



BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 031033-EI

IN RE: TAMPA ELECTRIC COMPANY'S
2004-2008 WATERBORNE TRANSPORTATION
CONTRACT WITH TECO TRANSPORT
AND ASSOCIATED BENCHMARK

TESTIMONY AND EXHIBIT
OF

JOANN T. WEHLE
REDACTED VERSION

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1 **BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**

2 **PREPARED DIRECT TESTIMONY**

3 **OF**

4 **JOANN T. WEHLE**

5
6 **Q.** Please state your name, address, occupation and employer.

7
8 **A.** My name is Joann T. Wehle. My business address is 702 N.
9 Franklin Street, Tampa, Florida 33602. I am employed by
10 Tampa Electric Company ("Tampa Electric" or "company") as
11 Director, Wholesale Marketing & Fuels.

12
13 **Q.** Please provide a brief outline of your educational
14 background and business experience.

15
16 **A.** I received a Bachelor of Business Administration Degree
17 in Accounting in 1985 from St. Mary's College in Notre
18 Dame, Indiana. I am a CPA in the State of Florida and
19 worked in several accounting positions prior to joining
20 Tampa Electric. I began my career with Tampa Electric in
21 1990 as an auditor in the Audit Services Department. I
22 became Senior Contracts Administrator, Fuels in 1995. In
23 1999, I was promoted to Director, Audit Services and
24 subsequently rejoined the Fuels Department as Director in
25 April 2001. I became Director, Wholesale Marketing and

1 Fuels in August 2002. I am responsible for managing
2 Tampa Electric's wholesale energy marketing and fuel-
3 related activities.

4
5 **Q.** Please state the purpose of your testimony.

6
7 **A.** The purpose of my testimony is to present information
8 about Tampa Electric's solicitation for waterborne coal
9 transportation, evaluation of the bids received, the
10 reasonableness of the market prices established for the
11 company's waterborne coal transportation contract as a
12 result of that activity, and the sufficiency of the
13 Request for Proposal ("RFP") and market analysis
14 activities to establish new contract market rates.
15 Finally, my testimony addresses the issue of whether
16 Tampa Electric's coal transportation benchmark should be
17 modified or eliminated.

18
19 **Q.** Have you previously testified before the Florida Public
20 Service Commission ("Commission")?

21
22 **A.** Yes. I filed testimony before this Commission in Dockets
23 No. 010001-EI, No. 011605-EI, No. 020001-EI and No.
24 030001-EI. My testimony in these dockets described the
25 appropriateness and prudence of Tampa Electric's fuel

1 procurement activities, fuel supply risk management and
2 fuel price volatility hedging activities, incremental
3 hedging O&M costs resulting from maintenance and
4 expansion of the risk management and hedging plan and the
5 company's actual waterborne coal transportation costs.
6

7 **Q.** Have you prepared an exhibit in support of your
8 testimony?
9

10 **A.** Yes. Exhibit No. ____ (JTW-1), containing three
11 documents, was prepared under my direction and
12 supervision.
13

14 **Waterborne Coal Transportation Background**

15 **Q.** How does Tampa Electric currently transport coal to its
16 power stations?
17

18 **A.** Tampa Electric has a five-year integrated transportation
19 services contract with TECO Transport to deliver coal
20 from various U.S. Midwestern locations on the
21 Mississippi, Ohio and Green rivers to its generating
22 stations via river barges and ocean-going vessels. The
23 previous contract expired as of December 31, 2003, and
24 Tampa Electric executed a new contract with TECO
25 Transport on October 6, 2003.

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Q. Why is this type of integrated transportation used?

A. Beginning in the late 1950s Tampa Electric recognized the need to develop a water transportation system that could reliably and efficiently move coal down the Mississippi River and its tributaries and then across the Gulf of Mexico. The transportation system was formed to lower costs and to provide reliable transportation of coal for the benefit of Tampa Electric's ratepayers. When this integrated system was formed, rail rates to Florida from coalfields in the Midwest were so high that coal was not competitive compared to oil. Water transportation was an alternative in some regions, but a reliable water system for coal delivery to Florida did not exist. The development of an efficient integrated waterborne transportation system was necessary for Tampa Electric to utilize lower-cost coal as a fuel source.

Q. Please describe in more detail the development of the integrated transportation system.

A. The development of the integrated transportation system began during the 1950s. In the 1940s and early 1950s, all electric generation in peninsular Florida was fueled

1 with oil. Steam generating units used residual oil, and
2 many small municipal systems relied on diesel engines and
3 No. 2 distillate oil. Since all oil contracts were based
4 on prices posted in the world petroleum markets on the
5 day of delivery, there was no real competition. Oil
6 suppliers were also able to hold Florida's electric
7 utilities captive to market prices because of the state's
8 location and high rail rates. These market prices were
9 high relative to other areas of the country where
10 alternative fuels, such as coal, were available. Tampa
11 Electric was very concerned about the long-term
12 implications of total dependence on oil priced on a spot
13 basis.

14
15 For these reasons, Tampa Electric's management
16 investigated the availability of other fuels when
17 planning for its Gannon Station in the early 1950s. Both
18 coal and natural gas were considered in the
19 investigation. Nuclear power was then in its infancy and
20 not available for operation on a commercial scale.

21
22 **Q.** Why did using coal require a waterborne transportation
23 network?

24
25 **A.** At the time that Tampa Electric was preparing to build

1 Gannon Station, the principal disadvantage of coal was
2 transportation costs. Rail rates to Florida from the
3 Midwest were so high that coal was not competitive with
4 oil, and the company did not want to be held captive by a
5 total dependence on rail transportation. Waterborne
6 transportation systems from the area did not exist. A
7 new mode of transportation had to be devised if coal was
8 to become a viable alternative for Florida utilities.

9
10 **Q.** Describe the first stage of developing the integrated
11 waterborne transportation system.

12
13 **A.** In 1955, Tampa Electric decided to use coal as the fuel
14 for Gannon Unit 1, which was scheduled to be operational
15 in 1957. Tampa Electric entered into a long-term
16 contract for coal and waterborne transportation to the
17 plant from the coal supplier. In spite of the contract,
18 the supplier refused to deliver, leaving Tampa Electric
19 dependent on the spot market for replacement coal
20 purchases. Although Tampa Electric immediately sued for
21 non-compliance, the case was not resolved until 1963.
22 Thus in 1959 Tampa Electric, frustrated by its total
23 dependence on others and an inadequate waterborne
24 transportation market, decided to participate in a joint
25 venture to form a transportation company that could more

1 effectively move its purchased coal from the Midwest to
2 Tampa, Florida.

3
4 **Q.** How did the company determine that a terminal facility at
5 the base of the Mississippi River was needed?

6
7 **A.** Logistics of coal transfer, quality control issues and
8 storage needs led to a short-term lease of a terminal
9 facility on the Mississippi River below New Orleans.
10 Tampa Electric was concerned about risks due to storing
11 coal at the aging terminal facility. Therefore, a new
12 company was formed to build and operate a modern facility
13 for transloading and storage. Tampa Electric still
14 utilizes this terminal, built in Davant, Louisiana in
15 1965, to transfer, store and blend its coal.

16
17 **Q.** What is the purpose of the terminal facility?

18
19 **A.** The primary purpose for the terminal facility is to
20 transfer coal from river barges to ocean vessels or from
21 barges to land storage facilities, and from such land
22 storage facilities to vessels. It also provides the
23 company with the ability to blend coals, which has become
24 a more common practice over the years as environmental
25 requirements have become stricter. The storage space is

1 of special importance due to the distance of the supply
2 sources from Tampa and limited ground storage space at
3 waterfront power plant sites in Tampa.
4

5 **Q.** What was the result of developing the waterborne coal
6 transportation system?
7

8 **A.** The effects of adding another coal transportation
9 alternative were dramatic. When the waterborne
10 transportation system began operations, rail rates to
11 Florida began to drop almost immediately. Even with the
12 reduction in rail rates, which benefited Tampa Electric's
13 customers on the small portion of its coal that was
14 delivered by rail, prices paid by Tampa Electric for
15 water transportation by its affiliate have consistently
16 been lower than the rail alternative. This is
17 demonstrated by the company's costs being below its
18 waterborne coal transportation benchmark year after year.
19 In addition, the fact that there are separate and
20 distinct rail and water transportation systems has
21 benefited utilities in the bidding and purchase of coal.
22 It has also greatly increased the reliability of the
23 delivery system by providing alternatives. The savings
24 in the use of coal as a primary fuel for boilers versus
25 oil and gas can be directly attributed to the existence

1 of a waterborne delivery system. The water
2 transportation system has saved Tampa Electric's
3 customers hundreds of millions of dollars in fuel
4 transportation costs during the period from 1988 to 2002
5 alone, as demonstrated by the company's actual waterborne
6 coal transportation costs compared to its transportation
7 benchmark. Finally, the lowering of rail rates in
8 response to the competition of water transportation has
9 benefited ratepayers throughout the state.

10
11 **Waterborne Coal Transportation Contract Requirements**

12 **Q.** Are there existing Commission orders that address Tampa
13 Electric's waterborne coal transportation services
14 agreement with its affiliate, TECO Transport?

15
16 **A.** Yes, the existing transportation order was first
17 established in a settlement agreement approved in Order
18 No. 20298 in Docket No. 870001-EI-A. This order is
19 Document No. 1 of my exhibit. Order No. 20298, drafted
20 by then Commission Staff Counsel, Michael B. Twomey, was
21 issued on November 10, 1988 and represents the policy of
22 this Commission until changed.

23
24 This settlement agreement recites that:

25 In accordance with the Commission's direction,

1 Staff, Office of Public Counsel ("OPC") and
2 Tampa Electric have met to discuss the methods
3 by which market pricing can be adopted for
4 affiliate coal and coal transportation
5 transactions between Tampa Electric and its
6 affiliates. As a result of these discussions,
7 Staff, OPC and Tampa Electric agree as follows:
8 Public Counsel and Staff agree that the
9 specific contract format, including the pricing
10 indices which Tampa Electric may include in its
11 contracts with its affiliates, are not subject
12 to this proceeding and Tampa Electric may
13 negotiate its contracts with its affiliate in
14 any manner it deems reasonable. [emphasis
15 added]

16
17 With respect to TECO Transport and Trade ("TTT"), the
18 settlement agreement provides:

19 8. The parties agree that the record in this
20 proceeding indicates that the prices currently
21 paid by Tampa Electric to TTT are reasonable.

22 9. Tampa Electric, however, agrees to this
23 establishment of a benchmark price to be used
24 prospectively for regulatory review purposes.

25 10. The coal transportation benchmark price

1 will be the average of the two lowest comparable
2 publicly available rail rates for coal to other
3 utilities in Florida. This rail rate will be
4 stated on a cents/ton-mile basis representing
5 the comparable total elements (i.e.,
6 maintenance, train size, distance, ownership,
7 etc.) for transportation. The average cents per
8 ton-mile multiplied by the average rail miles
9 from all coal sources to Tampa Electric's power
10 plants yields a price per ton of transportation.
11 The result will become the "benchmark price" as
12 shown on Attachment 3.

13
14 The example transport benchmark calculation shown on
15 Attachment 3 to this order is the benchmark calculation
16 that has been in use since 1988. The Commission each
17 year thereafter made specific findings that the prices
18 paid under the waterborne transportation services
19 contract were below the market price as established by
20 the benchmark.

