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April 23, 2001

Blanca S. Bayo, Director  
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Re: Docket No.: 010283-EI

Dear Ms. Bayo:

On behalf of the Florida Industrial Power Users Group, enclosed for filing and distribution are the original and 15 copies of the following:

- ▶ Direct Testimony of Gerard J. Kordecki on behalf of the Florida Industrial Power Users Group.

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If you have any questions, please contact me. Thank you for your assistance.

Sincerely,

*Vicki Gordon Kaufman*

Vicki Gordon Kaufman

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cc: All Parties of Record

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DOCUMENT NUMBER - DATE  
05068 APR 23 2001  
FPSC-RECORDS/REPORTING

**BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**

In re: Calculation of gains and appropriate )  
regulatory treatment for non-separated )  
wholesale energy sales by investor-owned )  
electric utilities )  
\_\_\_\_\_ )

Docket No. 010283-EI

Filed: April 23, 2001

**DIRECT TESTIMONY**

**OF**

**GERARD J. KORDECKI**

**ON BEHALF OF**

**THE FLORIDA INDUSTRIAL POWER USERS GROUP**

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7 **DOCKET NO. 010283-EI**

8 **I. Introduction**

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

10 A. My name is Gerard J. Kordecki. My business address is 10301 Orange Grove Drive,  
11 Tampa, Florida 33618. I am self employed as an energy and regulatory consultant.

12 **Q. Please summarize your educational background and work experience.**

13 A. I received a Bachelor of Science degree in Advertising in 1963 and a Master of Arts in  
14 Marketing in 1965. Both degrees are from the University of Florida. I also pursued  
15 graduate study in Economics at the University of Florida. I worked for Tampa Electric  
16 Company for 33 years in various capacities involving marketing, conservation, resource  
17 planning and rates and regulation. I have participated in the development of and supervised  
18 the preparation of numerous studies and plans involving conservation goals and programs,  
19 cost allocations, rates, load research and resource plans. Since January 1999, I have  
20 consulted with power plant developers, merchant plant applicants and industrial and  
21 institutional utility customers on rates, regulatory policy and transmission access issues.

22 **Q. Mr. Kordecki, have you previously testified before the Florida Public Service**

1 **Commission ("FPSC" or "Commission")?**

2 A. Yes, I have testified regarding the subjects identified in my preceding answer on more  
3 than 36 occasions which included rate cases, determination of need hearings and various  
4 conservation dockets. I have also participated in a number of rule hearings, agenda  
5 conferences and Commission workshops.

6 **II. Background**

7 **Q. Describe some of the major changes you have observed during your 33 years**  
8 **experience in the electric industry in Florida.**

9 A. Before the 1980s, most wholesale sales were made to serve the native load requirements  
10 of the purchasing utility. In the late 1970s and early 1980s, the effect of OPEC on oil prices  
11 changed the power market. Those utilities with coal capacity sold to oil-burning utilities  
12 to displace high-priced oil units. Of course, this was only done when selling utilities did  
13 not need the lower cost capacity for their retail customers. Most of these transactions were  
14 done on the Florida Broker System. The savings were split between the seller and the buyer.  
15 There were little or no significant sales outside of Florida. A number of utilities built or  
16 purchased coal capacity in anticipation of even higher oil costs. In the 1980s, this was  
17 termed "oil-back out." The wholesale market continued to revolve around requirements  
18 sales and the as-available sales on the Florida broker to displace oil.

19 The 1990s brought about changes in capacity availability. Utilities built very few  
20 new generating units and cogeneration potential declined. This situation wasn't limited to  
21 Florida. It was widespread through the U.S. as supply tightened. The present shortages of  
22 capacity (California and the far West), which are familiar to everyone, are a result of this

1 lack of construction. Even the three Peninsular Florida IOUs are increasing their capacity  
2 levels by adopting a 20% reserve margin (up from 15%) for 2004.

