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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

REBUTTAL TESTIMONY OF H. A. GOWER

DOCKET NO. 900796-EI

Q. Please state your name, business address and occupation.

A. My name is Hugh Gower, and I am a partner in Arthur Andersen & Co., a firm of independent public accountants, at 133 Peachtree Street N.E., Atlanta, Georgia 30303.

Q. Are you the same Hugh Gower who submitted direct testimony in this docket on September 28, 1990.

A. Yes, I am.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my rebuttal testimony is to explain why the proposal made by Mr. Robert Scheffel Wright on behalf of the Office of Public Counsel ("OPC") to limit the revenue recovery which will be associated with Plant Scherer Unit No. 4 (Unit No. 4) represents inappropriate regulatory policy which would not be in the best interest of ratepayers.

Q. Please state your understanding of Mr. Wright's proposal.

A. As I understand his testimony, Mr. Wright proposes that the Commission limit FPL's recovery of the capital it will invest in the unit and associated transmission facilities to the amount of the estimated initial investment and limit the return on the capital invested to current estimated capital costs. Any actual costs in excess of these current estimates would be absorbed by FPL's investors.

Q. Do you agree with Mr. Wright's proposed limitations on FPL's recovery of the Scherer Unit No. 4 capital costs?

A. No, there are two major flaws in Mr. Wright's proposal which make it an inappropriate regulatory policy not in the best interests of FPL's customers. These reasons are:

(1) Such a limitation would create a level of financial risk which is totally inconsistent with cost-based rate regulation, the cost of which would render the transaction unacceptable, and

(2) Such a limitation would create a strong bias against long-run decisions necessary to meet customers' needs at the lowest cost.

Q. Why would such a limitation be inconsistent with cost-based regulation?

A. Under cost-based rate regulation, it is widely acknowledged that utilities will have an opportunity to recover actual legitimate costs of their capital investments and operating expenses. In return, utilities' investors accept lower returns on their capital than would be required for competitive enterprises due, at least in part, to the consequent reduced risk. Under this arrangement, utilities' customers bear a large part of the risk of cost increases resulting from a variety of causes, but in return benefit from lower current prices for the service they receive. This benefit is significant because of the capital intensity of utilities and the long period of years for which investments in plant facilities provide service. Mr. Wright's proposed limitation would be a significant departure from this arrangement which provides great mutual benefit to both customers and investors.

Q. How would Mr. Wright's proposed limitation on capital cost recovery change the present arrangement?

A. Mr. Wright's proposed limitation on capital cost recovery would be analogous to requiring FPL to enter into a long-term firm fixed price contract which would be considerably more risky than cost-based regulation.

Additional risks would arise from the need to forecast for thirty years or more any additional capital investments in the unit to comply with now unforeseeable regulation or to improve or maintain the plant's performance. Likewise, it would be necessary to forecast long term capital cost rates for the same period of time.

Even the boldest forecaster-investor would likely insist upon a risk premium far beyond that inherent in the 14.5% equity capital cost rate used for planning purposes currently. Absent a sufficient risk premium, the transaction subject to Mr. Wright's proposed limitations would be unacceptable to a prudent investor; with such a risk premium, the cost of service would be unacceptable to customers.

Q. How would Mr. Wright's proposal create a bias against long-run decisions necessary to meet customer needs at the lowest cost?

A. Implementation of Mr. Wright's proposal would encourage utilities to avoid long-run decisions by sending the message that they will be penalized for changes in planning estimates--even those which are beyond their control. Obviously, the shorter the planning horizons, the lower the risk of error.

Q. Shouldn't the Commission hold FPL to its estimate of revenue requirements, since estimated revenue requirements were used as a component in selecting the best alternative?

A. No. Forecast assumptions and estimates are subject to change in any of the capacity scenarios considered by FPL. As long as investment decisions are based on reasonable and prudent cost comparisons, management should not be penalized for unpredictable changes in assumptions and estimates. By approving the acquisition, the Commission is indicating to management that its decision-making process is both reasonable and prudent; to disallow unforeseen prudently incurred costs would indicate to management that it is futile to make long-run decisions where assumptions are subject to change. Instead, management would focus on short-run decisions where variables are subject to little or no change. These short-run decisions can result in an outcome which is opposite to the interest of both the customer and the utility investor.

Q. How should the Commission assure that the best alternatives are selected?

A. The Commission, through oversight, should ensure that adequate procedures and systems are in place for management to make reasonable and prudent investment decisions. If additional costs are incurred, the same rule applies. If the Commission states that additional costs are to be disallowed rate treatment, regardless of the reasonableness or prudence of the cost, utility management would be encouraged to opt for something other than the least cost alternative.

Q. Are there any other flaws in Mr. Wright's proposal?

A. Mr. Wright's proposal does not address the non-quantified benefits which were considered in FPL's selection of the purchase of Unit No. 4. FPL's investment decision was based on a consideration of overall benefits--quantified and non-quantified. The present value of revenue requirements may vary with actual results; however, a consideration of all benefits may still indicate that the purchase of Unit No. 4 is the best alternative.

Q. Please summarize your position with respect to Mr. Wright's proposal.

A. Mr. Wright's proposal should be rejected by the Commission because it would create financial risks which are undesirable, bias utility planning decisions against long run decisions and not serve the interests of FPL's customers or investors.

Q. Does this conclude your testimony?

A. Yes.