21
22 Moreover, in Order No. PSC-93-0443-FOF-EI issued March
23 23, 1993, this Commission approved a stipulation that
24 reaffirmed the waterborne coal transportation benchmark.
25 This stipulation remains in effect until changed by

1 Commission order. Staff or any other party may disagree
2 with that policy, but the policy is currently in effect
3 and was in effect at all times in 2003 when Tampa
4 Electric issued its RFP on June 27, 2003, evaluated its
5 future transportation services options and ultimately
6 executed a new contract with TECO Transport.
7

8 **Q.** Is Tampa Electric required to issue an RFP for waterborne
9 transportation services prior to executing a new contract
10 with its affiliate?
11

12 **A.** No. Tampa Electric is not required to issue an RFP. The
13 RFP is an information-gathering tool that provides market
14 price data. However, both the contractual requirements
15 of the existing contract with TECO Transport and the
16 policy of this Commission provide that contract rates can
17 be set through any reasonable market price determination.
18 As previously described, the Commission, in approving the
19 stipulation that established the transportation
20 benchmark, specifically stated, "Tampa Electric may
21 negotiate its contracts with its affiliate in any manner
22 it deems reasonable." [Order No. 20298, page 17]
23

24 **Q.** If Tampa Electric was not required to issue an RFP for
25 waterborne transportation services prior to executing a

1 new contract with its affiliate, why did the company do
2 so?

3
4 **A.** In early 2003, the company met with Florida Public
5 Service Commission Staff ("Staff") and parties on
6 numerous occasions to discuss various fuel issues,
7 including waterborne transportation. In those meetings,
8 Staff questioned the company about its plans for meeting
9 its transportation needs in 2004 and beyond. Staff
10 strongly encouraged Tampa Electric to issue an RFP.
11 Ultimately, Tampa Electric decided to issue an RFP as
12 part of its good-faith efforts to obtain the most
13 relevant and timely waterborne transportation market data
14 available.

15
16 **Q.** Was the RFP the only effort Tampa Electric made to
17 determine reasonable market prices for a waterborne
18 transportation services contract for the period 2004
19 through 2008?

20
21 **A.** No. The company also hired Brent Dibner of Dibner
22 Maritime Associates, LLC ("DMA"), an expert consultant in
23 the maritime industry, to conduct an independent
24 evaluation of the waterborne transportation markets.
25 This consultant's extensive knowledge of and experience

1 in these markets were utilized in modeling appropriate
2 and reasonable market rates for each segment of the
3 waterborne transportation services that Tampa Electric
4 requires. Tampa Electric also hired Sargent & Lundy
5 ("S&L"), an engineering design consulting firm, to
6 evaluate the rail proposals the company received in
7 response to its RFP.

8
9 **2004 Waterborne Coal Transportation Arrangements**

10 **Q.** Please describe in detail Tampa Electric's efforts to
11 secure reliable coal transportation for deliveries
12 beginning January 1, 2004.

13
14 **A.** In June 2003, Tampa Electric prepared a RFP for vendors
15 to provide proposals for waterborne deliveries of coal
16 from suppliers in the Midwest to its Big Bend Station.
17 The solicitation was sent to all 24 vendors known to
18 Tampa Electric and DMA to provide such transportation
19 services. The solicitation was also described in several
20 industry publications. This served to inform other
21 potentially interested parties, to whom copies of the RFP
22 were provided upon request. Tampa Electric followed a
23 similar RFP process to establish the contract for
24 waterborne transportation for the period 1999 through
25 2003. A comparison of the 1997 and 2003 bid processes is

1 provided as Document No. 2 of my exhibit.

2

3 **Q.** Did Tampa Electric state, in its RFP, a preference for
4 the services to be provided by an integrated provider
5 versus contracting for each segment of transportation
6 separately? If so, why?

7

8 **A.** Yes, the company's RFP did state such a preference.
9 Specifically, the RFP stated, "Tampa Electric prefers
10 proposals for integrated waterborne transportation
11 services, however proposals for segmented services will
12 be considered." Tampa Electric continues to prefer
13 integrated waterborne transportation services because of
14 the benefits of receiving priority handling of its coal
15 transportation needs, having first call on dedicated
16 transportation resources and benefiting from
17 administrative efficiencies from dealing with one entity
18 in the day-to-day management of the waterborne coal
19 transportation services. These factors greatly increase
20 the reliability and flexibility of Tampa Electric's fuel
21 delivery. The direct testimony of Tampa Electric's
22 witness Dibner enumerates the administrative efficiencies
23 that result from having a single contact point for all
24 services. In addition, the terminal in Davant, Louisiana
25 provides much needed storage, helps with quality control

1 issues and allows for custom coal blending. The terminal
2 is in an ideal location for deliveries from the Midwest
3 and can accommodate large vessels delivering
4 international shipments as well.

5
6 **Q.** Is the terminal near Davant, Louisiana the only location
7 or terminal facility that can meet Tampa Electric's
8 terminal services needs?

9
10 **A.** No. As stated in the RFP, "terminal facilities should be
11 accessible to Mississippi River barge traffic and capable
12 of receiving and discharging inland river barges from
13 domestic suppliers in Panamax-sized vessels for offshore
14 coal." Any terminal that meets this requirement and has
15 the flexibility and storage capacity to store different
16 types of coal in separate piles and to blend coal would
17 be able to meet Tampa Electric's needs.

18
19 **Q.** Why does Tampa Electric require, in the RFP, the ability
20 to receive coal at a terminal facility that is accessible
21 to Mississippi River barge traffic and able to receive,
22 unload and store Panamax-sized vessels for foreign coal?

23
24 **A.** The requirements included in the RFP are driven primarily
25 by Tampa Electric's coal quality requirements and supply

1 portfolio. The vast majority of Tampa Electric's coal
2 originates at docks on the Ohio River and the upper
3 Mississippi River system because the design fuel for Big
4 Bend Station boilers, Illinois Basin coal, is mined in
5 this area of the United States. This necessitates that
6 the transloading and storage terminal facilities be
7 accessible to Mississippi River barge traffic. It would
8 not be cost-effective to use any other waterborne
9 transportation system to deliver coal to Tampa from these
10 regions.

11
12 The company also purchases and blends foreign coal with
13 domestic coal and petroleum coke at the terminal for its
14 Polk Power Station. Foreign coal deliveries are
15 primarily made by the larger Panamax-sized vessels due to
16 efficiency concerns. A terminal that can receive larger
17 vessels provides Tampa Electric with the flexibility of
18 being served by a variety of vessels, providing the
19 company opportunities for discounted rates in the freight
20 market when available. The ability of the terminal to
21 receive and unload Panamax-sized vessels enables Tampa
22 Electric to rely on foreign coal blended with domestic
23 coal to meet operational and environmental requirements.

24
25 Q. Can Tampa Electric have foreign coal delivered directly

1 to Tampa rather than having it delivered to the terminal
2 and then to Tampa?

3
4 **A.** No. There are several reasons why Tampa Electric cannot
5 have foreign coal delivered directly to Tampa. First,
6 Tampa Electric's generating stations do not have deep
7 draft access that would allow a Panamax vessel, which is
8 the size typically used to transport foreign coal, to
9 approach, dock and unload coal. In addition, no other
10 facilities in Tampa that could be accessed by a Panamax
11 vessel have permits to store and blend coal, nor the
12 facilities to do so. Second, Tampa Electric requires the
13 use of a terminal facility for coal storage and blending.
14 Tampa Electric requires additional storage beyond what is
15 available at its generating stations to effectively
16 segregate and store the different types of coal it uses.
17 The company does not use foreign coal without blending it
18 with coal from domestic sources, and Tampa Electric does
19 not have existing facilities or the space to build
20 facilities to meet all of its blending needs at the
21 generating stations. As stated previously, no other
22 local facilities currently exist. Third, since Tampa
23 Electric's domestic coal must be processed at a terminal
24 facility prior to Gulf transportation, moving the foreign
25 coal to the terminal facility is currently the most

1 efficient and cost-effective method of handling foreign
2 coal. The foreign coal that must be transported to the
3 terminal represents less than ten percent of the total
4 coal used by Tampa Electric.

5
6 **Q.** Please describe the process that Tampa Electric used to
7 evaluate the bidders' proposals.

8
9 **A.** Tampa Electric took a systematic approach to evaluate the
10 bids. The main steps that formed the evaluation process
11 were:

12 1. Tampa Electric evaluated bids to determine
13 compliance with bid requirements. Late responses
14 and those that did not meet certain minimum
15 financial and operational criteria were
16 disqualified.

17 2. The company clarified proposal information through
18 discussions with individual bidders and requested
19 additional information, if needed, to fully evaluate
20 bids.

21 3. Tampa Electric made any adjustments required for bid
22 comparisons, such as where bid response terms and
23 conditions varied or did not meet RFP
24 specifications.

25 4. The company and its consultant used models to

1 determine the appropriate market rates for the
2 future contract, given the tonnage and length of
3 move requirements, where the company did not receive
4 a valid bid response.

5 5. A complete analysis of evaluated bids and an
6 assessment of the market were then provided to Tampa
7 Electric's management.

8 6. In accordance with terms of the then existing
9 contract between Tampa Electric Company and TECO
10 Transport, Tampa Electric provided the market rates
11 established during the process described above to
12 TECO Transport for its right of first refusal.

13 7. TECO Transport accepted the market rates, and Tampa
14 Electric proceeded with contract negotiations for
15 services for January 1, 2004 through December 31,
16 2008.

17 8. The new contract was executed on October 6, 2003,
18 and parties in Docket No. 030001-EI were provided a
19 copy for review.

20
21 **Q.** Why was TECO Transport given an opportunity to match the
22 established market prices?

23
24 **A.** A common practice in the fuel supply and transportation
25 business is to negotiate with suppliers a "Right of First

1 Refusal" clause in long-term agreements. Such a clause
2 existed in the contract between TECO Transport and Tampa
3 Electric.

4
5 **Q.** In general, why is it beneficial to include a "Right of
6 First Refusal" clause in these types of contracts?

7
8 **A.** The "Right of First Refusal" provision encourages the
9 vendor to provide these highly capital-intensive
10 transportation services while protecting the buyer, Tampa
11 Electric, as well as its ratepayers, through a periodic
12 re-assessment of the competitive market prices for these
13 services. In addition, the provision requires the vendor
14 to meet or beat current market prices, which benefits
15 ratepayers because it ensures the lowest prices for those
16 services.

17
18 **Q.** What evaluations did Tampa Electric perform regarding the
19 bids received in response to its solicitation for
20 waterborne coal transportation services?

21
22 **A.** Tampa Electric received one inland river bid, one
23 terminal bid and two rail bids. Tampa Electric evaluated
24 each of the four bids, with the assistance of two outside
25 consulting firms.

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Q. Please describe Tampa Electric's evaluation of the rail transportation bids received in response to its RFP for waterborne transportation services.

A. Tampa Electric received two rail transportation proposals in response to its RFP. Although the bids were non-conforming since they were not for the provision of waterborne transportation, Tampa Electric reviewed the responses and identified key factors related to the proposals that supported the need for further analysis. The first of these factors was the identification of necessary modifications and their associated costs for the capital improvements and new capital investment required for rail deliveries to Tampa Electric's generating stations. Tampa Electric's facilities currently do not have the infrastructure to directly receive rail deliveries. Secondly, the company recognized that there could be additional transportation costs, such as trucking costs from existing coal supply sources to a rail loading facility, that needed to be taken into account. Third, Tampa Electric needed to evaluate the impact on cost-effectiveness of acquiring coal from different supply locations in the event that rail service were used instead of waterborne

1 transportation services. Finally, the timing of the rail
2 service infrastructure construction had to be considered
3 given Tampa Electric's needs beginning January 1, 2004.
4 To aid Tampa Electric in evaluating the rail
5 transportation bids, the company hired S&L to review the
6 bids and complete an analysis of the above-mentioned
7 factors.

