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July 9, 1996

HAND DELIVERED

Mr. Robert V. Elias
Staff Counsel
Division of Legal Services
Room 370N - Gerald L. Gunter Building
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Re: Prudency Review to Determine Regulatory
Treatment of Tampa Electric Company's
Polk Unit; FPSC Docket No. 960409-EI

Dear Mr. Elias:

Pursuant to the discussion at the end of the Prehearing Conference in the above docket, we enclose Tampa Electric's revised Prehearing Statement. This revised version contains all of Tampa Electric's revisions and we would appreciate your substituting this revised version in place of the company's original input into the Prehearing Order.

Also enclosed is a 3.5" high density diskette containing the above document in WordPerfect 6.1 for Windows format.

Please acknowledge receipt and filing of the above by stamping the duplicate copy of this letter and returning same to this writer.

- ACK
- AFA
- APP _____
- CAF _____
- CMU _____
- CTR _____
- EAG *Dubey*
- LEG JDB/pp
- LIN Enclosures

Thank you for your assistance in connection with this matter.

Sincerely,

James D. Beasley
James D. Beasley

OPC cc: All Parties of Record (w/enc.) (hard copy only)
RCH _____ Division of Records and Reporting (w/enc.) (hard copy only)

DOCUMENT NUMBER-DATE

07240 JUL-96

FPSC-RECORDS/REPORTING

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Prudence Review to Determine
Regulatory Treatment of Tampa Electric
Company's Polk Unit.

) DOCKET NO. 960409-EI
) REVISIONS SUBMITTED:
) July 9, 1996
)

PREHEARING STATEMENT OF TAMPA ELECTRIC COMPANY

Pursuant to the Order Establishing Procedure¹ issued in the above docket on April 30, 1996 and Rule 25-22.038(3), Florida Administrative Code, Tampa Electric Company ("Tampa Electric" or "the company") submits the following as its Prehearing Statement in this proceeding:

A. APPEARANCES

LEE L. WILLIS
JAMES D. BEASLEY
KENNETH R. HART
Ausley & McMullen
Post Office Box 391
Tallahassee, Florida 32302

and

HARRY W. LONG, JR.
TECO Energy, Inc.
P.O. Box 111
Tampa, Florida 33601-0111
On behalf of Tampa Electric Company

1 Order No. PSC-96-0567-PCO-EI

B. WITNESSES

Witness

Subject Matter

(Direct)

1. Girard F. Anderson
(Tampa Electric) Mr. Anderson will explain the broad corporate policy decisions made during the siting and construction of the Polk IGCC unit which underscore the prudence of Tampa Electric's actions and the resulting expenditures made in connection with the project. As background information, his testimony will address the circumstances surrounding the Commission's approval of the company's Polk Integrated Gasification Combined Cycle ("IGCC") unit and the steps which the company took to implement that approval.
2. Thomas L. Hernandez
(Tampa Electric) Mr. Hernandez will explain the analytical basis for the conclusion that the Polk IGCC unit remains the most cost-effective and prudent means of providing needed capacity on Tampa Electric's system. He will discuss Tampa Electric's ongoing review of key planning and forecast assumptions and the results of several annual cost-effectiveness studies. These studies were performed subsequent to the Commission's order approving the Polk IGCC unit and they repeatedly and consistently affirmed the correctness of the Commission's decision.
3. Hugh W. Smith
(Tampa Electric) Mr. Smith will describe the fuel price and availability forecasts and the forecast assumptions relating to the alternative fuels considered, which were used by Mr. Hernandez in supporting the company's conclusion that Polk Unit One continues to be the most cost-effective solution to the need for additional capacity identified by this Commission in Order No. PSC-92-0002-FOF-EI. Mr. Smith will also discuss the environmental considerations which were a major factor in establishing the acreage requirements at the Polk site.

4. Charles R. Black
(Tampa Electric)

Mr. Black will discuss the detailed costs associated with the construction of the Polk Power Station, including land acquisition and site development costs, and describe the very stringent project management and cost control efforts undertaken which have resulted in prudent and reasonable expenditures. He will explain the IGCC technology employed at the Polk Power Station and discuss the fuel use flexibility afforded by the technology which has allowed the company to explore the use of alternative feedstock fuels, such as petroleum coke ("pet coke"), which can increase the cost-effectiveness of the project.

5. Thomas F. Bechtel
(Tampa Electric)

Mr. Bechtel, Director of the U.S. Department of Energy ("DOE") Clean Coal Technology Program's Morgantown Energy Technology Center, will provide an overview of the DOE's Clean Coal Polk Project and explain how the project has furthered the program's objectives. He will also discuss DOE's monitoring of the costs associated with the project and the basis for DOE's conclusion that Tampa Electric has managed all aspects of the Polk IGCC project in a professional and prudent manner.

6. John R. Rowe, Jr.
(Tampa Electric)

Mr. Rowe will explain why the appropriate regulatory treatment for Tampa Electric's Polk related costs is full inclusion in rate base, especially in light of the cost cutting and cost control measures implemented by Tampa Electric which will permit the company to freeze its base rates through 1998. He will also explain why no change in the current rate base treatment of Tampa Electric's Port Manatee site is warranted.

