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April 1, 2002

-VIA HAND DELIVERY-

Ms. Blanca S. Bayó
Division of the Commission Clerk
and Administrative Services
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

Re: **Docket Nos. 020166-EQ and 001574-EQ**

Dear Ms Bayò:

Enclosed for filing on behalf of Florida Power & Light Company ("FPL") in Docket Nos. 001574-EQ and 020166-EQ are the original and fifteen copies of the Responsive Comments of Florida Power & Light Company. If you or your staff have any questions regarding this transmittal, please contact me at (850) 222-2300.

Respectfully,

Charles A Guyton
Attorney for Florida Power &
Light Company

cc: Richard Bellak

Responsive Comments of Florida Power & Light Company

FPL submits these comments in response to the rulemaking proceeding initiated by the Florida Public Service Commission to amend Rule 25-17.0832, Florida Administrative Code, relating to firm capacity and energy contracts. FPL's comments support the proposed rule modification initiated by the Commission. The amendments proposed by the Commission address primarily the reduction of the minimum term of the Standard Offer Contract from ten years to five years. FPL supports this modification. Although FPL has taken the approach of requesting a waiver on a case by case basis, it does not oppose this proposed change. This amendment to Rule 25-17.0832 will alleviate the need to file recurring and expensive rule waiver requests. Given the number of rule waiver requests that have been granted, this amendment essentially captures Commission policy.

On the other hand, FPL is concerned with and strongly opposes the suggestion by Lee County, Miami-Dade County and Montenay-Dade ("the Parties") for additional amendments to Rule 25-17.0832. The suggested amendments are contrary to established Commission policy in implementing Statute 366.051. The amendments proposed include: 1) basing the Standard Offer rates, terms and conditions on the purchase of power rather than only on the construction alternative, 2) using revenue requirements as the basis to calculate payments pursuant to a Standard Offer Contract, 3) allowing the Qualifying Facility to specify the duration of the contract, 4) providing for a

minimum of 20 % of the energy payment pursuant to the Standard Offer Contract to be based on the projected energy cost used by the utility at the time the contract is executed, and 5) excluding all demand side management alternatives not implemented or under contract from the utility's analyses in identifying its avoided unit. Adoption of these provisions would reverse twenty years of Commission cogeneration policy reflected in the current rule. Most, if not all, of the arguments presented by the Parties in support of their proposed amendments have been presented to the Commission in the past and have been rejected by the Commission. FPL believes it is a waste of the Commission's time to consider the amendments proposed by the Parties. These amendments significantly increase risks and costs to utility customers by subjecting them to payments higher than the purchasing utility's avoided costs.

The rulemaking proceeding initiated by the Commission addressed the reduction of the minimum term of the Standard Offer Contract from ten to five years. The result of this modification is to limit the risk that customers will be tied to long-term contracts that do not reflect the avoided cost of the utility. The additional amendments proposed by the Parties will have the opposite result in that they will increase the risk to the customers and result in payments to qualifying facilities that are higher than the avoided costs of the purchasing utility.

Section 366.051 establishes the rates for purchases from cogenerators and small power producers at rates equal to the purchasing utility's full avoided cost. The Commission has taken a balanced approach in implementing the

statute by balancing the allocation of the risks and benefits associated with purchases from Qualifying Facilities.

Basing Standard Offer Contracts on Purchase Options

Early on in its consideration of cogeneration rules the Commission considered and rejected the idea being advanced by the Parties, paying the higher of a construction or a purchased alternative as avoided cost. The Commission expressed a willingness to consider a purchase alternative as a measure of avoided cost, but only if the purchase was less costly than construction:

> Several intervenors, notably Dade County, urged us to consider all alternatives to additional construction available to a utility in pricing QF capacity. If other supply side alternatives, such as off system firm power purchases, are identified as available **and less costly** than construction of the statewide avoided unit, we will take that into account in pricing the standard offer. We will not consider supply side alternatives more costly than the value of deferral because **it would not benefit the ratepayers to pursue them**, regardless of the source. (Emphasis added.)

In re: Amendment of Rules 25-17.80 through 25-17.89 relation to cogeneration. 83 FPSC 10:150,166 (Order No. 12634). The Commission recognized then, as it should now; that using purchases as a measure of avoided cost was appropriate only when such cost was lower than construction cost. Any other arrangement penalizes customers.

