BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Petition of Florida Power Corporation for Order Authorizing A Return on Equity for Florida Power's Investment In The SunShine Intrastate and the SunShine Interstate Pipelines	)	Docket No.: 930281-EI Filed: June 4, 1993

DIRECT TESTIMONY

OF

PAUL R. CARPENTER

FOR

FLORIDA GAS TRANSMISSION

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ON BEHALF OF FLORIDA GAS TRANSMISSION

Q. Please state your name, address and position.

A. My name is Paul R. Carpenter. My business address is 125 Summer Street, Boston, Massachusetts 02110. I am the President of Incentives Research, Inc.

Q. Would you briefly describe Incentives Research, Inc.?

A. Incentives Research provides economic and financial consulting services to public and private sector clients, primarily in the fields of energy markets and industry structure, regulatory policy analysis, financial economics methods and antitrust.

Q. Please summarize your educational and professional background.

A. I received a Ph.D. in Applied Economics from the Massachusetts Institute of Technology, a M.S. in Management from MIT and a B.A. in Economics from Stanford University. For over ten years I have been involved in research and consulting on matters relating to energy economics and policy, with a particular focus on the natural gas industry. I have testified before Congress, the Courts and before the FERC, state and Canadian provincial regulatory commissions in many of the important cases resulting from the transition to the new regulatory policies that are being applied to the gas pipeline industry. In particular, I have been involved in several cases at the Federal and

state levels in which the appropriate regulatory policy toward new pipeline certification was at issue. These and other engagements are listed in my curriculum vitae, which is attached to this testimony as Exhibit ___ (PRC-1).

Q. Have your research or consulting engagements resulted in any publications?

A. Yes, these are listed in my c.v.

Q. Have you previously testified before the Florida Public Service Commission?

A. Yes, I testified recently in the proceeding involving the request by the SunShine Pipeline, the intrastate portion of the SunShine project, for a certificate of need from this Commission, Docket No. 920807-GP.

Q. Dr. Carpenter, what assignment were you given with respect to this proceeding?

A. I was asked by Florida Gas Transmission Corp. ("FGT") to evaluate the economic and regulatory policy implications of Florida Power Corporation's ("FPC's") proposed equity participation and requested regulatory treatment of its investment in the proposed SunShine project.

Q. How have you organized your prepared direct testimony?

A. I begin with a brief summary of my conclusions and recommendations. Thereafter, I have divided my testimony into four major sections. First, I describe my understanding of FPC's equity participation in the SunShine project and its proposed regulatory treatment. In the next two sections I evaluate whether or not this equity participation will

likely produce net economic benefits to FPC's electric ratepayers and whether it will likely cause additional costs to be borne by other gas and electric consumers in Florida. In the final section, I provide a detailed discussion of my recommendations based on this evaluation.

SUMMARY OF TESTIMONY AND RECOMMENDATIONS

Q. Dr. Carpenter, could you please summarize briefly your conclusions and recommendations based on your evaluation of the issues in this proceeding?

A. Yes. I have reached the following basic conclusions:

- **FPC's equity participation in the SunShine project is not likely to produce benefits for its electric ratepayers sufficient to justify the project risks they are being asked to bear through FPC's proposed guaranteed return mechanism in this case.**

Most of the ratepayer benefits alleged by FPC in its testimony flow not from its position as an equity participant in SunShine, but from its position as the primary shipper on the project. FPC's equity participation is not at all necessary to obtain these putative benefits. Moreover, the SunShine project as it is currently proposed and subscribed is a highly risky venture. FPC has not demonstrated why it should receive preapproval of a mechanism that would allow it to force its ratepayers to bear these project risks when it is unwilling to make such a commitment to the project on behalf of its own shareholders.

- **FPC's proposed equity participation will likely lead to higher costs for Florida electric and gas ratepayers.**

Because of the inherent conflict of interest between FPC's position as

an equity owner and principal shipper on the SunShine project, there can be no assurance that FPC's selection and utilization of SunShine is the most timely or economically efficient capacity expansion for Florida relative to the alternatives. Inefficient or untimely capacity expansion will lead to increased costs and stranded or unutilized investment on the existing pipeline systems which would result in increased rates to other electric and gas ratepayers in Florida. FPC will also have incentives to bias its own resource planning decisions to favor gas, and more precisely, gas via the SunShine project. Evidence for this incentive can be found in the decision by FPC to prematurely convert its Anclote plant to natural gas in order to promote the SunShine project.

Based on these conclusions I suggest two policy recommendations in this case in decreasing order of attractiveness:

1. **Prohibit FPC from taking an equity interest in the SunShine project.**

This policy would have the effect of eliminating any unwarranted exposure to project risks by ratepayers and it would eliminate the adverse incentive effects of FPC's dual role such that true competitive market forces could be relied upon to determine whether and when new pipeline capacity should be constructed in Florida.

2. **If FPC equity participation is permitted, the proposed regulatory treatment should be denied.**

Even if there were a justification for equity participation in principle, the proposed regulatory treatment improperly shifts project

risks to FPC's ratepayers without a corresponding benefit.

THE SUNSHINE PROJECT AND FPC'S PROPOSED REGULATORY TREATMENT

Q. Dr. Carpenter, what is your understanding of the physical and ownership structure of the proposed SunShine pipeline project?

A. The proposed SunShine project consists of a natural gas pipeline involving intrastate and interstate pipeline segments to be constructed from southern Mississippi to a terminus in central Florida. The intrastate segment is the SunShine Pipeline, a partnership consisting of Coastal Southern Pipeline Company (Coastal Southern), TCPL SunShine Ltd. (TCPL SunShine), a subsidiary of TransCanada Pipelines USA Ltd., and Power Energy Services Corp. (PESCORP), a subsidiary of Florida Power Corporation (FPC). FPC is a FPSC-regulated electric utility company. TCPL SunShine was admitted as a 30 percent partner on May 5, 1993 at which time PESCORP's stake was reduced from one-third to 30 percent. Also on May 5th, Coastal Southern took the place of ANR Southern (another Coastal Corporation subsidiary) in the partnership, with that ownership position being reduced from 67 to 40 percent.

The interstate portion of the project is called the SITCO Pipeline, owned 40 percent by ANR Southern, 30 percent by TCPL Interstate Ltd. and 30 percent by Power Interstate Energy Services Corporation (PIESCORP), a subsidiary of FPC.

Q. What is the status of the SunShine project?

A. SunShine has applied for a certificate of need before this Commission in Docket No. 920807-GP. SITCO filed an application for a Section 7(c) certificate with the FERC on May 27, 1993.

I understand that SunShine has signed precedent agreements with FPC, Peoples Gas, the City of Lakeland and Chesapeake Utilities. The contracted maximum daily quantities (MDQs) are shown in Table 1. SunShine has signed precedent agreements for firm MDQ's totalling 177,000 MMBtu per day or 71 percent of its total proposed capacity in 1995. The comparable percentage commitment under current precedent agreements appears to be slightly more than 50 percent of its proposed capacity in 1999. It is noteworthy that the vast majority of this commitment is from FPC itself -- at least 70 percent of the currently subscribed MDQ for 1995.

Q. What is FPC seeking in this proceeding?

A. FPC's request in this proceeding is outlined in the testimony of its witness Mr. Wieland. While it is difficult to discern from this testimony the exact nature and mechanics of FPC's proposal, it appears that FPC is asking the Commission to pre-approve two items:

(1) an explicit allowed return on equity for FPC's equity investment in PESCORP and PIESCORP; and

(2) recovery of this allowed return on equity through

Table 1

SunShine/SITCO
Volume Under Precedent Agreement (MDQ)

	1995	1996	1997	1998	1999 -2019
FPC-Anclote	120.0	120.0	120.0	120.0	120.0
FPC-Anclote (Summer)*	8.3	8.3	8.3	8.3	8.3
Peoples Gas	37.5	37.5	37.5	37.5	37.5
Peoples Gas (Summer)*	5.2	5.2	5.2	5.2	5.2
City of Lakeland	5.0	5.0	5.0	5.0	5.0
Chesapeake Utilities	1.0	1.0	1.0	1.0	1.0
Peoples Gas			25.0	25.0	25.0
FPC-Polk 1				45.0	45.0
FPC-Polk 2					45.0
Total Under Agreement	177.0	177.0	202.0	247.0	292.0
SunShine Capacity (Intrastate)	249.5	249.5	249.5	424.5	549.5
SITCO Capacity (Incremental Interstate)	80.0	80.0	80.0	83.2	89.2
Total Capacity	329.5	329.5	329.5	507.7	638.7
Percentage Subscribed	54%	54%	61%	49%	46%

* 20,000 MDth/day for 5 months is equivalent to 8.3 MDth/day (20*5/12) for one year.

