

BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 041291-EI

In the Matter of

PETITION FOR AUTHORITY TO RECOVER
PRUDENTLY INCURRED STORM RESTORATION
COSTS RELATED TO 2004 STORM SEASON
THAT EXCEED STORM RESERVE BALANCE,
BY FLORIDA POWER & LIGHT COMPANY.



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THE .PDF VERSION INCLUDES PREFILED TESTIMONY.

VOLUME 4

Page 380 through 500

PROCEEDINGS: HEARING

BEFORE: CHAIRMAN BRAULIO L. BAEZ
COMMISSIONER J. TERRY DEASON
COMMISSIONER RUDOLPH "RUDY" BRADLEY
COMMISSIONER CHARLES M. DAVIDSON
COMMISSIONER LISA P. EDGAR

DATE: Thursday, April 21, 2005

TIME: Commenced at 9:00 a.m.

PLACE: Betty Easley Conference Center
Hearing Room 148
4075 Esplanade Way
Tallahassee, Florida

REPORTED BY: LINDA BOLES, RPR
Official FPSC Reporter
(850) 413-6734

APPEARANCES: (As heretofore noted.)

DOCUMENT NUMBER-DATE

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FLORIDA PUBLIC SERVICE COMMISSION

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1 PROCEEDINGS

2 (Transcript follows in sequence from Volume 3.)

3 COMMISSIONER BAEZ: Go back on the record. Good
4 morning, everyone. I think we have a preliminary matter,
5 Ms. Fleming.6 MS. FLEMING: Yes, Chairman. I was just updated this
7 morning. Yesterday OPC entered into the record, which was
8 ~~identified as hearing Exhibit 34, one of their exhibits was~~9 FPL's Answer to OPC's 6th Request to Produce Documents, Item
10 Number 43. That answer did not include FPL's updated answer.
11 The updated answer can be found in staff's composite exhibit,
12 which is identified as hearing Exhibit 2.13 COMMISSIONER BAEZ: So there's no, there's no
14 addition that, no additions that need to be made or deletions?15 MS. FLEMING: No. Just a clarification for the
16 record that the updated answer is in the record, but it's under
17 staff's Exhibit 2.18 COMMISSIONER BAEZ: All right. Are there any
19 questions from the parties?20 MR. MCGLOTHLIN: We appreciate staff's attention on
21 that matter.22 COMMISSIONER BAEZ: All right. If there's nothing
23 else, then we can go ahead and, Mr. McGlothlin, you can call
24 your next witness.

25 MR. MCGLOTHLIN: Yes. We call Michael Majoros. I

1 don't believe he was present when witnesses were sworn.

2 COMMISSIONER BAEZ: Mr. Majoros.

3 MICHAEL J. MAJOROS, JR.

4 was called as a witness on behalf of the Citizens of the State
5 of Florida and, having been duly sworn, testified as follows:

6 DIRECT EXAMINATION

7 BY MR. McGLOTHLIN:

8 Q Please state your name and address for the record.

9 A My name is Michael J. Majoros, Jr. My address is
10 1220 L Street, N.W, Washington, D.C.

11 Q Mr. Majoros, did you prepare and submit on behalf of
12 CPC direct testimony in this docket?

13 A Yes, I did.

14 Q And did you also provide some additional direct
15 testimony in response to the amended petition of FP&L?

16 A Yes.

17 Q And subsequently did you supplement your testimony to
18 address the summary of the FPL depreciation filing?

19 A Yes, I did.

20 Q With respect to those three separate testimonies, do
21 you have any changes or corrections to make at this point?

22 A No.

23 Q Do you adopt the prefiled testimony and the questions
24 and answers contained therein as your testimony here today?

25 A Yes, I do.

1 MR. McGLOTHLIN: I request that the direct testimony
2 and the two supplements to his direct testimony be incorporated
3 in the record as though read.

4 COMMISSIONER BAEZ: Without objection, show the
5 direct and the two sets of supplemental direct testimony by
6 Witness Majoros entered into the record as though read.

7 BY MR. McGLOTHLIN:

8 ~~Q Mr. Majoros, did you also prepare and submit with~~
9 your testimony the exhibits that have been identified earlier
10 as MJM-1 through MJM-10?

11 A Yes.

12 MR. McGLOTHLIN: And I believe, Chairman Baez, a
13 number has been assigned to that.

14 COMMISSIONER BAEZ: For the record, those exhibits
15 previously identified as MJM-1 through MJM-10 have been marked
16 as Exhibits 13 through 22 respectively

DIRECT TESTIMONY

OF

MICHAEL J. MAJOROS, JR.

DOCKET NO. 041291-EI

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I. Introduction

Q. Please state your name, position and business address.

A. My name is Michael J. Majoros, Jr. I am Vice President of Snavely King Majoros O'Connor & Lee, Inc. ("Snavely King"), an economic consulting firm located at 1220 L Street, N.W., Suite 410, Washington, D.C. 20005.

Q. Please describe Snavely King.

A. Snavely King was founded in 1970 to conduct research on a consulting basis into the rates, revenues, costs and economic performance of regulated firms and industries. The firm has a professional staff of 15 economists, accountants, engineers and cost analysts. Most of its work involves the development, preparation and presentation of expert witness testimony before Federal and state regulatory agencies. Over the course of its 33-year history, members of the firm have participated in more than 1,000 proceedings before almost all of the state commissions and all Federal commissions that regulate utilities or transportation industries.

Q. Have you prepared a summary of your qualifications and experience?

A. Yes. Appendix A is a summary of my qualifications and experience. It also contains a tabulation of my appearances as an expert witness before state and Federal regulatory agencies.

1 **Q. At whose request are you appearing?**

2 A. I am appearing on behalf of the Florida Office of Public Counsel ("OPC").

3 **Q. What is the purpose of your testimony?**

4 A. The Office of Public Counsel requested that I review Florida Power & Light's
5 ("FPL" or "the Company") proposed storm cost recovery claims; to express an
6 opinion regarding the reasonableness of FPL's claims; and, if warranted, make
7 alternative recommendations.

8 **Q Please summarize your testimony.**

9 A. Florida Power & Light has requested authority to collect \$356 million (system)
10 from customers as a Storm Cost Recovery Clause surcharge, over two years
11 with interest. I will show that FPL's proposal seeks to require customers to pay,
12 through the storm surcharge, O&M costs that are already covered through the
13 base rates that customers pay. I will also discuss certain principles of
14 capitalization, retirement and cost of removal accounting that should be applied
15 to FPL's storm damage request. Finally, I will demonstrate that in its request,
16 FPL fails to take into account the 2002 stipulation that, OPC asserts, requires
17 FPL to demonstrate that expenses (including storm-related expenses) have
18 caused its earned rate of return on equity capital to fall to below 10 percent
19 before seeking to increase customers' rates for any reason. I will quantify the
20 impact of that omission. I will show that, once adjustments have been made to
21 recognize these considerations, the amount of the negative balance in FPL's
22 storm reserve is reduced from \$356 million to approximately \$46.9 million.

