ORIGINAL

BEFORE THE FLORIDA
PUBLIC SERVICE COMMISSION

DOCKET NO. 041291-EI
FLORIDA POWER & LIGHT COMPANY

IN RE: FLORIDA POWER & LIGHT COMPANY'S PETITION FOR AUTHORITY TO RECOVER PRUDENTLY INCURRED STORM RESTORATION COSTS RELATED TO THE 2004 STORM SEASON THAT EXCEED THE STORM RESERVE BALANCE

March 8, 2005

REBUTTAL TESTIMONY & EXHIBITS OF:

K. MICHAEL DAVIS

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REBUTTAL TESTIMONY OF K. MICHAEL DAVIS

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I. INTRODUCTION AND SUMMARY

Q. Please state your name and business address.

A. My name is K. Michael Davis, my business address is 9250 West Flagler Street, Miami, Florida 33174.

Q. Did you previously submit direct and supplemental direct testimony in this proceeding?

A. Yes.

Q. What is the purpose of your rebuttal testimony?

A. I will respond to portions of the testimony submitted on behalf of the Florida Office of Public Counsel (OPC) by Michael J. Majoros, Jr., which address the proper treatment and accounting for costs charged to the Storm Damage Reserve.

Q. Are you sponsoring any exhibits?

A. Yes. I am sponsoring Exhibit KMD-3, the study filed on October 1, 1993 in Docket No. 930405-EI (the 93 Study), which included accounting standards for storm restoration costs that FPL was required to file pursuant to Commission Order No. PSC-93-0918-FOF-EI, issued June 17, 1993 in Docket No. 930405-EI (the 93 Order). The Commission approved the 93 Study in 1995 in Commission Order No. PSC-95-

0264-FOF-EI, issued February 27, 1995 (the 95 Order), attached to my rebuttal testimony as Exhibit KMD-4. I am also sponsoring Exhibit KMD-5 which describes the Company's computation of lost revenues.

Q. Please briefly describe the purpose of your rebuttal testimony.

A. As described in my direct and supplemental direct testimony, the Company has incurred estimated total storm restoration costs of $999 million. Storm restoration costs have been accounted for in compliance with the 93 Study approved in the 95 Order. Estimated insurance reimbursements cover $109 million of those damages, leaving an amount charged to the reserve of $890 million (system). The $890 million (system) storm restoration cost, net of the Storm Damage Reserve positive balance of $354 million at December 31, 2004, results in a deficiency of $536 million on a total system basis. Using the factor proposed by FPL in this proceeding, the jurisdictional portion of the deficiency of $533 million would be collected over approximately three years.

Mr. Majoros has proposed that the Company not recover $309 million. This disallowance is based on the Company's initial estimated storm restoration costs of $818 million. As I indicated in my supplemental direct testimony, the estimated restoration costs charged to the Storm Damage Reserve increased by approximately $180 million (original estimate $710 million, current estimate $890 million), although no new categories of costs have been identified.

The Commission should not adopt Mr. Majoros' recommended disallowance or the reasons for his proposed disallowance. Mr. Majoros either ignores or does not accurately characterize relevant Commission Orders. Ten years after the Commission approved the 93 Study in a docket in which OPC participated, Mr. Majoros would change the standards after the fact and impose a staggering financial burden on the Company. In addition, Mr. Majoros' implication that FPL may be "double billing" or making money on storm events is simply not true. He is in error regarding the characterization of removal costs and certain storm restoration activities. Aside from proposing that the Commission ignore practices it previously approved, Mr. Majoros has provided no reason to deny the Company recovery of storm restoration costs.

II. COMMISSION STANDARDS FOR THE STORM DAMAGE RESERVE

Q. Do standards exist for determining what costs are chargeable to the Storm Damage Reserve?

A. As I stated in my direct testimony, the Commission authorized the creation of the Storm Damage Reserve and, in 1995, approved standards for charging costs to the Storm Damage Reserve. The Company has accounted for storm restoration costs in compliance with these standards since they were approved in 1995.

Q. On Page 15 of his direct testimony, Mr. Majoros asserts that the Commission never adopted accounting standards for the Storm Damage Reserve and, therefore, OPC is free to propose new standards that would be applied retroactively to determine the accounting for storm restoration costs. Do you agree?

A. No. The Commission did approve standards for the Storm Damage Reserve in Docket No. 930405-EI. Mr. Majoros has omitted mention of the 93 Order, which is important in understanding the purpose and context of the study submitted by the Company. That Order stated (page 4):

> "From the record in this docket it is unclear what storm related expenses FPL intends [to] draw from the reserve fund. For example it is unclear whether normal salaries would be charged to the fund if employees worked on storm related tasks. In addition, employees repairing storm damage would be required to spend time away from their everyday work tasks which would result in "catch up" expense. It is unclear from the record whether FPL intends to draw "catch up" expense from the reserve fund. The record reflects that such "catch up" expense is not recoverable under FPL's current insurance policy. In addition it is unclear whether the cost of damaged assets would be accounted for at replacement cost or net book value. For example, if there were $100 million of net book value of assets that were destroyed and it took $200 million to replace those, what accounting entries would be made?
>
> FPL shall address these questions in the company study discussed above."

In compliance with the 93 Order, the Company submitted the required study on October 1, 1993. The 93 Study is attached as Exhibit KMD-3.

The Commission addressed the accounting standards of the 93 Study in the 95 Order at pages 4-5 as follows:

> "...the study addressed the issues raised in the [June 17, 1993] order concerning the types of expenses that would be charged to the reserve. However, we have the authority to review any expenses charged to the reserve for reasonableness and prudence. FPL stated that it would use the actual restoration cost approach for determining the appropriate amounts to be charged to the reserve. This methodology is consistent with the manner in which replacement cost insurance works.
>
> In accounting for the restoration and replacement costs to plant, the gross original cost of the replaced plant should be retired by a credit to the plant accounts and a debit to the depreciation reserve. Then, a credit would be made to the plant accounts so that the replacement gross plant would be reduced by the available balance of the storm reserve until it is equal to the value of the plant it replaced. In addition, the depreciation reserve would be credited with an amount equal to the gross cost of the replaced plant. This would restore the plant accounts and depreciation reserve to their original values prior to the damage caused by the storm."

In the ordering paragraphs at the conclusion of the 95 Order (page 6), the Commission expressly stated: "ORDERED that the storm damage study submitted by Florida Power & Light Company is hereby found to be adequate." The 95 Order is attached as Exhibit KMD-4.

Understanding the purpose and context of the 93 Study and recognizing the Commission's substantive review of the study, it is clear that the 95 Order reflected the Commission's approval of the study and the standards that the Company has been using over the last decade. Putting aside OPC's participation in Docket No. 930405-EI, its position in this proceeding ignores the fact that these issues were fully aired and considered by the Commission Staff in making their recommendation to the Commission and ultimately, by the Commission in issuing the 95 Order.

Q. Did other parties participate in Docket No. 930405-EI?

A. Yes. In the approximate two years between the time the Docket was opened and issuance of the 95 Order, all parties had an opportunity to be heard. In addition to FPL, Florida Industrial Power Users Group (FIPUG), OPC, and four other intervenors, participated in the proceeding. OPC now seeks to suggest that these issues somehow are new. Yet, clearly the Commission was provided with the diverse opinions of not only its own staff but also of FPL and two of the major parties to the current proceeding. After a thorough review, the Commission issued the 95 Order approving the standards and methodology in the 93 Study. FPL has relied upon this decision since that date.

Q. Is the 95 Order unclear to you in its approval of the study?

A. No. Mr. Majoros' claim that the Commission did not "bless" the study (page 15) cannot be squared with the portions of the orders quoted above, or with the title of the 95 Order which is (emphasis added):

NOTICE OF PROPOSED AGENCY ACTION
***ORDER APPROVING STORM DAMAGE STUDY* AND**
ADJUSTMENTS TO SELF INSURANCE MECHANISM

The title of the order removes any doubt that the order approved the study. For FPL to have concluded otherwise, and to have used an accounting approach other than as described in the 93 Study without further Commission action would have been completely untenable. The discussion in the 95 Order clearly demonstrates that the Commission understood that FPL would apply the standards recommended in the 93 Study in its accounting for storm costs and that it found FPL's recommended

accounting appropriate for regulatory purposes. Certainly I, as Chief Accounting Officer of the Company, would have no reason to conclude anything to the contrary.

Q. What is the significance of the 95 Order's mention of a possible future rulemaking on uniform guidelines?

None. It appears the Commission may have been considering whether to open a rulemaking to establish uniform guidelines for all Florida utilities. But, in the ten years since the 95 Order was issued the Commission has not initiated such a rulemaking, a clear indication that the Commission found no reason to do so. Therefore, the standards set forth in the 93 Study, as approved by the Commission in 1995, have remained applicable to FPL. As a result, FPL has no alternative but to follow the accounting standards set forth in the 93 Study.

Q. Has the Commission issued any orders since the 95 Order that changed the standards approved for FPL in that Order?

A. No. There have been several orders dealing with the Storm Damage Reserve; however, none of them changed the standards approved in the 95 Order. In fact, Order No. PSC-95-1588-FOF-EI, issued December 27, 1995 in Docket No. 951167-EI and Order No. PSC-98-0953-FOF-EI, issued July 14, 1998, in Docket No. 971237-EI, both referenced the 95 Order.

More recently, in Order No. PSC-04-1150-PCO-EI, Docket No. 041291-EI, issued November 18, 2004, in Docket No. 041291-EI the Commission stated:

> "On September 9, 2004, Florida Power & Light Company (FPL) filed a petition for approval to establish as a regulatory asset for storm damage costs that exceed the $345 million balance of the Storm Reserve. FPL also sought authorization for the future recovery of

reasonable and prudently incurred storm damage costs in excess of its Storm Reserve fund. By Order No. PSC-04-0976-PAA-EI, issued October 8, 2004, in Docket No. 041057-EI (and consummated by Order No. PSC-04-1114-CO-EI, issued November 9, 2004), this Commission found it was unnecessary to create a separate regulatory asset to do this because allowing a negative balance to be recorded in the Storm Reserve served the same purpose and was contemplated by Rule *25-6.0143, Florida Administrative Code.* This Commission made its decision with the understanding that FPL will continue booking amounts consistent with its current accounting practice. The amounts are subject to our review and approval, in the event that a subsequent petition for recovery of storm-related damages is filed." [emphasis added]

Q. Has FPL adhered to the approved standards?

A. Yes. As I stated earlier, after the approval of the 93 Study, the Company has consistently followed the methodology recommended in that Study. Between 1993 and 2003 the Company has experienced 8 storms totaling $152.0 million in aggregate restoration costs, all of which have been charged against the Storm Damage Reserve. The Company has followed the standards set forth in the 93 Study in its accounting for storm restoration costs for all these storms. In that timeframe, I am not aware of any audit by the FPSC Staff that has disclosed any errors on the part of the Company or any inconsistency with the 93 Study approved by the Commission in the 95 Order. It does not appear that Mr. Majoros is making any allegation to the contrary, except perhaps with regard to the costs of a salt spray and a vegetation study. I address these two items later in my rebuttal testimony.

Q. Has the Commission conducted audits of storm damage costs using these standards?

A. Yes. On February 7, 2005 the Audit Staff of the Florida Public Service Commission issued a report on the costs that the Company charged to the storm reserve (the

Audit). Ileana Piedra, the Audit Manager, attached the Audit to her direct testimony as Exhibit IHP-1. At page 4 of 12, Exhibit IHP-1 notes that the Audit Staff read the "approved study...and [the 95 Order]" in connection with the Audit. The Audit had no findings that FPL improperly charged any costs to the storm reserve or that the Company did not follow the standards of the 93 Study approved by the Commission.

In fact, in her direct testimony at page 7, Ms. Piedra states: "FPL has recorded the above costs as proposed in its 1993 study and discussed in the 1995 order, using the actual costs." It is apparent that the PSC Staff after conducting its own independent review concluded that FPL has charged costs to the Storm Damage Reserve consistent with the methodology set forth in the 93 Study. Commission orders and the Staff's Audit all point to a consistent application of the approach that the Company recommended and the Commission approved.

Q. Do you agree with Mr. Majoros' statement that "...FPL wants the customers to bear 100% of the risk of storm damage..." (Page 12, Line 17)?

A. No. Mr. Majoros inappropriately equates recovery of the deficit in the Storm Damage Reserve with the risk of storm damage. In doing so, he ignores the fact that as a result of the hurricanes the Company lost revenues due to customer outages and incurred other costs that were not charged to the Storm Damage Reserve. Further, he ignores the fact that none of the increases in the annual accruals for storm damages during the 1990s were accompanied by an increase in the rates charged to customers, and instances where the Company made voluntary contributions to the Storm Damage Reserve. Finally, he fails to recognize that restoration costs are, as discussed by FPL

witness Moray P. Dewhurst in his rebuttal testimony, a foreseeable cost that for good reasons has not been fully provided for in the normal cost of service used in setting base rates. Consequently, it is entirely appropriate under cost-based rate regulation for the Company to seek recovery of the resulting deficit.

Q. Has the Commission previously recognized that restoration costs may exceed the balance in the Storm Damage Reserve resulting in a need for recovery from customers?

A. Yes. The Commission recognized exactly this type of situation in Order No. PSC-98-0953-FOF-EI, issued July 14, 1998, stating:

> "FPL's financial resources from the lines of credit and the fund appear to be sufficient to cover most storm emergencies. However, the costs of storm damage incurred over and above the balance in the reserve and the costs of the use of the lines of credit would still have to be recovered from the ratepayers.
>
> In the event FPL experiences catastrophic losses, it is not unreasonable or unanticipated that the reserve could reach a negative balance. Rule 25-6.0143 (4)(b), Florida Administrative Code, recognizes that charges to a reserve may exceed the reserve balance resulting in a negative balance, as was the case of Gulf Power Company in Order No. PSC-96-0023-FOF-EI, issued January 8, 1996, in Docket No. 951533-EI." (emphasis added)

In addition, the Commission ordered FPL to file a study on the reasonableness of the level of the reserve and accrual by no later than December 31, 2002.

Q. Did FPL file the study requested by the Commission?

A. Yes, FPL filed the study on September 28, 2001. That study was the basis for the petition filed by FPL on the same date which requested permission to increase the accrual from $20.3 million to $50.3 million.

Q. What was the outcome of FPL's request?

A. The Company agreed to withdraw its request as part of the negotiated settlement reached with OPC and other parties that produced a $250 million reduction in base rates. But, as discussed by Mr. Dewhurst in his rebuttal testimony, the settlement agreement included a key provision that addressed storm deficits. Paragraph 13 of the 2002 Stipulation and Settlement states:

> "In the event there are insufficient funds in the Storm Damage Reserve and through insurance, FPL may petition the FPSC for recovery of prudently incurred costs not recovered from those sources. The fact that insufficient funds have been accumulated in the Storm Damage Reserve to cover costs associated with a storm event or events shall not be evidence of imprudence or the basis of a disallowance..."

Q. What do you conclude from this?

A. The customers have benefited from the settlement agreement which reduced base rates by $250 million. Also, the Company relied on existing assurances that a deficit would be recoverable. This rate reduction and the settlement agreement are further discussed in the rebuttal testimony of Mr. Dewhurst.

Q. Do you have any comments on the "OPC Storm Damage Guidelines"?

A. Mr. Majoros states that he endorses what he describes as "OPC Storm Damage Guidelines" (pages 5-6). If OPC thought their guidelines were superior to those recommended by FPL and approved by the Commission, they should have raised them in Docket No. 930405-EI or at least well in advance of a major event resulting in a Storm Damage Reserve deficit so that expectations of relevant constituents could have been properly adjusted in the event of any changes. The record in Docket No. 930405-EI indicates that OPC did raise the incremental cost approach which was apparently rejected by the Commission in approving the 95 Order. It is not

appropriate for OPC to ignore the standards approved by the Commission in the 95 Order, to subsequently let 10 years and other storms pass (all accounted for in accordance with the 95 Order) and, only after a storm fund deficit has been created, propose a different set of standards for retroactive application. This is not the appropriate forum to discuss changing those standards.

But OPC's guidelines, in any event, are flawed. For example, OPC's proposal to adjust storm damages for instances where the Company expense is less than the amount planned in a particular category of expense is an inappropriate benchmark. There are innumerable reasons why the Company might spend more or less than the budgeted amount in any given year or business cycle, especially on a category by category basis. The budget is a plan built on management expectations of the business circumstances during the period the expenses will be incurred. As expectations change or actual circumstances become known, management must revise its plan to reflect the changes. Thus, a Company's plan for tree trimming may change by a significant percentage solely due to changing circumstances. Such a change would not ordinarily be reflected in the budget. Likewise, actual expenditures and, therefore, budget variances also will show movement solely due to changes in circumstances whether or not there are hurricanes. OPC's proposed guidelines in this respect are inherently flawed. FPL's methodology is straightforward, follows the 93 Study approved by the Commission and avoids endless debate regarding why a particular budget variance existed.

Q. What observations can you make regarding the effect of OPC's proposed guidelines in this particular instance?

A. Even if OPC's guidelines were accepted, there are several examples of how applying Mr. Majoros' and OPC's inappropriate benchmarking would not result in any change to the amount of the requested recovery. Call Center costs charged to the Storm Damage Reserve consisted of incremental costs of staffing this function and training employees, including a significant number of non-care center employees assigned to the care centers during the storm, on process changes and information relative to responding to customer inquiries in each of the specific restoration situations following the hurricanes. The Company spent nearly all of its tree trimming budget ($47.0 million vs. $46.0 million). Significantly more was spent on storm restoration and was properly charged to the Storm Damage Reserve. The Materials and Supplies budget for Power Systems was almost spent in its entirety ($26.9 million vs. $25.4 million), yet incrementally more was spent on storm restoration.

Q. How would changing the standards retroactively prejudice FPL?

A. FPL has followed the existing standards in accounting for storm damage costs and has relied on these standards in a number of ways. FPL has charged actual storm restoration costs to the Storm Damage Reserve as required by Commission Orders. As a result, a deficit in the reserve was created and left on the balance sheet at December 31, 2004, as required by Commission Orders. Also, FPL has structured its response to storms under the belief that the accounting standards approved in the 95 Order were still applicable. As I discuss below, changing the rules after the Company has restored power and created a Storm Damage Reserve deficit of $536 million is

unfair and would raise serious questions regarding the ability of the Company and of investors to rely on Commission Orders as governing and controlling precedents.

Q. Please explain the importance of maintaining the existing standards as they relate to the way in which FPL has booked the costs and reported them in its balance sheet at December 31, 2004 and how this avoids prejudicing FPL?

A. FPL has relied on the existing standards in reporting its financial condition to the Securities and Exchange Commission and shareholders. Those costs were booked in accordance with those standards and were included in the Storm Damage Reserve deficit that was reported as an asset in the Company's 2004 financial statements. Changing the standards retroactively would undermine the basis for financial reporting with potentially serious consequences for the capital market's perception of regulatory risk. The nature and significance of this risk is discussed by Mr. Dewhurst.

FPL charged its actual restoration costs to the Storm Damage Reserve in 2004, even though a deficit was created. The appropriateness of this action was reaffirmed in Order No. PSC-04-0976-PAA-EI, issued October 8, 2004 in Docket No. 041057-EI. FPL relied on that Order along with the 95 Order and multiple Orders issued between 1995 and 2004 to maintain the storm deficit on its balance sheet as an asset rather than charging the deficit to expense in 2004.

Statement of Financial Accounting Standards No. 71, Accounting For the Effects of Rate Regulation (SFAS No. 71), requires that the effects of rate regulation be

recognized by companies like FPL. Implicit in this requirement is that the ratemaking authority, in the case of a cost deferral like the Storm Damage Reserve deficit, will allow recovery of those costs in the future. Absent that intent by the ratemaking authority, the costs should have been expensed as they would have been for a non-rate regulated entity.

In the 95 Order and other Orders, the Commission authorized defined charges to the Storm Damage Reserve, subject to review for "reasonableness and prudence." The Commission emphasized that in the event of catastrophic loss causing the Storm Damage Reserve to become deficient, the Company could petition for emergency relief. Further, the Commission provided assurance that in such circumstances it would "act quickly to protect the company and its customers" (the 93 Order, page 3).

