

ORIGINAL

MCWHIRTER REEVES
ATTORNEYS AT LAW

TAMPA OFFICE:
400 NORTH TAMPA STREET, SUITE 2450
TAMPA, FLORIDA 33602
P. O. BOX 3350 TAMPA, FL 33601-3350
(813) 224-0866 (813) 221-1854 FAX

PLEASE REPLY TO:

TALLAHASSEE

TALLAHASSEE OFFICE:
117 SOUTH GADSDEN
TALLAHASSEE, FLORIDA 32301
(850) 222-2525
(850) 222-5606 FAX

August 21, 2001

VIA HAND DELIVERY

Blanca S. Bayo, Director
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Re: Docket No.: 010827-EI

Dear Ms. Bayo:

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

- ▶ Florida Industrial Power Users Group's Prehearing Statement.

Please acknowledge receipt of the above on the extra copy of each and return the stamped copies to me. Thank you for your assistance.

Sincerely,

Vicki Gordon Kaufman
Vicki Gordon Kaufman

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Gulf Power Company's Petition for Approval of Purchased Power Arrangement Regarding Smith Unit 3 for Cost Recovery Through Recovery Clauses Dealing with Purchased Capacity and Purchased Energy.

Docket No.: 010827-EI

Filed: August 21, 2001

FLORIDA INDUSTRIAL POWER USERS GROUP'S PREHEARING STATEMENT

The Florida Industrial Power Users Group (FIPUG), pursuant to Order No. PSC-01-1532-PCO-EI, hereby files its Prehearing Statement.

A. APPEARANCES:

JOHN W. MCWHIRTER, JR., McWhirter Reeves McGlothlin Davidson Decker Kaufman Arnold & Steen, P.A., 400 North Tampa Street, Suite 2450, Tampa, Florida 33601-3350 and **JOSEPH A. MCGLOTHLIN** and **VICKI GORDON KAUFMAN**, McWhirter Reeves McGlothlin Davidson Decker Kaufman Arnold & Steen, P.A., 117 South Gadsden Street, Tallahassee, Florida 32301.

On Behalf of the Florida Industrial Power Users Group.

B. WITNESSES:

| <u>Witness</u> | <u>Subject Matter</u> | <u>Issues</u> |
|----------------|--|---------------|
| Jeffry Pollock | Mr. Pollock is currently in the process of developing testimony. | |

C. EXHIBITS:

| <u>Exhibit</u> | <u>Witness</u> | <u>Description</u> |
|----------------|----------------|---|
| | Jeffry Pollock | Mr. Pollock is currently in the process of developing exhibits. |

D. STATEMENT OF BASIC POSITION:

The Commission should not approve the purchased power agreement (PPA) between Gulf and Southern Power. The PPA is not the most cost-effective alternative for ratepayers and would be more expensive than rate-basing Smith Unit 3. Gulf inappropriately compares only the

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first 10 years of the transaction period - the most costly period for the rate-based plant. Further, Gulf uses inappropriate assumptions which, when corrected, demonstrated that the PPA is more expensive than rate basing the unit, even when the analysis is done only over a ten-year period. Smith 3 is being built on Gulf land which has been in the Gulf rate base for years. There has been no determination of market value for the land or any means established to reimburse consumers for the costs they have incurred to support this land so that it can be made available to an unregulated entity. These valuable assets should not be transferred to an affiliate until the Commission determines that customers have received full value for all transferred property (including the land and other infrastructure at the plant site) that they have been supporting in base rates.

Not only is the PPA not the most cost-effective alternative, it also deprives ratepayers (and this Commission) of other significant benefits of ownership. For example, under the PPA, the potential profit from wholesale sales Southern Power makes from Smith 3 can be diverted to Southern Power's shareholders. If Smith 3 is included in rate base, the major portion of any profits from wholesale transactions will flow to ratepayers. Further, under the PPA, this Commission will have no authority to require power to be provided to the Florida grid in times of emergency or to require any additions or extension of facilities at Smith 3, if necessary.

E. STATEMENT OF ISSUES AND POSITIONS:

Legal Issues:

ISSUE 1: Is the proposed transfer of ownership of Smith Unit 3 to Southern Power consistent with Commission Order No. PSC-99-1478-FOF-EI, issued August 2, 1999, in Docket No. 990325-EI, the determination of need for Smith Unit 3?