23 **Q. Do you have an exhibit which summarizes FPL's basic estimates?**

24 A. Yes, Exhibit ___(MJM-1) summarizes FPL's basic estimates.

1 **II. Approach to the Analysis**

2 **Q. Please describe the manner in which you approached your analysis of**
3 **FPL's request.**

4 A. My basic approach is based upon recognition of the fact that casualty losses,
5 even catastrophic ones, are not a new phenomenon with respect to the proper
6 accounting principles that should be applied. The basic accounting rules that
7 govern the addition and subsequent depreciation of capital investments, as well
8 as the proper accounting treatment to be afforded operations and maintenance
9 expense, are not rendered inapplicable by the magnitude of the losses.

10 Essentially, the issue is not whether FPL will be allowed to recover
11 prudently incurred costs; rather, the questions are when FPL will recover those
12 costs and whether and to what extent FPL should be allowed to increase rates
13 for the purpose. While the nature of the catastrophe may well warrant the
14 acceleration of the period of recovery, care must be taken to ensure that the
15 special measures adopted to meet the circumstances do not require customers
16 to pay twice for the same costs, whether they are expense or capital, and do not
17 abuse the storm fund and depreciation-related accounts by allowing FPL to
18 expense items it should capitalize and depreciate over time.

19 **Q. Given the magnitude of the storms, how can "normal" accounting**
20 **principles be applicable?**

21 A. There is certainly no dispute regarding the extent of damage or the fact that FPL
22 spent enormous sums of money to repair its system and restore service.
23 However, the situation should be viewed in perspective. FPL contends the
24 negative balance in its storm reserve is \$356 million. The net book value of

1 FPL's electric plant in service is roughly \$10.6 billion (FPL November 2004
2 surveillance report), and over time, FPL has accumulated a reserve of \$1.1
3 billion for the sole purpose of defraying the costs of removing transmission and
4 distribution assets as they are retired. This reserve is separate and apart from
5 the Storm Damage Reserve. Exhibit___(MJM-2), which includes a spreadsheet
6 prepared by the Company, quantifies this \$1.1 billion reserve.

7 FPL's net income for the twelve months ending November 2004 was
8 \$902 million. As I will show later in my testimony, FPL could apply some \$271
9 million to reduce the negative storm reserve balance and still earn a healthy rate
10 of return for the year. While the absolute damage figures are large, and while I
11 do not wish to diminish either the disruptions caused by the storms or the
12 tremendous efforts that were necessary to restore service, the Commission
13 should view the situation in context and not lose sight of accounting principles
14 applicable to casualty losses.

15 This objective is best met by reviewing FPL's proposal to ensure that only
16 extraordinary expenditures (whether capital items or O&M expenses) that are
17 incremental to those the utility would incur under normal circumstances are
18 charged to the storm reserve. I regard this as the "overarching objective" of the
19 analysis of FPL's proposal.

20 **Q. How did you implement this approach in your analysis?**

21 **A.** Upon being engaged by the Office of Public Counsel, I was pleased to learn that
22 OPC was already in the process of formulating, for purposes of its involvement in
23 the docket, a set of specific criteria designed to ensure that only extraordinary
24 expenses would be booked to the Storm Reserve. Having reviewed those

1 guidelines, I endorse them. However, I do have some reservations concerning
 2 the expensing of any capital costs at all. Therefore, from my perspective, the
 3 OPC's criteria are, if anything, generous to FPL. Where the available data allows
 4 me to do so, I have recommended specific adjustments to the Commission. The
 5 OPC's guidelines are:

6 **OPC Storm Damage Guidelines**

7 CAPITAL ADDITIONS:

- 8
- 9 A. All capital additions should be booked to plant in service at current book
 10 cost of materials and labor. Only additional, extraordinary capital-related
 11 expenses should be booked to the storm reserve.
 12
- 13 B. All retirements resulting from 2004 storms should be booked based on
 14 existing, approved depreciation/retirement procedures.
 15
- 16 C. The cost of removal expense related to the plant items that have been
 17 retired due to 2004 storm damage should be excluded from storm
 18 recovery expenses that are charged to the storm damage reserve
 19 account, and should instead be charged to the reserve for accumulated
 20 cost of removal.
 21

22 OPERATING AND MAINTENANCE EXPENSES:

- 23
- 24 D. All base salaries from all bargaining unit labor costs should be excluded
 25 from storm recovery expenses charged to the storm damage reserve
 26 account.
 27
- 28 E. Only those costs of materials and supplies that exceed the material and
 29 supplies expense anticipated under normal operations should be charged
 30 to the storm reserve.
 31
- 32 F. All insurance recoveries, less deductibles, should be eliminated from the
 33 storm recovery amounts.
 34
- 35 G. The amount charged to the storm damage reserve account should
 36 exclude all expenses associated with the following activities:
 37 1. **Operating expenses and overheads for company-owned** vehicles.
 38 2. Storeroom expense.
 39 3. Advertising expense.
 40 4. Employee training expense.

- 1 5. Management overheads except for overtime when working on
2 storms.
- 3 6. All other allocated expenses included in normal operations and
4 existing budgets.
- 5 7. Labor costs associated with repairs and replacements that have been
6 identified as job or work orders, but that have not yet been worked
7 and that will be completed by existing, full time employees or regular,
8 budgeted contract personnel.
- 9 8. Labor costs associated with any work or activity related to the storm
10 other than the jobs or work orders identified in (7) above that will be
11 completed by any employees as part of their regular job duties.
- 12 9. Call center activities should be excluded except for non-budgeted
13 overtime associated with the storm event.
- 14 10. No uncollectible expenses or lost revenues should be booked to the
15 storm reserve.
- 16 11. No expenses associated with cash advances made to employees
17 should be booked to the storm reserve.
18

19 **Q. Why are these principles important?**

20 A. First, the Commission has no specific rule in place that governs the matter. Next,
21 the sheer size and magnitude of 2004 storm events require specific direction for
22 accountants wading through thousands of bills. Ratepayers must be protected
23 from "double billing." The utility must not be allowed to make money from the
24 storm events. It is therefore imperative that the Commission direct the company
25 to follow specific accounting guidelines that it deems appropriate.

26 **III. Background**

27 **Q. Please explain the Storm Damage Reserve.**

28 A. In 1992 Florida suffered severe damage from Hurricane Andrew. As a result,
29 utilities found it difficult to procure reasonably priced commercial insurance for
30 storm damage to transmission and distribution facilities. They petitioned the
31 Commission to authorize self-insurance programs. The Commission authorized

1 FPL to self-insure for transmission and distribution storm damage in Docket No.
2 930405-EI (Order No. PSC-93-0918-FOF-EI, Issued June 17, 1993).

3 **Q. Did FPL have a storm damage reserve prior to that order?**

4 A. Yes. On page 6 of his direct testimony, K. Michael Davis states, "FPL's Storm
5 Damage Reserve was started in 1946, and became a funded reserve in 1958."
6 In 1991 the Company received Commission approval to discontinue its annual
7 accrual to the reserve (Docket No. 910257-EI, Order No. 24728, Issued July 1,
8 1991), however, customers continued to pay the then \$3 million per year annual
9 amount through rates.