7. Elizabeth A. Townes
(Tampa Electric)

Ms. Townes will explain how the Polk regulatory treatment proposed by Mr. Rowe should be reflected in the company's accounting system and in the surveillance

reports filed periodically with the Commission. She will also identify the specific costs Tampa Electric proposes to include in its rate base and net income reporting for regulatory purposes.

(Rebuttal)

1. John R. Rowe, Jr.
(Tampa Electric)

Mr. Rowe will point out that no party has established through credible evidence that Tampa Electric lacked a rational basis for its post need hearing Polk-related decisions given what was known at the time those decisions were made. Instead, as Mr. Rowe explains, the Staff and other intervenors have based their assertions on faulty hindsight in an attempt to validate their basic premise that the Commission was mistaken in its approval of the IGCC technology instead of a gas-fired combined cycle unit at the Polk site. Mr. Rowe also discusses why alternative ratemaking issues should not be addressed in this proceeding.

2. Stephen L. Thumb
(Energy Ventures
Analysis, Inc.)

Mr. Thumb describes the significant differences in the fundamentals of supply and demand for coal and natural gas which explain why the prices for these fuels are not linked and why the price differential between these two fuels should be expected to grow over time. Mr. Thumb also describes the unanticipated circumstances which led to a wide range of uncertainty among forecasters as to when (but not whether) the excess supply of gas which materialized over the last ten years would end, leading to sharply higher gas prices. Finally, Mr. Thumb explains that Mr. Breman's testimony is irretrievably incorrect as the result of a flawed statistical analysis and its failure to take into account the anomalous events of the last several years which have temporarily masked an upward trend in gas prices.

3. Hugh W. Smith
(Tampa Electric)

Mr. Smith, although observing that today's gas prices are actually higher than those forecasted by Tampa Electric, emphasizes that reasonableness at the time a forecast is made rather than accuracy measured by hindsight is the proper standard for this proceeding. He then explains why Tampa Electric's fuel forecasts have consistently met this standard of reasonableness. Mr. Smith goes on to explain the reasonableness of Tampa Electric's use of as-available natural gas and petroleum coke feedstock in the company's Polk cost-effectiveness studies.

4. Thomas L. Hernandez
(Tampa Electric)

Mr. Hernandez points out that the Commission and Staff have periodically considered and found reasonable the same planning methodology and basic assumptions used by Tampa Electric in connection with its ongoing Polk project cost effectiveness studies. He also explains the circumstances which underscore the reasonableness of the company's assumptions. Finally, he explains that differences in generation mix, system economics, and DOE funding render meaningless the apparent parallels which the Staff and intervenor have attempted to draw between the prudence of Tampa Electric's Polk investment and the decisions by other utilities not to construct IGCC units on their systems at the present time.

5. Charles R. Black
(Tampa Electric)

Mr. Black will explain that, contrary to OPC Witness Larkin's assertions, the timing and extent of Tampa Electric's gasifier-related financial commitments would have been precisely the same under either a phased or integrated construction schedule for the plant. He further explains that even if it had made sense from an economic standpoint to abandon the IGCC project in favor of a gas-fired combined cycle unit, which it did not, a phased construction schedule would not have reduced the company's gasifier-related sunk costs and would have had no

meaningful effect on the company's IGCC cost-effectiveness analysis. He will describe the adjustments in plant design and construction which have allowed the company to deliver an extremely cost-effective resource.

C. EXHIBITS

<u>Exhibit</u>	<u>Witness</u>	<u>Description</u>
<u>(HWS-1)</u>	Smith	Interrogatories filed in Dockets 950379-EI and 960409-EI
<u>(TLH-1)</u>	Hernandez	Eight documents relied upon by Mr. Hernandez in support of his prepared direct testimony
<u>(CRB-1)</u>	Black	Twenty-seven documents relied upon by Mr. Black in support of his prepared direct testimony
<u>(JRR-1)</u>	Rowe	Eight documents relied upon by Mr. Rowe in support of his prepared direct testimony
<u>(EAT-1)</u>	Townes	Ten documents relied upon by Ms. Townes in support of her prepared direct testimony
<u>(Rebuttal)</u>		
<u>(SLT-1)</u>	Thumb	Ten documents relied upon by Mr. Thumb to support his testimony.
<u>(HWS-2)</u>	Smith	Five documents relied on by Mr. Smith support his testimony.
<u>(TLH-2)</u>	Hernandez	Ten documents relied on by Mr. Hernandez to support his testimony.
<u>(CRB-2)</u>	Black	Three documents relied upon by Mr. Black to support his testimony.

