BEFORE THE
FLORIDA SERVICE PUBLIC COMMISSION

In the Matter of : DOCKET NO. 950001-EI

Fuel and Purchased Power Cost Recovery Clause with Generation Performance Incentive Factor

AFTERNOON SESSION

VOLUME 3

Pages 310 through 438

PROCEEDINGS: HEARING

BEFORE: COMMISSIONER J. TERRY DEASON
COMMISSIONER JULIA L. JOHNSON
COMMISSIONER DIANE K. KIESLING

DATE: Wednesday, March 8, 1995

TIME: Commenced at 9:30 a.m.

PLACE: Fletcher Building
FPSC Hearing Room 106
101 East Gaines Street
Tallahassee, Florida

REPORTED BY: JOY KELLY, CSR, RPR
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APPEARANCES:

(As heretofore noted.)

I N D E X

WITNESSES - VOLUME 3

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P R O C E E D I N G S

(Hearing reconvened at 1:05 p.m.)

(Transcript continues in sequence from Volume 2.)

COMMISSIONER DEASON: Call the hearing back to order. Mr. Kaufmann, I believe you were inquiring.

MR. KAUFMANN: I was, but we need a witness, Your Honor.

COMMISSIONER DEASON: I guess it would help, wouldn't it? Maybe, can you do answers and questions? (Laughter)

You would be surprised, we have a lot of attorneys around here who tried to answer questions within their questions.

MR. KAUFMANN: I will if you let me. (Laughter)

COMMISSIONER DEASON: We try not to do that, though.

Mr. Kaufmann?

RENE SILVA

resumed the stand as a witness on behalf of Florida Power and Light Company and, having been previously sworn, testified as follows:

CONTINUED CROSS EXAMINATION

BY MR. KAUFMANN:

Q Good afternoon, Mr. Silva. I have handed out and you should have in front of you now what I would like to be marked Exhibit 43 for identification, which is an article regarding natural gas prices from the February 8, 1995, Wall Street Journal. Do you have that in front of you now?

(Exhibit No. 43 marked for identification.)

A Yes.

Q Did you in the last minutes have any chance to read that?

A I glanced at it, yes.

Q Would you mind reading for us the first and fourth paragraphs of that article?

A "Natural gas futures prices suffered their biggest daily decline in almost two months amid expectations the chill that settled over the northeast last week might be short-lived.

"Analysts said natural gas inventories are running at levels about 25% higher than last year despite the cold snap of last week. An unusually warm winter has caused prices for both natural gas and heating oil to remain soft through most of the heating season."

Q Thank you.

Mr. Silva, is it correct to say that since May of 1994, your natural gas costs have been tied to the market price?

A Yes.

Q Is it also correct to say that FP&L purchases 40% of its natural gas for the period beginning March 1995 on the spot market as compared to only 10% prior to February 1995?

A Yes.

MR. KAUFMANN: I have no further questions at this time.

COMMISSIONER DEASON: Mr. Howe?

CROSS EXAMINATION

BY MR. HOWE:

Q Hello, Mr. Silva.

Mr. Silva, over what time period were modifications made to the eight generating units on Florida Power and Light's system?

A The modifications began in early 1994 and they were completed at the end of -- by the end of February of this year, so about a year.

Q Did Florida Power and Light include any of these costs of plant modifications in its fuel adjustment projections in any of the previous fuel adjustment dockets?

A No.

Q Why not?

A We were trying to, first of all, determine whether it would be appropriate to recover those costs through the environmental clause, and also we were trying to get a better estimate near the time of completion so that we could present to the Commission a good estimate of what the total costs would be. And we had the schedule for these modifications through the year 1994, so we were waiting to factor it at this time.

Q You mentioned the environmental clause. Do you believe that these expenditures, these plant modifications that you are requesting -- the costs that you are requesting to recover through the fuel clause, that Florida Power and Light could have alternatively requested recovery through the environmental clause?

A We examined that possibility and we believe that it could have been but that it was a better fit under the fuel clause because the central focus of the modifications was to reduce fuel costs.

Q The costs that Florida Power and Light incurred for the plant modifications, those were essentially to reduce emissions, were they not?

A They were to reduce emissions, yes.

Q Was Florida Power and Light required by any regulatory agency or governmental body to reduce the sulfur content of its fuel oil -- I'm sorry, to increase the sulfur content of its fuel oil so that modifications would have to be made to its emission control systems?

A No.

Q Did Florida Power and Light then essentially elect voluntarily to burn a higher sulfur fuel and that the cost of the emissions modifications were just necessitated by that voluntary decision?

A That's correct. And the decision was based in order to reduce fuel costs for the customers.

Q Mr. Silva, can you give an example of a voluntary plant modification that Florida Power and Light has made or might make that wouldn't reduce fuel costs? (Pause)

A I believe that there are certain -- I don't know if you would call them modifications. But, for example, the installation of the CEMs, the monitoring devices that are required by environmental restrictions or by law, have nothing to do with reducing fuel costs.

We are making plant modifications and installing new equipment in order to comply with the law.

Q My question, though, went to voluntary modifications, those that Florida Power and Light is not compelled to install because of governmental edict.

A I understand. I missed that part of your question.

I can't think of any at this point. I know that there is ongoing work in upgrading equipment at our plants; but I haven't focussed on which ones they are making unless they have some relation to fuel, because that's what I focus on.

Q Virtually any voluntary modification to a generating unit would be to either keep it on line, which would -- well, first, for example, would you make modifications if necessary to keep a generating unit on line?

A Well, certainly you could do that to lengthen the life of a plant. You could also do it if an equipment modification might reduce your operating costs, nonfuel operating costs. Those would be types that would not, in my opinion, flow through the fuel clause.

Q They wouldn't flow through the fuel clause but you wouldn't make those modifications, would you -- for example, you wouldn't make modifications to extend the life of a plant if the system would operate more efficiently with a lower net fuel cost with the plant off line, would you?

A I think you might do it if you could avoid a cost that is not a fuel cost, i.e., a capital cost or an O&M cost, even though it doesn't gain you anything in terms of fuel.

Q The modifications that were made to the eight generating units that comprise the approximately $2.8 million that you are requesting to recover through the fuel clause, how much of that $2.8 million was for capital improvements?

A What do you mean by "capital improvement"?

Q Maybe I should ask you. In your previous answer you referred to O&M costs and capital costs. Would you please define capital costs, and then we'll see if any of these modifications fit within your definition.

A Well, absent the fuel clause and our ability to recover these costs through the fuel clause, I would anticipate that the modifications would be capitalized. But they were not done either to extend life or to reduce O&M, they were simply made in order to enable us to burn a cheaper fuel.

So I would say that they would have been capitalized except in this instance we are proposing that they be recovered through the fuel clause. But they are not capital additions or modifications that we would have done absent the benefit of fuel clause savings.

Q Given that the modifications were completed, I believe you said, in February of this year?

A Yes.

Q Have they been capitalized on Florida Power and Light's books at this time? And I should correct that, have the expenditures been placed in accounts that are considered capital accounts?

A I know they have been booked but I don't know in what accounts they have been placed.

Q Do you know if the Commission were to grant the Company's request whether the Utility would have to modify the booking of these expenses as they are currently reflected on the Utility's books?

A I don't know that.

Q If Florida Power and Light has basically guessed wrong, if some anomaly in the marketplace would cause high sulfur fuel to cost more than low sulfur fuel, would Florida Power and Light propose to give the money back?

A No.

Q Will these modifications lower Florida Power and Light's average fuel cost?

A Yes.

Q Will these modifications improve Florida Power and Light's ability to make economy sales?

A I haven't seen any calculation that looks at that. But all other things being equal, I would assume so.

Q Would these modifications enable Florida Power and Light to earn additional revenues through the gain on economy of sales, which I understand are calculated on a split-the-savings basis?

A To the extent that they enabled us to sell more, I assume that we would derive that benefit, yes.

Q Would you agree that, if you do derive that benefit, that Florida Power and Light's investment will on the one hand reduce its fuel costs but, on the other hand, would reduce its profits to the Company?

A Could you repeat the question again.

Q Would you agree that if Florida Power and Light is able to make additional economy sales that essentially these modifications will allow Florida Power and Light on the one hand to reduce its expenses, its fuel costs, but on the other hand to increase its profits -- which I'm lumping gains on economy of sales in as a profit.

A I think yes. But I think that that would be the case if we recovered it through base rates, as well.

Q And if you recovered it through base rates, it would be an investment designed to generate a return, would it not?

A Yes.

Q And would you agree that the fuel clause recovery mechanism is intended as a reimbursement for expenses to provide a matching between expenses and revenues for a category of expenses that are considered volatile?

A Well, I think that prior discussion with Mr. Birkett has indicated that the fuel clause and the order that implements the fuel clause agrees with the fact that these types of modifications are allowed under the fuel clause. That modifications that would otherwise be recovered through base rates but whose primary purpose is the reduction of fuel costs, as it is in this case, can be recovered through the fuel clause.

So I think that what we are proposing here is consistent with the intent of the fuel clause.

Q Well, do you have a copy of that order?

A No, I do not. (Witness provided document.)

Q Mr. Silva, I have just given you a copy of

Commission Order 14546. I believe the Commission has already taken official notice of that order, it was issued July 8, 1995, in Docket No. 850001-EI-B.

Would you take a look there at Page 5 of Order No. 14546, and specifically at Paragraph No. 10.

A Yes.

Q Is that the provision you were referring to, Mr. Silva?

A Yes.

Q Would you note, please, that that paragraph begins with the words, "Fossil fuel-related costs normally recovered through base rates." What do you consider fossil fuel-related costs to be?

A Those are costs related to the use of fossil fuels.

Q For example, if Florida Power and Light didn't have any nuclear units, would all its costs be fossil fuel related?

A I don't think so.

Q Well, what costs do you believe would be fossil fuel related?

A Well, oil is a fossil fuel. The modifications that we are talking about here are being implemented in order to burn a different type of oil, which is a fossil fuel. So in my mind, that is a fossil fuel-related cost.

I think it also talks about "normally recovered through base rates." So it doesn't restrict it to fuel costs per se, because those would be recovered through the fuel clause anyway, not normally through base rates. So clearly the intent is to broaden it beyond fuel. And my reading is that something that is done in order to use fossil fuel, and further, to save fuel costs to the customers, fits under this paragraph.

Q Well, in that regard, is it the Company's position that they should be allowed to recover these costs through the fuel clause because there are savings or because there is a change in the sulfur content of the fuel? Let me give you an example, if I might.

Would Florida Power and Light believe that this paragraph under Order No. 14546 would allow it to seek recovery if it put in place plant modifications that allowed it to burn the lower sulfur oil that it was previously burning but more efficiently?

A I think, to the extent that the end result was a fuel savings to the customer, that that would meet this requirement.

Q Well, do you believe that plant modifications designed to allow the utility to burn low sulfur fuel oil more efficiently would fit within this definition?

A It could, subject to the Commission reviewing it on a case-by-case basis.

Q Do you believe it would -- would it only apply, would the Company's position as to those fuel-related costs for which it could seek recovery be limited to physical plant modifications at generating units?

A I can't predict what the Company's position would be in a hypothetical case. I'm trying to show how this particular instance, which is specific and which talks about modifications to let us burn a higher sulfur and therefore cheaper fuel at the plant, meets this requirement. I don't know that I could speculate as to what might or might not be -- might also fit under this clause at this time. I haven't really thought about it.

Q At the time of the Utility's last rate case, did Florida Power and Light anticipate that in the future it might make plant modifications to enable it to provide electricity at a lower cost?

A I don't know.

Q Well, that's one of the requirements of this paragraph, is it not, Mr. Silva, that it would be costs which were not recognized or which were not anticipated in the cost levels used to determine current base rates?

So you don't know what the Company's anticipation was at the time of its last rate case?

A In 1983, I do not know as part of the rate case what were the Company's intentions.

MR. CHILDS: Well, I would object to that characterization. If you look to the order, it does use the word "anticipated," but it uses it by saying "anticipated in the cost levels used to determine current base rates." So I think it is more than, "Did you think about doing it," but, "Were your cost levels adjusted to reflect it," so I object to that characterization.

MR. HOWE: The objection is well-taken.

COMMISSIONER DEASON: Thank you, Roger.

MR. HOWE: But I think I can still go down this path.

COMMISSIONER DEASON: I'm sure you can.

Q (By Mr. Howe) Mr. Silva, do you know whether at the time of the Utility's last case the Utility made any pro forma adjustments -- assuming we're dealing with historic test years at that time. But, if not, whether they included in their projections any anticipated future modifications to its generating units to enable those units to burn fuel more efficiently or less expensively?

A My perception is that the pro forma was for a test period that was no longer than about 1985, and I don't know what specifically was included in that pro forma projection.

Q Do you know whether that test period included any anticipated expenses for plant modifications to improve efficiencies or to lower the cost of fuel on Florida Power and Light's system but which were not instituted by the Company?

A I do not know. I really don't.

MR. HOWE: I have no further questions. Thank you, Mr. Silva.

COMMISSIONER DEASON: Mr. McWhirter?

CROSS EXAMINATION

BY MR. McWHIRTER:

Q Mr. Silva, on Page 20 of your testimony you indicate that $8 million of the savings will occur this summer and then an additional $81 million in savings will occur in the subsequent four years.

Can you give me the rationale for writing off the total cost in the first six months of the savings rather than spreading the cost over the period during which the savings will occur?

A The calculations as to over what period to recover the costs were performed under the direction of

Mr. Birkett. But my --

Q So you don't know what the rationale is for that?

A But my understanding is that, given the savings that were realized, that the impact on the customer would be lower if these costs were recovered quickly. And that's the only explanation that I understood was the basis for our decision.

Q I think that explanation is a little bit general for me to understand. Why will the costs be lower if we recover it from the customers in the first six months rather than over the four-year period?

A I'm afraid that I was not involved in the calculation or the underlying assumption, so I can't answer that question.

Q All right, sir. The reason that these modifications have come in is because of concerns that the Environmental Protection Agency may conclude that a less expensive grade of fuel would exceed your opacity limit. Why is it you chose to bring these modifications through the fuel clause rather than the environmental clause?

A In reading the provisions that govern what is recovered through the environmental cost recovery clause and the fuel clause, we found that it was a more accurate, more appropriate fit to recover through the fuel clause because it was a change that was specifically aimed at the reduction of fuel costs. And the order that we have been discussing specifically talks about the ability of the Company to request and the Commission to grant recovery of such costs through the fuel clause, and we thought that it was a better, more appropriate fit there.