3 FERC Order 888 brought about a second change in the market. This order required  
4 transmission-owning utilities to allow power suppliers (including IPPs, marketers, merchant  
5 plants, etc.) to use their transmission systems to make wholesale sales. Many of these  
6 FERC-defined utilities can sell energy at market-based rates--whatever the market will bear.  
7 In fact, all utilities in Florida have this market-based rate authority. Two, I believe, can only  
8 make market-based sales outside of Florida; however, this changes the "opportunity cost"  
9 for in-state wholesale sales when the purchases are to supply retail customers, specifically  
10 DSM and other non-firm customers.

11 In the late 1990s, and especially in the last two years, we find ourselves with  
12 dwindling capacity, broader markets due to expanded transmission access, and market  
13 pricing, which can take advantage of the lower reserves.

14 **Q. Mr. Kordecki, what effect do you believe these conditions have on Florida utilities**  
15 **today?**

16 A. When utilities were buying power, they were paying more. When they were selling,  
17 they could take advantage of higher pricing over a larger geographical area. Except for  
18 cost-based emergency sales, wholesale sales probably were made out of state, even if the  
19 energy could have been sold in state but at lower prices. So power that might have been  
20 sold on the Florida Broker in the 1980s may have been sold elsewhere. In state, there were  
21 probably situations where buying utilities were willing to make longer term purchase  
22 commitments to ensure themselves of power availability; that is, to be first in line.

1       **Q. Is your answer a condemnation of the buying and selling practices of Florida**  
2       **utilities?**

3       A. No, it is not a condemnation. The utility reactions to shortages in supply are very  
4       rational. On the selling side, it is good business, encouraged by FPSC incentives, to  
5       maximize profits for the good of retail customers. On the buying side, utilities try to obtain  
6       a reliable energy supply at the lowest cost. These should be the objectives of every utility  
7       trading floor. However, the concern in this volatile trading market is that retail customers  
8       not assume risks or higher costs because wholesale sales are not adequately or properly  
9       priced at the true costs of these discretionary sales.

10      **Q. What is your understanding of the events that have led up to this hearing?**

11      A. The Florida Commission Staff concluded that utilities no longer needed an incentive to  
12      make wholesale sales. It asked the Commission to consider doing away with the incentive.  
13      Utilities responded by suggesting that the incentive should be broadened. There have been  
14      a series of hearings focusing on the question of whether it continues to be necessary to offer  
15      incentives to investor-owned utilities to encourage them to maximize their wholesale sales.

16             On May 10, 2000, a hearing was held on this issue in Docket 991799-EI. As a result  
17      of that hearing, the Commission issued Order No. PSC-00-1744-PAA-EI on September 26,  
18      2000. This Order allowed incentives to be applied to all non-separated wholesale power  
19      sales that exceed a benchmark. The incentive applies to both firm and non-firm sales,  
20      except for emergency sales. The Commission also dealt with the calculation of gains and  
21      the appropriate regulatory treatment for revenues and expenses associated with non-  
22      separated wholesale power sales. This aspect of the Order was Proposed Agency Action

1 (PAA) because there was no issue or evidence presented in the May 10<sup>th</sup> hearing on this  
2 subject. On October 11, 2000, FIPUG filed a motion for clarification of parts I and II of the  
3 Order, protested part III of the Order, and requested a hearing on the PAA section.

4 FIPUG pointed out that the Order, as written, could ignore higher cost replacement  
5 purchased power when determining the cost of an incremental sale even if the cost of  
6 replacement power far exceeds any benefits retail customers would derive from the  
7 wholesale sale. FIPUG asserted that the Commission did not intend to design an incentive  
8 that might promote such a bizarre result.

9 The formula for calculating the gains on wholesale sales should consider all of the  
10 costs of the sale. When a utility lacks capacity to meet the demand of its retail customers  
11 because it has entered into a non-separated wholesale transaction, the cost of replacement  
12 power is not to serve retail customers, but should be considered a cost of the wholesale  
13 transaction, exclusive of other appropriate costs involved in the transaction. The  
14 assumption is that the Commission wants wholesale sales to be made when, and only when,  
15 captive customers, who bear the cost of the plant in rate base, benefit from the wholesale  
16 sale. The Commission should require that the marginal cost on the utility system, whether  
17 generated or purchased, should be used in the calculation of the cost of a non-separated sale.

