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August 17, 1998

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Ms. Blanca S. Bayo, Director
Division of Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, FL 32399-0850

Re: Petition by Tampa Electric Company for Approval of Cost Recovery for a new Environmental Program, the Big Bend Units 1 and 2 Flue Gas Desulfurization System: FPSC Docket No. 980693-E1

Dear Ms. Bayo:

Enclosed for filing in the above docket, on behalf of Tampa Electric Company, are the original and fifteen (15) copies of Rebuttal Testimony of Thomas L. Hernandez.

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

Thank you for your assistance in connection with this matter.

Sincerely,


James D. Beasley

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Enclosures

cc: All Parties of Record (w/enc.)

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1 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

2 REBUTTAL TESTIMONY

3 OF

4 THOMAS L. HERNANDEZ

5
6 Q. Please state your name, business address and position with
7 Tampa Electric Company.

8
9 A. My name is Thomas L. Hernandez. My business address is 702
10 North Franklin Street, Tampa, Florida, 33602. I am the Vice
11 President-Regulatory Affairs for TECO Energy, Tampa Electric
12 Company's parent.

13
14 Q. What is the purpose of your rebuttal testimony?

15
16 A. Through a series of issue identification conferences, the
17 parties have agreed that all issues relating to how costs
18 associated with Tampa Electric's proposed FGD system will be
19 recovered through the Environmental Cost Recovery Clause
20 (ECRC) would be more appropriately considered when Tampa
21 Electric requests authorization of an ECRC factor for recovery
22 of the FGD system. However, Florida Industrial Power Users
23 Group (FIPUG) witness Selecky has raised several issues which
24 appear to be related to cost recovery through the ECRC. The

1 purpose of my rebuttal testimony is to address the
2 deficiencies in Mr. Selecky's direct testimony.

3 Q. On page 3 and page 4 of his testimony, Mr. Selecky claims that
4 Tampa Electric's Petition for Cost Recovery is premature. How
5 do you respond?

6
7 A. I disagree with his assessment. First of all, we are not
8 seeking recovery of any of the actual costs associated with
9 our proposed FGD system in this proceeding. Instead, Tampa
10 Electric is seeking a determination by the Commission that the
11 proposed project is reasonable, prudent and the most cost-
12 effective means of complying with the SO₂ emissions
13 limitations of Phase II of the Clean Air Act Amendments
14 (CAAA). In addition, Tampa Electric is seeking confirmation
15 that the project-related costs determined by the Commission to
16 be reasonably and prudently incurred will be recovered through
17 the ECRC.

18
19 Tampa Electric has evaluated numerous alternatives in an
20 attempt to select the most appropriate and cost-effective
21 alternative available to the Company. All of our analyses
22 clearly indicate that the proposed FGD system is the most
23 cost-effective and otherwise appropriate means of achieving
24 this end. Mr. Selecky has presented no evidence to the
25 contrary.

1 Given the appropriateness of the FGD project, it is therefore
2 not premature to determine that the ECRC is the appropriate
3 mechanism for cost recovery of the FGD system. This
4 Commission has encouraged utilities to seek an early
5 determination for capital expended for environmental
6 compliance so that guidance can be provided by the Commission
7 with respect to such projects. Consequently, the Commission
8 should find that the proposed FGD project is the most cost-
9 effective alternative and is eligible for ECRC recovery at the
10 earliest possible time so that all parties can plan
11 accordingly.

12

13 Q. At page 3 of his testimony, Mr. Selecky repeats a legal
14 opinion given to him by counsel for FIPUG to the effect that
15 Tampa Electric was required, as a matter of law, to file under
16 Section 366.825, Florida Statutes (1997), for a prudence
17 review before seeking cost recovery. Mr. Selecky further
18 asserts that since Tampa Electric has not done so and, in his
19 view, has failed to provide the information required under the
20 above-mentioned Section, Tampa Electric's Petition in this
21 proceeding is premature. Do you agree?

22

23 A. Mr. Selecky is simply wrong in this assertion. I am not
24 testifying as a legal expert nor, to my knowledge, is Mr.
25 Selecky. However, the flaws in Mr. Selecky's assertions were

1 addressed directly in Tampa Electric's responses to the
2 motions to dismiss filed by FIPUG and OPC in this proceeding.

3

4 Q. On page 4 of his testimony, Mr. Selecky states that the
5 Company's proposal is premature because we do not know what
6 the Company's financial picture will be in the year 2000. How
7 do you respond?

8

9 A. This line of argument is not germane to this proceeding and
10 represents an effort to re-litigate an issue which has already
11 been squarely and unambiguously decided by this Commission.
12 In Docket No. 930613-EI, the Commission rejected the Office of
13 Public Counsel's attempt to relate ECRC recovery to Gulf's
14 earnings picture. The Commission states in Order No. PSC-94-
15 0044-FOF-EI:

16 Thus, we find that the legislature clearly intended
17 the recovery of investment carrying costs and O&M
18 expenses through the environmental cost recovery
19 clause. For this reason, Public Counsel's argument
20 must be rejected.

21 Accordingly, we find that if the utility is
22 currently earning a fair rate of return, that it
23 should be able to recover, upon petition, prudently
24 incurred environmental compliance costs through the
25 ECRC if such costs were incurred after the

1 effective date of the environmental compliance cost
2 legislation and if such costs are not being
3 recovered through any other cost recovery
4 mechanism.