Q This is, on the whole of the magnitude of your annual gross revenues $2.7 million, is a miniscule amount. Do you have other similar modifications of other facilities that are on the drawing boards that will be brought forward in prospective rate cases, to your knowledge, or cost recovery cases, to your knowledge?

A Not to my knowledge.

Q Your orimulsion issues on that plant up in Manatee County, there was some modifications required to accommodate the orimulsion fuel. Were those costs passed through the fuel clause?

A Well, no costs related to the orimulsion conversion have been passed through the fuel clause. That was an issue that was discussed before the Commission last summer; however, we have not begun to operate on orimulsion. So the Commission's order on that that we could recover costs of conversion on an accelerated basis through the fuel cost clause is still pending our ability to get the permits and to begin operation. Which we don't anticipate will happen before 1998.

Q What's the magnitude of those costs, conversion to make orimulsion possible?

A I believe that FP&L's component share of the capital costs is $66 million.

Q Will you attempt to collect that $66 million in a six-month period if you conclude it enables you to develop a lower fuel cost?

A The Commission's order enables us to recover on an accelerated basis using one-half of net fuel savings proceeds produced by the orimulsion conversions. To the extent that fuel savings exist and they are large, we can recover quickly. If they are not as large, then we cannot recover as quickly. But the formula has been set.

Q But you don't think that approach is appropriate for this modification?

A I don't know, because I didn't really participate in the calculation of how to recover it other than through the fuel clause.

MR. McWHIRTER: I tender the witness.

COMMISSIONER DEASON: Staff?

CROSS EXAMINATION

BY MS. BROWN:

Q Just a few questions, Mr. Silva.

You stated earlier that the modifications to all of the generating units have been completed as of the end of last month?

A Yes.

Q Were the final costs for those modifications different than what you originally projected?

A Let me clarify a point.

The work has been completed and the units with the modifications have been placed in service. There are some pending invoices that still require us to keep the cost as an estimate until those are cleaned up. The current estimate is about $2.844 million and I can give you the exact number of that estimate. It is $2,844,705.

Q That's your current estimate?

A That's our current estimate of what the final amount will be.

Q Which is in the range, is it not, of what you originally projected?

A Yes.

Q In the last 13 months, Mr. Silva, has the difference between your natural gas estimates and your actual natural gas costs put Florida Power and Light in the position where its overrecovery of fuel costs would exceed the Commission-established 10% threshold for requesting a midcourse correction?

A No. Because natural gas costs are only a part of our fuel expense for the period. And even though in a number of instances or most of the time during that period gas costs have been lower than we had anticipated, there have been other factors during the period -- and there are many, beginning with the amount of sales, the costs of other fuels, the availability of other sources of energy, et cetera -- that combined with natural gas have resulted in the variance being relatively small and certainly less than 10%.

Q If the discrepancy between your natural gas estimates and your actual costs did exceed 10%, you would, would you not, request a midcourse correction from the Commission --

A Yes.

Q -- to balance it out?

A Yes. And further, if we even thought that it would come close to the 10% variance, we would come and inform the Commission. We would wait until that actually happened, but we would inform the Commission ahead of time and try to prevent that variance from developing to that level.

Q And you have done that in the recent past, have you not?

A Yes. I believe more than ten times in the last 15 years and maybe perhaps four times in the last five years.

MS. BROWN: We have no further questions.

COMMISSIONER DEASON: Commissioners, questions?

Mr. Silva, I have just a couple of questions. and I'm not really sure if you're the correct witness, maybe Mr. Birkett would be; and if need be, I can ask those questions when he testifies on rebuttal.

My question is: The cost of the modifications which you are seeking to be included in on the current fuel factor, those, I believe you agree, are capital costs, are they not?

WITNESS SILVA: I believe that under normal circumstances they would be capitalized, Commissioner.

COMMISSIONER DEASON: And is it your understanding that the Company has or will be including those costs as capital costs in its accounting records?

WITNESS SILVA: Well, I don't know if they have been included as capital costs to date. Certainly, if we were to recover them through the fuel clause, they would not be also part of our acid base -- rate base, if you would.

COMMISSIONER DEASON: Well, that's my concern. And I guess my question, to be more direct, is what is the mechanism that you will employ to ensure that that does not happen?

WITNESS SILVA: Let me venture -- and perhaps it would be better if you asked in this level of detail Mr. Birkett. But we would begin to recover through the fuel clause and it would not be reflected in base -- in the rate base. And if we had a subsequent rate case, at that time, the undepreciated value would be considered for then moving as part of the rate base, so that recovery through the fuel clause would discontinue and it would be then henceforth treated as a capital asset, the undepreciated portion.

I think the intent of all this is, as I read the Commission's intention in its order, is not provide a disincentive to the Commission -- I'm sorry, to the Company to make a change that would be beneficial to the customer simply because there may be a long period of time between rate cases. But the mechanism I know exists because it has been implemented in the past in other situations and the safeguards do exist. But I can't speak in detail to those.

COMMISSIONER DEASON: Okay. So you don't know if those costs will be capitalized on your books and that the recovery of those costs will be reflected in some type of an accelerated depreciation such that the net book value would be zero after recovery?

WITNESS SILVA: I believe that there is no decision that requires accelerated depreciation except to the extent that, based on our request, the Commission were to approve it.

In other words, if the Commission were to approve that we could recover those costs during the current or the projected period, then certainly they would be totally depreciated and they would never go into the books.

However, there are two parts to our request: One is that we recover through the fuel clause; the other is that we recover it through the projected period.

We could recover it, for example, as an alternative, through the fuel clause but between now and the year 1999. And if we had a rate case in '97 or '98, at that time the undepreciated value of those assets might be then shifted into base rates.

COMMISSIONER DEASON: Redirect?

MR. CHILDS: Yes, I have several questions.

REDIRECT EXAMINATION

BY MR. CHILDS:

Q You were asked some questions, Mr. Silva, about the potential for economy sales associated with these units for which the modifications have been made. Are all those units fueled on oil?

A All the units use oil, yes.

Q Are you aware of the Company making any significant level of economy sales using oil as the source of fuel?

A I don't know the fuel that is used to make economy sales.

Q Okay. Do you know of any recognized experts in the area for forecasting prices of natural gas?

A I'm sorry?

Q Are you aware of any recognized experts in the area of forecasting the prices for natural gas?

A Yes. We work closely with at least one expert, Petroleum Industry Research Associates. And there are others that we talk to frequently.

Q Has it been your experience that all experts agree as to the price level of natural gas on a forecasted basis?

A No, they certainly disagree significantly.

Q Are you aware as to whether Florida Power and Light's forecasted prices for natural gas in a six-month period is higher or lower than that being currently forecasted by other companies in Florida?

A We compared our forecasted price of natural gas; and invariably, in the state of Florida, our forecast is the lowest of any utility, be it investor-owned, a local distribution company. The ones that we had access to the information, we were the lowest.

Q You were asked some questions about, I believe it is, the December 2, 1994, and the February 6, 1995, sections from the Wall Street Journal containing some futures market prices for natural gas. Do you recall those questions?

A Yes.

Q What is the futures market?

A The futures market is a forum, in essence, where some buyers on any given day and some sellers on any given day can agree to trade for delivery of fuel in the future at a set price. The price at which they agree to trade in the future will fluctuate significantly from day to day, from hour to hour.

For example, for April 1995, the trading started 18 months before. And every day and every hour of every trading day the price will fluctuate. And the price today on the futures market for gas is $1.45 per MMBtu; but since trading started in that market, there has been a low of $1.36, which is close to the current price. But there also been a high of $2.31. And it just happens that those are the prices that at a given time a seller sold at that price thinking that prices would be going lower, and a buyer purchased at that price thinking that the price would be going higher, so he was making a bargain at that price. And that's what the futures market in my opinion represents.

Q Does the information published in the Wall Street Journal reflect the volume traded at the prices that are quoted for natural gas?

A It talks about the open interest but not necessarily the total volume traded.

MR. CHILDS: Okay. Mr. Kaufmann, there were some questions that you had on A Schedules that you passed to the witness and I can't find my any more. Do you happen to have another copy?

MR. KAUFMANN: Sure. (Pause)

Q (By Mr. Childs) Mr. Silva, do you recall being asked questions by Mr. Kaufmann concerning the Schedule A3 that were furnished by FPL in response to Florida Steel's Interrogatory No. 1?

A Yes, sir.

MR. CHILDS: I have distributed, Commissioner, a copy of a Schedule A1, which is Page 4 of BTB-4 -- excuse me, BTB-4, which has been marked and stipulated in this record as Exhibit 10.

Q (By Mr. Childs) Now, some of the questions that you were asked, Mr. Silva, as to the variances between forecasted levels of fuel and the actual levels of fuel prices -- that is, for gas -- cover the period April 1994 through September 1994, are they not?

A Yes.

Q Would you look at Line 29 of this sheet I just gave you, Schedule A1?

A Yes.

Q And would you look under the percent difference column in dollars?

A Yes. The percent difference between the estimated and the actual for the entire period is 1.3%.

Q And that's a negative?

A That's a negative.

MR. CHILDS: All right.

I'd like to have this sheet marked for identification, Commissioner.

COMMISSIONER DEASON: I thought you indicated it was already part of Exhibit 10 and in this record.

MR. CHILDS: It is. And I did sufficiently identify it, that's fine.

Q (By Mr. Childs) Mr. Silva, are you aware of any futures markets for commodities that are not volatile in price?

A No, sir. It strikes me that by definition for anyone to take the trouble to establish a futures market it requires it to be volatile. For example, at one point in the past we asked representatives of the New York Mercantile Exchange why there wasn't a futures market for coal, which, of course, we use in our plants, as well. And the answer was, there's no volatility, there's no point in establishing a market when everybody agrees what the price is and what it is going to do.

MR. CHILDS: I have no further questions.

COMMISSIONER DEASON: Exhibits?

MR. CHILDS: I would look to move Mr. Silva's exhibits on direct, which are, I believe, Exhibit 11.

COMMISSIONER DEASON: Without objection, Exhibit No. 11 will be admitted. Mr. Kaufmann, do you wish to move any exhibits at this time?

MR. KAUFMANN: Yes, Exhibits 40 through 43.

COMMISSIONER DEASON: Without objection, Exhibits 40 through 43 will be admitted.

(Exhibit Nos. 11 and 40 through 43 received in evidence.)

COMMISSIONER DEASON: Thank you, Mr. Silva.

(Witness Silva excused.)

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COMMISSIONER DEASON: Mr. Kaufmann, I believe your witness is next.

MR. KAUFMANN: Mr. Fietek.

STEVEN M. FIETEK

was called as a witness on behalf of Florida Steel Corporation and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. KAUFMANN:

Q Mr. Fietek, you have already been sworn in this docket. For the record, could you please state your name, name, address and by whom you are employed?

A My name is Steven M. Fietek. My address is 60 South Sixth Street, Suite 2150, Minneapolis. I'm currently employed by Dahlen, Berg & Co.

Q By whom were you retained in this case?

A I was retained by Florida Steel Corporation.

Q Do you have in front of you what has now been marked as Exhibit 22, which is a set of documents entitled, "Direct Testimony of Stephen Fietek," and attached schedules?

A Yes.

Q Did you prepare these documents to be your testimony and sponsored schedules in this docket?

A Yes.

Q Do you have any corrections, revisions or alterations to your testimony at this time?

A Yes.

Q And what is the nature of those changes and why did they come about?

A I have one change to my direct testimony. Based upon my review of the issues raised by Mr. Silva in his rebuttal testimony -- he raised several issues. There's one issue in particular which he raised which related to the heat count, the number of Btus per megawatt-hour.

In reviewing that rebuttal testimony, I determined that I agree with that testimony and, therefore, would reduce the overestimated costs which I feel that FPL had overestimated from 65 million down to the 43 million adjustment proposed by Mr. Silva in his rebuttal testimony. And I have put that on to one page here as far as a summary of that.

MR. KAUFMANN: Commissioners, I would ask that that summary of that change to his testimony be distributed and attached as a revision to his testimony?

COMMISSIONER DEASON: First of all, let's distribute that, and we'll take a break and let all parties review that. And then it may be appropriate just to identify that as an exhibit and have it admitted into evidence.

MR. KAUFMANN: Yes, sir. (Pause)

COMMISSIONER DEASON: The document which is being distributed will be identified as Exhibit No. 44.

(Exhibit No. 44 marked for identification.)

COMMISSIONER DEASON: And we'll take ten minutes at this time.

(Brief recess.)

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COMMISSIONER DEASON: I call the hearing back to order. Mr. Kaufmann.

Q (By Mr. Kaufmann) Mr. Fietek, with the addition of the changes that are on Exhibit No. 44, does your testimony now correctly reflect your testimony in this docket?

A Yes.

Q Given those changes in the testimony as already filed, would you please summarize your position in this case?

MR. CHILDS: Well, if you are going to summarize, before you -- I was going to raise this when he got to the point of asking to have the testimony inserted, and perhaps I had better do it now if the summary is going to address the change.

COMMISSIONER DEASON: Please proceed.

MR. CHILDS: I would object to what is styled "Changes to the Direct Testimony of Steven Fietek" being made a part of testimony. It goes beyond a change or correction and instead relates to something that was pointed out in the rebuttal testimony of Mr. Silva to Mr. Fietek's testimony.

I think if Mr. Fietek at some point wanted to say that in making his calculation he omitted to reflect the impact of heat rate, that's fine. But to state that he does not agree with the issues raised in Mr. Silva's testimony with with the exception of one, as he does on Line 10, changes the whole thrust of this so that it is not a correction to his testimony, it is additional direct.

COMMISSIONER DEASON: Let me ask you this question. Would you be agreeable to having this become part of the record if Line 10 and the first four words on Line 11 are stricken?

MR. CHILDS: Yes.

COMMISSIONER DEASON: Mr. Kaufmann?

MR. KAUFMANN: If that's what it takes. I'm surprised there's an objection to a concession and admission of this nature, but if it is necessary, all right.

COMMISSIONER DEASON: Given that, then, all of Line 10 and the first four words of Line 11 will be stricken.

Mr. Kaufmann, you may proceed.

