BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Progress Energy Florida, Inc.'s petition for approval of storm cost recovery clause for extraordinary expenditures related to Hurricanes Charley, Frances, Jeanne, and Ivan.	Docket No.: ____________________ Submitted for Filing: November 2, 2004

PETITION

Pursuant to Sections 366.04 and 366.05, Florida Statutes, Rule 25-6.0143, F.A.C., and the orders of the Florida Public Service Commission ("PSC" or the "Commission"), Progress Energy Florida, Inc. ("PEF" or the "Company") respectfully petitions the Commission for establishment of a Storm Cost Recovery Clause to allow PEF to recover extraordinary expenditures related to Hurricanes Charley, Frances, Jeanne, and Ivan, which between mid-August and late September 2004 struck the State of Florida, causing billions of dollars in damage and leaving 8.8 million Florida residents without power. In a span of just six weeks, PEF incurred extraordinary storm-related costs -- approximately $366 million.

For the reasons set forth in detail below, PEF requests the Commission to establish a Storm Cost Recovery Clause that will allows PEF to recover from its ratepayers over two years its reasonable storm costs in excess of the balance in its storm reserve. The clause should provide for the recovery of the Company's storm-related Operation and Maintenance (O&M) costs, including in part its costs in excess of typical charges under normal operating conditions for capital expenditures. As allocated to the Company's retail jurisdiction, based on current estimates, the total amount to be recovered is $251.9 million. The $251.9 million plus interest will be recovered over two years in equal amounts, resulting in the recovery of $132.2 million in 2005 and $128 million in 2006, based on a January 1, 2005 start date. PEF's storm-related costs classified as capital expenditures will <u>not</u> be recovered directly from customers under the Storm

Cost Recovery Clause. Rather, the $50.1 million in storm-related capital expenditures allocated to the Company's retail jurisdiction will be reported in surveillance reports and absorbed in current rates until the Company's next base rate adjustment.

The Storm Cost Recovery Clause should further incorporate the same procedural and substantive mechanisms as other cost recovery clauses implemented by the Commission, including, for example, the true-up of estimates of costs and sales to actual costs and sales, with interest provided for any amounts carried forward that are under or over the actual costs, and the determination that the costs were reasonable and prudently incurred. Storm costs recovered under the clause will be recovered from all retail customers and will be allocated among customers in the various rate classes in the same manner that costs were allocated among the rate classes in the Company's last base rate proceeding. The impact to the average residential customer bill (1,000 KWH per month) is expected to be $3.81 for 2005 and $3.59 for 2006. These estimates are based on a start date of January 1, 2005 and would change if that date moved.

A Storm Cost Recovery Clause will serve the public interest. It will end the regulatory uncertainty concerning recovery mechanisms that currently exist for costs incurred due to the infrequent, catastrophic hurricane or major storm. Commercial insurance coverage is no longer available for such storms, and the storm reserves established by the Commission were not designed to cover them. All parties benefit from the Storm Cost Recovery Clause. PEF can fulfill its statutory obligation to serve by safely and expeditiously restoring power for its customers with the understanding that PEF will be timely reimbursed, just as PEF was before with insurance coverage, for its reasonable and prudently incurred costs to prepare for, respond to, and recover from catastrophic storms. Customers certainly benefit from the continued assurance that their electric service will promptly and safely be restored following such major storms.

In further support of this Petition, PEF states as follows:

I. Preliminary Information

1. The Petitioner's name and address are:

Progress Energy Florida, Inc.
100 Central Avenue
St. Petersburg, FL 33701

2. All pleadings, motions, orders, and other documents directed to Petitioner should be served on the following:

Gary L. Sasso
James Michael Walls
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Carlton Fields
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Bonnie E. Davis
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Progress Energy Service Company, LLC
106 E. College Avenue, Ste. 800
Tallahassee, FL 32301-7740

3. All pleadings, motions, orders, and other documents served by hand or express courier to Petitioner should be served on the following:

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II. Facts and Relevant Background

4. PEF is an investor-owned electric utility, regulated by the Commission, and is a wholly owned subsidiary of Progress Energy, Inc., a registered holding company under the Public Utility Holding Company Act ("PUHCA"). PEF serves approximately 1.5 million retail customers in its service area in Florida. Its service area comprises approximately 20,000 square miles in 35 of the state's 67 counties, encompassing the cities of St. Petersburg and Clearwater and densely populated areas surrounding Orlando, Ocala, and Tallahassee. PEF supplies electricity at retail to approximately 350 communities and at wholesale to about 21 Florida municipalities, utilities, and power agencies in the State of Florida.