FPC's fuel adjustment clause.

Q. Is FPC asking the Commission at this time to set an allowed return on equity percentage, e.g., 14 percent, for its investments in PESCORP and PIESCORP?

A. At this time, FPC does not appear to be asking the Commission to establish a specific return on equity. It appears to be asking the Commission for pre-approval of a mechanism that would explicitly and directly set the earned return on its investments in PESCORP and PIESCORP (as opposed to allowing those earned returns to vary from the allowed rate according to the actual performance of SunShine and SITCO) at some unspecified rate near the upper end of FPC's allowed rate for its electric business. Correspondingly, FPC is asking for recovery of that return from its electric ratepayers through the fuel adjustment clause.

Q. How is the FPC regulatory proposal intended to work?

A. Project sponsors currently anticipate that SunShine and SITCO will be project-financed with 75 percent non-recourse debt and 25 percent equity, the latter contributed by the project's partners. SunShine's allowed return on equity will be determined by this Commission (implicit in the approval of negotiated rates) while SITCO's will be set by the FERC.

PESCORP and PIESCORP, as holders of 30 percent of the equity in SunShine and SITCO, will see their year-to-year equity

returns directly determined by the actual performance of SunShine and SITCO. FPC, in turn, holds the equity of PESCORP and PIESCORP and -- if the Commission were not to approve FPC's proposed mechanism -- would see its actual year-to-year equity return also determined by the performance of PESCORP and PIESCORP.

The investment for which Mr. Wieland is requesting an allowed return is FPC's investment in PESCORP and PIESCORP. Under FPC's proposal, this Commission would be charged with setting two returns on equity: one for SunShine (implicit in the rates which SunShine has negotiated with potential shippers), and one for FPC's investments in PESCORP and PIESCORP. The effect of FPC's proposed mechanism is to sever any relationship between SunShine's and SITCO's actual performance and FPC's equity investment.

FPC argues that such an arrangement eliminates any conflict of interest between its roles as SunShine owner and shipper. Indeed this is true with respect to its own (FPC) economic well-being. But it is far from true when considering FPC's role as an agent for its ratepayers, who will bear a very unreasonable cost and risk allocation under the proposed terms. The return on FPC's equity investment would be effectively riskless, bearing little or no relation to SunShine's actual performance. I address the inequities and incentive defects of such an arrangement later in my testimony.

Q. If SunShine and SITCO are allowed equity returns and FPC is also

separately allowed an equity return on its investments in PESCORP and PIESCORP, won't that lead to double-collection from FPC's electric customers of the return on FPC's equity investment?

A. Under normal circumstances it would. Here, however, in conjunction with its request for an explicit allowed return on equity for its PESCORP and PIESCORP investments, FPC is proposing a fuel adjustment clause treatment that purportedly will eliminate the potential for double-collection. Specifically, FPC is proposing to reflect the following in its fuel adjustment clause:

(1) payments to SunShine and SITCO for transportation services (including a contribution to SunShine and SITCO's actual returns on equity based on the rates negotiated for service);

(2) a credit equal to all actual earnings by PESCORP and PIESCORP on their investments in SunShine and SITCO; and

(3) the explicit FPSC allowed return on FPC's equity investment in PESCORP and PIESCORP.

The combination of (1) and (2) effectively removes (FPC's ownership share of) SunShine and SITCO's actual, earned equity returns from the rate being passed through to FPC's electric ratepayers. Instead, FPC's electric ratepayers wind up paying, via a "true-up" after the fact, FPC's allowed return on its PESCORP and PIESCORP investments through

the inclusion of (3) in the fuel adjustment clause.

Q. Does this mechanism affect the allocation of project risks between FPC's shareholders and its electric ratepayers?

A. Yes it does. A key economic effect of this mechanism is that the true-up feature makes FPC's investment in SunShine riskless from the point of view of FPC's (actually Florida Progress's) shareholders. A party bears the economic risk of a project when it is exposed to variation in the project's cash flows, and hence return on investment, through time. Because the true-up mechanism assures FPC's shareholders of a given return, and because FPC's electric ratepayers are required to make up the difference between the project's actual performance and its allowed return, the ratepayers are being forced to bear FPC's portion of the SunShine project's business risks.

But clearly, such an arrangement is highly unusual and appears to violate the intent of traditional regulatory policy regarding how risk should be borne and compensated. To determine whether such a mechanism is appropriate in this case, it is first necessary to consider whether the proposed arrangement will confer net benefits on FPC's ratepayers. In other words, is the equity participation by FPC in SunShine likely to be a "good deal" for its ratepayers? This is important for the Commission to evaluate because the ratepayer exposure to project risk through the proposed mechanism effectively makes them the functional equivalent of equity holders in the project.

FPC'S EQUITY POSITION IS UNLIKELY TO PRODUCE BENEFITS FOR FPC'S ELECTRIC RATEPAYERS

Q. Why does FPC insist on equity ownership in the SunShine project?

A. In his prepared direct testimony, FPC witness Pollard states that FPC's motive in obtaining an equity position in the new pipeline was "to maximize the benefits of FPC's gas strategy for its ratepayers." Mr. Pollard identifies four categories of benefits that he asserts flow from FPC's equity position (p.14), although he does not attempt to quantify the value of any of them:

(1) enhanced credibility of the second pipeline during the early development phase;

(2) assurance that the new pipeline would be regulated by the FPSC;

(3) assurance that the pipeline design would meet FPC's present and future electric generation needs; and

(4) improved FPC fuel supply acquisition through its pipeline management position.

Q. Do you agree with Mr. Pollard's assessment?

A. No, I do not. Assuming for the sake of argument that these are meaningful benefits, the first three obviously flow from FPC's role as the primary shipper on the project and have nothing to do with its being an equity owner. This is implicitly acknowledged by Mr. Pollard himself when he asserts on page 7 of his direct testimony (in reference to FPC's 1992 negotiations with the two pipeline proposals from ANR

and United) that: "Since FPC's gas requirements represented an anchor load upon which their pipeline project could be based, ANR and United agreed to grant such an equity option to FPC." In other words, FPC's "leverage" that allowed it to insist on the project's physical design, FPSC regulatory status, and indeed its equity position, flowed from its status as the primary shipper and "anchor load" for the project. In his review for FPC of the merits of taking an equity position in the SunShine pipeline, Mr. John J. Hibbs reached the same conclusion: "...FPC is obviously in an excellent bargaining position given the fact that *it is the keystone shipper.* Simply put, without FPC, the Sun will not Shine!" (Emphasis added. See the December 2, 1992 letter of Mr. Hibbs to Mr. Pollard which I attached as Exhibit 18 (PRC-8) to my testimony in the need proceeding.)

Q. Did FPC claim any of these benefits as a shipper on the project during the need certification proceeding?

A. Yes it did. In fact, FPC argued at that time that these benefits could be totally divorced from its decision to take an equity position in the project. Having tied these benefits in the prior proceeding to its status as a shipper on the project, it is now improper and misleading for FPC to claim that they derive from its position as an equity owner. First, it has been FPC's view that its role as anchor shipper in concert with the benefits of pipeline-to-pipeline competition clearly are the driving forces for ensuring that FPC's present and future needs are met.

Second, for the "competitive atmosphere" to be responsible for the FGT Phase III customer benefits claimed by FPC in the need proceeding, both pipeline sponsors and prospective shippers had to be treating the SunShine project as credible. Nowhere in his direct testimony in the need proceeding does Mr. Pollard state that it was FPC's equity position that led to the project being perceived as credible by shippers. To the contrary, in his rebuttal testimony in that proceeding Mr. Pollard argued that: "The commitment of FPC to ship gas on the SunShine Pipeline is what made the project a viable competitive threat to FGT." Similarly, in his rebuttal testimony in the need proceeding, SunShine witness Mr. Bradley pointed to the commitment of the anchor shipper and the subsequent regulatory filing as the evidence of the credibility of the project:

> Q. Why did SunShine file its application for a Determination of Need with the Commission prior to the time that it had secured Precedent Agreements for all of its planned capacity?
>
> A. ...By making a regulatory filing the project sponsors are signalling the market that they have committed resources to the success of the project. ...With the anchor load committed, SunShine believed that it was time to signal the market that it was committed to proceed and that there was

a credible alternative to FGT for service.

Docket No. 920807-GP, Final Hearing, TR 924.

Nowhere in his testimony does Mr. Bradley state that the credibility of the SunShine project was due to FPC's equity participation.

Finally, FPC went to great lengths in the prior proceeding to explain to the Commission that it had negotiated several "outs" in its equity ownership arrangement. Simple logic makes it difficult to see how such a noncommittal, contingent "commitment" could be the driving force behind the credibility of a project.

