TESTIMONY OF C. MARTIN MENNES

DOCKET NO. 001148-EI

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Docket No. 001148-EI
Florida Power & Light Witness Mennes
Exhibit No. __ (CMM-_)
Direct Testimony

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Review of Florida Power & Light Company's proposed merger with Entergy Corporation, the formation of a Florida transmission company ("Florida transco"), and their effect on FPL's retail rates.	**DOCKET NO. 001148-EI**

TESTIMONY OF
C. MARTIN MENNES

Q. Please state your name and occupation.

A. My name is C. Martin Mennes. I am Vice President, Transmission, Operations and Planning of Florida Power & Light Company ("FPL").

Q. Please briefly describe your educational and business experience.

A. I graduated with Honors from the University of Florida. I have a Post Graduate Certificate of Proficiency in Electrical Engineering from the University of Miami and completed the Program for Management Development from the Harvard University Graduate School of Business.

I began working at FPL in 1968 in the area of protective relay and control systems. Since then I have held the positions of Manager of System Protections, Manager of System Operations, Manager of Bulk Power Markets, and Director of Power Supply. In February 2000 I assumed my present position.

I am a registered Professional Engineer in the State of Florida. My industry related activities outside of Florida include serving as chairman of the following:

North American Electric Reliability Council ("NERC") Performance Subcommittee, NERC Security Coordinator Subcommittee, and Southeastern Electric Reliability Council ("SERC") Operating Committee. I am presently serving as vice chairman for the NERC Market Interface Committee and I am on the NERC Technical Steering Committee.

Q. What is the purpose of your testimony in this proceeding?

A. I am presenting testimony addressing two issues on behalf of FPL. First, I will address FPL's decision to transfer ownership of its transmission assets to GridFlorida. Second, I will address what Mr. Holcombe describes in his testimony as FPL's "cost off-sets" (which are included in his Exhibit BLH-3). In his testimony, Mr. Holcombe addresses the reasonableness of the estimated start up costs and preliminary annual operating budget for GridFlorida, and the amount of these costs properly considered to be additional costs associated with GridFlorida's establishment. The "cost off-sets" in Mr. Holcombe's testimony represent those costs that would have been incurred by the GridFlorida Companies (FPL, Tampa Electric Company, and Florida Power Corporation) even without GridFlorida formation, as well as those costs the Companies will no longer incur after GridFlorida commences operations. To determine the additional cost associated with GridFlorida, Mr. Holcombe reduces the total costs of GridFlorida by the cost off-sets.

These matters relate to Issues 4 and 5 in Prehearing Order No. PSC-01-1485-PSCO-EI.

Q. Are you sponsoring any exhibits to your direct testimony?

A. No.

I. DECISION TO TRANSFER OWNERSHIP OF TRANSMISSION ASSETS

Q. Please explain why FPL participated in the development of a Regional Transmission Organization ("RTO").

A. As explained by Messrs. Hoecker and Naeve, the Federal Energy Regulatory Commission ("FERC") in Order No. 2000 required FPL to join a FERC-approved RTO under the timetable included in that Order. Shortly after FERC issued Order No. 2000, FPL began analyzing the options available to it to comply with FERC's requirements. FPL concluded that there are a number of benefits to active participation in RTO development, including the ability to provide meaningful and timely input during the formation process to help ensure that the RTO would benefit FPL customers.

Q. Were there alternative approaches available to FPL?

A. The alternative to active participation was to take a wait-and-see approach to RTO formation. This approach, however, would result in substantial risk that FERC would require FPL to join an RTO developed by others without regard to Florida's specific circumstances and needs. FPL did not consider this as a viable alternative, as it would not benefit FPL's customers.

Q. What factors did FPL consider when developing an RTO?

A. First and foremost, FPL was concerned that any RTO in which it would participate would benefit FPL's customers. That is, FPL wanted to ensure that the RTO would be

structured to ensure that it would continue to provide reliable service and make proper short- and long-term decisions that minimize costs consistent with the need to maintain reliability. This includes ensuring that the RTO would plan for necessary facilities to meet future needs and take all steps necessary such that those facilities would be constructed.