5. Prior to Hurricane Andrew in 1992, commercial property insurance was generally available to utilities at reasonable prices with adequate coverage for storm damage to transmission and distribution facilities. Florida Power & Light Company (FP&L), for example, had a transmission and distribution limit of $350 million per occurrence with a 1992 premium of $3.5 million. <u>In re: Petition to implement a self-insurance mechanism for storm damage to transmission and distribution system and to resume and increase annual contribution to storm and property insurance reserve fund by Florida Power and Light Company</u>, Order No. PSC-93-0918-FOF-EI, Docket No. 930405-EI, 1993 Fla. PUC Lexis 761, at *1 (June 17, 1993). Following Hurricane Andrew, however, when insurance policies had to cover storm costs approaching $300 million for FP&L, the investor owned utilities in Florida experienced difficulty renewing their insurance programs for transmission and distribution lines with

adequate coverage at a reasonable cost. FP&L, for example, was offered only $100 million as an annual aggregate loss for transmission and distribution at a minimum premium of $23 million. Id. As a result of the reluctance of commercial insurance carriers to provide reasonable transmission and distribution coverage, the investor owned utilities petitioned the Commission to implement self-insurance plans for storm damage to their transmission and distribution systems.

6. Since 1993, PEF has been operating under a self-insured plan for storm damage to its transmission and distribution systems that was approved by the Commission. The plan includes (1) the continued search for commercial insurance where it is reasonably available, which currently exists only for storm damage to generation facilities; (2) the accrual of monies for an unfunded storm reserve to address storm costs incurred as a result of a category 3 or less storm; and (3) the ability to request additional cost recovery in the event that storm costs exceed the storm reserve. Under this plan, PEF annually reports to the Commission on, among other things, its efforts to locate traditional insurance and its evaluation of the Company's exposure to storm damage and the adequacy of its storm reserve. In re: Petition of Florida Power Corporation for authorization to implement a self-insurance program for storm damage to its T&D lines and to increase annual storm damage expenses, Order No. PSC-93-1522-FOF-EI, Docket No. 930867-EI, 1993 Fla. PUC Lexis 1339 (October 15, 1993). The storm reserve accrual was originally set at $3 million annually based on a statistical study that examined probable storm occurrence, probable storm intensity, and probable level of storm damage. Id. at *5-6. This annual storm reserve accrual was increased to $6 million annually effective January 1, 1994. Order No. PSC-94-0852-FOF-EI, Docket No. 940621-EI. Before any offset of storm reserves against storm-related costs, the balance in PEF's storm reserve will be $46.9 million (system) as of December 31, 2004.

7. When the Commission granted PEF's request to implement its self-insurance plan, the Commission acknowledged that PEF's accrual to the storm reserve might not be adequate if a severe storm was experienced. The Commission declined the Company's request at that time to establish a mechanism for recovery of costs in excess of the available balance in the reserve. The Commission did not foreclose this option, however, directing the Company to petition the Commission for "appropriate regulatory action" if the Company experienced significant storm related damage. The Commission assured the Company that it would "expeditiously review any petition for deferral, amortization, or recovery of prudently incurred costs in excess of the reserve." Id. at *8.

8. In August and September 2004, four hurricanes (Charley, Frances, Jeanne, and Ivan) and one tropical storm (Bonnie) struck the State of Florida, ultimately impacting virtually every county in PEF's service territory and causing over two million cumulative customer outages during the course of the storms. Not since the 1880s has the destructive power of four hurricanes struck a single state, and never in Florida's history has this occurred. The economic devastation resulting from the impact of these storms on homes and businesses across Florida is in the billions of dollars. The storms have also exacted an enormous toll on PEF's transmission and distribution systems across Florida.

STORM PREPARATION AND MOBILIZATION

9. PEF's storm response efforts, and storm-related costs, commence well before the impact of hurricanes or storms are experienced in PEF's service territory. The goal of storm preparation efforts is to minimize the time needed to restore service following a storm. Storm response readiness is an around the clock effort that typically begins 96 to 72 hours before a storm is expected to have an impact on the Company's service territory. The Company

mobilizes internal resources that track storm course and intensity and estimate the need for and placement of additional personnel and materials as the storm passes through the service territory. Staging and logistic activities include predicting the storm path and intensity, determining the number and location of staging points for restoration activities, determining the number and placement of additional damage assessment and line and tree crews, and augmenting customer service representation. Outside work crews are recruited, organized, and dispatched to be in position to begin restoration efforts as soon as safety guidelines permit.

