The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Committee on Innovation, Industry, and Technology

BILL:	SB 796
INTRODUCER:	Senator Gruters
SUBJECT:	Public Utility Storm Protection Plans
DATE:	March 4, 2019
REVISED:	

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Wiehle	Imhof	IT	**Pre-meeting**
2.			IS	
3.			AP	

I. Summary:

SB 796 creates a recovery clause[1] for storm protection costs instead of recovering these costs through base rates, as is done now; provides for recovery of a return on capital costs (profit) through the clause; and potentially requires Public Service Commission (PSC or commission) approval of recovery without consideration of the cost. The bill makes specific legislative findings that it is in the public interest to promote storm protection activities that will add to reduced restoration costs and outage times and increase reliability.

The bill applies to only public utilities, which are the investor-owned utilities (IOUs): Florida Power and Light, Duke Energy Florida, Gulf Power Company, Tampa Electric Company, and the Florida Public Utilities Corporation. Initially, the bill builds on PSC rule, requiring that, as part of the storm hardening plan required by the rule, each IOU must submit to the commission for review and approval a transmission and distribution storm protection plan. The plan must be updated at least every 3 years after the date of their initial approval and must be submitted to the commission for approval or modification.

The commission must approve or modify the proposed plan, as appropriate, pursuant to ch. 120, F.S., and must do so within 6 months after the IOU initially submits the plan. In reviewing the plan, the commission must consider:

- Whether the plan enhances reliability, strengthens infrastructure, and reduces restoration costs and outage times in a prudent, practical, and cost-efficient manner.

[1] Most of an investor-owned utility's costs and profits are recovered through base rates, the per-kilowatt-hour charges on a customer's bill. Recovery clause charges are additional charges, usually in separate line item charges on the bill. A recovery clause is typically used to make an annual recovery of costs that are difficult to plan for, are a simple pass-through of actual costs, do not include capital costs or a return on those capital costs, and for which regulatory lag in recovering such costs would be problematic.

- Whether transmission and distribution storm protection of electric infrastructure is feasible, reasonable, or practical in certain areas of the public utility's service territory, including, but not limited to, flood zones and rural areas.

The bill provides that, to maintain reasonable electric rates, an IOU's storm protection plan may not include the undergrounding of more than 4 percent of the IOU's lateral distribution lines per year.

All actions an IOU takes in implementation of a storm protection plan are "considered" prudent, but a party may challenge the prudence of the costs associated with such actions.

The bill also addresses IOU benefits under federal tax reform. Under the bill, instead of returning these benefits to customers through rate reductions, the money would be placed in a storm protection reserve account to be used to fund the full commission-approved annual revenue requirements of the storm protection cost recovery clause.

The bill requires the commission to adopt rules to implement and administer its provisions.

The bill takes effect July 1, 2019.

II. Present Situation:

Electric Utilities and the Public Service Commission

Chapter 366, F.S., provides for regulation of electric utilities in Florida. Section 366.02, F.S., provides definitions for these purposes.

- "Commission" means the Florida Public Service Commission.
- "Electric utility" means any municipal electric utility, investor-owned electric utility, or rural electric cooperative which owns, maintains, or operates an electric generation, transmission, or distribution system within the state.
- "Public utility" means every person, corporation, partnership, association, or other legal entity and their lessees, trustees, or receivers supplying electricity … to or for the public within this state; but the term "public utility" does not include either a cooperative now or hereafter organized and existing under the Rural Electric Cooperative Law of the state; a municipality or any agency thereof; ….

The commission has grid reliability authority over all Florida electric utilities.[2] It has full economic regulation authority over the public utilities, including setting rates, and ensuring service quality standards.[3] The public utilities are the investor-owned utilities: Florida Power and Light, Duke Energy Florida, Gulf Power Company, Tampa Electric Company, and the Florida Public Utilities Corporation.

[2] Sections 366.04(2)(c) and 366.05(8), F.S.
[3] Section 366.04(1), F.S.

Hurricane-Related Costs

Until recently, the subject of electric utility costs associated with a hurricane meant the costs of post-hurricane repair of the electric grid, the system of transmission and distribution lines and associated infrastructure. Then after the 2004-2005 hurricane seasons, there was an emphasis on storm hardening and the resulting costs. The IOUs now incur, and recover from their ratepayers (their customers), two types of costs associated with hurricanes and storms: after-the-fact repair costs and pre-storm hardening costs.[4]

Storm hardening and cost recovery are governed by PSC rule.[5] The rule applies to all IOUs and is intended:

- To ensure safe, adequate, and reliable electric transmission and distribution service for both operational and emergency purposes;
- To require the cost-effective strengthening of critical electric infrastructure to increase the ability of transmission and distribution facilities to withstand extreme weather conditions; and
- To reduce restoration costs and outage times associated with extreme weather conditions.