D. STATEMENT OF BASIC POSITION

Tampa Electric Company's Statement of Basic Position:

All of the costs associated with Tampa Electric's Polk Unit One have been prudently incurred and should be approved by this Commission without disallowance or resort to an alternative ratemaking mechanism. The positions of Staff and intervenors stem in no small part from their basic premise, that this Commission erred in Decision No. PSC-92-0002-FOF-EI (the "Need Order") in not requiring that Tampa Electric build a natural gas-fired, combined cycle unit instead of the IGCC unit which the Commission found to be the most cost-effective alternative, following extensive investigation. This flawed premise cannot be screened by the assertion that their criticisms relate primarily to the period following the Need Hearing. The Staff and other parties have failed to substantiate any tangible set of circumstances, occurring after the Need Hearing, that required, as a matter of prudence, that the project approved by the Commission be jettisoned in favor of the natural gas-fired, combined cycle generation alternative already rejected by the Commission for Tampa Electric's system.

In the company's view, the Commission made the correct decision in the Need Order, based on an extensive and well-examined record. Tampa Electric's ongoing cost-effectiveness studies, which were conducted as a matter of prudence, have consistently affirmed the correctness of the Commission's endorsement of the Polk IGCC project. These ongoing cost-effectiveness studies were based on reasonable assumptions at the time each study was conducted.

The question before the Commission in this proceeding, in evaluating the prudence of the company's Polk-related investment, is whether or not the company had a rational basis for the project-

related decisions made subsequent to the Commission's approval of the Polk IGCC unit. The question is not what the Commission would have done had it been exercising the power of management at the time or whether another reasonable person confronted with the same set of facts and circumstances could have made different decisions. Instead, the Commission should satisfy itself that there was a rational basis for Tampa Electric's project-related decisions, given the facts which were known, or should have been known, at the time the decisions in question were made. Under this standard, the prudence of Tampa Electric's project decisions and the resulting investment is very clear.

In its September 5, 1991 Petition for Determination of Need, Tampa Electric explicitly asked this Commission to approve the construction of a 220 MW IGCC Unit and related facilities at a site located in Polk County. During the Need Hearing, the size of the proposed project was increased to 260 MW, as noted at page 8 of the Need Order. In the Need Order, this Commission announced several conclusions in the course of approving this petition, none of them tentative or interim, which bear directly on the present inquiry.

The Need Order provides the following:

FINAL APPROVAL OF POLK IGCC UNIT

It is ordered by the Florida Public Service Commission that, for the reasons, and with the conditions, set out in the body of this order, Tampa Electric Company's Petition for Determination of Need for a Proposed Electrical Power Plant and Related Facilities in Polk County is hereby Granted. (Need Order, p. 17)

FINAL APPROVAL CONDITIONED ONLY ON RECEIPT OF DOE GRANT

We have considered all issues relevant to those topics (set forth in Section 403.519, Florida Statutes) and we hold, for the reasons set out below, that Tampa Electric has demonstrated

the need for the proposed 220 MW IGCC plant. We approve the construction on the condition that TECO does receive the \$120 million grant from the Department of Energy to help defray the costs of the project. (Need Order, p. 3);

APPLICATION FILED AT A REASONABLE TIME

Given the lead time necessary for utilities to construct new generating facilities, TECO's petition was filed at a reasonable time. (Need Order, p. 4);

IGCC UNIT WILL CONTRIBUTE TO STATEWIDE RELIABILITY

We believe the addition of the proposed IGCC plant will contribute to the reliability of the electric system of the State of Florida by providing capacity in the time frame in which it is needed. (Need Order, p. 5);

POLK IGCC UNIT REPRESENTS THE MOST COST-EFFECTIVE ALTERNATIVE

...In this proceeding the determinative issue is whether it is cost effective for TECO and TECO's ratepayers to incur the higher capital cost of an IGCC unit to enable use of lower cost coal fuel. That appears to be the case here, because the DOE grant significantly lowers the total capital cost of the project. As we will explain in detail below, the IGCC unit is the most cost-effective alternative to meet TECO's capacity needs. That fact drives our decision to grant TECO's petition. (Need Order, p. 6);

TECO's IGCC unit with DOE funding is more cost-effective than the combined cycle unit in Docket No. 910004-EU. (Need Order, p. 15);

TECO FUEL PRICE FORECAST REASONABLE

With certain reservations, we find that TECO's fuel price forecast is reasonably adequate for planning purposes. (Need Order, p. 6);

PROJECT COST-EFFECTIVE UNDER A WIDE VARIETY OF FUEL PRICE ASSUMPTIONS

Due to concerns regarding the sensitivity of TECO's fuel forecasts, our Staff asked TECO to perform an economic comparison of its proposed IGCC unit (using coal) and the phased combined cycle unit from Docket No. 910004-EU (using five different gas forecasts for the phased CC unit). Throughout the capacity factor range in which TECO plans to operate its IGCC unit (around 80%) the IGCC plant was cost

effective under all fuel price scenarios. ...The (revenue requirements) analysis concluded that TECO's proposed IGCC unit is cost effective under all fuel price scenarios, including our Staff's "acid test", at both the low capacity factor of 60% and the expected capacity factor of 80%. ... TECO also performed a cost comparison between its proposed IGCC project and FPL's current avoided unit, a 1997 IGCC unit. Compared to FPL's avoided unit, TECO's proposed project is more cost-effective. (Need Order, pp. 10-11);

PROJECT ALTERNATIVES ADEQUATELY EXPLORED

TECO demonstrated in this proceeding that it adequately explored the construction of alternative generating technologies. (Need Order, p. 12);

