State of Florida

Public Service Commission

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-M-E-M-O-R-A-N-D-U-M-

DATE: March 18, 2004

TO: Director, Division of the Commission Clerk & Administrative Services (Bayó)

FROM: Division of Economic Regulation (Bohrmann, Haff, McNulty)
Office of the General Counsel (C. Keating, Rodan, Vining)

RE: Docket No. 040001-EI – Fuel and purchased power cost recovery clause with generating performance incentive factor.

AGENDA: 03/30/04 – Regular Agenda – Decision on Motions for Reconsideration/Clarification of Final Order - Oral Argument Requested on Issue 2

CRITICAL DATES: None

SPECIAL INSTRUCTIONS: None

FILE NAME AND LOCATION: S:\PSC\GCL\GCO\WP\040001.RCM.DOC

Case Background

By Order No. PSC-03-1461-FOF-EI, issued December 22, 2003, in Docket No. 030001-EI ("Fuel Order"), the Commission established fuel and capacity cost recovery factors for investor-owned electric utilities to apply for billing purposes in calendar year 2004. On January 6, 2004, Tampa Electric Company ("Tampa Electric") filed a motion for reconsideration of that portion of the Fuel Order which addressed the costs and savings associated with the shutdown of Tampa Electric's Gannon Units 1-4. At the same time, Tampa Electric filed a request for oral argument on its motion. The Office of Public Counsel, Florida Industrial Power Users Group ("FIPUG"), and Florida Retail Federation (collectively, "Intervenors") filed a joint response in opposition to Tampa Electric's motion on January 13, 2004.

On January 6, 2004, the Intervenors filed a joint motion for reconsideration of that same portion of the Fuel Order. Tampa Electric filed a response in opposition to Intervenors' joint motion on January 13, 2004.

On January 6, 2004, Florida Power & Light Company ("FPL") filed a motion for clarification or, in the alternative, reconsideration of that portion of the Commission's Fuel Order concerning a growth adjustment used to establish the baseline for determining incremental power plant security costs. No party filed a response to FPL's motion.

The Commission has jurisdiction over this subject matter pursuant to Chapter 366, Florida Statutes, including Sections 366.04, 366.05, and 366.06, Florida Statutes.

Discussion of Issues

Issue 1: Should the Commission grant Tampa Electric Company's request for oral argument on its motion for reconsideration of Order No. PSC-03-1461-FOF-EI?

Recommendation: Yes. Oral argument may aid the Commission in its understanding and disposition of the underlying motion. (C. KEATING)

Staff Analysis: In its request for oral argument, Tampa Electric asserts that oral argument on the matters raised in its motion for reconsideration will assist the Commission in its deliberations and provide the Commission the opportunity to request clarification of the arguments presented, as necessary. No party has filed pleadings in opposition to Tampa Electric's request for oral argument.

Rule 25-22.060, Florida Administrative Code, provides that the Commission, at its discretion, may grant a request for oral argument on a motion for reconsideration of a final order, such as the Fuel Order. The Commission has traditionally granted oral argument upon a finding that oral argument would aid the Commission in its understanding and disposition of the underlying motion. Given the complexity of the matters at issue and given that approximately four months have passed since the Commission's original vote on these matters, staff believes that oral argument on Tampa Electric's motion may assist the Commission in its understanding and disposition of the motion. Thus, staff recommends that the Commission grant Tampa Electric's request for oral argument on its motion for reconsideration, which is addressed in Issue 2, below.

Issue 2: Should the Commission grant Tampa Electric Company's motion for reconsideration of Order No. PSC-03-1461-FOF-EI?