Under the rule, each IOU filed an initial plan for the PSC's review and approval, after which each utility's plan must be updated every three years. In a proceeding to approve a utility's plan, the commission is to consider whether the utility's plan meets the desired objectives of enhancing reliability and reducing restoration costs and outage times in a prudent, practical, and cost-effective manner to the affected parties.

The rule requires each utility storm-hardening plan to contain a detailed description of the construction standards, policies, practices, and procedures to be employed to enhance the reliability of overhead and underground electrical transmission and distribution facilities. Each filing must, at a minimum, address the extent to which the utility's storm hardening plan:

- Complies with a specified national safety code;
- Adopts specified extreme wind loading standards;
- Is designed to mitigate damage to underground and supporting overhead transmission and distribution facilities due to flooding and storm surges; and
- Provides for the placement of new and replacement distribution facilities to facilitate safe and efficient access for installation and maintenance.

Each storm hardening plan must explain the systematic approach the utility will follow to achieve the desired objectives of enhancing reliability and reducing restoration costs and outage times associated with extreme weather events. The explanation of the deployment strategy must include, but is not limited to, the following:

- A description of the facilities affected, including technical design specifications, construction standards, and construction methodologies employed;
- The communities and areas within the utility's service area where the electric infrastructure improvements are to be made;

[4] Florida Public Service Commission, *Review of Florida's Electric Utility Hurricane Preparedness and Restoration Actions 2018*, 5 (July 2018).
[5] Fla. Admin. Code R. 25-6.0342 (2007).

- The extent to which the electric infrastructure improvements involve joint-use facilities on which third-party attachments exist;
- An estimate of the costs and benefits to the utility of making the improvements, including the effect on reducing storm restoration costs and customer outages; and
- An estimate of the costs and benefits to third-party attachers affected by the electric infrastructure improvements, including the effect on reducing storm restoration costs and customer outages realized by the third-party attachers.

Approval of an IOU's storm-hardening plan does not guarantee the IOU the recovery of all costs incurred to implement the plan. After the IOU takes steps to implement the plan, the IOU must seek cost recovery during its next general rate case proceeding, where the PSC reviews the costs and determines whether they were prudently incurred before adding the approved costs to the IOU's base rates.[6] This helps to protect the IOU's ratepayers.

Each IOU has a rate-case settlement in place with a provision freezing the IOU's base rates and they can't get an increase to recover these costs until the settlement expires and they initiate another rate case.

Recovery Clauses

The vast majority of an IOU's general costs of providing service, including the IOU's profit, or allowed range of rates of return, is recovered through base rates. Base rates are set in a rate case, where all of an IOU's projected costs of doing business are reviewed and individual costs or categories of costs can be reviewed separately for a determination of accuracy and prudency. All approved costs are added together, an allowed range of rates of return is set, and a "revenue requirement" is established, the total revenue necessary to recover all these costs and the profit. The rates for different customer classes are then set that will provide recovery of this revenue requirement. The process protects the interests of both the IOU and its ratepayers.

There are, however, some exceptions where costs are recovered through a recovery clause, an additional charge usually in separate line item charge on the bill. The primary recovery clause is the fuel-cost recovery clause charge. Fuel costs can vary, sometimes significantly, from year to year and are recovered through the fuel-cost recovery clause. A recovery clause is used when the costs at issue are volatile, unusual, or short-term and are therefore difficult to plan for, and when regulatory lag in recovering such costs would be problematic. Recovery clause proceedings are typically conduced on an annual basis and provide only for a pass-through of actual costs. As capital expenditures are typically made based on long-term plans, recovery clauses typically do not include capital costs or a return on those capital costs. An IOU cannot use a recovery clause to recover capital expenses and a rate of return on those expenses when there is an existing, applicable rate-settlement agreement containing a rate freeze.[7]

[6] Florida Public Service Commission, *Review of Florida's Electric Utility Hurricane Preparedness and Restoration Actions 2018*, 12 (July 2018).
[7] *See*, e.g., *Citizens of the State v. Graham*, 213 So. 3d 703, 715-717 (Fla. 2017).