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I. PURPOSE OF TESTIMONY

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

A. My name is Steven M. Fietek. My business address is 2150 Dain Bosworth Plaza, 60 South Sixth Street, Minneapolis, Minnesota. I am a consultant with Dahlen, Berg & Co., a consulting firm specializing in energy-related matters.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to address deficiencies in Florida Power & Light (FPL) Company's petition for approval of fuel cost recovery factors and capacity cost recovery factors as filed by FPL in Docket No. 950001-EI, dated January 17, 1995.

Q. By whom were you engaged?

A. Dahlen, Berg & Co. was engaged by Florida Steel Corporation (Florida Steel) who operates a steel recycling and manufacturing plant in Jacksonville, Florida. Florida Steel is a customer of FPL who purchases electric power pursuant to FPL's Commercial/Industrial Load Control Program (CILC-1) tariff. Florida Steel's Jacksonville facility is one of FPL's largest industrial customers, with a peak load of nearly 45 mW and annual energy consumption of nearly 220,000 mWh. The cost of doing business for Florida Steel is directly and substantially affected by FPL's electric rates. Therefore, Florida Steel is interested in assuring that rates charged by FPL are reasonable.

Q. What is the scope of work you performed in this case?

A. I reviewed FPL's petition, direct testimony, and exhibits filed in this case.

Q. How is your testimony organized?

A. My testimony is presented in the following sections.

- Section III, Natural gas costs are overstated by $65.5 million

- Section IV, Equipment modifications should be capitalized and depreciated
- Section V, Purchased power capacity cost allocations should be reviewed

II. STATEMENT OF QUALIFICATIONS

Q. Please summarize your experience in the area of public utility regulation.

A. I conducted discovery, performed analyses and prepared testimony on behalf of the Iowa Energy Consumers related to Midwest Power Systems' filing for a general rate increase in Iowa State Utilities Board Docket No. RPU-94-4.

I conducted discovery, performed analyses and prepared testimony on behalf of the Coalition of Industrial Energy Users related to IES Utilities, Inc.'s filing for a general rate increase in Iowa State Utilities Board Docket No. RPU-94-2.

I conducted discovery, performed analyses and prepared testimony on behalf of the Minnesota Alliance for Fair Competition related to subsidization and cost allocation issues in the matter of its complaint against Minnegasco, a Division of Arkla, Inc., in Minnesota Public Utilities Commission Docket No. G-008/C-91-942.

I conducted discovery, performed analyses and prepared a class cost of service study on behalf of the Minnesota Energy Consumers related to Minnegasco's filing for a general rate increase in Minnesota Public Utilities Commission Docket No. G-008/GR-93-1090.

I conducted discovery, performed analyses and prepared testimony on behalf of the

Northern Illinois Committee for Fair Competition related to cost allocation and subsidization issues in the matter of its complaint against Northern Illinois Gas Company, NICOR, and NICOR Energy Services in Illinois Commerce Commission Docket No. 93-0111.

I conducted discovery, performed analyses and prepared testimony on behalf of the Minnesota Alliance for Fair Competition on the value of Minnegasco's name and reputation in Minnesota Public Utilities Commission Docket No. G-008/GR-93-1090.

I conducted discovery, performed analyses and prepared testimony on behalf of the Independent Heating Contractors Association of Wisconsin related to cost allocation and subsidization issues in Wisconsin Power & Light Company's filing for a general rate increase in Public Service Commission of Wisconsin Docket No. 6680-UR-109.

I conducted discovery, performed analysis and prepared a report on behalf of Nebraska Municipalities in KN Energy, Inc.'s 1993 filing for a gas rate increase in Nebraska.

Q. Do you have any additional experience evaluating company filings to determine if proposed costs to provide a service are necessary, prudent, allowable according to applicable regulation, and properly allocated to customers?

A. Yes. I have extensive experience in evaluating company cost proposals as an Auditor and Supervisory Auditor with the Department of Defense, Defense Contract Audit Agency. I have performed and supervised the performance of audits to determine if the costs allocated to a service are necessary, prudent, allowable according to applicable regulation, and properly allocated to customers for each service. These audits are performed based on the principles contained in the Cost Accounting Standards, the cost principles contained in the Federal Acquisition Regulations, and the cost principles of the Office of Management and Budget.

Q. Would you outline your educational background?

A. In 1981, I graduated *cum laude* with a B.A. degree in business administration, major emphasis in professional accounting, from Eastern Washington University, Cheney, Washington. In May 1985, I successfully completed the Certified Public Accountant examination and received certification in November 1985.

Q. Please describe your professional background.

A. From 1982 to 1983, I worked as a staff auditor with Lincoln Mutual Savings Bank. From 1983 to 1984, I was a staff accountant, also with Lincoln Mutual Savings Bank. From 1984 to 1989, I served as an auditor and a senior auditor with the Department of Defense, Defense Contract Audit Agency. From 1989 to 1993, I was a Supervisory Auditor, also with the Agency. In 1986 and 1987, I also taught a principles of cost accounting course at Highline Community College. In February 1993, I joined Dahlen, Berg & Co. as a consultant.

SECTION III. NATURAL GAS COSTS ARE OVERSTATED BY $65.5 MILLION

Q. What is FPL's projected total cost of fuel for the period April 1995 through September 1995?

A. FPL has included in its Fuel Cost Recovery filing a projected total cost of fuel of $544,755,274 for the period April 1995 through September 1995, as shown in FPL

Appendix II, Schedule E3, page 1, line 6.

Q. How many types of fuel has FPL included in its projected total fuel cost of $544,755,274 for the period April 1995 through September 1995?

A. As shown on Exhibit 22 (SMF-1), Schedule 1, FPL has included five types of fuel in its total fuel cost of $544.8 million for the period April 1995 through September 1995: Heavy Oil ($150.1 million), Light Oil ($0.9 million), Coal ($51.2 million), Natural Gas ($287.7 million) and Nuclear ($54.9 million).

Q. Based on FPL's projected fuel mix, which type of fuel will have the greatest effect on FPL's total projected cost of fuel?

A. Because natural gas represents 52.8% of FPL's total projected fuel cost from April 1995 through September 1995, the cost of natural gas will have the greatest effect on FPL's total fuel costs during this period.

Q. Have you reviewed FPL's natural gas cost projections?

A. Yes. I have reviewed FPL's natural gas cost projections and have found several facts in FPL's filing which demonstrate that FPL's natural gas cost projection is overstated by at least $65.5 million.

Q. What facts in FPL's filing support this conclusion?

A. First, FPL's filing of its actual October 1994 and November 1994 fuel costs shows that FPL overestimated its natural gas costs by more than 31%, when the actual average cost of $1.7392 per Mcf is compared to the estimated average cost of $2.5349 per Mcf (FPL Appendix III, Schedule A6, line 45). Second, FPL admitted that its original fuel cost estimate for October 1994 through March 1995 was overstated and reduced its estimate by 18.8% stating:

> The originally projected average unit cost of natural gas generation for the six month period [October 1994 through March 1995] was $20.130/Mwh

> and the updated estimated average unit cost is $16.343 per mWh. This 18.8% decrease in the average unit cost of natural gas is primarily due to higher than projected U.S. supply of natural gas resulting from increased domestic deliverability, Canadian imports and storage capability. (FPL Appendix III, Exhibit BTB-6, page 6, note 6)

Third, FPL admitted in the direct testimony of Rene Silva that "it is projected that these factors will result in 1995 average natural gas prices remaining essentially the same as 1994 average natural gas prices." (Page 8, lines 17 through 19)

Q. Did FPL recognize this lower average cost of natural gas when it projected its natural gas cost for the period April 1995 through September 1995?

A. No. FPL did not recognize this lower actual average cost of natural gas when it projected its natural gas costs for the period April 1995 through September 1995 but instead continued to use its higher original estimate for October 1994 through March 1995 as the starting point for projecting its future gas costs.

Q. What is the average cost of natural gas included in FPL's fuel cost projection for the period April 1995 through September 1995?

A. The average cost of natural gas included in FPL's fuel cost projection for the period April 1995 through September 1995 is $21.16 per mWh as shown in Exhibit 22 (SMF-1), Schedule 2, or 29.5% greater than FPL's revised estimated cost of natural gas of $16.343 per mWh for the period October 1994 through March 1995.

Q. Has the cost of natural gas increased since FPL revised its natural gas cost estimates for the period October 1994 through March 1995?

A. No. The cost of natural gas has not increased since FPL revised its natural gas cost estimates for the period October 1994 through March 1995. In fact, the cost of natural gas has decreased since the end of November as shown in the graph in Exhibit 22 (SMF-1), Schedule 3, which presents the price of natural gas futures as reported in the Wall Street Journal on December 2, 1994 and January 20, 1995 for the period April 1995 through September 1995.

Q. What would be the effect of correcting FPL's natural gas cost projections to reflect the lower cost of natural gas recognized by FPL?

A. If FPL's natural gas cost projections were corrected to reflect the lower cost of natural gas, FPL's total projected cost of fuel for the period April 1995 through September 1995 would decrease by $65.5 million as shown on Exhibit 22 (SMF-1), Schedule 4.

Recommendation

Q. What should the Commission do to protect ratepayers?

A. The Commission should require FPL to reduce its projected fuel costs for the period April 1995 through September 1995 by at least $65.5 million using FPL's projected average natural gas cost for the period October 1994 through March 1995. Otherwise, FPL will collect revenues for a level of costs it may not incur resulting in a shift of costs and revenues from present ratepayers to future ratepayers.

IV. EQUIPMENT MODIFICATIONS SHOULD BE CAPITALIZED AND DEPRECIATED

Q. How should the $2.8 million in proposed equipment modifications to FPL's generating plants be treated?

A. The $2.8 million in proposed equipment modifications to FPL's generating plants should be capitalized and depreciated over the remaining useful life of each plant.

Q. How should FPL's proposed equipment modifications be recovered from FPL's ratepayers?

A. FPL's proposed equipment modifications should be recovered from FPL's ratepayers in the same manner as other investments in plant and equipment are recovered. FPL should include the cost of the modifications in its rate base and the related depreciation cost in its O&M expenses. FPL can file a general rate case to recover these costs from ratepayers whenever FPL believes it has an overall revenue deficiency.

Q. What treatment has FPL requested for its proposed \$2.8 million of equipment modifications?

A. On page 19 through 21 of Rene Silva's direct testimony, FPL requested that the Commission allow it to expense the entire \$2.8 million of proposed equipment modifications and include the entire cost in FPL's fuel cost recovery factor for the period of April through September 1995.

Q. Should the Commission approve FPL's proposal to recover this type of cost through the fuel cost recovery factor in this case?

A. No. The Commission should not approve FPL's proposal to recover this type of cost through the fuel cost recovery factor in this case because FPL's proposal requires current ratepayers to pay more than those costs which are required for providing them service.

Q. How does FPL's proposal result in a mismatch of revenues and expenses?

A. FPL's proposal to expense all of the equipment modification costs in a six month period results in a mismatch of revenues and expenses because FPL's equipment modifications will be used for providing utility services over the remaining life of each plant, not just for providing service during the period of April through September 1995.

Q. Does FPL's proposal result in current ratepayers paying more costs than those which are required for providing them service?

A. Yes. FPL's proposal results in current ratepayers paying more costs than those which are required for providing them service because the cost of the equipment modifications are used and useful for providing service in current and future periods, not just the six month period proposed by FPL. Approving FPL's proposal will result in current ratepayers subsidizing the cost of equipment which will be used in providing service to future ratepayers

Recommendation

Q. What do you recommend regarding FPL's proposal?

A. The Commission should require FPL to capitalize and depreciate its investment in plant and equipment. To do otherwise requires current ratepayers to pay for more costs than those which are used for providing current service.

Q. How should the recovery of these costs be determined if the Commission chooses to allow FPL to recover these costs through the fuel cost recovery factor?

A. The Commission should require FPL to capitalize and depreciate the equipment modifications over the remaining useful life of each plant and include in the fuel cost recovery factor only those costs necessary in providing electric service during the period in which the fuel cost recovery factor is in effect.

V. CAPACITY COST ALLOCATION SHOULD BE REVIEWED

Q. What allocation factor does FPL use to allocate its purchased power capacity costs to customer classes under its proposed capacity cost recovery (CCR) factor for the period April through September 1995?

A. FPL uses a 12 CP allocation factor to allocate its purchased power capacity costs to customers under its proposed CCR factor for the period April through September 1995.

Q. Does this allocation factor reflect how these costs are incurred?

A. No. This allocation factor may not reflect how FPL's purchased power capacity costs are incurred because this factor may not recognize the difference in capacity cost causation between firm and interruptible customers and the voltage level at which customers are served.

Q. What is the effect of FPL not recognizing these differences?

A. The effect of FPL not recognizing these differences in the development of its 12 CP allocation factor would result in FPL's interruptible customers who receive electric service at transmission voltages being assigned more capacity costs than they cause to be incurred.

Recommendation

Q. What do you recommend?

A. Because of the short procedural schedule in this proceeding, I have not had time to conduct discovery or to perform the analyses necessary to make a specific recommendation. I do, however, recommend that the Commission require FPL to justify that its proposed capacity cost allocation factor is based on cost causation and recognizes the differences between firm customers and interruptible customers who receive electric service at transmission voltage levels.

Q. Are there any other issues that the Commission should consider before changing

FPL's rates in this proceeding ?

A. Yes. Before the Commission changes FPL's rates in this proceeding, the Commission should address whether FPL is earning an excessive return on common equity resulting in unjust and unreasonable rates. However, because of the short procedural schedule in this proceeding, Florida Steel has not had time to perform the analyses necessary to make specific recommendations on this issue.

Q. Does this conclude your direct testimony?

A. Yes. It does.

Q (By Mr. Kaufmann) Mr. Fietek, given that change, would you please summarize your testimony and position in this case?

A Yes. My testimony presents for the Commission's consideration the view that Florida Power and Light's estimated natural gas costs for the period of April 1995 through September 1995 are overstated.

Florida Power and Light has included in its fuel cost recovery filing a projected total cost of fuel of about $544 million. Of that $544 million, natural gas represents $287 or $288 million, or about 52% to 53% of the total. Also included are costs for heavy oil, 150 million; light oil, about 1 million; coal, 51 million.

I reviewed Florida Power and Light's direct testimony and noted in Appendix 3, Schedule A-6, that FP&L for the period October '94 and November '94 had overestimated its natural gas costs. Then I looked at the Appendix 3, Page 6, Note 6, in which FP&L noted that for the period October 1994 through March 1995 that the originally projected average unit cost for natural gas generation was 20.13 megawatt-hours per megawatt-hour, and that the updated estimated unit average would be 16.343 per megawatt-hour. This is an 18.8% decrease.