Q. Did the specific goals included in Order No. 2000 affect the Company's evaluation?

A. Yes. As a general matter, FERC's goals in Order No. 2000 are consistent with those I just enunciated, i.e., ensuring reliable service at reasonable cost. Order No. 2000's goals thus reinforced the goals that FPL felt must be satisfied in forming an RTO.

Q. Did these goals influence FPL's decision regarding a proper structure for an RTO?

A. Yes. Once it determined the goals it was trying to accomplish, FPL analyzed the two basic approaches to RTO formation to determine how best to satisfy those goals: A for-profit transmission company ("Transco") and a non-profit independent system operator ("ISO"). FPL determined that a for-profit Transco is the best way to meet the goals of efficiency and reliability that would benefit FPL's customers.

Q. Why did FPL determine that a for-profit Transco is a better option than a non-profit ISO?

A. After analyzing the poor performance of and high costs associated with most ISOs developed in other regions of the country, most notably California, New York, and New England, FPL believed, and continues to believe, that a for-profit Transco is the

most efficient structure for satisfying Order No. 2000. Based on these other experiences, FPL believes that ISOs, which are not accountable to anyone and have no interest in ensuring that costs are efficiently incurred, do not have proper incentives to operate efficiently or attempt to reduce costs. A for-profit Transco, on the other hand, will seek to meet its earnings projections, and thus will have proper incentives to minimize costs to do so. Also, a for-profit Transco can have proper incentives to efficiently operate the transmission system. Finally, a Transco that owns assets will have greater financial strength, and thus will have access to capital when it needs it and at lower cost than a non-profit ISO. These attributes of a for-profit Transco ultimately benefit customers through low cost, reliable service.

Q. Why did FPL decide that it would transfer ownership of its transmission facilities to GridFlorida?

A. FPL had a serious concern that without its assets a Transco in Florida would not be successful, as FPL owns approximately half the transmission facilities in the State. One reason for FPL's concern was its belief that a Transco will need to own significant assets for a successful Initial Public Offering ("IPO"), as investors in a company are buying a piece of that company, and thus want to ensure that the company has sufficient assets to operate efficiently. An IPO is important because it will provide funds the Transco needs and increase the accountability of the directors and officers of the Transco (and thus independence).

Q. Was this decision premised on a particular structure for the Transco?

A. Yes. FPL's decision was premised on the expected structure of GridFlorida as filed with, and approved by, FERC. In particular, FPL's decision was premised on transferring ownership of its assets to a Transco in Florida that will be the RTO. If a structure or RTO is adopted that is different than GridFlorida as approved by FERC, and FPL is encouraged or required to participate, FPL will need to re-analyze whether transferring ownership of its facilities continues to be appropriate.

II. COST OFF-SETS

Q. Please describe the "cost off-sets" used by Mr. Holcombe in his testimony to develop the costs properly attributed to GridFlorida.

A. As I explain above, the "cost off-sets" in Mr. Holcombe's testimony represent those costs that would have been incurred by the GridFlorida Companies even without GridFlorida formation, as well as those costs the Companies will no longer incur after GridFlorida commences operations. The cost off-sets are used by Mr. Holcombe to determine the additional cost associated with GridFlorida, i.e., Mr. Holcombe reduces the estimated total costs of GridFlorida by the cost off-sets to determine the incremental costs associated with GridFlorida. The cost off-sets are included in Exhibit BLH-3, Tables 1 and 2.

Q. Please explain the rationale for the costs off-sets.

A. A useful analogy is to consider how one determines the additional operating costs of a new car. One cannot simply look at the fact that the new car will require $20 a week in gasoline and assume that the new automobile results in an additional fuel cost each week of $20. If it used to cost $15 a week in gas for the old car, the additional cost of

the new car is only $5. Similarly, if the old car on average required $3 a week in maintenance costs, but the new car is under warranty and thus will not have any out-of-pocket maintenance costs, that amount should be deducted from the total cost of the new car to determine the car's additional cost. As this example shows, costs that would have been incurred with the old car, as well as those costs that no longer will be incurred, must be considered when determining the additional costs associated with the new car.