The Company has relied on the ability to effect timely recovery of reasonable and prudently incurred costs to support creation and maintenance of the deficit in the Storm Damage Reserve as an asset. Any inability to recover reasonable and prudently incurred storm damage costs would impair the ability of FPL to rely on SFAS 71 as a basis for recognizing the effects of rate regulation in its financial statements. This, in turn, could adversely affect the amounts reported on the income statement and balance sheet of the Company, frustrating regulatory objectives and increasing the regulatory risk perceived by those who rely on the Company's financial statements. Such a consequence should not be taken lightly. Losing an ability to rely upon established rules and precedents could have devastating effects on

the Company's ability to attract and retain necessary capital. To put this in context, expensing the storm deficit instead of reporting it as an asset would have reduced FPL's 2004 Net Income by 44%. This reduction is material and would have a significant effect on investors' perception of FPL.

Q. Why would changing the rules after the fact prejudice FPL regarding its response to the storm?

A. In response to significant hurricane damage the Company mobilizes all available employees with one common objective - restore power to customers as safely and as quickly as possible. This effort requires the involvement of linemen and other field personnel to actually restore power and staff personnel to enable and support the restoration effort through damage surveys, organizing and running restoration sites, and other support activities. These support activities run the gamut from distributing food to crews in the field to patrolling feeders and laterals. All of the restoration activities are performed pursuant to detailed restoration plans that are updated at least annually and practiced several times before hurricane season begins. As a result of our planning and practicing, the Company is prepared to begin its restoration activities as soon as it is safe to do so. All of the costs associated with annual planning activities and practicing for storm restoration are charged to normal operating expenses, not the Storm Damage Reserve.

The duties normally performed by staff personnel generally do not go away; they are merely deferred or performed by others during storm restoration. Both the backfill and catch up work necessary to ensure that these duties are caught up generally

involve overtime or the use of contractors or temporary labor that is charged to normal operating expense, not the Storm Damage Reserve. The Company incrementally spent $7.0 million on contractors and outside professional services and $9.0 million of overtime was charged to normal operating expenses during the last two months of 2004. If, for example, the Company were denied recovery of the regular payroll associated with personnel working on storm restoration, it might make financial sense to utilize contractors to perform the restoration work rather than incurring the additional overtime and other costs for backfill and catch up work. Ultimately that decision would depend on an assessment of the effect of using those contractors on the restoration effort versus the avoidance of an additional cost burden on the Company and its shareholders. That is not an acceptable position in which to place the Company and its management. The Company wishes only to have one interest and purpose during the restoration activities – to restore power as quickly and safely as possible. In any case, changing the rules after the fact precludes the Company from making this assessment. Also, the ability to make that specific assessment is further limited because the Company, relying on the approved standards, had no reason to specifically track this overtime or outside services.

III. THE DOUBLE COUNTING AND COST SAVING ALLEGATIONS

Q. Is Mr. Majoros correct that the existing standards result in customers paying twice for the same costs?

A. No. Mr. Majoros claims (pages 11-14 and 17-19) that the existing standards require customers to "pay twice" for base salaries (regular payroll) and FPL vehicle expense – once in base rates and a second time in the Storm Restoration Surcharge. He is not correct.

Before addressing the "pay twice" claim it is important to emphasize that charging these costs to the Storm Damage Reserve was clearly set forth in the 93 Study and approved by the Commission in the 95 Order. Actual restoration costs were defined to include "FPL payroll costs, costs associated with the use of vehicles and equipment..." and again set forth in the more detailed description of actual restoration costs: "FPL employee payroll – regular, overtime, and temporary relieving pay" and "Charges for FPL owned or leased vehicles and equipment which are considered part of the Company's normal operating fleet" (Exhibit KMD-3, page 8 and Attachment 1, page 2). These are specific provisions responsive to the Commission's own questions posed in the 93 Order, such as "...whether normal salaries would be charged to the fund if employees worked on storm related tasks." (Order, page 4).

As stated above, FPL relied on these existing standards. Even if Mr. Majoros were correct in his criticism of this standard, the effect of any change should be prospective

only. But, Mr. Majoros is not correct in his criticism. FPL's base rates are designed under the assumption of normal costs and normal revenues. Normal costs include regular payroll and vehicle charges. The revenue requirement is divided by a normal level of sales to set the base rates. During the hurricanes there were very significant outages during which sales and corresponding revenues were lost. Thus, while hurricanes result in reductions of some base rate costs because those costs are charged to the Storm Damage Reserve, there also are reductions of base rate revenues. Even if there were merit to Mr. Majoros' concern, to determine whether there was any "double dipping" one would have to ask whether total avoided base rate costs are greater than lost base rate revenues. In the case of the 2004 hurricanes, the Company estimates lost base rate revenues of $38.2 million, the calculation of which is attached as Exhibit KMD-5, while only $32.0 million in estimated regular payroll was charged to the Storm Damage Reserve. Even if FPL vehicle expense of $5.3 million were added to regular payroll as proposed by Mr. Majoros, the total would remain less than lost base rate revenues. Moreover, as I described previously there are other incremental, base rate expenses such as for catch up and backfill work that also would have to be taken into account under his approach. In addition, the $32 million of regular payroll cited by Mr. Majoros would not have been charged entirely to the operating expense categories normally associated with base rates. On an annual basis, approximately 6% of regular payroll is charged to cost recovery clauses and other and approximately 22% is charged to capital. If these percentages are applied to the regular payroll amount cited in Mr. Majoros' testimony, they would yield approximately $1.9 million for cost recovery clauses and other and $7 million for

capital. Also, the adjustment proposed by Mr. Majoros to capitalize property additions and cost of removal is estimated to include approximately $22.9 million of payroll. These amounts are not additive, they merely serve to illustrate the fallacy of the simplistic approach taken by Mr. Majoros.

In addition, I would note that there is an inconsistency between Mr. Majoros' proposed adjustment for regular salaries and OPC's guidelines which propose adjusting only bargaining unit payroll. Bargaining unit regular payroll charged to the Storm Damage Reserve aggregated only $9.5 million. As should be obvious from the foregoing discussion, even if it were appropriate to revisit the storm accounting standards in this proceeding, there are numerous issues that would have to be factored into any decision to move to the approach advocated by Mr. Majoros. Of course, these are the same types of issues that were addressed in connection with the 93 Study that was approved in 1995.

Q. Does Mr. Majoros ignore other incremental costs not charged to the Storm Damage Reserve?

A. Yes. This is an important element in the overall impact of the hurricanes that is ignored by Mr. Majoros in his allegations of "double dipping" and cost savings by FPL.

As I indicated above FPL suffered lost base rate revenues of $38.2 million. I also described earlier the backfill and catch up overtime costs that are not charged to the Storm Damage Reserve even though directly caused by the hurricanes. Further, the

Company estimates that uncollectible accounts receivable increased nearly $6 million as collection efforts were suspended because field collectors were mobilized for storm duty.

Mr. Majoros has not taken the lost revenues or the incremental costs into account. His implication that FPL may be making money from the storm events (Majoros Testimony, page 6) is simply not true.

IV. SPECIFIC CRITICISMS OF STORM COST ACCOUNTING

Q. Mr. Majoros testifies on Pages 16-17 of his direct testimony that the cost of two studies should not be charged to the Storm Damage Reserve. Please comment.

A. The Company has contracted for two studies, one involving an evaluation of salt spray, sand and salt water intrusion problems in coastal communities, and the other involving post-storm vegetative conditions. The nature of and necessity for these studies are discussed in the testimony of FPL witness Geisha Williams.

Q. Mr. Majoros also claims on Page 17 that projects incomplete as of December 31, 2004 are not necessarily related to storm damage. Please comment.

A. The Storm Damage Reserve includes incomplete projects totaling $43.4 million as of December 31, 2004. The need for these projects is discussed in Geisha Williams' testimony. The necessity for performing follow up work directly related to storm damage is not unique to Hurricanes Charley, Francis and Jeanne. For example, one

type of follow up work was described in detail in a Commission Order issued December 27, 1995, in Docket No. 951167-EI (page 4):

> "FPL suffered extensive salt water damage to underground facilities as a result of Hurricane Andrew and the March 1993 Storm. It is the Company's intent to repair these facilities as they fail, or during any normal upgrading of the facilities. Certain of these facilities are expected to fail in the near future. Based on engineering estimates of anticipated future repair costs, an insurance settlement of $6.7 million was reached. This is a final settlement; if the repairs exceed this amount the Company will not be able to file for additional insurance reimbursement.
>
> It appears from FPL's petition that the Company wishes to establish a separate liability for the $6.7 million, rather than placing it in the reserve. The $6.7 million received by the Company represents a settlement of claims for which neither the actual total amount nor the timing of the replacement can be accurately determined. This is exactly the situation a storm reserve is designed to cover. Therefore, we find that this amount shall be added to the reserve and the after tax amount added to the fund. By doing so, the amount can be invested and accrue interest. This will help to mitigate any costs for repairs should they exceed the Company's original estimates. As the repairs are actually completed, the reserve shall be charged for the cost of the repairs." (emphasis added)

The appropriate criteria for determining whether the follow up work should be charged to the Storm Damage Reserve is the root cause of needed repair and restoration of the system to pre-hurricane status, not the timing of the work.

Q. Please address Mr. Majoros' specific criticisms of the Company's accounting for base salaries.

A. As discussed earlier in my testimony, Mr. Majoros has chosen to ignore the existence of incremental costs incurred by the Company in backfill and catch up work. Also, he ignores the fact that not all of the regular salaries charged to the Storm Damage Reserve would have been charged to expense categories normally associated with base rates. Should a decision be made to remove any or all of regular payroll,

provision should be made for all of these items. Also, the adjustment proposed by Mr. Majoros to capitalize a portion of the restoration costs includes approximately $22.9 million of payroll.

Q. Please address Mr. Majoros' testimony regarding FPL vehicle expense.

A. On Page 18 of Mr. Majoros' direct testimony, he proposes to make an adjustment of $5,261,887 as "these vehicles have already been included in the annual budget". The Company did charge its vehicle expenses to the Storm Damage Reserve, just as it had proposed to do so in the 93 Study that was approved in the 95 Order. In proposing this adjustment, Mr. Majoros ignores the fact that some of these vehicle costs would not have been charged to expense categories normally associated with base rates. On an annual basis, approximately 47% of the annual vehicle costs are charged to capital projects. Assuming the same split is applied to the vehicle costs charged to the Storm Damage Reserve, would yield approximately $2.4 million. Also, as discussed above for payroll, the adjustment proposed by Mr. Majoros to capitalize property additions and cost of removal includes approximately $4.3 million of vehicle charges. These amounts are not additive, they merely serve to illustrate the fallacy of the simplistic approach taken by Mr. Majoros.

Q. Please address Mr. Majoros' direct testimony on Page 19 regarding tree trimming expense.

A. FPL's practice with respect to tree trimming during storm restoration is to trim only what is necessary to allow the Company to safely restore service to its customers. Mr. Majoros states "Tree trimming expense should be limited to the amounts which exceed FPL's normal expenses." As discussed earlier in my testimony, the

benchmark analysis proposed by Mr. Majoros is inappropriate. Nevertheless, because FPL spent and charged to normal expenses all but approximately $1 million of the amount it had budgeted for tree trimming in 2004, it would appear that even under Mr. Majoros' logic the $89.4 million incurred and charged to the Storm Damage Reserve for tree trimming should be recoverable.

Q. Please address Mr. Majoros' direct testimony on Page 19 regarding call center expense.

A. I have previously discussed the inappropriateness of this benchmark adjustment. However, even under Mr. Majoros' view, these costs should be recoverable since only incremental costs were charged to the Storm Damage Reserve. The Company did not charge normal costs of operation for the Call Center to the Storm Damage Reserve.

Q. Do you have any comments regarding OPC's guidelines on Materials and Supplies charged to O&M?

A. Yes. Again this is an inappropriate benchmark adjustment as discussed earlier. Nevertheless, even under Mr. Majoros' reasoning any adjustment would be insignificant because virtually the entire 2004 budget was spent without consideration of amounts charged to the Storm Damage Reserve.

Q. Is Mr. Majoros correct that FPL is following an inappropriate accounting methodology for the replacement of plant in service destroyed by the hurricanes?

A. No. In determining the amounts to be charged to the Storm Damage Reserve, FPL is following the accounting standards approved in the 95 Order. As with the various

cost categories already discussed, the time to establish standards is before not after the event occurs.

The existing standards are designed to maintain the plant in service and depreciation accounts at the same levels after the hurricanes as existed before the hurricanes. This recognizes that the reason for replacing the assets was not to improve the system, but to restore it to the condition that existed before the hurricanes.

If the Commission adopts Mr. Majoros' recommendations, plant in service would increase, accumulated depreciation would decrease and annual depreciation expense would immediately increase due solely to the impact of hurricanes. This would place upward pressure for a long-term increase in electric rates because of an increase in return requirements as well as an increase in cost of service.

Q. Why would plant in service increase under the OPC approach endorsed by Mr. Majoros?

A. Plant in service would increase because the poles, wires and other equipment and related installation costs are generally higher even at normal costs than the costs associated with the property destroyed by the hurricanes and retired. This increase is due to inflation and other factors occurring between the time the destroyed assets were installed and when they were replaced.

In addition, as described in the 93 Study, the normal costs of the replacement assets would have to be estimated because the assets are being replaced under extraordinary

conditions. It is impossible to track the normal cost associated with the replacement assets under the conditions that exist when the Company is restoring service after a hurricane.

Q. Why would accumulated depreciation decrease under the OPC approach endorsed by Mr. Majoros?

A. Accumulated depreciation would decrease for the following reasons:

- The assets being replaced have not reached the end of their normal lives; therefore they have not been fully depreciated.
- Likewise, because the cost of removal associated with the destroyed assets is calculated in the same manner as depreciation, the full normal cost of removing the destroyed assets has not been accumulated.

The combined effect of these circumstances is to leave a deficit or shortfall in accumulated depreciation for the destroyed assets. This shortfall increases rate base resulting in an immediate increase in revenue requirements. Also, the shortfall will have to be factored into future depreciation rates resulting in higher costs to customers in the future. This is in addition to the fact that those customers face their own risk of future catastrophic hurricane events.

Q. Why would depreciation expense immediately increase under the OPC approach endorsed by Mr. Majoros?

A. Depreciation expense would immediately increase because of the higher plant in service balances. Annual depreciation expense is determined by applying an approved depreciation rate to plant in service balances. As plant in service increases,

so does depreciation expense, without any change in rates. The change in rates discussed in my previous answer could compound the effects of this increase.

Q. Wouldn't the fact that the equipment is newer offset these increases in depreciation expense?

A. The fact that the equipment is newer would certainly mitigate the effects because of the longer remaining life. Whether it would offset the full effect would depend on the amount of the cost differential for the assets, the remaining lives of those assets, and the extent to which the original cost and removal cost of the destroyed asset had been accumulated.

Q. Does the Company consider the effects of hurricanes in determining depreciation rates?

A. No. Because hurricanes occur at irregular intervals and the physical effects vary from storm to storm, the Company excludes the effects of hurricanes from the depreciation studies used to obtain Commission approval for depreciation rates. Inclusion of the hurricane related effects would potentially understate the life characteristics of plant and overstate the cost of removal, thereby overstating the depreciation expense associated with normal operations.

Q. Is Mr. Majoros correct in his assertion on Page 23 of his direct testimony that the existing standards inappropriately treat the removal reserve?

A. No. As I previously discussed, only a portion of the normal removal cost related to the destroyed assets would have been accrued since those assets generally would have remaining life left. The removal cost component included in the depreciation rate takes into account a future cost to remove an asset assuming normal retirements. This

removal cost component is determined based on the historical relationship of removal cost to the plant investment and excludes extraordinary retirements such as those caused by hurricanes. As such, the removal costs embedded in accumulated depreciation are designed to cover normal end of service life retirements, not catastrophic events like hurricanes.

Q. Is Mr. Majoros correct in his assumptions on removal cost related to the assets retired resulting from the hurricane?

A. No. Mr. Majoros would lead you to believe that the removal cost collected is related solely to the assets that would be retired for extraordinary events. The $1.1 billion that Mr. Majoros referenced relates to the estimated removal cost associated with all of the Transmission and Distribution system assets. In order to identify the removal cost associated with the assets retired due to the hurricanes, the specific assets to be retired must be identified along with the vintage year. Then, the component of removal cost included in depreciation expense would need to be multiplied times the cost of the asset retired to determine the annual amount for each year that the depreciation rate was used and changed to reflect any represcription of depreciation rates. The total of all these annual amounts would be accumulated to determine the amount of removal cost included in the accumulated depreciation reserve related to the retirements associated with the hurricane.

Q. Has FPL estimated the capital additions, removal costs, and retirements that it expects to record as a result of storm restoration under the recommended approach, "Actual Restoration Cost" approved in the 93 Study?

A. Yes. FPL estimates that approximately $58 million of capital additions, $12.2 million in removal costs, $36.4 million in retirements, $21.7 million in Contributions in Aid of Construction, and $48.5 million in other recoveries will be recorded in March 2005. The effect of recording these amounts is to restore the plant and reserve accounts to their pre-storm balance. This approach is consistent with the 93 Study and 95 Order.

These estimates do not include the effects of approximately $18 million of the approximately $43.4 million of incomplete projects identified in Exhibit KMD-2 as "Remaining Work."

V. CONCLUSION

Q. Would you please summarize your testimony?

A. Yes. My rebuttal testimony refutes all the major points in Mr. Majoros' testimony.

He erroneously asserts that the Commission never adopted accounting standards for the Storm Damage Reserve and, therefore, OPC is free to propose new standards that would be applied retroactively to determine the accounting for storm damage costs. I disagree. In the 95 Order the Commission approved standards for charging

restoration costs to the Storm Damage Reserve. In the 10 years since that Order was issued, nothing has occurred that would change the applicability of those standards. The standards accepted by the Commission in that Order were appropriate then, and remain appropriate for purposes of addressing FPL's request in this proceeding. Any changes to the established standards should be done on a prospective basis.

FPL has followed the existing standards in charging storm damage costs, and has maintained its financial books and records and prepared its 2004 financial statements, in accordance with those standards. A decision to deny recovery of reasonable and prudently incurred storm damage costs could impair the ability of FPL to rely on SFAS 71 for creation and maintenance of regulatory assets. This, in turn, could adversely affect the income statement and balance sheet of the Company and negatively affect the Company's ability to attract and retain capital. The Commission's Audit Staff after conducting an independent review agrees that FPL has recorded storm costs as proposed in the 93 Study using actual costs. In stark contrast, Mr. Majoros believes it would be appropriate to change the rules at any point and apply new standards retrospectively. If OPC wishes to change the existing standards for charges to the Storm Damage Reserve it should petition the Commission with that request and provide the level of detail and explanation that was provided in the 93 Study. I would note that OPC participated in the docket in which the 93 Study was reviewed and approved. OPC has had 10 years to raise any concerns or objections regarding the standards set forth in the 93 Study. But the fact remains that the issues raised by OPC in this proceeding were essentially the same

issues fully considered in Docket 930405-EI, culminating in the issuance of the 95 Order.

Mr. Majoros erroneously claims that the existing standards require customers to "pay twice" for base salaries (regular payroll) and FPL vehicle expense – once in base rates and a second time in the Storm Restoration Surcharge. I disagree. FPL's base rates are designed under the assumption of normal costs and normal revenues. During the hurricanes there were very significant outages during which sales and corresponding revenues were lost, and incremental expenses incurred that were not charged to the Storm Damage Reserve. Thus, while hurricanes result in reductions of some base rate costs (through charges to the Storm Damage Reserve); they were more than offset by greater reductions of base rate revenues and increases in other costs charged to normal operations. Mr. Majoros ignores the fact that not all of base salaries and vehicle expense is charged to expense categories normally associated with base rates. He also ignores the fact that the costs he proposes to capitalize include both regular payroll and vehicle costs.

Mr. Majoros erroneously makes several specific criticisms of storm cost accounting which I have addressed in this testimony. The Company has charged the costs of two studies and $43.4 million for future work in its determination of the Storm Damage Reserve deficit, all of which are a direct result of storm damage and therefore should be recoverable. His position on tree trimming expense, call center costs and materials

and supplies, even if accepted, would permit recovery of the amounts charged to the Storm Damage Reserve.

