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**BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION**

DOCKET NO 891345-EI

**REBUTTAL TESTIMONY
OF
M. R. BELL**

Gulf Power



**DOCUMENT NUMBER-DATE
04453 MAY 21 1990
FPSC-RECORDS/REPORTING**

1 GULF POWER COMPANY
2 Before the Florida Public Service Commission
3 Rebuttal Testimony of
4 Mark R. Bell
5 In Support of Rate Relief
6 Docket No. 891345-EI
7 Date of Filing May 21, 1990

8 Q. Would you please state your name, business address, and
9 occupation?

10 A. My name is Mark R. Bell, and I am a partner in Arthur
11 Andersen & Co., a firm of independent public
12 accountants, at 133 Peachtree Street, N.E., Atlanta,
13 Georgia, 30303.

14 Q. Mr. Bell, have you previously submitted testimony in
15 this proceeding?

16 A. Yes. I submitted prefiled direct testimony on my
17 independent review of the financial forecast used by
18 the Company in this rate proceeding.

19 Q. What is the purpose of your rebuttal testimony?

20 A. The purpose of my rebuttal testimony is:
21 - To comment on certain issues related to the operation
22 and maintenance (O & M) expense budgeting process which
23 were raised by Mr. Helmuth W. Schultz III in his
24 testimony filed on behalf of the Office of Public
25 Counsel.
 - To explain why Mr. Schultz fails in his attempt to

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1 discredit the Company's budgeting process based on the
2 examples cited in his testimony.

3 - To point out specific errors or inaccuracies in the
4 comments or proposals suggested by Mr. Schultz with
5 respect to the Company's budgeting process or budgeted
6 amounts specifically related to the Employee Relations
7 and labor budgets.

8

9 Q. Mr. Bell, are you familiar with Mr. Schultz's
10 description of how the Company's O & M budget was
11 developed?

12 A. Yes, I am.

13

14 Q. Do you agree with Mr. Schultz's description of that
15 process?

16 A. No, not entirely. In his description of the budget
17 process, Mr. Schultz has omitted several components.
18 He does not include important steps such as the review
19 of planning unit documentation performed by planning
20 unit directors, the approval process by the appropriate
21 vice-presidents, and the review of each planning unit
22 budget for compliance with budget procedures and
23 completeness performed by the Corporate Planning
24 Department.

25

1 Q. Are there any other steps in the budget process which
2 Mr. Schultz has not identified?

3 A. Yes. On page 4 of his testimony, Mr. Schultz states,
4 "After the planning units prepare their budgets, the
5 budgets are submitted to the O & M Review Committee for
6 approval. The budgets are then provided to the Budget
7 Committee for final approval." This description omits
8 an extremely important step in the O & M budgeting
9 process related to the responsibilities of the O & M
10 Review Committee. Before the planning units' budgets
11 are submitted to the Budget Committee for final
12 approval, the O & M Review Committee specifically
13 reviews each planning unit's requests and each
14 corporate controlled budget amount. A representative
15 of the planning unit is present during this specific
16 review and must be able to provide explanations to the
17 Committee which support budgeted amounts for which the
18 planning unit is responsible. During this process, the
19 Committee reviews the activity analyses provided by the
20 planning units, along with a three-year historical
21 budget-to-actual variation analysis. The planning unit
22 must be able to explain any budget requests which seem
23 unusual in light of prior year budget-to-actual
24 variances. This detailed scrutiny of the planning
25 units' budget support is an extremely important

1 component of the budget preparation and review process
2 but is not included in Mr. Schultz's summary of the
3 O & M budget process.
4

5 Q. Mr. Bell, in his testimony, Mr. Schultz expresses
6 general reservations about the credibility of the
7 Company's O & M budget process and his concerns that
8 certain of the Company's O & M budget procedures are
9 not proper. Did your independent review of the
10 Company's forecast support Mr. Schultz's concerns?

11 A. No, it did not. As I stated in my prefiled direct
12 testimony, it is my opinion that the Company's
13 financial forecasting system conforms with the American
14 Institute of Certified Public Accountants (AICPA)
15 guidelines for preparing a financial forecast, is
16 adequate for its purpose, is complete and logically
17 founded, and can be relied upon to produce consistent,
18 reliable results based upon the stated assumptions. As
19 a result of the work performed by me or under my
20 supervision, I concluded that the 1990 O & M budget was
21 prepared based on the forecasting procedures as
22 established by the Company. During my review, I noted
23 no evidence that supports Mr. Schultz's position that
24 the Company's O & M budget procedures include any
25 weakness that "lessens the credibility" of the

1 Company's budgeting process.

2

3 Q. Mr. Schultz states on page 4 of his testimony that the
4 Company's procedures with respect to preparing the
5 O & M budget "appear to have been followed" but then
6 states "I do not believe the Company's reference levels
7 are properly developed." Do you agree with his
8 statement with respect to the reference levels?