Q. What about Mr. Pollard's second benefit of equity ownership, the assurance of FPSC regulation of the SunShine Pipeline?

A. Again, it was FPC's position as anchor shipper and not as equity participant that allowed it to (apparently) dictate to ANR that SunShine be proposed as an intrastate pipeline. FPC's *Natural Gas Transportation Study and Recommendations* (attached to my testimony in the need proceeding as Exhibit 18 (PRC-7)) states:

> FPC's gas load has provided the basis upon which ANR and United have been willing to spend several millions of dollars in project design, lobbying for Florida pipeline legislation and marketing the balance of the project's capacity. [III-13]

In that same report, the authors state:

> Concurrently [November 1991], a drive spearheaded by

United was underway to prepare legislation for filing in the 1992 Legislative Session. FPC sublimated its legislative efforts to those of United as the most efficient and cost-effective way to promote enactment of a Florida gas regulatory statute... The Natural Gas Transmission Pipeline Siting and Regulatory Act was signed into law by Governor Chiles on June 24, 1992. [I-3].

Thus, according to FPC, United, which ultimately lost in its bid for FPC's load, led the drive for the Florida Natural Gas Transmission Pipeline Siting and Regulatory Act that would place intrastate pipelines under FPSC jurisdiction. Moreover, the Act was signed into law five months before FPC decided which of the three pipelines it would commit to. These facts do not square with Mr. Pollard's view that FPC's equity ownership had something to do with the SunShine Pipeline being proposed as an intrastate line.

Q. What about the fourth benefit cited by Mr. Pollard, that "participating in the management of a gas pipeline will enable FPC to identify new and/or less expensive source of gas and to know how to access those supplies?"

A. Of all of the benefits cited, this is the only one that at least can be claimed to flow from the equity position alone. Essentially, Mr. Pollard is arguing that as a member of the management committee of

SunShine, FPC will have access to superior information about gas supplies and upstream access that would be unavailable to the pipeline's shippers.

Q. Wouldn't this constitute a potential benefit?

A. There are two aspects that are troublesome. If FPC will have special access to superior information as Mr. Pollard alleges, FPC's equity position will have given it an undue advantage over its competitors -- especially competing power generators using the SunShine and SITCO systems. This undue advantage is the very kind of preference that regulators often seek to eliminate. Indeed, the FERC has promulgated rules to restrict, and in some cases prohibit, the flow of information from an interstate pipeline to its affiliates.

Second, in a truly competitive environment it is not clear that there can be information advantages that would yield significant, persistent benefits. If there are such potential benefits, they should also be available from third parties through some type of contractual or agency arrangement.

In fact, FPC itself appears to have already delegated its upstream transportation arrangements on third-party pipeline systems to ANR Southern. (See the February 12, 1993 letter agreement between FPC and ANR Southern attached to this testimony as Exhibit ___ (PRC-2).) Such an arrangement would no doubt have been available to FPC absent its equity position and the cited agreement

does not depend on the approval of FPC's equity participation in this proceeding.

Q. Even if Mr. Pollard's claimed benefits of equity ownership are illusory, can he cite the level of shipper commitment in Table 1 as an indication that the project is viable and that, therefore, FPC's equity position is likely to be a "good deal" for ratepayers?

A. No he cannot, for two reasons. The first concerns whether the committed volumes are sufficient to pay for a significant fraction of the facility's capital costs. The second concerns how much FPC ratepayers ought to pay and how much risk they need bear in order to participate in any project benefits that are real.

The first problem becomes clear when one compares the contractual levels to the volumes which are necessary for SunShine to be able to recover its cost of service (and earn its expected equity return) at the rates which are promised in the precedent agreements. As I described in detail in my testimony in the need proceeding, SunShine's 52.5 cent per MMBtu initial rate for the intrastate portion of the project is a levelized rate that is based on 100 percent load factor utilization of the project in its expanded 1999 configuration. Thus, the relevant commitment levels to consider are those associated with the 1999 volumes. As Table 1 clearly illustrates, the precedent agreements that have been signed to date indicate that the combined SunShine/STTCO project is less than half-subscribed (in volumetric

terms) in this time period.

Furthermore, because the project's promised rates are based on capturing the economies of scale associated with the expanded 1999 configuration, if only the committed 292,000 MMbtu per day of demand materializes by 1999, there is no *economic* option available to the sponsors to "down-size" the project to match the low demand and to avoid losing massive amounts of money. According to SunShine's complete pro-forma financial simulation of the SunShine and SITCO projects, which I have included in my workpapers to this testimony, both full subscription ***and*** utilization of the project in 1999 are essential to achieving break-even cost recovery at the rates which have been negotiated.

Q. What are the implications of this fact and the current 1999 subscription levels on SunShine for this proceeding?

A. The economics and timing of the project, its current subscription level and the rates which have been offered combine to indicate that this is a very risky venture as proposed. To illustrate the riskiness of the project, I have calculated what the revenue shortfall for the intrastate portion of the project on a present value basis would be should subscriptions stay at their current levels shown in Table 1. The financial implications are shown in Table 2. As indicated, the 1995 present value of the pre-tax revenue shortfall from such an outcome would be $516 million. This amount is more than twice the total equity

Table 2

Sunshine/SITCO Is Facing A Sizable Revenue Shortfall With Current Precedent Agreement Volumes

Rate of Return: 10.42%

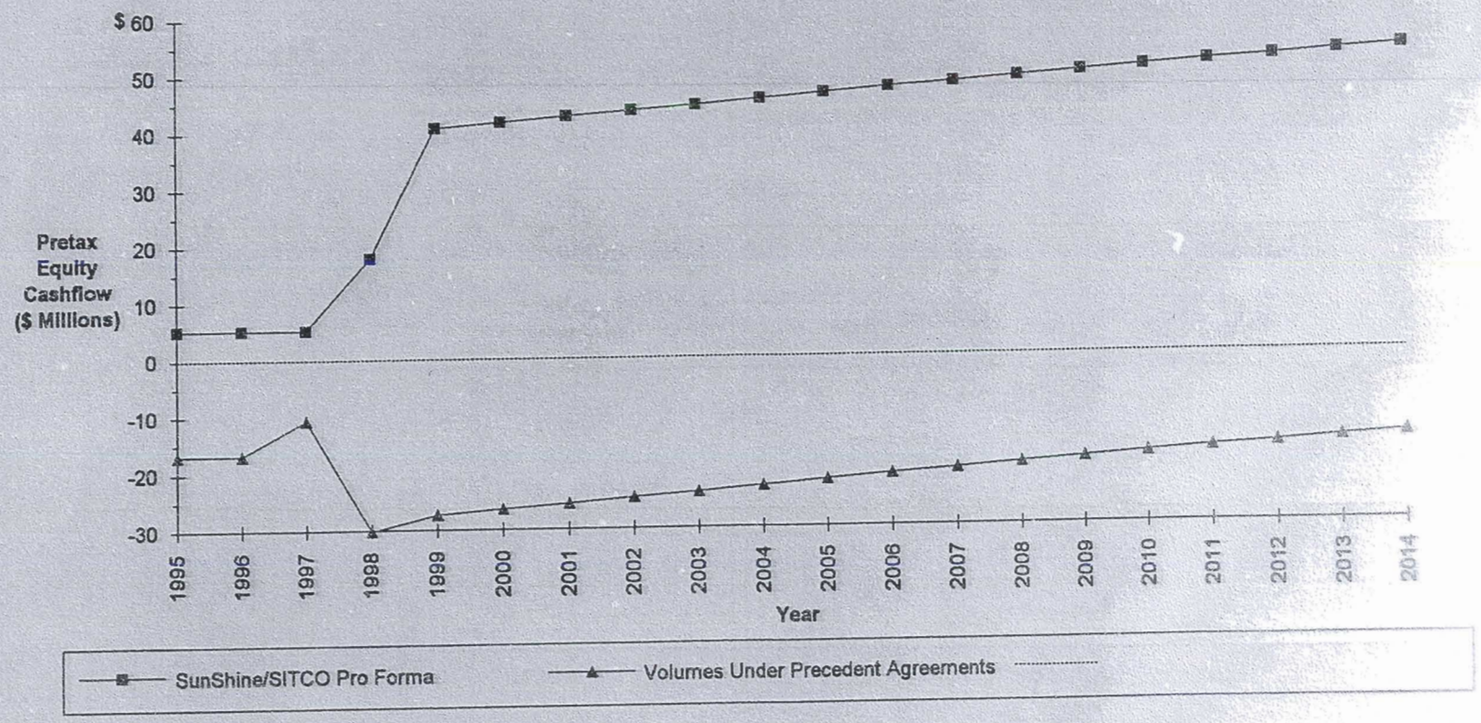
Unit Rates:
SunShine: $0.525
SITCO: $0.148
SunShine/SITCO: $0.673