With respect to capital issues, the existing standards are designed to make the customer neutral with regard to rate base. In fact, if FPL records the removal costs as Mr. Majoros is suggesting it would shift this responsibility to future customers.

Q. Does this conclude your rebuttal testimony?

A. Yes, it does.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 930405-EI

TRANSMISSION AND DISTRIBUTION INSURANCE REPLACEMENT

FLORIDA POWER & LIGHT COMPANY OCTOBER 1, 1993

STUDY

October 1, 1993

Study Required by FPSC Order No. PSC-93-0918-FOF-EI Docket No. 930405-EI.

I. Requirement

In the above Order the Commission required, in part, that Florida Power & Light Company (FPL or Company) file a study indicating the appropriate amount that should be contributed to the Storm and Property Insurance Reserve Fund (Storm Fund) annually. The Company was required to include in the study the type of costs it intends to charge to the reserve and information concerning the treatment of all Hurricane Andrew related transmission and distribution (T&D) damages under its then existing insurance policy. The order required that the study be filed three months from the date of the vote in the docket which took place on May 25, 1993. At the Agenda Conference on August 17, 1993, the Commission approved a request by the Company for an extension of the filing date to October 1, 1993. This study has been prepared to meet these specific requirements as set out in the Order.

II. Management Summary

The Company's Storm and Property Insurance Reserve (Reserve) was originally established to cover losses from hurricanes and tropical storms. In the 1980's the Commission expanded the potential use to include losses resulting from retrospective premium assessments associated with the Company's nuclear property insurance.

The Storm and Property Insurance Reserve (Reserve) is currently a "funded reserve." The company recognizes an expense on an annual basis as an accrual to build the Reserve. Then, in order to fund the Reserve, a contribution is made to an external fund, custodied by Melon Bank, equal to the accrual less deferred income taxes, since accruals to the reserve are not currently deductible for income tax purposes. Throughout the rest of this study we will refer only to the Reserve, and the accrual amounts which represent gross accruals to the Reserve rather than the "net-of-tax" contributions which would be made to the Storm Fund.

Until June 1,1993, FPL had replacement cost insurance covering damage to T&D facilities resulting from storms. In the aftermath of Hurricane Andrew, this T&D coverage is unavailable at a reasonable cost and the Company is now self insured for all storm related damage to T&D facilities. While we believe that some insurance may become available in the future at a fair cost, a level of self insurance must be anticipated into the foreseeable future. Self insurance will result in a greater dependance on the Reserve and special customer assessments may be needed to offset losses, therefore, a review of the costs to be charged against the Reserve and the amount of the annual accrual to the Reserve may be appropriate.

The primary questions addressed by this study are: 1) what costs should be charged to the Reserve during the period of self-insurance, and 2) what is the appropriate annual accrual.

1. Costs To Be Charged to the Reserve

Attachment I was developed to present the alternatives for determining costs to be charged to the Reserve when self insured. The amounts presented represent estimated costs for Hurricane Andrew assuming the Company had been self insured for T&D damage when the storm occurred. Three alternatives are presented on this attachment; 1) the actual restoration cost approach, 2) the actual restoration cost approach with a net book value adjustment, and 3) the incremental cost approach.

The Company recommends that the actual restoration cost approach, without adjustment, be used. A "net book value adjustment" will increase the Company's financing requirements, rate base and ongoing depreciation expense resulting in higher revenue requirements and ultimately higher customer rates. Initially the incremental cost approach appears appropriate, however, after evaluating the result, and the numerous adjustments based on estimates and allocations that are required to arrive at incremental cost, we do not believe that the method provides a benefit when compared to use of the simple and more straightforward actual restoration cost approach. Under the actual restoration cost approach, without adjustment, the only review required would be for the necessity and reasonableness of the costs actually incurred and recorded on the Company's books. Further, since the actual restoration cost approach mirrors replacement cost insurance, this approach allows the company to easily switch from self-insurance to traditional insurance if and when it becomes available at reasonable rates. (See Part VII for additional discussion.)

2. Appropriate Annual Accrual

We believe that there is no one precise amount that can be calculated which will be the appropriate accrual. The appropriate accrual depends on many factors, including the availability of insurance, the Reserve balance, the purpose the Reserve is expected to serve, the frequency of required amortization of losses in excess of the Reserve balance, the level of customer revenues acceptable to cover storm losses, and the actual occurrence of storms and their impact on customer facilities. Considering these factors, FPL believes that the annual accrual should remain at its currently approved level of $7.1 million.

In the short-term (i.e. five years) if a catastrophic storm such as Hurricane Andrew were to strike FPL's service territory, the Reserve balance would be inadequate to cover the loss under any reasonable accrual scenario and, therefore, some type of special customer assessment would be necessary. Even long-term, our analysis shows that it is unreasonable to expect that the Reserve will have a balance sufficient to cover losses from all potential catastrophic storms even if the estimated average annual loss is accrued. Therefore, it will be necessary to utilize a combination of the Reserve and special assessments. Thus, we believe the primary objectives of the Reserve become to cover losses from moderate storms and avoid frequent special customer assessments.

Considering these objective, our statistical analysis shows that with an annual accrual of $7.1 million a) the Reserve is expected to have a positive balance, b) the potential for an extreme positive or negative reserve balance is limited (there is a relatively low level of variability in the reserve), and c) on average, special assessments will only be needed once in every ten years. At the same time, total potential payments by customers, both to provide for the accrual and special assessments, would be expected on average to be only about 0.3% of total revenue.

In addition, from a pragmatic short-term perspective, the current balance ($74 million) in the

Reserve increased by annual accruals of $7.1 million over the next five years (7.1 million x 5 = 35.5 million) would result in a Reserve balance of $109.5 million, which is adequate to cover storm losses, assuming the average expected loss of $20.3 million was actually incurred in each of the next five years. However, if FPL does not experience any significant storms within the next several years, reasonably priced insurance could again become available, reducing our reliance on the Reserve. If accruals to the Reserve are set at the level of the estimated average annual loss this would create an unnecessarily high Reserve balance. We are also proposing to reduce the accrual level by the amount of premiums related to any new insurance obtained. In this way the annual accrual will be adjusted to reflect the availability of insurance.

Storm restoration expenses are a legitimate cost of service and as such should be recovered from utility customers. These costs can be collected in advance (prepaid by accruals to a reserve) or collected after the fact through a special assessment. We are proposing that a combination of these two methods is both appropriate and necessary. To the extent that the costs are collected in advance, through an accrual, it is appropriate to set the accrual at the amount embedded in base rates, which is the amount actually being contributed by customers. $7.1 million represents the amount customers are currently contributing for both insurance premiums and accruals to the Reserve. FPL included the amount of insurance premiums included in base rates as a component of the accrual because traditional insurance was not available. If and when insurance does become available it would be appropriate to adjust the annual accrual so that the combination of insurance premiums and Reserve accrual remains at $7.1 million. It would also be appropriate, on an ongoing basis, to review the status of the Reserve, accrual level and underlying assumptions in detail in conjunction with rate proceedings so that rate recovery and any necessary changes in the accrual can be matched at that time.

3. Conclusion

We believe that the use of the actual restoration cost approach for determining the appropriate amounts to be charged to the Reserve is the proper method to use. This approach is simple, straight forward and is consistent with and would work much like replacement cost insurance.
The Company is currently accruing $7.1 million annually to build the Reserve. We believe the $7.1 million accrual should remain in effect at the present time. We would propose, however, that to the extent some amount of T&D insurance again becomes available at a reasonable price, and until the Company's next rate case, the accrual be reduced by the amount of any premium related to the new insurance. The $7.1 million is equal to the cost embedded in FPL's base rates to cover accruals to the Storm Reserve and T&D insurance premiums, and represents what we currently believe to be the appropriate accrual amount.

III. Background

As a result of the unavailability of reasonably priced insurance for its T&D facilities in the aftermath of Hurricane Andrew, and with the approaching expiration of FPL's current policy on May 31, 1993, FPL prepared a self insurance proposal for consideration by the Commission, on April 19,1993. FPL requested approval of the self insurance proposal prior to the start of the 1993 hurricane season which began on June 1, 1993. FPL's self insurance proposal included three parts:

1. Annual contributions to the Storm Fund in the amount of $7.1 million, net-of-tax.
2. Obtaining a dedicated $300 million line of credit.
3. Authorization to recover losses in excess of the Reserve balance over a period of five years through a charge to customers.

The matter went to hearing before the Commission on May 17,1993. The Commission voted on the matter at a special agenda conference held on May 25, 1993 and the final order was issued on June 17, 1993.

In their decision, the Commission acknowledged the adverse effects that Hurricane Andrew has had on FPL's efforts to obtain reasonably priced T&D insurance at an adequate level of coverage and agreed that a self insurance program is a reasonable approach for the Company to follow at this time. The Commission recognized the changing nature of the insurance markets and indicated that, in the future, a combination of self insurance and traditional insurance may become a viable alternative.

The Commission agreed that there is a need for lines of credit to provide for liquidity under the self insurance plan but decided that the appropriate amount of the lines of credit would not be subject to pre-approval. They stated that the needs will vary through time depending on FPL's circumstances including liquidity, the level of the Reserve balance and the T&D inventory. The Company was given the discretion to increase or decrease the amount of the lines of credit established for storm damage liquidity.

The Commission found that FPL should resume and increase its contribution to the Storm Fund by $7.1 million, net-of-tax, effective June 1, 1993. However, FPL's request that the $7.1 million be reduced by the commitment fees for the dedicated lines of credit was rejected. The $7.1 million represents the amount embedded in FPL's base rates, $3 million for Storm Fund contributions and $4.1 million for traditional T&D insurance. The Commission also required that FPL prepare a study indicating the amount that should be contributed to the Storm Fund annually.

The Commission declined to approve the automatic Storm Loss Recovery Mechanism requested by the Company, but they did indicate that if the magnitude of a future storm loss is great, FPL could petition the Commission to act quickly to allow expense recovery from customers. FPL would be allowed to defer the storm damage loss until the Commission acted on the petition. The Commission provided assurance that the Company's petition would be acted on quickly and expeditiously in an emergency situation. The Commission made it clear that the vote did not foreclose or prevent further consideration at a future date of some type of a cost recovery mechanism.

In addition to presenting the Commission's decision on the above issues, the order pointed out that it was unclear what storm related expenses FPL intends to charge against the Reserve or whether the cost of damaged assets would be accounted for at replacement cost or net book value. As a result, and so that the issue related to the appropriate annual accrual to the Reserve could be addressed, the Commission ordered that FPL submit a study. This document represents the study, the specific requirements of which have been discussed earlier under the caption "Requirement".

Finally the order required that the Company file an annual report with the Commission, beginning January 1, 1994, addressing: 1) FPL's efforts to obtain traditional insurance for

the T&D windstorm risk; 2) the status of the proposed industry wide program to insure against losses from natural disasters and any decision made related to participation in that program; 3) an update of the Company's exposure to storm damage and the adequacy of the Reserve; and 4) FPL's assessment of the feasibility and cost effectiveness of a risk sharing plan among the investor owned electric utilities in Florida.

IV. Methodology for Long-Term Statistical Study

FPL's original filing in this docket included a statistical analysis of the annual damage that can be expected to the Company's T&D system as a result of storms. The analysis indicated that, over the long term, FPL could expect to incur damage to its T&D facilities of $19.5 million annually, on average, as a result of hurricanes. While the purpose of the analysis was only to evaluate the economic benefits of purchasing the limited T&D insurance coverage that had been offered to the Company and the results were admittedly "rough" due to the unpredictable nature of hurricanes and the assumptions that had to be made, the analysis was based on the best information available to the Company and provides the starting point for this study.

Utilizing this same methodology and calculating the Hurricane Damage Potential Index, or HDP, as published by Dr. Grey of Colorado State University, the Expected Damage in HDP Units that the state of Florida could expect in damage to T&D facilities annually is 3.329 HDP units. By applying the annual probability of Category I through V storms and the $270 million estimate of Hurricane Andrew T&D damage as the basis for a category IV storm, adding the additional insurance deductibles for non-T&D damage to be charged to the Reserve, and applying 35%, the percentage of FPL-owned T&D facilities within the state of Florida, FPL's average annual loss can be estimated at approximately $20.3 million per year. However, simply putting $20.3 million into a Reserve each year is not a correct answer to the problem. The $20.3 million does not consider the beginning balance in the Reserve which, as of June 1, 1993, totalled $74 million nor does it consider those times when damages exceed the level of the Reserve, or, alternately, when the Reserve balance becomes too high. Nor does it consider that all or a portion of future losses may be covered by traditional insurance. It should also be noted that $20.3 million dollars represents the long-term average annual loss and does not provide an indicator of the loss which can be expected in any given year.

To determine an appropriate amount to put in the Reserve each year it is necessary to perform an additional statistical analysis using a computer simulation technique known as Monte Carlo Simulation, as well as make a number of additional assumptions related to the considerations discussed in the preceding paragraph. This simulation, which uses the damage indices mentioned above, evaluates the effects of four potential policies. Policy I sets the annual accrual equal to FPL's expected annual loss from future hurricane damage, $20.3 million, and assumes no additional action will be taken in the event that future losses exceed the Storm Reserve. Policy II sets the annual accrual equal to $20.3 million, as in Policy I, but, if future losses exceed the Reserve, assumes a special assessment over a five year period to return the Reserve to the $74 million target. Policy III sets the annual accrual to $7.1 million, the amount the Company is currently accruing, and, if future losses exceed the Reserve, assumes a special assessment over five years to return the Reserve to the $74 million target. Policy IV has no annual accrual but, again if future losses exceed the Reserve, assumes a special assessment over five years to return the Reserve to the $74

million target. Using the Monte Carlo Simulation Model to simulate future hurricane landfalls in Florida and charges against the Reserve, FPL was able to study the impact on the Reserve for each of the four policies. The results were tracked through the simulation process for a period of 33 years and repeated for a total of 500 iterations for each of the four Policies.

As can be seen in detail in Attachment 3, Policy III, setting the annual accrual to $7.1 million and special assessments over a five year period to restore the Reserve once losses exceed the balance, is superior to the other policies. Policy I, provides the most uncertainty regarding Storm performance and has the highest probability of the Reserve having a negative balance of any of the alternatives. Policy II has the greatest probability of maintaining reserve balances above zero. This performance is gained by charging today's customers an expected $1.30 for every expected $1.00 in future hurricane losses. The resultant build up in reserve balance may ultimately require a reduction in annual accruals paid by future customers or prove to be redundant if insurance markets eventually return to more normal conditions. Policy IV, a pay-as-you-go policy, sets the target balance of $74 million as a cushion and illustrates that the amount chosen for an accrual can be relatively arbitrary so long as it is within a range low enough as to not result in unbounded Reserve growth and includes a mechanism to address restoration of reserve balances when losses exceed the Reserve. Analysis indicates that an accrual as low as $9 million would result in some fund growth over time, if potential negative balances do result in special assessments.

We believe that the Company's current accrual of $7.1 million is fair to customers as well as stockholders since it a) provides reasonable assurance of the reserve being greater than zero, b) has a good measure of stability to assure intergenerational equity c) would, on the average, only require the Company to implement special assessments once in every 10 years, and d) is the amount currently provided in rates for insurance premiums and accruals to the Storm Fund. While the other policies have some merit on their own, Policy III has the greatest probability of assuring that current customers do no overpay for storm costs.

In addition, in the short-term an accrual of $7.1 million coupled with the existing reserve balance would be adequate to cover the expected losses and avoids an unnecessarily high build up in the reserve if reasonably priced T&D insurance once again becomes available.

V. Treatment of Hurricane Andrew Related T&D Damages (Under Prior Insurance Policy)

Until May 31,1993, FPL's T&D facilities were insured by Arkwright Mutual Insurance Company through a replacement cost policy. Among other things, this policy covered FPL's T&D facilities for loss or damage arising from a windstorm designated by the National Oceanic and Atmospheric Association as a tropical storm or hurricane with a $20 million deductible and covered other losses with a $1 million deductible. In the event of a loss, the policy payed the lesser of the cost to repair or the cost to replace the property with material of like kind and quality. Generally, the policy covered the cost of direct labor charges, including overhead costs attributed to the repair or replacement of the damaged property, and the cost of materials and supplies used in repairing or replacing the damaged property, along with the direct expenses associated with handling of materials and supplies by storeroom personnel. Further, the policy payed an additional amount of 83.61% of direct labor charges, which was designed to cover the cost of administrative, supervisory and engineering expenses and applicable employee benefits. Examples of items not covered are damage related to normal wear and tear, costs arising from the interruption of business, loss or

damage to currency deeds or securities or losses arising from radioactive contamination. Since the language in the policy was broadly worded, it is not practical to specifically identify every cost which was or was not covered by the policy.

FPL has received advances from Arkwright; however, as of this date, FPL has not submitted its full claim, since restoration work and damage assessment is still in process. Currently, the major cost areas at issue are the amount of damage to underground facilities as a result of the storm surge and the proper level of the overhead charges. Negotiations are continuing.

By letter dated July 30, 1993, in conjunction with Docket No. 910081-EI et. al., Order No. PSC-93-0211-FOF-EI, FPL filed a report with the Commission which provides an accounting of Hurricane Andrew restoration costs incurred as of June 30, 1993, and the disposition of insurance proceeds received. As indicated in the report, FPL has incurred (direct) restoration costs in the T&D function, exclusive of substations which were covered under the non-T&D insurance policy, of approximately $246 million. We continue to expect total T&D costs to reach approximately $270 million. Through June 30, we had received advances from Arkwright totaling $220 million. The report is included in the **Appendix** to this study. The Commission required the Company to file the next report by December 31, 1993.

VI. Industry Mutual Insurance Coverage

As was discussed at the hearing, an industry mutual, Line Insurance Company ("Line"), was developed to pursue providing T&D property insurance to electric utility companies. In July 1993, Line provided premium indications to 39 utilities and expected that 20 utilities would join the program. As of late September, only eight utilities (including FPL) have indicated a positive commitment to Line's program. To have a viable program, Line has indicated that either additional utilities must commit to the project or the reinsurance program must be restructured. Line is working (with Marsh & McLennan) to resolve the issues and make the program a viable option. While we continue to believe that some viable form and level of affordable T&D insurance coverage will ultimately become available at some point in the future, efforts to secure such insurance have not materialized.

VII. Charges to the Reserve Under Self Insurance

In conjunction with self insurance for T&D facilities the Company has been asked to consider the appropriateness of charging the Reserve for the incremental cost associated with storms and with the net book value of destroyed property only. Incremental cost would represent costs incurred for storm restoration to the extent that those costs exceed costs which would normally have been incurred. The determination of incremental costs should also consider revenues lost as a result of the storm conditions. To the extent normal cost levels are not recovered due to lower than normal sales, the loss of revenue can be viewed as resulting in normal cost becoming incremental costs. We interpret the net book value adjustment to include capitalization of the normal or fair costs of new facilities installed as a result of the storm, and only charging the Reserve for any abnormal or premium cost of capital additions and for the unrecovered investment in the facilities replaced and retired.

In general, we believe there are three options for calculating charges to the Reserve which we have termed: 1) the actual restoration cost approach, 2) the actual restoration cost approach with a net book value adjustment and 3) incremental cost approach. **Attachment**

1 has been prepared to compare these alternatives. The starting point for the comparisons is the estimated restoration cost for damage to FPL's T&D facilities resulting from Hurricane Andrew. Our analysis indicates that, had FPL been self insured for losses resulting from Hurricane Andrew, calculation of losses charged to the Reserve based on these three approaches would be:

1. Actual Restoration Cost Approach - $270 million
2. Actual Restoration Cost Approach With Net Book Value Adjustment - $228 million
3. Incremental Cost Approach - $299 million

We believe that the actual restoration cost approach, without adjustment, should be used to calculate charges to the Reserve.

1.) Actual Restoration Cost Approach

We would define actual restoration costs to be those direct and indirect costs which are incurred to safely restore customer service, or to return plant and equipment to its original operating condition. In general, these costs include FPL payroll costs, costs associated with the use of vehicles and equipment, inventory costs, payments for outside services provided by contractors and other utilities, security services and crew support costs such as food, lodging, transportation and miscellaneous temporary subsistence costs. Development of a complete, detailed listing of all costs that could possibly be incurred as the result of a storm is neither practical or possible. On pages 2 and 3 of **Attachment 1** we have provided representative examples of the types of activities and related costs that would fit the definition of actual restoration cost and can reasonably be expected to be incurred as a result of a storm.

