



February 3, 2023

The Honorable Andrew Giles Fay
Chairman
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

**Re: Peoples Gas System, Inc. - Test Year Notification
Pursuant to Rule 25-7.140, Florida Administrative Code**

Dear Chairman Fay,

Peoples Gas System, Inc. (“Peoples” or the “company”) proudly continues to support the growth and economic vitality of Florida by providing safe, reliable, and clean natural gas to Floridians while evolving with changing energy markets and maintaining exceptional customer service. However, strong customer demand, the impacts of inflation, and higher costs of capital have significantly impacted the company’s operations.

After careful consideration, Peoples has concluded that it is necessary to seek rate relief. This letter is notice to the Florida Public Service Commission (“Commission”) that Peoples intends to petition for a general base rate increase on April 4, 2023, for new rates effective January 2024, and that the company proposes to use projected calendar year 2024 as the test period in that proceeding.

About Peoples

Peoples is expanding its system as Florida grows. The company was formed in 1895 and is the largest natural gas local distribution company in Florida. Through its 14 service areas, the company safely and reliably serves approximately 470,000 residential, commercial, industrial, and electric power generation customers in 39 of Florida’s 67 counties, including five major metropolitan areas. Peoples is a subsidiary of Emera Incorporated (“Emera”), a geographically diverse energy and services company headquartered in Halifax, Nova Scotia, Canada. Emera also owns our affiliate, Tampa Electric Company (“Tampa Electric”).

Florida’s Remarkable Growth

Florida’s growth has been remarkable, especially over the past few years. The state’s abundant natural resources, favorable tax system, balanced approach to regulation, and other thoughtful policy choices have helped make Florida one of the fastest-growing states in America. Florida is a national leader in new business formation and net population in-migration. While other states

have experienced population declines, Florida's population is expected to be 22.6 million people in 2024, up 1 million since January 1, 2021.

Florida's population growth means: more new home construction; more hotels, hospital, stores, and restaurants; new and expanded roads and other construction; and more gas-fired electricity generation. As Florida grows, Peoples must: invest in new mains, laterals, service lines, and meters; hire team members to operate and maintain a growing system; and spend money building, upgrading, and moving the company's gas distribution infrastructure to accommodate construction. Peoples believes these activities are necessary to serve customer demand and support Florida's competitiveness.

Here are some measures of Peoples' system expansion:

From January 1, 2021, to December 31, 2022, Peoples added approximately 40,000 (10 percent) and approximately 1,500 (four percent) new residential and commercial customers, respectively. The company expects to add almost 28,000 new residential and approximately 1,200 new commercial customers from January 2023 to December 2024.

From January 2021 to December 2022, the company added approximately 1,200 miles of main and services and anticipates adding approximately 1,000 miles from January 2023 to December 2024. Residential sales for 2024, measured in therms, are expected to be up 12 percent over 2021 actuals.

The investments required to support this remarkable expansion contribute to the company's need for rate relief as do the demands of changing energy markets.

Changing Energy Markets

Peoples is a *local* gas distribution company, but its operations are influenced by weather, political activity, and economic factors around the world - all of which are beyond the company's control. Although natural gas prices recently have been more volatile, the abundant supply of domestic natural gas has reduced the cost of natural gas well below levels a decade ago and made the United States a major exporter of natural gas. Customer demand for natural gas is high in Florida because it is affordable, reliable, and safe, and while some states have attempted to restrict the use of natural gas, policymakers in Florida have wisely preserved natural gas as a choice for consumers. Natural gas has also replaced coal as the primary fuel for generating electricity in the state.

Gas customers in all classes are demanding faster and more reliable service, more information, and the ability to communicate with Peoples using multiple communication platforms. They also want alternative ways to receive natural gas such as liquefied natural gas ("LNG") and compressed natural gas ("CNG"), and innovative, Florida-sourced, carbon-friendly renewable energy solutions like renewable natural gas ("RNG").

Peoples has been an industry leader and has embraced these changes by: focusing on safety and outstanding customer service; supporting the growth and economic vitality of Florida; serving the natural gas needs of electric generators; advancing the growth of RNG, LNG, and CNG; and

striving to keep its customer rates fair, just, reasonable, and competitive relative to other energy options.

