental regulation enacted, became effective, or whose effect was triggered after the company's last test year upon which rates are based; and,
> 3. such costs are not recovered through some other cost recovery mechanism or though base rates. (p. 6-7)

A discussion of each of the three ECRC criterion identified above in Order is presented in sections (1), (2), and (3) respectively. This discussion is followed by a section which addresses other matters in TECO's petition related to cost recovery schedules and rate impacts. The final section is a summary statement recommending approval of TECO's petition.

1. Such costs were prudently incurred after April 13, 1993

This ECRC criterion limits cost recovery to prudently incurred costs which have occurred subsequent to the establishment of Section 366.8255, Florida Statutes on April 13, 1993. This ECRC criterion is substantially satisfied because none of TECO's FGD Plan expenses were incurred prior to calendar year 2000.

For purposes of the ongoing ECRC proceedings, this criterion limits cost recovery to those which are prudently incurred. As indicated in a following section, TECO must implement the FGD Plan as approved by the EPA. The EPA's final decision on TECO's proposed FGD Plan is not expected until some time in 2001. Consequently, the specific activities and costs listed in the FGD Plan may change. Program implementation issues, such as these, are

typically addressed in the ongoing ECRC proceedings and not necessary to resolve at this time.

2. The activity is legally required to comply with a governmentally imposed environmental regulation enacted, became effective, or whose effect was triggered after the company's last test year upon which rates are based

This section of Order No. PSC-94-0044-FOF-EI allows cost recovery for environmentally required activities but excludes activities which are elective, discretionary, or generally image enhancement activities.

The FGD Plan is a requirement of both the CFJ and the Consent Decree. The Consent Decree, at Paragraph 31 requires TECO to develop a plan addressing all operation and maintenance changes needed to maximize the availability of the existing scrubbers at Big Bend Units 1,2, and 3. The plan may be in two phases. TECO elected to proceed with a two phased plan. The first phase consisting of overtime and spare parts inventories has been submitted to the EPA and approved. TECO anticipates filing phase II of the FGD Plan with the EPA in the spring of 2001. EPA will have 60 days to issue its decision. TECO must receive prior written approval from the EPA before implementing any changes to the FGD Plan.

TECO's settlement with the DEP does not require a detailed FGD Plan. Section V(D) of the CFJ simply states that TECO "...shall maximize scrubber utilization on all four boilers." Because the FGD Plan is a direct requirement of the Consent Decree at Paragraph 31, it is reasonable to conclude that the FGD Plan also satisfies the more general requirements of the CFJ.

Based on the forgoing analysis, staff believes TECO's petition satisfies the ECRC criterion that the proposed activity is legally required.

3. Such costs are not recovered through some other cost recovery mechanism or though base rates

The purpose of this ECRC criterion is to ensure that the environmental compliance costs are incremental to those used in setting current base rates.

TECO's current base rates were set in Docket No. 920324-EI. The 1992 rate case addressed the cost of scrubbing only Big Bend Unit 4. At that time of TECO's last rate case, TECO was not

projected to incur costs associated with scrubber facilities at Big Bend Units 1, 2 or 3 because scrubber facilities were not planned for those generating units at that time. As previously stated, the Consent Decree and the CFJ require TECO to implement the FGD Plan. The implementation of the FGD Plan began in calendar year 2000. Therefore, the FGD Plan costs were not considered when TECO's base rates were set.

Bases on the above analysis, staff believes that the environmental compliance costs are incremental to those used in setting current base rates.

Cost recovery schedules and rate impact

Subject to Commission approval, FGD Plan costs will be included in the cost recovery true-up filings for calendar year 2000 and in the projections for calendar year 2001. TECO's most recent estimates of the FGD Plan costs are listed in the tables below. TECO'S updated FGD Plan estimate of $1,615,000 for O&M activities is $20,000 less than the their estimate included with the petition. The level of capital investment to implement the FGD Plan is still projected to be $5,130,000.

Approximately $261,000 in capital expenditures and approximately $936,000 for O&M activities were incurred prior to June 2, 2000 when TECO filed this petition. TECO admits in items 12 and 13 of its petition that some costs to implement its FGD Plan were incurred by the time TECO filed this petition. Recovery of these incurred costs is addressed in Issue 2.

Table 1

Big Bend Unit 1&2 FGD Activities			
Description	Projected Completion Date	Cost ($000)	
		Capital	O&M
Preventive Maintenance	12/1/00		250
Oxidation Air Control Improvements	12/1/00		10
Tower Water,Air,Reagent & Startup Piping Upgrade	12/1/00	100	25
Sub Total		100	285

Table 2

Big Bend Unit 3 FGD Activities			
Description	Projected Completion Date	Cost ($000)	
		Capital	O&M
Duct Work Improvements	10/1/00	50	100
Quencher System Improvements	10/1/00		165
Electrical System Reliability Improvements	12/1/00	310	80
Tower Control Improvements	12/1/00	10	10
DBA System Improvements	6/1/01	25	150
Booster Fan Reliability Improvements	6/1/01	930	40
Tower Piping, Nozzle, and internal improvements	6/1/01	230	110
Absorber System Improvements	6/1/01	420	415
Tower Demister (packing) Improvements	6/1/01	530	
Sub Total		2,505	1,070

Table 3

Common Support System Projects			
Description	Projected Completion Date	Cost ($000)	
		Capital	O&M
Limestone Supply Reliability Improvements	6/1/01	1,120	100
Gypsum De-Watering Improvements	6/1/01	100	10
Stack Reliability Improvements	6/1/01	275	50
Waste Water Treatment Reliability Improvements	12/1/01	1,030	120
Sub Total		2,525	280

Item 16 of TECO's Petition states that TECO is not requesting a mid-course change in the ECRC factors for year 2000. Based on the available information, it appears there will not be a significant rate impact. The actual program expenditures will be addressed in the November 2000 ECRC hearing and will be subject to audit.