10 **Q. Currently, how does the Storm Damage Reserve work?**

11 A. As stated, FPL's Storm Damage Reserve is a funded account. It is increased by
12 annual accruals in amounts approved by the Commission, along with the fund's
13 earnings, and reduced by actual storm damage costs charged to it. In 1993 the
14 annual accrual to the Storm Reserve was set at \$7.1 million. The accrual was
15 increased to \$10.1 million effective January 1, 1994. (Docket No. 930405-EI,
16 Order No. PSC-95-0264-FOF-EI, Issued February 27, 1995.) In Docket No.
17 951167-EI the Company successfully petitioned the Commission to increase the
18 annual accrual to \$20.3 million effective January 1, 1995. (Docket No. 951167-EI,
19 Order No. PSC-95-1588-FOF-EI, Issued December 27, 1995.)

20 **Q. What is the balance in the Storm Damage Reserve?**

21 A. As of December 31, 2004, the Storm Damage Reserve had a balance of \$354
22 million (system). This is before any storm-related charges due to the 2004
23 hurricanes. (Davis Direct, p. 8) If all of FPL's estimated Storm Damage Costs
24 were charged to the reserve, they would result in a negative balance of \$356

1 million (system), as shown in my Exhibit____(MJM-1) which is attached to my
2 testimony.

3 **Q. How does FPL report and account for the Storm Damage Reserve?**

4 A. FPL accounts and reports the Storm Damage Reserve as a Regulatory Liability.

5 As stated in FPL's December 31, 2003 FERC Form 1

6 7. Regulatory Matters

7
8 Regulation – FPL is subject to regulation by the
9 Florida Public Service Commission (FPSC) and the
10 Federal Energy Regulatory Commission (FERC). Its
11 rates are designed to recover the cost of providing
12 electric service to its customers including a
13 reasonable rate of return on invested capital. As a
14 result of this cost-based regulation, FPL follows the
15 accounting practices set forth in Statement of
16 Financial Accounting Standards No. (FAS) 71,
17 “Accounting for the Effects of Certain Types of
18 Regulation.” FAS 71 indicates that regulators can
19 create assets and impose liabilities that would not be
20 recorded by non-rate regulated entities. Regulatory
21 assets and liabilities represent probable future
22 revenues that will be recovered from or refunded to
23 customers through the ratemaking process.
24 (Florida Power & Light Company, December 31, 2003
25 FERC Form 1 Report, pages 123.1.)
26

27 Conceptually, a Regulatory Liability is an amount owed to ratepayers until it is
28 spent on its intended purpose, as opposed to a Regulatory Asset which is an
29 amount assumed to be recoverable from ratepayers. (Statement of Financial
30 Accounting Standards No. 71, paragraphs 9 and 11.) Regulatory Liabilities are
31 not grouped with Regulatory Assets on FPL's balance sheet.

32 **Q. Will you please summarize FPL's storm cost recovery proposal?**

33 A. Yes. In August and September, 2004, four hurricanes struck Florida in rapid
34 succession: Charley, Frances, Jeanne and Ivan. Of these, Charley, Frances and

1 Jeanne impacted FPL's service territory. These hurricanes caused significant
2 damage and left many residents without power, thus causing FPL to incur certain
3 extraordinary costs.

4 On September 9, 2004, FPL filed a petition with the Commission,
5 requesting that it be authorized to establish a regulatory asset for storm damage
6 costs that exceed the \$345 million balance of the Storm Damage Reserve Fund.

7 By Orders issued and consummated October 8, 2004, and November 9, 2004,
8 the Commission found it unnecessary to create a separate regulatory asset
9 because Rule 25-6.0143, Florida Administrative Code, by directing that all costs
10 be charged to the storm reserve, enabled the utility to record a negative balance
11 and thereby defer recognition of the expense pending consideration of its
12 petition. (Docket No. 041291, November 18, 2004 Order Establishing Procedure
13 ("Procedure Order"), p. 1.) FPL also sought future recovery of reasonable and
14 prudently incurred storm damage costs in excess of its Storm Damage Reserve
15 Fund. (Procedure Order, p. 1.)

16 The Commission made its decision regarding FPL's request to establish a
17 regulatory asset with the understanding that FPL will continue booking amounts
18 consistent with its current accounting practice. The Commission noted that the
19 amounts are subject to its review and approval in the event that a subsequent
20 petition for recovery of storm-related damages was to be filed. (Procedure Order,
21 p. 1, emphasis added.)

22 On November 4, 2004, FPL petitioned the Commission to establish a
23 Storm Cost Recovery Surcharge to recover extraordinary hurricane related costs.
24 Specifically:

1 FPL respectfully requests that the Commission enter
2 an order allowing FPL to recover, subject to true-up,
3 an amount equal to the difference between the
4 amount in the Storm Reserve as of August 31, 2004,
5 adjusted for the monthly storm fund accruals and the
6 storm fund earnings through the period September 1,
7 2004 to December 31, 2004, and the actual amount of
8 prudently incurred storm restoration costs associated
9 with storms occurring during the calendar year 2004,
10 net of insurance proceeds, (the "Storm Reserve
11 Deficit" or "Deficit"). FPL proposes to initiate recovery
12 of the jurisdictional portion of the estimated Storm
13 Reserve Deficit of \$356 million (system), or \$354
14 million (jurisdictional), through a monthly surcharge
15 "Storm Restoration Surcharge" to apply to customer
16 bills based on a twenty-four month period (the
17 "Recovery Period"). FPL proposes that the recovery
18 period commence January 1, 2005. (Petition, p. 10-
19 11, footnotes deleted.)
20

21 **Q. What is your opinion regarding FPL's proposed Storm Cost Recovery**
22 **Surcharge?**

23 A. FPL has violated the principles that I delineated above in several respects. First,
24 FPL has improperly moved O&M expenses to the storm fund that customers
25 already bear through the base rates they pay. Second, FPL apparently intends
26 to include all storm-related capital expenditures in its recovery claim.

27 The effect of the improper O&M charges would be to require customers to
28 pay the same costs twice. By charging even normal costs associated with its
29 capital replacements to the storm reserve, FPL would distort the expected rate
30 base increase and bypass normal depreciation practices, leading to distortions in
31 depreciation expense accounts. In addition, FPL would require customers to
32 pay, through a surcharge, the costs of removing damaged plant items when
33 customers have already paid that cost and FPL has accumulated those

1 payments in a reserve marked for the purpose. Finally, and most significant in
2 terms of the dollars involved, FPL has failed to recognize the impact of a
3 stipulation and order that, I am advised, requires FPL's earnings to drop below
4 10 percent ROE before the Company seeks to require customers to bear the cost
5 of reducing the deficiency in its storm reserve. The effect of these failures and
6 departures is to overstate the costs that should be charged to the Storm Damage
7 Reserve.