Then I noted that on Page 8 of the direct testimony of Mr. Silva that he noted that it is projected that these factors, referring to the factors I just discussed, will result in 1995 average natural gas prices will remain essentially the same as 1994 average natural gas prices.

From that point, I looked at the estimated natural gas prices per megawatt-hour in their filing for April '95 through September '95 and noted that they were $21.16 per megawatt-hour. Referring back to the statement that was made in FP&L Appendix 3, Page 6, where he noted that it would be actual cost was $16 per megawatt-hour for the period in 1994 and then the statement that it was projected that natural gas prices '95 would remain the same, essentially the same, as 1994 average prices, which was $16, I computed a difference of about $4.50 per megawatt-hour and applied that to Florida Power and Light's estimate and came up with a difference of 65.5 million.

Now, I have made just one change to my direct testimony based upon the rebuttal testimony of Mr. Silva, in which, since Florida Power and Light is increasing its generation of natural gas through the use of natural gas, they're going from about 17% or 18% for generation up to about 33% or up to about 50% of the cost in the future as opposed to about 25% or 30% of their total costs in the past, but the increase in this generation using natural gas results in less efficient units, more Btu per megawatt-hour. And requiring more Btu per megawatt-hour requires the adjustment that Mr. Silva pointed out in his rebuttal testimony which, if he made the adjustment as I calculated, it would be 43 million as opposed to 65 million.

My testimony also goes on to make recommendations regarding the $2.8 million in plant modifications, equipment modifications. Essentially, FP&L has proposed to expense $2.8 million worth of equipment modifications which I believe should be capitalized and depreciated, included in rate base.

Basically, expensing those $2.8 million in expenses or allowing them to go through the fuel cost recovery clause essentially requires the ratepayers during the period of April through September 1995 to pay the entire cost of those modifications. However, those modifications will be beneficial to ratepayers over a substantially longer period of time; and that, as is traditionally done, the expense is matched up with the benefit or the costs and expenses matched up; and that ratepayers who are benefiting from these costs in the future should pay for those costs and today's ratepayers shouldn't pay any more for the cost of being provided service than that which is justified.

And expensing the entire 2.8 million today or running it through the fuel adjustment clause requires today's ratepayers to pay for costs which are going to benefit the used and useful for ratepayers in the future. So I recommend that that 2.8 million be capitalized and treated as rate base.

That concludes my summary.

MR. KAUFMANN: I would proffer Mr. Fietek for cross.

COMMISSIONER DEASON: Mr. Kaufmann, do you wish to have the prefiled testimony inserted into the record?

MR. KAUFMANN: Yes, I do.

COMMISSIONER DEASON: Without objection, the prefiled testimony will be inserted into the record.

(REPORTER'S NOTE: For convenience of the record, Mr. Fietek's prefiled direct testimony has been inserted at Page 346.)

MR. CHILDS: No questions.

COMMISSIONER DEASON: Mr. Howe?

MR. HOWE: No questions.

COMMISSIONER DEASON: Mr. McWhirter?

MR. McWHIRTER: No questions.

COMMISSIONER DEASON: Ms. Brown?

MS. BROWN: No questions.

COMMISSIONER DEASON: Commissioners? I assume then there will be no redirect. Do you wish to move exhibits into the record?

MR. KAUFMANN: Yes, I move for the admission of Exhibit 44.

COMMISSIONER DEASON: Without objection, 44 will be admitted. And I believe there was a prefiled exhibit, as well?

MR. KAUFMANN: That would be 22, I think is the testimony and schedules.

COMMISSIONER DEASON: Okay. Exhibit 22 without objection also shall be admitted.

Thank you, Mr. Fietek.

WITNESS FIETEK: Thank you.

(Exhibit Nos. 22 and 44 received in evidence.)

(Witness Fietek excused.)

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COMMISSIONER DEASON: I believe the next scheduled witness is Mr. Mestas?

MS. BROWN: We have two rebuttal witnesses for Issues 10A, 10B and 10C.

COMMISSIONER DEASON: Are we going to go ahead and do rebuttal for Power and Light before we move into TECO?

MS. BROWN: I think that makes sense.

COMMISSIONER DEASON: That's fine with me.

MR. CHILDS: I call Mr. Birkett.

BARRY T. BIRKETT

was called as a rebuttal witness on behalf of Florida Power and Light Company and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. CHILDS:

Q You have been previously sworn and identified yourself, Mr. Birkett. At this point I ask you, do you have before you a document entitled, "Rebuttal Testimony of Barry T. Birkett, Docket No. 950001-EI, February 3, 1995"?

A Yes, I do.

Q Was that prepared by you as your rebuttal testimony for this proceeding?

A Yes, it was.

Q Is the document you are sponsoring as part of that testimony prepared by you or under your direction, supervision or control?

A Yes, it was.

MR. CHILDS: Commissioner, I believe that the document Mr. Birkett is sponsoring at this time has been identified as Exhibit No. 18. I would ask that the prepared testimony of Mr. Birkett be inserted into the record, assuming there are no changes or corrections?

WITNESS BIRKETT: There are none.

COMMISSIONER DEASON: Without objection, prefiled testimony will be inserted into the record.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

REBUTTAL TESTIMONY OF BARRY T. BIRKETT

DOCKET NO. 950001-EI

FEBRUARY 3, 1995

Q. State your name and business address.

A. My name is Barry T. Birkett and my business address is 9250 West Flagler Street, Miami, Florida 33174.

Q. By whom are your employed and in what capacity?

A. I am employed by Florida Power & Light Company (FPL) as the Manager of Rates and Tariff Administration

Q. Have you previously testified in this docket?

A. Yes, I have.

Q. What is the purpose of your rebuttal testimony?

A. My rebuttal testimony will rebut certain portions of the direct testimony of Steven M. Fietek who was engaged by Florida Steel Corporation (Florida Steel).

Specifically, my testimony will demonstrate that:

1. Florida Steel witness Fietek's conclusion that FPL's projected fuel charge should be reduced does not appropriately consider the Fuel Cost Recovery process and procedures.

2. Florida Steel witness Fietek's position that the \$2.8 million expenditure for equipment modification should be recovered through base rates, capitalized and depreciated over the remaining useful life of each plant fails to consider Commission Order No. 14546, fuel savings realized by customers, and that recovering the \$2.8 million over the six month fuel cost recovery period is the most economic alternative.

3. Florida Steel witness Fietek's position that FPL's capacity cost allocation methodology does not properly reflect how the purchased power capacity costs should be allocated among the rate classes is an inappropriate issue since this matter has already been decided by the Commission. Additionally, Florida Steel was a party in that proceeding and agreed that the methodology was appropriate.

<u>Fuel Cost Recovery Process</u>

Q. Do witness Fietek's conclusions regarding the natural gas forecast and his proposed reduced fuel charge appropriately

consider the process and procedures utilized in the Fuel Cost Recovery Clause?

A. No. Witness Fietek's proposal fails to consider appropriate elements necessary in the development of a projected fuel factor. Moreover, he appears to ignore the many other elements that support a fuel charge, e.g. other fuels' prices, sales and load forecasts, maintenance schedules, etc. The Fuel Cost Recovery process and procedures contain adequate safeguards and opportunities to ensure customers and the companies are protected. When the Fuel Clause was established, the Commission recognized that actual results would differ from projections, especially since fuel prices are volatile. As a result, safeguards such as the filing of monthly A-Schedules, the 10% mid-course correction guidelines and the true-up mechanism, where variances are routinely handled, were put in place. The Commission also recognized that any time an estimate and true-up procedure is utilized, some timing differences occur.

FPL routinely reviews its inputs that were used to develop the projected fuel charge to determine if there are any changes that combined would result in a significant variance in fuel costs for the period. If a change is warranted at any time, FPL notifies the Commission.

Equipment Modifications to Generating Facilities

Q. Has Florida Steel witness Fietek considered Commission Order No. 14546 in arriving at his recommendation regarding FPL's request to recover the cost of certain equipment modifications through the fuel clause?

A. Florida Steel witness Fietek's testimony does not reflect any such consideration. I addressed how Order No. 14546 applies to FPL's request for recovery of the equipment modification costs in my prefiled testimony in this docket.

Q. Has Florida Steel witness Fietek addressed the reason why FPL is implementing certain equipment modifications to some of its generating facilities?

A. No. Mr. Fietek's recommendation fails to reflect the fact that this project was undertaken to enable FPL to use a less expensive grade of residual fuel oil at some of its generating facilities. The projected fuel savings that will be realized by FPL's customers, including Florida Steel, is approximately $81.3 million over the next five years. Additionally, as of December 1994, $4.9 million in fuel savings has already been realized by FPL's customers, since many of these equipment modifications have been implemented and placed in service.

Q. Has FPL performed an economic evaluation of alternative periods for

recovery?

A. Yes. An analysis was performed and determined that recovery of the $2.8 million in equipment modifications over the six month period as compared to recovery over the years 1995 through 1999 saved FPL's customers, including Florida Steel, $157,032 on a net present value basis, or $977,526 using nominal dollars, in carrying charges. This analysis is provided as Rebuttal Document No. 1 (BTB-9) of my testimony.

Capacity Cost Allocation Methodology for Off-System Capacity Purchased Power Cost

Q. Is the allocation methodology used by FPL appropriate.

A. Yes. The methodology is appropriate and was approved by the Commission.

Q. In what proceeding was FPL's capacity cost allocation methodology approved?

A. FPL's capacity cost allocation methodology was approved in Order No. 24840 in Docket No. 910580-EQ (docket specific to FPL) and Order No. 25773 in Docket No. 910794-EQ (generic docket).

Q. Was Florida Steel a party to these proceedings?

A. Yes. Florida Steel, as a named member of the Florida Industrial Power User's Group (FIPUG), was a party to these proceedings.

FIPUG petitioned the Commission to change the way in which FPL classified, allocated and priced off-system capacity purchased power costs. Furthermore, FIPUG agreed with FPL's allocation methodology as demonstrated in their written workshop comments filed on November 20, 1991 in Docket No. 910794-EQ which state that:

"FIPUG concurs that the cost of service study from the last rate case should be the basis for driving the demand allocation factors. The factors to be used in the proposed recovery mechanism should be derived form current load research data. Further, that load research data should be updated annually. For purposes of deriving the appropriate demand allocation factors under the recovery mechanism, all rate classes should be treated in the same manner as they were in each utility's most recent base rate case."

Q. Does the calculation of the Capacity Payment Clause factors recognize the differences in capacity cost causation between firm and interruptible service customers?

A. Yes. First, I assume that Mr. Fietek's reference to "interruptible" customers is intended to refer to customers taking service under FPL's Commercial/Industrial Load Control Program (CILC). The Capacity Payment Recovery Clause Factor for Transmission level CILC customers is based solely on the characteristics of those transmission customers, and therefore, is appropriate in relationship to both non-transmission and non-CILC customers. Additionally, consistent with

Order No. 25773 in Docket No. 910794-EQ, the allocation for each rate class is developed using FPL's last approved cost of service methodology for fossil production plant and is updated annually using current load factor information. This methodology is not, as Mr. Fietek states, 12 CP; it is actually 12 CP and 1/13. While I do not believe it is necessary to discuss the difference in this context, I do want to prevent any confusion.

The difference in costs between firm and CILC is reflected in base rates where CILC customers pay a lower rate reflecting the benefit which is realized due to their interruptibility. No additional benefit should be reflected in the CPRC.

As the Commission found in for Energy Conservation Cost Recovery (ECCR) costs in Docket No. 930759-EG, Order PSC-93-1845-FOF-EG, issued on December 29, 1993, if CILC customers were excused from paying their share of CPRC costs they would be receiving benefits in excess of those which they provide the system through their willingness to be interrupted. Any additional incentive provided through the CPRC would result in them being over compensated for their interruptibility. In other words, FPL's other customers would be paying more for that interruptibility than they would receive in benefits.

Q. **Is Florida Steel witness Fietek's issue regarding FPL's capacity cost allocation methodology appropriate?**

A. No. This is an inappropriate issue since this matter has already been decided by the Commission in a proceeding to which Florida Steel was an active party.

Q. Does this conclude your testimony?

A. Yes.

Q (By Mr. Childs) And, Mr. Birkett, would you summarize your testimony?

A My rebuttal testimony addresses portions of the testimony filed by Steven Fietek on behalf of Florida Steel in which Mr. Fietek concludes that FPL's projected fuel charge should be reduced and FPL's proposal to recover $2.8 million in plant modifications through the fuel clause should not be approved.

Florida Steel's proposal to reduce FPL's proposed fuel charge fails to consider the many elements in the development of the fuel factor and inappropriately focuses on the natural gas price forecast to the exclusion of all the other elements. Their proposal also fails to consider fuel cost recovery processes and procedures which contain adequate safeguards to ensure that both customers and the utilities are protected.

When the fuel clause was established, the Commission recognized that actual results would differ from projections, especially since fuel prices are volatile. As a result, the Commission put in place safeguards such as the filings of monthly A Schedules, the 10% midcourse correction guidelines, and true-up mechanism. FPL routinely reviews the inputs used to develop the projected fuel charge. If a change is warranted at any time, FPL notifies the Commission.

Florida Steel's proposal regarding the plant modifications apparently fails to consider the Commission's Order 14546, the fuel savings realized by FPL's customers, including Florida Steel, as a result of the modifications, and that the recovery of the $2.8 million in the projected period is the most economic alternative for FPL's customers.

That concludes my summary.

MR. CHILDS: We tender Mr. Birkett for cross examination.

CROSS EXAMINATION

BY MR. KAUFMANN:

Q Mr. Birkett, would it be unreasonable for you to change your recommendation to the Commission before the fuel factor is set if data becomes available to you prior to the factor being set which indicates that your fuel cost estimates are incorrect and that better data is now available?

A No, that would not be unreasonable. In fact, FPL has done so on several occasions in the past years when it has become clear that the fuel cost factor, based on current information, should be changed; we have brought that information to their attention and in many cases modified the factor before we submit it to them for final approval.

Q You're talking about the stage of the process where we are now, not midcourse correction?

A That's correct.

Q And how far off were you in those cases where you did make that recommendation?

A I don't remember the specifics of those cases, but I believe in each one it became -- it was clear to us that if we did not make a change that we would exceed the 10% midcourse correction guideline during the period, and thus it made sense to change the factor before even putting it into effect.