Item 17 of TECO's Petition states that TECO will be allocating the cost of the FGD Plan to rate classes on an energy basis because the program is a Clean Air Act compliance activity. The Commission determined in 1994, that costs for Clean Act Compliance Activities should be allocated to rate classes on an energy basis. This has been Commission practice since the guidelines were established in Order No. PSC-94-0393-FOF-EI, issued April 6, 1994. Program implementation issues, such as this one, are typically addressed in the ongoing ECRC proceedings and not necessary to resolve at this time.

F. Conclusions

Based on the forgoing review of TECO's FGD Plan and application of the Commission's ECRC criteria to TECO's FGD Plan, staff recommends the Commission find the FGD Plan eligible for cost recovery through the ECRC.

ISSUE 2: Should costs incurred prior to June 2, 2000, the date TECO filed its petition, be recovered through the ECRC, pursuant to Order No. PSC-94-1207-FOF-EI?

RECOMMENDATION: No. Section 366.8255(2), Florida Statutes, only allows for recovery of prospective costs. In addition, TECO was not subjected to "extraordinary circumstances" as defined in Order No. PSC-94-1207-FOF-EI. However, TECO may include the costs incurred prior to June 2, 2000, in its surveillance reports. (STERN)

STAFF ANALYSIS: Section 366.8255(2), Florida Statutes, provides:

> An electric utility may submit to the Commission a petition describing the utilities proposed environmental compliance activities and projected environmental costs... (Emphasis added.)

Staff interprets this section of the statute to mean that if a utility chooses to submit a petition, it may do so only for anticipated future costs, not for costs already incurred.

In Order No. PSC-94-1207-FOF-EI, issued October 3, 1994, in Docket No. 940042-EI, the Commission stated, "environmental compliance cost recovery, like recovery through other cost recovery clauses, should be prospective." In that Order the Commission recognized that it might find exceptions to the prospective costs requirement in "extraordinary circumstances." The Commission stated that whether extraordinary circumstances existed would be determined case-by-case, based on the facts of each case. The key to determining extraordinary circumstances is "whether the utility could reasonably have anticipated the changes [in environmental regulations] and the costs." Examples of extraordinary circumstances provided in the Order were rapidly changing laws, imposition of unanticipated costs, and environmental emergencies.

Through interrogatories, staff brought the problem of incurred costs to TECO's attention. TECO explained that it had to implement parts of the Consent Decree immediately, due to time schedules in the Consent Decree and the previously scheduled outage of Big Bend Unit 3. The unit had to be altered to meet the requirements of the Consent Decree and the most efficient time to do it was during a planned outage. The Consent Decree was signed in February and the outage had been scheduled to occur in March and April, 2000. If TECO had not acted immediately, it would have had to schedule another outage.

TECO also explained that it wanted to avoid recovering costs associated with FGD optimization and utilization in a piecemeal fashion and so it chose to request recovery of the FGD activities "under one program." TECO further explained that the outage provided an opportunity to perform the required work and afforded the best means to comply an estimate of the initial scope and costs for compliance with the FGD Plan.

First, it is incumbent upon TECO to incur costs prudently if it wants to recover those costs through any mechanism. It appears that TECO acted responsibly by making the required improvements to Unit 3 during a previously planned outage. However, TECO can not recover all environmental costs that are prudently incurred through the ECRC. TECO can only recover costs that are prudent and prospective or prudent and incurred under extraordinary circumstances through the ECRC. Some of TECO's costs may have to be recovered through base rates.

Second, staff sees nothing extraordinary in TECO's situation. The settlement agreement did not result from regulations that changed too quickly or costs that could not be anticipated. TECO participated in settlement negotiations for months and had input into the requirements of the agreement. That TECO entered a settlement agreement is also not extraordinary. Companies whose operations have potential to cause significant environmental degradation are often required to address allegations that they violated environmental regulations. The alleged violations are more often resolved through settlements than through hearings or trials. Finally, there was no emergency.

In summary, TECO's request for recovery of costs incurred prior to June 2, 2000, should be denied because TECO was not subject to extraordinary circumstances, as defined by the Commission, and the costs are not prospective, as required by Section 366.8255, Florida Statutes.

ISSUE 3: Should this docket be closed?

RECOMMENDATION: Yes, this docket should be closed upon issuance of a Consummating Order unless a person whose substantial interests are affected by the Commission's decision files a protest within 21 days of the issuance of the proposed agency action. (STERN)

STAFF ANALYSIS: If no timely protest to the proposed agency action is filed within 21 days of the date of issuance of the Order, this docket should be closed upon the issuance of a Consummating Order.