8 **IV. Categories of Costs**

9 **Q. Does the Company describe the types of costs it proposes to transfer to**
10 **storm recovery?**

11 A. Yes, they are summarized in the Direct Testimony of K. Michael Davis (page 9,
12 emphasis added):

13 All costs incurred in connection with the three named
14 hurricanes which hit FPL's service territory in 2004,
15 both capital and O&M, have been charged to the
16 storm reserve.
17

18 **V. Operations and Maintenance Costs**

19 **Q. Turning first to FPL's proposed treatment of O&M expenses, what is your**
20 **basic objection?**

21 A. By moving all O&M expenses associated with the storm repair effort to the storm
22 reserve, without taking into account the normal level of expenditures funded by
23 base rates that customers pay, FPL effectively requires customers to pay twice
24 for the same costs. I refer to the practice as "double dipping."

25 **Q. Why does FPL's O&M proposal result in a double-dip?**

1 A. FPL proposes that all costs relating to the storms be charged to the Reserve.
2 This fails to recognize that FPL's basic rates include recovery of normal costs,
3 such as base salaries, fleet expenses, and materials.

4 The Company confirms that this is the case in its response to OPC's
5 Interrogatory No. 27, which I have attached as Exhibit___(MJM-3). There, when
6 asked "With respect to payroll expense associated with the company's storm
7 repair activities, does the company agree or disagree with the proposition that
8 the company should exclude from the amount of costs to be booked to the storm
9 reserve (1) all base salaries and (2) average or budgeted overtime?" The
10 Company responded, "See FPL's objections filed February 2, 2005 in Docket No.
11 041291-EI. Notwithstanding and without waiving its objections, FPL responds
12 'Disagree.'"

13 Thus, FPL's proposal would collect twice; once through base rates and
14 again through the Storm Damage Recovery Clause. This is not fair to ratepayers
15 and would unjustly enrich FPL's management and shareholders.

16 **Q. Why does FPL use this approach?**

17 A. FPL wants the customers to bear 100 percent of the risk of storm damage, a
18 concept that the Commission has rejected in the past. In its Order No. PSC-93-
19 0918-FOF-EI, issued June 17, 1993 in Docket No. 930405-EI, the Commission
20 stated:

21 FPL seeks approval for a Storm Loss Recovery
22 Mechanism that would guarantee 100% recovery of
23 expense from ratepayers, over and above the base
24 rates in effect at the time of implementation. This
25 would effectively transfer all risk associated with
26 storm damage directly to ratepayers, and would

1 completely insulate the utility from risk. We decline to
2 approve such a mechanism at this time.

3
4 FPL's cost recovery proposal goes beyond the
5 substitution of self-insurance for its existing policy.
6 The utility wants a guarantee that storm losses will
7 have no effect on its earnings. We believe it would be
8 inappropriate to transfer all risk of storm loss directly
9 to ratepayers. The Commission has never required
10 ratepayers to indemnify utilities from storm damage.
11 Even with traditional insurance, utilities are not free
12 ~~from this risk. This type of damage is a normal~~
13 ~~business risk in Florida.~~

14
15 If FPL experiences significant storm-related damage,
16 it can petition the Commission for appropriate
17 regulatory action. In the past, the Commission has
18 acted appropriately to allow recovery of prudent
19 expenses and has allowed amortization of storm
20 damage expense. Extraordinary events such as
21 hurricanes have not caused utilities to earn less than
22 a fair rate of return, and FPL has shown no reason to
23 believe that the Commission will require a utility to
24 book exorbitant storm losses without recourse.

25
26 Therefore, we decline to authorize the implementation
27 of a Storm Loss Recovery Mechanism, in addition to
28 the base rates in effect at the time, for the recovery,
29 over a period of five years, of all prudently incurred
30 costs in excess of the reserve to repair or restore T&D
31 facilities damaged or destroyed by a storm.
32

33 While FPL's "double dipping" approach might be appropriate for
34 calculating tax losses and insurance claims, it is absolutely wrong when seeking
35 a rate increase from customers. The Commission should implement strict
36 accounting procedures for FPL to follow to eliminate the increased rates that
37 result when customer are required to pay twice for the same expense.

38 **Q. What types of operations and maintenance ("O&M") costs does FPL**
39 **propose to recover through the Storm Recovery Surcharge?**

1 A. The types of costs the Company proposes to recover are listed on Exhibit
2 ___KMD-1 to Mr. Davis' testimony. They include:

- 3 • FPL Payroll
4 • Contractor & Foreign Utility
5 • Vehicle & Fuel
6 • Materials
7 • Logistics
8 • Other
9

10 ~~Mr. Davis does not break these costs out between capital costs and O&M costs.~~

11 **Q. Does OPC propose to eliminate all of these expenses?**

12 A. Absolutely not. Millions of dollars were spent for thousands of workers who
13 cleared the storm damage, and replaced damaged plant. The labor costs,
14 meals, and lodging for these outside crews and their vehicles are clearly
15 extraordinary storm expenses and should be booked to the storm reserved. By
16 the same token, the basic wages and vehicle cost of the company's employee
17 work force and vehicle fleet have been paid for through basic rates and should
18 be excluded from being charged to the storm reserve.

19 FPL readily admits that if an employee worked on the storm, the basic
20 wages plus any overtime would be charged to the storm fund. No basic FPL
21 salary or other expenses should be charged to the storm fund.

22 **Q. Doesn't the Company claim that its accounting procedures were approved
23 by the Commission?**

24 A. FPL states repeatedly, both in testimony and in discovery, that it has charged
25 storm related expenses to the Storm Reserve in accordance with the accounting
26 treatment described in its study submitted in Docket No. 930405-EI and
27 approved by the Commission in Order No. PSC-95-0264-FOF-EI, issued

1 February 27, 1995. However, a careful reading of the order shows that the
2 Commission approved an increase to the storm reserve itself and expressed its
3 intent to engage in rulemaking and workshops regarding procedures. That never
4 happened.

5 **Q. Please explain.**

6 **A. After summarizing FPL's study, the Commission said the study was "adequate."**

7 It then added, "We are considering the appropriateness of opening a rulemaking
8 proceeding to establish uniform guidelines for determining when the storm
9 damage reserve should be charged and what costs should be charged to it."
10 (Order No. PSC-95-0264-FOF-EI at page 5.) While I am not an attorney, and I
11 don't intend to offer a legal opinion, it appears to me the Commission did not
12 "bless" FPL's approach to the extent FPL now claims. In my opinion as an
13 accountant, the proposal would abuse the storm reserve and mistreat customers.
14 I explain the basis for my belief later in my testimony.