FIPUG: No. When the Commission certified Smith 3 as the least-cost method for meeting the forecasted future demand of Gulf's retail consumers, the approval was based upon Gulf owning the plant. There was no testimony or discussion regarding the transfer of Smith 3 to an affiliate and such a transfer was never contemplated or discussed at the need determination hearing. The process Gulf has used to enter into the PPA has effectively excluded alternative suppliers from participation. The PPA subverts the statutory process to the detriment of consumers.

ISSUE 2: Must the Commission make the specific findings required by the Energy Policy Act of 1992, 15 USCA § 79z-5a(c), before Smith Unit 3 can be transferred to Southern Power?

FIPUG: No position at this time.

ISSUE 3: Will Gulf's proposed purchase power agreement with Southern Power affect the Commission's ability to direct Gulf Power to make additions or extension of facilities to the plant and equipment at the Smith site pursuant to Section 366.05, Florida Statutes?

FIPUG: Yes. Section 366.05(1) gives the Commission authority to “require repairs, improvements, additions and extensions to the plant and equipment of any public utility...” Pursuant to section 366.02(1), Southern Power is not a public utility; therefore, if the transfer occurs, the Commission will have no authority to require Gulf (who will no longer own the plant) or Southern Power (over whom the Commission has no jurisdiction) to make any improvements, additions or extensions at Smith 3.

ISSUE 4: Must Gulf Power demonstrate changed circumstances since Order No. PSC-99-1478-FOF-EI was issued in order for Gulf’s petition to be approved?

FIPUG: Yes. The law is well-settled that there must be a terminal point in every administrative proceeding at which the parties may rely on a decision as being dispositive. Clearly, the need order, which contemplates that Gulf will own the plant, is final. Therefore, Gulf must demonstrate a significant change in circumstances to change the order. Gulf has failed to do so.

ISSUE 5: Will the Commission have the same authority, pursuant to Section 366.04(2)(c), Florida Statutes, over the disposition of power from Smith Unit 3 into the Florida grid: A) If Smith Unit 3 is in the rate base of a Florida utility? B) If Smith Unit 3 is owned by Southern Power Company?

FIPUG: A) If Smith Unit 3 is in rate base, the Commission will have authority under Section 366.04(2)(c) (part of the Commission’s Grid Bill authority) to take those actions necessary to foster reliability within the grid for operational and emergency purposes. Such authority extends to the electric utilities, as defined in section 366.02(2).

B) If Southern Power owns Smith Unit 3, the Commission will have no such authority, as Southern Power is not an electric utility.

Technical Issues:

ISSUE 6: What is the projected difference in costs to Gulf’s retail customers, if any, between Gulf Power’s proposed purchased power arrangement with Southern Power, including the transfer of Smith Unit 3, and rate base treatment of Smith Unit 3?

FIPUG: Even using the assumptions Gulf proffers (with which FIPUG strongly disagrees), the transaction would be at best a “wash.” However, lowering the ROE to a reasonable level and making other reasonable changes to the assumptions show that rate-basing the unit is significantly more cost-effective. In addition, the Commission will lose jurisdiction over Smith Unit 3 (and all the attendant authority that comes with that) if the unit is transferred.

ISSUE 7: What is the projected difference in fuel costs to Gulf's retail customers, if any, between Gulf Power's proposed purchased power arrangement with Southern Power, including the transfer of Smith Unit 3, and rate base treatment of Smith Unit 3?

FIPUG: There should be none, but Gulf could potentially follow the practice used by other utilities to enhance profitability by selling electricity generated with lower cost coal-burning generators in the competitive wholesale market in other states and replacing the power sold with power generated from Smith 3. Further, one advantage of rate-base generation is that while retail customers pay for all of the costs of the unit, they also receive all the benefits, including margins from the temporary use of the capacity by non-native load customers. To the extent that such sales are made, the net fuel costs would be lower. The PPA would allow Southern Power Company to retain margins from the use of Smith 3 in other markets. Therefore, the PPA would create a lost opportunity cost for retail customers.

ISSUE 8: What risks and benefits to retail ratepayers should the Commission consider in deciding whether to grant Gulf's request for approval of the proposed purchase power arrangement with Southern Power regarding Smith Unit 3?