Commitment to Safety and Customer Service

The safety of Peoples' team members, contractors, customers, and the public is paramount. The company's commitment to exceptional customer service runs a close second. Peoples is proud of its record in both areas.

On the safety side, the company's Occupational Safety and Health Administration (OSHA) injury rate for team members and contractors is an industry low. Peoples was awarded the Industry Leader Accident Prevention Award from the American Gas Association for a DART (days away, restricted, or transferred) incidence rate below the industry average in 2022. Peoples also received Gold Shovel Standard Certification for its use of underground damage prevention best practices and has required the same of its strategic partners. The company continues to have excellent Pipeline and Hazardous Materials Safety Administration ("PHMSA") compliance results.

Peoples has a record of outstanding customer service:

In 2022, the company ranked highest in the *south* midsize segment of the J.D. Power Gas Utility Residential Customer Satisfaction study for the 10th year in a row, and highest in the south segment of the Gas Utility Business Customer Satisfaction study for the fourth year in a row and sixth time since 2016.

Peoples has led the *nation* in the J.D. Power residential study in eight of the past ten years and ranked highest in the nation in the business study the past three years.

Peoples was named the Most Trusted Utility in the nation for the eighth time in the 2022 Cogent Syndicated Utility Trusted Brand & Customer Engagement: Residential study by Escalent.

Escalent also named Peoples a Trusted Business Partner (two consecutive years, one of the easiest utilities in the nation with which to conduct business, an Environmental Champion (eighth consecutive year), and a Customer Champion (ninth consecutive year).

Commitment to Sustainability and the Environment

Customer interest in sustainable and renewable energy continues to grow and has expanded beyond solar. To support Florida's clean energy future, Peoples is pursuing, and its rate case filing will include, three innovative RNG projects that will deliver sustainable, carbon-neutral, pipeline-quality gas made in Florida to customers in Florida. Projects like these reflect partnerships with farmers, counties, municipalities, and others to drive economic development, reduce methane emissions, and deliver Florida-sourced natural gas to customers.

For eleven years, the company has systematically replaced legacy pipe with new pipe through its Cast Iron Bare Steel/Problematic Plastic Pipe program ("CIBS/PPP"). This program has reduced gas leaks, lowered carbon emissions, and enhanced the efficiency of the company's distribution

system. The company also continues to support customers who seek CNG and LNG - oil and diesel alternatives – as part of their energy solutions.

Peoples Supports the Communities it Serves

Peoples has a strong track record of helping its customers through challenges caused by public health issues, volatile economic conditions, and severe weather. During the COVID-19 pandemic, Peoples and its team members supported customers and offered payment assistance to over 6,000 residential and commercial customers. These support activities included: (1) extensive outreach efforts; (2) implementation of modified payment arrangement guidelines to provide greater flexibility to customers; (3) revised service disconnection/reconnection guidelines; and (4) personal call follow-ups with customers who had not reconnected service after three days to offer creative options for assistance.

Because most of its natural gas infrastructure is underground and less susceptible to wind damage, Peoples' natural gas service provides significant energy resiliency benefits to Florida during severe weather. During Hurricane Ian, only about 800 of the company's customers experienced service disruptions, even though some of the company's territories were in the hardest hit areas. Backup generation fueled by natural gas allows hospitals, nursing homes, residential communities, and other essential services to continue operations during and after major storms.

Other Factors

Meeting the strong demand for natural gas, navigating changing markets, and increasing customer expectations has been challenging. Like other businesses, Peoples has experienced higher than expected inflation, labor market challenges, supply chain disruptions, and higher interest costs. Although the company has worked diligently to moderate them, the combined impact of growth and these factors is challenging the company's ability to continue to (1) safely and effectively operate and maintain its growing systems under current rates while (2) earning a fair rate of return on its investments. Consequently, Peoples finds itself with a need to petition for a general base rate increase as the term of its 2020 Agreement draws to a close.

Peoples' Last Rate Case

The company's last general rate case was filed on June 8, 2020, in Docket No. 20200051-GU, and yielded the Stipulation and Settlement Agreement approved by the Commission in Order No. PSC-2020-0485-FOF-GU, issued December 10, 2020, in Docket Nos. 20200051-GU, 20200166-GU, and 20200178-GU ("2020 Agreement"). This agreement authorized the company to implement new base rates and charges and established a return on equity ("ROE") midpoint of 9.90 percent with a range of 8.90 percent to 11.00 percent effective January 1, 2021. The base revenue increase of \$58 million included \$23.6 million of revenue requirements transferred from the CIBS/PPP Rider. The 2020 Agreement authorized Peoples to amortize \$34 million of depreciation reserve surplus as a credit to depreciation expense from 2020 through 2023.