Using Revenue Requirements Rather than Value of Deferral to Calculate Capacity Payments

The Revenue Requirements methodology for use in calculating capacity payments was rejected in the early days of QF rulemaking, in the early 80s. The preferred methodology to be used in calculating avoided costs payments has always been the value of deferral methodology. The Commission also resolved the revenue requirements versus value of deferral issue in Order No. 12634. There it said:

> We believe that the value-of-deferral methodology is superior to a revenue requirements methodology for a couple of reasons. First, revenue requirements are based on a thirty-year depreciation life for a power plant. The payments are relatively high in the early years and relatively low in the later years; if ratepayers receive service from the plant for thirty years, the disadvantage of the high payments in the early years is offset by the benefit of low payments in the later years. That symmetry is missing if a QF makes only a ten-year commitment; a QF would receive the high end of the deferred revenue requirements stream without a concomitant obligation to provide service in exchange for relatively low deferred revenue requirements in later years. Second, capacity payments based on deferred revenue requirements would overpay the QF in early years, thus getting into the thorny problem of securing all capacity payments for a number of years, not just those made pursuant to the early payment option.
>
> The value-of-deferral methodology overcomes these problems. First the deferral method pays the QF only what it earns in any given year, the value of an annual deferral, thus eliminating the security question in ordinary circumstances. Second, the value-of-deferral method will, over the thirty-year depreciation life of the avoided unit, pay a QF the same amount it would have received if its capacity payments had been based on deferred revenue requirements. That is, at the end of the thirty years, a QF would have received the same total amount on a present value basis, under either methodology; the difference between the two methods lies in the level of payment in any given year in that thirty year period. Levelizing capacity payments based on avoided revenue requirements mitigates but does not cure the problem; using the value of annual deferral as the benchmark, levelized capacity

payments based on deferred revenue requirements still overpay a QF in the early years.

The Commission's observations in 1983 are equally valid today. The revenue requirements methodology advanced by the parties unduly benefits QFs at the expense of customers.

The value-of-deferral methodology balances the benefit of purchasing from QFs with the risk of the purchasing utility paying more than full avoided cost. While theoretically a contract term equal to the life of the avoided unit using a revenue requirement methodology will yield payments on a net present value basis that are equal to payments using the value of deferral methodology, the practical result of this approach is a significant shift in risks to the customers of payments for purchased power at rates that are considerably higher than avoided costs. Should the QF walk away for any reason prior to the 30 or 40 year contract, the customers would pay more than the avoided cost. This problem is exacerbated by a history of decreasing generating capacity costs.

Allowing the QF to Specify Contract Duration – Minimum Term

The burden of justifying the term of the Standard Offer Contract has been placed on the utility, where it belongs. The minimum term specified in the Standard Offer Contract allows the Commission to implement, through its rules, a policy that once again balances risks. The minimum term needs to be long enough to incorporate planning needs and QF contractual requirements while at the same time protecting the customers from paying higher than avoided costs.

The narrow criteria that has to be met in order to qualify for a Standard Offer contract are such that the potential exists for payments to result in a subsidy. The five year minimum term mitigates this risk. Furthermore, allowing the QF to specify the term of the contract results in a significant shift in risks. The QF will only take into account its interests in deciding the term and will not consider a balancing of risks vs. benefits for the customers.

In originally approving a ten-year minimum term, the Commission was concerned about customers receiving capacity deferral benefits. It was recognized delivery for ten years was important from a planning perspective. Order No. 12634 at 168. Given the long unit permitting and construction times at that time, ten years was a reasonable term, but given the shorter terms currently prevalent, a five year term is reasonable from a planning perspective.

Energy Payments based on Projected Energy Costs

The energy payments associated with a Standard Offer Contract are tied to the actual cost of the fuel associated with the avoided unit or the as-available energy cost. The Commission explained the rationale for this linkage in Order No. 12634:

> The rule provides for a firm energy price that is also linked to the avoided unit. Commencing with the anticipated in-service date of the avoided unit, the QF will receive the lesser of the as available energy cost of the utility planning the avoided unit or the energy cost associated with the avoided unit itself. The energy cost associated with the avoided unit is defined as the cost of fuel, in cents per KWH, that would have been burned in the avoided unit, calculated by multiplying the average market price of the fuel that

would have been burned in the statewide avoided unit by the average heat rate associated with it. [Rule 25-17.83(6)]. The rule requires payment of the "lesser of" because in those situations where a utility's incremental fuel cost were less that the fuel cost of the avoided unit, it would not be economical to dispatch it.