10. These activities are directed and coordinated through the Company's central storm management center, which in turn is integrated with the Company's regional service network. As a storm strikes PEF's service territory, damage assessment and prioritization of service restoration begins. Damage assessment includes verification of outages and downed or damaged facilities and equipment, determining resource needs, and establishing a schedule of restoration efforts and times. Once service restoration begins, the storm center continues to manage and direct the deployment of personnel and material to restore service beginning with the most critical customers and outages that have the greatest impact on the most customers. These storm preparation and management efforts are crucial to mitigating the duration of service outages, providing updates on restoration times, and accomplishing restoration as cost-effectively as exigent circumstances permit.

HURRICANE CHARLEY

11. On August 13, 2004, the first of four hurricanes struck land. The eye of Hurricane Charley made landfall at Punta Gorda in Charlotte County. At that time, Hurricane Charley was a category 4 hurricane on the Saffir-Simpson Hurricane Scale (rating hurricanes on a scale of 1 to 5 based on the destructive power of their winds), with winds of 145 miles per hour. Charley's

strongest gusts were measured at 180 miles per hour at Punta Gorda. Hurricane force winds extended outward up to 25 miles from the center of the storm, and tropical force winds extended outward up to 85 miles from the storm's center. Hurricane Charley proceeded on a north to northeast path across Florida, traveling through much of PEF's service territory, including the densely populated areas around Orlando, before leaving the state. The counties in PEF's service territory affected by Hurricane Charley were Citrus, Franklin, Gilchrist, Orange, Polk, Osceola, Highlands, Seminole, Volusia, Lake, Pinellas, and Hardee. 502,000 customers were left without electric service at the peak of Hurricane Charley's impact on PEF's service territory. This represents 32.7% of PEF's total number of customers.

12. As a result of Hurricane Charley, PEF experienced widespread damage to its transmission and distribution system. For example, PEF had to repair 630 damaged transmission structures, restore 83 de-energized substations, and repair or replace 700 miles of downed transmission lines. The Company used 667 miles of primary and secondary wire, replaced 3,820 poles, replaced 1,880 overhead and underground transformers, installed 31,140 insulators, and installed 27,710 splices during the work associated with the damage caused by Hurricane Charley. The total transmission and distribution storm-related costs are approximately $145.3 million. Of that amount, capital expenses are $37.5 million, and the storm-related O&M costs are $107.8 million.

13. PEF also suffered substantial damage to its generation facilities as a result of Hurricane Charley. This damage includes damaged roofs at Avon Park, a damaged cooling tower at Tiger Bay, damaged electrical connections for circulating water pumps at the Hines Energy Complex, damaged station batteries at Rio Pinar, a damaged equipment shelter, fence, and electric supply lines for water supply at Debary, damaged main lube oil pumps and a

damaged fence at Turner, and damage to the fence line at Intercession City. The total storm-related generation costs are $624,000. Of this total, $61,000 will be capitalized. The remaining $563,000 consists of storm-related O&M.

14. During Hurricane Charley, PEF mobilized 3,623 line and service personnel and 1,499 tree personnel in addition to its own personnel to ensure repairs were completed as efficiently as possible. PEF also handled 465,670 customer outage calls. All customers that were able to receive power were restored nine days after PEF started restoration work. Six days later, on August 28, 2004, PEF outage levels returned to historical average outage levels.

15. The total cost for the repairs or replacements to PEF's system caused by Hurricane Charley is approximately $146 million. Of this amount, approximately $37.5 million, will be capitalized. The remaining $108.4 million consists of Operation and Maintenance (O&M) costs that are properly chargeable against the Company's self-insured Storm and Property Insurance Reserve and qualify for payment from the Reserve.

HURRICANE FRANCES

16. On September 4, 2004, just a couple of weeks after Hurricane Charley, Hurricane Frances, a category 2 hurricane at the time it made landfall in Florida, reached the area between Fort Pierce and West Palm Beach with sustained winds of 105 miles per hour. Over the next several days, Hurricane Frances crossed over Florida and entered the Gulf of Mexico north of Tampa in PEF's service territory. Strong winds with gusts of near 100 miles per hour affected PEF's service territory for almost a full day. The storm also dumped 6-12 inches of rain on PEF's service territory with some regions receiving considerably more rain. The impact of Hurricane Frances on PEF's service territory was widespread: 30 of the 35 counties that PEF

serves were affected by the storm. 832,898 PEF customers lost power from Hurricane Frances during the course of the storm. This represents 54.4% of PEF's total number of customers.