Q So if you have information which gives you some strong indication that you will require a midcourse correction if you don't change it now, you would recommend changing it now?

A I will -- I say yes, but maybe rephrase to it the standpoint that if we believed today that we would be filing a midcourse correction -- that, you know, our current indications are that we would, the variance would exceed 10% of the fuel costs -- then we would be proposing a change at this time. But since our projections are not as such, then we have not proposed a change.

Q So unless you anticipate being wrong by at least 10% at some point during the period, even though you know you are going to be wrong, you would recommend the factor as it is?

A No. I don't think -- and maybe I misspoke. The 10% I would not use as a firm guideline in this case. I mean, that is the kind of magnitude we're looking at.

But I would agree, you know, that even though we know that the actuals will not match our forecasts if they are not of, you know, if the differences are not of significant magnitude at this point in time, we would not propose a change. Because there are many things that could happen over the course of the period; and, you know, quite often just as things, you now, may look now that to some -- some things that will lower fuel costs, there will be some things that happen which will result in higher fuel costs or lower revenues to the extent that they would offset what's there currently.

Q You don't have any current information as to those offsetting items, do you?

A No, I don't have an estimate at this time of what is going to happen. I do know there has been an analysis and we have relooked at our inputs and do believe that what we have filed is appropriate.

MR. KAUFMANN: Thank you. No further

questions.

COMMISSIONER DEASON: Mr. Howe?

MR. HOWE: No questions.

COMMISSIONER DEASON: Mr. McWhirter?

MR. McWHIRTER: No questions of Mr. Birkett.

COMMISSIONER DEASON: Staff?

MS. BROWN: We have one question, Mr. Birkett.

CROSS EXAMINATION

BY MS. BROWN:

Q If the costs of the modifications were capitalized for any period longer than one month, how would that affect the overall cost of the modifications to the ratepayers?

A That would increase the overall costs in modifications because there would be a carrying cost associated with that capitalization which would raise the costs over the pure expense level which FPL is proposing to include in rates at this time.

MS. BROWN: No further questions.

COMMISSIONER DEASON: Commissioners?

Mr. Birkett, were you in the room when I asked Mr. Silva some questions concerning the accounting of the modification costs?

WITNESS BIRKETT: Yes, I was, Commissioner.

COMMISSIONER DEASON: What is your

understanding of the accounting treatment which would be afforded these costs if the Commission were to decide to have those costs included, totally included, in this six months projection period?

WITNESS BIRKETT: Commissioner, what would happen -- let me back up. At the present time, those costs are included in capital accounts. Now, what we would do is reflect, you know, make adjustments to reflect that those costs are being removed and go ahead and expense those accounts in this period so that there would be a pure expense, nothing would be treated as capital, there would be no depreciation or any other capital type costs associated with them.

COMMISSIONER DEASON: Redirect?

MR. CHILDS: I have no redirect. I would like to move into evidence Exhibit No. 18.

COMMISSIONER DEASON: Without objection, Exhibit 18 shall be admitted.

MR. CHILDS: I would like to ask that Mr. Birkett be excused, he has to catch an airplane shortly to go testify elsewhere.

COMMISSIONER DEASON: Mr. Birkett, you are excused.

MR. CHILDS: Thank you.

(Exhibit No. 18 received in evidence.)

(Witness Birkett excused.)

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MR. CHILDS: Our next witness is Mr. Silva.

RENE SILVA

was called as a rebuttal witness on behalf of Florida Power and Light Company and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. CHILDS:

Q Mr. Silva, you have been previously sworn and identified. At this point, I ask do you have before you a document entitled, "Rebuttal Testimony of Rene Silva, Docket No. 950001-EI, February 3, 1995"?

A Yes.

Q Is that your rebuttal testimony for this proceeding?

A Yes.

Q And were the two documents that you are sponsoring prepared by you or under your direction, supervision and control?

A Yes.

Q Do you have any changes or corrections to make either to your testimony or to the documents that you are now sponsoring?

A No, sir.

Q Do you adopt this as your testimony?

A Yes.

MR. CHILDS: Mr. Commissioner, we ask that the prepared rebuttal testimony of Mr. Silva be inserted into the record as though read.

COMMISSIONER DEASON: Without objection, it will be so inserted.

MR. CHILDS: And the documents he is sponsoring have been marked for identification as 19 and 20.

COMMISSIONER DEASON: Very well.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

FLORIDA POWER & LIGHT COMPANY

REBUTTAL TESTIMONY OF RENE SILVA

DOCKET NO. 950001-EI

February 3, 1995

Q **Please state your name and address.**

A. My name is Rene Silva. My business address is 9250 W. Flagler Street, Miami, Florida 33174.

Q. **By whom are you employed and what is your position?**

A. I am employed by Florida Power & Light Company (FPL) as Manager of Forecasting and Regulatory Response in the Power Generation Business Unit.

Q. **Have you previously testified in this docket?**

A. Yes.

Q. **What is the purpose of your testimony?**

A. My rebuttal testimony rebuts the direct testimony of Witness Steven M. Fietek, filed on behalf of Florida Steel Corporation. Specifically, my testimony will address the concerns that Mr. Fietek expressed regarding FPL's projected cost of natural gas for the April through

September 1995 period. My testimony shows that Witness Fietek's conclusion that FPL's projected fuel cost is excessive is invalid, that his methodology is flawed, and that he fails to recognize the difference between the price of gas supply ($/MMBTU) that FPL purchases, and the cost of gas generation ($/MWH) that FPL incurs in generating electricity using gas as a fuel.

Q. On page 5, lines 14-16 of his testimony, Witness Fietek states that FPL's natural gas cost projection for the April through September 1995 period "is overstated by at least $65.5 million." Do you agree?

A. No. FPL's projected cost of natural gas generation for the April through September 1995 Fuel Cost Recovery period (projected period) is based on FPL's November 1994 gas price forecast for the projected period, which reflects then current gas market conditions and perceptions, as well as the cost of gas transportation to FPL, gas supply contract pricing terms, the quantity of gas expected to be used in FPL's system, the efficiency in heat rate (BTU/KWH) with which gas is used in each of FPL's generating units, FPL's projected load requirements and the cost and availability of other sources of energy during the projected period. FPL's projected cost is correct and appropriate for use in the Fuel Cost Recovery Clause for the projected period.

Witness Fietek has calculated his $65.5 million figure by inappropriately applying FPL's updated average unit cost of gas generation (in $/MWH) for the October 1994 through March 1995 period (current period) to FPL's projected gas generation (in MWH) during the projected period and subtracting that product, without explaining why its use is justified, from FPL's projected cost of gas generation for the projected period. Witness Fietek inexplicably refers to this difference as FPL's excessive cost.

Q. **Why is Witness Fietek's methodology inappropriate?**

A. Because it (1) arbitrarily, and without any justification, assumes that the current period gas generation cost estimate (in $/MWH) should be used as the projected fuel cost estimate (in $/MWH) for a future period, and in so doing, (2) fails to recognize a number of significant factual (and one projected) differences between the projected period and the current period that affect FPL's cost of gas generation.

Witness Fietek's methodology erroneously equates FPL's cost of electric generation using gas (in $/MWH), which I refer to as gas generation, to the price of gas in the market (in $/MMBTU), thus ignoring other determinants of the cost of gas generation. In addition, he assumes erroneously that the price of gas in the market will not change between the current period ending in March 1995, and the projected period. Therefore, for these reasons, his results are invalid.

Q. What are the key differences between the current period, ending March 1995 and the projected period that affect the cost of gas generation?

A. There are four significant differences between the projected period and the current period that are correctly reflected in FPL's projected cost of gas generation for the projected period, and which witness Fietek fails to consider.

First, the average heat rate of gas generation during the projected period is approximately 9.87% higher than for the current period. This means that, on average, it will take 9.87% more gas to generate a megawatt-hour (MWH) in the projected period. Had Witness Fietek reflected this heat rate difference (that we know will occur) in his calculation, his $65.5 million would have been reduced to $43.6 million.

Second, FPL's average firm gas transportation rate will increase by approximately 12.8% from the current period, ending March 1995, to the projected period because FPL will receive, beginning in March 1995, 200,000 MMBTU per day of additional gas transportation from the higher-tariff FTS-2 firm service associated with Florida Gas

Transmission's Phase III pipeline capacity expansion. Had Witness Fietek also reflected this known increase in the gas transportation cost in his calculation, his result would have been further reduced to $35.5 million.

Third, during the projected period, FPL will receive approximately $1.0 million in credits from its gas supplier, compared to about $12.4 million of credits for the current period ending March 1995. These credits were obtained by FPL for its customers as part of the negotiated agreement, concluded in May 1994, to replace prior gas supply contracts with a new long-term contract. Had Witness Fietek's calculation also reflected this known reduction in credits, his result would have been further reduced to less than $14 million.

Fourth, we project that, on average, FPL's gas supply price will be $0.10/MMBTU higher during the projected period than for the current period, ending March 1995. Witness Fietek assumes that the gas market price will not change. Applying FPL's projected gas supply price increase to Witness Fietek's calculations further reduces his result to about $3.3 million, or less than 1.2% of FPL's total projected cost of gas.

It should be noted that the only determinant of the cost of gas generation ($/MWH) discussed in Witness Fietek's testimony is the market price of natural gas ($/MMBTU). My testimony shows that his implied gas price position (no change from the current period), with which we disagree, accounts for less than $14 million.

Q. **Why is the average heat rate of gas generation higher in the projected period?**

A. Because as the quantity of natural gas used in FPL's generation system increases, more gas is allocated to generating units that utilize gas less efficiently. During the projected period, gas generation is projected to be approximately 13.6 million MWH; this is 5.4 million MWH or 65.7% more than the 8.2 million MWH (Rebuttal Document No.1, line 14, column H (RS-4)) for the current period, ending March 1995. FPL dispatches its most efficient units first, so the additional gas generation is provided by less efficient units. As a result, the average heat rate for gas generation in the projected period is 8,527 BTU/KWH; this is 766 BTU/KWH, or 9.87% higher than the 7,761 BTU/KWH (Rebuttal Document No.1, line 72, column H (RS-4)) for the current period, ending March, 1995.

Q. **How would you calculate the impact of heat rate that witness Fietek's calculation failed to reflect?**

A. As I have stated above, Witness Fietek's proposed methodology is invalid. Therefore, I have performed different calculations in order to quantify the magnitude of the error in Witness Fietek's calculation due to each of the four differences described above.

Multiplying the $/MMBTU average cost of gas in the current period ending March 1995, shown in Document No.1, line 62, column H ($2.1057/MMBTU) by the total MMBTU used in the projected period (115,917,400 MMBTU), and then subtracting that product ($244,087,269) from FPL's total projected cost of gas for the projected period ($287,711,489) results in $43,624,220, instead of Witness Fietek's $65,533,519. The difference between these figures is the heat rate effect.

Q. Please explain why the gas transportation cost will be higher in the projected period.

A. During the current period ending March 1995, FPL is transporting approximately 51.2 million MMBTU of gas at $0.54/MMBTU, the tariff approved by the Federal Energy Regulatory Commission (FERC) for FTS-1 (existing firm gas transportation service provided by Florida Gas Transmission (FGT) to FPL and other Florida customers), including compressor fuel charges. FPL is also transporting about 6.2 million MMBTU of gas at $0.86/MMBTU, the tariff approved by FERC for FTS-2 (new firm gas transportation service scheduled to begin on

March 1, 1995, upon completion of FGT's Phase III pipeline expansion), including compressor fuel charges. FPL's weighted average cost of firm transportation during the current period ending March 1995 will be about $0.576/MMBTU.

During the projected period, FPL will transport approximately 74.2 million MMBTU at $0.54/MMBTU (FTS-1), and about 36.6 million MMBTU at $0.86/MMBTU (FTS-2). FPL's weighted average cost of firm transportation during the projected period will be about $0.649/MMBTU, or $0.074/MMBTU higher than in the current period. As a result, FPL's gas cost during the projected period will reflect an $8,143,100 increase due to the known higher cost of transportation, compared to what Witness Fietek erroneously calculated using (implicitly) the current period unit cost of firm transportation ($0.576/MMBTU) to calculate the total cost for the projected period.

Q. **What is the impact of the increase in the transportation cost that Witness Fietek's methodology failed to reflect?**

A. The $8,143,100 increase due to the higher firm transportation cost was not reflected in Witness Fietek's calculation. Subtracting this amount from the $43,624,220 shown above reduces the figure to $35,481,120.

Q. What is the effect of the reduction in credits that Witness Fietek's calculation failed to reflect?

A. Approximately $21.5 million. During the current period, ending March, 1995, the $12.4 million in credits are divided by the 63,680,761 MMBTU of gas FPL is purchasing. This credit amount reduces FPL's unit cost of gas by $0.1943/MMBTU, and thus contributes to the lower ($2.1057/MMBTU) cost of gas during the current period. For the projected period, the $1.0 million in credits, divided by the 115,917,400 MMBTU of gas FPL projects to purchase, will reduce FPL's cost of gas by only $0.0088/MMBTU. The difference, $0.1855/MMBTU, multiplied by the 115,917,400 MMBTU of gas FPL will purchase in the projected period results in $21,502,678. This is the amount that Witness Fietek's calculation failed to reflect. This effect of known reduced credits should be subtracted from the $35,481,120 shown previously to reduce the figure to $13,978,442.

Q. Please explain how FPL's projected difference in the gas supply price affects the cost of gas generation in the projected period.

A. The weighted average cost of gas supply (for that portion of the gas delivered through firm transportation) during the projected period is $1.86/MMBTU, or $0.10/MMBTU higher than for the current period (Rebuttal Document No.2 (RS-5)). This price increase reflects our view that greater gas market demand in August and September will push gas supply prices to the higher levels that existed in the first quarter of 1994. Multiplying the $0.10/MMBTU projected price difference between the projected period and the current period ending March 1995, by the quantity of gas delivered under firm transportation in the projected period (110,790,000 MMBTU) results in $10,637,271. This is the effect of the difference in FPL's projected price of gas supply between the two periods. Witness Fietek's methodology erroneously implies that this effect is $65.5 million.

If this $10,637,271 is subtracted from the $13,978,442 shown above, only $3,341,171 remains. This difference relates to changes in the cost of interruptible gas transportation and the cost of gas supply delivered through interruptible transportation.