To capture the actual restoration costs associated with a storm, FPL would use the work order system as was done for Hurricane Andrew. In an emergency situation the focus of attention must be on restoring service and not on completing paperwork. The field accounting must be as simple as possible. Identifying and capturing actual restoration costs incurred as the result of a storm is relatively simple and straightforward. Actual restoration costs are closely related to costs which would be expected to be provided for under a replacement cost insurance policy when insurance is available.

Depending on the future level of replacement cost insurance, varying levels of reliance on the reserve can be anticipated. It is probable that future storm losses will be covered by some combination of insurance proceeds and charges to the reserve. Use of the actual restoration cost approach is consistent with replacement cost insurance and avoids the cumbersome (and potentially arbitrary) accounting for storm restoration utilizing two different methodologies . The use of the actual restoration cost approach also avoids the need to determine what portion of insurance proceeds apply to capitalized costs, normal costs or to non-incremental costs, which would be required, if either the net book value or incremental cost approach is used for determining the cost to be charge to the Reserve.

It is important to note that actual restoration costs charged to the storm work order(s) would not include all costs resulting from a storm. Specifically excluded would be costs which are an indirect result of the storm. In particular, overtime incurred by Company personnel in work areas not directly affected by the storm due to loss of some personnel to storm

assignments (backfill work) and costs associated with work which must be postponed due to the urgency of the storm restoration and accomplished after the restoration is completed (catch-up work) would not be included. In addition, revenues lost by the Company due to the disruption of customer service or the disappearance of customers after the storm would not be included. While these are real costs incurred by the Company as a result of the storm, quantification of these costs must be based on estimates and an arbitrary time period for tracking these costs would be required. For Hurricane Andrew we believe these indirect costs to total approximately $48 million; however this is a rough estimate. While the actual restoration cost approach does not consider these indirect costs, the indirect costs are partially covered since there is also no adjustment to remove costs which would normally be incurred during the restoration period. In this way the use of the actual restoration cost approach to charge the Reserve when self insured would work much like replacement cost insurance.

2.) Actual Restoration Cost Approach With Net Book Value Adjustment

A net book value adjustment would require a clear identification of facilities destroyed by the storm and the normal cost to replace these facilities to calculate the amount to be capitalized. Also, the original cost of destroyed assets and the accumulated depreciation associated with those assets would need to be developed to determine the charge to the Reserve.

The damage done to the T&D facilities by a storm includes both capital and maintenance work. Capital work entails the replacement of a complete retirement unit of property as defined in FPL's Property Unit Catalog. This would include setting a new pole or replacing a span of conductor equal to or greater than a defined retirement unit. Maintenance work involves replacement of less than a retirement unit of property or putting existing facilities back into operation. Maintenance work, for example, would include resetting a toppled pole, rehanging downed conductor and replacing a length of conductor of less than a retirement unit. While capital versus maintenance work is defined and generally identifiable under normal conditions, in a storm restoration situation the distinction can at times become less exact.

Additionally, specific retirements must be based on estimates. Distribution property is treated as mass property in FPL's accounting system. Under the mass property concept the cost of distribution plant is recorded at a retirement unit account level and maintained in total by vintage year of addition to plant in service. The identification of specific vintage year for individual components of property is not maintained. Therefore, to record retirements, a statistical aging program is typically used to estimate the vintage year and original cost to be retired. Transmission properties are maintained by identifiable units of property and specific vintage year of addition, which are the basis of determining the original cost of the asset to be retired. These methods would be used to estimate the original cost for the retirement and to calculate the net book value of T&D property replaced and to be charged to the Reserve as a result of a storm.

The cost of both storm related capital and maintenance work can be substantially higher than the normal cost of the same work due to the adverse working conditions, the increased support costs and the need to restore service as quickly as possible. If costs are to be capitalized, the amount capitalized should be based on normal cost, and the incremental capital work costs incurred in excess of this amount should be treated as abnormal maintenance and charged to the Reserve. This is consistent with National Association of

Regulatory Commissioners (NARUC) Interpretations of the Uniform System of Accounts for Electric and Gas Utilities No. 26-EG, revised July 1987. These Interpretations included the following question and answer:

> Question:
> Considerable damage has been done to utility property by storms. It has become necessary in some instances to go to great expense to replace individual units of property. If the total cost of installing the new plant is charged to plant, a very high unit price results. Is it permissible under such circumstances to charge a normal or "fair" cost to plant and to charge the remaining cost to maintenance?
> Answer:
> Each case should be considered on its merits and presented to the Commission. It is recognized under the conditions cited that the abnormal expenditure is due to the necessity of restoring the property to operating condition without delay and as such a part of the cost is chargeable to maintenance.

The company has the ability to develop "normal" costs for capital work utilizing its existing engineering and cost estimating systems, construction practices, and the actual/estimated quantities of materials installed during the reconstruction period. The result of this process is an estimate of the installed cost that would have been recorded under non-storm conditions.

The Company was asked to consider the appropriateness of capitalizing the cost of the new facilities in the normal manner and charging the Reserve for only the net book value, or unrecovered cost, of the facilities destroyed. To the extent insurance becomes available, a net book value adjustment would be inconsistent with replacement cost insurance recovery. While a net book value adjustment is an alternative, we do not believe it is necessary or appropriate. The cost of replacing and restoring the system to the level of service and conditions that existed prior to the storm are not an on-going cost of service in that there is no incremental benefit other than the restoration of service. The net book value adjustment would increase the Company's rate base and expenses resulting in increased revenue requirements and higher customer rates in the long run. The Company will be adversely affected since the financing cost and ongoing higher depreciation expense associated with the capitalized costs will reduce earnings until base rates are adjusted in conjunction with a rate case. If a net book value adjustment is to be made, capitalized costs should continue to be based on the normal or fair cost of the new facilities, not the premium costs caused by the storm situation. In addition we believe that if a net book value adjustment is made, such an adjustment should be made only in conjunction with the actual restoration cost approach for charging the Reserve. Applying this adjustment in conjunction with the incremental cost approach would defeat the implied purpose of attempting to capture incremental cost, i.e., to charge the Reserve for only those costs in excess of the costs the Company would have normally experienced and thereby leave the Company's earnings level neither negatively or positively affected.

3.) Incremental Cost Approach

While it may seem reasonable in theory to charge only incremental costs resulting from a storm to the Reserve, we believe that there is not a clear benefit derived by attempting to quantify incremental cost. Both direct incremental and indirect incremental costs should be considered if an incremental cost approach is to be used. Recoverable incremental costs

would exclude reasonably estimable and quantifiable costs that would be charged to expenses normally in the absence of a storm. We believe such charges to be straight time FPL employee payroll charged to the storm work order, appropriate loadings for pension, welfare, taxes and insurance applicable to the straight time payroll, and a representative level of normal Company vehicle use charges. If the incremental cost approach is to be used then all incremental costs should be considered, including backfill work, catch-up work and revenues lost by FPL as a result of the storm. While incremental cost can be calculated, it requires starting with actual restoration cost and making numerous adjustments which depend on estimates and allocations. The complexities are apparent when the incremental costs column on page 1 of **Attachment 1** is reviewed. In addition, the exclusion of non-incremental, or normal, costs is based on the premise that these costs are recovered through base rates. Therefore, such an adjustment is only appropriate to the extent that the Company had a normal level of revenue during that period of time. In fact, FPL did not have a normal level of sales after Hurricane Andrew and we believe that the lost revenue experienced exceeded the level of non-incremental expenses included as part of the cost of restoring the T&D system after the storm. The adjustments required to develop the incremental costs are explained on page 6 of the attachment.

Even if the incremental cost approach for calculating charges to the reserve were used, actual restoration costs incurred as a result of the storm would still need to be captured and recorded. Excluding T&D, FPL's properties are still insured at replacement cost and some amount of reasonably priced T&D insurance is expected to again become available in the future. In addition, the field accounting must remain simple and it would be unworkable to attempt to record only incremental costs to the storm work order. Furthermore, each storm can be expected to impact the Company in a unique way and the assumptions and the estimation and allocation techniques needed to calculate indirect incremental costs and non-incremental costs might need modification. We can envision extensive debate before the Commission over these calculations which could result in unnecessary delays. As is the case with the net book value adjustment, the incremental costs approach would be inconsistent with replacement cost insurance recovery when some level of insurance is obtained. In contrast we view the actual restoration cost approach as relatively simple and fair. For these reasons we believe that substantial time and effort could be saved, and debate before the Commission avoided, by simply charging the Reserve for costs incurred directly as a result of storm restoration and clearly attributable to the storm.

VIII. Accounting Entries related to T&D Restoration Costs Under Self Insurance

On February 10, 1993 the FPSC issued order No. PSC-93-0211-FOF-EI in Docket No. 910081-EI which authorized FPL to utilize a specific accounting treatment in conjunction with Hurricane Andrew restoration costs.. The Company had requested approval of this accounting treatment based on the Commission Rule dealing with the use of accumulated provision accounts, certain NARUC interpretations and the anticipated recoveries under FPL's insurance policies, in a letter to the Commission dated January 6,1993. The letter included an example of the accounting entries to record storm related costs and insurance proceeds under this accounting method (Attachment A to the Company's letter). A copy of the Company's request letter and the Commission's Order of approval are included in the **Appendix** to this study.

Attachment 2 has been prepared to demonstrate the accounting entries that would be made when self insurance is necessary. Examples are included for each of the three alternative

approaches for determining charges to the Reserve. The amounts used in these accounting entry examples are based, to the greatest extent possible, on the estimated Hurricane Andrew costs previously identified in Attachment 1.

Page 1 of **Attachment** 2 includes the accounting entries for the actual restoration cost approach. As previously discussed, we believe this to be the appropriate approach for determining charges to the Reserve. The entries required with this approach are basically the same as those which will be made in conjunction with Hurricane Andrew based on the Commission's Order, the only exception being that with self insurance the actual restoration costs result in a negative balance in the Reserve.

Accounting entries for the actual restoration cost with a net book value adjustment approach are shown on page 2 of the Attachment. In this case a portion of the actual restoration cost is transferred to the plant accounts and, therefore, the negative balance in the Reserve is reduced.
While this lower negative balance in the Reserve gives the appearance that a storm had a lesser impact, as discussed earlier, this approach will ultimately result in higher customer rates.

Page 3 of the Attachment includes the accounting entries for the incremental cost approach. Of the three alternatives presented this approach, which charges non-incremental costs to maintenance expense and incremental costs to the Reserve, would result in the largest negative balance in the Reserve.

ATTACHMENTS

ALTERNATIVE APPROACHES FOR DETERMINING AMOUNT CHARGED TO THE STORM RESERVE
UNDER A SELF INSURANCE PROGRAM FOR T&D FACILITIES
(Hypothetical- Based on Hurricane Andrew Estimated Restoration Cost)
$ millions

	Actual Restoration Cost	Actual Restoration Cost w/Net Book Value Adjustment	Incremental Cost
(1) Total T&D Restoration Costs (a)	**$270**	**$270**	**$270**
(2) Insurance Proceeds (b)			
Proceeds	0	0	0
(3) Net Book Value Adjustment (b)			
Capital Additions @ Normal Cost		(51)	
Net Book Value of Retired Assets		9	
Total Net Book Value Adjustment		(42)	
(4) Non-Incremental Cost Adjustment (b)			
Straight-Time (S-T) Payroll:			
Total S-T Payroll			(25)
Less: Amount Capitalized (@normal %)			11
Non-Incremental Payroll (Operating)			(14)
Loading on Non-Incremental Payroll			(3)
Vehicle Charges (Non-Incremental)			(2)
Total Non-Incremental Cost Adjustment			(19)
(5) Incremental Indirect Costs (b)			
Lost Revenue			46
Catch-up Work			1
Back-fill Work			1
Total Incremental Indirect			48
Amount Charged to Reserve	**$270**	**$228**	**$299**

Notes (a) See pages 2 and 3 for examples of activities and related costs components which would be captured through a storm work order
(b) See pages 4 - 6 for methodology and assumptions

Actual Restoration Costs

COSTS INCURRED AS THE RESULT OF A STORM TO RETURN PLANT AND EQUIPMENT TO ITS ORIGINAL OPERATING CONDITION, SAFELY RESTORE SERVICE TO CUSTOMERS, OR COSTS THAT ARE CLEARLY ATTRIBUTABLE TO THE STORM AND ARE REASONABLY QUANTIFIABLE

The following are examples of types of activities and related costs:

- o storm preparation
- o survey for damage assessment - (including engineering assessments)
- o direct repairs
- o costs of temporary housing for restoration crews and support personnel and their related subsistence costs
- o costs to staff and operate staging areas
- o costs incurred to operate centers for damage assessment, repairs and control
- o fuel and related costs for back-up generators
- o incremental costs incurred to meet storm related customer service needs
- o incremental cost incured to operate trouble call phone centers
- o special advertising and media costs
- o employee assistance

Costs will be captured in the accounting system by the following source groups:

Payroll

FPL employee payroll- regular, overtime, and temporary relieving pay.

Vehicle and Vehicle Equipment

FPL Owned and Leased - Charges for FPL owned or leased vehicles and equipment which are considered part of the Company's normal operating fleet. Expenses for operating and maintaining while being used in storm restoration work. Such costs include all costs normally included as a component of the Company's vehicle charge-out rate and expenses for repairing vehicles damaged while being used in storm restoration work.

Materials and Supplies Inventories

Material and supplies inventory costs directly related to storm restoration activities. Inventory issues (and return items) shall include, as appropriate, an adjustment to the stores loading rate to reflect the incremental costs of storeroom operations not charged directly to the storm restoration work orders.

Actual Restoration Costs - continued

Miscellaneous Cash Payments (Cash Voucher Source)

Contractor and Outside Services - electrical contractors, other utility crews, line clearing and debris removal, security, temporary employees and other professional or outside services incurred as a result of the storm.

Rental Vehicles and Equipment - rental expense including operating and maintenance costs to the extent paid for by FPL. Accident repair costs if the direct result of storm restoration activities.

Employee Owned Vehicle Usage - reimbursement at the Company's standard mileage rate.

Damage repairs to employee vehicles if damages were incurred as a result of restoration activities.

Crew Support Costs and Employee Related Expenses - hotel and lodging, catering services including food, water and employee meal reimbursements, transportation and miscellaneous temporary subsistence allowances. Miscellaneous travel and business related employee reimbursements.

Special Equipment & Facilities Rental - rental cost and the related costs of operating and maintaining communication equipment, office equipment, special use and heavy equipment, and costs related to the use of temporary facilities if incurred as a result of the storm or in the support of restoration activities.

Miscellaneous office supplies, courier/ messenger service, and data processing equipment rental, supplies and services.

Helicopters - rental/lease and operation costs if incurred as the result of the storm or storm restoration activities. Incremental operating costs of Company owned aircraft if incurred as the result of the storm or in support of restoration activities.

Advertising and media relations - safety and storm related public service advertising and media costs.

Costs resulting from injuries to personnel incurred as a result of restoration activities.

Miscellaneous Other Non-Cash Charges (Journal Voucher Charges)

Pension, Welfare, Taxes and Insurance - applied to the appropriate FPL payroll charges.

Appropriate Engineering Overhead costs applied - to the extent not included in the direct charges above.

Increase in uncollectible customer accounts receivable write-offs directly attributable to the storm.

Miscellaneous Journal Voucher charges - Employee overtime meal allowances paid through the payroll system, storm related expenses charged by corporate credit card and paid directly by the Company and, apprpriate corporate charge-backs.

(1) **Total T&D Restoration Costs**

Estimated based on actual costs incurred for Hurricane Andrew as of June 30, 1993.

(2) **Insurance Proceeds**

To the extent insurance becomes available in the future, proceeds would be applied to off-set the amount charged to the reserve.

(3) **Net Book Value Adjustment**

Capital Additions @ Normal Cost

Estimated installed costs under normal non-storm conditions. Costs are developed using the Company's normal engineering and cost estimating systems and practices and the estimated/actual quantities of materials installed during the reconstruction. For purposes of this study the capital additions were estimated based on amounts recorded for Hurricane Andrew as of June 30. 1993.

Net Book Value of Retired Asset

Undepreciated value of retired asset (original cost less accumulated provision for depreciation). Computed using normal Company practices for determining original costs and net book value of retired assets. For purposes of this study net book value was estimated based on retirements recorded for Hurricane Andrew as of June 30, 1993 and an assumed fifty percent depreciated value.

(4) Non-Incremental Cost Adjustment

Total Straight-Time Payroll

Payroll charged to the storm work order for regular hours worked (i.e.excludes charges for overtime hours and temporary relieving pay). Amount applicable to T&D is computed based on the overall ratio of S-T payroll to Total payroll charged to the storm work order for all functions, multiplied times the total of T&D payroll charged to the storm work order. To the extent available the actual straight-time payroll charged to T&D storm work orders would be used.

Less: Amount Capitalized (@ normal %)

Total T&D S-T payroll (from above) multiplied by the percentage of T&D S-T payroll normally charged to capital projects under non-storm conditions. For purposes of this study the year-to-date period immediately preceding the storm (January- July 1992) was use as a period representative of non-storm conditions.

Non-Incremental Payroll (Operating)

Total Straight Time Payroll less Amount Capitalized (from above)

Loadings on Non-Incremental Payroll

Non-Incremental Payroll (Operating) from above, multiplied by the appropriate pension, welfare, taxes and insurance loading rates applicable to regular payroll. The components of pension, welfare, taxes and insurance are the same components normally used in computing the Company's payroll loading rates.

Vehicle Charges (Non-Incremental)

Total T&D Vehicle charges included in the storm work order, multiplied by the overall ratio of regular payroll hours to total payroll hours charged to the storm work order for all functions (*). This product was then multiplied by the percentage of T&D Vehicle charges normally charged, under non-storm conditions, to operating expense. For purposes of this study the year-to-date period immediately preceding the storm (January- July 1992) was used as a period representative of non-storm conditions. (*) To the extent available for future storms the actual ratio applicable to only T&D work would be used.

(5) Incremental Indirect Costs

Lost Revenue

Estimated KWH not sold as a result of the storm outages, multiplied by the retail system average base rate (non-clause) revenue per kwh. For purposes of this study the period used to determine the average revenue/Kwh was the twelve month period ended 12/31/92. The estimate of kw hours not sold was obtained from the Company's January 15,1993 response to the FPSC's October 20, 1992, Hurricane Andrew data request, Question No. 9, which was computed based on the number of customers without power each day between August 24, 1992 and December 28. 1992. (Estimated 1,083,000 mwh not sold x $42.97 = 46.5 million.)

Catch-up Work

Estimated at $1 million. Data for Hurricane Andrew not available.

Back-fill Work

Estimated at $1 million. Data for Hurricane Andrew not available.

Exhibit No. _____
KMD - 3
Docket No. 041291-EI
FPL Witness: K.M. Davis
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March 8, 2005

ACCOUNTING FOR STORM DAMAGE
SUMMARY OF ACCOUNTING ENTRIES
($ Million)

Exhibit No. KMD - 3
Docket No. 041291-EI
FPL Witness: K.M. Davis
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EXAMPLE: Actual Restoration Cost Approach

(BB) Beginning balance before storm.
(1) Record costs incurred from storm (assume $270).
(2) Record insurance proceeds (assume $0).
(3) Transfer amount from Storm Fund to cover costs incurred in excess of insurance recovery (limited to BB).
(4) Retire cost of property removed (assume $18 cost).
(5) Capitalize new additions at normal cost estimate (assume $51).
(6) Transfer unrecovered costs to the Reserve.
(7) Apply Reserve to offset the retirement in the Depreciation Reserve and credit Plant-in-Service in an amount necessary to reduce the costs of the new asset to equal the original cost of the retired asset.
(EB) Ending balance

Cash (Acct. 131)

DR	CR
(2) 0	(1) 270
(3) 74	
(EB) 196 (b)	

Deferred Debit-Storm Costs and Recovieries (Acct. 186)

DR	CR
(1) 270	(2) 0
	(3) 74
	(5) 51
	(6) 145
(EB) 0	

Plant-In-Service (Acct. 101)

DR	CR
(BB) 18	
(5) 51	(4) 18
	(7) 33
(EB) 18 (c)	

Depreciation Reserve (Acct. 108)

DR	CR
4) 18	(BB) 9
	(7) 18
	(EB) 9

Storm Fund/Deferred Tax-Assets (Accts. 128/190) (a)

DR	CR
(BB) 74	
	(3) 74
(EB) 0	

Reserve-Accumulated Provision for Property Insurance Reserve (Acct. 228.1)

DR	CR
	(BB) 74
(3) 74	
(6) 145	
(7) 51	
(EB) 196 (d)	

NOTES
(a) Combined for ease of presentation only.
(b) To be temporarily funded through the line of credit.
(c) To be recovered through future depreciation expense.
(d) To remain in the reserve pending future disposition under Rule No. 25-6.014.