17. As a result of Hurricane Frances, PEF experienced extensive damage to its transmission and distribution system. For example, PEF had to repair 211 damaged transmission structures and re-energize 105 substations knocked out or shut down due to the storm. Approximately 1,131 miles of transmission lines were downed or damaged. The Company used nearly 500 miles of primary and secondary wire, replaced 33,088 insulators, replaced 2,800 distribution poles, replaced 1,560 overhead and underground transformers, and installed 69,693 splices in the course of its storm-related work due to Hurricane Frances. The total transmission and distribution storm-related costs are approximately \$123.2 million. Of that amount, capital expenses are \$9.4 million and the storm-related O&M costs to date are \$113.8 million.

18. PEF again suffered damage to its generation facilities as a result of Hurricane Frances. Crystal River Unit 3 had a forced outage due to a failed line insulator and a 230kv bus fault. The Company further experienced excessive flooding at Debary and the Hines Energy Complex requiring the Company to rent pumps and generators. The Company also experienced damage to the well pump shed at Debary, along with tree and brush removal and fence repairs at Debary. At the Hines Energy Complex, the Company experienced erosion to the cooling pond divider dam. Finally, the Company also had to remove trees and had fence repairs at Turner. The total storm-related generation costs are approximately \$5.4 million. \$500,000 of this total will be capitalized. The remaining \$4.9 million are storm-related O&M costs.

19. In addition to its own personnel, PEF mobilized 2,819 system line and service personnel and 1,782 tree personnel to deal with the damage caused by Hurricane Frances. PEF handled 929,228 customer outage calls during the course of the storm. The Company was able

to restore power to all customers who could receive power six days after it commenced storm restoration work. Eight days later, on September 20, 2004, PEF outage levels returned to historical average outage levels.

20. The total cost of the damages to PEF's system caused by Hurricane Frances is approximately $128.6 million. Of this amount, approximately $9.9 million, will be capitalized. The remaining $118.7 million consists of O&M costs that are properly chargeable against the Company's self-insured Storm and Insurance Property Reserve and qualify for payment from the Reserve.

HURRICANE IVAN

21. On September 16, 2004, the eye of Hurricane Ivan made landfall near Gulf Shores, Alabama as a category 4 hurricane with maximum sustained winds of 130 miles per hour. It continued northward through Alabama, Tennessee, and Virginia, entering the Atlantic Ocean and then traveled South to re-enter Florida on September 20 as a tropical storm. PEF customers in Bay, Franklin, Gulf, Jefferson, and Wakulla counties in PEF's service territory lost power from Hurricane Ivan. At its peak, 8,891 PEF customers were without power as a result of Hurricane Ivan. This represents .6% of PEF's total customers.

22. As a result of Hurricane Ivan, PEF experienced further damage to its transmission and distribution system. During Hurricane Ivan, in addition to PEF's own personnel, PEF mobilized 300 line and service personnel and 100 tree personnel to ensure repairs were completed as efficiently as possible. PEF also handled 55,700 customer outage calls. All customers who were able to receive power had their power restored in two days. One day later, PEF outage levels returned to historical average outage levels.

23. The total cost of damages caused by Hurricane Ivan is approximately $5.7 million. Of this amount, approximately $145,000 will be capitalized. The remaining $5.6 million consists of O&M costs that are properly chargeable against the Company's self-insured Storm and Insurance Property Reserve and qualify for payment from the Reserve.

HURRICANE JEANNE

24. On September 25, 2004, Hurricane Jeanne, the record fourth hurricane to hit Florida in one hurricane season, made landfall near Stuart, Florida. Hurricane Jeanne was a category 3 hurricane with 120 miles per hour winds. Hurricane force winds were also recorded up to 70 miles from the center of Jeanne. It moved northwest across Florida and through PEF's service territory and then proceeded north out of Florida. Again, the impact on PEF's service territory was widespread as 722,012 customers in 33 out of the 35 counties that PEF serves lost power due to Hurricane Jeanne. This represents 47% of PEF's total number of customers.

25. As a result of Hurricane Jeanne, PEF again experienced significant damage to its transmission and distribution system. The storm damaged 853 miles of PEF's transmission lines and 86 substations. During the course of its storm restoration work, PEF installed 222 miles of primary and secondary wire, replaced 100 poles, and installed 570 transformers, 7,860 insulators, and 19,970 splices. The total transmission and distribution storm-related costs are approximately $85.6 million. Of that amount, capital expenses are $7.4 million, and the storm-related O&M costs are $78.2 million.