8
9 **Q.** Please describe S&L's methods for evaluating the costs
10 and associated operational considerations if rail
11 deliveries were made to the plants.

12
13 **A.** S&L reviewed the rail transportation bids, assessed the
14 capital costs proposed in the bids and determined other
15 costs and factors that should be evaluated by Tampa
16 Electric. As a result of its analysis, S&L determined
17 that it was necessary to modify the bidder's design to
18 reflect realistic design parameters that take into
19 account Tampa Electric's specific facilities and
20 operating needs. S&L also estimated costs that were
21 omitted from the bidder's proposal. The S&L cost
22 estimates included construction, installation,
23 modification and operating changes. For each of the
24 bidder's two proposals, S&L provided an analysis of
25 estimated capital costs, installation costs, fixed and

1 variable operating costs and demurrage costs. In
2 addition, the S&L report listed the environmental
3 considerations that would need to be studied prior to
4 acceptance of any of these proposals, such as additional
5 dust, noise abatement, wetlands reconstruction and permit
6 modifications.

7
8 The report from S&L stated that the capital costs
9 provided by the bidder included costs for new equipment
10 only and did not address installation or other
11 modification costs necessary to ready Tampa Electric's
12 facilities for direct rail deliveries. Nor were
13 operating costs addressed in the bidder's proposals. In
14 addition, S&L stated that given the facility design, the
15 unloading and demurrage rates included in the bidder's
16 proposal appeared aggressive and that this could result
17 in increased costs to Tampa Electric and its ratepayers.

18
19 **Q.** Was S&L's analysis thorough and complete?

20
21 **A.** Yes, it was. I have reviewed the data utilized and the
22 methods of analysis employed by S&L. I also asked Tampa
23 Electric personnel who specialize in generation
24 engineering to review the assumptions, analysis and
25 conclusions of the report. They concluded that the

1 report is a reasonable analysis of the costs of
2 installing rail unloading facilities at Big Bend and Polk
3 stations and of the operational and environmental impacts
4 of the rail transportation proposals. In addition, S&L
5 is a longstanding full-service engineering consulting
6 firm with extensive experience designing power plants and
7 related facilities. The S&L report was prepared under
8 the supervision of a Professional Engineer licensed in
9 Florida. Given this, I am satisfied that the analysis
10 completed by S&L was a thorough and complete
11 consideration of the factors that could reasonably be
12 anticipated to affect Tampa Electric's operations and
13 costs if either of the rail transportation proposals were
14 accepted.

15
16 **Q.** With respect to the rail transportation bids, what were
17 the results of the S&L analysis?

18
19 **A.** The results of the S&L analysis for each rail
20 transportation proposal showed that estimated capital
21 costs for infrastructure additions and improvements
22 greatly exceeded the bidder's estimates for these same
23 capital improvements. In addition, Tampa Electric would
24 incur additional operating expenses. In each case, the
25 capital, installation and facility modification costs

1 estimated by S&L exceed the bidder's estimates by more
2 than 400 percent. Operating costs were estimated to
3 increase by a minimum of one million dollars and up to
4 approximately three million dollars annually. Capital
5 costs could increase if additional environmental
6 restrictions are required, such as fully enclosed coal
7 transfer conveyors. These potential costs were not
8 included in the S&L analysis. Other costs, such as costs
9 for demurrage penalties and required environmental
10 studies, have not been quantified, but they are factors
11 that must be considered. S&L estimated that the total
12 costs to prepare Tampa Electric's facilities for direct
13 rail deliveries and for operational changes ranged from
14 \$27 million to over \$53 million.

15
16 **Q.** Did you consider any other factors when evaluating the
17 rail transportation proposals?

18
19 **A.** Yes. In addition to evaluating the high capital costs for
20 infrastructure and operating costs previously described,
21 Tampa Electric considered the impact on cost-
22 effectiveness of acquiring coal from different supply
23 locations in the event that rail transportation were used
24 instead of waterborne transportation. The company also
25 considered how the rail proposals would affect overall

1 transportation costs given Tampa Electric's current coal
2 supply contracts.

3
4 Tampa Electric has contracts with suppliers to deliver
5 coal to barges at various specific locations on the
6 Mississippi and Ohio rivers. Utilizing rail
7 transportation instead of waterborne transportation would
8 necessitate additional costs to truck or short haul the
9 coal from the suppliers' contractual delivery locations
10 to the nearest rail loading facilities. The company
11 determined that these costs could range from an
12 additional \$2.00 to as much as \$6.00 per ton, depending
13 on distance. Tampa Electric reviewed its portfolio of
14 coal sources and found that the vast majority of its
15 current coal supplies are not located close to rail
16 facilities. Using rail transportation would therefore
17 make these supply sources more expensive in the short run
18 and potentially non-competitive in price in the future.

19
20 As previously stated, the rail proposal grossly
21 understates or ignores substantial additional capital and
22 operating costs that must be considered to provide a
23 reasonable comparison. The incremental short haul
24 transportation cost to deliver coal to a rail facility is
25 easily quantified and reasonably certain, and it is a

1 true incremental cost of using rail service.
2 Consequently, incremental short haul transportation costs
3 must be included in an analysis of the total rail cost
4 alternative in order to have a meaningful comparison to
5 the waterborne transportation rate. It is also
6 appropriate to adjust for the bidder's synfuel adder;
7 expected demurrage charges, using the bidder's proposed
8 demurrage rates; the bidder's published tariff fuel
9 surcharge; and the incremental cost for rail deliveries
10 to Polk Station. When these estimated additional costs
11 are considered, the adjusted rail rate is well above the
12 market rates included in the TECO Transport contract
13 effective January 1, 2004. A detailed calculation is
14 shown in Document No. 3 of my exhibit.

15
16 There are other costs and impacts that needed to be
17 considered. Additional costs for environmental impact
18 mitigation and permitting or other factors would
19 certainly exist but were not included in the adjusted
20 rail rate. The rail proposals did not provide services
21 that are currently provided by the terminal facility as
22 part of the integrated waterborne transportation
23 contract. As previously stated, Tampa Electric requires
24 the ability to receive deliveries of foreign coal from
25 large, deep draft Panamax vessels as well as storage and

1 blending capabilities at a terminal facility to create
2 multiple custom blends of coal utilizing both domestic
3 and foreign coals. These facilities are not currently
4 available in the vicinity of Tampa, Florida, and the
5 company does not have the space to install them at its
6 plants. The company cannot receive Panamax vessels at
7 its plants due to draft restrictions. The rail proposals
8 also do not include costs for deliveries of pet coke from
9 Texas. Providing all of the above-listed services would
10 result in additional costs to Tampa Electric that
11 increase overall rail transportation costs.

12
13 Another important consideration was that the rail
14 proposals require significant time for construction prior
15 to the commencement of rail transportation service.
16 Since Tampa Electric's coal transportation needs began
17 January 1, 2004, the company would need to obtain short-
18 term waterborne transportation services to meet its
19 requirements until the rail construction could be
20 completed. The need for short-term waterborne
21 transportation services would certainly result in
22 increased costs that are not included in the rail
23 transportation proposals and would result in higher costs
24 to ratepayers.

25

1 Q. What did you conclude as a result of the evaluation of
2 the rail transportation proposals?

3
4 A. Given the significant costs for capital infrastructure
5 and the additional operating and transportation costs
6 that would result from choosing to use rail
7 transportation, as well as concerns about future supply
8 limitations due to the distance from a rail loading
9 facility, Tampa Electric determined that the bidder's
10 proposals were not competitive. I recommended rejecting
11 both proposals.

12
13 Q. Did Tampa Electric engage in other activities regarding
14 the evaluation of the other transportation proposals?

15
16 A. Yes. Tampa Electric hired DMA to assist with the
17 evaluation of waterborne transportation proposals. DMA
18 evaluated the waterborne transportation bids and
19 constructed market models to assess appropriate market
20 prices for the transportation services segments. DMA
21 provided Tampa Electric with its determination of the
22 appropriate waterborne transportation market prices in a
23 report that includes descriptions of its methodologies,
24 evaluations, market assessments and supporting
25 information. The report provided by DMA is provided as

1 an exhibit to the testimony of Tampa Electric witness
2 Dibner.

3
4 **Q.** Have you reviewed the models and analyses DMA used to
5 determine the appropriate market prices for each of the
6 three segments included in the waterborne transportation
7 system?

8
9 **A.** Yes, I have reviewed the proposals submitted in response
10 to Tampa Electric's RFP, the data used by DMA's
11 proprietary models, the modeling methodologies and the
12 analyses conducted by DMA to evaluate the waterborne
13 transportation bids and to determine the market price for
14 each segment of the waterborne transportation services.
15 DMA conducted a thorough and complete evaluation of the
16 bids. I believe that DMA's long experience in and
17 extensive knowledge of the maritime industry allowed it
18 to conduct a reasonable and thorough market assessment
19 and to establish market prices that accurately reflect
20 the markets for the services Tampa Electric requested.

21
22 **Q.** Do you agree with the recommendations made by DMA?

23
24 **A.** Yes, I do. I believe that they are reasonable and
25 appropriate and take into account the best information

1 available regarding the status of the waterborne
2 transportation markets and Tampa Electric's operational
3 requirements.

4
5 **Q.** How did Tampa Electric determine the appropriate market
6 prices for each of the three segments included in the
7 waterborne transportation system?

8
9 **A.** Tampa Electric reviewed the responses to the RFP and its
10 consultants' findings. The company also utilized its
11 knowledge of the waterborne transportation market and
12 Tampa Electric's needs. The company rejected some
13 proposals for the reasons previously described in this
14 testimony or in the testimony of Tampa Electric witness
15 Dibner. Tampa Electric then relied on the results of
16 DMA's report and the market prices established therein.

17
18 **Q.** Please describe DMA's findings or evaluation results that
19 were provided to Tampa Electric.

20
21 **A.** The inland river bid was only for a portion of Tampa
22 Electric's requirements, and the bidder is in Chapter 11
23 bankruptcy status. The bankruptcy and related activities
24 raised questions about the bidder's fleet status and its
25 potential to provide transportation services given its

1 existing financial circumstances. The terminal bid was a
2 bona fide bid for full terminal services. Tampa Electric
3 did not receive any ocean bids. Therefore, the terminal
4 bid determined the market price, and the market analysis
5 performed by DMA determined the appropriate market prices
6 for the inland river and ocean transportation segments.

7
8 **Q.** What recommendations did DMA make regarding the market
9 price components for a new waterborne transportation
10 contract?

11
12 **A.** DMA recommended cost structures comprising fixed and
13 variable charges, and a fuel component, if applicable,
14 for each segment. In addition, DMA recommended
15 escalation methodologies and initial fuel price levels.
16 They are detailed in Tampa Electric witness Dibner's
17 direct testimony.

18
19 **Q.** Are the rates determined through the RFP process,
20 industry review and market modeling sufficient to
21 determine appropriate market prices for this agreement?

22
23 **A.** Yes. Using the bids received in response to the RFP and
24 market analyses provided by Tampa Electric's consultant,
25 Tampa Electric has demonstrated that the prices

1 established by valid bid and by market modeling represent
2 the market for the transportation services that will be
3 provided under the new contract that began January 1,
4 2004. The activities that DMA performed to evaluate the
5 bids are described in detail in the testimony of witness
6 Dibner.