	Pro Forma Volumes			Current Precedent Agreement Volumes			Revenue Shortfall	
year	Sunshine/SITCO MDQ (MDth/day)	SITCO MDQ (MDth/day)	Implied Revenues ($ Millions)	Sunshine/SITCO MDQ (MDth/day)	SITCO MDQ (MDth/day)	Implied Revenues ($ Millions)	By year ($ Millions)	Present Value ($ Millions)
1995	249.5	80.0	65.6	177.0	0.0	43.5	22.1	22.1
1996	249.5	80.0	65.6	177.0	0.0	43.5	22.1	20.0
1997	249.5	80.0	65.6	202.0	0.0	49.6	16.0	13.1
1998	424.5	83.2	108.8	247.0	0.0	60.7	48.1	35.7
1999	549.5	89.2	139.8	292.0	0.0	71.7	68.1	45.8
2000	549.5	89.2	139.8	292.0	0.0	71.7	68.1	41.5
2001	549.5	89.2	139.8	292.0	0.0	71.7	68.1	37.6
2002	549.5	89.2	139.8	292.0	0.0	71.7	68.1	34.0
2003	549.5	89.2	139.8	292.0	0.0	71.7	68.1	30.8
2004	549.5	89.2	139.8	292.0	0.0	71.7	68.1	27.9
2005	549.5	89.2	139.8	292.0	0.0	71.7	68.1	25.3
2006	549.5	89.2	139.8	292.0	0.0	71.7	68.1	22.9
2007	549.5	89.2	139.8	292.0	0.0	71.7	68.1	20.7
2008	549.5	89.2	139.8	292.0	0.0	71.7	68.1	18.8
2009	549.5	89.2	139.8	292.0	0.0	71.7	68.1	17.0
2010	549.5	89.2	139.8	292.0	0.0	71.7	68.1	15.4
2011	549.5	89.2	139.8	292.0	0.0	71.7	68.1	13.9
2012	549.5	89.2	139.8	292.0	0.0	71.7	68.1	12.6
2013	549.5	89.2	139.8	292.0	0.0	71.7	68.1	11.4
2014	549.5	89.2	139.8	292.0	0.0	71.7	68.1	10.4
2015	549.5	89.2	139.8	292.0	0.0	71.7	68.1	9.4
2016	549.5	89.2	139.8	292.0	0.0	71.7	68.1	8.5
2017	549.5	89.2	139.8	292.0	0.0	71.7	68.1	7.7
2018	549.5	89.2	139.8	292.0	0.0	71.7	68.1	7.0
2019	549.5	89.2	139.8	292.0	0.0	71.7	68.1	6.3

	Millions of $
Total Pretax Shortfall (PV in 1995)	515.7
FPC's Equity Investment @ 30% Ownership	61.2
Total Equity Invested @ 75%D. / 25%E.	204.0
SunShine	154.7
Sitco	49.3

Figure 1

Equity Cashflow Is Negative
Under Current SunShine/SITCO Subscription Level



Source: SunShine/SITCO Financial Pro-Formas, PRC Workpapers

to be invested in the project under the proposed 75/25 debt/equity capital structure.

Q. Why does this matter if SunShine is to be project-financed?

A. The high risk and strongly deferred timing of investment recovery in the project portend a potential problem in obtaining early non-recourse, project-based financing. As Figure 1 illustrates, revenues under current precedent agreement subscription levels are clearly insufficient to cover both operating costs and debt service requirements throughout the project lifetime, and particularly in the early years of the project, (i.e., pretax cash flow to equity from the project would be negative).

In this regard, lenders to the project will understandably ask that certain conditions be met and guarantees provided by the project's sponsors before they will provide financing on a non-recourse basis. One such condition will almost certainly be that non-recourse financing will not be available until contracts are signed that obligate shippers to pay demand charges sufficient to cover the project's debt service at its 1999 built-out configuration. This means it is likely that during the initial phases of the project, FPC, and its ratepayers under the proposed mechanism, will not likely be fully protected by non-recourse financing of the project's debt, *even at full subscription levels prior to 1999.*

Q. What are the implications of the above for FPC's electric ratepayers

and for its proposed equity true-up?

A. As I mentioned earlier, FPC is proposing that its investments in PESCORP and PIESCORP be guaranteed a rate of return at the upper end of its allowed rate for its electric business. This return would be automatically passed-through to electric ratepayers and it would be guaranteed by virtue of the fuel adjustment clause "true-up" procedure being requested by FPC. That is, regardless of whether Sunshine earns less or more than this allowed rate, FPC electric ratepayers must pay the same rate of return in the costs of gas.

Mr. Wieland's Exhibit___(KHW-1) attempts to illustrate the effect on ratepayers of the proposed mechanism for 1999. He compares a symmetric range of actual SunShine returns between 11 percent and 15 percent to a guaranteed FPC return of 13 percent. When SunShine's actual return is below 13 percent, ratepayers pay more to make up the difference. When SunShine's actual return is above 13 percent, ratepayers receive a credit for the amount above 13 percent.

But Mr. Wieland's example is not very realistic. What he neglects to illustrate is that SunShine's levelized rate structure tilts the time profile of the project's return on equity, reducing it in earlier years and increasing it in later years. FPC is clearly aware of this fact, for in its draft Section VI: Option To Hold Ownership Position of the *Natural Gas Transportation Study & Recommendations*, it states:

Due to the fact that pipeline rates are levelized over 25 years, but sales do not reach the ultimate projected level until 1999, the return on equity is depressed in the first years of the project. ... For example, the return on equity in the ANR projection rises from approximately 2-6 percent in the initial years to 20-30 percent in the latter years of the project. [P.VI-3]

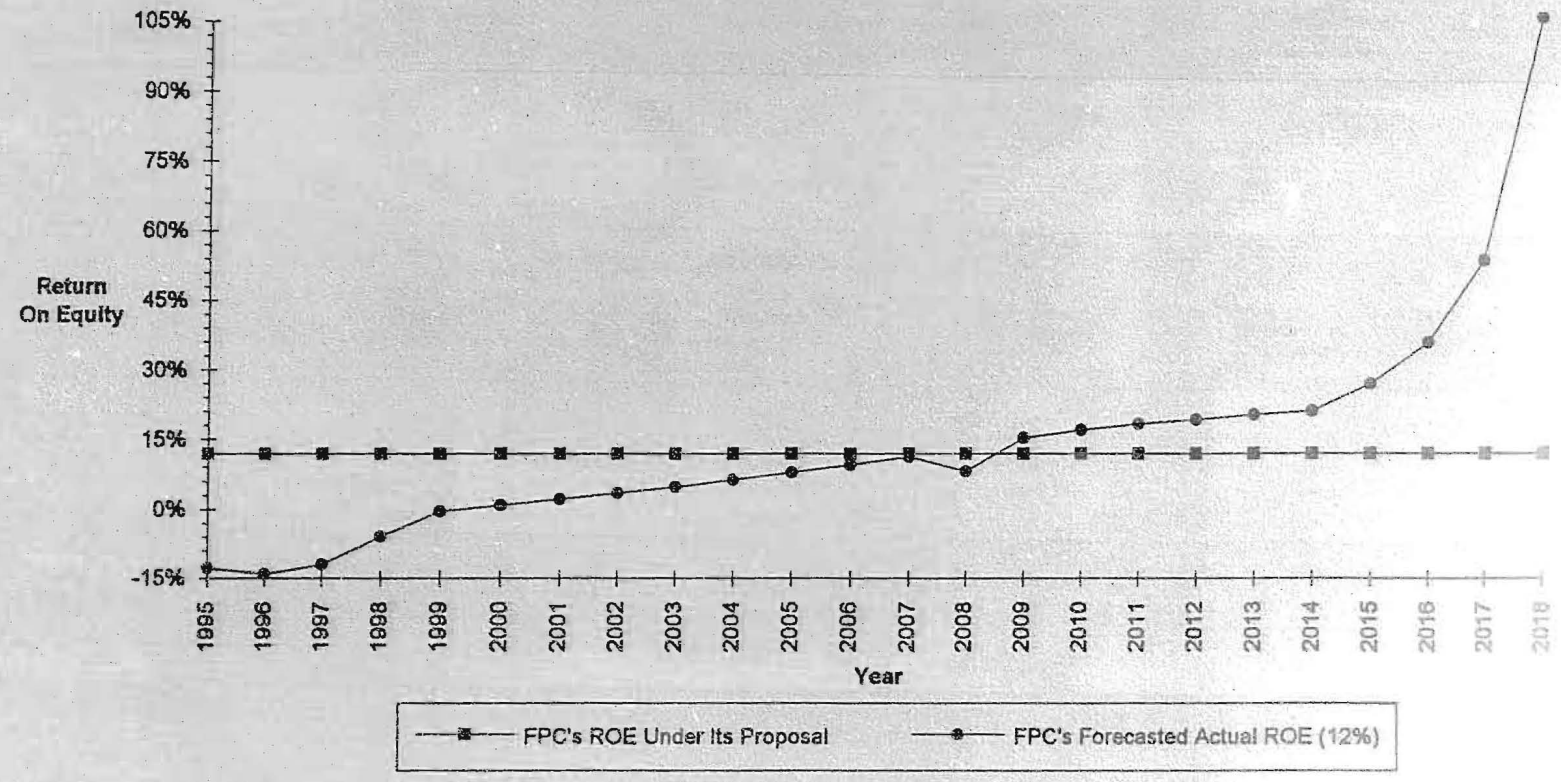
Furthermore, Mr. Wieland's illustration shows a symmetric outcome, i.e., that ratepayers are as likely to receive a credit as they are to pay for a loss. This is extremely unrealistic given the current undersubscription of the project.