Undergrounding Lines

The construction of underground electrical distribution systems is more expensive than overhead systems, and the ratepayers served by the underground line are responsible for the difference in the costs between underground and overhead. The costs and benefits of storm hardening are factored into the cost difference calculation for new construction or conversion to underground facilities.[8]

The data collected after Hurricane Irma showed that underground lines suffered minimal outages during storms. It should be noted that while underground facilities fared particularly well during Hurricane Irma, they still are susceptible to damage caused by uprooted trees and flooding, and these repairs typically take longer to complete.[9]

In response to data requests from PSC staff, the three largest IOUs[10] stated that approximately 40 percent of all distribution lines are underground and that the majority of recent underground projects were for new construction, rather than the conversion of overhead to underground. Since 2006, the installed underground facilities have increased by approximately 5,300 miles for the IOUs. The total amount of installed underground facilities during the past five years was approximately 2,200 miles for an average rate of 440 miles/year.[11]

In an effort to further the deployment of underground facilities, Duke Energy Florida and Florida Power and Light have initiated targeted undergrounding programs that: began in 2018, focused on historically poor performing lateral circuits[12] to replace several hundred miles of overhead lines, and were funded through current base rates. Duke Energy Florida's pilot program is scheduled over a period of ten years and Florida Power and Light's for three years. The goal for each program is to test different construction techniques and identify impediments to converting these targeted overhead facilities to underground.[13]

Federal Tax Reform Benefits

The federal Tax Cuts and Jobs Act of 2017 took effect January 1, 2018, and reduces the federal corporate income tax rate from 35 to 21 percent. These tax cuts will produce a financial benefit for the IOUs, and the PSC is reviewing each utility's circumstances to determine whether those benefits must be returned to customers and, if so, how. Four of the five IOUs[14] have previous

[8] Florida Public Service Commission, *Review of Florida's Electric Utility Hurricane Preparedness and Restoration Actions 2018*, 12 (July 2018).
[9] *Id*., 30.
[10] Florida Power and Light, Duke Energy Florida, and Tampa Electric Company.
[11] Florida Public Service Commission, *Review of Florida's Electric Utility Hurricane Preparedness and Restoration Actions 2018*, 11-12 (July 2018).
[12] An IOU's distribution grid consists of feeder and lateral circuits. Feeders run outward from substations and can serve thousands of customers. Laterals branch out from feeders and are the final portion of the electric delivery system, serving smaller numbers of customers and typically associated with residential areas. Florida Public Service Commission, *Review of Florida's Electric Utility Hurricane Preparedness and Restoration Actions 2018*, 9-10 (July 2018).
[13] *Id*., 12.
[14] The four IOUs are Duke Energy Florida, Tampa Electric Company, Gulf Power Company, and Florida Public Utilities Company. Press Release, Florida Public Service Commission, *PSC Asserts Jurisdiction to Recover Tax Savings for Customers* (Feb. 6, 2018), available at http://www.floridapsc.com/Home/Newslink?id=11594 (last visited February 28, 2019).

rate case settlement agreements that contain provisions for flowing tax cut benefits back to customers, and that process will proceed in accordance with these terms. Currently, Florida Power and Light is the only IOU that does not have such an agreement.

III. Effect of Proposed Changes:

The bill creates s. 366.96, F.S., to create a recovery clause for storm protection costs, provide for recovery of a return on capital costs (profit) through the clause, and potentially require commission approval of recovery without consideration of the cost.

The bill makes legislative findings and creates the following definitions.

- "Commission" means the Florida Public Service Commission.
- "Public utility" or "utility" has the same meaning as in s. 366.02(1), F.S.
- "Transmission and distribution storm protection plan" means a public utility plan for the overhead hardening of electrical transmission or distribution facilities, the undergrounding of electrical distribution facilities, and increased vegetation management.
- "Transmission and distribution storm protection plan costs" means the reasonable and prudent costs of an approved transmission and distribution storm protection plan.
- "Vegetation management" means actions that a public utility takes to prevent or curtail vegetation from interfering with the utility's infrastructure, including, but not limited to, mowing the vegetation, applying herbicides, trimming trees, and removing trees or brush near electrical transmission and distribution facilities.

The bill requires that, as part of the storm hardening plan required by commission rule,[15] each IOU must submit a transmission and distribution storm protection plan to the commission for review and approval. The plans must be updated at least every three years after the date of their initial approval and must be submitted to the commission for approval or modification.

The bill provides that, to maintain reasonable electric rates, an IOU's storm protection plan may not include the undergrounding of more than 4 percent of the IOU's lateral distribution lines per year.