18 FIPUG's second contention is that proper regulatory policy should prevent a utility  
19 from double collection of costs. No O&M costs collected from wholesale customers should  
20 be retained by the utility when these costs are already paid by retail customers in their base  
21 rates. When calculating gains from non-separated wholesale sales, no revenue recovered  
22 as O&M costs should be considered part of the gain to be divided between the utility and

1 customers because it is a cost reimbursement, not profit on the sale.

### 2 **III. Summary**

3 **Q. Please summarize the elements of your testimony.**

4 A. My testimony will address the issues raised by FIPUG in its protest and recommend  
5 "costs" which should be included in the calculation of the gains on making a wholesale sale.  
6 Such "costs" determine the margin or profit of an energy/capacity sale between utilities as  
7 defined by the Federal Energy Regulatory Commission (FERC). I will recommend a proper  
8 basis for determining the profit from applicable sales and a profit pooling mechanism that  
9 should be adopted to ensure that retail customers are protected against unwise wholesale  
10 sales.

11 **Q. What is the guiding principle for calculating the profit on these sales for the  
12 protection of retail customers?**

13 A. The revenues from non-separated sales must be reduced by removing the full costs  
14 attributable to the transaction. This procedure will protect retail customers from being  
15 required to subsidize the sale.

### 16 **IV. Types of Sales**

17 **Q. Are all wholesale sales the same?**

18 A. Not at all. There are numerous variations on the theme ranging from short-term  
19 emergency sales to long-term firm full requirements sales. In this case, we are dealing only  
20 with two broad categories of sales. These are firm and non-firm non-separated wholesale  
21 sales.

22 **Q. What do you mean by separated and non-separated sales?**



1 A. Separated sales are wholesale sales in which the generating plant, ancillary assets and  
2 all allocated expenses are removed from the rate base for ratemaking purposes. The utility  
3 keeps all the revenue from the sales and bears all of the expense related to the sale. Non-  
4 separated sales are wholesale sales in which the assets remain in the retail rate base. All  
5 revenue is allocated to retail customers and all fixed costs are borne by retail customers.

6 **Q. Define a non-separated sale.**

7 A. As stated above, a non-separated sale involves a sale where the utility has not broken  
8 out the cost components of the wholesale transaction and reduced its retail rate base for  
9 those components. The revenues from non-separated sales must be reduced by their "costs"  
10 so retail ratepayers do not subsidize wholesale transactions. The remainder or profit is  
11 distributed to retail customers or shared by retail customers and the utility, depending on  
12 whether the utility has met a sales or incentive benchmark.

13 **Q. What types of wholesale sales are classified as non-separated?**

14 A. Most non-separated sales are non-firm transactions, no longer than a year. Also  
15 included are firm sales of less than one year, and there may be some seasonal non-firm sales  
16 and sales which have some level of firmness depending on certain circumstances or events.  
17 Examples of sales with some degree of firmness might be a sale from a single generating  
18 unit (unit power sale), which is a firm sale only while the unit is on line. If the unit has a  
19 forced or planned outage, the sale is discontinued. Another example might be a reservation  
20 sale in which Utility A contracts with Utility B to make a purchase (normally over an  
21 extended period of time). The purchasing Utility A pays a fee to have the right of purchase,  
22 but it must notify the selling Utility B a set number of hours in advance on the day before

1 Utility A takes the capacity. At the point of notification, if Utility B has the power, the  
2 purchase for the next day becomes firm. There are an infinite number of ways to structure  
3 transactions which may have some level of firmness.

4 **Q. When does the distinction between separated and non-separated sales become**  
5 **important to customers?**

6 A. Generally only when there is a rate case or when rates are under a return on equity  
7 ceiling that requires a refund to customers when the ceiling is breached. Classification of  
8 a sale is important to utilities because it affects their stated regulatory earnings. Utilities file  
9 monthly earnings surveillance reports. If a sale is separated between rate cases, it doesn't  
10 affect base rates of retail customers, but it may trigger an over earnings situation. In the  
11 case of both separated and non-separated sales, the allocation of fuel costs is most important  
12 in protecting retail customers.