7
8 **Q.** Do you believe that appropriate market rates have been
9 established?

10
11 **A.** Yes. The appropriate market rates have been established
12 using the bona fide terminal bid received and the results
13 of the detailed and thorough analyses conducted by DMA
14 for the inland river and ocean transportation segments.

15
16 **Q.** After accepting the established market prices, how did
17 Tampa Electric proceed?

18
19 **A.** According to the terms of Tampa Electric's then existing
20 waterborne transportation contract, TECO Transport had
21 the right to review and decide to meet or beat the market
22 prices established. Therefore, Tampa Electric
23 communicated the rates to TECO Transport for that
24 purpose.

25

1 Q. What was the next step in establishing a new contract for
2 waterborne transportation services?

3
4 A. Tampa Electric negotiated a new contract with TECO
5 Transport and incorporated the terms established in the
6 solicitation and the rates provided as a result of DMA's
7 market analysis into a new five-year waterborne
8 transportation agreement. The contract was signed on
9 October 6, 2003.

10
11 Q. How do the market prices established for the new contract
12 compare to the waterborne coal transportation costs of
13 the contract for the previous period?

14
15 A. The market price established for the new contract is
16 [REDACTED] per ton lower than the rates that were in effect
17 for the third quarter of 2003, as shown on page 68 of
18 witness Dibner's report.

19
20 Q. How do the rates established in the new contract compare
21 to rail transportation rates for an equivalent level of
22 service?

23
24 A. Once the rail rate is adjusted to include all expected
25 and appropriate costs that could be quantified, including

1 incremental operating costs and the costs for capital
2 additions and improvements required to receive coal by
3 rail, the waterborne rate is [REDACTED] per ton less than the
4 rail rate. This is included in Document No. 3 of my
5 exhibit.

6
7 **Q.** Have any modifications been made to Mr. Dibner's market
8 analysis since the contract was executed on October 6,
9 2003 with TECO Transport?

10
11 **A.** Yes. In December 2003, Mr. Dibner notified Tampa
12 Electric that he had detected offsetting calculation
13 errors in his ocean transportation model. The correction
14 of the ocean model resulted in a market rate that is
15 \$0.03 per ton higher than the rate originally
16 communicated to TECO Transport and included in the
17 contract executed on October 6, 2003. The correction
18 also changed the fuel, fixed and variable composition of
19 the ocean segment rate.

20
21 **Q.** Were modifications made to the contract?

22
23 **A.** No, Tampa Electric's contract with TECO Transport that
24 was executed on October 6, 2003 was not modified because
25 TECO Transport had already accepted the lower rate and

1 related terms. Tampa Electric analyzed the new market
2 rate and found that the expected overall cost difference
3 between the two ocean-segment rates over the contract
4 period was insignificant. Tampa Electric reaffirmed that
5 the executed contract reflects appropriate market rates.
6

7 **Sufficiency of the Waterborne Coal Transportation Benchmark**

8 **Q.** How does the Commission independently verify that
9 waterborne coal transportation services are being
10 provided at a reasonable cost to Tampa Electric's
11 ratepayers?
12

13 **A.** This Commission established a waterborne coal
14 transportation benchmark to address this issue. Each
15 year Tampa Electric compares its actual cost for
16 waterborne coal transportation against the average of the
17 lowest costs paid by Florida municipal utilities for coal
18 deliveries by rail. The comparison is submitted to the
19 Commission for review, and as long as Tampa Electric's
20 actual cost is at or below the benchmark, the cost is
21 deemed reasonable. If Tampa Electric's waterborne
22 transportation costs exceed the benchmark in any given
23 year, the company must justify any costs greater than the
24 benchmark amount before the Commission allows recovery
25 through the fuel clause.

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Q. Is the waterborne transportation benchmark still sufficient to evaluate Tampa Electric's affiliated coal transportation costs?

A. Yes. In Order No. 20298, issued on November 10, 1988 in Docket No. 870001-EI-A, the Commission stated,

If one considers the objective of coal transportation to be the movement of coal from the mine to the generating plant, then rail service and the total waterborne system are not only comparable, but competitive to a large degree, as well. We believe using the average of the two lowest publicly available rail rates for coal being shipped to Florida will provide a reasonable market price indication of the value being provided by TECO's affiliate waterborne system.

Tampa Electric believes that the benchmark is still useful and sufficient for evaluating the prudence of its actual waterborne transportation costs and that the average rail rate comparison serves as a reasonable market proxy for waterborne transportation costs. This

1 benchmark is the best alternative for comparison
2 currently available. Tampa Electric witness Dibner also
3 addresses this issue in his direct testimony.
4

5 **Q.** Should Tampa Electric's waterborne coal transportation
6 benchmark methodology be modified or eliminated?
7

8 **A.** No. Tampa Electric believes the benchmark is still a
9 useful tool in evaluating the prudence of its waterborne
10 transportation costs. As stated above, the rail rate
11 comparison is the best alternative for comparison
12 currently available. In addition, to date Tampa Electric
13 has always been able to collect the verifiable
14 information necessary to calculate the benchmark for
15 timely filing with the Commission. However, if the
16 Commission decides the benchmark is no longer the
17 appropriate tool to evaluate Tampa Electric's affiliated
18 coal transportation costs, then Tampa Electric recommends
19 that the Commission totally eliminate the benchmark and
20 rely on the RFP results and market analysis completed in
21 2003 to determine that the contract costs are reasonable.
22 The market rates will be in effect for the next five
23 years with the escalation factors described in detail in
24 Mr. Dibner's testimony. The process conducted by Tampa
25 Electric in 2003, in lieu of the benchmark evaluation,

1 ensures that the company and its customers pay market
2 rates for waterborne transportation services provided by
3 the affiliate.
4

5 **Q.** Please summarize your testimony.
6

7 **A.** Although Tampa Electric was not required to issue an RFP
8 for waterborne transportation services, the company
9 engaged in extensive market survey and analysis
10 activities that included issuing an RFP, hiring two
11 specialized consulting firms to assist with its
12 evaluation of the bids received in response to its RFP
13 and directing one of these expert consultants to model
14 the waterborne transportation markets. S&L concluded
15 that the rail proposals received did not identify all of
16 the necessary capital costs to modify Tampa Electric's
17 facilities to accept rail deliveries, nor did they
18 account for changes in Tampa Electric's expected
19 operating costs. Tampa Electric determined that the rail
20 transportation proposals were not competitive
21 alternatives when all potential costs, the schedule for
22 completion of rail infrastructure construction and
23 environmental impacts were considered.
24

25 DMA provided Tampa Electric with an analysis of the two

1 waterborne transportation bids and a thorough and
2 effective study of the inland river, terminal and ocean
3 market rates that meet Tampa Electric's full requirements
4 for waterborne transportation services for the period
5 2004 through 2008. DMA's evaluation of the inland river
6 and terminal bids resulted in its recommendation to
7 reject the non-conforming river bid, to use the terminal
8 bid to set the market rate for that segment and to use
9 DMA's analysis of the transportation markets to set
10 appropriate market rates for the inland river and ocean
11 transportation segments. Tampa Electric agreed with
12 DMA's recommendations. Tampa Electric used these rates
13 to negotiate a new transportation contract with TECO
14 Transport for the years 2004 through 2008. As previously
15 stated, TECO Transport had the right to meet or beat the
16 market prices established for the new contract period,
17 under the terms of its then existing contract with Tampa
18 Electric. The market analysis and the RFP provided a
19 meaningful and sufficient basis to evaluate the
20 waterborne transportation markets and to determine the
21 appropriate market rates for Tampa Electric's new
22 contract for waterborne transportation services.

23
24 Finally, Tampa Electric's existing transportation
25 benchmark methodology remains valid. However, if the

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Commission determines that the methodology should be changed, Tampa Electric recommends that the benchmark be totally eliminated and that the RFP and market analysis should determine the reasonableness of Tampa Electric's transportation costs for the duration of the contract period.

Q. Does this conclude your testimony?

A. Yes, it does.

EXHIBIT NO. _____
TAMPA ELECTRIC COMPANY
DOCKET NO. 031033-EI
(JTW-1)
DOCUMENT NO.1
PAGE 1 OF 25
FILED: JANUARY 5, 2004

EXHIBIT TO TESTIMONY OF
JOANN T. WEHLE

DOCUMENT NO. 1

Order No. 20298

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into affiliated) DOCKET NO. 870001-EI-A
cost-plus fuel supply relationships) ORDER NO. 20298
of Tampa Electric Company.) ISSUED: 11-10-88
)

The following Commissioners participated in the disposition of this matter:

KATIE NICHOLS, Chairman
THOMAS M. BEARD
GERALD L. GUNTER
JOHN T. HERNDON
MICHAEL MCK. WILSON

APPEARANCES:

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ORDER IMPOSING MARKET-BASED PRICING ON COAL PRODUCED
FROM AN AFFILIATE AND ACCEPTING SETTLEMENT
AGREEMENT ON IMPLEMENTATION OF MARKET-BASED METHODOLOGY

BY THE COMMISSION:

SUMMARY

We have determined as a matter of policy that utilities seeking the recovery of the cost of coal purchased from an affiliate through their fuel and purchased power cost recovery

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clauses shall have their recovery limited by a "market price" standard, rather than under the "cost-plus" standard now in effect. We also have accepted a stipulation among the parties to this docket which provides a methodology for implementing the market pricing standard for not only the coal Tampa Electric Company (TECO) purchases from an affiliate, but the transportation and handling services it purchases from affiliates, as well.

BACKGROUND

In February, 1986, we opened Docket No. 860001-EI-G for the purpose of investigating the affiliated cost-plus fuel supply relationships between Florida Power Corporation (FPC) and TECO and their respective affiliated fuel supply corporations. Also in February, 1986, we had established Docket No. 860001-EI-F, Investigation Into Certain Fuel Transportation Costs Incurred By Florida Power Corporation in Order No. 15895 for the purpose of determining why FPC's costs to transport coal by its affiliated waterborne system exceeded its costs to transport coal by non-affiliate rail. In September, 1987, we issued Order No. 18122, which removed TECO from Docket No. 860001-EI-G, established this docket for hearing the TECO issues.

After considering the post-hearing briefs of the parties and our Staff's recommendations, we, at our September 6, 1988 Agenda Conference, determined that affiliated coal should be priced at market price for recovery through the utilities' fuel cost recovery clauses. We directed our Staff to conduct discussions amongst the affected parties for the purpose of determining how best to establish and implement market pricing mechanisms.

After extensive negotiations, the parties to this docket arrived at a stipulated agreement which provided a methodology for establishing "market" price proxies for all of TECO's affiliated fuel transactions. This Order describes the TECO hearing in this docket, as well as the stipulated agreement, which we accept and approve.

Before describing TECO's affiliated fuel and fuel transportation system, it is worth noting that TECO did not object to the adoption of a market pricing system so long as the system fairly represented the price received for comparable coal on the competitive market. TECO also took the position, as did all parties, that market pricing should cut both ways and that any lower of cost or market method or market price cap method should be rejected. While TECO took the position that cost-plus pricing has provided an effective means of ensuring that only reasonable and prudently incurred fuel costs have been passed on to its customers, it agreed that the cost-plus methodology was administratively costly and caused unnecessary regulatory tension because it left the lingering suspicion, even in the face of outstanding results, that it resulted in higher costs to customers than would have been available through arm's-length contracts. Consequently, as will be noted below, the hearing in this docket was not over whether a market pricing system should be adopted but, rather, how it should be adopted.