ACCOUNTING FOR STORM DAMAGE
SUMMARY OF ACCOUNTING ENTRIES
($ Million)

EXAMPLE: Actual Restoration Cost with Net Book Value Adjustment Approach

(BB) Beginning balance before storm.
(1) Record costs incurred from storm (assume $270).
(2) Record insurance proceeds (assume $0).
(3) Transfer amount from Storm Fund to cover costs incurred in excess of insurance recovery (limited to BB).
(4) Retire cost of property removed (assume $18 cost).
(5) Capitalize new additions at normal cost estimate (assume $51).
(6) Record deficiency from retirement to storm costs.
(7) Transfer unrecovered costs to the Reserve.
(EB) Ending Balance

Cash (Acct. 131)

DR	CR
(2) 0	(1) 270
(3) 74	
(EB)196 (b)	

Deferred Debit-Storm Costs and Recoveries (Acct. 186)

DR	CR
(1) 270	(2) 0
(6) 9	(3) 74
	(5) 51
	(7) 154
(EB) 0	

Plant-In-Service (Acct. 101)

DR	CR
(BB) 18	
(5) 51	(4) 18
(EB)51 (c)	

Depreciation Reserve (Acct. 108)

DR	CR
	(BB) 9
(4) 18	(6) 9
	(EB) 0

Storm Fund/Deferred Tax-Assets (Accts. 128/190) (a)

DR	CR
(BB) 74	
	(3) 74
(EB) 0	

Reserve-Accumulated Provision for Property Insurance (Acct. 228.1)

DR	CR
	(BB) 74
(3) 74	
(7) 154	
(EB) 154 (d)	

NOTES

(a) Combined for ease of presentation only.
(b) To be temporarily funded through the line of credit.
(c) To be recovered through future depreciation expense.
(d) To remain in the reserve pending future disposition under Rule No. 25-6.014.

ACCOUNTING FOR STORM DAMAGE
SUMMARY OF ACCOUNTING ENTRIES
($ Million)

Exhibit No. _____
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EXAMPLE: Incremental Cost Approach

(BB) Beginning balance before storm.
(1) Record costs incurred from storm (assume $270).
(2) Record insurance proceeds (assume $0).
(3) Transfer amount from Storm Fund to cover costs incurred in excess of insurance recovery (limited to BB).
(4) Retire cost of property removed (assume $18 cost).
(5) Capitalize new additions at normal cost estimate (assume $51).
(6) Record non-incremental cost adjustment as maintenance expense.
(7) Record lost revenue, catch-up and backfill adjustment as a credit to maintenance expense.
(8) Transfer unrecovered costs to the Reserve.
(9) Apply reserve to offset the retirement in the Depreciation Reserve and credit Plant-In-Service in an amount necessary to reduce the costs of the new asset to equal the original cost of the retired asset.
(EB) Ending Balance

Cash (Acct. 131)

DR	CR
(2) 0	(1) 270
(3) 74	
(EB) 196 (b)	

Deferred Debit-Storm Costs and Recoveries (Acct. 186)

DR	CR
(1) 270	(2) 0
(7) 48	(3) 74
	(5) 51
	(6) 19
	(8) 174
(EB) 0	

Plant-In-Service (Acct. 101)

DR	CR
(BB) 18	
(5) 51	(4) 18
	(9) 33
(EB) 18 (c)	

Depreciation Reserve (Acct. 108)

DR	CR
	(BB) 9
(4) 18	(9) 18
	(EB) 9

Maintenance Expense

DR	CR
(6) 19	(7) 48
(EB) 29	

Reserve-Accumulated Provision for Property Insurance (Acct. 228.1)

DR	CR
(3) 74	(BB) 74
(8) 174	
(9) 51	
(EB) 225 (d)	

Storm Fund/Deferred Tax Assets (Accts. 128/190) (a)

DR	CR
(BB) 74	
	(3) 74
(EB) 0	

NOTES (a) Combined for ease of presentation only.
(b) To be temporarily funded through the line of credit.
(c) To be recovered through future depreciation expense.
(d) To remain in the reserve pending future disposition under Rule No. 25-6.014.

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Attachment 3
Page 1 of 6

Estimating Average Hurricane Losses Chargeable to the Storm Reserve Over the Long Term Under the Self Insurance Program

Mr. Hoffman's direct testimony of April 19,1993 discussed FPL's methodology of estimating average annual T&D damages chargeable to the Storm Reserve. That methodology is reviewed below.

During the 94 years between 1899 and 1992 a total of 155 hurricanes struck the continental United States. The distribution of those hurricanes by category at time of landfall is shown on the table below.

	Category of Hurricane					
	I	II	III	IV	V	All
Hurricane Landfalls	60	34	44	15	2	155
Percentage	39%	22%	28	10%	1%	100%

Florida landfalls by hurricanes during that period totalled 55. From that information, the annual probability landfall in Florida by category of hurricane can be calculated by multiplying the percentage breakdown for each category by 55 and dividing by the number of years (94). For example, the annual probability of a Florida landfall by a category III hurricane is 28% (or 44 divided by 155) of 55 divided by 94 or 0.1661 as shown in the next table.

	Annual Probability of Hurricane Landfall in Florida By Category					
Category	I	II	III	IV	V	All
Probability	0.2265	0.1283	0.1661	0.0566	0.0076	0.5851

Dr. Grey of Colorado State University has published an index of the relative potential for damage for each category of hurricane. The index is called the Hurricane Damage Potential Index or HDP. That index may be combined with the probabilities above to develop an annual expected hurricane damage index value as shown in the next table.

Category	(A) HDP Index Value	(B) Annual Probability	(A) * (B) Expected Damage in HDP Units
I	1	.2265	0.226
II	4	.1283	0.513
III	9	.1661	1.495
IV	16	.0566	0.906
V	25	.0076	0.189
Cumulative Totals		.5851	3.329

Thus, in total, the state of Florida could expect an average value of 3.329 HDP units of damage to T&D facilities annually.

Damages incurred as a result of Hurricane Andrew were used to calibrate the HDP index value in terms of dollars of damage to T&D facilities. Andrew was a category IV hurricane with an index value of 16. Actual damage to T&D facilities was $270 million. In addition, $8 million in deductibles for damages to insured non-T&D facilities would have been incurred assuming current policy provisions had applied to Hurricane Andrew. Total damages that could be recoverable through the Storm Reserve were thus $270 plus $8 or $278 million. Therefore, each unit of damage, expressed in terms of the index, is $278 million divided by the index value for a category 4 storm (16) or $17.4 million.

Future average annual T&D damage for the entire state from hurricanes should thus be 3.329 times $17.4 million or $57.8 million. FPL owns 35% of all T&D facilities located within Florida, and would expect to incur a like proportion of all hurricane damages to T&D facilities within the state. Thus, FPL should expect to incur an average of 35% of the annual expected damage to T&D in Florida or approximately $20.3 million per year.

Evaluating an Appropriate Annual Accrual Amount

Introduction

FPL has utilized a Monte Carlo Simulation Model to study the problem of determining the proper annual contribution to the Storm Reserve. The model was designed to simulate future hurricane landfalls in Florida and charges against the Storm Reserve. The resulting balance was tracked through the simulation process for a period of 33 years. This process was repeated for a total of 500 iterations for each of several alternative contribution levels.

All damage estimates and Storm Reserve balances used in the simulation were expressed in 1992 dollars, and a real rate of return of .20% (net of inflation) was applied to Storm Reserve balances for each simulation year.

This analysis does not consider the potential for future purchase of insurance coverage for T&D facilities. The availability and price of such coverage has been severely constrained since the Andrew experience. Insurance markets may eventually settle to the point where it is once again possible to obtain policies for reasonable premiums.

FPL Storm Reserve Study

An analysis was conducted for the FPL Storm Reserve. In this study, the initial reserve balance was set to $74 million, and a total study period of 33 simulated years was used. The 33 year period is adequate to illustrate the behavior that could be expected with each of the several annual contribution levels considered, and allows simulated Storm Reserve charges to be compared against the hypothesized results.

A total of four alternative administrative policies were evaluated by means of these simulations. Two input variables were used to differentiate each of the administrative policies evaluated in this analysis. The annual accrual amount was the first study variable. Another necessary part of administrative policy for the Storm Reserve, and the second study variable, is the response to be taken in the event that the Storm Reserve is depleted. One possible response, studied as Policy I, is merely to continue annual accruals in the belief that the Storm Reserve will eventually "overcome" past losses. An alternative response is to schedule supplemental payments in addition to normal accruals whenever Storm Reserve balances are depleted. Such payments could be used to bring the Storm Reserve back to any desired target. This alternative response is evaluated with policies II, III, and IV. In the simulation process supplemental payments were scheduled over a five year time period, beginning the first year after the simulated loss occurred. The target balance for which payments in addition to annual accruals were scheduled was set at $74 million, an amount sufficient to cover FPL's portion of a moderate (Category III-IV) hurricane striking randomly along Florida's coastline.

The four alternative administrative policies examined by simulation were:

Policy I - Annual accrual equal to FPL's expected annual loss from future hurricane damage ($20.3 million). No additional action taken in the event that future losses exceed the Storm Reserve.

Policy II - Annual accrual equal to FPL's expected annual loss from future hurricane damage ($20.3 million). In the event that future losses exceed the Storm Reserve the annual accrual would continue and additional payments sufficient to return the Storm Reserve to the targeted $74 million would be scheduled over a 5-year time horizon with no consideration of annual accruals.

Policy III - Annual accrual equal to $7.1 million. In the event that future losses exceed the Storm Reserve the accrual would continue and additional payments sufficient to return the Storm Reserve to the targeted $74 million would be scheduled over a 5-year time horizon with no consideration of annual accruals. The selection of $7.1 million for the annual accrual was based on consideration of

fairness to stockholders as well as ratepayers as it is the amount currently provided in rates for payment of insurance premiums for T&D coverage as well as accruals to the Storm Reserve.

Policy IV - No annual accrual. In the event that future losses exceed the Storm Reserve payments sufficient to return the Storm Reserve to the targeted $74 million would be scheduled over a 5-year time horizon.

Each policy was simulated for 500 iterations. The simulated damages were assessed against the Storm Reserve in the year after the hurricane landfall to mimic the actual delay that occurs in assessing and repairing actual damages. Each iteration was terminated after completing a simulation of 33 years duration and the results were tabulated.

A number of variables were tracked during each iteration. These variables enabled the performance of each alternative policy to be evaluated according to several criteria. The criteria of interest were:

1) The future annual probability that the Storm Reserve will be solvent. A Storm Reserve without a positive balance is unlikely to fulfill any useful purpose. The probability that the Storm Reserve will be solvent was calculated for each future year in the 33 years simulated. For each year "n", this probability is equal to the percentage of the 500 iterations for which the Storm Reserve balance was positive. Annual probabilities for each alternative administrative policy are shown on Chart V, attached. The probability of reserve solvency for year 33 for each policy is presented on the table below.

2) The relative stability of future Storm Reserve balances. Extreme reserve balances, whether positive or negative would mean that the administrative policy was either collecting too much or too little relative to actual losses. Extreme Reserve balances might require future changes to the administrative policy for the Reserve. If future Storm Reserve balances reach too high a level, then corrective action such as refunds to customers and/or termination of annual accruals may be required. Such action would mean that past customers had paid a disproportionate amount for hurricane losses. Similarly, balances could decline to a point in the future where the Storm Reserve could become a debit balance to be recovered from customers rather than a credit balance to offset potential losses. The measure of relative stability of future Storm Reserve balances used in this study was the standard deviation of Storm Reserve balances in year 33.

3) The portion of annual revenues required by the Storm Reserve was used to indicate the relative burden imposed by the each policy alternative. The portion of annual revenues is expressed as a percentage, based on the sum of all accruals to the Storm Reserve including regular annual accruals and, if applicable, any additional accruals scheduled whenever the Storm Reserve became insolvent. The maximum expected burden, defined as the percent of gross revenue required to support the fund for year 33 for 95% of all simulations for each respective policy , is shown in the table below. The probability for

each year of the 33 year period is shown in graphical form in Chart VI, attached. The expected value for each year is considerably less than the maximum value shown on the chart. These 95% values are intended to demonstrate the level of burden associated with relatively severe losses as opposed to average or expected losses.

Simulation results are presented in both table and chart format. The tables below summarize the results by providing values for year 33 for each of the three variables of interest.

Statistics for Alternative Policies in Year 33			
Policy	Probability of Reserve Solvency	Standard Deviation of Balance	Maximum (95% Confidence Level) of All Charges as a Percent of Revenues
I	0.65	$364	0.4%
II	0.95	$171	1.6%
III	0.81	$140	1.6%
IV	0.63	$ 82	1.6%

Discussion of Results

Policy I suffers in several regards. It has the highest "Standard Deviation of Balance" indicating that future Storm Reserve performance is more uncertain than any of the alternatives, and that the viability of this alternative is weakest. The relatively high potential for large positive or negative balances increases the risk of a significant inter-generational wealth transfer if this alternative were adopted. Further, the probability that the reserve will be solvent is lower than that of all other alternatives. This performance reflects the lack of any planned corrective action when and if cumulative annual losses exceed long run expected averages. Average payments as a percent of revenues is lower than other alternatives, but this is merely a reflection of the Storm Reserve's inability to cover losses if they are larger than the expected long run average and does not reflect a cost savings.

Policy II has the highest probability of remaining solvent. However, this strength is gained at the expense of a built in bias for transfer of wealth from current customers to future customers. As illustrated in Chart II, the expected Storm Reserve balance grows over time. While this may, on the surface, appear to be desirable, it actually represents a transfer of wealth from customers of one generation to the next. Analysis shows that total payments under this policy would be expected to exceed total losses by approximately 31% during the first 33 years. Overpayment in early years results in a fund buildup that explains why average payments as a percent of revenue declines in later years under this alternative.

Policy III provides performance that compares reasonably well to that of Policy II with regard to

future solvency, and uncertainty about future balances is reduced from Policy I and II. This policy also avoids the wealth transfer bias associated with the constant growth in expected future Storm Reserve balances exhibited by Policy II.

Policy IV amounts to a "pay-as-you-go" policy. In effect, the target balance ($74 million) would serve as a cushion to absorb cumulative losses until depleted, at which time supplemental (as opposed to annual contribution) payments would be scheduled to bring the Storm Reserve back to the target level. This policy illustrates that the amount chosen for annual accrual can be relatively arbitrary so long as it is within a range low enough so as not to result in unbounded growth in expected future Storm Reserve balances, and if it is combined with a mechanism to address insolvency.

The charts attached provide a more detailed analysis of some of the performance indicators. The first four charts address the distribution of future Storm Reserve balances for each alternative administrative policy. Each of these four charts shows the expected future Storm Reserve balance as well as a 90% confidence interval for future balances. These charts offer the best indication of the risk of inter-generational wealth transfers incurred with the selection of each alternative policy.

Uncertainties about the future balance of the Storm Reserve is indicated by the "spread" in the range of possible values within the 90% confidence band shown on each chart. This risk is measured directly by the standard deviation of the balance and, as shown on the table, Policy I results in the highest risk of this type.

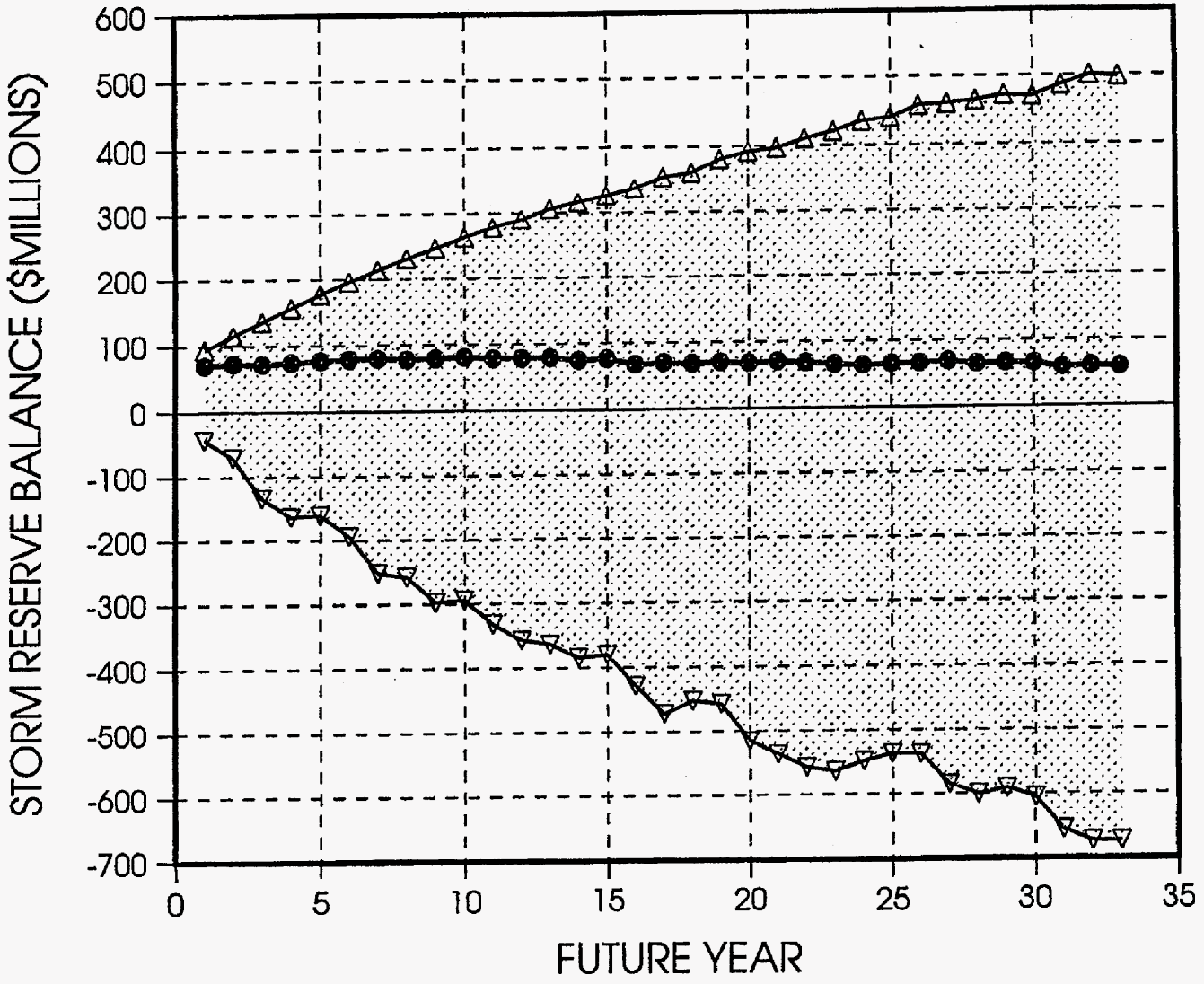
Bias is a systematic risk that current customers will be called upon to pay an amount higher or lower than their fair share of costs associated with hurricane damage. Any consistent trend in the expected balance of the Storm Reserve is an indication of this type of risk. The only policy that exhibits this form of risk is Policy II. Policy II exhibits a tendency to accumulate ever increasing balances indicating that customers would tend to pay more than their fair share of costs. Storm Reserves under Policy II exhibit a positive bias (they grow) because total accruals will exceed total debits by an expected ratio of 1.31 to 1.

The fifth chart, labelled "Probability of Storm Reserve Solvency", plots the percentage of simulation iterations for which Storm Reserve balances were above zero in each future year. This chart is designed to facilitate comparison of the alternative administrative policies in terms of their potential for maintenance of the Storm Reserve's ability to cover future losses. Note that performance of Policies II and III dominate Policy I in that the probability that the Storm Reserve would remain solvent is greater in each future year for those policies than it is for Policy I. This reflects the fact that Policy I does not have any mechanism to facilitate Storm Reserve balance recovery in the event of catastrophic loss. Policy IV's performance in this regard is somewhat below Policy I in earlier years, but their performances cross in or near year 33.