A. Incremental Start-Up Costs

Q. Please describe generally where the FPL estimated cost off-sets are included in Table 1 to Exhibit No. BLH-3.

A. The FPL estimated costs Mr. Holcombe uses as off-sets to GridFlorida start-up costs are included in columns 7 and 10 of BLH-3, Table 1. Column 7 describes the FPL estimated costs associated with retail load, and column 10 represents estimated costs associated with wholesale load (all of which in Table 1 represents FPL costs).

Q. Please explain GridFlorida Facilities Project costs, and the FPL off-set thereto, included in Mr. Holcombe's testimony.

A. GridFlorida's Facilities Project costs, which are included at column 1, line 3 of Table 1, represent GridFlorida's costs associated with building spaces, e.g., the costs associated with procuring and managing headquarter facilities, back-up facilities, and a control center. The FPL offset of $635,000 ($588,000 associated with retail load, included in column 7, line 3 of the Table, and $47,000 associated with wholesale load included in column 10, line 3) consists of the estimated cost to GridFlorida associated

with the lease by GridFlorida of three FPL facilities prior to commercial operations. The costs are off-sets because they do not represent an additional cost above what FPL's effective costs for the building spaces would have been even if GridFlorida was not formed. That is, these are costs that FPL would have incurred absent GridFlorida, but effectively is avoiding as a result of the lease payments.

Q. What are the three leases included in the FPL off-set to GridFlorida's Facilities Project costs?

A. The FPL off-set is associated with the following leases:

- $107,607 for building lease fees associated with leasing 11,000 sq. ft. of the FPL control center. This figure represents the cost to GridFlorida to lease the facility for 90 days prior to commercial operations, with the remainder included in the annual lease costs.
- $495,000 for building lease fees associated with leasing office space at the FPL control center for 12 months prior to commercial operations. This figure assumes 50 project personnel, with an average of 250 sq. ft. per person at an estimated cost of $39.13 per sq. ft., plus approximately $6,000 to lease 50 workstations.
- $32,400 for building lease fees to lease the disaster control facility for 12 months prior to commercial operations. This figure is based on a 1,200 sq. ft. facility at the FPL Customer Service Center East at $27 per sq. ft.

Q. Please explain the FPL estimated cost off-set associated with System Operations.

A. System Operations costs are included at line 4 of Table 1. The off-set for FPL estimated costs is $10,985,000 ($10,171,000 in column 7 and $814,000 in column 10). This figure represents an estimate of the allocation of costs for FPL's EMS system to GridFlorida. Like the leases, this cost is an offset because it is not a new cost that results from establishing GridFlorida. Instead, it represents an allocation of costs FPL would be incurring whether or not GridFlorida was established.

Q. Please describe briefly how those costs were allocated.

A. All applications that will be shared by FPL and GridFlorida were allocated based on the number of SCADA points associated with transmission functions. Licensing costs also were allocated using the same methodology, except to the extent license restrictions prohibit GridFlorida from using such license.

B. <u>Incremental Operating Expenses</u>

Q. Please describe generally where the FPL estimated cost off-sets are included in Table 2 to Exhibit No. BLH-3.

A. Like Table 1, the FPL estimated costs Mr. Holcombe uses as off-sets to GridFlorida operating expenses are included in columns 7 and 10 of BLH-3, Table 2. Again, column 7 describes the FPL estimated costs associated with retail load, and column 10 represents estimated costs associated with wholesale load (some or all of which are associated with FPL).

Q. Please explain the FPL estimated cost off-set associated with O&M for FPL transferred assets.

A. Estimated O&M costs associated with FPL transferred assets, included at line 1 of Table 2, are made up of three elements: O&M on the fixed assets to be transferred, estimated property tax on tangible assets, and cost-based leases for operating facilities and shared equipment. The cost-offset, which FPL no longer will incur, totals approximately $57 million ($52.882 million dollars associated with retail load included in column 7 and $4.231 million dollars associated with wholesale load included in column 10). It consists of the following:

- $34.113 million in O&M on FPL's transferred assets, which is based on estimated 2001 O&M expenses adjusted to year 2003;
- $20 million for estimated property tax on tangible property, poles, and wires, estimated based on 1999 data; and
- $3 million for leases for offices, services centers, and shared station equipment that is owned by FPL.