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THE TECO AFFILIATE SYSTEM

There are two primary components to the TECO affiliate coal supply system:

1. The coal supply affiliate (Gatliff Coal Company); and
2. The waterborne transportation system (TECO Transport and Trade Corporation).

Gatliff Coal Company

Gatliff Coal Company (Gatliff) is a subsidiary of TECO Coal, Inc. which, like TECO, is a subsidiary of TECO Energy, Inc. The other subsidiary of TECO Coal, Inc., Rich Mountain Coal Company controls a handling facility with coal-sizing capability on the Norfolk Southern Railroad in Tennessee, but is not currently operational and supplies no coal to TECO.

According to TECO witness John R. Rowe, Jr., Assistant Vice-President of TECO, TECO's Gannon Station units were constructed in the 1950's and 1960's with wet bottom boilers designed to burn Western Kentucky No. 9 coal having a 3% to 4% sulfur content and low ash-fusion temperature characteristics. This high sulfur, low ash-fusion coal was in abundant supply adjacent to the inland waterway system and was, said Rowe, the most inexpensive coal that could be purchased. However, with the passage of the Clean Air Act in 1970 and the associated Florida State Implementation Plan, TECO found it necessary to burn coal at Gannon Station which produced an average of not more than 2.0 lbs. per million BTU of sulfur dioxide, with a maximum of 2.4 lbs. per million BTU of sulfur dioxide. The requirement for coal that met the combined low sulfur and low ash-fusion characteristics created a serious fuel supply problem for TECO at its Gannon Station because such coal was extremely rare according to Rowe.

To meet the applicable air quality regulations, TECO converted four of the six coal burning units at Gannon Station to low sulfur oil and began a worldwide search in 1971 for a source of low sulfur, low ash-fusion coal that would be suitable for its boilers. The search revealed that there were many foreign and domestic coals that were low sulfur, but few that also met the necessary ash-fusion and slagging characteristics required of the Gannon wet bottom boilers. Suitable seams of coal were found in the western United States, but the high cost and lack of dependability of available transportation were of great concern to TECO and, ultimately, made the use of these coals prohibitively expensive. Polish coal was used for a time but labor and other problems shut off the supply of this coal in 1979-80. Ultimately, suitable eastern coals were narrowed to the Blue Gem seam in eastern Kentucky, and test burns in 1973 revealed that it could successfully be burned in the two largest Gannon Station units.

Gatliff (then named Cal-Glo Coal, Inc.) mined the Blue Gem seam in large quantities in a market that was dominated by many small producers. TECO first began purchasing coal from Cal-Glo

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in early 1973. Subsequently, when Cal-Glo experienced financial problems, TECO made it a loan to keep it viable and finally purchased the entire operation by August of 1974. In 1980, the State of Florida modified its sulfur dioxide emission limits to permit Gannon Units Nos. 1-4 to burn Blue Gem coal. Since then, all six units at Gannon station have burned Blue Gem coal. Cal-Glo Coal, Inc.'s name was changed to Gatliff Coal Company in 1982.

TECO's initial 1974 contract with Gatliff called for the price of coal to be established by an independent consultant's survey of market prices. This practice was continued until 1978 when this Commission ordered a change to a cost-plus a return on equity pricing system. See Order No. 7987 in Docket No. 760846. On March 2, 1978, TECO signed a new contract with Gatliff, which provided that coal would be mined and supplied to TECO on a cost-plus basis with Gatliff being entitled to earn the same mid-point return on its invested equity as allowed to TECO by this Commission. This contract was approved by the Commission in Order No. 8278 and its term was extended through December 31, 1996.

In 1981 this Commission hired the consulting firm of Emory Ayers Associates, Inc. to conduct a study to determine if the cost-based price paid by TECO to Gatliff was in line with market prices. The Emory Ayers study concluded that the cost-based coal price was in line with the market for the long term supply of this type coal and the study established a reasonable market price for this coal as of 1981.

TECO submits that its control of a sizable reserve of the relatively scarce Blue Gem coal in the eastern United States is absolutely critical to the reliable operation of its Gannon Station in view of the remaining lives of the boilers. TECO, said Rowe, believes this coal provides a least-cost alternative, which is superior to other environmental compliance solutions and assures that the utility will have a source of environmentally acceptable coal for the remaining lives of the Gannon units.

TECO Transport and Trade

TECO Transport and Trade Corporation, is a subsidiary of TECO's parent company, TECO Energy, Inc. TECO Transport and Trade in turn, has five separate subsidiary operating companies which make up the water transportation system. Except for a small (less than ten percent or about 500,000 tons per year) share of TECO's requirements of Gatliff's sales, which are delivered to Gannon Station directly by rail, all of TECO's coal is delivered to Big Bend and Gannon Stations by barge under the direction of TECO Transport and Trade Corporation.

Mid-South Towing, which was established in 1959, owns or operates ten tow boats and over three hundred river barges. It transports coal from the coal fields near the Ohio River to the Electro-Coal Transfer facility some 40 miles down river from New Orleans.

The Electro-Coal Transfer facility is over 200 acres in size, provides on-ground storage for 4.5 million tons and

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controls over three miles of riverfront. It was established in the early 1960s and provides a location for river vessels to discharge coal and transfer it to ocean vessels or to ground storage. Bulk products hauled for others are also stored or transloaded by Electro-Coal.

Gulfcoast Transit was established in 1959 to carry coal from Electro-Coal to TECO's generating stations. It owns 11 ocean-going, tug-barge combinations ranging in size from 9,000 tons to 38,000 tons. According to Rowe, Gulfcoast pioneered the ocean-going, coal shuttle idea for coal to peninsular Florida. Gulfcoast hauls coal for TECO and backhauls phosphate and other bulk products for others. When Gulfcoast delivers the coal to Tampa, it is off-loaded by G. C. Service Company, TECO Transport and Trade's stevedoring and snip repair group. TECO Towing, the fifth component of TECO Transport and Trade, was formed to move ICC-regulated bulk commodities and is currently inactive. According to Rowe, the third party transactions have provided significant savings to TECO's ratepayers by spreading the fixed costs of affiliated operations over a larger tonnage base.

Mr. Rowe testified that the transportation system was formed to lower costs and provide reliable transportation of coal for the benefit of the utility's ratepayers. He said that when the system was first formed, rail rates to Florida from the Midwestern coal fields were so high that coal was not competitive with oil. Because TECO did not want to be held captive by excessive dependence on rail transportation and a reliable water system for coal delivery to Florida did not exist, TECO, said Rowe, took the initiative and developed a water transportation system beginning in 1959 with the formation of Gulfcoast and Mid-South. Initially joint ventures with Peabody Coal Company and Virginia-Carolina Chemical Company, these operations were wholly-owned by TECO by May of 1968.

From 1959 to 1965 the transfer of coal from river barges to ocean vessels was accomplished by "mid-streaming" (direct vessel-to-vessel transfer at anchor) between New Orleans and Baton Rouge. When the mid-streaming proved unsatisfactory for the long term, TECO and Peabody Coal Company first leased an existing transloading facility at Myrtle Grove and, then, in October, 1968, incorporated Electro-Coal for the purpose of building and operating a more modern transloading and storage facility at Davant, Louisiana, some two miles south of Myrtle Grove on the Mississippi. According to Rowe, the new Electro-Coal facility was finished in 1965 and survived Hurricane "Betsy," which virtually demolished the old Myrtle Grove terminal. By May, 1968, TECO had purchased Peabody's 50 percent ownership in Electro-Coal and, thereafter, wholly-owned all of the transportation companies.

Mr. William N. Cantrell, Vice-President for Regulatory Affairs for TECO, testified that the cost-plus pricing system should be modified because it had caused: (1) substantial regulatory concerns for the Commission; (2) a substantial commitment of resources by the utilities in complying with the Commission's regulatory needs; and (3) ratepayer doubts concerning the use of a cost-plus concept. He said that while

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TECO believed that the cost-plus pricing system had been fair and reasonable from its ratepayers' prospective, the utility had undertaken a search for another acceptable pricing alternative, which would continue to provide an assured, reliable source of services and products from affiliates, at a competitive price, with far less regulatory tension.

Mr. Cantrell stated that the market price approach was attractive from a theoretical point of view because it should reflect the arm's-length value of the goods or services being transferred. To do this properly, he said, involved being able to identify the proper product and geographic markets in order to compute comparable market prices. He added that doing this was extremely difficult in the case of the waterborne transportation of coal to Tampa, as provided by TECO Transport Trade, and the supplying of low sulfur, low ash-fusion coal produced by Gatliff. Cantrell said that despite the lack of comparables for the waterborne transportation and the Blue Gem coal, it was still possible to develop a market-based approach by establishing a base price, using an analysis of the market, and then provide for indexing of the base price in the same manner as did many arm's-length contracts negotiated by independent parties. He said that TECO was proposing such contracts for both Gatliff Coal and TECO Transport and Trade.

As testified to by Cantrell, TECO proposed a new coal contract with a term of ten years and a minimum annual tonnage of 1.1 million tons. It would have a base price set for the 1.1 million minimum tonnage level and a lower price for supplemental tonnage above the minimum. According to Cantrell, the proposed base prices would ensure that TECO, at the inception of the contracts, would pay no more for coal than it did under the cost-plus pricing system. Beginning in 1989 the price would be adjusted quarterly based upon appropriate indices. During the fifth year of the contract, a price adjustment of plus or minus 10 percent could be made in the adjusted contract price if it differed from an assessment of what the market price of the coal would be. Thereafter, the new contract price would be adjusted on a quarterly basis by the use of indices. During the tenth contract year, TECO would again assess the marketplace and determine a market-based price for the coal needed at Gannon Station. Gatliff would have an opportunity to match the market price and, thereby, extend the contract or to decline and allow TECO to contract elsewhere.

Mr. Cantrell said that the base price under the proposed coal contract would be similar to the price paid under the current contract, which he said was at or below the market for coals of a quality that could be burned at Gannon Station. He said that the base coal contract price would be indexed by publicly reported indices related to "labor," "materials and supplies," and "maintenance and equipment."

According to Cantrell, the new transportation contracts would have terms of ten years with minimum annual tonnages of 1,750,000 tons for river transportation and 4,000,000 tons for the terminal and Gulf transportation. As with the proposed coal contract, the proposed transportation contracts would have base prices for the minimum tonnage levels and lower base prices for supplemental tonnages. Like the coal contract, the

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transportation contracts would be indexed for their first five years with a market-price adjustment in the fifth year based upon an assessment of the market. In the tenth year, the market would again be reassessed with TECO Transport and Trade having the opportunity to match the new price.

Mr. Cantrell said the base price for the transportation contracts would be similar to the price paid under the cost-plus contract, which he said was, by all measures that TECO could find, below a market price for the transportation of coal. The transportation base prices would be indexed by publicly reported indices for "fuel" and "variable" components.

Mr. Cantrell closed by saying that the proposed contracts represented a market-based approach because they were similar to the base price, indexed contracts commonly entered into between arm's-length parties in the competitive market.