Q. Have you computed what the likely time profile of ratepayer impacts will be under the FPC proposal to guarantee its rate of return?

A. Yes, I have. To evaluate the extent and likely asymmetry of FPC ratepayer impacts I first computed what the projected annual return on equity would be for the combined SunShine and SITCO project under the assumption that the projects are fully subscribed and utilized. These calculations are based on the pro-forma financial simulations provided by SunShine and the results are depicted in Figure 2, Panel A. Note that the annual ROE under the best possible market circumstance for the project does not reach the 14 percent level suggested by FPC as appropriate for its equity in PESCORP and PIESCORP until the year 2009. This time profile occurs because return has been deferred until late in the project's life to accomplish

Figure 2
Panel A

FPC's Forecasted Actual ROE Is Well Below Its Proposed ROE For Many Years (Full Subscription Volumes)



Source: SunShine/SITCO Financial Pro-Formas, PRC Workpapers

the levelization of rates.

In sharp contrast, the impact on ratepayers under the proposed mechanism is depicted in Figure 2, Panel B, which indicates what the annual and cumulative ratepayer contribution to FPC would be under the proposed mechanism at a 14 percent return -- again assuming full subscription and utilization levels. As the figure indicates, by the year 2009 ratepayers would have contributed approximately $100 million in riskless equity return to FPC before they would begin to see credits appearing on their electric bills.

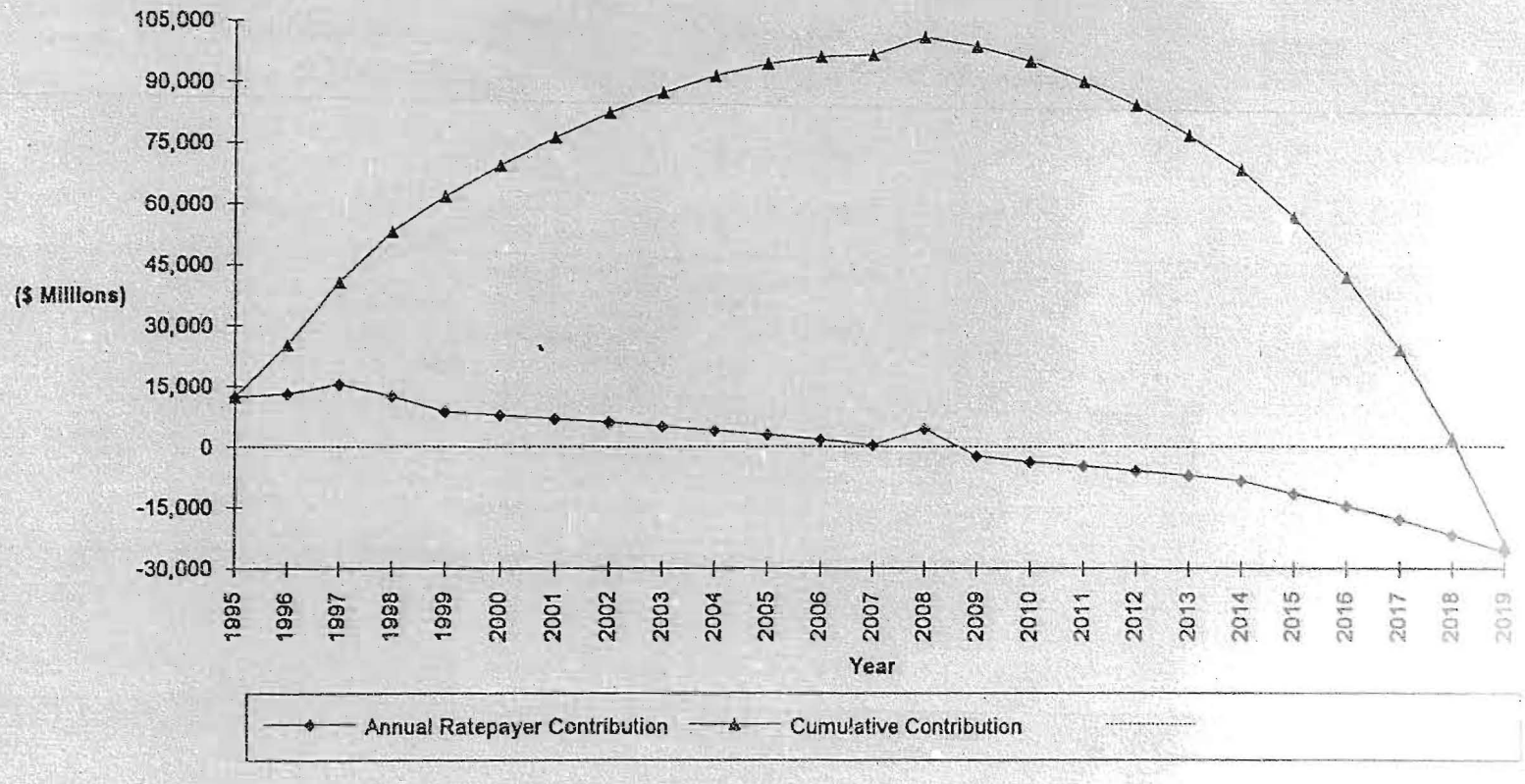
Q. What would be the ratepayer impact under the assumption that the project was undersubscribed?

A. The impact would be significant. To illustrate, I have prepared Figure 3 which shows the annual and cumulative ratepayer contribution under the proposed regulatory treatment, based on the assumption that subscription levels for the project do not rise above those currently shown in precedent agreements. As indicated, ratepayers never receive a credit and by the end of the project's life they would have contributed approximately $450 million to FPC for its investment in PESCORP and PIESCORP.

These figures indicate just how risky and unattractive this arrangement is for FPC's ratepayers. It also indicates the potential size and timing of the cross-subsidy that the project would receive if the Commission were to approve this unusual and unjustifiable scheme.