Recommendation: No. Tampa Electric's motion for reconsideration fails to identify any point of fact or law that the Commission overlooked or failed to consider in rendering its Fuel Order and, therefore, should be denied. (C.KEATING, HAFF, BOHRMANN)

Staff Analysis: As noted in the Fuel Order, Tampa Electric is required to cease operating coal-fired generation at its Gannon Station by December 31, 2004, pursuant to a Consent Final Judgment ("CFJ") entered into with the Florida Department of Environmental Protection, signed December 6, 1999, and a Consent Decree ("CD") entered into with the United States Environmental Protection Agency and Department of Justice, signed February 29, 2000. The Fuel Order addresses, among other things, the recovery of replacement fuel costs incurred by Tampa Electric as a result of its decision to shut down Gannon Units 1-4 prior to December 31, 2004. (Pages 13-21 of the Fuel Order are devoted to this issue and are attached hereto for reference as Attachment A.) In addressing this issue, the Commission stated, at page 21 of the Fuel Order, the following:

> But for TECO's decision to cease operations at Gannon Units 1 through 4 when it did, the company would not have incurred the replacement fuel costs that we have determined to be reasonable. Further, but for that same decision, the company would not have achieved O&M savings estimated at $10,521,000 for 2003. Because these O&M savings derive from the same finite decision that resulted in replacement fuel costs, we believe that, under the unique circumstances presented, the replacement fuel costs to be borne by customers should be offset to some extent by the amount of savings. . . . Taking into account all of the competing evidence in the record on this point and the unique circumstances presented, we believe that a fair and reasonable sharing of the O&M savings associated with the units' closure will be achieved by providing 80% of the estimated O&M savings, or $8,416,800, to ratepayers as an offset to TECO's recoverable fuel costs, and providing TECO the benefit of the remaining 20% of the O&M savings.

Arguments of the Parties

In its motion for reconsideration, Tampa Electric first argues that the Commission erred by effectively disallowing recovery of prudently incurred costs. Tampa Electric notes that the Commission found that the replacement fuel costs associated with Tampa Electric's decision to shut down Gannon Units 1-4 were prudently incurred. Tampa Electric asserts that the Commission is legally obligated to allow full recovery of those costs.

Next, Tampa Electric argues that the Commission erred by considering base rate costs as the basis for an adjustment to fuel and purchased power costs. Tampa Electric asserts that an evaluation of base rate costs may be performed only during a full rate proceeding when all expenses and investments are considered, and that the Commission's decision in the fuel and purchased power cost recovery clause ("fuel clause") proceedings must be confined to fuel and purchased power costs.

Further, Tampa Electric argues that, assuming it is appropriate to consider base rate costs in the fuel clause, the Commission erred by failing to consider cost factors other than O&M costs in determining whether savings were achieved as a result of the shut down of Gannon Units 1-4. Tampa Electric asserts that the Commission erroneously focused on only one estimate of O&M savings associated with the shut down of Gannon Units 1-4 and failed to consider other costs related to the same transaction, in particular increases in O&M costs related to Tampa Electric's other generating units. Tampa Electric asserts that to determine if savings exist, the Commission must calculate the combined effect of all of the factors directly related to compliance with the CFJ and CD, including increased investment in generating plant, increased depreciation expense, and increased maintenance expenses at other generating units. Otherwise, according to Tampa Electric, the Commission would fail to adhere to the principle of symmetry that requires both ratepayers and utilities be treated in a similar manner.

Finally, Tampa Electric argues that the Commission failed to consider several unintended adverse consequences of its decision. Tampa Electric claims that based on the Commission's decision and the principle of symmetry, the Commission would be required to allow a surcharge to fuel adjustment factors for increases in costs prudently incurred by a utility when it takes actions which increase O&M expenses or investment which then reduce the utility's fuel and purchased power costs, such as scheduled maintenance costs that improve reliability and availability of a generating plant. Further, Tampa Electric asserts that the Commission's decision operates as a significant and unintended penalty which will have a chilling effect on a utility's pursuit of O&M savings under circumstances where it runs the risk that such savings will be isolated and used to offset recovery of prudently incurred fuel and purchased power costs. In addition, Tampa Electric asserts that the Commission's decision injected uncertainty in Tampa Electric's full recovery of prudently incurred costs required to comply with the CFJ and CD.