Ms. Roberta S. Bass, a Planning and Research Economist in the Fuel Procurement Bureau of the Commission's Division of Electric and Gas, provided an overview of the organizational structure of TECO Transport and Trade Corporation and TECO Coal Corporation. In addition to describing the organizational relationships discussed in Mr. Rowe's testimony, Ms. Bass described the contractual relationships between TECO and the various affiliates and the manner in which costs were allocated between TECO and non-utility business. Generally, TECO's affiliated goods and services have been provided at the cost of providing them, plus a return on invested equity at a rate equal to that of the mid-point on equity authorized to TECO by this Commission. Likewise, costs are allocated between TECO and third party business directly, where possible, and otherwise on a percentage-of-use basis.

Mr. Hugh Stewart, General Engineer at the Federal Energy Regulatory Commission, testified on behalf of the Staff of the Florida Public Service Commission. Mr. Stewart testified that TECO's affiliate coal program had generally been successful because it took the time to determine that the coal transportation and production services were cost-effective before it acquired an ownership interest in the facilities. In this regard, he cited a study prepared for TECO, by an independent consultant, before it committed to coal, showing that coal could be economically produced and shipped to the Gannon Station. In the same vein, Stewart said that it was only after contracting in the competitive market for coal supply and transportation services that TECO acquired its ownership interest in the barge operations and the transloading facility. Stewart also testified that TECO contracted with an independent coal mine engineering consultant to determine the cost of producing coal from the Gatliff reserves before acquiring an ownership interest in those reserves.

Mr. Stewart acknowledged that if the wet bottom boilers at TECO's Gannon Station were to operate at maximum efficiency, TECO not only had to obtain coal with low sulfur levels, but low ash-fusion characteristics too. He acknowledged that coal of this type is relatively scarce and said that, after an apparently extensive search, TECO discovered that coal of this type was being mined by Coal-Glo Coal, Inc. from the Blue Gem

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Seam in eastern Kentucky. Stewart noted that TECO executed a ten year contract with Coal-Glo for the supply of coal and did not acquire an ownership interest in the mining company until after the mine experienced financial difficulties.

Mr. Stewart discussed the several expansions of annual throughput capacity that had been accomplished at the Electro-Coal Terminal and voiced the opinion that the 1969 expansion from 4.0 to 6.0 million tons per year was justified by TECO's Big Bend generating units, the first of which was scheduled to come on line in 1970. He said that it was his opinion that the subsequent expansions - to 12.0 million tons per year in 1982 and to 25.0 million tons per year in 1984 - were to meet expected export markets and that no allocation of these expansions should be made to TECO's utility business.

On cross-examination, Mr. Stewart acknowledged that he had developed a "sanity check," using the publicly reported rail coal rates paid by Florida municipally-owned utilities, which showed that the total transportation costs paid by TECO to its affiliate were less than the surrogate rail cost.

Mr. John Pyrdol, Energy Economist with the Energy and Fuels Analysis Branch of the Federal Energy Regulatory Commission, also testified on behalf of the Staff of the Florida Public Service Commission for the purpose of discussing the benefits of a market price cap for affiliated transactions and to calculate the market price for the coal TECO purchases from its affiliate, the Gatliff Coal Company.

Mr. Pyrdol stated that it was important to utilize a market price for the allowable cost of coal purchased from an affiliate because a market price attempted to replicate a price resulting from an arm's-length transaction, where a utility would have nothing to gain, and something to lose, by accepting a higher than market-competitive price. By contrast, he said, a utility's incentive to pay the lowest possible price for coal may be blunted or otherwise subordinated by a willingness to accept a higher price from an affiliate mining operation. Pyrdol contended that this willingness to accept a higher affiliate price could stem from either: (1) a desire to keep the affiliate "whole", even if the affiliate prices are excessive; or (2) to help the affiliate earn greater profits.

Mr. Pyrdol testified that cost-plus contracts of the type between TECO and its affiliates are used almost solely when a utility is buying coal from an affiliate supplier and almost never in arm's-length contracts. He said that the most common form of arm's-length contract in the utility coal business is the base price plus escalator contract. According to Pyrdol, the cost-plus contract allows the seller to recover all of its costs plus a guaranteed profit. This allows the utility to keep its affiliate supplier whole by paying all of its costs of production, while insuring its profit margin. In contrast to this type of contract, Pyrdol said the base price plus escalator contract does not give the supplier a guaranteed, full cost pass-through, plus guaranteed profit. Rather, he said, the base price plus escalator contract is set up to have the price reflect competitive market conditions, both when the base price is established and in any changes made to this

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price. In the base price plus escalator contract, a base price is established at the outset of the contract, and then the price is changed by a set of market-sensitive indices which can increase or decrease the price. These indices, which are a subject of contract negotiation, typically are publicly reported and reflect changes in the components of production such as labor, fuel, taxes and others. These contracts may also contain "market recaper" provisions, which, after a given number of years, allow the base price to be raised or lowered to meet the current market.

Pyrdol said that the risk of non-recovery of costs in the competitive, arm's-length coal transaction is borne by the seller, not the buyer. He said that, similarly, this risk should be borne by the affiliate mine and not by the ultimate buyer, the utility ratepayer. Pyrdol testified that it was his opinion that all of TECO's affiliate fuel-related contracts suffered from the same potential conflicts of interest that the coal contract was subject to, and that market-price caps should be established for the barge and transloading contracts as well. He added that he did not have the necessary information to construct the transportation-related market prices and was, therefore, testifying only to a market price cap for Gatliff coal. Mr. Pyrdol noted that the Federal Energy Regulatory Commission has used a market price test and cap for affiliated coal operations since 1981.

Mr. Pyrdol said that there are many unique characteristics found in different regional and local coal markets serving different utility power plants and that, therefore, the calculation of a market price must consider the particular circumstances of the coal market in question. He said that there are essentially three steps to be followed in determining a market price for a given coal. First, the product market must be identified. Second, the geographical boundaries of the market must be determined. Third, select transactions should be examined within the product and geographic markets in order to determine the market price.

In constructing his market price cap for Gatliff coal, Pyrdol testified that he accepted TECO's representations that the Gannon boilers required low sulfur coal with low ash-fusion characteristics and, therefore, limited his analysis to similar quality coal. He next determined this type coal was found in limited quantities in eastern Kentucky, parts of Alabama, Illinois, Tennessee, Virginia and in some western states. After further analyzing these coal sources, he determined to further limit his analysis to coal produced in the Blue Gem Stream in eastern Kentucky, where Gatliff is located.

In determining which transactions to include in his analysis, Pyrdol elected to eliminate transactions on the spot market and focus on transactions involving longer-term, larger-volume contracts because the Gatliff transaction is a contract arrangement. He further determined that, generally, eastern utilities do not utilize coal that is both low in sulfur and in ash-fusion temperature and, therefore, it was difficult to find price information to calculate a market price for the Gatliff coal. In lieu of the market price information of comparable coal, Pyrdol used a 1981 study commissioned by

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this Commission entitled "A Market Survey of Boiler Fuel for Tampa Electric Company's Gannon Plant." This study, which was conducted by Emory Ayers Associates, Inc. and filed with this Commission on June 1, 1981, identified a contract market price for Blue Gem coal of \$40 per ton as of 1981. To arrive at an adjusted market price for Blue Gem coal for each year 1981-1987, Pyrdol said he adjusted the 1981 \$40/ton price for the Gatliff coal by the average annual percentage change in prices experienced by all coal produced in Bureau of Mines District (BOM) No. 8. BOM No. 8 includes eastern Kentucky, southern West Virginia, and parts of Virginia and Tennessee, and, according to Pyrdol, is the source of the highest-quality, highest-priced coal produced in Appalachia. Mr. Pyrdol said that when he compared the adjusted market prices to the actual prices TECO paid to Gatliff, he concluded that the Gatliff prices had been in line with the market price from 1981 to 1985 but had been higher than the market in 1986 and 1987.

Mr. Pyrdol recommended that the Commission limit the recovery of Gatliff coal through TECO's fuel adjustment clause to the adjusted market price for all future sales of the Gatliff coal to TECO. In doing so, Pyrdol noted that only a portion of the so-called Gatliff coal is actually produced by the Gatliff mine. He said the rest is purchased from independent mines at a price (\$28-\$31/ton in 1984) significantly below the cost of coal to TECO, and averaged for cost purposes with the coal actually produced by Gatliff. Specifically, Pyrdol said that in 1986, Gatliff actually produced 689,000 tons of coal while it bought 860,000 tons from other producers. Mr. Pyrdol took the position that the adjusted market price resulting from his methodology should only apply to the coal actually produced by Gatliff, while the less expensive coal that Gatliff buys from independent mines and resells to TECO should reflect the actual purchase price to Gatliff and not the higher market price. He said that since the Gatliff/TECO coal contract required TECO to take only a minimum of 500,000 tons per year, TECO should minimize the take of Gatliff coal and maximize its take of the less expensive Blue Gem coal produced by independent suppliers.

On cross-examination, Mr. Pyrdol acknowledged that his adjusted market price was based upon the total sales of BOM No. 8 coal to utilities and that it did, in fact, include some sales under spot market contracts. He accepted the removal of the spot sales as being reasonable and acknowledged that their removal, plus a quality characteristics adjustment suggested by TECO's Mr. Cantrell would increase his 1987 adjusted market price for Gatliff coal from approximately \$36.60/ton to about \$39.60/ton.

Mr. Harry T. Shea, Chief of the Bureau of Fuel Procurement, Division of Electric and Gas, Florida Public Service Commission, testified on behalf of the Commission Staff. Mr. Shea testified that the Commission's fuel procurement guidelines contained in Order No. 12645 state that all purchases from affiliated companies should be priced at levels not to exceed those available on the competitive market and that contracts with affiliated companies should be administered in a manner identical to the administration of a contract with an independent company. Mr. Shea said the

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Commission should evaluate the reasonableness of the cost of fuel-related goods and services obtained from affiliate companies by one of three methods.

Mr. Shea's first and preferred method, where possible, was to establish a "market test" or market price by comparison to the price of similar products or services purchased in competitive markets. His second preferred method was by comparison to a price calculated by allocating an affiliate's fixed and variable costs to utility operations and non-utility operations based upon tonnage or some other appropriate measurement. A return on invested equity could be set equal to the midpoint of the utility's allowed range or equal to that realized by other companies in the same type of business. Mr. Shea's third and least preferred methodology was essentially a cost-of-service methodology that would involve reviewing the affiliate's expenses and capital structure to determine what a reasonable price should be. Shea stressed that the last methodology should only be employed when the market test and cost allocation methodologies were not applicable.

Mr. Shea testified that he would recommend using the methodology presented by Mr. Pyrdol to evaluate a comparable market (F.O.B. mine) price for Gatliff Coal Company. He said that he agreed with Pyrdol that a market price evaluation would be preferable for TECO's transportation affiliates, but added that he could not recommend such a methodology because he was unable to identify a sufficient number of comparable transactions to define a market price for the services provided by these companies.

CONCLUSION

As a result of this hearing and the companion hearing in Docket No. 860001-EI-G concerning Florida Power Corporation, we have concluded that it is desirable, where possible, to gauge the reasonableness of fuel costs sought to be recovered through a utility's fuel adjustment clause by comparison to a standard that attempts to measure what a given product or service would cost had it been obtained in the competitive market through an arm's-length contract with an unaffiliated third party. We believe that limiting cost recovery in this manner will best serve the interests of TECO's customers by insuring that they are not required to pay more than a market price for the fuel component of their electricity because of an affiliation between their utility and a fuel supplier.