Figure 2
Panel B

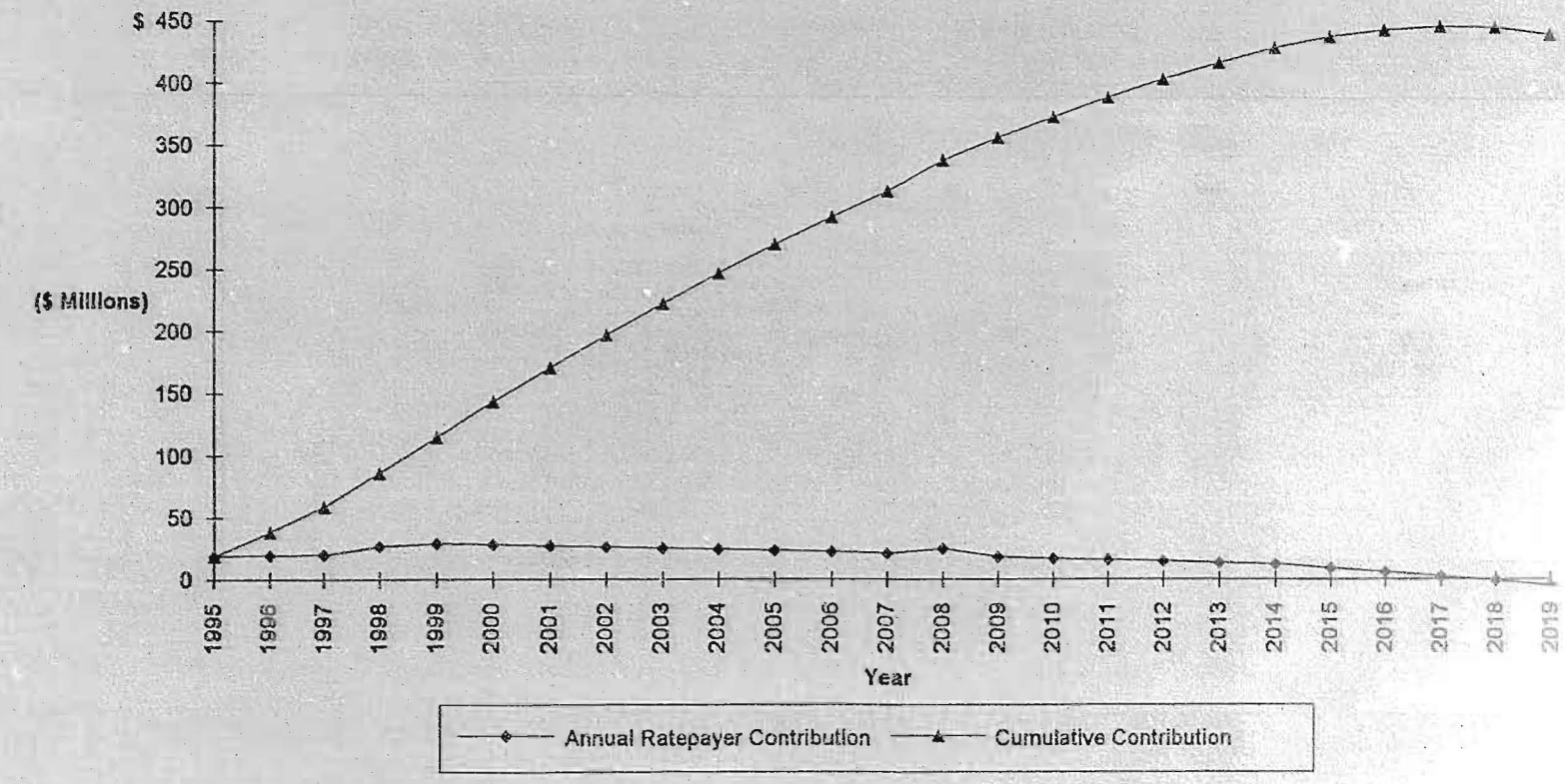
Annual and Cumulative Ratepayer Contribution to FPC's Allowed Return on Equity (Full Subscription Volumes)



Source: SunShine/SITCO Financial Pro-Formas, PRC Workpapers

Figure 3

Annual and Cumulative Ratepayer Contribution to FPC's Allowed Return on Equity (Current Precedent Agreement Volumes)



Source: SunShine/SITCO Financial Pro-Formas, PRC Workpapers

Q. What do you conclude from this evaluation?

A. I conclude that FPC's proposed regulatory treatment, even under the best of market circumstances, will result in significantly higher costs to its ratepayers in the early years of the project. From the ratepayers point of view, the true-up mechanism undoes much of the advantage to ratepayers of SunShine's negotiated levelized rates in that they are being asked to shoulder the burden of the deferred recovery of and on the project's investment necessary to achieve that levelization.

Of equal or more importance, ratepayers are being asked through this mechanism to bear the risks of undersubscription and underutilization of the project. Given SunShine's currently low subscription level, this risk is extremely high. If FPC truly believed that there was an economic need for the SunShine pipeline, as claimed in the prior proceeding, it would not be asking its ratepayers to bear these risks as a condition of its equity participation in the project. A valid need is one that can be served profitably without special subsidies.

Q. You mentioned earlier that FPC has suggested that it be allowed a return under its proposed mechanism at the upper end of its equity return for its electric business. Would such a level be economically justified in this case?

A. No it would not. FPC's rationale for this suggestion is apparently that

gas pipeline transportation is a more competitive and risky enterprise than is the generation and distribution of electric power. While this may be true in principle, what FPC fails to recognize is that under the proposed regulatory treatment it is asking ratepayers to bear these increased risks, not its shareholders. It is simply inappropriate for shareholders to be guaranteed a return to compensate them for risks which they are not bearing. This means that a maximum allowed return under such a mechanism would be a riskless rate (such as the prevailing rate on U.S. Treasury bills -- currently about 3 percent).

But even this rate would be too high to fully protect ratepayers if they were being asked to bear a significant undersubscription and underutilization risk. This is because the chances that the project will be undersubscribed and underutilized is undoubtedly greater than the chance that it would be oversubscribed and overutilized. That is, the risks that ratepayers will be asked to bear will not be symmetric around an expected value as Mr. Wieland's illustration would lead one to believe.

FPC'S PROPOSED EQUITY PARTICIPATION WILL LIKELY LEAD TO HIGHER COSTS FOR FLORIDA ELECTRIC AND GAS RATEPAYERS

Q. Other than the direct effects of the proposed regulatory treatment on FPC electric ratepayers, are there other ways in which both electric and gas ratepayers in Florida may face increased costs due to FPC's equity participation in SunShine?

A. Yes, there are. The other effects arise from the inherent conflict of

interest that will exist between FPC's position as both a shipper on and an owner of the SunShine project. These effects were discussed at length in my testimony during the need certification proceedings for the SunShine Pipeline. The conflict of interest itself was recognized by FPC in its Task Force Study and by Mr. Hibbs in his analysis that I previously cited.

Q. Could you briefly describe the ways in which FPC's conflict of interest in SunShine may manifest itself?

A. Yes. There are effectively three ways that the conflict of interest can result in increased costs to Florida electric and gas ratepayers:

1. By tilting the competitive playing field in favor of SunShine such that the least costly or most timely pipeline expansion project is not ultimately constructed.

2. By creating an incentive for FPC to bias its gas purchase decisions toward the utilization of SunShine and away from the utilization of potentially more economic supply sources available on another pipeline.

3. By biasing FPC's resource planning decisions toward its own electric generation which utilizes gas from SunShine and away from other resources that may be more economic.

In my testimony in the need proceeding I described how the first two of these incentives can result in increased costs to existing ratepayers by requiring them to pay rates for expansion capacity that

were higher than they otherwise would face if more efficient or timely capacity expansion were constructed, or if capacity on the existing FGT pipeline would be "stranded" or underutilized such that existing customers would be required to pay higher rates than they otherwise would.

Regarding the third bias, in the need proceeding, evidence from an evaluation performed by analysts from Florida Progress Corporation, and reported in the referenced Task Force Study, indicated that FPC's conversion of the Anclote facility to burn gas via the SunShine project was being prematurely advanced in order to benefit SunShine, notwithstanding a cost to FPC's ratepayers. Since Anclote is the primary load for the initial and subsequent phases of the project, this cast into serious doubt whether the pipeline was needed in the time frame that it is being proposed. To the contrary, it is a strong indication that the conflict of interest between FPC's position as an owner and a shipper on the project is already threatening to induce increased or unnecessary costs to ratepayers that are not offset by significant benefits.

All of these biases result to some extent from the fact that equity ownership creates an economic incentive for FPC to alter its decisions to favor the SunShine project and the facilities it will supply over other alternatives. These incentives will exist despite the proposed regulatory treatment because FPC will still want to avoid any

possibility or appearance that the SunShine assets are underutilized or not "used and useful," which could expose it to potential disallowance or regulatory penalties on future recovery of costs or return under the fuel adjustment clause.

RECOMMENDATIONS

Q. Dr. Carpenter, based on your evaluation of FPC's equity participation in the SunShine project and its proposed regulatory treatment of that investment, what policy do you recommend the FPSC follow in this proceeding?

A. In my opinion there are two possible policies which could be pursued, *in decreasing order of attractiveness*. After each I will provide a brief explanation of my rationale:

1. Prohibit FPC from taking an equity interest in the SunShine project.

This policy would have the beneficial effect of ensuring that there is no conflict of interest with FPC's role as a potential shipper on the project. It would create fair and equal competition for new pipeline capacity in the state that would be unaffected by cross-subsidies to one project because FPC's electric ratepayers would no longer be asked to involuntarily bear the project's risks of undersubscription and underutilization. This would minimize the potential for overcapacity and stranded investment costs to be borne by ratepayers and it would eliminate any incentives for FPC to

inefficiently alter its resource planning in favor of one project.

Moreover, FPC has not demonstrated that there are sufficient ratepayer benefits from its equity participation to outweigh the clear project risks that FPC's and other Florida ratepayers are being asked to bear. Under current subscription levels and the proposed rate mechanism, FPC equity participation in SunShine is simply not a good deal for ratepayers.