15 **Q. Should FPL be allowed to recover "each and every cost" relating to storm
16 damage recovery through a surcharge?**

17 **A.** No. The circumstances in this case are very different from those previously
18 experienced. First, three major hurricanes in a single year is at best unusual,
19 both for FPL and for its ratepayers. FPL has been accruing \$20.3 million per
20 year in its Storm Damage Reserve Fund since 1995 and customers have never
21 been asked to pay more for specific storm expenses. The fund currently has a
22 balance of \$354 million. And now the Company is faced with a deficiency of
23 \$356 million in its storm reserve. Unlike in the past, it wants ratepayers to pay for
24 that deficiency separately and above from what ratepayers are already paying to

1 cover the day-to-day operations of the Company and the fund. The Commission
2 ruled that the Company could petition for recovery – but did not guarantee that it
3 would provide recovery through means that would not affect earnings. Clearly,
4 the Commission deliberately retained its ability to view a request in light of all
5 relevant circumstances and tailor its response accordingly.

6 **Q. Can you provide an example of a clearly inappropriate expense FPL**
7 **proposes to charge to the Storm Damage Fund?**

8 A. Yes. The sheer magnitude of the storm accounting justifies an audit, which is
9 under way. The incentive clearly exists for the company to add projects that
10 may be in its existing budgets or for projects that are questionable as they relate
11 to 2004 storm restoration efforts. Two such examples were provided in the
12 Company's response to OPC POD No. 19, that was designed to obtain copies of
13 uncompleted work orders that exceed \$100,000 as of 12/31/04. (Exhibit
14 ____(MJM-4)) The Company's response included a project that is listed at
15 \$1,035,520. The project name is "Identify salt spray, sand and water intrusion
16 problems in coastal communities." In view of the known fact that FPL serves
17 coastal communities that have been subject to salt spray, sand and salt water
18 intrusion since the beginning of time, I would question whether (1) this study has
19 anything to do with restoration of 2004 storm damages, and (2) whether the
20 company, as the holder of the franchise, has a basic obligation to be
21 knowledgeable about the subject. If this study is viable, it should be paid for from
22 base rate revenues.

1 Likewise, the Company included an additional \$341,000 for a third party
2 assessment to determine the relative state of vegetative conditions post storm.
3 Both of these projects relate to future company operations, not to storm recovery.

4 **Q. What is the Company policy relating to the booking of costs to the storm**
5 **fund?**

6 A. **Company witness Davis states, "The use of the fund is restricted to un-insured**
7 **losses** that are covered by the storm and property damage reserve." (Davis,
8 Direct Testimony, Pg. 7, L 19-22). The above projects do not relate to storm
9 losses, but to future operations.

10 The Company lists over \$40 million in projects that are incomplete as of
11 December 31, 2004, three months after the last storm hit the Company's
12 operating territories. However, all of the customers have long since had their
13 service restored. If their service is working, how are the customers to know
14 whether the replacements are because the facilities are old and worn out, or
15 because they have been damaged and don't work?

16 **Q. Do you disagree with the recovery of all of FPL's proposed O&M costs?**

17 A. As I stated earlier, many expenses identified by the Company are truly
18 extraordinary in nature. However, I believe the amounts approved for recovery
19 should not include normal levels of expenses as measured by the budget. I have
20 the following specific disagreements:

- 21 • Base Salaries – FPL proposes to charge the full labor costs associated
22 with storm recovery efforts to the Storm Damage Reserve. This includes
23 normal base salaries, which are already included in the Company's annual
24 budget. The ratepayers are paying for these salaries through base rates.

1 They should not be required to pay for them twice. Based on the
2 Company's response to Late Filed Exhibit No. 10 to the January 28, 2005
3 deposition of Mr. Robert Adams, it appear that FPL has charged \$32
4 million in regular salaries to the Storm Reserve. See Exhibit__(MJM-5).
5 This amount should be removed from the Company's storm damage
6 claim.

-
- 7 • Vehicle Expense – According to Exhibit No. __ (KMD-1), FPL proposes
8 to recover \$19.4 million in Vehicle & Fuel Expense related to the
9 hurricanes. OPC's Interrogatory No. 31, attached as Exhibit__(MJM-6)
10 to my testimony, requested a detailed breakdown of all costs related to
11 company-owned vehicles that FPL has booked, or proposes to book to the
12 storm reserve. In response, FPL provided the breakdown of \$8,088,117 in
13 costs. These expenses included \$1.7 million for depreciation, \$4.6 million
14 in maintenance, \$947 thousand for fuel, and \$842 thousand in
15 overhead/support. Although Company vehicles have been used in the
16 storm recovery effort, these vehicles have already been included in the
17 annual budget. In fact, the response goes on to identify the portion of the
18 \$8.1 million that FPL would have incurred in the normal course of
19 business, whether or not there were hurricanes in 2004. That amount
20 was \$5,261,887. This is the amount included in the annual budget. In
21 other words, of the \$8.1 million relating to company owned vehicles
22 included in the storm reserve, only \$2.8 million relates to extraordinary
23 costs. As I am able to calculate it at this time, the adjustment related to

1 vehicle expense should be a removal of \$5,261,887 from the storm
2 damage claim.

3 • Tree Trimming – Tree trimming expense should be limited to the amounts
4 which exceed FPL’s normal expenses. I do not have sufficient information
5 to make an adjustment for tree trimming expense at this time.

6 • Call Center Expense – Call center expenses for the storm recovery should
7 be limited to the call overloads created by the storms. I do not have
8 sufficient information to make an adjustment for call center expense at this
9 time.

10 **Q. Do you have an exhibit which summarizes the O&M expense adjustments**
11 **you discuss above?**

12 A. Yes, these expense adjustments are summarized on Exhibit___(MJM-7).

13 **Q. Now that the storms have passed and operations have returned to normal,**
14 **does the Company plan to continue to charge costs in the Storm Reserve,**
15 **related to these hurricanes?**

16 A. That appears to be the case. OPC Interrogatory No. 35 asks whether the
17 company agrees or disagrees with the proposition that labor costs associated
18 with repairs and replacements that have been identified as job or work orders,
19 but that have not yet been worked and will be completed by existing, full time
20 employees or regular, budgeted contract personnel should be excluded from
21 amounts booked to the storm reserve. In its response, FPL states, “FPL
22 disagrees. If labor costs associated with repairs and replacements are related to
23 storm restoration they should be charged to the storm reserve.”

24 **Q. Do you agree with this practice?**

1 A. No. Once normal operations have resumed, outside contractors have been sent
2 home, and employees are back to working a normal workweek, any remaining
3 storm-recovery activities should be performed in the normal course of business
4 and should not be booked to the storm account. FPL should be required to
5 demonstrate that it has incurred extraordinary expense before it is allowed to
6 receive extraordinary recovery.

7 **VI. Capital Costs**

8 **Q. How does the Company plan to handle capital costs relating to storm**
9 **damage repair?**

10 A. All costs incurred in connection with the three named hurricanes which hit FPL's
11 service territory in 2004, both capital and O&M, have been charged to the storm
12 reserve. (Direct Testimony, K. Michael Davis, Pg. 9, L 19-22)

13 The Company has itemized its storm damages by each Hurricane in Mr.
14 Davis' Exhibit KMD-1, and that amounts to \$710 million, net of insurance
15 reimbursements of \$108 million.