We note that no party to this docket has alleged that either TECO's Gatliff coal or its TECO Transport and Trade rates are unreasonable and should be disallowed. In fact, after accepting the adjustments urged by TECO, witness Pyrdol's adjusted market price for Gatliff coal was within a dollar of the actual price then being paid for that coal. Likewise, TECO's affiliated waterborne rate for the entire route was shown to be significantly lower than the comparable rail rate/ton/mile being paid by several Florida Municipal electrical systems, whose coal and transportation rates are publicly reported.

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Irrespective of whether any imprudence or unreasonable expenses are found and disallowances made, we agree with the parties to this case that a change from cost-plus pricing is warranted. While we believe that the current system has been generally successful in allowing only reasonable and prudent costs to be passed through the utilities' fuel adjustment clauses, we concur with TECO's position that it has been administratively costly, caused unnecessary regulatory tension, and left the lingering suspicion that it has resulted in higher costs to a utility's customers.

Implicit in cost-plus pricing is the requirement that one is capable of conducting a cost-of-service analysis of a business to determine that its expenses are both necessary and reasonable. This is a methodology that is demanded for monopoly utility services, and which usually proves to be complex, expensive and time consuming. It is a methodology which requires a high degree of familiarity with the capital requirements and expenses necessitated by the operation of the business being reviewed. Cost-of-service analysis of affiliate operations places additional demands upon the regulatory agency in terms of time, expense and acquiring additional expertise. All come at some additional cost that must eventually be borne by the ratepayer, either in his role as a customer or as a taxpayer. Furthermore, there seems to be no end to the types of affiliated businesses that we are expected to become sufficiently familiar with so that we might judge the reasonableness of their costs on a cost-of-service basis.

Cost-of-service regulation for public utilities is necessitated by their monopoly status and the attendant lack of significant competition, if any, for their end product. Cost-of-service regulation exists as the proxy for competition to insure that utilities provide efficient, sufficient and adequate service and at a cost that includes only reasonable and necessary expenses. Cost-of-service regulation of some type is essential when there is no competitive market for the product or service being purchased; it is superfluous when such a competitive market exists.

There is another reason for switching to a market pricing system that was alluded to in TECO's statement that the current system, no matter how outstanding the results, left lingering suspicions that it resulted in higher costs. That this might be true may be seen by contrasting affiliated and non-affiliated contracts. The latter, with few exceptions, are characterized by arm's-length transactions entered into in the competitive marketplace. Typically, the contracts result from competitive bidding systems in which the contract is awarded to the qualified bidder submitting the lowest bid. In any event, the utility's negotiator has clearly defined loyalties and knows whose interests he or she is to protect. In contrast to this, the typical affiliate contract is let without the benefit of competitive bidding. Instead, confident that the contract will be given to the affiliate, representatives of the two companies negotiate the rate at which the product or service will be purchased.

Considering the many advantages offered by a market pricing system, we, as a policy matter, shall require its

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adoption for all affiliated fuel transactions for which comparable market prices may be found or constructed.

In concluding, we note the following caveats: (1) from the record in this case, we are convinced that market prices can be established for the affiliated coals; (2) market prices for the transportation-related services should be established if possible, but if not, methodologies for reasonably allocating costs should be suggested; and (3) cost-of-service methodologies should be avoided, if possible

PROPOSED STIPULATION AGREEMENT

In accordance with our directions at our September 6, 1988 Agenda Conference, our Staff, the Office of Public Counsel and TECO met to discuss the methods by which market pricing could be adopted for the affiliated coal and coal transportation transactions between TECO and its affiliates. As a result of numerous and lengthy negotiations, the parties have arrived at a Stipulation (Attachment A to this Order) which they have submitted for our approval.

According to the Stipulation, TECO shall be free to negotiate its contracts with its affiliates in any manner it deems to be fair and reasonable. TECO agrees to prudently administer the provisions of its contracts. Furthermore, TECO agrees to report to the Commission the actual transfer prices paid by it to its affiliates under the contracts in the normal course of the fuel adjustment proceedings.

With respect to Gatliff Coal Company, the Stipulation provides a benchmark for regulatory review of the coal purchased by TECO from Gatliff by utilizing an initial market price for TECO's transactions with Gatliff of \$39.44/ton F.O.B. Mine, as of December 31, 1987. For purposes of regulatory review, this base price will be escalated or de-escalated by the annual percentage change in BOM District 8 Data for Coal Shipments as reported on Form 423 for the weighted average price per million BTU of contract transactions (excluding all spot transactions), which meet TECO's Gannon Station specifications for heat content, sulfur content, ash content, and content and pounds sulfur dioxide per million BTU. An example of the benchmark market price and calculation is shown on Attachment 1 to the Stipulation, as well as the Gannon Station coal specifications.

As described in Paragraph 7 of the Stipulation, a 5% zone of reasonableness will be established around the adjusted market price for purposes of regulatory review. TECO's actual transfer price paid to Gatliff, based upon the total average price of Gatliff produced coal and coal purchased and resold as Gatliff coal, would be the cost allowed for recovery through TECO's fuel adjustment clause so long as the transfer price fell within the described zone of reasonableness. If the actual transfer price exceeded the ceiling of the 5% zone of reasonableness, the excess would be disallowed for recovery unless TECO adequately justified the reasonableness and prudence of the excess. (See Appendix 2 to the Stipulation). If the actual transfer price fell below the floor of the 5% zone of reasonableness, TECO would recover through its fuel

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clause only the actual transfer price.

Pursuant to the Stipulation, the parties agreed that the record in this proceeding indicated that the prices currently paid by TECO to TECO Transport and Trade are reasonable. Notwithstanding this, TECO agrees to the establishment of a benchmark price for coal transportation services to be used prospectively for regulatory review purposes. While TECO stated that it will execute its new contracts with TECO Transport and Trade at approximately the currently existing rates, which are less than current rail rates between the same points, the reasonableness of its actual transfer price for all of the transportation and transportation-related services from mine to generating plant would be compared to a coal transportation benchmark price. As shown on Attachment 3 to the Stipulation, the transportation benchmark would be calculated by averaging the two lowest comparable publicly-available, rail rates (in cents per ton-mile) for coal to other utilities in Florida and then multiplying that average times the average rail miles from all of TECO's coal sources to TECO's generating plants. The product would then have added to it the costs of privately-owned rail cars on a per ton, per trip basis. The total would be the coal transportation benchmark price. The actual transportation transfer price paid by TECO to TECO Transport and Trade, pursuant to its contracts, would be recoverable through the fuel adjustment clause, as long as it was equal to or less than the benchmark price. Any excess above the benchmark would be disallowed for cost recovery unless justified by TECO.

Pursuant to its terms, the Stipulation would be effective upon Commission approval, which was provided at our October 18, 1988 Agenda Conference.

In his letter forwarding the Stipulation, counsel to TECO represented that he had supplied counsel to the Florida Industrial Power Users Group (FIPUG) [the only other party to the proceeding] with a copy of the Stipulation and had been advised that FIPUG had no objection to the Commission's final action on it.

We believe that the proposed Stipulation meets our policy guidance and is in the public interest and shall, therefore, approve it. Briefly, with respect to the coal, the initial price is consistent with witness Pyrdol's modified methodology for vintaging the 1981 cost determined by the Emory Ayers study. Likewise, the initial price is consistent with the price TECO has recently been paying for this coal, a price no party has sought disallowances for.

The initial coal benchmark price will be escalated or de-escalated by the average annual percentage change in a large number of contract coal transactions for coal mined in the same BOM District as the Gatliff coal. Only those contracts that meet or exceed TECO's Gannon Station quality specifications will be included. These factors, coupled with the fact that many of these contracts were executed at approximately the same time as the Gatliff contract, go a long way towards fulfilling the goal of replicating a comparable coal for market pricing purposes. We are confident that the changes indicated by this

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large group of contracts will adequately reflect changes in the "market."

If one considers the objective of coal transportation services to be the movement of the coal from the mine to the generating plant, then rail service and the total waterborne system are not only comparable, but competitive to a large degree, as well. We believe using the average of the two lowest publicly available rail rates for coal being shipped to Florida will provide a reasonable market price indication of the value being provided by TECO's affiliate waterborne system.

In view of the above, it is

ORDERED by the Florida Public Service Commission that market-based pricing for affiliate fuel and fuel transportation services shall be used for the purposes of fuel cost recovery where a market for the product or service is reasonably available. It is further

ORDERED that the Stipulation (Attachment A) of the parties to this docket detailing methodologies for calculating market prices for Gatliff coal and the coal transportation services of TECO Transport and Trade Corporation is approved.

By ORDER of the Florida Public Service Commission, this 10th day of NOVEMBER, 1988.

STEVE TRIBBLE, Director
Division of Records and Reporting

(S E A L)

MBT

by: Kay Ferguson
Chief, Bureau of Records

NOTICE OF FURTHER PROCEEDINGS OR JUDICIAL REVIEW

The Florida Public Service Commission is required by Section 120.59(4), Florida Statutes, to notify parties of any administrative hearing or judicial review of Commission orders that is available under Sections 120.57 or 120.68, Florida Statutes, as well as the procedures and time limits that apply. This notice should not be construed to mean all requests for an administrative hearing or judicial review will be granted or result in the relief sought.

Any party adversely affected by the Commission's final action in this matter may request: 1) reconsideration of the decision by filing a motion for reconsideration with the Director, Division of Records and Reporting within fifteen (15) days of the issuance of this order in the form prescribed by Rule 25-22.060, Florida Administrative Code; or 2) judicial

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review by the Florida Supreme Court in the case of an electric, gas or telephone utility or the First District Court of Appeal in the case of a water or sewer utility by filing a notice of appeal with the Director, Division of Records and Reporting and filing a copy of the notice of appeal and the filing fee with the appropriate court. This filing must be completed within thirty (30) days after the issuance of this order, pursuant to Rule 9.110, Florida Rules of Appellate Procedure. The notice of appeal must be in the form specified in Rule 9.900(a), Florida Rules of Appellate Procedure.

ATTACHMENT A

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Investigation into Affiliated) DOCKET NO. 870001-EI-A
Cost-Plus Fuel Supply Relationships) Submitted for filing 10/13/88
of Tampa Electric Company)

STIPULATION

1. At the Commission's Agenda Conference on September 6, 1988, the Commission reviewed the affiliated cost-plus fuel supply relationships between Tampa Electric Company ("Tampa Electric") and its affiliates, Gatliff Coal Company ("Gatliff") and TECO Transport and Trade ("TTT"), and determined that cost-plus pricing should be replaced with market pricing for fuel supply relationships of Tampa Electric wherever possible.

2. In accordance with the Commission's direction, Staff, Office of Public Counsel ("OPC") and Tampa Electric have met to discuss the methods by which market pricing can be adopted for the affiliated coal and coal transportation transactions between Tampa Electric and its affiliates. As a result of these discussions, Staff, OPC and Tampa Electric agree as follows:

3. Public Counsel and Staff agree that the specific contract format, including the pricing indices which Tampa Electric may include in its contracts with its affiliates, are not subject to this proceeding and Tampa Electric may negotiate its contracts with its affiliates in any manner it deems to be fair and reasonable. Tampa Electric agrees to prudently administer the provisions of such contracts.

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4. The transfer prices paid by Tampa Electric under contracts with its affiliates shall be reported to this Commission in the normal course of the fuel adjustment proceeding.

Gatliff Coal Company

5. In order to provide a benchmark for regulatory review of the coal purchased by Tampa Electric from Gatliff, Staff, Public Counsel and Tampa Electric agree that the initial market price to be used for computing the regulatory benchmark for Tampa Electric's transactions with Gatliff should be \$39.44/Ton FOB Mine as of December 31, 1987.

