

ORIGINAL

M E M O R A N D U M

OCTOBER 17, 2002

TO: DIVISION OF THE COMMISSION CLERK AND ADMINISTRATIVE SERVICES

FROM: OFFICE OF THE GENERAL COUNSEL (KEATING) *WCK*

RE: DOCKET NO. 020001-EI - FUEL AND PURCHASED POWER COST RECOVERY CLAUSE WITH GENERATING PERFORMANCE INCENTIVE FACTOR.

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Attached is the Direct Testimony of Matthew Brinkley, on behalf of Commission Staff to be filed in the above-referenced docket.

WCK/jb

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11315 OCT 17 02

FPSC-COMMISSION CLERK

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Fuel and purchased power  
cost recovery clause with  
generating performance incentive  
factor.

DOCKET NO. 020001-EI

FILED: OCTOBER 17, 2002

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the DIRECT TESTIMONY OF MATTHEW BRINKLEY, on behalf of the Commission Staff has been furnished to the following, by U.S. Mail, this 17<sup>th</sup> day of October, 2002:

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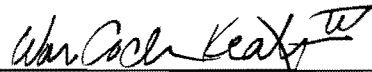
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*DOCKET NO.:* 020001-EI - [Fuel and purchased power cost recovery clause with generating performance incentive factor.]

*WITNESS:* Direct Testimony of Matthew Brinkley  
Appearing on Behalf of Staff

*DATE FILED:* October 17, 2002

DOCUMENT NUMBER DATE

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FPSC-COMMISSION CLERK

DIRECT TESTIMONY OF MATTHEW BRINKLEY

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Q. Please state your name and business address.

A. My name is Matthew Brinkley. My business address is 2540 Shumard Oak Blvd., Tallahassee, Florida, 32399.

Q. By whom are you employed and in what capacity?

A. I am employed by the Florida Public Service Commission as a Regulatory Analyst IV in the Bureau of Surveillance/Finance, Division of Economic Regulation

Q. Please provide a brief description of your educational background and your professional experience.

A. I received a Bachelor of Science degree with a major in Accounting and a minor in Finance from Florida State University in 1991. I received a Master of Business Administration from Florida State University in 1992. I received my Certified Public Accountant license in 1992 and practiced public accounting from 1992 to 1994.

Since joining the Florida Public Service Commission in 1994, I have held responsibilities relating to accounting, finance, and economic research and other accounting and ratemaking matters.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to propose that the Commission, in determining whether and to what extent "incremental" expenses may be recovered through the fuel clause, consider offsetting expenses proposed for recovery through the fuel clause with any base rate benefits associated with those expenses.

Q. Do you believe that offsetting is appropriate?

1 A. Yes. The Florida Public Service Commission is responsible for setting  
2 rates that allow the recovery of costs prudently incurred by a rate  
3 regulated utility under its jurisdiction. Rates can be set to recover  
4 costs through base rates, set either directly through rate cases or  
5 through the approval of rate case settlements brought before the  
6 Commission, or through factors set in cost recovery clauses like the  
7 fuel cost recovery clause. The Commission is responsible for ensuring  
8 that costs are not recovered through both base rates and cost recovery  
9 clauses simultaneously. I believe offsetting is necessary to guard  
10 against double recovery.

11 **Q. How does offsetting relate to the measurement of incremental expenses?**

12 A. When an expense is incurred to support a particular utility function,  
13 the expense may reduce other current or future expenses or increase  
14 current or future revenues. Reduced base rate expenses must be offset  
15 against proposed fuel clause expenses or those expenses would be  
16 recovered twice; once in base rates and now in the fuel clause.  
17 Similarly, since additional revenues were not contemplated at the time  
18 base rates were set, total rates would be too high if these new revenues  
19 were not used to offset proposed fuel clause expenses.

20 **Q. Could you give a few general examples of offsetting expenses?**

21 A. Yes. New remote metering technology expenses may replace five meter  
22 readers, a new truck with infrared capabilities may cut maintenance  
23 expense and save capital costs by replacing transformers only when they  
24 need replacing, or more frequent cleaning of generation equipment may  
25 extend the useful life of the equipment. In these cases, base rate

1 expenses reduce base rate expenses. so these are merely illustrative  
2 examples.