We do believe TECO has adequately considered the conservation measures that would be reasonably available to avoid the need for this proposed plant. (Need Order, p. 13);

The record demonstrates that TECO adequately explored and evaluated the availability of purchased power from other utilities. (Need Order, p. 15);

SUFFICIENT INFORMATION PROVIDED FOR DECISION

TECO provided sufficient information on the site design and engineering characteristics of its 220 MW unit to enable us to adequately evaluate its proposal. (Need Order, p. 8);

The Need Order was a final and definitive charge to Tampa Electric to go forward with its plans to construct an IGCC unit at the Polk site, and this is exactly what the company did. The Staff and other parties to this proceeding suggest, in various ways, that the Need Order, containing the language set forth above, was tentative or interim in nature. We respectfully submit that no reasonable person could come to that conclusion.

With the Commission's Need Certification in hand, the company proceeded with the tasks of securing the required site certification and environmental permits, preparing detailed site development and engineering plans and ordering the equipment and materials necessary to construct the plant in a timely manner.

As the costs of the plant components and site preparation became clearer from the completion of the permitting process and detailed engineering, the company made a number of changes in the construction schedule and in the configuration of the project, none of which compromised the essential nature of the project. These adjustments allowed Tampa Electric to build the approved unit cost-effectively.

The intervenors and Staff suggest that Tampa Electric's decision not to phase construction of the IGCC unit, as anticipated at the time of the need hearing, represented a material deviation from the need order. Based on this faulty premise, the parties further assert that the decision to abandon the phased construction schedule deprived the company of a last clear change to switch to a gas-fired, combined cycle unit without incurring any gasifier-related sunk costs. The simple truth is that these assertions have no basis in fact.

Putting aside for the moment the fact that there has never been any reason to abandon the IGCC technology since it has remained consistently cost-effective, the "opportunity" to change generation technology without incurring gasifier-related sunk cost never existed. From the beginning the Polk IGCC unit was planned and constructed as an integrated unit. The phased construction described during the need hearing represented a more expensive construction approach adopted only to meet an expected need for additional capacity in 1995, a year before the integrated unit could be put on line. When Tampa Electric's ongoing studies indicated that the needed capacity could be deferred to 1996, the company reverted to the more economic integrated construction approach. However, the key point which the parties have missed is that the timing of Tampa Electric's financial commitments with regard to the gasifier portion of the plant would have been precisely the same under either the

phased or integrated construction approach. Their suggested last clear change to switch to natural gas-fired technology never existed.

TAMPA ELECTRIC TIGHTLY CONTROLLED PROJECT COSTS

The company put in place a stringent cost control and project management mechanism to insure that costs would be prudently incurred. For instance, when the detailed engineering for the planned hot gas clean up system suggested a cost much greater than either the Department of Energy or Tampa Electric expected, the company worked closely with DOE to scale back the system to keep the total project costs within budget while assuring DOE that all of the anticipated test data from the hot gas cleanup system demonstration would be obtained. This adjustment had no impact on the Commission's prior project cost-effectiveness analysis since the benefits of the hot gas clean up system had not previously been considered. However, the opportunity for incremental benefits associated with the scaled down system was preserved.

In view of a ready market near the plant, the company also modified the project plan to include a facility for the production of sulfuric acid rather than the sulfur recovery system originally planned. This change will result in increased by-product revenues to offset project costs. While the parties take issue with these decisions and assert that they represent a material departure from the project approved in the Need Order, these decisions represent nothing less than the prudent cost management which the Commission expects from the company. Tampa Electric has been able to complete the construction of the project at a cost which is estimated to differ from the pre-engineering estimate presented in the Need Hearing by only 4.3%, excluding land acquisition and site development costs. This was a considerable accomplishment considering that the company was bringing into service a new technology for which the

detailed engineering had not been completed at the time of the Need Hearing.

Tampa Electric was not in a position to estimate site development costs with any precision at the time of the Need Hearing, since site development costs would be primarily a function of the environmental permit conditions and detailed engineering studies which remained to be completed. The land and site development costs reflected in the estimated total completion cost of \$506 million are reasonable and compare very favorably with the total land and site preparation costs which Florida Power Corporation expects to incur in connection with its new power plant that is also sited inland on mined phosphate property in Polk County.

TAMPA ELECTRIC REGULARLY AFFIRMED PROJECT COST-EFFECTIVENESS AFTER THE NEED HEARING

Tampa Electric continued to evaluate the cost-effectiveness of Polk Unit One subsequent to the Need Hearing. This evaluation included a continued review of key planning assumptions and forecasts and a review of several cost-effectiveness studies completed during the construction of Polk Unit One. The review of key planning assumptions included new developments in the demand and energy forecasts, fuel price and availability forecasts, and updates to the Polk unit construction cost estimates. Using the best available information at the time of each evaluation, Tampa Electric concluded in each review that the IGCC unit remained the most cost-effective energy resource alternative. There have been numerous Commission proceedings and Staff reviews, including the review of Tampa Electric's Ten Year Site Plan filings and Conservation Goals proceeding, since the Need Hearing in which the Commission found that Tampa Electric's planning assumptions and methodology and the resulting expansion plans were reasonable and suitable.