Test Year Request

Peoples intends to seek general rate relief pursuant to the provisions of Section 366.06(3), Florida Statutes, as soon as the new rate schedules, the petition relating thereto, and the minimum filing requirements can be completed and filed. The company plans to file on April 4, 2023 and proposes to use a projected test year ending December 31, 2024, with a historic base year ending December 31, 2022. Given the expected impacts of future customer demand, inflation, and changes in the capital markets, the company's proposed 2024 test year will reasonably reflect the economic and operating conditions expected during the first 12 months that the company's proposed new rates will be in effect and will be more representative than a historic test year.

Peoples is finalizing its 2024 test year revenue requirement calculations but anticipates requesting a net incremental base rate revenue increase of approximately \$125 million to \$135 million, which excludes about \$12 million of revenue requirements transferred from the CIBS/PPP Rider. The company will not request interim rates or that its petition for rate relief be processed using the proposed agency action process authorized in Section 366.06(4), Florida Statutes.

Major Factors Necessitating a General Base Rate Increase

The major factors driving the need for a rate case include strong customer and rate base growth, plus associated increases in depreciation expenses, property taxes and operations and maintenance ("O&M") expenses to operate the company's system safely and reliably that are outpacing the company's revenue growth. As a result of these factors, which are largely driven by external forces, and to fulfill its obligation to serve, the company expects to earn below the bottom of its approved ROE range in 2023 and earn approximately two percent ROE in 2024 without rate relief.

1. Rate Base Growth

Peoples is committed to keeping up with Florida's remarkable growth. However, Peoples invests capital to meet growth and to: (1) improve the reliability, resiliency, and efficiency of its operations; (2) sustain (maintain) its system; and (3) replace legacy pipe. In total, Peoples expects the need to invest over a billion dollars in its system from January 1, 2022, to December 31, 2024. Due to this significant investment, approximately \$90 million of the company's revenue requirement increase from the 2020 Settlement is attributable to rate base growth. About half of this amount is return on rate base and the other half is increased depreciation expense and higher property tax expense associated with higher plant balances.

A. Customer Growth and Environmentally Friendly Projects

As previously noted, Peoples is investing heavily in new gas mains, laterals, and meters to serve thousands of new residential and commercial customers across the state. The company is also investing in environmentally friendly projects to meet specific customer needs and support changing energy markets. Three RNG projects will bring sustainable, made-in-Florida, pipeline-quality RNG to customers in Florida. A planned pipeline expansion will enhance Florida's market presence in the LNG market and support marine transportation, which is an important part of Florida's economy. The Big Bend-FGT lateral project supports

Tampa Electric's transition to efficient natural gas generation at Big Bend Station. These projects are supported by revenue from customer-specific contracts, but nevertheless contribute to the company's overall rate base growth. The company expects to invest approximately \$600 million to support customer growth and environmental sustainability from January 1, 2022 to December 31, 2024, of which \$150 to 160 million is attributable to major, customer specific projects.

B. Reliability, Resiliency, and Efficiency

Peoples has made significant plant investments to maintain and improve the reliability, resiliency, and efficiency of its systems. This category includes many projects that enhance the safety and reliability of the natural gas supply to customers by maintaining adequate pressure or flow and ensuring availability of primary and secondary supply feeds, mandatory relocation activities and infrastructure in the company's 14 service areas. It also includes major projects approved in the 2020 Agreement in Jacksonville, Panama City, and Southwest Florida that provided resiliency and the capacity to serve the growing communities across the state. Since then, other major projects include the Dade City Connector, the Work and Asset Management System, and improvements to its Tampa distribution system. The company expects to invest approximately \$405 million to enhance reliability, resiliency, and efficiency from January 1, 2022 to December 31, 2024.