The sixth chart, labelled "All charges as a Percent of Total Revenue" illustrates that none of the policies examined would, with a 95% confidence, require payments in excess of about 1.6% of annual revenue in any future year. Clearly this would indicate that no policy considered in this analysis should be excluded from consideration for fear that it could unduly burden customers if severe losses occur.

Attachment 3
Chart I

RANGE OF FUTURE STORM RESERVE BALANCES
WITH ADMINISTRATIVE POLICY I
USING CONSTANT 1992 DOLLARS



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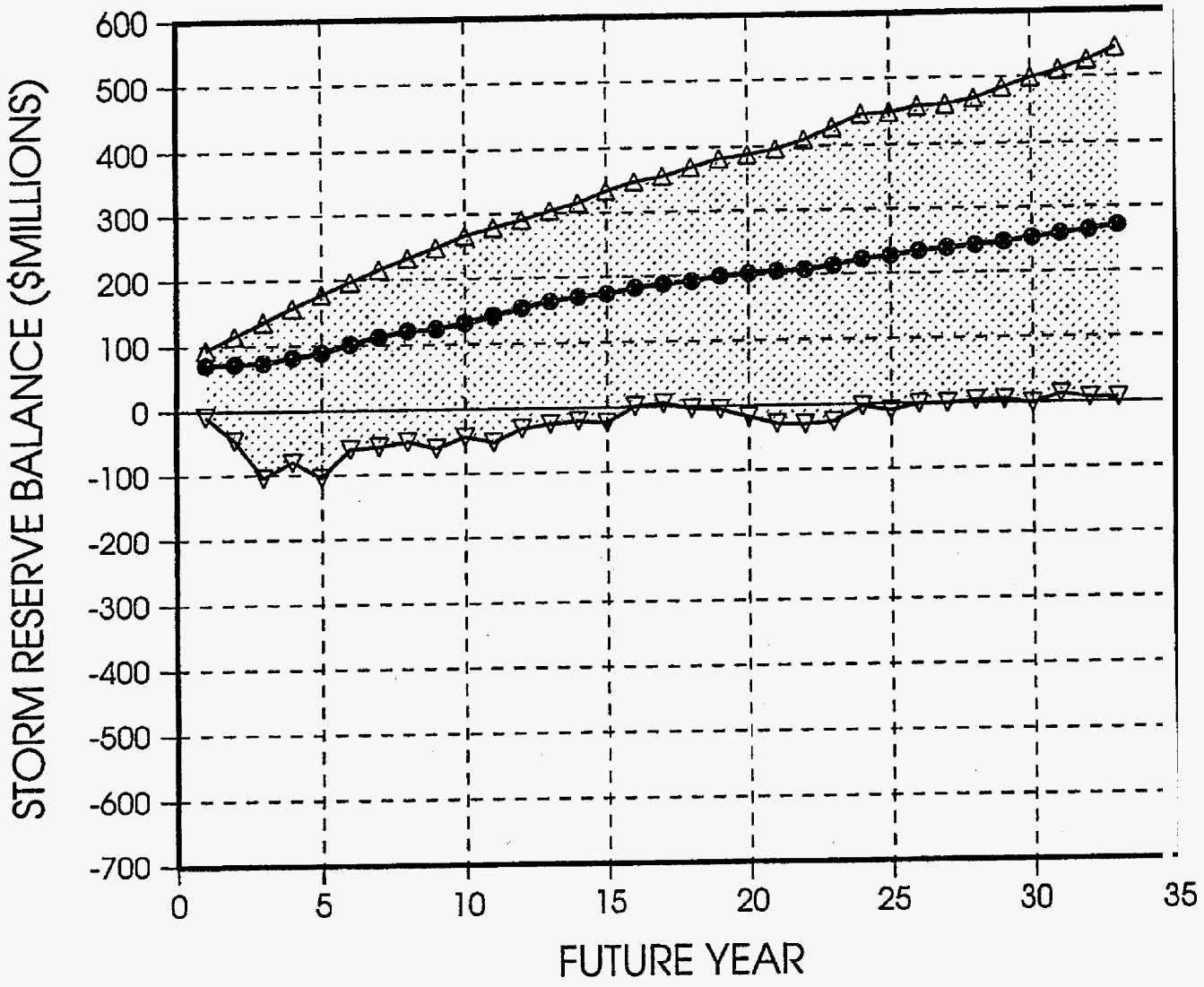
Attachment 3
Chart II

RANGE OF FUTURE STORM RESERVE BALANCES
WITH ADMINISTRATIVE POLICY II
USING CONSTANT 1992 DOLLARS



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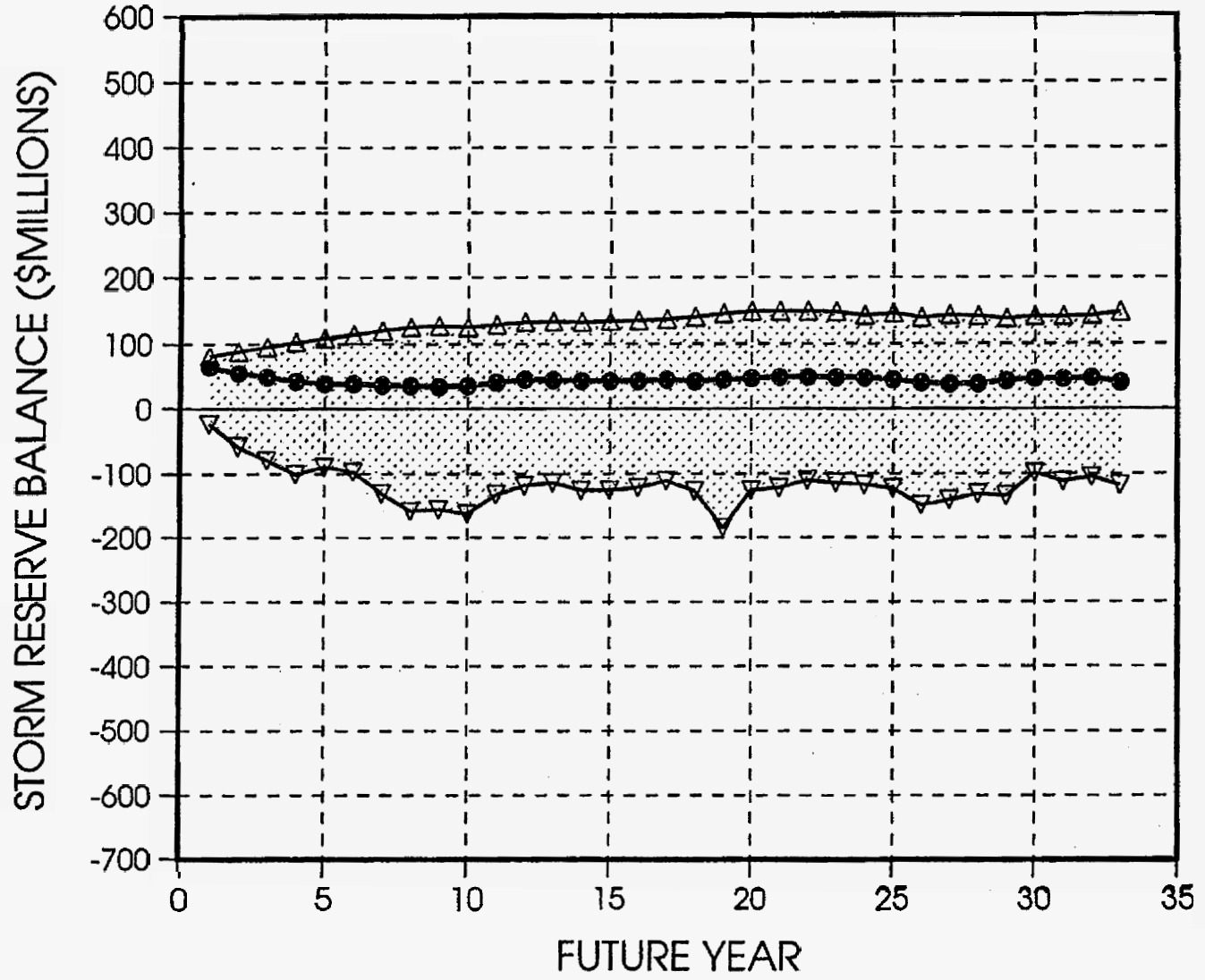
Attachment 3
Chart III

RANGE OF FUTURE STORM RESERVE BALANCES
WITH ADMINISTRATIVE POLICY III
USING CONSTANT 1992 DOLLARS



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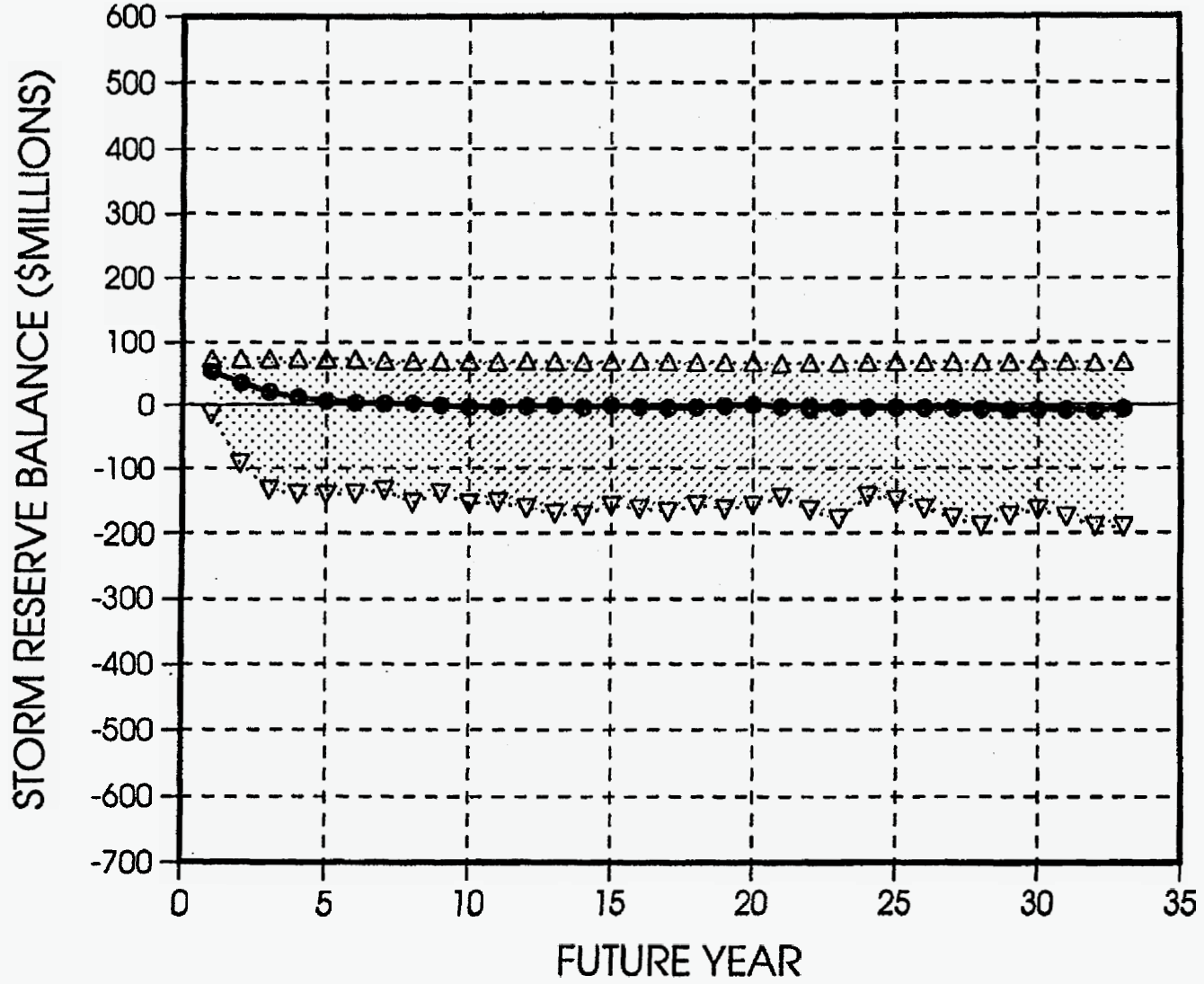
Attachment 3
Chart IV

RANGE OF FUTURE STORM RESERVE BALANCES
WITH ADMINISTRATIVE POLICY IV
USING CONSTANT 1992 DOLLARS



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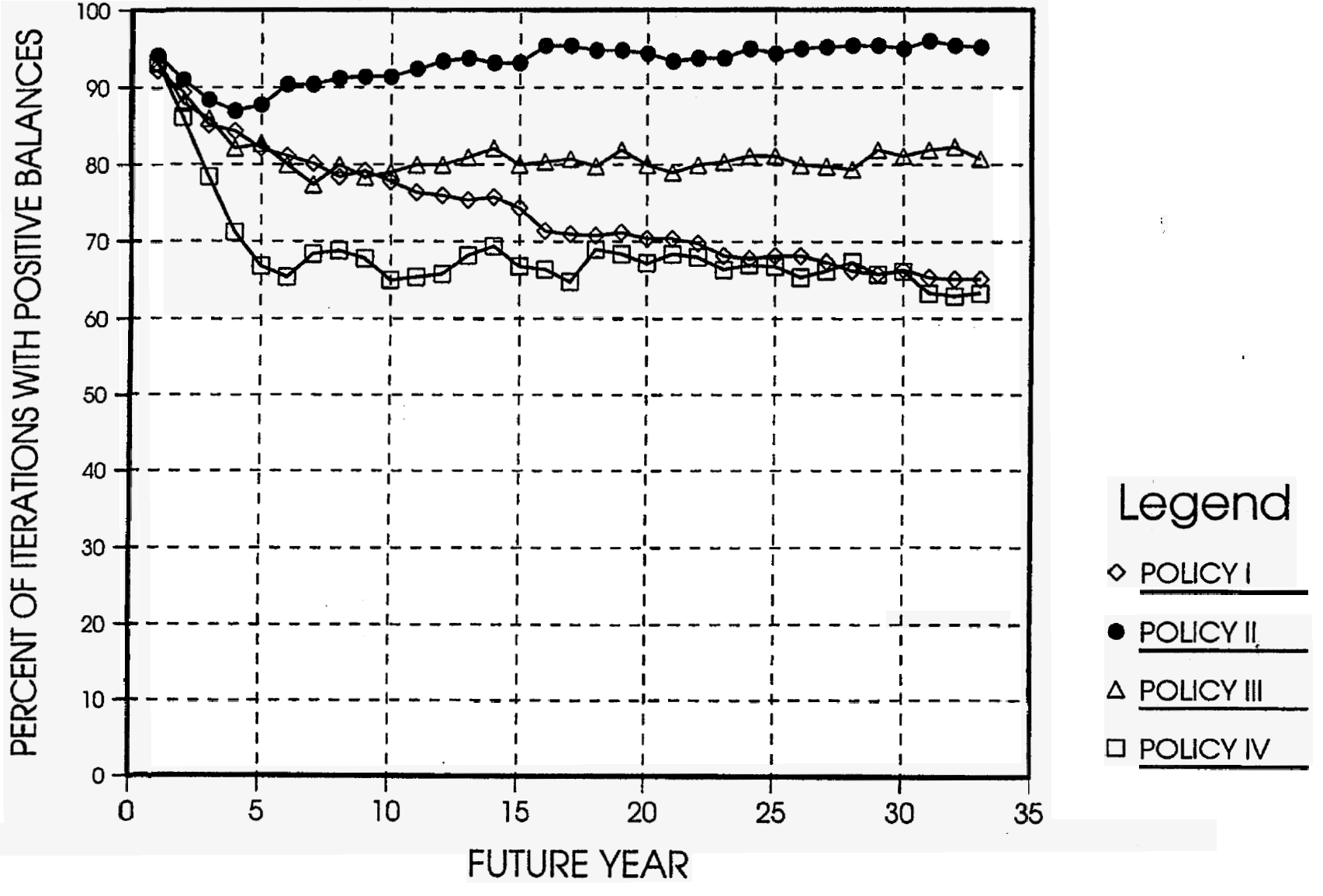
Attachment 3
Chart V

PROBABILITY OF STORM RESERVE SOLVENCY

UNDER EACH ALTERNATIVE ADMINISTRATIVE POLICY

FOR EACH FUTURE YEAR 1 THROUGH 33



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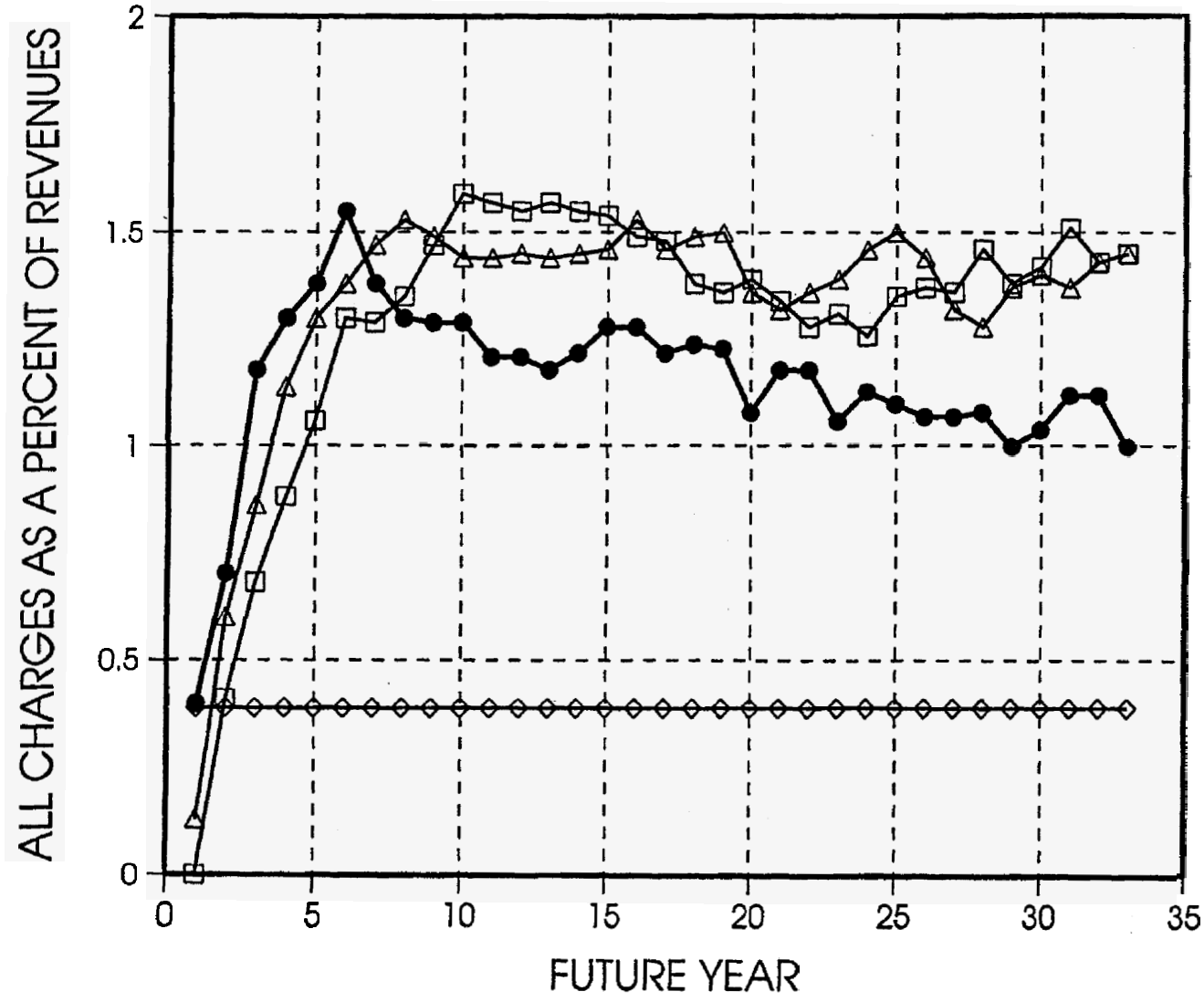
Attachment 3
Chart VI

ALL CHARGES AS A PERCENT OF TOTAL REVENUES

MAXIMUM AMOUNTS AT 95% CONFIDENCE LEVEL

UNDER EACH ALTERNATIVE ADMINISTRATIVE POLICY



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APPENDIX

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P.O. Box 029100, Miami, FL 33102

January 6, 1993

Mr. Timothy Devlin
Director of Auditing and Finance
Division of Auditing and Financial Analysis
Florida Public Service Commission
101 East Gaines Street
Tallahassee, Florida 32399-0872

Re: Accounting for Damages Caused by Hurricane Andrew

Dear Mr. Devlin:

On August 24, 1992, Hurricane Andrew struck South Florida resulting in extensive damage to Florida Power & Light Company's (FPL) transmission and distribution facilities and to the buildings and equipment at the Cutler and Turkey Point power plants. Despite the extensive damage caused by Hurricane Andrew, the cost of reconstruction is not expected to have an adverse effect on future earnings, since FPL has insurance coverage of $350 million on transmission and distribution facilities and more than $6 billion on power plants. In addition, the Florida Public Service Commission (FPSC) recognized the need to provide for such losses and allowed FPL to accrue for storm losses. Therefore, FPL had over $90 million in its Storm and Property Insurance Reserve to cover insurance deductibles and uninsured storm losses.