13 **Q. Why do customers benefit from non-separated wholesale sales?**

14 A. Retail customers pay base rates that cover the capital carrying costs and the fixed O&M  
15 expenses attributable to facilities in the retail rate base. However, retail customers do not  
16 require use of the generation capacity 100% of the time. When capacity is not being used  
17 to serve the retail load, retail customers can benefit from off-system wholesale sales if the  
18 revenue from these sales is used to reduce the utility's fuel cost recovery factor or other  
19 costs recovered through the cost recovery clauses.

20 Customers will always appear to "benefit" from a wholesale sale any time the sales  
21 revenue exceeds incremental sale costs. Sales of unneeded capacity should be encouraged,  
22 but care needs to be taken in today's active wholesale market that the incentive to make

1 wholesale sales does not backfire and encourage off-system sales when capacity is needed  
2 to serve retail customers. If the utility can keep any portion of the revenue from off-system  
3 sales, but not face any risk when the rate-based capacity is diverted to wholesale  
4 transactions, then there is no corresponding disincentive to avoid risky wholesale sales.

5 **Q. What differentiates firm sales from non-firm sales?**

6 A. Utilities may enter into binding contracts with wholesale customers to maintain a firm  
7 supply of power to a wholesale customer, regardless of if the sale eventually proves to be  
8 profitable or unprofitable. For example, if Utility A has a sale to City C which will supply  
9 City C's full electrical requirements for more than one year, this would be a firm sale that  
10 should be separated from Utility A's rate base to accurately reflect its earnings. If the sale  
11 were less than one year, it would be a non-separated sale.

12 Non-firm sales may be recallable by the utility if capacity is needed to serve retail  
13 and wholesale requirements or to supply capacity to another utility which is in an  
14 emergency capacity situation. Let's say Utility A is making a non-firm sale to Utility B.  
15 Utility A's retail load rises to a level which requires Utility A to discontinue or recall the  
16 sale to Utility B. The key element of this non-firm sale is that there should be a superior  
17 obligation (meeting retail demand) which the selling Utility A should meet before it can  
18 make or continue a sale to Utility B.

19 **Q. Are utilities required to recall a non-firm sale in order to serve retail customers?**

20 A. By stated custom, yes, but not by FPSC mandate. It is my opinion that the FPSC should  
21 assert its authority to ensure that there is no doubt as to the regulatory policy of the state on  
22 this subject. The practice has been to recall the non-firm sales in capacity shortfall

1 situations. It is my opinion that FIPUG is correct that a utility should be required to recall  
2 a non-firm sale in order to meet retail load demand. Now that the expanded shareholder  
3 incentive covers all wholesale sales, excluding firm long-term transactions, FIPUG has  
4 expressed legitimate concern that a utility may be tempted to maintain or enter into a non-  
5 firm sale to the detriment of its retail customers, and specifically, its non-firm retail  
6 customers.

7 **Q. How can non-firm wholesale sales that are not recalled affect non-firm retail**  
8 **customers?**

9 A. Non-firm retail customers may be forced to purchase optional power or even be  
10 interrupted while the utility is making a wholesale sale. Non-firm customers pay for the  
11 capacity in their overall retail rates, though these rates may be less than firm customers'  
12 rates. Non-firm customers pay less for this capacity because they have volunteered to be  
13 interrupted or purchase third-party option power when capacity is needed by a utility to  
14 protect its firm retail load. Non-firm customers were not informed and they did not bargain  
15 for the utility to use their loads as a vehicle to make wholesale sales.