An IOU must include in its transmission and distribution storm protection plan any information required by commission rule to address the proposed electric infrastructure improvements, as well as sufficient information to demonstrate that the transmission and distribution storm protection plan costs are not included in the IOU's base rates.

The commission must approve or modify the proposed plan, as appropriate, pursuant to chapter 120, and must do so within 6 months after the IOU initially submits the plan. In reviewing the plan, the commission must consider:

- Whether the plan enhances reliability, strengthens infrastructure, and reduces restoration costs and outage times in a prudent, practical, and cost-efficient manner.
- Whether transmission and distribution storm protection of electric infrastructure is feasible, reasonable, or practical in certain areas of the public utility's service territory, including, but not limited to, flood zones and rural areas.

[15] Fla. Admin. Code R. 25-6.0342 (2007).

The bill creates a storm protection cost recovery clause by implication, requiring the PSC to conduct an annual proceeding to allow IOUs the opportunity to justify and recover transmission and distribution storm protection plan costs through such a clause. All actions taken in the implementation of a transmission and distribution storm protection plan are considered prudent, but a party may challenge the prudence of the costs associated with such actions.

The annual plan costs recoverable through the recovery clause may not be included in the utility's base rates but must be recovered through the clause and must be allocated to customer classes pursuant to the most recently approved rate design. For all capital costs recoverable through the clause, the IOU must be allowed to also recover the annual depreciation on such costs and a return on the depreciated balance of these capital costs, calculated at the IOU's weighted average cost of capital using the return on equity last approved by the commission in a rate case or settlement order.

The bill also addresses IOU benefits of federal tax reform. Under the bill, instead of returning these benefits to customers through rate reductions, the money would be placed in a storm protection reserve account to be used to fund the full commission-approved annual revenue requirements of the storm protection cost recovery clause. (This may avoid giving ratepayers a reduction in base rates for the tax benefits only to charge an equivalent amount in storm protection charges.)

If there is an actual or projected surplus in the reserve account at the end of a calendar year, it must be returned to customers through the storm protection cost recovery clause. If, on the other hand, the utility projects that the balance of its reserve will be insufficient to cover the projected full revenue requirements in any calendar year, the commission must establish a factor that, taking into account projected sales, is intended to recover the required cumulative annual revenue for transmission and distribution storm protection costs, net of the amount funded by the storm protection reserve account.

The cost recovery factor must be based on costs incurred by, as well as projections of, the transmission and distribution storm protection plan costs for the prospective recovery period.

The storm protection cost recovery clause cost-recovery factor must provide for periodic true-up of the utility's storm protection plan costs relative to projections. The true-up must occur at least annually and must further require that any refund or collection made as part of the true-up process include interest based on the 30-day commercial paper rate.

The bill requires the commission to adopt rules to implement and administer its provisions.

The bill takes effect July 1, 2019.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. State Tax or Fee Increases:

None.

E. Other Constitutional Issues:

Each IOU may have to wait until its currently applicable rate settlement agreement expires to use the storm protection cost recovery clause provisions of the bill. Both the federal and State constitutions prohibit passage or implementation of a law impairing the obligation of contracts.[16] A settlement agreement is a contract, and this prohibition would be applicable. The question, then, is whether the State's "significant and legitimate public purpose" outweighs the intrusion into the parties' bargain.[17] Allowing an IOU to recover capital expenses and a rate of return despite a rate freeze provision in a settlement agreement would completely abrogate that provision, so the impairment appears severe, heightening the scrutiny.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

Public utilities will incur unknown costs to develop and implement the transmission and distribution storm protection plans, which will be passed on to their customers. Customers will get the benefits of the energy grid improvements, but these benefits cannot be quantified with any certainty because they depend on many variables, such as what improvements are made and the details of future storms and outages.

C. Government Sector Impact:

The PSC will incur costs to adopt the required rules and to hold hearings to develop the disaster preparation and energy grid improvement plans. There will be additional costs to continue to monitor and periodically modify the plans. These costs have not yet been estimated.

[16] U.S. CONST. art. I, s. 10 and FLA. CONST. art. I, s.10.
[17] *See*, e.g., *Searcy, Denney, Scarola, Barnhart & Shipley, Etc., et al. v. State of Florida*, 209 So. 3d 1181 (Fla. 2017), 1192

These proceedings will also involve the Office of Public Counsel,[18] which will also incur costs.