Q. Please explain the FPL estimated cost off-set associated with Salaries and Benefits.

A. This offset, included at line 3, is associated with reduced personnel that currently perform functions FPL no longer will perform after GridFlorida begins operations. FPL estimates a reduction in 27 employees. The estimated annual salary and benefits for each of these employees, $101,250 per employee per year, comes from the assumptions used to develop the Accenture Blueprint. The total of this off-set for FPL is $2.733 million ($2.531 million included in column 7 and approximately $202,000, representing FPL's share of the total included in column 10).

Q. Please explain the FPL estimated cost off-set associated with Lease Back Arrangements –FPL.

A. Because FPL is not transferring land and land rights to GridFlorida, FPL and GridFlorida will enter in a land use agreement to allow GridFlorida access to its facilities. The $19.444 million included in line 5, column 7 and the $1.556 million included in line 5, column 10 represent the estimated cost of FPL's land use fees.

Q. Please explain the FPL estimated cost off-set associated with Control Center Facilities and Building Services.

A. This cost off-set is found at line 8, and totals $1.796 million (the amount included in column 7 and the entire amount included in column 10). It represents the estimated cost to GridFlorida to lease the necessary space at FPL's control center to plan, operate, and control the transmission system. It is based on a lease for 45,000 square ft. at an estimated $39.13 per sq. ft., plus an annual inflation factor of 2 percent to estimate the year 2003 lease cost.

Q. Please explain the FPL estimated cost off-set associated with Disaster Recovery Facility.

A. The $31,000 included in line 10, column 7 and the $2,000 included in line 10, column 10 represent the estimated cost to GridFlorida to lease FPL's disaster recovery facility. The total is based on an annual lease for 12,000 sq. ft in FPL's existing disaster recovery facility at an estimated $27.00 per sq. ft., plus an annual inflation factor of 2 percent to estimate the year 2003 lease cost.

Q. Please explain the FPL estimated cost off-set associated with Storm Fund.

A. The $4.259 million included in line 13, column 7 and the $341,000 included in line 13, column 10 represents the cost off-set to FPL's forecasted storm fund accrual as a result of FPL transferring its transmission assets.

Q. Please explain the FPL estimated cost off-set associated with Telecommunications.

A. GridFlorida's expected cost for Telecommunications is included at line 15 of Table 2. This is an operating expense associated with the voice and data communications lines needed by GridFlorida. FPL's off-set to the total expected cost for GridFlorida is estimated at $750,000 (the amount included in column 7 plus the total amount included in column 10), representing the estimated telecommunications costs FPL would have incurred had GridFlorida not commenced operations, but will avoid after GridFlorida becomes operational. The $750,000 is made-up largely of an allocation of telephone bills associated with transmission operations that FPL no longer will be responsible for when GridFlorida commences operations.

Q. Please explain the FPL estimated cost off-set associated with Meetings, Travel, and Seminars on Line 17 and Employee Training Budget included on Line 22.

A. These figures, totaling $71,000 and $39,000 respectively, represent estimates of avoided costs for meetings, travel, and seminars and training for the 27 employee reductions at FPL identified above. The figure for meetings, travel, and seminars is based on an estimated annual expense of $2,632 per employee and the figure for training is based on an estimated annual expense of $1,421 per employee. These calculations were based on assumptions used to develop the Accenture Blueprint.

Q. Please explain the FPL estimated cost off-set associated with FERC Fees.

A. This figure is equal to FPL's load ratio share of the $1 million estimate for GridFlorida's FERC fees included in the Accenture Blueprint. It represents costs FPL would have incurred had GridFlorida not commenced operations.

Q. Does this conclude your testimony?

A. Yes.