16 **Q. Is there a difference between a non-separated firm sale and a non-firm sale during**  
17 **a capacity shortage?**

18 A. Yes, a non-separated firm sale normally has no recall rights unless conditions or events  
19 for recall are explicitly stated in the contract. Typically, there are no recall rights in firm  
20 sales contracts. If Utility A is in a capacity shortage, it must attempt to purchase power on  
21 the wholesale market to meet its obligations to serve retail and wholesale customers. If the  
22 capacity shortage occurs at a time when the utility is making wholesale sales, logic would

1 dictate that the replacement power is being purchased to serve the wholesale sale, not the  
2 retail customers, who should have a higher priority of service from the utility's capacity.  
3 Utility A should not be allowed to purchase power and pass those costs directly through to  
4 retail customers via a recovery clause, but this can happen if care is not taken to prevent it.  
5 If Utility A cannot find enough power to cover its firm wholesale and retail demand, it can  
6 interrupt non-firm retail customers (interruptible, load management and curtailable). In this  
7 example, the costs incurred during the capacity shortfall are borne by the utility's non-firm  
8 customers who essentially "pay" so Utility A can make a wholesale sale to another utility.  
9 The potential adverse effects of a firm wholesale sale or a non-firm sale that is not recalled  
10 during a capacity shortage are, for all practical purposes, the same. There is the real  
11 potential for the costs of these sales to be inappropriately shifted to retail customers.

## 12 **V. FIPUG's Protest**

13 **Q. Mr. Kordecki, with the above background in mind, describe FIPUG's protest.**

14 A. Order No. PSC-00-1744-PAA-EI, Section III-Calculation of Gains and Appropriate  
15 Regulatory Treatment, contains four findings by the Commission which are the subject of  
16 this hearing. FIPUG has no disagreement with the general principles of the Commission  
17 decision but believes more specificity in the application of those principles is needed to  
18 equitably deal with the costs of wholesale transactions so that retail ratepayers are held  
19 harmless.

20 **Q. Describe the first aspect of the PAA Order which requires more specificity.**

21 A. Item #1 of the PAA states:

22 Each IOU shall credit its fuel and purchased power costs recovery

1 clause for an amount equal to the incremental cost of generating the  
2 energy for each sale.

3  
4 **Q. What is FIPUG's concern with this statement?**

5 A. The proper costing of incremental wholesale sales helps the Commission determine  
6 how well the utility is managing its assets in meeting its obligation of supplying reliable  
7 power at reasonable rates. If marginal or incremental costs are properly estimated, then  
8 cross-subsidy issues between retail customers and wholesale customers are minimized when  
9 making wholesale transactions. If there are any purchased power costs which are higher  
10 than the utility's marginal generating costs of its units, such cost must be included as the  
11 cost of the non-separated sale. When purchased power is the highest cost power on the  
12 utility system, it is the incremental cost.

13 **Q. Can you give us some examples?**

14 A. Yes. Let's say a utility is making a short-term firm sale of 100 megawatts at  
15 \$55/MWH of which \$45/MWH is considered the incremental cost (fuel \$40 and \$5 for  
16 everything else). A capacity shortfall occurs and the utility cannot meet its retail and  
17 wholesale requirements (in this example, the utility has no non-firm load). The utility then  
18 purchases 100 megawatts at \$70/MWH for five hours in the afternoon. In the calculation  
19 of the incremental costs of the 100 megawatt sale, the incremental costs in those five hours  
20 becomes \$70 plus any incremental "other" costs. In the calculation of the costs of the non-  
21 separated transaction, the \$70/MWH should be averaged into the calculation of the  
22 incremental costs of the sale.

23 Now we change the utility load from all firm to include 100 megawatts of non-firm

1 load. The utility has a third-party option purchase provision in its tariff. The same  
2 anticipated capacity shortfall occurs and a purchase will be made by the utility. The  
3 incremental cost to make the 100 megawatt sale and maintain the retail and wholesale  
4 requirements is the same as the earlier example, where the utility had all firm retail load.  
5 The question posed in this example is: should the utility treat the purchase as part of the  
6 incremental cost to make the sale or should the utility be allowed to pass through the  
7 purchase costs of the 100 megawatt purchase to those customers whose non-firm tariffs  
8 have a third-party purchase option. The proper costing procedure is to count the 100  
9 megawatt purchase as a part of the incremental cost of the sale. The existence of non-firm  
10 load is to help protect firm load from interruptions during capacity shortfalls. Non-firm  
11 load was never intended to help the utility make or protect off-system wholesale sales.