9 A. No, I do not.

10

11 Q. Please explain.

12 A. First, Mr. Schultz may not fully understand the concept
13 of the O & M budget reference level. As stated in
14 Mr. Gilbert's rebuttal testimony, the O & M reference
15 level is a level of O & M expenses established by the
16 Budget Committee each year for use in determining the
17 amount of documentation required to be submitted to the
18 Budget Committee for review in the budget approval
19 process. The reference level should be seen as a means
20 to improve efficiency and effectiveness of the budget
21 process. It is not, and should not be construed as, a
22 rigid requirement based on an inflexible formula to be
23 blindly computed by management without considering the
24 specific facts and current circumstances.

25

Secondly, Mr. Schultz specifically cites several

1 examples relating to 1989 reference levels which he
2 believes support his assertion that the reference
3 levels were not properly developed. He believes that
4 errors in the 1988 budget, which affected the 1989
5 reference levels, ultimately "flow into" the 1990
6 budget. As discussed more fully in Mr. Gilbert's
7 rebuttal testimony, Mr. Schultz fails to recognize that
8 the adjustments made to those reference levels were
9 proper adjustments to either correct errors in
10 previously computed reference level amounts (such as
11 the miscalculation of Employee Relations reference
12 level related to employee group insurance) or to
13 incorporate changes in circumstances to more accurately
14 reflect expected expenditures in the forecast period
15 (such as the repeal of Florida's state sales tax on
16 services and the transfer of corporate office building
17 expenses out of "Corporate-controlled" costs). Thus,
18 these adjustments actually enhance the credibility of
19 Gulf's budgeting process.

20
21 Q. Mr. Bell, you reviewed the Company's 1989 O & M budget
22 in connection with the Company's 1988 retail rate case
23 filing. In your review of the Company's 1989 O & M
24 budget, did you note any changes to the reference
25 levels originally communicated to the planning units?

1 A. Yes, I did. In my review of the Employee Relations
2 planning unit budget support, I noted that the 1989
3 reference level was improperly stated on the original
4 Resource Summary due to an error in computing the
5 reference level as described by Mr. Gilbert in his
6 rebuttal testimony. I also noted that the actual 1989
7 reference level used in the 1989 budget process
8 properly reflected the correction of that error.
9

10 Q. Do you believe that the change the Company made to the
11 Employee Relations reference level indicates that the
12 Company's reference levels were improperly developed or
13 that such modifications affect the use of the Company's
14 budget as the source for test year data used to
15 establish rates?

16 A. No. As stated in my prefiled direct testimony, my
17 review of the Company's financial forecast was designed
18 to ensure that the Company's forecasting system meets
19 the relevant professional standards as prescribed by
20 the AICPA. Those standards require that the process
21 used to develop the financial forecast provide for
22 "seeking out the best information that is reasonably
23 available at the time" and that "information used in
24 preparing financial forecasts should be consistent with
25 the plans of the entity." Based on these

1 authoritative guidelines, the changes made by the
2 Company to its O & M reference levels were not only
3 appropriate, but were in fact required, to make the
4 forecast properly reflect the best information
5 available and the intentions of management. In my
6 opinion, modifications to the reference levels to
7 reflect known errors or changes in circumstances serve
8 to increase rather than lessen the credibility of the
9 Company's budgeting process.

10

11 Q. Mr. Schultz notes on page 5 of his testimony that only
12 one of the five "modifications" to reference levels was
13 outlined in the Company's Budget Message. Do you
14 believe that this is a weakness in the Company's
15 budgeting process?

16 A. No. As I stated above, the Company's responsibilities
17 with respect to developing a proper forecast include
18 the requirement to use the best information available
19 at the time. Over the course of the process, facts and
20 circumstances may change and those changes should be
21 addressed in the final budget. Allowing properly
22 documented changes in budget information to reflect
23 known facts or circumstances, especially to correct
24 known errors in or misstatements of budget data,

25

1 is certainly not a weakness in the forecasting system.

2

3 Q. On page 15 of his testimony, Mr. Schultz states that
4 "if the Company happens to be over or under the budget
5 which had been established at a certain level in the
6 prior year, the reference level could remain unadjusted
7 and would not reflect any over or under budgeting in
8 the prior year." Do you agree with this statement?