Even though Tampa Electric's Polk project was proven cost-effective under all of the gas price forecast scenarios considered by the Commission in the Need Hearing, in 1991 and 1992, some of them very unrealistic, Tampa Electric took to heart the Commission's caution, at page 6 of the Need Order, to pay close attention to the continued accuracy of its fuel price forecasts, especially with regard to the anticipated differential between forecasted gas and coal prices. Subsequent to the Need Hearing, the company repeatedly reevaluated its fuel price forecasting methodology and consulted a wide variety of external forecasts in order to insure the forecasting vigilance expected by the Commission. Tampa Electric's fuel forecasts were based on rational and reasonable assumptions. The company's continued forecast of divergence between coal and gas prices is consistent with reasonable expectations with regard to future trends in the energy market. The question to be addressed in this proceeding is not whether the company's forecasts were accurate when judged on the basis of hindsight. Instead, the question to be asked is whether there was a rational basis for the forecasts used by Tampa Electric, given what was known at the time the forecasts were made. The answer, which is without credible contradiction, is that the company's fuel forecasts were based on reasonable assumptions.

The Staff and other parties attempt to make much of the fact that Tampa Electric has forecasted rising gas prices over the last several years in the face of lower than expected actual gas prices. However, their concern is based on a lack of understanding of the natural gas supply and demand fundamentals which have determined gas prices over the last ten years. Since the mid-1980's and until recently, there has been a huge oversupply of natural gas, referred to as a gas bubble, building in the U.S. This oversupply resulted in a downward trend in gas prices and, significantly, in a dramatic decrease in drilling and exploration activity by producers who realized that the low gas prices would not permit them to recover the

large costs of that activity. Given these circumstances, knowledgeable forecasters knew that it would be only a matter of time before the oversupply situation abated due to increased demand and the lack of replenishing drilling activity.

Tampa Electric's projected prices were based, in effect, on a forecast that natural gas oversupply and excess deliverability would decrease in the very early 1990's, resulting in sharply higher gas prices. However, a number of unforeseeable events postponed this event. Long term fuel price forecasts are based on average or normal weather conditions but the much warmer than normal winter weather experienced over the last several years resulted in a dramatic decrease in demand for natural gas, thereby postponing the end of the gas bubble. In addition, a tax incentive which expired in 1992 created drilling incentives which artificially boosted supply on a temporary basis. As a result, there was widespread disagreement among fuel price forecasters as to when, but not whether, the oversupply would end.

Tampa Electric was correct in predicting a significant decrease in excess deliverability, resulting in an upward trend in gas prices which we see today. In fact, the company's 1992, 1993, 1994, and 1995 forecast of 1996 gas prices were all significantly less than today's actual gas prices. The company's expectation that excess deliverability would decrease in the early 1990's was a bit premature when viewed through hindsight, but was reasonable nonetheless, given what was known at this time.

Other assumptions used in the cost-effectiveness analyses were updated throughout time. As the construction and other project-related expenses were incurred in reliance on the Need Order, Tampa Electric factored these "sunk costs" into the economics of switching to another generation technology. It would have been foolish to

ignore these sunk costs in its ongoing cost-effectiveness studies since these prudently incurred costs would have been passed through to its customers in the event of project abandonment or modification. The company also considered, in its economic analysis at various times, the availability of a tax credit under Section 29 of the IRS code and, alternatively, the use of an economic pet coke blend as a feedstock for the plant's gasifier. These additional inputs to the company's various forecasts were demonstrably rational and reasonable. In short, Tampa Electric constantly examined and tested the key assumptions underlying its cost-effectiveness analyses to insure that our customers would enjoy the maximum benefit possible from the plant addition.

CONCLUSION

Tampa Electric has constructed the Polk IGCC project, which this Commission approved, in a prudent manner. The company has monitored the cost-effectiveness of the project, both prior to and during the construction phase. The company has constantly reviewed and tested its analyses, including its fuel price forecast methodology and economic assumptions to insure a high confidence level in its cost-effectiveness analyses. The company has carefully monitored and controlled project-related costs. In short, Tampa Electric has done everything necessary to warrant Commission approval of its full investment in the Polk IGCC project.

E. STATEMENT OF ISSUES AND POSITIONS

Issue 1:

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Legal Issue

What is the appropriate legal standard of review in a prudence review?

Tampa Electric:

The test for prudence is one of reasonableness.

A determination of prudence or imprudence calls for an inquiry into the reasonableness of management's judgement, i.e., whether there was a rational basis for the judgement rather than an inquiry into the wisdom of the judgement. The standard is not what the Commission would have done had it been exercising the power of management at the time or whether another reasonable person confronted with the same set of facts and circumstances could have made different decisions. Instead, the issue is only whether there was a rational basis for Tampa Electric's project-related decisions given the facts which were known, or should have been known, at the time the decisions in question were made.

ISSUE 2: 1

Planning Issues

Was the continued construction of the Polk IGCC unit by Tampa Electric Company reasonable and prudent?

