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MEMORANDUM

TO: The Honorable Finance Committee Members
Honorable Council Member Bill Gulliford, Chair
Honorable Council Member Anna Brosche, Vice Chair
Honorable Council Member Danny Becton
Honorable Council Member Aaron Bowman
Honorable Council Member Lori N. Boyer
Honorable Council Member John R. Crescimbeni
Honorable Council Member Reggie Gaffney

CC: Paul E. McElroy, JEA, Chief Executive Officer
Melissa Dykes, JEA, Chief Financial Officer
Kirk Sherman, Council Auditor
Jason Gabriel, General Counsel
Margaret M. Sidman, Deputy Legislative Affairs and Managing Deputy
Lawsikia J. Hodges, Deputy General Counsel

FROM: Jody L. Brooks, Assistant General Counsel

RE: **JEA Fuel Cost Adjustment**

DATE: August 28, 2015

I. Question Asked.

Whether overfunded amounts related to JEA's fuel cost adjustment practice, which are typically refunded to customers, may be used for other purposes such as JEA debt repayment or reduction?

II. Short Answer.

Probably not based upon pass through cost principles supported by the Florida Public Service Commission's ("PSC") guiding principles regarding the fuel cost adjustment practice.

Under such PSC principles, a refund of any overage to customers is inherent in the application of a fuel cost adjustment practice. However, after researching this matter, no specific law or regulation was found governing the use of overfunded amounts related to the fuel cost adjustment practice.

III. Discussion.

There does not appear to be any specific laws or regulations on how revenue generated from the fuel adjustment charge in excess of the amount of JEA's actual fuel cost is to be allocated, but based on PSC's application of pass through cost principles, any overages would flow back to the customers. Guiding principles on the use of fuel recovery can be found in the PSC regulations.

The fuel cost adjustment is a regulatory tool designed to *pass through* to utility customers the costs associated with fuel purchases. The fuel cost adjustment is recognized by virtually all state commissions, by the Federal Energy Regulatory Commission and is used by most municipal electric utilities and rural electric cooperatives. In Order No. 6357, the PSC discussed the purpose of the fuel adjustment clause as follows:

> A fuel adjustment clause is intended to compensate for day-to-day fluctuations in the cost of fuel which cannot be anticipated in the base rates. It should be constructed and applied so as to reimburse the utility for the increase in the cost of fuel as related to generation. *It also operates so as to pass on to the customer any savings realized by the utility from decreased cost of fuel. (Order No. 2515-A, dated April 24, 1959). . . It should be emphasized that a utility does not make a profit on its fuel costs. . . .* The charge reflected on a customer's bill each month is designed only to provide for the recovery of fuel costs experienced by the utility in generating the customer's power. Conversely, it can and has resulted in a credit to the customer's bill when the price falls below the base cost of fuel. While some may question the propriety of allowing fuel costs to be recovered through an automatic adjustment clause, recent events underscore the basic reasons why such is done for this particular cost item as opposed to others. First, electric utilities rely largely upon fossil fuels to generate power; only Florida Power and Light Company now has a nuclear unit on the line and in service. Thus, their dependency on purchasing large quantities of fossil fuels will continue to exist for many years. Presently, fuel costs represent a substantial portion of operating costs; in some instances, fuel costs alone comprise more than half of a company's total operating costs. Any fluctuation, then, in fuel costs will have a

> significant impact on a company's earnings and can work to the detriment of the ratepayer or the utility depending on the direction of the movement unless some means exists to recoup those increased costs or refund those savings as quickly as possible. Rate cases are time consuming and expensive, and do not lend themselves to these objectives. Second, fuel costs are a highly volatile cost item unlike other costs of the utilities, such as wages and maintenance. When the volatility factor is coupled with the magnitude of fuel costs, one can readily conclude that the fuel adjustment clause is both a necessary and proper regulatory tool to insure that both the customer and the utility receive the benefits of responsive recognition to changes in the cost of generating electricity. We do not have the slightest doubt that a type of recovery clause should be retained by the utilities in order to accomplish this goal." Order No. 6357, issued November 26, 1974, in Docket No. 74680-CI, <u>In re: General investigation of fuel adjustment clauses of electric companies</u>.

As noted in the PSC Order, any realized savings in the application of a fuel cost adjustment should be passed on to the customer. The fuel cost adjustment is a mechanism for reflecting costs of fuel and purchased power on a dollar-for-dollar basis and the use of any realized savings for purposes other than a return to customers would appear be in conflict with the application of this practice.

IV. Conclusion.

Inherent in a fuel cost adjustment is that cost savings are to be passed on to the customers and JEA's use of these savings for other purposes may be in conflict with the application and operation of this practice under PSC guiding principles and regulations.