9 A. No. As Mr. Gilbert explains in his rebuttal testimony,
10 and as I mentioned previously in this testimony, the
11 reference level is used to determine the level of
12 documentation required to be submitted to the O & M
13 Budget Review Committee to support the planning units'
14 budgets and not as a starting point in developing the
15 budget. Budget variance reports which quantify
16 historical differences between actual and budgeted
17 expenses are used by management of each planning unit
18 to develop their current year budgets. Also, as I
19 previously mentioned in describing the responsibilities
20 of the O & M Budget Review Committee, the review of
21 historical budget-to-actual results is an important
22 step in the O & M budget review process. The O & M
23 Budget Review Committee is provided a three-year
24 historical budget-to-actual report for use in its
25 review of the planning units' budget requests and

1 activity analyses. The planning unit must be able to
2 explain any budget requests which seem unusual in light
3 of variations between historical budgeted and actual
4 amounts. This part of the budget review process
5 mitigates the risk that prior year actual-to-budget
6 variations may not be considered in the current
7 reference level and may therefore "carryover" to future
8 budgets.

9
10 Q. On page 13 of his testimony, Mr. Schultz proposes an
11 adjustment to the Company's O & M budget related to the
12 employee complement. He uses an annualized wage rate
13 based on 1989 actual wages to compute his adjustment.
14 Do you agree with his use of this average wage rate?

15 A. No. I do not believe that it is reasonable to assume
16 that the average salary of all employees of the Company
17 at any point in time would approximate the average
18 salary related to normal vacancies. Normal vacancies
19 generally do not include many upper-management
20 positions which would have higher salaries; therefore,
21 the actual average salary of the Company's employees
22 would generally be higher than the average salary for
23 the vacant positions. Once again I refer to the AICPA
24 forecast guideline which requires "seeking out the best
25

1 information that is reasonably available at the time."
2 I believe that use of an average salary based on the
3 budgeted salaries of currently vacant positions would
4 more accurately reflect the best information available
5 for computing this adjustment.

6

7 Q. Mr. Bell, on page 14 of his testimony Mr. Schultz
8 states that the election of some planning units not to
9 use the Company's model for determining budgeted
10 payroll shows "there is a lack of consistency in the
11 operation of the Company's formal budgeting process."
12 Do you agree with this observation?

13 A. No. As Mr. Gilbert discusses in his rebuttal
14 testimony, the labor model to which Mr. Schultz refers
15 is merely a tool offered to the planning units to
16 assist in the clerical calculation of their labor
17 budgets. It is by no means a required part of the
18 Company's "formal budgeting process" and is no more
19 accurate than other methods that may be employed to
20 calculate labor budget amounts. In my opinion, the
21 decision by the various planning units to use or not
22 use that specific labor model has no impact on the
23 accuracy or credibility of the Company's labor budget
24 and does not result in an inconsistency in the
25 Company's forecasting methodology.

1 Q. Do you have any further comments with respect to the
2 matters related to the budget process raised by
3 Mr. Schultz?

4 A. Yes. In my opinion, the inferences made by Mr. Schultz
5 with respect to the credibility of the Company's
6 budgeting process are without merit. Mr. Schultz has
7 failed to recognize certain key steps in the O & M
8 budget process and has attempted to discredit the
9 entire budgeting process using isolated examples that
10 are not supported by the facts. In fact, the
11 modifications made in the budget process referred to by
12 Mr. Schultz serve to enhance, rather than lessen, the
13 credibility of the budget process. In summary, I want
14 to repeat my conclusion, based on my review of the
15 Company's entire financial forecasting system, that the
16 system conforms with relevant professional standards,
17 is adequate for its purposes, is complete and logically
18 founded, and can be relied upon to produce consistent,
19 reliable results based on the assumptions.

20
21 Q. Does this conclude your testimony?

22 A. Yes.

23
24
25

AFFIDAVIT

STATE OF FLORIDA)
)
COUNTY OF ESCAMBIA)

Docket No. 891345-EI

Before me the undersigned authority, personally appeared
M. R. Bell, who being first duly sworn,
deposes and says that he/she is the Partner of
Arthur Andersen & Company, Witness for Gulf Power
Company and that the foregoing is true and correct to the best
of his/her knowledge, information and belief.

Mark R. Bell

Sworn to and subscribed before me this July 10 day of
May, 1990.

William W. Silas, Jr.
Notary Public, State of Florida at Large

My Commission Expires: Notary Public, Fulton County, Georgia
My Commission Expires Feb. 11, 1992