History has demonstrated the inherent uncertainty associated with forecasting fuel costs. Once again, the suggestion that the energy payments should be, in part, tied to forecasted fuel prices shifts the risks from the QF to the customer. Each time the Commission has taken up the issue of payments to QFs in the past, the outcome has been to mitigate risks associated with energy payments by tying them to the current market price at the time of the purchase.

Excluding Demand Side Management Alternatives not Implemented or under Contract

Finally, the issue of excluding demand side management alternatives that are not implemented or currently under contract only serves to artificially increase the avoided costs associated with the avoided unit. The process of identifying the next unit to be avoided typically starts with the Ten Year Site Plan. The Ten Year Site Plan represents the utility's current official generation expansion planning document. The demand side alternatives included in the plan are previously presented and approved by the Commission. Order No. PSC-99-1942-FOF-EG approved FPL's demand side management targets included in FPL's generation expansion plan. To exclude the approved demand side management plan in the utility's determination of its next unit to be avoided can

only result in Standard Offer Contracts with payment terms and conditions higher than the Utility's avoided cost.

The Commission has previously considered and rejected this conservation argument on several occasions. Perhaps the clearest rejection of this argument is found in Order No. 13247:

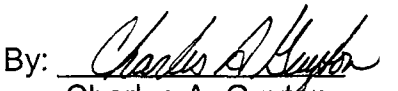
> During these proceedings, considerable debate was fostered by the QF intervenors as to which load forecast should be used to determine the in-service date of the statewide avoided unit. The QFs contended that the load forecast should exclude the effects of utility sponsored demand side conservation programs. In our opinion, **these arguments are totally without merit**. Specifically we reject the testimony of Dr. Spann and Mr. Seidman regarding this subject. The Commission's cogeneration rules implicitly require that the effects of utility sponsored conservation programs be reflected in the utilities' load forecasts for the purpose of determining the timing of the statewide avoided unit. Rule 25-17.83(4) describes certain evidence and the scope of analysis to be presented to the Commission by each utility to assist the Commission in determining the statewide avoided unit. Rule 25-17.83(4)(a) specifically requires each utility to identify its next planned uncertified generating unit to be added to its system pursuant to its <u>most current long range generation expansion plan</u> (emphasis added). The only adjustment to the utility's generation expansion plan is the specified exclusion of anticipated purchases from qualifying facilities that are not currently under contract. Logic, as well as past Commission practice since the adoption of the Florida Energy Efficiency and Conservation Act (FEECA) dictates that a utility's most current long range generation expansion plan must be based on the utility's most current "expected case" load forecast, inclusive of conservation. Had we desired to treat conservation differently, we would have expressly stated so as was done with regard to non-contracted QF capacity.
>
> The fact is, we do not desire to exclude the effects of utility sponsored conservation programs from the load forecasts or generation expansion plans of the Florida utilities in determining the statewide avoided unit. The reason for this was clearly stated in Mr. Jenkins' testimony: conservation in the aggregate is significantly more cost effective than cogeneration (TR 1107-12). **As such, exclusion of the effects of utility sponsored conservation programs from the load forecast in this proceeding would result in payments to qualifying facilities in**

excess of the utilities' avoided costs and hence, subsidization of cogeneration by the general body of Florida ratepayers. This is clearly contrary to the intent of the Commission's *cogeneration rules and policy.* (Emphasis added.)

Conclusion

FPL concludes, for the reasons set forth herein, that the amendments proposed by the Commission serve to capture Commission policy. FPL supports the changes proposed by the Commission. On the other hand, FPL strongly opposes the additional amendments to Rule 25-17.0832 proposed by Lee County, Miami-Dade County and Montenay-Dade. These additional proposed amendments are contrary to Commission policy and only serve to increase the risk that customers in the state of Florida will pay higher than avoided cost for the power purchased pursuant to a utility's Standard Offer Contract.

Respectfully submitted,

By: 

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