5 In addition, this order is consistent with numerous decisions
6 by this Commission allowing cost recovery under the fuel,
7 capacity, conservation and environmental clauses for the
8 Florida investor-owned utilities that was not dependent on
9 earnings.

10

11 Since the Commission has already determined that earning
12 within an allowed return on equity range should not impact the
13 recovery of costs through the ECRC, it is not necessary to
14 address or speculate about the Company's financial status in
15 the year 2000 in order to consider the reasonableness and
16 prudence of the Company's proposal.

17

18 Q. On page 5 of his testimony, Mr. Selecky further states that
19 the FPSC should not decide whether to allow recovery through
20 the ECRC at this time because we will be making assumptions
21 about events that will not be known until 2000. Therefore, he
22 concludes, customers could be forced to pay rates that are
23 higher than the actual costs of providing service. Could you
24 please address Mr. Selecky's concern?

25

1 A. Yes. I disagree with his concern. The Company will only flow
2 costs through the ECRC that have been approved by the
3 Commission. These costs will be identifiable and prudent as
4 measured by the Commission, and will only be recovered after
5 the Commission has reviewed such costs. Therefore, customers
6 will never be "forced to pay rates that are higher than the
7 actual cost of providing service."

8
9 Q. Witness Selecky states that a different cost recovery
10 treatment or no cost recovery at all may be warranted because
11 the Company may earn in excess of its allowed return on equity
12 range. Could you please address this statement?

13
14 A. Yes. This Commission has an effective, continuing
15 surveillance program that assures that the Company is earning
16 within a return on equity range considered reasonable by the
17 Commission. Therefore, there should not be a concern that the
18 Company is overearning on its retail rate base at the same
19 time that it is recovering costs through the ECRC.

20
21 In addition, cost recovery through the ECRC is unrelated to
22 what the Company is earning on its rate base. The ECRC was
23 established by the legislature and has been implemented by
24 this Commission to provide for recovery of any environmental
25 compliance costs not recovered in base rates and which are

1 incurred after April 13, 1993. There has never been an
2 earnings test with respect to any of the various cost recovery
3 clauses. Neither the fuel, capacity, conservation or
4 environmental cost recovery clauses have an earnings test.

5

6 Q. Do you disagree with Mr. Selecky's conclusion that the
7 earnings cap mechanism currently in place prevents customers
8 from paying excessive rates (Mr. Selecky's direct testimony
9 beginning at page 6, line 8.)

10

11 A. I would say that his observation is irrelevant. Again, Tampa
12 Electric is not proposing actual cost recovery at this time.
13 Even if it were, the rate freeze or earnings cap is not
14 designed to prevent Tampa Electric from recovering otherwise
15 appropriate cost recovery amounts. The current rate freeze
16 has nothing to do with the appropriateness of Tampa Electric
17 recovering its environmental compliance costs after the rate
18 freeze expires. After the stipulation period, the
19 Commission's continuing surveillance program remains in effect
20 to monitor the level of the Company's earnings.

21

22 Q. On pages 7 and 8 of his testimony, Mr. Selecky, while
23 conceding that it is premature to address cost recovery issues
24 at this time, nevertheless goes on to suggest that wholesale

1 sales be allocated a share of the FGD System costs. How do
2 you respond to his proposed cost allocation?

3
4 A. The question of what costs will be allocated to the wholesale
5 jurisdiction should be raised, if at all, in an ECRC cost
6 recovery proceeding when Tampa Electric proposes to commence
7 cost recovery. We do not believe at this phase of the
8 proceeding that issues regarding cost allocation are relevant
9 to determining the reasonableness and prudence of the
10 Company's selection of its proposed FGD system as the most
11 cost-effective means of complying with Phase II of the CAAA
12 and the appropriateness of the ECRC as the recovery mechanism
13 of prudently incurred project-related costs.

14
15 In any event, it is clear that Mr. Selecky's concerns are
16 based on a misunderstanding of Tampa Electric's current cost
17 allocation practices. In the normal course of events, Tampa
18 Electric would allocate costs such as those related to the FGD
19 system to its retail and firm wholesale load, on an equal-
20 cents-per-Kwh basis. Therefore, Mr. Selecky's concerns with
21 regard to firm wholesale sales are unfounded. To the extent
22 that Mr. Selecky is suggesting that fixed costs, such as the
23 FGD- related costs, should be allocated to economy energy
24 sales, he is advocating a course of action which would be
25 illogical and unfair to retail and wholesale economy energy

1 customers alike. First of all, the allocation of fixed costs
2 to economy transactions is inconsistent with the economic
3 objective of engaging in such transactions and would lead to
4 a reduction in the number and volume of such transactions. As
5 a result, the retail ratepayers would suffer the loss of the
6 80 percent revenue credit of the margin earned by Tampa
7 Electric from these sales. In addition, the allocation of
8 such fixed costs to economy energy transactions would result
9 in double recovery of SO₂ compliance costs. To the extent
10 that economy energy transactions cause Tampa Electric to incur
11 incremental SO₂ compliance costs, those costs are
12 automatically included in the quotes made under the current
13 Florida Broker mechanism.

14

15 Q. Does this conclude your testimony?

16

17 A. Yes, it does.

18

19

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