C. Legacy Pipe Replacement

The company's CIBS/PPP program continues to provide important safety, reliability and environmental benefits to Peoples, its customers, and the State of Florida. Although the related costs are recovered via a rider, the capital being invested in this valuable program contributes to the company's rate base growth. The company expects to invest approximately \$80 million to replace legacy pipe from January 1, 2022 to December 31, 2024.

2. Depreciation Expense

The company's rate base growth has been accompanied by a commensurate increase in depreciation expense, which is projected to increase from about \$55 million in 2021 to a projected \$90 million in 2024. Of this \$35 million increase, about 25 percent is attributable to the proposed new depreciation rates associated with the depreciation study filed with the Commission on December 28, 2022.

3. Pipeline Safety and Compliance with Changing Federal Requirements

The costs of safely operating the company's growing system and changing federal safety and security requirements continue to increase and will be reflected in the rate base and O&M expense levels in the test year:

The protection of the company's underground pipeline system is critical to safe operations. Peoples has invested in the people, technology, and process to improve the prevention of excavation damages caused by others. However, as Peoples' system grows, so too does the need

to spend resources on safely locating and repairing underground facilities. The number of trips to identify underground facilities to accommodate construction in Florida and other reasons (“locates”) has grown from about 415,000 in 2015 to 630,000 in 2022 and is forecasted to continue to increase into 2024. Despite effort to increase public and construction industry awareness, Peoples experiences almost 2,000 damages by third parties annually which equates to approximately 5 damaged facilities a day.

Peoples has invested in technology to advance safety management including the enhancement of the Supervisory Control and Data Acquisition (SCADA) System, which monitors and manages the flow of gas, the implementation of a GPS and barcoding system to geographically pinpoint underground facilities within inches. Additionally, Peoples has deployed three vehicles outfitted with MobileGuard units that offer more efficient state-of-the-art leak detection.

The pace of new national PHMSA safety regulations has accelerated, so Peoples has adapted to comply with the PIPES 2020 Act and the first set of new regulations to enhance safety, which involves installation of Rupture Mitigation Valves. Peoples will be required to comply with future federal requirements such as new rules adopted pursuant to the Leonel Rondon Act, new greenhouse gas measurement and reduction mandates, the Mega Rule Rin 2 & 3, the proposed Standards update, and other requirements established during the PHMSA reauthorization in 2024.

The company prioritizes the protection of its assets from physical and cybersecurity attacks using a holistic approach to mitigate both risks. Peoples’ physical and cybersecurity activities are subject to regulation by the United States Department of Homeland Security and the United States Transportation Security Administration, both of which continue to impose more rigorous and costly cybersecurity requirements. The company is facing additional pressure to secure its physical assets. Consequently, the company, and its shared service provider (Tampa Electric), continue to invest in technology, controls, and processes to meet the evolving regulatory landscape, and to protect the company’s system.

4. Inflation

The effects of inflation have been felt by our customers and Peoples has not been immune. Annual inflation was less than two percent when the company filed its last rate case but increased to about five and eight percent in 2021 and 2022, respectively. The company is hopeful that the pace of inflation will moderate somewhat in 2023 and 2024; however, the higher costs the company paid in 2021 and 2022, and is expecting to pay in 2023, are now reflected in the cost of labor and capital additions. The company does not expect the prices it pays for goods and services in 2023 and 2024 to revert to 2020 levels. The company has been able to effectively manage its overall O&M expense levels and the company’s 2022 O&M expense levels were more than 10 percent below the Commission’s benchmark. Nevertheless, the increasing costs of labor, contractors, materials, insurance, and healthcare benefits continue to put significant upward pressure on the company’s costs of doing business.

5. Cost of Capital

In response to the economic distress caused by the COVID-19 pandemic, the Federal Reserve quickly and aggressively decreased its interest rates, but now is raising them to combat inflation. These changes have impacted capital markets, long- and short-term borrowing costs, and the cost of common equity. Further interest rate increases by the Federal Reserve are expected. Increases to the company's cost of capital are expected to account for approximately \$35 million of the company's projected 2024 test year revenue requirement increase.

An appropriate ROE is essential for a regulated utility to attract the capital necessary to make long-term investments, maintain and improve the company's quality of service, and lower costs for customers over time. Peoples will request that the Commission approve an authorized ROE of 11.0 percent, with a range of plus or minus 100 basis points, reflecting the significant market increase in the cost of capital.