Even though the reconstruction effort and the determination of the amounts to be capitalized and expensed have not been finalized, we are requesting your concurrence with our proposed accounting treatment for these costs. Our proposed accounting treatment for the reconstruction costs is based on Commission Rule 25-6.0143 Florida Administrative Code, Use of Accumulated Provision Accounts 228.1, 228.2, and 228.4 and Interpretation Nos. 26-EG and 67-EG of the National Association of Regulatory Utility Commissioners, Interpretations of the Uniform System of Accounts for Electric and Gas Utilities, revised July, 1987.

Replacements, Retirements and Removal Costs

The cost of replacements of units of property will be charged to the appropriate plant accounts at the normal or "fair" cost and any amounts in excess of the normal or "fair" cost will be treated as abnormal maintenance expense. In addition, removal costs will be recorded at normal or "fair" cost with any excess considered maintenance. This accounting treatment is supported by Interpretation No. 26-EG:

Question:
Considerable damage has been done to utility property by storms. It has become necessary in some instances to go to great expense to replace individual units of property. If the total cost of installing the new plant is charged to plant, a very high unit price results. Is it permissible under such circumstances to charge a normal or "fair" cost to plant and to charge the remaining cost to maintenance?
Answer:
Each case should be considered on its merits and presented to the Commission. It is recognized under the conditions cited that the abnormal expenditure is due to the necessity of restoring the property to operating condition without delay and as such a part of the cost is chargeable to maintenance.

Retirements of damaged property will be recorded in the normal manner as prescribed by the FPSC's Uniform System of Accounts.

Reimbursements from Insurance Carriers and the Storm Fund

The amount withdrawn from the Storm Fund and charged to Account No. 228.1, Accumulated Provision for Property Insurance, will be sufficient, when added to the insurance recoveries, to cover all storm losses. This accounting treatment is supported by Commission Rule 25-6.0143, Section (4)(b):

> If a utility elects to use any of the above listed accumulated provision accounts, each and every loss or cost which is covered by the account shall be charged to that account and shall not be charged directly to expenses. Charges shall be made to accumulated provision accounts regardless of the balance in those accounts.

Since all storm losses will be covered in this manner, it is appropriate that all charges to other accounts be offset. Storm Fund withdrawals will first be used to offset amounts considered maintenance expense. However, when combined with insurance recoveries, all maintenance expense as well as all charges to capital accounts will be offset. The premature retirements charged to the Depreciation Reserve will be offset together with the associated net removal cost and, the Plant-in-Service account will be credited in the amount necessary to reduce the cost of the new asset to equal the cost of the replaced asset. This accounting treatment is supported by Interpretation No. 67-EG:

Question:
Under arrangements with another party, sometimes the United States Government, a utility company agrees, or is obliged, to remove, relocate, rearrange, reroute, or otherwise make changes in utility property, other than for the purpose of rendering utility service to the other party, for which the utility is reimbursed for all or a portion of the costs incurred. What is the proper accounting for such property changes and the reimbursements received from the other parties?
Answer:

The cost of plant retirements should be accounted for in accordance with the rules applicable thereto. The cost of new plant should be included in the appropriate plant accounts at actual cost of construction. The reimbursement received shall be accounted for (a) by crediting operation and maintenance expenses to the extent of actual expenses occasioned by the plant changes and (b) crediting the remainder to the reserve for depreciation, unless contractual terms definitely characterize residual or specific amounts as applicable to the cost of replacement. In the latter event, appropriate credits should be entered in the plant accounts.

FPL carries replacement value insurance coverage. Under this policy the insurance carrier first reimburses for the depreciated value of the property loss. When the property is replaced, the insurance carrier will reimburse for the replacement cost less the amount already paid for the depreciated value.

Attachment A provides an example of these accounting entries which are necessary to accurately record capital costs associated with the storm and to clear the storm account. I believe that the accounting treatment proposed appropriately recognizes the unusual circumstances involved in the restoration process and will effectively accomplish the following results: (1) damaged property will be retired and the new replacement will be recorded recognizing a 1993 vintage year; (2) the balances in the Plant-in-Service and Depreciation Reserve accounts will be restored to the pre-storm amounts; and (3) FPL's rate base will not be changed due to storm losses and the restoration effort unless the uninsured losses exceed the balance in Account No. 228.1, Accumulated Provision for Property Insurance.

It is imperative that FPL receive an indication of your concurrence with this proposed accounting treatment or your comments as soon as possible. At the present time we plan to close the storm work order to the appropriate accounts in March 1993. While some charges may be based on estimates this timing is necessary to facilitate the completion of depreciation studies the are required by the FPSC in Order No. PSC-92-1303-FOF-EI.

If you have any questions regarding this proposed accounting, please call me at (305) 552-4327 or Ed Hoffman at (305) 552-4071.

Sincerely,

K. M. Davis
Vice President and Controller

cc: Joseph D. Jenkins
William G. Walker, III

Attachment A

Example - Entries To Record Storm Related Costs and Clear Storm Account While Leaving Rate Base Unaffected

(BB) Beginning Balance before storm
(1) Record costs incurred from Storm (assume $4,520)
(2) Record insurance proceeds (assume $4,320)
(3) Transfer amount from Storm Fund to cover costs incurred in excess of insurance recovery (assume $200)
(4) Retire cost of property removed (assume $700)
(5) Record cost of removal at normal cost estimate (assume $20)
(6) Capitalize new additions at normal cost estimate (assume $2,500)
(7) Record as maintenance expense all costs incurred in excess of normal capital costs and removal costs ($4,520-$2,500-$20=$2,000)
(8) Apply Storm Fund withdrawal to offset charges to maintenance expense ($200)
(9) Apply insurance proceeds to offset removal costs ($20)
(10) Apply insurance proceeds to offset the retirement in the Depreciation Reserve ($700) and credit Plant-In-Service in an amount necessary to reduce the costs of the new asset to equal the original cost of the retired asset ($2,500-$700=$1,800)
(11) Apply insurance proceeds to offset remaining maintenance expense ($2,000-$200=$1,800)

Cash

(2) 4,320	(1) 4,520
(3) 200	
0	

Deferred Debit-Storm Costs and Recoveries (Acct. 186)

(1) 4,520	(2) 4,320
(8) 200	(3) 200
(9) 20	(5) 20
(10) 2,500	(6) 2,500
(11) 1,800	(7) 2,000
0	

Plant-In-Service (Acct. 101)

(BB) 10,000	
(6) 2,500	(4) 700
	(10) 1,800
10,000	

Depreciation Reserve (Acct 108)

	(BB) 6,000
(4) 700	(9) 20
(5) 20	(10) 700
	6,000

Maintenance Expense (a)

(7) 2,000	(8) 200
	(11) 1,800
0	

Accumulated Provision for Property Insurance

	(BB) 900
(3) 200	
	700

Storm Fund/Deferred Tax-Assets (b)

(BB) 900	
	(3) 200
700	

NOTES
(a) Charges depicted to maintenance expense account may be transacted on books through offset within the deferred debit account thereby reducing number of entries required.
(b) Combined for ease of presentation only

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In Re: Request for approval of Change in Depreciation Rates for Martin and Turkey Point Generating Site, to become effective 1-1-91, by Florida Power and Light Company.	DOCKET NO. 900 94-EI
In Re: Request for change in Depreciation Rates for Putnam and St. Johns River Power Park generating stations by Florida Power and Light Company.	DOCKET NO. 901001 EI
In Re: 1991 Depreciation Study for Florida Power and Light Company.	DOCKET NO. 910081-EI ORDER NO. PSC-93-0211-FOF-EI ISSUED: 02/10/93

The following Commissioners participated in the disposition of this matter:

J. TERRY DEASON, Chairman
THOMAS M. BEARD
LUIS J. LAUREDO

ORDER GRANTING PARTIAL WAIVER AND APPROVING ACCOUNTING TREATMENT

BY THE COMMISSION:

On November 12, 1992, this Commission entered Order No. PSC-92-1303-FOF-EI, approving depreciation and dismantlement rates for Florida Power and Light Company (FPL). Also, in that Order the Commission required FPL to file an updated comprehensive depreciation study by June 1993 with an effective date of January 1, 1993. The new study is an effort by the Commission to recognize any catastrophic effects of Hurricane Andrew on FPL's operations and plant. Subsequently, on November 30, 1992, FPL filed a request that the Commission waive the June 1993 comprehensive depreciation study deadline.

FPL argues that the June 1993 deadline is impractical and unrealistic due to 1) the current valuation of the effects of Hurricane Andrew and 2) the time and personnel it needs to prepare a comprehensive study. FPL's request provided two alternative filing schedules for the Commission's consideration.

FPL characterizes these alternative schedules as "accelerated" since a company normally has four years to file a comprehensive study and, according to FPL, the alternatives will result in studies for all functions in about two years. The first alternative offered by FPL is the filing of a transmission distribution and general study by December 1993 with an effective date of January 1, 1994; Nuclear Plants by December 1993, with an effective date of January 1, 1994; and Fossil Plants (depreciation and dismantlement) by December 1994, with an effective date of January 1, 1995. The second alternative calls for a complete comprehensive study covering all functions of plant to be filed by December 1994, with an effective date of January 1, 1995.

Our Staff suggests another alternative, a December 1993 filing date with a January 1, 1994 implementation of the depreciation study covering production, transmission, distribution and general plant. Dismantlement studies and decommissioning studies would be deferred until December 1994 with a January 1, 1995 implementation date. This would allow a comprehensive review of depreciation parameters for all categories of plant at the same time while allowing the review of extraordinary removal costs (fossil dismantlement and nuclear decommissioning) at a later time.

FPL at the agenda conference agreed with Staff's alternative and we are inclined to agree and find that its approval is in the public interest.

ACCOUNTING TREATMENT

Also in connection with the effects of Hurricane Andrew, FPL has requested approval of accounting treatment to record cost of removal and the cost of new plant at a normal or "fair" cost and to charge the remaining excess cost to maintenance expense.

FPL indicates that due to the necessity of restoring property damaged by Hurricane Andrew without delay, abnormal expenditures have been incurred. As an example, employees may have been working overtime to restore overhead lines. Under normal circumstances, no overtime pay would be incurred. Therefore, the difference between the straight-time pay and overtime pay would be considered "abnormal" and be charged to maintenance expense.

We agree with our Staff that FPL's request should be granted. We also agree that the abnormal cost charged to maintenance expense should be offset first by any insurance proceeds received. We further agree with FPL that the remaining insurance proceeds should then be applied to adjust the plant accounts so that the value of the replacement plant is equal to the gross book value of the

replaced plant prior to the damages caused by Hurricane Andrew. In addition we are requiring that FPL maintain adequate records so that a review of the appropriateness of the cost considered "normal" may be made by the Staff.

In connection with the accounting treatment, we are requiring that FPL provide a report by August 1, 1993 detailing the costs incurred and the disposition of insurance proceeds and monies obtained from FPL's storm damage fund through the period ending June 30, 1993. Thereafter, we will expect by December 31, 1993 a comprehensive report outlining both the costs described in the August 1st report and any subsequent additional costs incurred through December 1, 1993.

In consideration of the foregoing, it is

ORDERED by the Florida Public Service Commission that the request for waiver filed by Florida Power and Light Company is granted as modified in the body of this Order. It is further

ORDERED that Florida Power and Light Company's request for accounting treatment as described in the body of this Order is approved. It is further

ORDERED that Florida Power and Light Company shall file with this Commission a report by August 1, 1993 detailing the costs incurred and the disposition of insurance proceeds and monies obtained from its storm damage fund through June 30, 1993, and by December 31, 1993 another report outlining the costs described in the August report and any subsequent additional costs incurred. It is further

ORDERED that these dockets shall be closed.

By ORDER of the Florida Public Service Commission this 10th day of February, 1993.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

MRC:bmi

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Civil Procedure. The notice of appeal must be in the form specified in Rule 9.900 (a), Florida Rules of Appellate Procedure.

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P.O. Box 029100, Miami, FL 33102

July 30, 1993

Mr. Steve Tribble
Director of Records & Reporting
Florida Public Service Commission
101 East Gaines Street
Fletcher Building
Tallahassee, Florida 32399-0865

Dear Mr. Tribble,

In Order No. PSC-93-0211-FOF-EI issued in Docket Nos. 900794-EI, 901001-EI and 910081-EI dated February 10, 1993, the Commission approved, among other things, Florida Power & Light Company's (the Company) accounting treatment for Hurricane Andrew restoration costs and insurance proceeds. Also in this Order, the Commission required the Company to file a report by August 1, 1993, detailing the costs incurred and the disposition of insurance proceeds and monies obtained from the Storm Damage Fund through June 30,1993, and by December 31,1993 another report outlining the costs described in the August report and any subsequent additional costs incurred. This letter and Attachment 1 are in response to the Commission's request for the August report.

The accounting treatment approved by the Commission allows the Company to record the cost of removal and the cost of new plant at a normal or "fair" cost and to charge the remaining (abnormal) cost to maintenance expense. The abnormal cost charged to maintenance expense is to be offset first by any insurance proceeds received and the remaining insurance proceeds are to be applied to adjust the plant accounts so that the value of the replacement plant is equal to the gross book value of the replaced plant prior to the damages caused by Hurricane Andrew. This accounting treatment reflects the economics of the replacement cost insurance coverage and will result in no adverse effect on the Company's rate base or depreciation expense.

This report is preliminary from the standpoint that all costs for damages have not yet been incurred or recognized and additional insurance proceeds will be received. Although a significant amount of work remains to be completed, the major costs that have not yet been quantified relate to the long term potential damage to underground lines in the storm surge area and the cost to repair or replace inventory at the Turkey Point Plant. Through June 30, 1993 we have identified costs totaling $358.5 million related to damages caused by Hurricane Andrew. Insurance negotiations commenced immediately after the storm and are still proceeding. We have received a total of $250 million in advances from our insurers, $220 million under the policy covering non-nuclear property and $30 million for the nuclear property coverage. In addition, $21 million has been removed from the Storm Damage Fund which represents the deductible amounts related to the insurance policies. We are unable to predict when all hurricane related work will be completed or when a final insurance settlement will be obtained. Our estimate of the total damages resulting from Hurricane Andrew has not changed. We continue to estimate damage to the Transmission and Distribution system at $270 million and total damage at $415 million.

The costs associated with damages caused by Hurricane Andrew were captured in a manner that would facilitate insurance recovery. FPL utilized its work order system to capture the majority of these costs. Therefore, in Attachment 1 the costs have been identified in a manner consistent with the way these costs were recorded and processed on the Company's books and records. Some costs have not been identified because they are not covered under the insurance policies in a direct fashion and/or are difficult to quantify (e.g., lost revenues and overtime required by employees to "catch-up" on their normal job requirements after their storm assignment ended). Page 1 of Attachment 1 shows the costs incurred by source of the charge. Page 2 provides the amount of these costs that have been charged to plant accounts and the portion that is non-capital (considered to be maintenance). Page 3 further explains the amounts charged to Plant-in-Service and the Accumulated Provision for Depreciation. Page 4 lists the insurance proceeds received and the amount withdrawn from the Storm Damage Fund and discusses the disposition of these funds.

If you have any questions regarding this report please direct them to me at (305) 552-4332.

Sincerely,

Anne M. Grealy DTB

Anne M. Grealy
Director Regulatory Affairs

attachment

cc: Mary Bane
K. M. Davis
Timothy Devlin
Beth Salak
W. G. Walker, III

FLORIDA POWER & LIGHT COMPANY
HURRICANE ANDREW DAMAGE AND RESTORATION COSTS
SUMMARY OF CHARGES BY SOURCE
Amounts Recorded At June 30, 1993

	(1) Total Costs	(2) Payroll	(3) Vehicle	(4) Materials & Supplies	(5) Misc.
Repair of Facilities (a)					
Production	$85,646,189	$10,097,108	$352,764	$29,968,252	$45,228,065
Substation	8,396,188	1,663,798	232,479	5,113,703	1,386,208
Transmission Lines	24,658,535	4,359,932	396,933	4,869,579	15,032,091
Distribution	221,801,463	56,992,040	5,424,039	33,911,559	125,473,825
General Plant	4,944,351	887,716	49,963	23,981	3,982,691
Other Storm Related Costs					
Support Costs (b)	9,749,550	2,500,046	87,571	20,680	7,141,253
Employee Assistance (c)	1,297,992		1,676	38,287	1,258,029
Provision for Uncollectible Accounts (d)	2,000,000				2,000,000
Total	$358,494,268	$76,500,640	$6,545,425	$73,946,041	$201,502,162
Insurance Recoveries (to date)	(250,000,000)				
Storm Fund Withdrawal	(21,000,000)				
Total Net of Insurance	$87,494,268				

(a) Repair of Facilities - Includes costs for personnel assigned to plant sites, service centers, area headquarters, command and control centers, and staging areas and for activities such as storm preparation, damage assessment and direct repairs. Also includes costs of temporary housing and related subsistence costs for construction crews and support personnel, and costs incurred to operate centers for damage assessment, repairs and control.

(b) Support Costs- Includes costs incurred as a result of the storm but not directly in the restoration of service. Includes costs for activities such as media relations, public service advertising, procurement and other storm related activities performed by locations other than those engaged in the direct repair and restoration of service.

(c) Employee Assistance- Non payroll costs incurred to assist FPL employees who were significantly affected by the storm to allow them to return to work and to focus on those activities necessary to the restoration of service to our customers.

(d) Provision for Uncollectible Accounts- Estimated accrual for write-off of uncollectible customer accounts receivable resulting from the inability to locate customers and the impact on economic conditions following the storm.

Columns:

1 Costs recorded as of 06/30/93. Does not include payroll loadings for pension & welfare, taxes and insurance which are recoverable as a fixed percentage under the provisions of the insurance policies.
2 FPL direct labor - regular and overtime pay
3 FPL vehicle use charges
4 FPL inventory - net issues
5 Cash and Journal voucher sources. Includes charges such as payments to contractors and foreign (other) utilities , food and lodging, transportation, equipment and vehicle rental.

FLORIDA POWER & LIGHT COMPANY
HURRICANE ANDREW DAMAGE AND RESTORATION COSTS
SUMMARY OF AMOUNTS RECORDED TO CAPITAL & NON CAPITAL ACCOUNTS
Amounts Recorded At June 30, 1993

	(1)	(2)	(3)	(4)
	Total Costs	Net Plant In Service	CWIP	Non-Capital
Repair of Facilities				
Production	$85,646,189	$15,741,406	$2,784,516	$67,120,267
Substation	8,396,188	1,006,251	18,076	7,371,861
Transmission	24,658,535	9,900,480	2,433,340	12,324,715
Distribution	221,801,463	46,086,785		175,714,678
General Plant	4,944,351	1,397,267	610,937	2,936,147
Other Storm Related Costs				
Support Costs	9,749,550			9,749,550
Employee Assistance	1,297,992			1,297,992
Provision for Uncollectible Accounts	2,000,000			2,000,000
Sub-total	$358,494,268	$74,132,189	$5,846,869	$278,515,210
Insurance Recoveries	(250,000,000)	(73,010,948)	(8,759)	(176,980,293)
Storm Fund Withdrawals	(21,000,000)			(21,000,000)
Total Net of Insurance	$87,494,268	$1,121,241	$5,838,110	$80,534,917

Columns:

(1) Sum of columns 2, 3 & 4. Amounts and classifications are preliminary

(2) Amounts classified as Plant in Service (account 101/106) and Accumulated Provision for Depreciation (account 108). See Attachment 1 page 3 for additional detail.