FIPUG: First and foremost, the Commission must consider whether this is the most cost-effective alternative for the ratepayers. Gulf has admitted that it is not. Further, Gulf has failed to bid this project, so the Commission has no way to evaluate what more cost-effective alternatives are available. Second, if the Commission approves this transaction, it will lose control over the unit, including its ability to call on the unit during times of grid emergencies. Third, Southern Power will be able to use the unit to effectuate off-system sales to benefit only its shareholders and not Florida ratepayers. Fourth, Gulf as a regulated utility is claiming confidentiality to conceal the true facts from the general public. Fifth, because Southern Power does not have the obligation to serve retail customers, there is no guarantee that any of this capacity will be available beginning in Year 11. Further, retail customers may pay significantly higher costs to replace Smith 3 capacity either through a successor PPA or a rate base investment.

ISSUE 9: What is the difference, if any, in the impact of wholesale sales on Gulf's retail customers between Gulf Power's proposed purchased power arrangement with Southern Power, including the transfer of Smith 3, and rate base treatment of Smith 3?

FIPUG: If the PPA is approved, there is the potential that profits made from off-system wholesale sales will be retained by the shareholders of Southern Power. If Smith 3 is included in rate base, ratepayers will receive the major portion of the gains on wholesale sales. Due to certain contractual provisions, Southern Power will have the opportunity to structure off-system transactions for only the benefit of its shareholders. Further, these appears to be cross-subsidization which will enable

Southern to Power gain a potential predatory pricing advantage over potential wholesale competitors. The state of Florida should not give its imprimatur of propriety to this anticompetitive device by enabling Gulf to use the state exemption to the Sherman anti-trust act to undermine its purpose. Retail customers will also lose the considerable market value of the land and other infrastructure if the assets are not transferred at the appropriate value.

ISSUE 10: Based on the RFP process reviewed and approved by the Commission in Docket No. 990325-EI wherein the selection of Smith Unit 3 was recognized as a more cost-effective alternative to purchases from non-affiliated third parties, is the price to be paid by Gulf Power under the proposed purchased power arrangement with Southern Power no higher than the price Gulf would have paid to purchase power from a non-affiliate?

FIPUG: There is no way to know this since Gulf failed to bid out the PPA before entering into the proposed transaction with its affiliate at issue in this docket. However, since this is a transaction with an affiliate and not an arms-length transaction, it should be assumed the affiliate (since it was the only entity permitted to negotiate as to the transaction) proposed and received a higher price than could have been procured from a non-affiliate.

ISSUE 11: Is it necessary that Gulf Power demonstrate its proposed purchased power arrangement with Southern Power regarding Smith Unit 3 would be the least cost alternative for its retail customers? If so, has Gulf made such a demonstration?

FIPUG: Yes. In evaluating PPAs, the Commission must determine that the contract is the least-cost alternative. Gulf has not made such a determination and, in fact, has admitted that the PPA is not the least-cost alternative. Approving a contract that is not least-cost would undermine the provisions of the Power Plant Siting Act

ISSUE 12: If Gulf's proposed purchased power arrangement (PPA) with Southern Power is approved for cost recovery, should the Florida Public Service Commission condition its approval upon there being no modifications to the PPA without the prior consent of the Florida Public Service Commission?

FIPUG: While FIPUG does not believe the PPA should be approved, if it is, the Commission should require modifications to bring the PPA into line with rate base treatment and prohibit any modifications to the PPA without approval by the Commission after input from affected parties and an opportunity for hearing. Also, the Commission should ensure that the cost of voltage support to be provided from the unit beginning in Year 11 of the PPA is cost-based and no higher than Gulf could otherwise obtain under a FERC regulated tariff.

ISSUE 13: If Gulf's proposed purchased power arrangement (PPA) with Southern Power is approved, should Gulf file any price changes permitted under the PPA with the Florida Public Service Commission for prior review as to compliance with the

agreement and that the costs are prudently incurred?

FIPUG: While FIPUG does not believe that the PPA should be approved, if it is, all price changes should be submitted for prior review by the Commission as well as input from the affected parties and an opportunity for hearing.

ISSUE 13a: If Gulf's proposed purchased power arrangement (PPA) with Southern Power is approved, should the Florida Public Service Commission condition its approval upon there being no price changes permitted under the PPA without the prior consent of the Florida Public Service Commission?

FIPUG: Yes. Further, before approval of any such changes, the Commission should solicit input from affected parties and provide an opportunity for hearing.

ISSUE 14: Did Gulf seek competitive bids for the purchase of power and voltage regulation before entering into the contract with Southern Power? If not, should it have?

FIPUG: Gulf has admitted that it did not seek competitive bids. In order to demonstrate that its proposal is the most cost-effective alternative for ratepayers, Gulf should have bid it.