2. If FPC equity participation is permitted, the proposed regulatory treatment should be denied.

Even if there were a justification for equity participation in principle, the proposed regulatory treatment improperly shifts project risks to FPC's ratepayers. An alternative to the proposed mechanism would involve treating FPC's equity in SunShine as if it were any other unregulated asset, that is, segregated totally from FPC's regulated rate base. Unfortunately, however, a decision would still have to be made as to how much FPC's electric business would pay for service over SunShine. The Electric Fuels case (ironically cited by FPC as support for its proposed mechanism) illustrates the difficulty that the FPSC can have in such a circumstance. In that case, the Commission found it problematic to rely on a market price proxy for transactions between FPC and its coal transportation affiliate, IMT. As a result, it had to fall back on a cost allocation method to establish a price in lieu of an acceptable market proxy. In the case of SunShine, it would also be

difficult for the Commission to craft an appropriate market proxy for the price of transportation services on SunShine.

Another approach would be to simply pass through to ratepayers the rate which FPC negotiated in its precedent agreement with ANR. This would at least require FPC to bear some of the project's undersubscription and underutilization risks. (However, the headroom within the negotiated rate cap in the FPC precedent agreement would still allow FPC to pass on some of this risk to ratepayers.) But the Commission would have to be extremely vigilant to ensure that FPC was not unduly favoring the SunShine project and that other project costs or risk implications were not "leaking" into the rates for FPC's regulated services. For example, if the project were to impair FPC's creditworthiness or increase its cost of debt or equity, the FPSC would have to ensure that those effects were not reflected in higher rates for FPC's regulated services.

Q. Does this conclude your direct testimony?

A. Yes, it does.

Exhibit ___ (PRC-1)
Docket No.: 930281-EI

June 1993

PAUL R. CARPENTER
President
Incentives Research, Inc.
125 Summer Street
Boston, Massachusetts 02110
(617) 345-9970

Education

Ph.D. Massachusetts Institute of Technology, Cambridge, MA:
Applied Economics, 1984.

M.S. Massachusetts Institute of Technology, Cambridge, MA:
Management, 1978.

B.A. Stanford University, Palo Alto, CA:
Economics, 1976, (with Honors).

Employment

Incentives Research, Inc., Boston, MA:
(1983 - Present): President and co-founder of firm providing economic and financial counsel in the fields of oil and gas regulatory policy, economics, antitrust, and technology policy.

MIT Center for Energy Policy Research, Cambridge, MA:
(1981 - 1984): Research staff and post-doctoral fellow.

Putnam, Hayes & Bartlett, Inc., Cambridge, MA:
(1980): Associate.

NASA/Caltech Jet Propulsion Laboratory, Pasadena, CA:
(1978 - 1980): Economist and Project Task Manager.

MIT Energy Laboratory, Cambridge, MA:
(1976 - 1978): Research staff.

Professional Affiliations

International Association of Energy Economists
American Bar Association (Antitrust Section)
American Economic Association

Fields of Specialization

Industrial Organization
Antitrust
Regulation
Energy Economics
Corporate Finance and Strategy

Academic Honors and Fellowships

Stewart Fellowship, 1983
MIT Fellowships, 1981, 1982, 1983
Brooks Master's Thesis Prize (Runner-up), MIT, 1978

Publications

"Creating a Secondary Market in Natural Gas Pipeline Capacity Rights Under FERC Order No. 636," draft December 1992, Incentives Research Inc., (with Frank C. Graves).

"Review of the Component Design Report, Natural Gas Annual Flow Module, National Energy Modeling System," August 1992, prepared for the U.S. Department of Energy, Energy Information Administration.

"Unbundling, Pricing, and Comparability of Service on Natural Gas Pipeline Networks," November 1991, prepared for the Interstate Natural Gas Association of America (with Frank C. Graves).

"Review of the Gas Analysis Modeling System (GAMS): Final Report of Findings and Recommendations," August 1991, prepared for the U.S. Dept. of Energy, Energy Information Administration.

"Estimating the Cost of Switching Rights on Natural Gas Pipelines", The Energy Journal, October 1989 (with F. C. Graves and J. A. Read).

"Demand-Charge GICs Differ from Deficiency-Charge GICs", Natural Gas, Vol. 6 No. 1, August 1989 (with F.C. Graves).

"What Price Unbundling?", Natural Gas, Vol. 5 No. 10, May 1989 (with F.C. Graves).

Book review of Drawing the Line on Natural Gas Regulation: The Harvard Study on the Future of Natural Gas, Joseph Kalt and Frank Schuller, eds., in The Energy Journal, April 1988.

"Adapting to Change in Natural Gas Markets", in Energy, Markets and Regulation: What Have We Learned?, Cambridge: MIT Press, 1987 (with Henry D. Jacoby and Arthur W. Wright).

Evaluation of the Commercial Potential in Earth and Ocean Observation Missions from the Space Station Polar Platform, Prepared by Incentives Research for the NASA Jet Propulsion Laboratory under Contract No. 957324, May 1986.

An Economic Comparison of Alternative Methods of Regulating Oil Pipelines, Prepared by Incentives Research for the U.S. Department of Energy, Office of Competition, July 1985 (with Gerald A. Taylor).

"The Natural Gas Policy Drama: A Tragedy in Three Acts", MIT Center for Energy Policy Research Working Paper No. 84-012WP, October 1984 (with Arthur W. Wright).

Oil Pipeline Rates and Profitability under Williams Opinion 154, Prepared by Incentives Research for the U.S Department of Energy, Office of Competition, September 1984 (with Gerald A. Taylor).

Natural Gas Pipelines After Field Price Decontrol: A Study of Risk, Return and Regulation, Ph.D. Dissertation, Massachusetts Institute of Technology, March 1984. Published as a Report to the U.S. Department of Energy, Office of Oil and Gas Policy, MIT Center for Energy Policy Research Technical Report No. 84-004.

"Field Price Decontrol of Natural Gas, Pipeline Risk and Regulatory Policy", in Government and Energy Policy, Richard L. Itteilag, ed., Washington D.C., June 1983.

"Risk Allocation and Institutional Arrangements in Natural Gas", invited paper presented to the American Economic Association Meetings, San Francisco, December 1983 (with Arthur W. Wright).

"Vertical Market Arrangements, Risk-shifting and Natural Gas Pipeline Regulation", Sloan School of Management Working Paper No. 1369-82, September 1982 (revised April 1983).

Natural Gas Pipeline Regulation After Field Price Decontrol, prepared for U.S. Department of Energy, Office of Oil and Gas Policy, MIT Energy Lab Report No. 83-013, March 1983 (with Henry D. Jacoby and Arthur W. Wright).

Book Review of An Economic Analysis of World Energy Problems, by Richard L. Gordon, Sloan Management Review, Spring 1982.

"Perspectives on the Government Role in New Technology Development and Diffusion", MIT Energy Lab Report No. 81-041, November 1981 (with Drew Bottaro).

International Plan for Photovoltaic Power Systems, Solar Energy Research Institute with the Jet Propulsion Laboratory Prepared for the U.S. Department of Energy, August 1979 (co-author).

Federal Policies for the Widespread Use of Photovoltaic Power Systems, Jet Propulsion Laboratory Report to the U.S. Congress DOE/CS-0114, March 24, 1980 (contributor).

"An Economic Analysis of Residential, Grid-connected Solar Photovoltaic Power Systems", MIT Energy Laboratory Technical Report No. 78-007, May 1978 (with Gerald A. Taylor).

Speeches/Presentations

"GIC's and the Pricing of Gas Supply Reliability," California Energy Commission Conference on Emerging Competition in California Gas Markets, San Diego, Ca. November 9, 1990.

"The New Effects of Regulation on Natural Gas Field Markets: Spot Markets, Contracting and Reliability," American Economic Association Annual Meeting, New York City, December 29, 1988.

"Appropriate Regulation in the Local Marketplace", Interregional Natural Gas Symposium, Center for Public Policy, University of Houston, November 30, 1988.

"Market Forces, Antitrust, and the Future Regulation of the Gas Industry", Symposium on the Future of Natural Gas Regulation, American Bar Association, Washington D.C., April 21, 1988.

"Valuation of Standby Tariffs for Natural Gas Pipelines", Workshop on New Methods for Project and Contract Evaluation, MIT Center for Energy Policy Research, Cambridge, March 3, 1988.

"Long-term Structure of the Natural Gas Industry", National Association of Regulatory Utility Commissioners Meeting, Washington D.C., March 1, 1988.

"How the U.S. Gas Market Works - or Doesn't Work", Ontario Ministry of Energy Symposium on Understanding the United States Natural Gas Market, Toronto, March 18, 1986.

"The New U.S. Natural Gas Policy: Implications for the Pipeline Industry", Conference on Mergers and Acquisitions in the Gas Pipeline Industry, Executive Enterprises, Houston, February 26-27, 1986.

Various lectures and seminars on U.S. natural gas industry and regulation for graduate energy economics courses at Massachusetts Institute of Technology, 1984-85.