(3) Construction Work In Progress net of contractor retentions. Amount shown as insurance recovery is preliminary. Additional amounts will be recorded as jobs are transferred to plant in service status.

(4) Amount recorded in Deferred Debit Account 186 - includes normal and abnormal maintenance costs and amounts pending transfer to capital accounts.

FLORIDA POWER & LIGHT COMPANY
HURRICANE ANDREW DAMAGE AND RESTORATION COSTS
SUMMARY OF AMOUNTS TRANSFERRED TO PLANT IN SERVICE
AND ACCUMULATED PROVISION FOR DEPRECIATION
Amounts Recorded at June 30, 1993

(a) PLANT IN SERVICE

	(1) Account 101/106 Additions	(2) Retire-ments	(3) Insurance Recoveries	(4) Net Account 101/106 (1)+(2)+(3)
Production	$14,108,953	($4,234,953)	($10,496,302)	($622,302)
Substation	929,631	(351,036)	(542,458)	36,137
Transmission Lines	7,956,175	(2,689,484)	(5,406,524)	(139,833)
Distribution	39,939,420	(14,445,690)	(25,002,258)	491,472
General Plant	1,297,259	(469,713)	(834,994)	(7,448)
Total	$64,231,438	($22,190,876)	($42,282,536)	($241,974)

(b) ACCUMULATED PROVISION FOR DEPRECIATION

	(1) Removal Costs	(2) Salvage	(3) Retire-ments	(4) Insurance Recoveries	(5) Net Account 108 (4)+(5)
Production	$1,671,449	($38,996)	$4,234,953	($4,769,619)	$1,097,787
Substation	76,620		351,036	(438,293)	(10,637)
Transmission Lines	1,944,433	(128)	2,689,484	(4,413,631)	220,158
Distribution	6,334,042	(186,677)	14,445,690	(20,537,148)	55,907
General Plant	100,008		469,713	(569,721)	0
Total	$10,126,552	($225,801)	$22,190,876	($30,728,412)	$1,363,215

(a)+(b) NET PLANT IN SERVICE

	(1) Net Account 101/106	(2) Net Account 108	(3) Net (1)+(2)
Production	($622,302)	$1,097,787	$475,485
Substation	36,137	(10,637)	25,500
Transmission Lines	(139,833)	220,158	80,325
Distribution	491,472	55,907	547,379
General Plant	(7,448)	0	(7,448)
Total	($241,974)	$1,363,215	$1,121,241

Note:
In accordance with the accounting treatment approved by the Commission, capital additions and removal are based on "normal" non-storm costs. Insurance proceeds are applied to offset removal, salvage and retirements recorded in the Accumulated Provision for Depreciation accounts. In addition, insurance proceeds are applied to reduce the Plant-in-Service account in the amount necessary to reduce the cost of the new asset to equal the cost of the replaced asset. The balances, net of insurance recoveries, recorded in Plant-in-Service and Accumulated Provision for Depreciation as of June 30, 1993, are primarily the result of timing differences in processing and recording the individual components of additions, removal, salvage, retirements and insurance proceeds and will be subsequently adjusted so that the balance in Plant-in-Service and Accumulated Provision for Depreciation accounts are restored to the amounts that existed prior to the storm.

FLORIDA POWER & LIGHT COMPANY
HURRICANE ANDREW INSURANCE RECOVERIES
AND STORM FUND WITHDRAWALS
Amounts Recorded at June 30, 1993

$ MILLION

Date	Arkwrite Mutual Insurance Company	Nuclear Mutual Limited	Storm Damage Fund Withdrawals	Total Recoveries
Sep-92	$20	$10	$21	$51
Oct-92	80	10		90
Nov-92	58			58
Dec-92		10		10
Jan-93	40			40
May-93	22			22
Total to Date	$220	$30	$21	$271

Note:
Insurance advances and Storm Damage Fund withdrawals when received were used to off-set (credit) the storm related cost recorded in Miscellaneous Deferred Debit - Account 186. Beginning in March 1993 a portion of the insurance proceeds were transferred to Plant in Service and Accumulated Provision for Depreciation accounts to off-set the corresponding amounts recorded as additions, retirements, removal and salvage. In accordance with the accounting treatment approved by the Commission, insurance proceeds are credited to the Accumulated Provision for Depreciation for an amount equal to the cost of removal less salvage, plus the value of the asset retired. Insurance proceeds are also credited to Plant-In-Service in an amount necessary to reduce the cost of the new asset to the original cost of the asset retired. As additional amounts are placed in service and removal, salvage and retirements recorded, additional insurance proceeds will be transferred from Account 186 and credited to the appropriate capital accounts.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

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 & LIGHT COMPANY.	DOCKET NO. 930405-EI ORDER NO. PSC-95-0264-FOF-EI ISSUED: February 27, 1995

The following Commissioners participated in the disposition of this matter:

SUSAN F. CLARK, Chairman
J. TERRY DEASON
JOE GARCIA
JULIA L. JOHNSON
DIANE K. KIESLING

NOTICE OF PROPOSED AGENCY ACTION
ORDER APPROVING STORM DAMAGE STUDY AND
ADJUSTMENTS TO SELF INSURANCE MECHANISM

BY THE COMMISSION:

NOTICE IS HE REBY GIVEN by the Florida Public Service Commission that the action discussed herein is preliminary in nature and will become final unless a person whose interests are substantially affected files a petition for a formal proceeding, pursuant to Rule 25-22.029, Florida Administrative Code.

On April 19, 1993, Florida Power & Light Company (FPL) filed its petition to implement a self -insurance mechanism for storm damage to its transmission and distribution (T&D) system and to resume and increase its annual c ontributions to its Storm and Property Insurance Reserve Fund (Storm Fund). Because FPL's current T&D insurance expired on May 31, 1993, FPL requested consideration of its request on an emergency basis. Pursuant to notice, a hearing on FPL's petition was held on May 17, 1993.

In Order No. PSC -93-0918-FOF-EI, issued June 17, 1993, we found that FPL should implement a self -insurance approach. In addition, we found that FPL should have the discretion to establish a line of credit for storm damage liquidity; however, we found that the amount of the line of credit should not be subject

to pre -approval by the Commission nor should the amounts contributed to the Storm Fund be reduced by the commitment fees for any dedicated lines of credit. We also required FPL to submit a study detailing the appropriate amount that should be annually accrued to the reserve and the costs it intends to charge to the Storm Fund. Additionally, the study was to include information concerning the treatment of all Hurricane Andrew related T&D damages under existing policy. Until the appropriate amount was determined, an annual accrual of $7.1 million, net-of-tax, to the Storm Fund was set with the understanding that the amount beginning June 1, 1993, may be trued -up depending upon our findings resulting from the submitted study.

FPL submitted its study October 1, 1993. Over the past year, there have been several meetings regarding the study and related issues. These efforts have resulted in an agreement between the parties and staff on the appropriate level of annual contribution to the Storm Fund.

INCREASE IN STORM DAMAGE ACCRUAL

FPL's analysis of the annual accrual amount is based on the results of a statistical model which estimates the impact to the balance of the Stor m Fund due to various accrual amounts and special customer assessments. For modeling purposes, a special customer assessment was defined as the amount required to return the Storm Fund to the target level over a five year period. The Storm Fund target wa s $75,000,000 which was the approximate fund balance at the time of the study analysis. The amount of storm damage in a given year was indexed to an estimate of the long term average annual damage level of $20,300,000 but allowed to fluctuate above or below it.

The model was then used to simulate the Storm Fund balance over 33 years under four policies. The analysis of these policies provides insight to various self insurance approaches. FPL recommended Policy III while staff believes the study support s a compromise between Policies II and III.

Policy I sets the annual accrual equal to the long term annual average, assumes no special assessments and future losses exceeding the annual accrual are drawn from the Storm Fund. FPL's analysis suggests this policy is the most volatile with relatively high potential for large positive or negative balances. However, negative fund balances will result if the estimate is lower than the cumulative effect of actual damages. For example, if this policy were in pla ce at the time of Hurricane Andrew, the $270,000,000 in T&D damages

would have depleted the Storm Fund and FPL would have petitioned for relief. Therefore, this policy is not appropriate because it is not sufficiently robust to address the risks to FPL and its customers. Any error in estimating annual storm damage level and frequency of storms would tend to have a dramatic impact on the Storm Fund balance. A high degree of confidence in the accuracy of weather forecasting is required to justify a substan tial increase in the annual accrual amount. Staff believes this degree of precision in weather forecasting does not exist. Absent a rate case setting, implementing this policy also creates equity issues.

Policy II sets the annual accrual equal to the long term annual average and provides for special assessments to maintain the Storm Fund. FPL's analysis suggests this policy is the most likely to cause the Storm Fund to increase over time. Any errors in under estimating annual storm losses would be addressed through special assessments and, therefore, the Storm Fund is expected to remain solvent. However, this policy only addresses relief for FPL and suffers in similar areas as Policy I with regard to weather forecasting and inter-generational equity issues.

Policy III sets the annual accrual to the current amount of $7,100,000 and provides for special assessments to maintain the Storm Fund. FPL's analysis suggests this policy is the most likely to have an equal probability in having a positive Storm Fund balance as a negative fund balance in any given year. This means that the Storm Fund balance is not expected to increase or decrease but remain relatively constant over time. The difference between the accrual amount and cumulative storm losses a re addressed through special assessments. However, this policy tends to place the burden of self insurance on FPL's customers through special assessments. This is because the accrual amount is only 35 percent of FPL's estimated long term average of annual storm damages and eventually special assessments are expected to exceed the accrual amount. Staff believes that both FPL and its customers would be better insured if the accrual amount were increased such that the Storm Fund is likely to grow which in t urn would decrease dependence on special assessments to address unpredictable weather events.

Policy IV assumes no annual accrual and provides for special assessments to maintain the fund. Staff agrees that this policy is a "pay -as-you-go" policy which r elies on the Commission approving FPL's petitions for relief and spreading the costs over FPL's large customer base. This policy is not a viable alternative but helps to understand the interactions

between an accrual amount, special assessments and the fu nd balance. As stated in the study, Attachment 3, page 6,

"...This policy illustrates that the amount chosen for annual accrual can be relatively arbitrary so long as it is within a range low enough so as not to result in unbounded growth in expected future Storm Reserve balances, and if it is combined with a mechanism to address insolvency."

Staff's review of FPL's study indicates that an increase above the current $7,100,000 annual accrual is needed because the fund should be expected to grow due to the unpredictable nature of weather and to reduce dependence on a relief mechanism such as a special customer assessment. On page 6 of the study, FPL indicates that at least $9,000,000 in annual accrual is required to achieve some fund growth if there are any special assessments. Staff's concerns were addressed in various meetings and discussions on this matter and related issues with FPL, OPC and FIPUG. As a result of this dialogue, FPL sent to staff a proposed agreement (Attachment A) on December 20, 1994, to increase the storm damage accrual to $10,100,000 annually effective January 1, 1994. We find that the proposed agreement should be approved; however, the accrual amount and solvency of the Storm Fund should be reviewed and appropriately adjusted subject to Modified Minimum Filing Requirements or other rate proceeding.

STORM DAMAGE STUDY

FPL's study provided sufficient analysis to indicate the appropriate annual amount that should be contributed to the storm damage reserve fund at this time.

In addition, the study addressed the issues raised in the order concerning the types of expenses that would be charged to the reserve. However, we have the authority to review any expenses charged to the reserve for reasonableness and prudence. FPL stated that it would use the actual restoration cost approach for determining the appropriate amounts to be charged to the reserve. This methodology is consistent with the manner in which replacement cost insurance works.

In accounting for the restorati on and replacement costs to plant, the gross original cost of the replaced plant should be retired by a credit to the plant accounts and a debit to the depreciation reserve. Then, a credit would be made to the plant

accounts so that the replacement gross plant would be reduced by the available balance of the storm reserve until it is equal to the value of the plant it replaced. In addition, the depreciation reserve would be credited with an amount equal to the gross cost of the replaced plant. This would restore the plant accounts and depreciation reserve to their original values prior to the damage caused by the storm. In the event that the storm reserve is not sufficient to cover the credits to the plant accounts and the depreciation reserve, the utili ty would need to seek recovery through a petition to this Commission.

FPL also provided a summary of the treatment of the costs to restore its facilities damaged by Hurricane Andrew. As noted on page 7 of the study, FPL had not submitted its full claim at the time that the study was filed.

We are considering the appropriateness of opening a rulemaking proceeding to establish uniform guidelines for determining when the storm damage reserve should be charged and what costs should be charged to it.

TROPICAL STORM GORDON COSTS

By letter dated December 30, 1994 (Attachment B), FPL requested that it be allowed to expense, in 1994, approximately $4.5 million of costs to repair storm damage and restore service due to Tropical Storm Gordon. Rule 25 -6.0143(1)(b), F.A.C., requires that charges be made to the Accumulated Provision for Property Insurance (Storm Fund) account for all occurrences in accordance with the schedule of risks to be covered which are not covered by insurance. FPL is effectively requesting a waiver of this rule in order to expense the storm damage costs related to Tropical Storm Gordon.

We have expressed our concern that the accrual amount for storm damage needs to be increased above its current level in order for the Storm Fun d to grow and thereby reduce FPL's dependence on a relief mechanism such as a special customer assessment. If FPL's request is approved, the Storm Fund will be $4.5 million greater than it would be otherwise.

Based on the November 30, 1994 earnings surveillance report, FPL was earning 12.25% return on equity (ROE). This is within the company's authorized ROE range of 11.0% to 13.0%. The reported earned ROE of 12.25% includes the expense of Tropical Storm Gordon. Expensing the costs of Tropical Storm Gordon resulted in a

reduction in reported earnings of approximately .07% ROE. We do not believe this significantly impacts FPL's earnings.

Approval of FPL's request will have no negative impact on its customers. Since FPL does not appear to be over earning during 1994, no refund for 1994 is likely. Approval of FPL's request may have a beneficial impact on its customers in the future. Expensing the costs of Tropical Storm Gordon results in a greater Storm Fund balance that may avoid or reduce the need for a special assessment in the case of a major storm.

FPL's request to expense the $4.5 million cost of Tropical Storm Gordon in 1994 it therefore approved.

Based on the foregoing, it is

ORDERED that the request of Florida Power & Light Company to increase its annual storm damage accrual to $10,100,000, effective January 1, 1994, is hereby granted. The storm damage fund shall continue to be funded on a net-of-tax basis. It is further

ORDERED that the storm damage study submitted by Florida Power & Light Company is hereby found to be adequate. It is further

ORDERED that the request of Florida Power & Light Company to expense the $4.5 million cost of Tropical Storm Gordon rather than withdrawing it from the storm damage fund is hereby granted. It is further

ORDERED that this Order shall become final and effective and this docket shall be closed unless an appropriate petition for formal proceedings is received by the Division of Records and Reporting, 101 East Gaines Street, Tallahassee, Florida 32399-0870, by the close of business on the date indicated in the Notice of Further Proceedings or Judicial Review.

By ORDER of the Florida Public Service Commission, this 27th day of February, 1995.

/s/ Blanca S. Bayó

BLANCA S. BAYÓ, Director
Division of Records and Reporting

This is a facsimile copy. A signed copy of the order may be obtained by calling 1-904-488-8371.

(S E A L)

MAP

DISSENT

Commissioner Kiesling dissents on the issue of Tropical Storm Gordon Costs. Commissioner Kiesling would deny Florida Power & Light Company's request to expense the $4.5 million in storm costs and would order the costs withdrawn from storm damage reserves.

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

The action proposed herein is preliminary in nature and will not become effective or final, except as provided by Rule 25-22.029, Florida Administrative Code. Any person whose substantial interests are affected by the action proposed by this order may file a petition for a formal proceeding, as provided by Rule 25 -22.029(4), Florida Administrative Code, in the form

provided by Rule 25-22.036(7)(a) and (f), Florida Administrative Code. This petition must be received by the Director, Division of Records and Reporting, 101 East Gaines Street, Tallahassee, Florida 32399-0870, by the close of business on March 20, 1995.

In the absence of such a petition, this order shall become effective on the day subsequent to the above date as provided by Rule 25-22.029(6), Florida Administrative Code.

Any objection or protest filed in this docket before the issuance date of this order is considered abandoned unless it satisfies the foregoing conditions and is renewed within the specified protest period.

If this order becomes final and effective on the date described above, any party substantially affected may request judicial review by the Florida Supreme Court in the case of an electric, gas or telephone utility or by the First District Court of Appeal in the case of a water or wastewater utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days of the effective date of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

Q.
What was FPL's lost revenue during the hurricane caused outages during 2004? (Please detail the methodology used to make this calculation.)

A.
The total estimated losses in MWH delivered and Base Revenues due to the three hurricanes that impacted FPL's service territory are shown on the table below:

IMPACT OF HURRICANES CHARLEY, FRANCES AND JEANNE

HURRICANE	ESTIMATED/ACTUAL MWH LOSS	BASE REVENUE LOSS
1. CHARLEY	153,419	$5,123,100
2. FRANCES	663,275	$24,461,828
3. JEANNE	255,625	$8,653,101
TOTALS	1,072,319	$38,238,029

Methodology for Estimating Total Losses:

I. The methodology for estimating outage losses due to these hurricanes was as follows:

1. Each day the FPL's Power Systems Business Unit reported the number of customers without service.

2. FPL estimated the probable average Net Energy for Load (NEL) per customer that would have been consumed by FPL's customers absent these three hurricanes based on actual customer use during the four weeks immediately preceding the arrival of Hurricane Charley. More specifically, the estimated average NEL per customer on Mondays was the average of actual usage per customer during the four Mondays immediately preceding Hurricane Charley. Similarly, the estimated average NEL per customer on Tuesdays was the average of actual usage per customer during the four Tuesdays immediately preceding Hurricane Charley, and so on for each day of the week.

3. Because the effects of Hurricane Charley were largely limited to the Western and Northern geographic divisions of FPL's service territory, the average NEL per customer used in estimating Hurricane Charley's losses was based on actual NEL per customer usage in only these two geographic divisions during the four weeks immediately preceding Hurricane Charley. On the other hand, because the effects of Hurricanes Frances and Jeanne were felt throughout very broad areas of FPL's service territory, the average NEL per customer used in estimating MWH and base revenue losses due to Hurricanes Frances and Jeanne was based on actual NEL usage in FPL's entire service territory during the four weeks immediately preceding Hurricane Charley.

4. The number of customers reported without electrical service each day was multiplied by the estimated average NEL per customer for that day to obtain the estimated NEL loss for that day. This calculation was performed for each day in which FPL's Power Systems Business Unit reported customer outages due to Hurricanes Charley, Frances and Jeanne.

5. The daily estimated NEL losses related to each hurricane were added together and multiplied by an average rate of $36/MWH to obtain the estimated loss in base revenues caused by each of the hurricanes.

II. Methodology for estimating weather related losses due to these hurricanes for customers that did not lose electrical service was as follows:

1. Each of the three hurricanes made landfall and moved through and out of FPL's service territory at different paces. Hurricane Charley was compact and fast moving. Hurricane Frances was very slow moving and sat over FPL's service territory for quite some time. Hurricane Jeanne's path was similar to Frances although it moved faster. As such, Frances and to a much lesser extent Jeanne, had an impact on revenues from customers that did not lose power. This was the result of clouds and rain associated from those weather systems that reduced the average temperatures below what we would have expected ("normal"). The impact for Frances was approximately $2.5 million, $50 thousand for Jeanne and no impact for Charley.

Additionally, we reduced the amount of MWH lost by our average line loss of 7%. This resulted in lowering the amount of revenues lost by approximately $2.9 million.

The combination of revenues lost from customers without power and customers that had reduced power consumption due to below average weather, offset by average line losses equal base revenue losses in the table above.