Tampa Electric:

Yes. Tampa Electric's continued construction of Polk Unit One was reasonable and prudent. There were no changed circumstances subsequent to the issuance of the Need Order which required or even suggested a different course. Even though not required to do so, the company repeatedly evaluated the cost-effectiveness of the IGCC unit, both before and during the construction phase and confirmed its continuing cost-effectiveness each time.

Tampa Electric continually reviewed and tested the economic assumptions underlying its cost-effectiveness analyses and made adjustments where warranted. The company also continued to evaluate its fuel price forecasting methodology and consulted a broad collection of external forecasts. (Witnesses: Anderson, Smith, Hernandez, Black, Bechtel, Rowe)

ISSUE 3:

Were Tampa Electric Company's assumptions regarding sunk costs in each of its annual cost-benefit analyses reasonable?

Tampa Electric:

Yes. The construction and other project related costs incurred in justifiable reliance on the Commission's approval of the Polk IGCC unit represented costs prudently incurred. As such, these expenditures would have been appropriately recovered from Tampa Electric's customers in the event of project cancellation or modification. Therefore, in assessing the cost-effectiveness or ratepayer impact of continuing with the IGCC technology, it would have made no sense to exclude these costs from the cost-effectiveness calculations.

Tampa Electric's quantification of these sunk costs in each of its annual cost-benefit analyses was quite conservative since it was based only on dollars actually booked instead of all the commitments previously made. (Witness: Hernandez, Black)

ISSUE 4: 3

Were Tampa Electric Company's assumptions regarding variable operations and maintenance expense in each of its annual cost-benefit analyses reasonable?

Tampa Electric:

Yes. Tampa Electric's cost-benefit analyses were based on comparing total system revenue requirements for various generating alternatives and included the impact of total system O&M expense, fuel expense, and capital costs for Tampa Electric's existing and planned generating units. While the allocation between fixed and variable O&M costs varied between analyses, the total O&M expense associated with the IGCC, combined cycle, and combustion turbine technologies were comparable and reasonable for each of the cost-benefit analyses. (Witnesses: Black, Hernandez)

ISSUE 5: 4

Were Tampa Electric Company's assumptions regarding tax credits in its 1994 and 1995 Polk IGCC cost-benefit analyses reasonable?

Tampa Electric:

Yes. When the benefits associated with the Section 29 tax credit were reflected in Tampa Electric's cost-effectiveness studies, in 1994 and 1995, the company had every reason to believe that the tax code would be amended to permit Tampa Electric to claim the credit.

Prior to 1994, the company did not assume the

availability of the Section 29 tax credit in its cost-effectiveness analyses since the tax law had not yet been amended to extend the deadline for project completion required in order to qualify for the credit. Although the pet coke blend feedstock assumption suggested very significant benefits, it was displaced in the company's 1994 and 1995 studies in favor of the Section 29 tax credit assumption in light of the company's belief that the further amendments to the tax law required in order for the company to claim the credit could be accomplished in a timely manner. The two assumptions were interchangeable in terms of the anticipated benefits but they could not reasonably have been used together since Section 29 required that coal be burned in order for the syngas to qualify for the credit. When it became clear, in late 1995, that the probability of achieving the required amendment to the tax code had been reduced significantly as the result of a change in the congressional leadership, the company replaced the availability of the Section 29 credit in its cost-effectiveness assumptions with the use of a pet coke feedstock for the plant gasifier. (Witnesses: Rowe, Hernandez)

ISSUE 6: 5

Did Tampa Electric Company adequately address its declining demand and energy forecasts in each of its annual cost-benefit analysis?

Tampa Electric:

Yes. The company's demand and energy forecasts

used in the cost-benefit analyses were the same as the forecasts provided in Tampa Electric's 1992 rate case proceedings and its 1992, 1993, 1994, and 1995 Ten Year Site Plan filings. In all of the reviews of Tampa Electric's demand and energy forecasts, the Commission found that its forecasts were reasonable and suitable for planning purposes. The impact of each demand and energy forecast on system reliability and system production costs and generation expansion plans were included in each cost-benefit analysis. In fact, the deferral of the advanced combustion turbine from July 1995 to July 1996 was determined in the 1993 cost-benefit analysis and reported in Tampa Electric's 1994 Ten Year Site Plan filing.
(Witness: Hernandez)

ISSUE 7: 6

Fuel Issues

Has Tampa Electric Company demonstrated that its 1992, 1993, 1994, and 1995 fuel price forecasts were reasonable and prudent?

Tampa Electric:

Yes. Tampa Electric has demonstrated that its 1992 through 1995 fuel price forecasts were reasonable and prudent. Fuel price forecasting is a subjective and judgmental process requiring expertise in many areas of the energy business. As this Commission recognized in Order No. 23080, concerning FP&L's Martin Expansion Project:

We note, however, that the best fuel forecasts are only that: educated estimates of future market conditions. And, we observe that the only thing which is absolutely predictable in this area is that no matter who does it or how carefully it is done, the forecast will be incorrect. (Order No. 23080, p. 6)

Obviously, reasonable people can disagree over projections of oil and natural gas prices 20 to 30 years into the future. The Commission should not judge the reasonableness of a long range forecast based on a relatively short period of actual data when it is the long term trends which drive the savings associated with large capital projects such as the Polk IGCC unit. Tampa Electric's forecasts were in a zone of reasonableness at the time they were made. Tampa Electric correctly forecasted the upturn in natural gas prices which we see today but was unable to foresee that the decrease in excess deliverability which led to higher prices would be postponed by warmer than normal winter weather and other unpredictable circumstances.