Peoples has operated as a division of Tampa Electric Company since 1997, but on January 1, 2023, its assets were transferred to a separate corporation called Peoples Gas System, Inc., which is a subsidiary of TECO Gas Operations, Inc., which is a subsidiary of TECO Energy, Inc. Peoples' capital structure currently includes long-term and short-term debt allocations from Tampa Electric Company; however, during 2023, Peoples anticipates establishing an independent credit rating and raising capital through its own long-term debt issuances and short-term debt facility. Consequently, Peoples' cost of debt in the 2024 test year will reflect the impact of market rates commensurate with Peoples' independent credit rating.

Actions and Measures to Avoid Requesting a Rate Increase

The growth Peoples has experienced not only impacts its capital spending but also requires more resources for customer service, operations, maintenance, compliance, and other activities. Peoples has worked diligently to avoid seeking a base rate increase and continues to pursue efficiencies to help it meet its customers' strong demand for natural gas service in the communities it serves. The following are some of the actions taken by Peoples:

1. Since 2021, Peoples has been operating under the "rate freeze" and "stay out" provisions of the 2020 Agreement and has successfully managed its growth and earnings to operate within the range of returns allowed in the agreement. However, the company expects to earn an ROE of less than eight percent in 2023, which is well below the bottom of its approved ROE Range.
2. Peoples has pursued cost savings, cost avoidance, efficiencies, and better performance throughout its operations by reorganizing and redeploying resources to deliberately seek and implement process improvements. The company's deliberate approach has yielded improvements in damage prevention and other safety metrics, talent acquisition, customer experience, and project management. The company's commitment to formal process improvement continues to provide cost avoidance and efficiency while meeting the needs of Peoples' growing system.
3. The company has invested in critical technology to manage its operations to provide efficiencies and opportunities to expand on those efficiencies. In its 2020 rate case, Peoples

explained its plans to implement a Work and Asset Management system (“WAM”) to manage more efficiently the many operational, engineering, and construction activities involved in serving customers. WAM will be operational in 2023 and will begin to help moderate expense increases, improve operating efficiencies, and enhance customer service by automating functions that were previously performed manually. Peoples has also invested in improved call center technology, including an enhanced Interactive Voice Response (IVR) System, to provide further improvements to meeting customer service levels through the company’s call center. The pipeline safety improvements described above will help reduce carbon emissions and improve the efficiency of the company’s distribution system.

4. The 2020 Agreement contained a provision allowing Peoples to record depreciation expense credits totaling \$34 million during its term to keep rates stable and improve the ability to earn within its range of returns allowed in the Agreement. Peoples used \$14 million of these depreciation credits in 2022 and will use the remainder in 2023 consistent with the letter and spirit of the 2020 Agreement. Despite the company’s careful use of depreciation credits, Peoples expects to earn below the bottom of its authorized ROE range in 2023, the last year of the term of the 2020 Agreement.

5. Although it is not a base rate item, the price of the gas commodity is an important part of customer bills. Peoples has limited the impact of gas price volatility to customers by prudently managing the Purchased Gas Adjustment (PGA), which passes through the costs associated with the interstate capacity and commodity of natural gas. The company foresees that gas commodity prices will continue to stabilize which should help moderate customer bill increases in 2024.

Conclusion

Peoples is focused on safety, providing cleaner and greener energy for the communities it serves, and is proud of its best-in-class customer service. Safe and reliable natural gas service is a popular choice for residential customers, as well as essential to the growth and economic success of Florida’s many small, medium, large commercial and industrial businesses. The company is working diligently to sustainably grow with the state, meet demand for natural gas and superior customer service, and deliver high-quality natural gas distribution service at fair, just, and reasonable rates. The general base rate relief to be addressed in the company’s upcoming petition will be critically important to enable Peoples to maintain its financial integrity and support the growth of Florida while continuing to provide safe, reliable, responsible, and efficient service and to meet customer expectations.

Sincerely,



Helen J. Wesley

President and CEO, Peoples Gas System, Inc.

cc: All via Electronic Mail

Honorable Gary F. Clark, Commissioner
Honorable Andrew Giles Fay, Commissioner (Chair)
Honorable Art Graham, Commissioner
Honorable Mike La Rosa, Commissioner
Honorable Gabriella Passidomo, Commissioner
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