Panelist in University of Colorado Law School workshop on state regulation of natural gas production, June 1985. (Transcript published in University of Colorado Law Review.)

"Oil Pipeline Rates after the Williams 154 Decision", Executive Enterprises, Conference on Oil Pipeline Ratemaking, Houston, June 19-20, 1984.

"Issues in the Regulation of Natural Gas Pipelines", California Public Utilities Commission Hearings on Natural Gas, San Francisco, May 21, 1984.

"Financial Aspects of Gas Pipeline Regulation", Pittsburgh Conference on Modeling and Simulation, Pittsburgh, April 19-20, 1984.

"Natural Gas Pipelines After Field Price Decontrol", Presentations before Conferences of the International Association of Energy Economists, Washington D.C., June 1983, and Denver, November 1982.

"Spot Markets for Natural Gas", MIT Center for Energy Policy Research Semi-annual Associates Conference, March 1983.

"Pricing Solar Energy Using a System of Planning and Assessment Models", Presentation to the XXIV International Conference, The Institute of Management Science, Honolulu, June 20, 1979.

Testimonial Experience

Antitrust/Federal Court:

Deposition and Trial Testimony in State of Illinois v. Panhandle Eastern Pipeline Co. (Fed. Ct. for C.D. Ill) 1984-87.

Deposition Testimony in Sinclair Oil Co. v. Northwest Pipeline Co. (Fed. Ct. for Wyoming) 1987

Trial Testimony in City of Chanute, et al. v. Williams Natural Gas (Fed Ct. for Kansas) 1988

Deposition Testimony in Martin Exploration Management Co., et al. v. Panhandle Eastern Pipeline Co. (Fed. Ct. for Colorado) 1988 and 1992

Deposition and Testimony by Affidavit in Merrion Oil and Gas Co., et al., v. Northwest Pipeline Corp. (Fed. Ct. for New Mexico) 1989

Testimony by Affidavit in James River Corp. v. Northwest Pipeline Corp. (Fed. Ct. for Oregon) 1989

Deposition Testimony in Fina Oil & Gas v. Northwest Pipeline Corp. and Williams Gas Supply (New Mexico) 1992

Economic/Regulatory Testimony:

Before the Florida Public Service Commission, Application for Determination of Need for an Intrastate Natural Gas Pipeline by SunShine Pipeline Partners, FPSC Docket No. 920807-GP, April - May 1993.

Northwest Pipeline Corp., et. al, FERC Docket No. IN90-1-001, February 1993.

City of Long Beach, Calif., vs. Unocal California Pipeline Co., before the California Public Utilities Commission, Case No. 91-12-028, February 1993.

Alberta Energy Resources Conservation Board, on Applications of NOVA Corporation of Canada to Construct Facilities, January 1993.

Before the California Public Utilities Commission, on the Application of Pacific Gas & Electric Co. to guarantee certain financing arrangements of Pacific Gas Transmission Co. not to exceed $751 million.

Unocal California Pipeline Co., FERC Docket No. IS92-18-000, August 1992.

Before the California Public Utilities Commission, in the Rulemaking into natural gas procurement and system reliability issues, R.88-08-018, June 1992.

Alberta Energy Resources Conservation Board, Altamont & PGT Pipeline Projects, Proceeding 911586, March 1992.

Before the California Public Utilities Commission, on the Application of Southern California Gas Company for approval of capital investment in facilities to permit interconnection with the Kern River/Mojave pipeline, A.90-11-035, May 1992.

Northern Natural Gas, FERC Docket No. RP92-1-000, October 1991.

Florida Gas Transmission, FERC Docket No. RP91-187-000 and CP91-2448-000, July 1991.

Tarpon Transmission, FERC Docket No. RP84-82-004, January 1991.

Before the California Public Utilities Commission, on the Application of Pacific Gas & Electric Co. to Expand its Natural Gas Pipeline System, A.89-04-033, May 1990 and October 1991.

CNG Transmission, FERC Docket No. RP88-211, March 1990.

Panhandle Eastern Pipeline, FERC Docket No. RP88-262, March 1990.

Mississippi River Transmission, FERC Docket No. RP89-248, October 1989, September 1990.

Tennessee Gas Pipeline, FERC Docket No. CP89-470, June 1989.

Empire State Pipeline, Case No. 88-T-132 before the New York Public Service Commission, May 1989.

Before the U.S. Congress, House of Representatives, Committee on Energy and Commerce, Subcommittee on Energy and Power, Hearings on "Bypass" Legislation, May

Tennessee Gas Pipeline, FERC Docket No. RP86-119, 1986-87

Mojave Pipeline Co., FERC Docket No. CP85-437, 1987-88

Consolidated Gas Transmission Corp., FERC Docket No. RP88-10, 1988

Panhandle Eastern, FERC Docket No. RP85-194, 1985

On behalf of the Natural Gas Supply Association in FERC Rulemaking Docket No. RM85-1, 1985-86

On behalf of Panhandle Eastern Pipeline Co. in FERC Rulemaking Docket No. RM85-1, 1985

Coastal
The Energy People

CHARLES A. DIGLESBY
EXECUTIVE VICE PRESIDENT
NATURAL GAS GROUP
ANR PIPELINE COMPANY

Exhibit ___ (PRC-2)
Docket No. 930281-EI

February 12, 1993

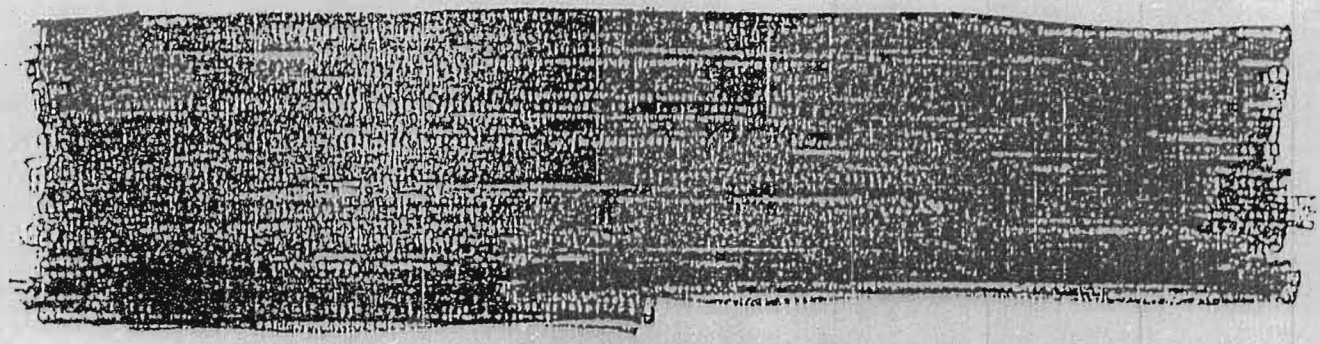
Mr. Stephen Watsey
Vice President, Purchasing and Stores
Florida Power Corporation
3201 Thirty-Fourth Street South
St. Petersburg, Florida 33711

Dear Steve:

Over the course of the past year, FPC and ANR Southern have worked together in attempting to ensure that FPC receives the lowest possible aggregate transportation rates for the volumes provided in those certain Precedent Agreements being executed contemporaneously herewith between ANR Southern Pipeline Company ("ANR Southern") and Florida Power Corporation ("FPC") for the firm transportation of natural gas on ANR Southern's proposed new interstate and intrastate natural gas pipeline systems, respectively known as SunShine Interstate Transmission Company ("SITCO") and SunShine Pipeline Company ("SunShine"). FPC has requested ANR Southern [redacted] The purpose of this letter is to set forth that agreement between the parties concerning the Aggregate Rate Cap and the assurance of maintaining the lowest possible aggregate transportation rates on SunShine, SITCO and upstream systems, to wit:

1. FPC hereby agrees to appoint ANR Southern as its exclusive agent for the first twenty (20) years of the Initial Term to acquire, hold and manage transportation capacity upstream of SITCO on third party systems for FPC's natural gas requirements up to a volume of 300,000 MMBtu. FPC and ANR Southern shall promptly negotiate the terms and provisions of a definitive agency agreement which shall include, without limitation, provisions for FPC to generally direct the activities of ANR Southern as its agent and for FPC's prior approval of agreements made on its behalf, with such approval not to be unreasonably withheld or delayed.

2. [redacted]



If you are in agreement with the foregoing, please indicate your acceptance by executing the duplicate originals of this letter in the space provided below and return one copy to the undersigned for our records.

Very truly yours,

ANR SOUTHERN PIPELINE COMPANY

By _____
Charles M. Oglesby

watscy3a.ltr

Accepted and Agreed to
this 12th day of February, 1993

FLORIDA POWER CORPORATION

By _____
Stephen Watsey, Vice President