16 Based on Mr. Davis' testimony and the itemization of the storm charges,
17 the Company has no plans to make any adjustments in the amounts it proposes
18 to pass on to customers for capital retirements and additions that are required
19 due to the 2004 storms.

20 **Q. What is the appropriate accounting methodology that should be used for**
21 **capital additions and retirements that were due to storm damage?**

22 A. An unregulated business would declare a casualty loss for the undepreciated
23 portion of the plant destroyed by the storm and book the entire replacement cost
24 to gross plant, including the extraordinary labor required to remove the old plant

1 and the extraordinary labor to install the new plant, less, of course, any insurance
2 that was collected for that purpose. Future depreciation expense might rise or
3 fall as a result of this accounting.

4 As a regulated utility, FPL is free to follow that same approach. However,
5 if the Commission is moved to provide more immediate measures to capture
6 extra-ordinary storm casualty losses, then the accounting entries are the same.

7 The accounting entries would be as follows:

- 8 a. Record total material and labor expenses to storm reserve.
- 9
- 10 b. Calculate total additions (material and labor) at current normal cost of
- 11 material and labor.
- 12
- 13 c. Subtract b. from storm reserve and book (add) to Plant in Service.
- 14
- 15 d. Calculate total recorded cost of retirements.
- 16
- 17 e. Subtract recorded cost of retirements and book (subtract) from Plant in
- 18 Service and accumulated depreciation.
- 19
- 20 f. Calculate the cost of removal for plant retirements resulting from the
- 21 storms and book (subtract) from the storm reserve and the
- 22 accumulated cost of removal reserve.
- 23

24 These procedures are the same as were recently agreed upon by the
25 Office of Public Counsel and Gulf Power in a stipulation filed with the FPSC on
26 January 28, 2005, regarding the recovery of Gulf's extraordinary storm expenses
27 due to Hurricane Ivan.

28 **Q. Does FPL plan to follow the accounting approach you have outlined?**

29 A. As far as I can determine, FPL does not intend to reduce its storm recovery
30 proposal to account for capital replacements, and this is wrong. In his
31 deposition, Mr. Davis described a variety of depreciation entries the company
32 plans to record in order to equalize the Company's capital accounts to the

1 amounts that existed prior to the hurricanes (Davis Deposition 1-28-05, pgs. 18-
2 27. My first conclusion after reading his deposition is that the company goes to
3 great lengths to avoid any increase in its plant in service and resulting
4 depreciation expense, while it ignores the fact that it has replaced substantial
5 quantities of its old facilities with brand new poles, transformers and conductors.
6 My second conclusion is that the company goes to great lengths to avoid any
7 adjustments to its storm recovery proposals that would reduce its accumulated
8 depreciation, and/or the \$1.1 billion of accumulated cost of removal reserve that
9 it has already collected from its customers.

10 **Q. Why would FPL's approach result in unreasonable charges being passed**
11 **through the storm reserve?**

12 A. FPL's approach goes far beyond OPC's principles. The approach would pass
13 through to customers, as storm related expenses, all the capital addition costs
14 that FPL incurred. Furthermore, under FPL's approach the new replacement
15 plant items would be artificially "aged" in order to arrive at a predetermined net
16 plant in service level equal to that which existed prior to the storms. Based on
17 discovery, FPL would label the adjustment required to achieve this artificial result
18 a "contribution in aid of construction." It would charge this adjustment to the
19 storm reserve, and thus to the amount that it wants customers to pay through a
20 two-year surcharge.

21 **Q. What is the impact of FPL's approach?**

22 A. The implementation of FPL's approach would distort plant in service and
23 depreciation accounts. New plant would be placed in service at the cost of older
24 vintages, meaning depreciation expense will be understated and depreciation

1 reserves will be inadequate, at the same time ratepayers would be asked to pay,
2 through a surcharge applied to bills for a two year period, amounts that should be
3 capitalized and depreciated over the lives of the associated plant items.

4 **Q. Is there anything else wrong with FPL's approach?**

5 A. Yes. To add insult to injury, even though FPL has collected \$1.1 billion from
6 ratepayers to cover the cost of removing Transmission and Distribution plant
7 items as they are retired, none of the cost of removal FPL actually incurred will
8 be charged to the cost of removal reserve. Instead, if the Commission approves
9 FPL's approach, the costs of removal will all flow through the storm reserve and
10 wind up as surcharges to ratepayers. Again, this would be accomplished by
11 running a "contribution in aid of construction" through the accumulated
12 depreciation account. This is inappropriate. The Commission should not allow
13 FPL to use accounting form over accounting substance to subvert reasonable
14 ratemaking principles. Consistent with the principles that I have endorsed in my
15 testimony, cost of removal should be charged to the cost of removal reserve.

16 **Q. Do you have any additional comments about FPL's depreciation rates and**
17 **cost of removal?**

18 A. Yes, the \$1.1 billion cost of removal reserve was built up by allowing FPL to
19 include a future cost of removal component in its annual depreciation rates. If
20 those funds are not available when needed, the Commission should consider
21 whether or not it is appropriate to continue to charge ratepayers for future cost of
22 removal.

23 **Q. Have you calculated an adjustment to the Company's storm damage claim**
24 **to reflect your capital recommendations?**

1 A. No. I do not have sufficient information to make such an adjustment at this time
2 because the Company has not provided such information.

3 **Q. What is your recommendation for the Commission regarding capital**
4 **replacements?**

5 A. The Commission should require the Company to document all of its entries to the
6 storm reserve and its plant accounts consistent with my recommendations and
7 withhold the Company's request for recovery from its customers until the
8 Company complies.

9 **VII. FPL's Failure to Apply 2004 Earnings Above 10% ROE to Reduce the**
10 **Negative Balance in its Storm Reserve**

11 **Q. Are FPL's service rates subject to a "rate plan"?**
12

13 A. Yes. I am informed that FPL's service rates are subject to a rate plan
14 established as the result of a 2002 settlement in Docket Nos. 001148-EI and
15 020001-EI. The Commission approved a stipulation in which parties agreed to
16 implement a "revenue sharing" plan in lieu of an authorized range of rate of
17 return on equity for a period of time. My understanding is that as part of the
18 arrangement FPL agreed it would not seek to increase base rates unless its
19 earnings fell below 10% return on equity.

20 **Q. What is OPC's position regarding this rate plan and the interplay with the**
21 **Storm Damage Reserve?**

22 A. I am advised that OPC's position is that the stipulation effectively requires FPL to
23 apply 2004 earnings above 10 percent ROE to reduce the negative balance in
24 FPL's storm reserve before seeking to increase customers' rates for the purpose.

25 **Q. Does any other OPC witness address this issue?**

1 A. Yes. While OPC's primary position is based on a legal argument, in his
2 testimony Mr. James A. Rothschild explains that, in view of the risk appropriately
borne by FPL and in view of current economic factors, in his opinion the 10
4 percent criterion would be a reasonable way to share the risk even if there were
5 no stipulation. Given what I have been advised is the legal effect of the
6 stipulation, and in light of Mr. Rothschild's opinion, I will identify the size of the
7 adjustment that would be needed to apply the 10 percent criterion.