26. In addition, PEF suffered damage at its generation facilities as a result of Hurricane Jeanne. This included excessive flooding at Debary and the Hines Energy Complex requiring the use of rental pumps. Also at Debary, the Company experienced damage to the P7 breaker cooling fan and tree removal and fence repairs. At the Hines Energy Complex, there was more

erosion to the cooling pond divider dam. There was further damage to the Generator Step Up Transformer (GSU) and bus work at the Bartow combustion turbines, and the umbilical (stack tubing) was destroyed at Tiger Bay. The Company's total storm-related generation costs are $612,000, which are all storm-related O&M costs.

27. PEF mobilized 2,622 system line and service personnel and 1,065 tree personnel in addition to its own personnel for Hurricane Jeanne. The Company handled 741,920 customer outage calls. Power was restored for all customers who could receive power five days after PEF commenced storm restoration work. Eleven days later, on October 12, 2004, system outage levels returned to their historical average.

28. The total cost of the damages to PEF's system caused by Hurricane Jeanne is approximately $86.2 million. Of this amount, approximately $7.4 million will be capitalized. The remaining $78.9 million consists of O&M costs that are properly chargeable against the Company's self-insured Storm and Insurance Property Reserve and qualify for payment from the Reserve.

THE CUMULATIVE EFFECT OF FOUR HURRICANES

29. As noted above, with prior Commission authority, PEF established an unfunded Storm and Insurance Property Reserve as a self-insurance mechanism designed in part to protect against the costs of hurricane and other storm related damage to the Company's transmission and distribution systems from category 3 or less storms. The self-insured Storm Reserve currently accrues $6 million annually and will have a balance of $46.9 million as of December 31, 2004 before any reserve funds are set-off against storm-related costs.

30. The effects of four back-to-back hurricanes hitting PEF's service territory were devastating. In total, the cost to restore PEF's system caused by Hurricanes Charley, Frances,

Jeanne, and Ivan is approximately $366.3 million (system). Of this total amount, capital expenditures are $54.9 million (system) and storm-related O&M costs are $311.4 million (system). These amounts are subject to further revision as the Company continues to receive and process its storm-related costs and invoices. Approximately 48% of the total costs are charges incurred to date, 49% of the total charges are outstanding, and 3% are estimates of work remaining to be done. The overwhelming priority following such severe storms is to address the health, safety, and welfare of customers and Florida residents by expeditiously repairing downed lines and restoring electric service. Following restoration, the Company must conduct sweeps of its transmission and distribution systems to identify and correct any further damage from the storms to ensure that its transmission and distribution systems are able to provide adequate and reliable service on an ongoing basis. To date, the Company's sweeps of its transmission and distribution systems have identified an additional $11 million in needed storm-related work. These sweeps are still being conducted by the Company today and may yield further storm costs.

31. Pursuant to Rule 25-6.0143, F.A.C., storm costs may be charged to the reserve account regardless of the balance in the Reserve. As a result, under the Rule the Commission contemplated potential negative reserves that necessarily, following a prudence determination, are recovered by the Company over a period that may be longer than one year. What the Commission does not provide under the Rule or otherwise is how the negative storm reserve balance will be recovered by the Company and over what period of time that recovery will occur. The Commission, in fact, earlier declined to authorize PEF's request to establish a regulatory asset for the expected excess storm costs above the storm reserve for Hurricanes Charley and Frances because the deferral of the negative balances from the costs of these storms in the storm reserve yields the same result. Rather, the Commission deferred any determination of how and

how long the recovery should occur, directing PEF to charge storm costs to the storm reserve pursuant to the rule, pending "a subsequent petition for recovery of storm-related damages." In re: Petition for approval to establish regulatory asset for costs in excess of Storm Damage Reserve Fund, by Progress Energy Florida, Inc., Order No. PSC-04-0977-PAA-EI, Docket No. 041085-EI, (October 8, 2004). PEF has complied with the Rule, resulting in a negative balance in the Storm Reserve of $311.4 million (system) so far from the hurricanes, or $264.5 million (system) once reserves are applied, with $251.9 million allocated to the Company's retail jurisdiction. PEF now complies with the Commission's additional direction by filing this subsequent petition for recovery of storm-related damages.

III. Relief Requested: A Storm Cost Recovery Clause

32. PEF requests Commission approval of a Storm Cost Recovery Clause that allows PEF to recover its reasonable storm costs in excess of the balance in its Storm Reserve. PEF proposes to commence the Storm Cost Recovery Clause for the excess storm costs above its storm reserves from hurricanes Charley, Frances, Ivan, and Jeanne upon issuance of the Commission's order on this Petition.

33. The storm costs to be covered by the clause include the Company's storm-related O&M costs and its incremental cost above those typically incurred under normal operating conditions for capital expenditures. The total PEF has incurred so far as a result of the four hurricanes is $311.4 million (system).