3 Q. What importance does the choice of a base year have in calculating  
4 incremental expenses?

5 A. At the time rates are set through a rate case, projected test year  
6 expenses are examined in order to determine revenue requirements which  
7 are then used to set rates. The projected test year is a snapshot of  
8 expenses. Only for the projected test year are rates set to recover the  
9 dollar amount of expense in a utility's Minimum Filing Requirements  
10 (MFRs). Each year subsequent to the projected test year, it is expected  
11 that the utility will sell more energy with the additional revenues  
12 covering increases in expenses since the projected test year, assuming  
13 the company's return on equity is stable. At a minimum, expenses from  
14 a base year used for comparison purposes need to be grossed up by the  
15 growth rate in energy sold since the base year.

16 Q. Order No. 14546 in Docket No. 850001-EI-B, issued July 8, 1985, states  
17 that "fossil fuel-related costs normally recovered through base rates  
18 but which were not recognized or anticipated in the cost levels used to  
19 determine current base rates and which, if expended, will result in fuel  
20 savings to customers" may be allowed recovery through the fuel clause.  
21 Could you comment?

22 A. Yes. It is my opinion that this provision was intended to encourage  
23 utilities to look for ways in which to lower costs recoverable through  
24 the fuel clause, and also to reduce a disincentive which would exist if  
25 costs were "recovered" through base rates while the benefit was

1 "recovered" through the fuel clause. I do not believe that it is  
2 intended to make the fuel clause an avenue for recovery of costs  
3 incurred to maintain and operate a process already in place upon the  
4 threat of higher costs otherwise.

5 **Q. What is the proper treatment of security costs?**

6 A. Security costs are appropriate for base rate treatment. Security costs  
7 protect assets, people, and reliability. Security costs have been and  
8 are still being recovered by the utilities through base rates. Both  
9 Florida Power & Light Company and Florida Power Corporation reported  
10 security costs in their MFRs filed in Docket Nos. 001148-EI and 000824-  
11 EI, respectively. The utilities' heightened security costs are simply  
12 previously unanticipated expenses which are being expended to protect  
13 against future base rate expenses, not to reduce current or future  
14 expenses which are recoverable through the fuel clause. Base rates are  
15 the appropriate place for expenses which protect against increases in  
16 base rates.

17 By Order No. PSC-01-2516-FOF-EI in Docket No. 010001-EI, issued  
18 December 26, 2001, the Commission found merit in the protection of  
19 nuclear generation facilities which could mitigate the threat of higher  
20 fuel costs if there was a nuclear outage. However, the approval was a  
21 stop gap measure in a time of crisis. Further, the request for recovery  
22 of these costs was made only 15 days prior to hearing in that docket,  
23 leaving little opportunity for review.

24 The Order further added "recognizing that these costs are not now  
25 clearly defined, we do not foreclose our ability to consider an



1 alternative recovery mechanism for these costs at a later time." I  
2 believe it appropriate to consider moving these security costs into base  
3 rates at least by December 31, 2005, the end of the rate settlements  
4 approved in Order No. PSC-02-0655-AS-EI, in Docket Nos. 000824-EI and  
5 020001-EI, issued May 14, 2002, for Florida Power Corporation and Order  
6 No. PSC-02-0501-AS-EI, in Docket Nos. 001148-EI and 020001-EI, issued  
7 April 11, 2002, for Florida Power & Light Company. By that time, all  
8 parties will be able to better evaluate whether these costs are of a  
9 limited nature as originally thought or of a long-term nature, and  
10 whether these costs are incurred to principally result in fuel savings  
11 or to protect base rate assets, personnel, and reliability. Until that  
12 time, it is appropriate to examine security costs in light of any  
13 offsetting base rate savings as illustrated earlier in my testimony

14 **Q. Briefly, could you summarize your testimony?**

15 **A.** Yes. It is prudent for the Commission to consider current and future  
16 base rate expense savings and incremental revenues as offsets in order  
17 to determine what is an appropriate level of "incremental" expense to  
18 be recovered through the fuel clause. When base year expenses are  
19 compared to current year expenses, base year expenses should be grossed  
20 up for the growth in energy sales in kilowatt-hours. Finally, security  
21 costs should be reexamined for inclusion in base rates once a better  
22 understanding of their nature and longevity is attained.

23 **Q. Does this conclude your testimony?**

24 **A.** Yes, it does.

25

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