In their joint response, Intervenors argue that Tampa Electric's motion for reconsideration inappropriately reargues points that the Commission considered and rejected in its deliberations on this issue. Intervenors note that Tampa Electric, at the Prehearing Conference, objected to inclusion of the issue now subject to reconsideration on the grounds that it mixed base rate and fuel cost recovery concepts, but that the issue was deemed appropriate by the Prehearing Officer. Intervenors assert that Tampa Electric, having not challenged that decision, cannot now complain that the issue is beyond the scope of the fuel clause. The Intervenors further contend that the Commission did not overlook or fail to consider Tampa Electric's position that the Commission could not consider base rate costs as the basis for an adjustment to fuel and purchased power costs. Intervenors state that the issue was discussed in both the testimony of Tampa Electric witness Jordan and FIPUG witness Brown, and that witness Jordan acknowledged that the Commission has, on a case-by-case basis, allowed recovery of certain expenses through the fuel clause that would traditionally be recovered through base rates. Intervenors further state that the Commissioners, in their deliberations, explicitly discussed and rejected Tampa Electric's position, noting instances in which the Commission had permitted capital and O&M expenditures, typically base rate items, to be recovered through the fuel clause.

Intervenors also assert that the Commission did not err by disallowing recovery of prudent expenses because it did not disallow recovery of such expenses. Rather, according to

Intervenors, the Commission ordered a sharing of O&M savings associated with the closure of Gannon Units 1-4.

Further, Intervenors assert that the Commission did not overlook or fail to consider the full context in which its decision was made. Intervenors assert that the Commission heard, considered, and discussed extensive evidence concerning the totality of the circumstances surrounding closure of Gannon Units 1-4 and the related costs. In response to Tampa Electric's arguments concerning "symmetry" of Commission decisions, Intervenors assert that without the sharing of savings required by the Fuel Order, the ratepayers would have suffered harm while Tampa Electric benefited.

Finally, Intervenors contend that Tampa Electric's assertions of adverse unintended consequences from the Fuel Order are merely conjecture, unsupported by experience following the Commission's past decisions to allow recovery of base rate items through the fuel clause, and inconsistent with the language in the Fuel Order indicating that the Commission's decision was based on the unique circumstances presented.

Analysis and Recommendation

The standard of review for a motion for reconsideration of a Commission order is whether the motion identifies a point of fact or law that the Commission overlooked or failed to consider in rendering the order. See Stewart Bonded Warehouse, Inc. v. Bevis, 294 So. 2d 315 (Fla. 1974); Diamond Cab Co. v. King, 146 So. 2d 889 (Fla. 1962); and Pingree v. Quaintance, 394 So. 2d 162 (Fla. 1st DCA 1981). In a motion for reconsideration, it is not appropriate to reargue matters that have already been considered. Sherwood v. State, 111 So. 2d 96 (Fla. 3rd DCA 1959); citing State ex.rel. Jaytex Realty Co. v. Green, 105 So. 2d 817 (Fla. 1st DCA 1958). Furthermore, a motion for reconsideration should not be granted "based upon an arbitrary feeling that a mistake may have been made, but should be based upon specific factual matters set forth in the record and susceptible to review." Stewart Bonded Warehouse, Inc. vs. Bevis.

Staff's analysis addresses Tampa Electric's arguments point by point and concludes that Tampa Electric has not identified any point of fact or law that the Commission overlooked or failed to consider in rendering that portion of the Fuel Order which addressed the costs and savings associated with the shutdown of Tampa Electric's Gannon Units 1-4.

As noted above, Tampa Electric first argues that the Commission erred by effectively disallowing recovery of prudently incurred costs. This argument, however, mischaracterizes the Commission's decision. The Commission determined that the replacement fuel costs incurred by Tampa Electric as a result of its decision to shut down Gannon Units 1-4 when it did were prudently incurred. The Commission did not "disallow" any portion of those costs. Instead, the Commission determined that the shut down of Gannon Units 1-4 resulted in O&M savings for Tampa Electric in 2003 and that these savings, because they resulted from the same finite decision which led to the replacement fuel costs to be borne by ratepayers, should be shared with ratepayers through an offset to the costs being recovered by Tampa Electric through the fuel clause. In other words, the Commission allowed recovery of all prudently incurred replacement fuel costs, then chose to offset those costs by a percentage of the associated O&M savings realized by Tampa Electric as a means of allowing ratepayers to share in those savings. Pursuant

to Chapter 366, Florida Statutes, the Commission has the exclusive authority and the obligation to set rates that it deems fair, just, reasonable, and compensatory. The Commission acted fully within its authority when it ordered that Tampa Electric's recoverable fuel costs be offset by O&M savings resulting from the same finite decision which led to replacement fuel costs. Thus, the Commission did not err in this regard.