34. Storm-related capital expenditures will be reflected on the Company's books and records in the following manner. The book value of capital investments that have been retired due to storm damage will be charged against the accumulated reserve. New storm-related capital expenditures will be added to plant in service in an amount equal to the capital expenditure that

would have been incurred under normal operating conditions. The Company uses a standard cost approach to determine this amount. Any capital expenditure above the level of what would have been incurred under normal operating conditions, whether related to labor or materials, will be classified as O&M and charged to the Storm Damage Reserve. The net effect of this accounting treatment is that capital expenditures will reflect that level of investment necessary to provide adequate and reliable service under normal operating conditions. As noted previously, these storm-related capital expenditures will be included in on-going surveillance reports to the Commission and will be absorbed by the Company in current base rates until the next base rate adjustment. The capital expenditures incurred to date as a result of four hurricanes is $54.9 million (system).

35. PEF further proposes to recover its storm costs over two years. Recovery of the storm damage costs over two years will likely avoid the need to issue long-term debt.

36. The excess storm costs above the Storm Reserve determined to be reasonable and prudently incurred will be included as a component of the non-fuel energy charge on the customers' bills. For 2005, including interest, on a retail jurisdictional basis this cost is $132.2 million, and for 2006 this cost is $128 million, based on a start date of January 1, 2005. The Company suggests that these costs be allocated among customers in the various rate classes in the same manner that costs were allocated in the Company's last approved cost of service study. Production demand costs will be allocated using the 12 Coincident Peak ("CP") and 1/13th Average Demand ("AD") method. Production Energy costs will be allocated using Energy. Transmission costs will be allocated using 12 CP, and Distribution costs will be allocated using a Non-Coincident Peak basis. In this manner, the allocation and calculation of the charges to customers for the excess storm costs above the Storm Reserve mirror the allocation and

calculation of costs under the Commission-approved cost of service study and other Commission-implemented cost recovery clauses.

37. The clause should further operate in the same manner as other cost recovery clauses, such as the fuel cost recovery clause, established by the Commission. PEF's projected storm costs and megawatt-hour sales will be submitted for review and then subject to true-up of the projections to actual costs and sales. Just as in other cost recovery clauses, PEF's costs will be subject to a determination of reasonableness and prudence, which PEF will have the burden to demonstrate. Further, the recovery of storm costs will be made subject to audit and a true-up mechanism. Interest will be applied to any amounts carried forward that are ultimately determined to be under or over actual storm costs. These steps will ensure that the Company obtains a dollar-for-dollar recovery of its actual storm-related costs and that customers pay no more than reasonable and prudently incurred storm-related costs. As a result, PEF's customers will be afforded the same review and protections under the Storm Cost Recovery Clause that they have under the other cost recovery clauses implemented by the Commission.

38. A Storm Cost Recovery Clause effectively balances the equities between the Company and its ratepayers. Implementation of the Storm Cost Recovery Clause will allow the Company's extraordinary storm costs after the hurricanes to be allocated directly and proportionately to the Company's customers who benefited from the Company's efforts to restore and otherwise maintain electric service during and immediately after the storms. Further, by providing certainty of recovery of the reasonable and prudent storm costs in an expeditious manner, PEF's customers will benefit from preservation of the Company's financial position.

IV. A Storm Cost Recovery Clause is Necessary, within the Commission's Authority, and Supported by Commission Precedent.

39. Prior to Hurricane Andrew in 1992, PEF, like the other investor owned utilities in Florida, maintained insurance that provided adequate coverage at reasonable rates for storm damage to the Company's transmission and distribution systems. At that time, the risk of loss from severe storms was borne by the insurance carriers, while the utilities and its ratepayers shouldered only the cost of the insurance premiums and the risk of paying the deductibles in the event of a covered storm. Following Hurricane Andrew, however, commercial insurance carriers withdrew property damage coverage for electric transmission and distribution systems at reasonable rates and adequate coverage limits. Thus, the risk of severe storm losses is a risk that the insurance industry evidently is no longer willing to assume.