Q. How will FPL reflect changes in gas market conditions on its projected cost of fuel?

A. We will continue to monitor and evaluate gas market developments, as well as changes in other fuels. Prior to the Prehearing Conference, we will determine whether changes in fuel market conditions (for gas and other energy sources) suggest that a change in the overall projected cost of fuel for the projected period is appropriate and, if so, we will propose a change at that time. Mr Birkett's Rebuttal Testimony also discusses, the process and procedures used to address the effects of changing fuel prices in the Fuel Cost Recovery Clause.

Q. **On page 6, lines 9-14 of his testimony, Witness Fletek states: "FPL did not recognize the lower actual average cost of natural gas when it projected its natural gas cost for the period April 1995 through September 1995 but instead continued to use its higher original estimate for October 1994 through March 1995 as the starting point for projecting its future gas costs." Do you agree?**

A. No. This is incorrect. The average gas supply price projected in FPL's price projection prepared in May, 1994 for the October, 1994 through March, 1995 period was $2.29/MMBTU. In November, 1994, the average projected gas supply price for the October, 1994 through March, 1995 period was reduced to $1.76/MMBTU, and a new gas price projection was developed, recognizing the reduced cost of gas, for the April through September 1995 period which resulted in an average gas supply price of 1.86/MMBTU (Rebuttal Document No. 2 (RS-5)). This November price projection is the one used in FPL's Fuel Cost Recovery filing of January 1995.

Q. **On page 7, lines 14-17 of his testimony, Witness Fletek recommends that the Commission reduce FPL's projected fuel cost by $65.5 million. Do you agree?**

A. No. Witness Fletek's testimony uses a flawed calculation in an attempt to support his conclusion that FPL used an excessively high price of gas supply in its calculation of the projected fuel cost for the April through September 1995 period. Moreover, in reaching his conclusion, Witness Fietek fails to recognize the difference between FPL's price of gas supply and its cost of electric generation using gas. As a result, although his testimony is intended as a criticism of FPL's gas price projection, it does not accomplish that objective because it criticizes a gas price projection that does not exist.

The calculation that resulted in Witness Fietek's $65.5 million figure is invalid because, as demonstrated in my testimony, it fails to reflect a number of significant known facts that affect the cost of gas generation, and his arbitrary assumption that current period costs should be used to estimate the cost for a future period has no justification. In addition, it would not be appropriate to adjust the total projected fuel cost for the projected period based solely on the perceived variation in a single fuel, without considering the effect of changes in prices of other fuels. Therefore his recommendation is without merit and should be rejected.

Q. **Does this conclude your rebuttal testimony?**

A. Yes, it does.

Q (By Mr. Childs) Would you please summarize your rebuttal testimony, Mr. Silva.

A Yes, sir.

Commissioners, my rebuttal testimony shows that the methodology used by Florida Steel to support its recommendation that FPL's proposed fuel cost recovery factors should be reduced is not valid because, one, it arbitrarily and without justification assumes that the current period costs should be used as the projected costs for the next period. And it fails, in so doing, to consider a number of factors that affect FPL's cost of gas generation during the April through September period.

My testimony shows that there are four significant factors that raise FPL's cost of gas generation. Now, three of those are facts, they are not in terms of what we think the market will do. The first is the average heat rate. The heat rate will be 9.9% higher and it will take 9.9% more gas to generate one megawatt of electricity. If you will look at this factor, this accounts for $21.9 million in costs compared to the $65.5 million that Florida Steel's testimony suggested we were overstating.

Second, FPL's average gas transportation rate, which is a FERC tariff, for firm transportation will increase by 12.8% during that next period. That is a fact. And that will account for an increase of $8.1 million when applied to Florida Steel's calculation.

Third, FPL will receive $11.4 million less in negotiated gas supply contract credits. These are credits that we have received as an inducement or incentive to enter into a contract and they will not continue further into the period. That accounts for another $21.5 million in Florida Steel's calculation.

Together, those three account for $51.5 million of the $65.5 previously stated.

The fourth factor is that we have projected that FPL's cost of gas supply, fuel price per se, on average will be 10% -- excuse me, 10 cents per MMBtu higher than during the current period. That essentially accounts for the remainder of the presumed overstatement of our fuel cost.

Florida Steel's methodology essentially assumes that the unit cost of gas generation does not change and it chooses to ignore these factors.

In addition, my rebuttal testimony states that it would not appropriate to adjust the proposed fuel cost recovery factor as recommended by Florida Steel based solely on a perceived price variation in a single fuel, natural gas, without considering the effect of changes in other factors, such as availability and costs of other sources of generation, purchased power, other fuels, and sales projections.

For these reasons, we believe that Florida Steel's recommendation to change FPL's proposed factor is without merit.

That concludes my testimony.

MR. CHILDS: We tender Mr. Silva for cross examination.

COMMISSIONER DEASON: Mr. Kaufmann?

MR. KAUFMANN: Thank you.

CROSS EXAMINATION

BY MR. KAUFMANN:

Q Mr. Silva, is it correct that your estimated costs for October 1994 through March 1995 would include the contract credits that you mentioned that you got starting in May 1994?

A Yes.

Q Would it also be correct that your estimated cost of gas would also include the transportation costs?

A Yes.

Q Now, these gas transportation costs are set by tariff and have not changed since your most recent estimated cost of gas, have they?

A That's correct.

Q Therefore, the only real reason for any -- reason for FPL's actual cost of gas per MMBtu to be significantly lower than FPL's estimated cost of gas per MMBtu is due to the cost of the natural gas supply?

A To the extent we agreed that they should be lower, that would be the only factor.

Q Now, you reestimated your cost of gas for January 1995 in your Rebuttal Document No. 1, Page 2; is that correct?

A Document 1, Page 2, shows what we referred to as the estimated actual costs for the October '94 through March 1995 period.

Q What is your reestimated cost of gas for January 1995?

A It is, in cents per kilowatt-hour, it is 1.6163 cents per kilowatt-hour.

Q And how much per MMBtu?

A That would be at Line 62, which is $2.1816 per MMBtu.

Q Now, how does this compare to FPL's actual cost of gas for January shown in the A3 schedule which we discussed earlier? Do you still have that? That would be Exhibit No. 40. (Pause)

A In the Schedule A3 for January '95, the actual cost of gas is $1.7999 per MMBtu.

Q In this reestimation of costs that are in Rebuttal Document No. 1, Page 2, those you just did this last January, did you not?

A Yes. Excuse me, the estimated actual was based on projections done in November. It has two months of actual, October and November.

Q But the actual is 1.7999?

A That's correct.

Q So even though you reestimated the cost of gas in your rebuttal testimony for the month of January, you're still 21% too high, aren't you?

A Yes.

Q Mr. Silva, you say on Page 5 of your rebuttal testimony that during the current period ending March '95 that FPL will receive 12.4 million in credits from your natural gas supplier; is that right?

A Yes.

Q You further state on Page 5 that these credits were negotiated by FP&L as of May 1994, correct?

A Yes.

Q Were these credits considered in your reestimated cost of natural gas for the period of December 1994 through March 1995, which is in this Rebuttal Document No. 1, Page 2?

A The credits have been included in all the estimates.

Q Mr. Silva, you say on Page 9 of your rebuttal testimony that these credits that FP&L has obtained from its gas supplier will reduce FP&L's cost of gas by 19.43 cents per MMBtu during the current period of March '95; is that correct? Ending March '95?

A Yes.

MR. KAUFMANN: Indulge us, please, Commissioners, we're getting out a document here.

(Pause)

I apologize, Commissioners, it will just be a moment. (Witness furnished a document)

I apologize I don't have extra copies of that response right now, I can provide them very shortly if it is necessary.

Q (By Mr. Kaufmann) Mr. Silva, I would like you to refer to FP&L's response to Florida Steel's Interrogatory No. 15, which I've just handed you, where FP&L was requested to explain the difference between FP&L's actual cost of natural gas in November of 1994 of $1.80 per MMBtu and your estimated cost of natural gas for December 1994 of $2.39 per MMBtu?

A Yes.

Q As shown on your Rebuttal Document No. 1; is that correct?

A Yes.

Q And what is that difference in price?

A The difference between projected December '94 and actual November '94 is 59 cents per MMBtu.

Q In response to the interrogatory that I have just handed you, you stated that 51 cents per MMBtu is due to contract credits; is that correct?

A Yes.

Q But on Page 9 of your rebuttal, you state that the credits will reduce the cost of gas by 19.43 cents. Is that correct?

A The number in Page 9 of my testimony talks about the total amount of credits, which is 12.4 million, to be received during the entire period of October through March; and it is divided, the entire MMBtu that FPL is purchasing during that period.

The question that I am responding to in response to your interrogatory compares November to December; and the credits are not uniform from month to month, so the two numbers really don't have any correlation.

Q Mr. Silva, I just handed you a document which is FP&L's response to Florida Steel's first set of interrogatories, Interrogatory No. 3.

MR. KAUFMANN: And I'd ask that it be marked for identification as Exhibit No. 45, I think is the next one.

COMMISSIONER DEASON: We need to interrupt for just a second. Mr. Silva, do you need some paper towels?

WITNESS SILVA: I believe so. It flowed back.

COMMISSIONER DEASON: We'll take a ten-minute recess at this time.

(Brief recess.)

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COMMISSIONER DEASON: Call the hearing back to order.

Mr. Kaufmann?

Q (By Mr. Kaufmann) Mr. Silva, do you have in front of you now Exhibit 54, which I just handed you, which is -- I'm sorry, 45 which is the FPL response to Florida Steel's first set of interrogatories, Interrogatory No. 3?

A Is that a question?

Q Yeah. Do you have that?

A Yes, I do.

Q Now, on Page 2 of that response, FPL provides its cost per MMBtu to transport gas under the FTS 1 Schedule for April of 1995 through September 1995; is that correct?

A Yes.

Q Now, in order to get the total transportation cost, that would involve adding columns C -- I guess that's supposed to be -- well, there is a column that says "C", demand charge, dollars per MMBtu. And then there's another Column C that says "commodity/rate dollars per MMBtu."

In order to get the total transportation rate, would it involve the addition of those two columns for any particular month?

A In order to get the total transportation rate, which is the actual cost, you'd have to add the demand charge plus the commodity charge.

Q Right. So, for instance, for April of 1995 under this exhibit, it would be taking the .4331 and adding to that the .0725; is that correct?

A April 1995?

Q Yes.

A Yes.

Q All right. So subject to check, would you agree that that's .5056? Or you can do the math yourself, if you like.

A Yes.

Q And going through September 1995 that that would escalate to .5059?

A Yes.

Q Now, on Page 8 of your rebuttal testimony, you state that you will be transporting 74.2 million MMBtu at .54 per MMBtu under FTS 1; is that correct?

A Yes. The difference between those two numbers is the compression fuel. That is not included in these tables.

Q Now, if you could refer back to the response to Interrogatory No. 3 again on Page 3?

A Yes.

Q That response provides the cost per MMBtu to transport gas under FTS 2, and that would also include April 1995 through September '95; is that correct?

A Yes.

Q All right. And if you did the same calculation adding the demand and the commodity rates, would you agree, subject to check, that beginning in April '95, the number would be .8077 escalating to .8080?

A Yes. And, of course, that sum is again different from the one in my rebuttal testimony because my rebuttal testimony includes the fuel for compression which these tables do not because you did not ask for it.

Q So the .86 that you mentioned in your

testimony includes compression?

A Yes.

Q All right. Mr. Silva, would you agree, subject to check, that the average natural gas prices during 1994 for FPL were approximately $2?

A I can't agree subject to check. Let me take a look at the information before me.

When you say "natural gas cost," specifically what are you referring to?

Q If you are looking at Schedule A3, Line 44 for the actuals, if you would take that for entire 1994, the average would be approximately $2?

A Well, if you want me to answer that question, you're going to have to give me time to calculate the average.

If I may say, this is not a straight average calculation because it's a weighted average-type calculation, so it's going to take me a few minutes to do this.

MR. KAUFMANN: I'll withdraw the question.

I have no further questions.

COMMISSIONER DEASON: Mr. Howe?

MR. HOWE: No questions.

COMMISSIONER DEASON: Mr. McWhirter?

MR. McWHIRTER: No questions.

placed into service at this time?

A Yes. It was placed in effect on March 1st.

Q All right. Thank you.

MS. BROWN: That's all.

COMMISSIONER DEASON: Redirect?

MR. CHILDS: I have no redirect.

I would like to move into evidence Exhibits 19 and 20.

COMMISSIONER DEASON: Without objection, Exhibits 19 and 20 are admitted.

(Exhibit Nos. 19 and 20 received in evidence.)

MR. CHILDS: And I'd like to ask that Mr. Silva be excused, please.

COMMISSIONER DEASON: Mr. Silva may be

excused.

(Witness Silva excused.)

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MR. KAUFMANN: I also ask that we --

COMMISSIONER DEASON: Exhibit 45 without objection --

Mr. Kaufmann, the admittance of Exhibit 45, and without objection, Exhibit 45 shall be admitted.

(Exhibit No. 45 received in evidence.)

COMMISSIONER DEASON: I believe now we can proceed into TECO's case with Mr. Mestas.

MR. BEASLEY: Yes, sir. I'd like to call Mr. Donald Mestas.

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DONALD MESTAS

was called as a witness on behalf of Tampa Electric Company and, having been duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. BEASLEY:

Q Sir, would you please state your name, your business address and your position with Tampa Electric?

A Yes. My name is Don Mestas. My business address is 702 North Franklin Street, Tampa, Florida 33602.

Q Were you in the room this morning when Commissioner Deason administered the oath?

A Yes, I was.

Q Mr. Mestas, did you prepare and submit in this proceeding a six-page document entitled "Prepared Direct Testimony of D. M. Mestas, Jr."?

A Yes.

Q If I were to ask you the questions contained in that testimony, would your answers be the same?

A Yes.

MR. BEASLEY: I'd ask that Mr. Mestas' testimony be inserted into the record as though read.

COMMISSIONER DEASON: Without objection, it will be so inserted.

Q (By Mr. Beasley) And you did not sponsor an exhibit, did you, sir?

A No.

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

PREPARED DIRECT TESTIMONY

OF

D. M. MESTAS, JR.

Q. Will you please state your name, business address and occupation?

A. My name is D. M. (Don) Mestas, Jr. My business address is 702 North Franklin Street, Tampa, Florida 33602, and I am Assistant Director, Cogeneration, for Tampa Electric Company, which is a Florida corporation with its principal offices in Tampa, Florida.