Second, Tampa Electric argues that the Commission erred by considering base rate costs as the basis for an adjustment to fuel and purchased power costs. The argument that "the Commission's decision in the fuel and purchased power proceeding must be confined to fuel and purchased power costs" is at odds with a long history of decisions in which the Commission allowed recovery of certain expenses through the fuel clause that would traditionally be recovered through base rates, such as capital and O&M expenses. See, e.g., Order No. 11217, issued October 1, 1982, in Docket No. 820155-EU (allowing recovery through the fuel clause of capital expenses associated with 500kV transmission line pursuant to oil-backout rule); Order No. 11223, issued October 5, 1982, in Docket No. 820055-EU, and Order No. 11658, issued March 2, 1983, in Docket No. 820533-EU (allowing recovery through the fuel clause of capital and O&M expenses associated with converting Gannon units from oil-fired to coal-fired pursuant to oil-backout rule); Order No. 23366, issued August 17, 1990, in Docket No. 900001-EI, pages 5-6 (allowing recovery through the fuel clause of capital expenses associated with rail cars used to transport coal); Order No. PSC-93-1331-FOF-EI, issued September 13, 1993, in Docket No. 930001-EI, pages 5-6 (allowing recovery through the fuel clause of capital expenses associated with natural gas pipeline lateral); Order No. PSC-95-1089-FOF-EI, issued September 5, 1995, in Docket No. 950001-EI, pages 9-10 (allowing recovery through the fuel clause of capital expenses associated with conversion of combustion turbine from single-fuel to dual-fuel capability); Order No. PSC-02-1484-FOF-EI, issued October 30, 2002, in Docket No. 011605-EI (allowing recovery through the fuel clause of incremental O&M expenses associated with new or expanded hedging programs); and Order No. PSC-02-1761-FOF-EI, issued December 13, 2002, in Docket No. 020001-EI, pages 3-4, 5-7, 9-11, 14-15 (allowing recovery through the fuel clause of incremental power plant security costs). Even in the Fuel Order that is the subject of Tampa Electric's motion for reconsideration, Tampa Electric was authorized to recover incremental power plant security costs, a type of cost traditionally recovered through base rates rather than the fuel clause. The rationale behind these decisions has largely been to allow recovery through the fuel clause of non-fuel costs not recognized or anticipated at the time of the utility's last rate case that, if expended, would create fuel cost savings for customers. Under this approach, customers benefit from fuel cost savings while the utility is made whole for the non-fuel expenses necessary to achieve that benefit. The Commission simply applied the converse of the rationale in this instance: customers were allowed to share in non-fuel cost savings achieved while the utility was made whole for its additional fuel expenses.

Consistent with this history and consistent with the Commission's statutory authority and obligation to set fair, just, reasonable, and compensatory rates, the Commission did not err by considering non-fuel costs as the basis for an adjustment to fuel and purchased power costs. Chapter 366, Florida Statutes, makes no distinction between cost recovery mechanisms, i.e., base rates and fuel clause recovery, where it requires the Commission to set fair, just, reasonable, and compensatory rates. Further, it is clear from the record that the Commission considered Tampa Electric's argument and rejected it. The Commission heard testimony from Tampa Electric

witness Jordan and FIPUG witness Brown concerning the appropriateness of offsetting replacement fuel costs with associated O&M savings. In its deliberations, the Commission took note of past decisions "mixing" fuel and non-fuel cost recovery in the fuel clause and, while recognizing that this was the first instance in which it was confronted with a situation where increased fuel costs resulted from the same finite decision which led to O&M savings, determined that it was not constrained from reaching the result it reached because the O&M savings at issue were non-fuel costs. (Tr. 1197-1199, 1205-1206, 1208, 1211, 1214-1216, 1266.)