ISSUE 14a: Was it necessary that Gulf seek competitive bids for the purchase of power and voltage regulation before entering into the contract with Southern Power? If so, did Gulf Comply with such bidding requirement?

FIPUG: Yes. In order for Gulf to demonstrate that the transaction for which it seeks approval is the least-cost alternative for ratepayers, it should have bid it. Gulf has admitted that it did not do so.

ISSUE 15: If Gulf's proposed purchased power arrangement with Southern Power is approved and Smith 3 is transferred, what assets will be transferred and what will be the transfer price?

FIPUG: Gulf proposes to transfer all assets related to Smith 3. The transfer price is unclear.

ISSUE 16: Have Gulf Power's retail customers been charged to date with any costs associated with Smith 3? If so, how will Gulf's customers be compensated for these prior costs if the proposed purchased power arrangement is approved and Smith Unit 3 is transferred to Southern Power?

FIPUG: Gulf's customers have been charged with AFUDC. It is unclear how (or whether) they will be compensated. Smith 3 is being built on land that has been in the retail rate base for many years. Customers should be entitled to a refund of the carrying costs they have paid.

ISSUE 17: As a matter of public policy, should a Florida regulated utility be allowed to construct a power plant for the benefit of a non-regulated affiliate when independent power producers cannot construct merchant plants in Florida, except under limited circumstances?

FIPUG: No. Under the current regulatory and legal climate, independent power producers have a very limited ability to construct plants in Florida, even though they offer pricing that would be extremely favorable. Until merchant power plants can compete on a level playing field, it is poor public policy to permit regulated utilities to enter into the kind of transaction at issue here with their affiliates.

ISSUE 18: If Gulf's petition is granted, what conditions, if any, should be imposed on Gulf due to the affiliate relationship between Gulf and Southern Power?

FIPUG: FIPUG does not believe Gulf's petition should be granted, but if it is, the PPA should be held in abeyance until Gulf's base rates are modified. Smith 3 should be offered for sale at auction at its book value to all qualified bidders. The sale contract should contain a right of first refusal to Gulf to purchase power from the plant for at least ten years at a price no higher than the cost of power would be if the plant were in the retail rate base. The prices under the contract should be modified to bring the PPA cost to a price that will be substantially less than it would be under rate base treatment.

ISSUE 19: Should the Commission approve the proposed purchase power arrangement regarding Smith 3 for cost recovery through the cost recovery clauses designated for addressing the recovery of costs associated with purchased capacity and purchased energy?

FIPUG: No.

F. STIPULATED ISSUES:

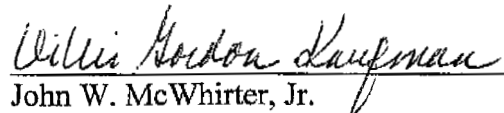
None.

G. PENDING MOTIONS:

FIPUG has no motions pending.

H. OTHER MATTERS:

None at this time.



John W. McWhirter, Jr.
McWhirter Reeves McGlothlin Davidson
Decker Kaufman Arnold & Steen, P.A.
400 North Tampa Street, Suite 2450
Tampa, Florida 33601-3350
(813) 224-0866 Telephone
(813) 221-1854 Telefax

Joseph A. McGlothlin
Vicki Gordon Kaufman
McWhirter, Reeves, McGlothlin, Davidson,
Decker, Kaufman, Arnold & Steen, P.A.
117 South Gadsden Street
Tallahassee, Florida 32301
(850) 222-2525 Telephone
(850) 222-5606 TeleFax

Attorneys for the Florida Industrial
Power Users Group

CERTIFICATE OF SERVICE

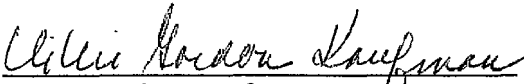
I **HEREBY CERTIFY** that a copy of the foregoing The Florida Industrial Power Users Group's Prehearing Statement has been furnished by (*) hand delivery, or U.S. Mail this 21st day of August, 2001, to the following:

(*) Marlene Stern
Florida Public Service Commission
Division of Legal Services
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Jeffery Stone
Beggs & Lane Law Firm
Post Office Box 12950
Pensacola, Florida 32576-2950

Roger Howe
Office of Public Counsel
c/o The Florida Legislature
111 West Madison Street, Room 812
Tallahassee, Florida 32399-1400

Ronald C. LaFace
Greenberg Traurig, P.A.
P.O. Drawer 1838
Tallahassee, FL 32303


Vicki Gordon Kaufman