Q. Would you please furnish a brief outline of your education background and business experience?

A. I was educated in the public schools of Tampa, Florida and the University of Florida in Gainesville, graduating in 1964 with a Bachelor of Industrial Engineering Degree. I have been employed at Tampa Electric Company since May of 1964 and have experience in engineering, marketing and other areas within the company. In August of 1980 I was appointed to the position of Assistant Director of Load Management in the company's Conservation and Load

Management Department. I currently serve as Assistant Director, Cogeneration in Tampa Electric's Energy Services & Planning Department.

Q. Have you previously testified before this Commission?

A. Yes. I testified in the Commission proceeding which resulted in Tampa Electric's currently approved conservation programs. I have also testified in Docket No. 820165-EU, which resulted in Commission approval of Tampa Electric's cogeneration agreement with Conserv, a qualifying facility, as well as in Docket No. 830199-EU, which resulted in this Commission's approval of Tampa Electric Company's small power production agreement with the City of Tampa. I have participated in the cogeneration rules implementation proceedings in Docket No. 830377-EU, which resulted in Order No. 13247. I testified in Docket No. 840399-EU regarding the provision of self-service wheeling and I have participated in a number of other hearings and workshops on conservation and cogeneration conducted by this Commission. I also testified in this Commission's Docket No. 881005-EG regarding capacity and energy payments to government solid waste facilities. I testified in this Commission's Docket No. 891049-EU involving revisions to the Commission's rules pertaining to cogeneration and small power production and in Docket No. 910004-EU regarding Tampa Electric's proposed standard offer contract for cogenerators and small power producers. I have testified in Docket No. 910603-EQ on negotiating contracts between QFs and electric utilities and in Docket Nos. 921288-EU, the Bidding Rule, and 931186-EQ, regarding amendments to the Cogeneration Rules to ensure consistency with the Bidding Rule.

Most recently, I appeared before the Commission in Docket No. 941155-EQ to request approval of certain assignments and modifications to a 1989 Standard Offer contract between Tampa Electric Company, Orange Cogeneration, L.P. and Polk Power Partners, L.P.

Q. What is the purpose of your testimony?

A. On December 20, 1994 the Commission voted in Docket No. 941155-EQ (Joint Petition for Expedited Approval of Contract Modifications to a 1989 Standard Offer Contract by Tampa Electric Company, Orange Cogeneration Limited Partnership and Polk Power Partners LP) to approve certain assignments and modifications of a standard offer contract Tampa Electric had entered into. One of the issues included in the Staff Recommendation was whether a

$1,106,760 option payment from Polk Power Partners LP ("Polk") to Tampa Electric "should be examined during Tampa Electric's next fuel adjustment proceeding." At this point no specific issues relative to the option payment have been raised in the fuel adjustment docket. Inasmuch as the CASR for this docket calls for preliminary lists of issues and positions several weeks after the utilities' testimony is due, we do not at this point know what, if any, issues will be raised concerning the option payment. Thus, the purpose of my testimony is to address, in a general way, the Staff's reference to the upcoming fuel hearing in its Report and Recommendation in Docket No. 941155-EQ. An additional purpose of my testimony is to make myself available as a witness to respond to any questions concerning the Polk option payment to Tampa Electric which may be raised at the next fuel adjustment hearing.

Q. Do you think the fuel adjustment proceeding is an appropriate forum in which to examine any issues relative to the option payment from Polk to Tampa Electric?

A. No I do not. As I indicated during the Agenda Conference discussion on December 20, 1994 regarding the Tampa Electric/Orange Cogeneration/Polk assignments and contract modifications, Tampa Electric believes that the option payment was properly booked as "other electric revenues" and should <u>not</u> be subject to further examination, especially not in the context of a fuel adjustment proceeding. The option payment represents a contribution towards Tampa Electric's revenue requirement which might otherwise be required of the company's electric customers. This option payment of $1.1 million was in addition to the estimated $1.5 to $4.5 million in additional direct benefits which Tampa Electric's customers will receive as a result of modifications to the standard offer contract.

Q. In Staff's discussion under Issue 6 in the Tampa Electric/Orange Cogeneration/Polk docket, the Staff concluded that the option payment "may be more appropriately credited to Tampa Electric's capacity recovery clause because this is where the capacity payments to Qfs are recovered." Do you agree?

A. No I do not. First of all, this was not a capacity payment to a QF. It was a negotiated settlement amount and an alternative to Tampa Electric constructing a temporary interconnection with the Orange Cogeneration site at a cost of approximately $2 million. Had that construction been performed, the payment Polk would have made to Tampa Electric would have been booked as a contribution in aid of construction ("CIAC") and would not have been included in any recovery clause. Such a payment would not have been properly flowed through a capacity cost recovery clause. The mere fact that Tampa Electric agreed to a more cost effective alternative than a CIAC of approximately $2 million should not affect the regulatory treatment of the consideration Tampa Electric received in exchange for its consent to the assignments and modifications of the standard offer contract.

Q. Does this conclude your testimony?

A. Yes it does.

Q Would you please summarize, Mr. Mestas?

A Yes. The purpose of my testimony is to address the issue identified as No. 23A regarding whether an option payment from Polk Power Partners to Tampa Electric Company, which was booked above the line as "other electric revenues," should be treated as a credit in the capacity cost recovery clause examined during this fuel adjustment proceeding.

The option payment by Polk Power Partners was made possible because of a mutually acceptable series of negotiations between Polk Power Partners and Tampa Electric Company. It was not a refund of payments made by our customers. It was a function of Tampa Electric conducting a prudent business practice in our day-to-day operations, and it represents a contribution towards Tampa Electric's overall revenue requirements which might otherwise be required of the Company's electric customers.

We believe the option payment we received should be treated the same as any other revenues. In addition to the option payment, our customers will receive additional fuel savings of up to $4.5 million, additional benefits which the Staff has previously agreed are reasonable as a result of these negotiations. What we have accomplished is both fair and symmetrical for all parties.

The option payment was negotiated as a cost-effective alternative to otherwise construct in a temporary interconnection to the Orange Co. cogeneration site at a cost of approximately $2 million. Had the temporary interconnection construction been performed, the entire payment would have been booked as a contribution in aid of construction, and as such would not have been included in any recovery clause.

Since Tampa Electric is permitted to earn a return within an allowable range, we should be able to seek opportunities to optimize our revenues, as well as striving to identify ways to reduce our costs in order to meet our overall revenue requirements and defer the need for future rate increases.

We agreed to a cost-effective alternative to the $2 million CIAC, and we ask that you concur with our conclusion that the regulatory treatment of the consideration Tampa Electric received should not be affected by this fuel adjustment proceeding. We should not be penalized for making the right decision.

This concludes my summary.

MR. BEASLEY: We tender Mr. Mestas for cross examination.

COMMISSIONER DEASON: Mr. Howe?

MR. HOWE: Thank you.

CROSS EXAMINATION

BY MR. HOWE:

Q Hello, Mr. Mestas.

A Hello, Mr. Howe.

Q With reference to your prefiled testimony and your summary, the temporary interconnection with the Orange Co. cogeneration site that would have had to have been built at a cost of approximately $2 million, why would that construction have been necessary in the absence of the settlement?

A The settlement allowed a delay in providing capacity from that facility. Absent the delay, the interconnection would have been provided by Tampa Electric to Orange Co., which would have allowed them to deliver capacity at an earlier date.

There was some concern by Orange Co. that an interconnection which was under construction by another utility company, there was some concern as to whether or not that might be available in time to deliver capacity to meet the commitment.

Q If Tampa Electric had, in fact, constructed this interconnection, would Tampa Electric have incurred a cost of approximately $2 million?

A Yes.

Q So the Company would have had an expenses investment of approximately $2 million, which would have been offset by a receipt of CIAC in equal amount, would it not?

A That's exactly correct, which is why this is a more cost-effective alternative.

Q When Tampa Electric is billed by a qualifying facility, is it billed separately for capacity and energy?

A If Tampa Electric Company has a capacity contract with a cogeneration customer, there is a stream of capacity payments provided the customer meets the performance criteria that they are entitled to. The energy payments are determined generally on an hour-by-hour basis in terms of the payment. The payment to that customer generally group together in a single payment, but the calculation of those two parameters are calculated independently of one another.

Q Does Tampa Electric have a contract with Polk Power Partners for the payment of both capacity and energy?

A Yes, it does.

Q Is Tampa Electric currently receiving capacity and energy from Polk?

A Beginning in January of this year, we began to receive capacity and energy from Polk Power Partners. The option payment we are making reference to was made in October of 1993 and had absolutely nothing to do with capacity payments.

Q How was payment made? Was it a check from Polk to Tampa?

A Yes. It was a wire transfer.

Q Does the payment of that -- what's it called? An option payment?

A Yes.

Q Was the payment of the option payment by Polk, did that have the effect of reducing receipts to Polk from Tampa Electric by an amount of $1,106,760 over the life of the contract?

A No.

Q Why not? Wouldn't Polk have received an additional -- wouldn't the net effect of Polk be that they would receive an additional $1.1 million from Tampa Electric in the absence of the option payment?

A You are adding apples and oranges here. Let me clarify that a moment. The $1.1 million that we agreed upon in terms of an option, other than temporarily constructing the interconnection, was the option payment I made reference to.

In terms of Polk delivering capacity

commencing January of 1995, to the extent they delivered that capacity and met the performance requirements, then payment to Polk for the entire amount of capacity they delivered, would be made in full. So those are two separate issues.

Now, if you want to add the fact that they made a payment, an option payment, to us of 1.1 million and received something else from us in January of 1995, in fact, or the net results of those two transactions, then, of course, you will reach some different conclusion.

Q Well, the conclusion I necessarily reach, isn't it that Polk Power Partners will receive $1.1 million less from Tampa Electric?

A No, sir. Polk Power Partners will receive the full capacity payment for the capacity they provided to us in January of 1995 including the entire energy payment as well. As I mentioned a moment ago, those are calculated together and paid in one lump sum. And if you look at the capacity payment and the energy payment, then they received what was allowed for and provided for in the contract.

Q But their net total receipts in dollars from Tampa Electric would necessarily be the receipt of capacity payments and energy payments net of the cash they paid to Tampa Electric of $1.1 million, wouldn't it?

A Certainly, if you wanted to include that expense, that's correct.

Q Under the original contract between Tampa Electric and Polk, when was Polk scheduled to start providing the capacity and energy to Tampa Electric?

A In January of 1995.

Q What was the benefit to Polk Power Partners from entering into this option payment agreement?

A It provided them with two things. The benefit was, initially, as I mentioned a moment ago, it was to avoid the construction of a temporary interconnection which would allow the Orange Co. cogen facility to deliver capacity to Tampa Electric by January of 1995. In lieu of that, we provided Polk Power Partners with an opportunity to delay delivery from Orange Co. to Tampa Electric by six months if they elected to deliver that capacity to us from the Orange Co. facility.

In the interim, their Mulberry energy facility, which is the facility to whom we originally contracted, is providing the capacity and energy to us in January of 1995 as provided for in the original contract.

Q So is the only effect of this option payment to change the point of delivery?

A There are several things here with respect to the option payment. One is it's in lieu of an interconnection payment, a temporary interconnection payment, as I mentioned a moment ago. The other option is an opportunity for Polk Power Partners to allow their Orange Co. facility, if they elect that option, to allow their Orange Co. facility to deliver the capacity to Tampa Electric Company beginning in June of 1995.

Q Excuse me, you said June of 1995?

A July of 1995.

Q And what was the reference to the January 1995 date?

A Well, Mr. Howe, when this contract was originally entered into, the in-service date of the capacity to be provided Tampa Electric Company was to commence on January 1, 1995. That has occurred. That capacity is being delivered to Tampa Electric Company from the Mulberry energy facility beginning in January 1, 1995.

Based on modifications to the agreement that we entered into with Polk Power Company -- Polk Power Partners, which included a negotiation with respect to the interconnection I mentioned a moment ago, it also included some performance requirements that were modified to allow us to receive that capacity during on-peak hours, and things of that fashion, which resulted in the $4.5 million of additional fuel saving benefits I mentioned a moment ago.

And in addition to that package, in terms of the negotiations relative to that agreement, we allowed them an option to have the capacity that they intended to provide to Tampa Electric under contract provided from an alternate facility as of July of 1995. And in the interim until that point in time, they would continue to deliver the capacity from the Mulberry energy facility.

Q Was the Mulberry energy facility the point of delivery to Tampa Electric under the original contract?

A Mr. Howe, both of those facilities are located in Florida Power Corporation's territory, and the energy and the capacity would have been wheeled to Tampa Electric via an interchange with Florida Power Corp from either facility. So the delivery mechanism is unchanged irregardless of the location of the two facilities.

Now, the problem was that the interconnection from Florida Power Corp to Orange Co. was in suspect, in terms of having it available in time to effectuate the delivery of capacity from Orange to TECO, beginning in January of '95. Their facility is very close to our service area between the two utilities, and it would have been economically a reasonable option for them to pursue; to have us construct a temporary interconnection facility, which is what began the initial negotiations with respect to this entire matter.

You missed much of the discussion during the agenda conference, and to step in at this point, puts you at somewhat of a disadvantage.

Q If a settlement between Tampa Electric Company and Polk Power Partners had -- or hypothetically had gone the other way and it required Tampa Electric Company in advance of the effective date of the cogeneration contract to make a cash payment to a cogenerator of, let's say, $1.1 million, would Tampa Electric consider that to be either a fuel or purchased power cost for which it would be entitled to recovery through the fuel adjustment clause?

A I can't -- well, I was going to say I can't envision any circumstance or example that you've painted, but I can now; and the answer would be, yes. And the circumstance is such that in situations whereby the company advances capacity payments to cogenerators in advance of the in-service date, we call those early capacity payments. And as such, we may recover those payments from our customers in terms of the fuel adjustment, the capacity recovery clause.

Q Is the only difference the name given to the payment whether it's capacity payment or option payment?

A No. There is a tremendous amount of difference here. We are talking about two different things entirely.

This payment has absolutely nothing to do with capacity payments. This payment is in lieu, and was negotiated in lieu of us constructing an interconnection line to Orange Co. The capacity that Polk and Orange will ultimately deliver to Tampa Electric Company will be such that if they meet the performance requirements, they will receive compensation for capacity delivered, the full capacity delivered. And so our customers will be receiving what we contracted for.