Third, Tampa Electric argues that, assuming it is appropriate to consider base rate costs in the fuel clause, the Commission erred by failing to consider cost factors other than O&M costs in determining whether savings were achieved as a result of the shut down of Gannon Units 1-4. The Commission had before it extensive testimony from Tampa Electric concerning the totality of the circumstances surrounding the decision to shut down Gannon Units 1-4 when it did and found that the estimate of O&M savings set forth in Exhibit MJM-5 to the testimony of OPC witness Majoros was the best statement of savings to use for the purpose of offsetting replacement fuel costs incurred as a result of Tampa Electric's decision to shut down Gannon Units 1-4 when it did. The Commission did not fail to consider the extensive evidence before it concerning the other cost factors suggested by Tampa Electric.

Fourth, Tampa Electric argues that the Commission failed to consider several unintended adverse consequences of its decision, suggesting that the Commission would be required to allow a surcharge to fuel adjustment factors for increases in costs prudently incurred by a utility when it takes routine actions, such as scheduled maintenance, which increase O&M expenses or investment but reduce the utility's fuel and purchased power costs. The Commission clearly took this into consideration, pointing out in the Fuel Order that its decision was based on the very unique circumstances presented. In its deliberations, the Commission noted that it was presented with an extraordinary circumstance where four generating units were required to be shut down as opposed to a circumstance where more modest O&M savings were generated by a new efficiency procedure. (Tr. 1209-1210.) Further, in its deliberations, the Commission made clear that it was not advocating a review of all O&M savings achieved by utilities for purposes of crediting such savings through the fuel clause. (Tr. 1206-1207.) While the Commission could not reasonably have speculated as to every possible consequence of its decision, it certainly considered the potential precedential value of its decision and clearly limited its decision to the extraordinary circumstances presented.

For the reasons set forth above, staff recommends that the Commission deny Tampa Electric's motion for reconsideration.

Issue 3: Should the Commission grant the Intervenors' motion for reconsideration of Order No. PSC-03-1461-FOF-EI?

Recommendation: No. The Intervenors' motion for reconsideration fails to identify any point of fact or law that the Commission overlooked or failed to consider in rendering its Fuel Order and, therefore, should be denied. (C. KEATING, HAFF, BOHRMANN)

Staff Analysis: The Intervenors seek reconsideration of the same portion of the Fuel Order for which Tampa Electric seeks reconsideration. The Intervenors argue that the Fuel Order does not go far enough in sharing with customers the O&M savings resulting from the shutdown of Gannon Units 1-4. Rather than arguing that the Commission erred in reaching its decision, the Intervenors argue that the Fuel Order did not properly reflect the Commission's vote. The Intervenors assert that the Fuel Order erroneously used the $10.5 million "Net Savings" shown in Exhibit MJM-5 to the testimony of OPC witness Majoros to represent the O&M savings related to replacement fuel costs through December 31, 2004, when the amount in Exhibit MJM-5 represented only O&M savings for 2003. The Intervenors assert that the Commission intended Exhibit MJM-5 to be used as the formula for calculating O&M savings that should be offset against associated replacement fuel costs, but the Fuel Order failed to account for 2004 savings. According to the Intervenors, using MJM-5 as a formula for calculating "Net Savings" for 2003 and 2004 results in a total offset of $31.9 million, after the 80/20 sharing of savings ordered by the Commission.

In response, Tampa Electric asserts that the Intervenors failed to identify any point of fact or law that the Commission overlooked or failed to consider in rendering the Fuel Order. Tampa Electric asserts that the Commission's deliberations reveal that its clear intent was to use the O&M savings reflected in Exhibit MJM-5 as the appropriate offset for all relevant time periods. Thus, Tampa Electric argues that the Fuel Order correctly reflects the Commission's intent.

Based on the standard of review set forth in Issue 2, staff recommends that the Commission deny the Intervenors' motion for reconsideration. The motion fails to identify any point of fact or law that the Commission overlooked or failed to consider in rendering the Fuel Order. Further, a review of the transcript of the Commission's deliberations leads to the conclusion that the Commission intended to use the O&M savings shown in Exhibit MJM-5 as the only offset to replacement fuel costs incurred as a result of the shut down of Gannon Units 1-4.