VI. Technical Deficiencies:

Lines 65-66 of the bill define the terms "public utility" and "utility" to have the same meaning as in s. 366.02(1), F.S., a term that includes both electric and natural gas utilities. The context of the bill's provisions appears to effectively limit the applications of this definition to only investor-owned electric utilities, but it might be clearer to make this limitation explicit. This could be done by changing the terms used to "electric utility" or "utility" and defining them to have the same meaning as in s. 366.8255, F.S., which is "any investor-owned electric utility that owns, maintains, or operates an electric generation, transmission, or distribution system within the State of Florida and that is regulated under this chapter." This would require changes in terminology throughout the bill.

Lines 67-71 and 75-80 define "transmission and distribution storm protection plan" to include the costs of "increased vegetation management" and define "vegetation management" in a broadly inclusive manner. Existing storm hardening plans include vegetation management[19] and the resulting costs are included in existing base rate charges,[20] so it is unclear how future vegetation management costs would be recovered. Even if the phrase "increased vegetation management" limits clause recovery in some way, it may be difficult to separate a base line of vegetation management activities and costs from increased activities and costs, particularly as time passes.

Lines 87-90 limit an IOU's undergounding of electric lines to "not . . . more than 4 percent of the utility's lateral distribution lines per year." It is unclear whether the total of "the utility's lateral distribution lines" would continually include *all* of an IOU's lateral distribution lines, or whether that total would decrease due to deletion of lateral distribution lines in excluded areas such as flood zones and rural areas under proposed 366.96(4)(b), F.S., and deletion of lines already hardened.

Lines 98-101 require the commission to approve or modify an IOU's transmission and distribution storm protection plan "pursuant to chapter 120 . . . within 6 months after the utility initially submits the plan." The effect of the reference to chapter 120 is unclear, but it may require a hearing. Currently, approval of a proposed storm hardening plan is done without a hearing and through use of a Proposed Agency Action Order, a quicker and more informal process. If a hearing is required, this is a short timeframe, for discovery, pleadings and responsive pleadings by all parties, hearings, and drafting a formal order.

Lines 133-142 require:

- Deposit of an IOU's tax reform benefits into a storm protection reserve account instead of returning those amounts to the IOU's customers as a reduction in electric rates;

[18] The Office of Public Counsel represents utility customers in PSC proceedings (s. 350.0611, F.S.).
[19] Florida Public Service Commission, *Review of Florida's Electric Utility Hurricane Preparedness and Restoration Actions 2018*, 5 (July 2018).
[20] *Id*., 12.

- The money in the reserve account must be used to fund the expenses of the storm protection cost recovery clause; and
- If there is an actual or projected surplus in the reserve account at the end of a calendar year, the surplus must be returned to customers through the storm protection cost recovery clause.

It is unclear what these provisions require. They could require a direct refund to the IOU's customers. However, as the bill equates a return of the benefits of a tax reform to customers through a reduction in the IOU's electric rates with a deposit of those benefit amounts in a storm protection reserve account, it seems more likely that the return of the surplus to customers will be through retention in the reserve account and reducing the next year's charge for the IOU's storm protection plan costs.

VII. Related Issues:

It is difficult to determine the effect of the bill's provisions on PSC authority, ability to review an IOU's storm protection actions and resulting costs, and ability to protect ratepayers. Currently, approval of an IOU's storm-hardening plan does not guarantee the IOU the recovery of all costs incurred to implement the plan. After the IOU takes steps to implement the plan, the IOU must seek cost recovery during its next general rate case proceeding, where the PSC reviews the costs and determines whether they were prudently incurred before adding the approved costs to the IOU's base rates.[21] This helps to protect the IOU's ratepayers.

In contrast, under the bill:

- In approving a plan, the PSC necessarily determines "Whether the transmission and distribution storm protection plan enhances reliability, strengthens infrastructure, and reduces restoration costs and outage times in a prudent, practical, and cost-efficient manner." (Lines 101-106)
- "All actions taken in the implementation of a transmission and distribution storm protection plan are considered prudent, but a party may challenge the prudence of the costs associated with such actions." (Lines 115-118)

While the meaning and effect of the word "considered" is unknown, these provisions suggest that the PSC's plan approval is a determination that the actions to be taken under the plan are prudent, practical, and cost-efficient, before the actions are taken, and that the statute deems any and all actions taken under a plan to be prudent and beyond PSC review authority. Additionally, the PSC's authority to review the resulting costs is limited to costs and issues contested by a party; it can do nothing of its own initiative. This appears to significantly weaken ratepayer protections.

VIII. Statutes Affected:

This bill substantially amends section 366.96 of the Florida Statutes.

[21] *Id*.

IX. Additional Information:

A. Committee Substitute – Statement of Changes:
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.