Q Would you agree the net financial burden on Tampa Electric though for its complete business dealing with Polk Power Partners will be $1.1 million less?

A No, sir, I can't agree to that. If you look at the other alternatives that were possible, and you touched on one of them whereby the revenue and the expense, had the interconnection been constructed, would have been a wash as far as Tampa Electric was concerned under that particular example. And payments to the cogenerator for the capacity and energy he delivered to us, which is the same capacity and energy he is delivering to us today, would have been recovered as received, as those benefits were received, through the fuel adjustment clause.

So I'm not sure I understood your question or that I agreed with your other question.

MR. HOWE: I have no further questions.

MR. McWHIRTER: I have no questions of Mr. Mestas.

COMMISSIONER DEASON: Staff?

CROSS EXAMINATION

BY MS. BROWN:

Q Mr. Mestas, we are not going to get into the merits of the standard offer contract that was renegotiated by TECO and Polk because the Commission has already ruled on that. We are going to limit our questions just to the manner of treatment of the dollars associated with the option payment.

Now, in your testimony you stated that the option payment would have cost the cogenerator $1.1 million, or did cost the cogenerator $1.1 million, as opposed to $2 million that it would have cost the cogenerator to pay for a temporary interconnection cost; is that correct?

A That's approximately correct, yes, around there.

Q Yes?

A Yes.

Q The point I'm trying to stress here is that either way, the costs that came from the cogenerator -- the cogenerator paid the costs either way; is that correct? It reimbursed -- if it had built the interconnection, it would have had to reimburse Tampa Electric Company for the costs to construct that, correct?

A Yes. We would have had that expense, and they would have reimbursed us for that expense.

Q Yes. And as it was, they paid you $1 million to execute the option agreement instead, correct?

A That's correct.

Q So the costs that were associated with either one of those alternatives fell to the cogenerator, not to Tampa Electric?

A Well, as I mentioned a moment ago, we mutually just agreed. And it was a benefit to the cogenerator, but he now had $1 million in cost rather than $2 million in costs.

Q Let me repeat my question, and would you please answer yes or no?

A Yes, ma'am.

Q The answer is yes?

A It was a $1 million cost to the cogenerator.

Q To the cogenerator --

A Yes.

Q -- not to Tampa Electric Company. Thank you.

Tampa Electric Company, however, did receive the revenues from the option transaction, correct?

A Yes, ma'am.

Q Okay.

A But there's other electric revenues above the line.

Q Right. Tampa Electric Company received the benefits; the cogenerator paid the costs, correct?

A Both parties received benefits.

Q That is true. I agree with you on that.

Now, with respect to the standard offer contract, Tampa Electric Company has the obligation under the terms of that standard offer contract to make capacity and energy payments to Polk Power Partners -- I guess it's the Mulberry facility now. Is that correct?

A That's correct.

Q And as Mr. Howe was asking you, there are those two components of Tampa Electric Company's obligations under the standard offer contract: The capacity payment component and the energy payment component, correct?

A That's correct.

Q The capacity payment component remains fixed; is that correct?

A Well, it remains fixed for the life of the contract. But within that capacity payment stream are built in escalations, so it's not the same quantity; the payment stream is fixed.

Q It is fixed from the date of execution of the contract, correct?

A Yes.

Q The energy payment component, however, can fluctuate; is that correct?

A That is correct. It's based on the hour by hour of marginal costs or the average charge-out rate for our Big Bend 4 Unit, whichever is lesser.

Q And it can go up. If it fluctuates, it can go up and down, and is there a --

A It could never be greater than the average charge-out rate of Big Bend 4 Unit.

Q Right.

A But it generally would fluctuate below that; in the neighborhood of $11 to $12 in megawatt hours sometimes.

Q Now, the obligation that Tampa Electric

Company has under the terms of the standard offer contract to make these capacity payments and energy payments to Mulberry are recovered dollar for dollar from Tampa Electric Company's ratepayers through the capacity cost recovery clause; is that correct?

A To the extent those payments are made, yes, ma'am.

MS. BROWN: Just a second, Commissioner.

(Pause)

Q (By Ms. Brown) So TECO is, in essence, guaranteed dollar-for-dollar recovery of all payments to the cogenerator from the ratepayer; and the company bears none of the risks associated with any fluctuating energy costs that may arise under that contract, correct?

A The payments are based on avoided energy cost and, theoretically, it's cost that we would otherwise incur if the cogenerator were not there. So conceivably, if for some month or period of time the cogenerator was unable to perform and provide the contracted commodity, then conceivably we could provide it at our cost, and the impact on our customers would have been unchanged.

Q But as you say, conceivably, that could happen. What happens --

A Well, that is what happens.

Q But it hasn't -- all right.

Would you agree, though, that the capacity cost recovery clause is a dollar-for-dollar recovery mechanism?

A It's a dollar-for-dollar recovery mechanism for dollars spent by the customers for benefits received by the customers. In other words, the point I was trying to make earlier was that this option payment is unrelated to a capacity payment.

Our customers made no expenditure with respect to the contribution from Polk Power Companies for the avoidance of the interconnection. And it's why I thought that the timing, whereby I made reference to the option payment of October 1993 in the delivery of capacity to Tampa Electric Company from Polk Power, Polk Power Partners, beginning in January of 1995 -- January of 1995 was the first occasion our customers had to make the capacity payment for the benefits they received.

Q You state in your testimony that -- and you said here -- you credited the option payment to other electric revenues and that represents a contribution toward Tampa Electric's revenue requirement?

A Yes, ma'am.

Q And by "revenue requirement," you are

referring to money that Tampa Electric needs to cover its base rate costs and to earn a fair rate of return on its investment, correct?

A Yes, ma'am.

Q So when you speak of revenue requirement, you do not consider the money that TECO collects from its adjustment clause, such as the fuel and purchased power clause, to be part of the revenue requirement, correct?

A That's correct.

Q Would you agree that there are many factors that affect TECO's ability to achieve its base rate revenue requirement, such as mild weather, loss of customers or an increase in base rate costs?

A Yes.

Q So in any given year, TECO bears the risk of meeting its revenue requirement; is that correct?

A Yes.

Q Would you agree that as a general principle, the Commission attempts to match the benefits of a transaction to the risks of that transaction?

A I would think so, yes.

Q So if the ratepayers are bearing the risks of -- primarily bearing the risk of the cogeneration contract that you have with Mulberry, shouldn't they also receive the benefits?

A Please allow me to elaborate a moment on that response.

Q Can I have a "yes" or "no" answer?

A Give me the question again.

Q Would you agree, as a general principle, that if the ratepayers are going to bear the risks associated with the cogeneration contract that you have with Mulberry, that they should also receive the benefits?

A Yes. And if you'll allow me to elaborate a moment.

Q Go ahead.

A As I mentioned a moment ago, there are substantial benefits that the cogenerators are receiving with respect to this contract that they were not going to receive prior to the revisions or the negotiations to it. The additional $4.5 million which they will be direct beneficiaries of in terms of lower fuel cost, that is a direct benefit as a result of this negotiation, which they otherwise would not have received.

If you look at the combined benefits associated with this package, as far as I can tell, hopefully, there are three winners in this agreement. Everyone won.

Polk Power Partners won in that they resolved an issue that's half of what their costs otherwise would have been. Our ratepayers received benefits of $4.5 million or more that they otherwise would not have received. And Tampa Electric Company booked $1 million as other electric revenues -- $1.1 million as other electric revenues, above the line, to help us meet our expenses and to provide us an opportunity to earn within an allowable range of return. So, yes, they received benefits as we all did.

Let me focus on the risks a moment. That's the other side of the equation. Those are the benefits.

The contract that Tampa Electric Company entered into in late 1980 with Polk Power Partners, the standard offer contract that you made reference to a moment ago, envisioned risks associated with these contracts. And it included a discount, if you'll recall, an 80% full avoided cost discount such that the capacity purchases from cogenerators who executed that standard offer contract was discounted initially in order to offset some of the risks.

Number two, with respect to this agreement, there are no early capacity payments. There are no premature payments for capacity that our ratepayers must attempt to recover over the life of the contract.

The agreement we have with Polk Power Partners is if they deliver capacity, meet the performance criteria, they receive payment. If they don't, they don't.

So to the extent they fail to perform the capacity payments that we would otherwise use to purchase capacity from that customer, could be used to purchase capacity from other sources. Our customers are clearly better off today than they were prior to the negotiations.

Q I just have one final question. Tampa Electric was able to benefit from the option payment from Polk because of the standard offer contract that it had with Polk Power Partners, correct?

A I don't necessarily agree with that. Is that a question?

Q Yes.

A Okay. The way I would like to look at it is we had a contract with Polk Power Partners to deliver capacity beginning in January 1995. They are doing that.

They are doing that. The contract did not have to be changed for them to do that. What we did was we entered into a negotiation with them which allowed them to use a different facility to provide the capacity which was going to be wheeled to us in either event from Florida Power Corporation. And in lieu of building an interconnect to them to allow them to accomplish that by the in-service date, we provided them with an opportunity to delay that and delay building the line by granting them a six-month delay.

So I would like to look at the contract for the purchase of capacity and energy as separate for the negotiated agreement we made with the supplier.

MS. BROWN: No further questions.

COMMISSIONER DEASON: Commissioners, questions?

Mr. Mestas, I have a question. The temporary interconnection that was avoided, is it avoided totally now; or is it going to have to be constructed at some point?

WITNESS MESTAS: No, sir, it's totally avoided.

COMMISSIONER DEASON: Okay. And it would have been necessary to have constructed that so that the contracted-for capacity could have been provided at the anticipated due date?

WITNESS MESTAS: So that the contracted capacity from the Orange Co. facility could have been delivered to Tampa Electric on the in-service date from the Orange Co. facility.

COMMISSIONER DEASON: Now, how does Orange Co. fit into the future plans of TECO?

WITNESS MESTAS: Well, to the extent that thatcustomer exercises -- the Polk Power Partners exercises the option to have the Orange Co. facility deliver the remaining capacity commitment to Tampa Electric Company beginning in July of this year, then it will be the facility which provides a contracted capacity to us. It will be delivered to Florida Power Corporation, which will then, of course, deliver it to Tampa Electric Company.

Polk Power Partners is a holding company; and if you recall, they had the two facilities: The Mulberry energy facility and the Orange Co. facility And as I mentioned a moment ago, the Mulberry facility is providing the capacity based on the in-service date required by the cogen contract of January 1995.

Based on our negotiated agreement and the various terms that we spoke of at the agenda conference, the changing in the performance requirements and things of that fashion, they have an option that they can elect to provide that capacity to Tampa Electric Company from this alternate, the Orange Co. facility, if they elect to do so. And I would imagine they are going to exercise that option.

They had intended to provide the capacity totampa Electric Company from the Orange Co. facility on or before January 1995. But the thing that was delaying that was their concern about whether or not an interconnection would have been completed on time. That interconnection was the interconnection they were going to have with the Florida Power Corporation to that facility.

And so, because of that concern they negotiated with us about initially, well, could we provide a temporary interconnection to the Orange Co. site so that they could deliver the capacity to us? We said we could. As we discussed it further, we reached aconclusion that it would be in everybody's best interest that in lieu of spending $2 million to build something and then take it back down, all the parties could benefit by this option payment that we discussed earlier today.

COMMISSIONER DEASON: The Power Corp interconnection will be completed by July?

WITNESS MESTAS: Yes.

COMMISSIONER DEASON: Redirect?

MR. BEASLEY: I have no redirect, sir.

COMMISSIONER DEASON: And I believe there is no exhibit?

MR. BEASLEY: No exhibit.

COMMISSIONER DEASON: Okay. Very well.

Thank you, Mr. Mestas.

(Witness Mestas excused.)

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COMMISSIONER DEASON: That concludes all witnesses in the 01 docket?

MS. BROWN: Yes, it does, Commissioner.

COMMISSIONER DEASON: Okay. What is remaining in the 01 Docket?

MS. BROWN: What is remaining is the Commission's decision on the outstanding issues.

COMMISSIONER DEASON: Did we contemplate any type of closing argument or anything of that nature?

MS. BROWN: I think that would be appropriate here. It's not contemplated in the Prehearing Order; but because probably the Commission will want to make a bench decision in the case, I think that would give all the parties the opportunity to sum up.

COMMISSIONER DEASON: Okay. Well, I'm not going to do that now. We're going to move into 02.

To the extent parties wish to make closing statements, it may be tomorrow. And if they wish not to be here tomorrow, then they waive their right to closing statement. We are going to go into 02 at this time.

MR. KAUFMANN: Commissioner, before you do that, regarding closing arguments, is there the possibility, from what I can see from the Prehearing Order, of a briefing as an alternative?

We can do it on a pretty quick schedule, but I think that there is a lot of information that was brought out on these issues. And I think a better presentation could be made in the form of a brief.

COMMISSIONER DEASON: If you can write it tonight and present it tomorrow, that's fine. But we're going to have either a brief or closing argument tomorrow, and a decision will be made tomorrow.

MS. BROWN: Commissioner, if I might just point out for the record, on Page 4 of the Prehearing Order under "Posthearing Procedures" the first sentence reads: "Unless the Commission reaches a decision on the issues in this case from the bench, Rule 25-22.056 provides that the parties shall file posthearing statements."

COMMISSIONER DEASON: I'm sorry, where are you? You're on Page 4?

MS. BROWN: Page 4.

COMMISSIONER DEASON: Under?

MS. BROWN: Posthearing procedures.

COMMISSIONER DEASON: Okay.

MS. BROWN: The Prehearing Order contemplates that if the Commission decides to reach a bench decision in the fuel docket, there will be no posthearing filings.

COMMISSIONER DEASON: Very well.

We are going to move into 02.

MR. CHILDS: Commissioner, could I be excused on 01 until tomorrow morning? You're not going to proceed with 01 any further?

COMMISSIONER DEASON: I'll tell you what my plans are; we are going to work until 5:00.

MR. CHILDS: Okay.

COMMISSIONER DEASON: But we are not going to go past 5:00. If by some miracle we were going to conclude 02 and we can get to closing arguments on 01 before 5:00, we'll do it.

MR. CHILDS: All right, fine.

COMMISSIONER DEASON: But I don't know what the likelihood of that is. It may be that 02 will take us until 5:00.

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(Thereupon, the hearing adjourned at 4:00 p.m, to reconvene at 9:30 a.m., at the same location at the same address.)

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(Transcript continues in sequence in Volume 4.)