12 **Q. Your example describes the utility making a 100 megawatt firm non-separated**  
13 **sale. What are the consequences if the sale is non-firm?**

14 A. If the utility does not recall the non-firm sale, the results are identical to a firm sale.  
15 The Commission should require non-firm wholesale sales to be recalled during a capacity  
16 shortfall. Without a recall requirement, the Commission should use the incremental cost  
17 treatment previously described so that retail customers are protected from unreasonable  
18 costs.

19 **Q. You have discussed situations where a utility finds itself both selling and buying**  
20 **in order to maintain a non-separated wholesale sale. If we change the example so that**  
21 **there is no purchased power available to cover the incremental sale during the**  
22 **capacity shortfall, what should the Commission require?**

1 A. I would hope that the utility would recall the sale voluntarily. If the sale is firm or  
2 not recalled, customers will be cycled or interrupted. Some type of credit amount taken  
3 from the proceeds of the sales should be credited to the affected customers. A credit would  
4 reflect that retail customers were adversely affected by a sale that was not in their best  
5 interest. A credit for megawatts interrupted would also be appropriate. The marginal costs  
6 of third-party purchases or marginal power purchases for firm power should be applied to  
7 the estimated hourly megawatts and refunded to affected customers.

8 **Q. What incentive is there for a utility to make sales that would adversely affect**  
9 **retail customers?**

10 A. My comments are not meant to assert that utilities would intentionally make  
11 imprudent wholesale sales from their perspective. I am sure that their various planning  
12 groups and trading floors look at incremental sales with great diligence. But there can  
13 always be unforeseen events, such as unit forced outages, higher loads than forecasted etc.,  
14 which may cause "unintended consequences" which result in higher costs which may be  
15 borne inequitably among the classes of customers. All incremental sales are made from  
16 reserves or excess capacity. When a utility uses non-firm load as part of its reserves and has  
17 a significant amount of its reserves supplied by non-firm load, aggressive wholesale sales  
18 activity can lead to higher incidences of "unintended consequences." The risks of  
19 interruptions or high cost third-party purchases for customers with this purchase provision  
20 increase when utilities have incentives to make more wholesale sales and are able to lay off  
21 the risks to retail customers.

22 **Q. What can be done to limit the risks of higher costs to retail ratepayers from**



1       **wholesale transactions?**

2       A.     The following measures would help mitigate the risk:

3           1.     Each non-separated sale should be priced at the marginal cost of the sale, as  
4       discussed earlier; and

5           2.     A cumulative profit pool should be adopted for all non-separated sales.

6       **Q.     Explain how the cumulative profit pool would work.**

7       A.     When sales are properly costed, there may be instances when a non-separated sale  
8       is not profitable and incurs a loss. Hopefully, most sales will result in gains. The fuel factor  
9       is only adjusted annually; therefore, instead of dealing with each sale individually, the net  
10      revenues or profits should be accumulated for all non-separated sales, whether firm or non-  
11      firm. To the extent there are losses from some sales and credits from others, these losses  
12      and credits would be netted against the profit pool. This would ensure that there are truly  
13      benefits to customers before an incentive is paid to the utility. Total incremental costs of  
14      sales should be accounted for before any incentive mechanism is applied.

15      **Q.     What is the second aspect of the PAA that concerns FIPUG?**

16      A.     Item 3 of the PAA provides:

17           Each IOU shall credit its operating revenues for an amount equal to  
18           the incremental operating and maintenance (O&M) costs of  
19           generating the energy for each such sale.  
20

21      O&M costs are hard to quantify; it is even more difficult to identify O&M expenses that are  
22      not already being collected in the utility's base rates. All O&M expenses charged to a  
23      wholesale transaction should be credited back 100% to the appropriate clause(s) unless a

1 utility supports the charge as a cost which is incremental to any present costs being  
2 collected by the utility in its base rates. If a cost is truly incremental, it may be appropriate  
3 to charge the sales with the cost and credit the utility's operating revenues. The utility  
4 carries a heavy burden of proof that a cost is incremental before any credit to operating  
5 revenues should occur. Remember that between rate cases and earnings restrictions, the  
6 utilities keep all revenue. It is appropriate for the utility to keep all revenue if it is an  
7 incremental cost recovery, but not appropriate for the utility to keep 100% of the money  
8 without sharing, if retail customers have already paid the cost through retail base rates.