8 **Q. Do you expect FPL to earn more than 10 percent ROE in 2004?**

9 A. Yes.

10 **Q. Has the Company performed any calculations demonstrating how much of**
11 **the storm restoration costs it could absorb before dropping to the 10**
12 **percent ROE threshold?**

13 A. No. The Company was asked to perform such a calculation in OPC's
14 Interrogatory No. 40, and refused to do so:

15 Q. Using the methodology and adjustments that are
16 consistent with those prescribed by the Florida Public
17 Service Commission for the preparation and
18 submission of monthly surveillance reports, please
19 calculate and state the amount of 2004 earnings that,
20 if applied to reduce the negative balance of the storm
21 reserve, would result in an earned rate of return for
22 FPL of (a) 11%; (b) 10.5%; and (c) 10% for calendar
23 year 2004.

24
25 A. Please see FPL's objections filed February 2,
26 2005 in Docket No. 041291-EI.

27
28 In its objection, FPL states:

29
30 Interrogatory No. 40: FPL objects to Interrogatory No.
31 40 to the extent it requires FPL to prepare information
32 in a particular format and perform calculations or
33 analyses not previously prepared or performed.

1 Further, FPL objects in that the interrogatory requires
2 FPL to conduct an analysis or create information not
3 prepared by FPL in the normal course of business.
4 Finally, the information needed to perform the
5 requested calculation is readily available to OPC
6 through normal procedures, or is not yet available.
7

8 **Q. Have you made this calculation?**

9 A. Yes. By my calculations, FPL could apply \$271 million to reduce the negative
10 balance of the storm reserve and still earn 10% return on equity capital for
11 calendar year 2004. My calculation is shown on Exhibit__(MJM-8).

12 **VIII. Summary**

13 **Q. Please summarize your recommendations.**

14 A. In this case, FPL has claimed that storm-related costs have resulted in a
15 negative storm reserve balance of \$356 million (system), which FPL wants to
16 collect from customers over a period of two years. However, this amount should
17 be reduced to remove O&M and capital costs that should not have been charged
18 to the storm reserve to begin with. To date I have estimated about \$38.6 million
19 (system) of those types of expenses. In addition to these reductions, FPL should
20 apply \$271 million (system), whether to satisfy the legal requirement of the 2002
21 ratemaking stipulation or to implement the recommendation of James Rothschild
22 to reflect an appropriate sharing of storm-related risks. As shown in
23 Exhibit__(MJM-7), the impact of my adjustments is to reduce FPL's proposed
24 surcharge from \$356 million to \$46.9 million. I recommend the Commission
25 emphasize its approval of a surcharge is limited to the specific 2004 events, and
26 does not authorize FPL to charge further amounts of storm related costs to the
27 reserve without specific Commission approval.

1 Q. Does this conclude your testimony?

2 A. Yes, it does.

1 **SUPPLEMENTAL TESTIMONY**

2 **OF**

3 **MICHAEL J. MAJOROS, JR.**

4 **DOCKET NO. 041291-EI**

5

6 **Q. Please state your name.**

7 **A. My name is Michael J. Majoros, Jr.**

8 **Q. Have you already submitted testimony in this proceeding?**

9 **A. Yes, I submitted direct testimony on February 8, 2005.**

10 **Q. What is the purpose of your supplemental testimony?**

11 **A. FPL filed an amendment to its initial storm cost request. FPL increased its initial**
12 **estimate of storm related costs from \$710 million to \$890 million (net of**
13 **insurance proceeds). I am filing this supplemental testimony to update my**
14 **Exhibit__(MJM-7) to incorporate FPL's revised estimate. As a result of FPL's**
15 **update, I have increased my estimated Retail Storm Deficiency from \$46.65**
16 **million to \$225.79 million.**

17 **Q. Are you sponsoring any additional adjustments as a consequence of the**
18 **amendment?**

19 **A. No. As I indicated in my direct testimony, my primary objection is to FPL's**
20 **accounting.**

21 **Q. Does this complete your supplemental testimony?**

22 **A. Yes, it does.**

1 has at a minimum a \$1.24 billion book depreciation reserve excess which it has
2 already charged to and collected from its customers in the past. While the parties
3 are debating the amount that FPL should charge to the storm damage reserve, it is
4 clear that however that comes out, FPL's book depreciation excess will far exceed
5 any deficient balance in the storm reserve that the Commission will determine in
6 this docket.
7

8 **Q. What is a book depreciation reserve excess?**

9 A. The book depreciation reserve is the amount of depreciation that FPL has charged
10 to and collected from its customers. A book depreciation *reserve excess* is the
11 amount of money that FPL has charged to and collected from its ratepayers in
12 excess of current requirements.
13

14 **Q. Can you verify that FPL has calculated a \$1.24 billion book depreciation
15 reserve excess?**

16 A. Yes. Exhibit____(MJM-10) attached to this additional supplemental testimony is
17 a copy of FPL's March 16, 2005 depreciation study transmittal letter and the
18 related attachment. FPL's calculated book depreciation reserve excess is shown
19 on page three of the attachment. It is the difference between the \$1.569 billion
20 "Unadjusted Excess" and the \$330 million "Allocated Bottom Line Reserve."
21

22 **Q. Mr. Majoros, your direct testimony identified a reserve of \$1.1 billion that
23 FPL has accumulated for the sole purpose of defraying the costs of removing**

1 transmission and distribution assets as they are retired. Is this the same
2 money that FPL has identified in its March 16, 2005 depreciation study as its
3 \$1.24 billion book depreciation reserve excess?

4 A. No. The cost of removal reserve which I identified in my direct testimony is
5 included in the book depreciation reserve. In other words, FPL has also charged
6 that money to its customers. Therefore, FPL's \$1.24 billion book depreciation
7 ~~reserve excess is over and above its cost of removal reserve which, including~~
8 production plant, now exceeds \$2 billion including production plant. (December
9 31, 2004 10K).

10
11 Q. Are you confusing this cost of removal reserve or the book depreciation
12 reserve excess with any nuclear decommissioning fund reserves?

13 A. No, the book depreciation reserve excess and the cost of removal reserve are
14 separate from nuclear decommissioning reserves.

15
16 Q. Are you saying that FPL has already collected more than enough money
17 from its customers to pay for a deficiency in its storm damage reserve?

18 A. Yes. Based on its own study, FPL has collected at least \$1.24 billion from its
19 customers in the form of excessive depreciation. This is far more than any of the
20 estimates of the storm damage reserve deficiency.

21
22 Q. Does FPL's depreciation study identify any book depreciation reserve
23 deficiencies for any of its plant functions?

1 A. The attachment to FPL's transmittal letter shows book depreciation reserve
2 excesses across the board. However, when I review the six-volume depreciation
3 study, I see that FPL may have calculated a small deficiency in the distribution
4 function. But that potential deficiency is much less than the overall book
5 depreciation reserve excess. FPL could eliminate that deficiency by transferring a
6 small portion of the overall book depreciation reserve excess to that function and
7 still have over \$1 billion to apply to the storm damage reserve.