40. At the current time, the investor owned utilities, including PEF, are required to resort to self-insurance for storm damage losses to their transmission and distribution facilities. In approving these self-insurance programs, the Commission required utilities to accrue storm damage expenses as part of rates for a reserve fund to offset future storm damage costs. See In re: Petition of Florida Power Corporation for authorization to implement a self-insurance program for storm damage to its T&D lines and to increase annual storm damage expenses, Order No. PSC-93-1522-FOF-EI, Docket No. 930867-EI, 1993 Fla. PUC Lexis 1339 (October 15, 1993); In re: Petition to implement a self-insurance mechanism for storm damage to transmission and distribution system and to resume and increase annual contribution to storm and property insurance reserve fund by Florida Power and Light Company, Order No. PSC-93-0918-FOF-EI, Docket No. 930405-EI, 1993 Fla. PUC Lexis 761 (June 17, 1993). The accrual of storm damage expense, however, was set at an amount that the utilities and Commission knew might not be adequate to cover the storm costs of extraordinarily severe storms like Hurricane

Andrew. The Commission reasonably sought to avoid a costly build up of significant reserves for storm damage that might not occur.

41. At the same time, however, the Commission recognized that it would be called upon to provide utilities with relief in the event that storm damage was so severe that the storm costs exceeded the accrued reserves. In the proceeding involving Florida Power & Light (FP&L), for example, the Commission ruled that "[o]ur vote today does not foreclose or prevent further consideration at a future date of some type of cost recovery mechanism, either identical or similar to what has been proposed in this petition." Order No. PSC-93-0918-FOF-EI, *11. Indeed, the Commission contemplated "special assessments" for customers to completely replenish the utility's storm reserve "in the case of a major storm." In re: Petition to implement self-insurance mechanism for storm damage to transmission and distribution system and to resume and increase annual contribution to storm and property insurance reserve fund by Florida Power & Light Company, Order No. PSC-95-0264-FOF-EI, Docket No. 930405-EI, page 6 (February 27, 1995) (recognizing that special assessments to customers in the case of a major storm may be required in ruling that FP&L should expense the costs of Tropical Storm Gordon to preserve its Reserve). In this regard, the Commission elected to keep its options open, providing in the PEF proceeding, that "[i]f [PEF] experiences significant storm related damage, it can petition for appropriate regulatory action," and the Commission "will expeditiously review any petition for deferral, amortization, or recovery of prudently incurred costs in excess of the reserve." Order No. PSC-93-1522-FOF-EI, *7, *8. See also Order No. PSC-93-0918-FOF-EI, *11 ("The Commission could implement a cost recovery mechanism, or defer the costs, or begin amortization, or such other treatment as is appropriate, depending on what the circumstances are at that time.").

42. The Commission's decision to retain flexibility when faced with storm damage above the utilities' reserves necessarily creates uncertainty surrounding the recovery mechanism. That uncertainty has been reflected in recent actions of the financial community. The two major rating agencies, Moody's and Standard & Poor's, have both taken action on the Company's rating due in part to the negative impact of storm related costs. Moody's put PEF's rating under review for possible downgrade and has cited the timing of the recovery of storm costs as one of their concerns. Standard & Poor's changed the rating outlook for PEF from stable to negative again citing "uncertainties regarding the timing of the recovery of hurricane costs ..." as one of the triggering events for the outlook revision. Implementation of a Storm Cost Recovery Clause would bring greater certainty to the financial markets and protect PEF's financial position for the benefit of PEF and its customers.

43. The Commission should bear in mind that PEF is not passing the full brunt of its storm costs above its storm reserves on to its customers even under the Storm Cost Recovery Clause it proposes. Only the reasonable and prudent storm-related O&M costs and the costs in excess of typical charges under normal operating conditions for capital expenditures necessitated by the storms are included in the Storm Cost Recovery Clause. PEF's storm-related capital expenditures will <u>not</u> be included under the Storm Cost Recovery Clause but instead will be reported in surveillance reports and absorbed in current rates until the Company's next base rate adjustment.

44. As the Commission acknowledged in its prior orders dealing with PEF's and FP&L's self-insurance plans for storm damage, the Commission has broad authority with respect to rates and service to implement mechanisms that fairly provide for recovery of the utilities' costs of service. Sections 366.04, .05, <u>Fla</u>. <u>Stats</u>.; <u>Storey v. Mayo</u>, 217 So. 2d 304, 307 (ruling

that "[t]he regulatory powers of the Commission, ... are exclusive and, therefore, necessarily broad and comprehensive."). Likewise, the Commission has broad authority to ensure reliability of the power grid in Florida for operational and emergency purposes, Section 366.04(2)(c), Fla. Stats., including the power to rectify inadequacies in the grid by requiring the installation or repair of necessary facilities "with the costs to be distributed in proportion to the benefits received." Section 366.05(8), Fla. Stats. Under such authority, the Commission may implement a Storm Cost Recovery Clause that allows PEF to "distribute" to customers costs of installing and repairing necessary facilities in an emergency response to restore and maintain reliability of the power grid during and following the devastating onslaught of Hurricanes Charley, Frances, Ivan, and Jeanne.