6. For purposes of regulatory review, this base price should be escalated/de-escalated by a market based index described in Attachment 1 to this Stipulation.

7. For purposes of regulatory review, the benchmark price shall be a band of 5% around the adjusted price determined as described in paragraph 6.

6. The results of this calculation will be applied as follows:

a. The benchmark price will be used to evaluate the average purchased price of coal from Gatliff.

b. Prices paid above the benchmark would be disallowed for cost recovery, unless justified by Tampa Electric.

c. An example application of this methodology is shown in Attachment 2 to this Stipulation titled "Public Counsel's Market Price Application."

TECO Transport & Trade

8. The parties agree that the record in this proceeding indicates that the prices currently paid by Tampa Electric to TTT are reasonable.

9. Tampa Electric, however, agrees to the establishment of a benchmark price to be used prospectively for regulatory review purposes.

10. The coal transportation benchmark price will be the average of the two lowest comparable publicly available rail rates for coal to other utilities in Florida. This rail rate will be stated on a cents/ton-mile basis representing the comparable total elements (i.e., maintenance, train size, distance, ownership, etc.) for transportation. The average cents per ton-mile multiplied by the average rail miles from all coal sources to Tampa Electric's power plants yields a price per ton of transportation. The result will become the "benchmark price" as shown on Attachment 3.

a. The benchmark price will be used to evaluate water transportation of coal services provided by TTT to Tampa Electric.

b. The price paid for water transportation of coal by Tampa Electric above the benchmark price would be disallowed for cost recovery unless justified by Tampa Electric.

General Provisions

11. The approval of this Stipulation will completely resolve all of the issues pending in this matter.

12. This Stipulation is based on the unique factual circumstances of this case and shall have no precedential value in proceedings involving other utilities before this Commission. The parties to the Stipulation

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reserve the right to assert different positions on any of the matters contained in this Stipulation if the Stipulation is not accepted by the Commission.

13. The parties hereto shall not unilaterally recommend or support the modification of this Stipulation or discourage its acceptance by the Commission.

14. The parties hereto shall not request reconsideration of or appeal the order which approves this Stipulation.

15. The parties urge that the Commission take final agency action at the earliest possible Agenda Conference approving this Stipulation.

16. This Stipulation shall be effective upon Commission approval. In the event that the Commission rejects or modifies the Stipulation, in whole or in part, the parties agree that this Stipulation is void unless otherwise ratified by the parties, and that each party may pursue its interests as those interests exist, and that no party will be bound to or make reference to this Stipulation before this Commission or any court.

17. While Staff for internal reasons prefers to signify its agreement with this Stipulation by writing a Staff memorandum recommending approval of the Stipulation, the Electric and Gas and Legal Staff of the Florida Public Service Commission has reviewed this Stipulation simultaneously with the signing; has given its approval of the specific language contained herein; and has committed to submit its recommendation requesting approval of this Stipulation by the Commission; and has committed not to unilaterally recommend or support the modification of this Stipulation or discourage its acceptance by the Commission.

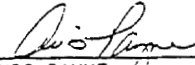
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ATTACHMENT A

DATED this 13th day of October, 1988.



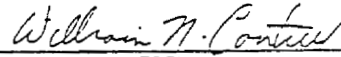
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EXAMPLE BENCHMARK MARKET BASED COAL CALCULATION

The base price of \$39.44 as of December 31, 1987 shall be adjusted by the annual percentage change in BOM District 8 Data for Coal Shipments as reported on Form 423 for the weighted average price per million BTU of contract transactions (excluding all spot transactions) which meet Tampa Electric's Gannon Station specifications (Note 4) for heat content, sulfur content, ash content and pounds sulfur dioxide per million BTU.

Example:

$$39.44 \times \frac{192.200}{189.015} \begin{matrix} \text{(Note 1)} \\ \text{(Note 2)} \end{matrix} = \$40.10$$

$$\text{Revised Benchmark } 40.10 \times 1.05 \text{ (Note 3)} = \$42.11$$

Notes

1/ Hypothetical index value for 1988.

2/ Actual index value for 1987.

3/ 5% zone of reasonableness.

4/ Specifications as follows:

Heat Content - 12,500 BTU/lb minimum
Sulfur Content - 1.5% maximum
Ash Content - 9.0% maximum
Sulfur Dioxide - 2.0 pounds per million BTU maximum

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ATTACHMENT

PUBLIC COUNSEL'S MARKET

PRICE APPLICATION

--Gatliff coal purchased¹

FOB mine	\$45/ton
Tons purchased	500,000
Total cost	\$22,500,000

--Market Benchmark \$40/ton

--Cost recovered through fuel clause
 $\$40/\text{ton} \times 500,000 = \$20,000,000$

--Cost disallowed recovery
 $\$20,000,000 - \$22,500,000 = \$2,500,000^*$

* The company would have to provide justification before recovery of these cost would be allowed.

1. This would include the total average price of Gatliff produced coal and coal purchased and resold as Gatliff coal.

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EXAMPLE BENCHMARK TRANSPORTATION CALCULATION

Average Rail Mileage to Tampa	974 miles	(Note 1)
x Average of Lowest Two Publicly-Available Florida Rail Rates	<u>x 1.98</u> c/ton-mile	(Note 2)
	<u>\$19.29</u>	
+ Costs of Privately-Owned Rail Cars	+ 2.00	
= Transportation Benchmark	<u>\$21.29</u>	(Note 3)

Notes

1/ Weighted average rail miles from all coal sources for Tampa Electric to plants. This is expected to be 974 miles for 1989.

2/ Cents per ton-mile for publicly available Florida utility rail coal transportation rates. For example, the current publicly available rail rates to Florida utilities on a cents per ton mile basis for 1988 are as follows:

JEA	1.92 c*
Orlando	2.03 c*
Lakeland	2.30 c
Gainesville	2.45 c

*Average of Lowest Two 1.98 c

3/ Calculated by multiplying average rail mileage to Tampa by Florida rail coal market cost (cents per ton-mile), then adding the costs of privately-owned rail cars. This benchmark will be compared to Tampa Electric's weighted average water transportation cost from all Tampa Electric coal sources.

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EXHIBIT TO TESTIMONY OF
JOANN T. WEHLE

DOCUMENT NO. 2

Comparison of the 1997 and 2003 Bid Processes

COMPARISON OF TAMPA ELECTRIC'S 1997 RFP AND 2003 RFP

RFP Term/Condition	Per Exhibit WBM-2		Tampa Electric
	1997 RFP	2003 RFP	Tampa Electric Comments
Integrated Proposal Requirement	Silent regarding integration.	Stated preference for integration.	The 1997 bid stated a requirement for integration. The first sentence on page one stated, "The Fuels Department of Tampa Electric is inviting proposals to provide integrated waterborne transportation services for the movement of coal from mid-west supply sources for final delivery to Tampa Electric's generating stations near Tampa, Florida."
River Tonnages	4.0 to 6.0 MM tons annually, for five years	3.25 to 5.00 MM tons annually for five years, except for consent decree triggering event, in which case 2007 tonnage is 2.0 to 4.0 MM tons and 2008 tonnage is 1.0 to 3.0 MM tons.	This is in accordance with the Consent Decree. In addition, providing the information allows potential suppliers to understand and account for the potential impact on the company's tonnage requirements in their proposals.
Terminal and Ocean Tonnages	7.5 to 8.5 MM tons annually, for five years	4.0 to 5.5 MM tons annually for five years, except for consent decree triggering event, in which case 2007 tonnage is 3.0 to 4.5 MM tons and 2008 tonnage is 2.0 to 3.5 MM tons.	This is in accordance with the Consent Decree. In addition, providing the information allows potential suppliers to understand and account for the potential impact on the company's tonnage requirements in their proposals.
Terminal Rate Elements	Fixed and Variable Rate Component	Fixed Rate Component only.	Given the nature of the costs to provide the service, the terminal rate should represent only a fixed component, which actually lowers risk to ratepayers.
Dead Freight	Silent regarding dead freight charges	Solicits dead freight charge	All potential charges should be disclosed and considered.
Notice by TECO of Annual Ton Declarations & Monthly Shipping Schedules	July 31 of each contract year for the following calendar year	September 30 of each contract year for the following calendar year	Giving notice later in the year provides Tampa Electric with more flexibility.
Loading/Unloading	River Barges: 4 free days for loading river barges. Ocean barges: 48 hours free unloading.	River barges: 3 free days for loading and 3 free days for unloading Ocean Barges: 48 hours free unloading Ocean Vessels at Terminal: 24 hour free unloading or loading at terminal	Provides specific operational parameters to potential suppliers, which allows potential suppliers to align and price their respective proposals to meet the company's requirements.
Terminal Storage Minimums	None Stated	1.4 MM tons: 8 individual stockpiles.	Provides specific operational parameters to potential suppliers, which allows potential suppliers to align and price their respective proposals to meet the company's requirements.
Minimum Discharge Rate of Panamax Vessels	Average discharge rate of 750 tons per hour	Minimum discharge rate of 900 tons per hour.	Provides specific operational parameters to potential suppliers, which allows potential suppliers to align and price their respective proposals to meet the company's requirements.
Open Period of Bid Proposals	Six months beyond closing date of solicitation.	Two months beyond closing date of solicitation.	Provides more certainty to bidders by releasing them earlier to pursue other opportunities.

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DOCUMENT NO. 3

Comparison of Waterborne and Rail
Transportation Rates Using Appropriate
Adjustments for Rail Costs Not Included in
Bidder Proposal Rates

**Comparison of Adjusted Rail Bid Rates and Waterborne Transportation Contract Rates
(\$ / Ton)**

(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)	(J)	(K)	(L)	(M)	(N)
River Dock	TT Total	Rail Bidder Rate	Bidder's Fuel Surcharge (Note 1)	Demurrage Rate (Note 2)	Bidder's Synfuel Adder	Incr. Cost to Polk Station (Note 3)	Adj. Total Rail Bidder Rate	Difference: TT Less Adj. Total Bid Rate	2004 Tons	TT Trans. Cost	Rail Bid Trans. Cost	Difference: TT Less Adj. Rail Bid
Cook												
Hamilton												
Caseyville												
Overland												
Rigsby & Barnard												
Mount Vernon												
Mound City												
Southern Indiana												
New Hope												
Empire Dock												
Yankeetown												
Owensboro												
Ken Mine		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Pyramid		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Green Coal		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Patnot		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Sebree		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
TTI		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Jefferson River Port		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Kentucky Lake Dock		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
GRT		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Cora												
Dekoven		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Powhatan		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Shawneetown		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Refineries Petcoke		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
BRT		N/A	N/A	N/A	N/A	N/A	N/A	N/A				
Cahokia	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	
Kellogg	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	
Kanipe Enterprises	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	

Average for All Docks on Contract

N/A

N/A

Average for Docks Common to TT and Rail Bid

Weighted Average Rate
Weighted Average for
Docks Common to TT and
Rail Bid

[Redacted]

Notes

[Redacted]

Sources

Columns A, B and C: Exhibit WBM-1
Column D: Rail proposal and Tariff 8200
Column E: Calculated weighted average rate. See note 2.
Column F: Rail proposal
Column G: Calculated weighted average rate. See note 3
Column H = (C) + (D) + (E) + (F) + (G)
Column J = (B) - (H)
Column K = Tampa Electric
Column L = (B) * (K)
Column M = (H) * (K)
Column N = (L) - (M)

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