In addition, Tampa Electric took very seriously this Commission's caution in the Need Order to pay careful attention to the forecasted price differentials between coal and gas. In fact, in the years following the Need Hearing, the price differentials between gas and coal decreased substantially in Tampa Electric's fuel forecasts. (Witness: Smith)

ISSUE 8:

7

Tampa Electric:

Has Tampa Electric Company demonstrated that pet coke is a reliable and viable fuel for the Polk IGCC Unit?

Yes. Texaco's proven, commercially available gasification technology, on which the Polk IGCC unit is based, is extremely flexible with respect to the feedstock used to create the syngas. Among the feedstocks used commercially are a wide range of coal (high and low sulfur) and petroleum coke/coal blends of up to 90% petroleum coke. Commercial experience underscores the viability of pet coke as a reliable feedstock for the Polk IGCC unit. Petroleum coke has been demonstrated to be commercially available and economically priced. In fact, at least four utilities in Florida are currently purchasing and burning pet coke in existing facilities. (Witnesses: Black, Smith)

ISSUE 9:

8

Tampa Electric:

Were Tampa Electric Company's assumptions regarding the combined use of as-available natural gas and light oil as the primary fuels for a combined cycle alternative in its 1994, 1995, and 1996 Polk IGCC cost-benefit analysis reasonable?

Yes. Using as-available gas during those times of the year when there would be relatively little demand for gas, and light oil during those periods of high demand for gas, was the most realistic and reasonable assumption for

Tampa Electric's system.

The hypothetical combined cycle unit considered in the company's 1994, 1995 and 1996 cost-effectiveness studies would have been operated at a low load factor, given the economics of Tampa Electric's system. It would have been dispatched after existing coal resources instead of as the first unit dispatched which is the case for the IGCC unit. Therefore, it would make no sense to assume firm natural gas transportation for this combined cycle unit since Tampa Electric would have no use for the gas transportation most of the time. The company's need for the gas would exist at the very times that gas would be in demand by others. Under these circumstances, one could not reasonably assume that Tampa Electric would have unused gas to sell at peak periods. Likewise, one could not reasonably assume that there would be an acceptable market for our unused gas during off-peak periods.
(Witnesses: Hernandez, Smith)

ISSUE 10:

Was it reasonable for Tampa Electric Company to assume as-available natural gas transportation rather than firm gas transportation in its 1992, 1993, 1994, and 1995 Polk IGCC cost-benefit analyses?

Tampa Electric:

Yes. For the reasons explained in response to Issue 9 above, the purchase of firm gas

transportation would not have been economic on Tampa Electric's system. An analysis of these two scenarios indicates that the use of firm gas transportation would have cost Tampa Electric ratepayers over \$100 million more than the as-available assumption used in Tampa Electric's cost-effectiveness studies. (Witnesses: Smith, Hernandez)

ISSUE 11: 9

Rate Base Treatment

What is the appropriate amount of the Polk IGCC Unit's cost to be included in rate base?

Tampa Electric:

The thirteen month average of the first full year of operation of the Polk unit should be included in rate base as shown on Exhibit ___ (EAT-1), Document 1, of the Direct Testimony of Elizabeth A. Townes. The amount shown includes the \$506,165,000 capital investment, accumulated depreciation of \$13,009,000, and working capital in the amount of \$13,029,000. (Witnesses: Black, Rowe, Townes)

ISSUE 12: 10

What is the appropriate amount of the Polk IGCC cost to be included in the calculation of net operating income?

Tampa Electric:

The full operating expense, which is currently estimated to be \$20,582,000, should be included in the calculation of net operating income as shown on Exhibit EAT-1, Document No. 1. This amount consists of a net O&M component of

\$3,816,000, depreciation expense of
\$22,301,000, and taxes of \$(5,535,000).
(Witnesses: Rowe, Townes)

ISSUE 13:

What are the appropriate capital structure components associated with the Polk IGCC Unit?

Tampa Electric:

The Polk unit should be treated like any other investment which is supported on a prorata basis by the company's total capital structure.

As explained in its June 21, 1996 motion requesting an order declaring certain issues to be beyond the scope of this proceeding, Tampa Electric objects to the consideration of this issue in this proceeding. This issue has nothing to do with the prudence of Tampa Electric's Polk investment. In Order No. PSC-96-0670-S-EI, this Commission adopted a joint stipulation, which resolves all Tampa Electric rate of return issues through 1998. In fact, paragraph 11 of the stipulation provides that the calculations of the actual ROE for each calendar year during the term of the stipulation will be done on an FPSC adjusted basis, using the appropriate adjustments approved in Tampa Electric's last full revenue requirements proceeding. To the extent that the staff or other parties wish to advance a case for a different capital structure, the time to advance such positions would be in Tampa Electric's next rate case or cost of

capital proceeding. (Witnesses: Rowe, Townes)

ISSUE 14: 12

What is the appropriate regulatory treatment for the Port Manatee site?