45. Implementation of a cost recovery clause is neither new nor unique. For example, the Commission has long recognized a fuel cost recovery clause that allows for the recovery of unpredictable variations in the cost of fuel with appropriate true-ups, interest, and cost review to protect the ratepayers' interests. See Citizens of the State of Florida v. Florida Public Service Commission, 403 So. 2d 1332, 1333 (Fla. 1981) (Overton, J., dissenting) (noting that the "fuel adjustment clause is not new and has been used by Florida utilities since at least 1925, ... and it is clear that the commission has authorized over the years fuel adjustments based upon average cost test periods of six months, ...).

46. Indeed, the Commission has extended the fuel cost recovery clause to cover other non-fuel costs under extraordinary circumstances when a utility could not have reasonably anticipated the costs. In re: Fuel and purchased power cost recovery clause and generating performance incentive factor, Order No. PSC-01-2516-FOF-EI, Docket No. 010001-EI, (Dec. 26, 2001) (approving FP&L's request to recapture security expenditures made in response to the

terrorist attacks of September 11, 2001 through the Fuel and Purchased Power Cost Recovery Clause on the grounds of extraordinary circumstances). See also In re: Fuel and purchased power cost recovery clause with generating performance incentive factor, Order No. PSC-04-0411, Docket No. 040001-EI, at 11-12 (April 21, 2004) (noting the "long history in which [the] Commission allowed recovery of certain expenses through the fuel clause that would traditionally be recovered through base rates."). The Commission allowed all the investor owned utilities to recover their security costs after September 11, 2001 under the cost recovery clause even though the Commission acknowledged that prior to September 11 "security costs were traditionally and historically recoverable through base rates." In re: Fuel and purchased power cost recovery clause and generating performance incentive factor, Order No. PSC-02-1761-FOF-EI, Docket No. 020001-EI, at *9, *16, *24, (December 13, 2002). The Commission permitted the recovery of these security costs under the cost recovery clause precisely because they were the "type of cost [that] was a potentially volatile cost, making it appropriate for recovery through a cost recovery clause[]," and because "of the extraordinary nature of the costs in question and the unique circumstances under which they arose." Id. at *9.

47. The Commission and affected utilities justifiably concluded that the cost of third-party insurance was prohibitive, and the extent of third-party coverage was inadequate for transmission and distribution facilities. At the same time, the Commission has understandably declined to incorporate into base rates charges for exceptional expenditures that may never occur. Yet, when such calamities do arise, regulated utilities must be permitted to allocate the expenses among the customers on whose behalf they are incurred in a timely manner. Thus, the storm-related costs are appropriate for recovery through a cost recovery clause because they are volatile, non-recurring extraordinary costs that are beyond the control of the Company.

48. By this Petition, PEF does not propose to discontinue the Storm Reserve. PEF is examining whether the current Storm Reserve accrual continues to be adequate and whether replenishment of the storm reserve fund should be accelerated. When PEF's efforts are complete, PEF proposes to report back to the Commission for further action, if necessary.

IV. Conclusion

49. Accordingly, PEF respectfully requests that the Commission grant its Petition and establish a Storm Cost Recovery Clause for the recovery of the prudent storm-related costs that PEF has incurred as a result of Hurricanes Charley, Frances, Ivan, and Jeanne. PEF requests that this Petition be scheduled for decision as soon as possible and is ready to work with the Commission and other interested parties to promptly respond to information requests.

50. PEF proposes to recover prudently incurred storm costs in excess of storm reserves over two years as a component of the non-fuel energy charge under the Storm Cost Recovery Clause. The clause should provide for the recovery of the Company's storm-related O&M costs and its costs in excess of typical charges under normal operating conditions for capital expenditures necessitated by the storms. The Storm Cost Recovery Clause should further incorporate the same procedural and substantive mechanisms as other cost recovery clauses implemented by the Commission, including, for example, the true-up of estimates of costs and sales to actual costs and sales, with interest provided for any amounts carried forward that are under or over the actual costs, and the determination that the costs were reasonable and prudently incurred. Storm costs recovered under the clause will be allocated among customers in the various rate classes in the same manner that costs were allocated among the rate classes in the Company's last base rate proceeding.

WHEREFORE, PEF respectfully requests that the Commission authorize and approve a Storm Cost Recovery Clause as set forth above to allow PEF to recover extraordinary expenditures related to Hurricanes Charley, Frances, Jeanne, and Ivan.

Respectfully submitted this 2nd day of November 2004.

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