9 **Q. What are the other items covered by the PAA?**

10 A. The second item in the PAA is:

11 Except for FPC, each IOU shall credit its environmental cost recovery  
12 clause for an amount equal to the incremental SO2 emission  
13 allowance cost of generating the energy for each such sale. FPC,  
14 because it does not have an environmental cost recovery clause, shall  
15 credit this cost to its fuel and cost recovery clause.  
16

17 It is my opinion that this is any appropriate cost that should be credited to the  
18 environmental cost recovery clause.

19 The last PAA item concerns transmission and capacity revenues and says:

20 In accordance with Order No. FPSC-99-2512-FOF-EI, issued  
21 December 22, 1999, in Docket No. 990001-EI, each IOU shall credit  
22 its capacity cost recovery clause for an amount equal to any  
23 transmission revenues or separately identifiable capacity revenues.  
24

25 Transmission and capacity costs paid to third parties in order to make a non-  
26 separated sale are part of the incremental cost of the sale. It should be clarified that these

1 costs should be removed from the revenues before profit on the sale is calculated and will  
2 be removed from the margin. Crediting is appropriate for transmission revenues and  
3 separately identifiable capacity revenues but a more accurate method would be to credit the  
4 fuel clause for non-firm transmission transactions and credit the capacity clause for firm  
5 transmission transactions. In this manner, revenue would track the firmness of assets and  
6 not credit capacity when there is no firm transmission capacity obligation.

7 **Q. Mr. Kordecki, please summarize your testimony.**

8 A. My testimony describes protections against some potential "unintended  
9 consequences" which may occur with aggressive wholesale sales activities among  
10 Commission jurisdictional utilities. If we think of these sales as new incremental sales to  
11 a utility system, then their costs should be treated as incremental. I recommend the  
12 following procedures be applied to non-separated wholesale sales:

13 • Each utility shall credit its fuel and purchase power recovery clause for an amount  
14 equal to the incremental fuel cost of generating the energy for each such sale. In the  
15 event wholesale power is purchased to serve retail load while non-separated sales  
16 are being made, the highest cost fuel shall be allocated to the wholesale sale not to  
17 the purchase used to meet retail load.

18  
19 If incremental crediting of the higher of either generated or purchased power costs is used  
20 for incremental non-separated sales, risks of higher cost to retail customers or non-firm  
21 retail customers due to these sales should be negated. The proper costs will be assigned to  
22 the cost causer-- the non-separated sales.

23 • All O&M costs assigned to non-separated sales should be treated as a cost and  
24 credited back to the fuel and/or capacity clause.

25  
26 If a utility can prove by clear and convincing evidence that the O&M cost is incremental,

1       that is, does not already exist in the retail customers' base rates and that no costs would exist  
2       without the sale, then and only then, can the O&M cost be taken from the margin or profit  
3       of the sale and credited back to the utility's operating revenues.

4       **Q.     Does this conclude your direct testimony?**

5       A.     Yes.

## CERTIFICATE OF SERVICE

I **HEREBY CERTIFY** that a copy of the foregoing Direct Testimony of Gerard J. Kordecki on Behalf of the Florida Industrial Power Users Group has been furnished by (\*) hand delivery, or U.S. Mail this 23rd day of April, 2001, to the following:

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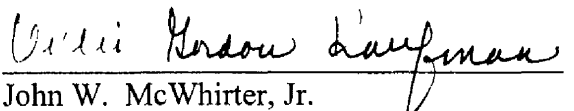
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