Tampa Electric:

Tampa Electric's entire investment in the Port Manatee site (\$4,879,076 as of March 21, 1996) should continue to be classified as property held for future use and included in rate base as the Commission determined in 1992 in Order No. 93-0165 in Docket No. 920324-EI. There has been no significant change in circumstances since the 1992 case which would warrant reconsideration of the Commission's decision.

An electric utility with the obligation to serve should have multiple options for the placement of new generating facilities. Consistent with this principle, utilities such as Florida Power & Light have a wide variety of future plant sites in rate base, including partially developed and undeveloped sites. The Port Manatee site provides a valuable option for a future power plant site or other utility-related use. While the site may not be suitable for a large coal or IGCC plant, it may be well suited for other kinds of new or emerging generation technologies. (Witnesses: Rowe, Smith)

ISSUE 15: 13

How should the capital, O&M and fuel costs associated with wholesale sales made from the

Polk IGCC unit be separated from the retail jurisdiction?

Tampa Electric:

The separation procedure to be used to separate capital and O&M was approved in the company's last rate case, Docket No. 920324-EI and will be followed.

As explained in its June 21, 1996 motion requesting an order declaring certain issues to be beyond the scope of this proceeding, Tampa Electric objects to the consideration of this issue in this proceeding. This issue has nothing to do with the prudence of Tampa Electric's Polk investment. As required by the Joint Stipulation, a portion of the company's Polk-related investment will be allocated to Tampa Electric's wholesale rate base. The separation procedure as approved in the company's last rate case will be used to separate capital and O&M. No other assignment of the Polk IGCC unit to wholesale rate base is necessary. Proposed changes to the currently approved jurisdictional separation procedure have nothing to do with the prudence of Tampa Electric's Polk-related investment. This issue can be addressed at such time as the company files an application to adjust its rates, without any prejudice to the position of any party. The allocation of fuel expense associated with a sale from the Polk IGCC unit can be addressed in the Fuel Adjustment

proceedings. (Witness: Rowe)

ISSUE 16:

Alternative Ratemaking Treatments

Should the Commission adopt an alternative method for cost recovery of Tampa Electric's Polk IGCC unit?

Tampa Electric:

No. Tampa Electric has voluntarily agreed to a ratemaking plan which will result in the commercial operation of a major plant addition without any adjustment of base rates to reflect the significant increase in revenue requirements through 1998. At the same time, the company will make a refund to customers of \$25 million, with the possibility of additional refunds in 1999. The company respectfully suggests that it would be difficult, if not impossible, to devise a more innovative and creative alternative to conventional ratemaking for a major plant addition than the approach already adopted by the Commission when it approved the Joint Stipulation.

As explained in its June 21, 1996 motion requesting an order declaring certain issues to be beyond the scope of this proceeding, Tampa Electric also objects to the consideration of this issue in this proceeding. This issue has nothing to do with the prudence of Tampa Electric's Polk investment. Tampa Electric respectfully suggests that there is simply no

useful purpose to be served in using the limited time allotted to this proceeding to consider cost recovery alternatives. Paragraph 11 of the above mentioned Stipulation provides that all reasonable and prudent expense and investment will be allowed in the computation of ROE during the Stipulation period. Once Tampa Electric's Polk investment has been proven prudent, the Stipulation requires that all of that prudent investment be reflected in the ROE calculation as opposed to alternative ratemaking approaches. Tampa Electric has proceeded prudently with the construction of the IGCC plant authorized by the Commission in the Need Hearing and sees no need to complicate the recovery of the company's prudent expenditures. Since no rate increase is pending to recover Tampa Electric's investment in the Polk IGCC, it would be premature to consider alternative methods for cost recovery. Issues of rate design and cost allocation are well beyond the scope of this proceeding. Issues related to recovery of stranded investment in the event Florida law is changed to allow retail wheeling are also entirely premature.

F. STIPULATED ISSUES

Tampa Electric: None at this time.

G. MOTIONS

Tampa Electric: On June 21, 1996, Tampa Electric filed a motion

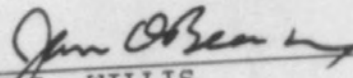
for an order declaring certain issues to be beyond the scope of this proceeding. In particular, the company requested an order declaring that issues 13, 15 and 16 above are beyond the scope of this proceeding.

H. OTHER MATTERS

Tampa Electric: None at this time.

DATED this 9th day of July, 1996.

Respectfully submitted,



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CERTIFICATE OF SERVICE

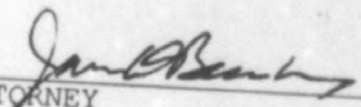
I HEREBY CERTIFY that a true copy of the foregoing Prehearing Statement, filed on behalf of Tampa Electric Company, has been furnished by U.S. Mail or by hand delivery(*) on this 9th day of July, 1996 to the following:

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