From the Commission's deliberations, the Intervenors have taken a single use of the word "formula" out-of-context and attempted to use that single reference as the basis for an additional $21.4 million offset that is not suggested anywhere else in the Commission's deliberations or vote. Further, the Intervenors have attempted to use references to Tampa Electric's "decision to cease operations at Gannon Units 1 through 4 prior to December 31, 2004" as the basis for asserting that the Commission must have intended to use Exhibit MJM-5 as a formula for calculating 2003 *and 2004* O&M savings to be offset against replacement fuel costs. Throughout the transcript of the Commission's deliberations, however, it is clear that the Commission recognized the O&M savings reflected in Exhibit MJM-5 as the amount of savings it wished to use to offset replacement fuel costs (Tr. 1210, 1266). It is also clear that the Commission recognized that Exhibit MJM-5 reflected estimates of 2003 O&M savings only (Tr.

1252-1253, 1257-1258, 1267-1268, 1271-1272). Nowhere in the transcript of those deliberations does the Commission suggest that an additional offset is required. The motion on this issue, which was unanimously approved, reads as follows:

> I would move that we would recognize the amount in Scenario 5 of Exhibit MJM-5 as O&M savings, and that we would attribute 80 percent of that savings to the ratepayers, which would be whatever that number calculates to be, something in excess of $8 million would be a reduction in fuel costs that would be passed through to customers.

(Tr. 1266.) In restating the motion before the vote, the Chairman added that "we recognize that the last six months of 2003 will be affected." (Tr. 1268.) Accordingly, the Fuel Order precisely reflects the Commission's vote.

Based on the foregoing, staff recommends that the Commission deny Intervenors' motion for reconsideration.

Issue 4: Should the Commission grant Florida Power & Light Company's motion for clarification, or in the alternative, reconsideration of Order No. PSC-03-1461-FOF-EI?

Recommendation: The Commission should clarify Order No. PSC-03-1461-FOF-EI as requested in Florida Power & Light Company's motion to more precisely reflect its vote. (C. KEATING)

Staff Analysis: By its motion, FPL asks the Commission to clarify that the portion of its Fuel Order approving an adjustment of the baseline used to determine incremental recoverable costs to reflect growth in kWh sales ("gross-up adjustment") is intended to apply only to incremental power plant security costs. FPL notes that the staff witness who proposed this adjustment filed testimony in response solely to the limited issue of the appropriate methodology for determining incremental power plant security costs. FPL further notes that at hearing the staff witness clarified that he was proposing a gross-up adjustment to apply only to incremental power plant security costs, consistent with the limited issue to which his testimony was directed. FPL states that the Fuel Order, however, does not explicitly state that this gross-up adjustment will apply only to incremental power plant security costs recoverable through the capacity cost recovery clause. If the Commission, by its Fuel Order, intends to apply the gross-up adjustment to determine the amount of other incremental costs recoverable through cost recovery clauses, then FPL asks the Commission to reconsider that decision.

In addressing this issue, the Commission stated, at page 30 of the Fuel Order, the following:

> We agree with staff witness Brinkley that base amounts used for calculating incremental security costs for recovery through the capacity cost recovery clauses should be adjusted for growth or decline in energy sales in kilowatt-hours from the base year to the current year. By adjusting the base year amounts for growth in energy sales, we believe utilities will collect through the capacity clause only those expenses that are truly incremental to the level of costs being recovered through base rates. For those utilities currently operating under a revenue sharing plan approved by this Commission, current year revenues shall be reduced by the amount of revenues refunded through the utility's sharing plan prior to application of this growth adjustment.

Given the limited issue that the Commission was asked to decide and the staff witness's clarification that his testimony was intended to address only that issue, staff believes that the clarification sought by FPL is appropriate. While the Fuel Order does make specific reference to "incremental security costs for recovery through the capacity cost recovery clauses," the Commission should clarify that its approval of the gross-up adjustment was intended to apply only to incremental power plant security costs recoverable through the capacity cost recovery clause. In making this clarification, the Commission does not preclude itself from considering or approving any future proposal to more broadly apply the gross-up adjustment to determine the amount of other incremental costs recoverable through cost recovery clauses.

In sum, staff recommends that the Commission clarify Order No. PSC-03-1461-FOF-EI as requested in FPL's motion to more precisely reflect its vote.

Issue 5: Should this docket be closed?

Recommendation: This docket is an ongoing docket and should remain open. (C. KEATING)

Staff Analysis: The fuel and purchased power cost recovery docket is an ongoing docket and should remain open.