8

9 **Q. From the standpoint of proper regulatory accounting is it appropriate to use**
10 **the surplus in the depreciation accounts to reduce or eliminate the negative**
11 **balance in the storm damage reserve?**

12 A. Yes. FPL's \$1.24 billion book depreciation reserve excess represents, by FPL's
13 own definition, excessive charges that it has collected from its customers.
14 Principles of regulatory accounting enable FPL to apply the excess in depreciation
15 reserves to reduce whatever negative balance in its storm damage reserve that the
16 Commission identifies in this case. I recommend that the Commission consider
17 this option.

18

19 **Q. Does this conclude your additional supplemental testimony?**

20 A. Yes, it does.

21

22

1 BY MR. McGLOTHLIN:

2 Q Mr. Majoros, are you ready to summarize your
3 testimony for the Commissioners?

4 A Yes, I am.

5 Q Please begin.

6 A My direct testimony explains that FP&L's proposal
7 seeks to require customers to pay through a surcharge operating
8 and maintenance costs already covered in base rates. It also
9 explains that the charges include capital costs such as plant
10 additions and cost of removal.

11 My testimony demonstrates that FPL has already
12 collected \$1.1 billion for cost of removal from customers, and
13 yet FPL does not want to use that money, rather it would charge
14 cost of removal from the storm to customers via a surcharge.

15 I adopt a set of principles developed by the Office
16 of Public Counsel. These principles seek to allow FPL to
17 charge its incremental operating and maintenance and capital,
18 but not normal charges to the storm reserve. As a result, I
19 have identified a few specific items which should be excluded.
20 I have also implemented the OPC's position that FPL should
21 absorb enough storm expenses to earn a 10 percent return on
22 equity.

23 My supplemental testimony adjusts my original
24 quantifications for an update submitted by Mr. Davis. My
25 resulting total is \$226 million -- is a \$226 million storm

1 reserve deficiency versus Mr. Davis's \$533 million storm
2 reserve deficiency.

3 My additional supplemental testimony discusses the
4 fact that FPL identified a \$1.24 billion depreciation reserve
5 excess over and above the \$1.1 billion cost of removal reserve
6 that I discussed in my direct testimony.

7 FPL acknowledges this as a reserve excess.

8 ~~Therefore, I recommend that the storm reserve deficiency be~~
9 eliminated by a portion of the depreciation reserve excess.

10 Finally, as noted at Footnote 2 of my Exhibit MJM-7 updated, my
11 \$226 million storm reserve deficiency estimate did not include
12 adjustments for costs of replacements to plant that should be
13 capitalized and the cost of removal that should be charged to
14 the reserve for cost of removal, final values for which have
15 not -- had not been provided at those times -- at that time.
16 But those adjustments must be made.

17 That ends my summary.

18 MR. MCGLOTHLIN: The witness is available for
19 cross-examination.

20 COMMISSIONER BAEZ: Mr. Perry.

21 MR. PERRY: I don't have any question for the
22 witness.

23 COMMISSIONER BAEZ: Mr. Wright.

24 MR. WRIGHT: Thank you, Mr. Chairman. I do have a
25 few.

CROSS EXAMINATION

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BY MR. WRIGHT:

Q Good morning, Mr. Majoros.

A Good morning.

Q We have met. I am Schef Wright. I represent the Florida Retail Federation. How many times have you testified on utility regulatory matters?

A Over 100 times.

Q And were the majority of those on issues related to accounting?

A Accounting and depreciation.

Q Have you testified with regard to the consistency of accounting methods with generally accepted accounting principles?

A That has been the subject of some of my testimony.

Q Are you generally familiar with the generally accepted accounting principles?

A Yes.

Q And with the standards of the Financial Accounting Standards Board?

A Yes.

Q Thank you. In your -- in the last batch of testimony you filed you recommended that the Commission direct FPL to use some of the accumulated depreciation reserve surplus to replenish the Storm Reserve Fund. Do I have that right?

1 A I didn't use the word "replenish." I think I'm
2 offsetting an excess against a reserve.

3 Q Okay. Are you familiar that, with FPL's testimony
4 that there are what they refer to as pricing issues involved in
5 using the accumulated depreciation reserve surplus in that way?

6 A Yes, I am, I'm aware that Mr. Davis has said that.

7 Q In your opinion, do such concerns preclude using the
8 depreciation reserve surplus as you have suggested?

9 A No.

10 Q Does using the accumulated depreciation reserve
11 surplus as you have suggested cause any problems or any
12 inconsistencies with generally accepted accounting principles?

13 A In my opinion, that's irrelevant. I'm not aware of
14 any, but GAAP does not drive regulation.

15 Q Same question with regard to the standards of the
16 Financial Accounting Standards Board.

17 A Well, that's part of GAAP.

18 Q Okay. So same answer?

19 A Same answer.

20 Q Thank you.

21 A I'm not disavowing GAAP. I'm just saying regulatory
22 decisions prevail in these circumstances.

23 Q Does that mean that regulators, as you understand it,
24 are not bound by GAAP?

25 A That is correct.

1 Q Thank you. I noted on Page 5 of your testimony that
2 you endorsed the Office of Public Counsel's storm damage cost
3 guidelines. My question for -- that's right, isn't it?

4 A That is correct.

5 Q Do you agree that those principles are consistent
6 with sound public policy?

7 A In my opinion they are.

8 Q Would it be your opinion that they are consistent
9 with appropriate ratemaking practices?

10 A Again, in my opinion they are. Although I had some
11 reservations, I think I mentioned it in my testimony, about,
12 about those principles. I think they're very generous to
13 utilities in that they would allow capital costs to be charged
14 to the Storm Damage Reserve, the incremental capital costs.
15 And personally I think all capital costs ought to be
16 capitalized.

17 Q Thank you. One more question along that line, and
18 that is if you have an opinion on, on this, I would like to ask
19 you whether it would be your opinion that applying the Public
20 Counsel's guidelines would result in fair, just and reasonable
21 rates?

22 A I believe that is correct. Yes.

23 Q Thank you. At Pages 11 and 12 you talk about an
24 accounting phenomenon or a payment phenomenon that you refer to
25 as double-dipping.

1 A Yes.

2 Q I just want to make sure that, that I'm clear on what
3 you're saying here. Is what you're saying that FPL's proposal
4 would result in customers paying for the exact same labor
5 services two times?

6 A Yes. Conceptually, in my opinion, yes. Now that is
7 as they relate to O&M, operating and maintenance expenses.

8 ~~Q Did you want to expand on that any?~~

9 A The reason --

10 Q I don't understand why you made that, that
11 clarification. So if you could clarify, I'd appreciate it.

12 A Because, I'm making that distinction because
13 operating, operating and maintenance expenses are included in
14 the annual operating budget.

15 Capital expenses, remember, I said that in
16 addition -- and that's what the budget is for and that's what
17 rates are based on. Capital is assumed to be capitalized and
18 depreciated. So I think that the capital expenditures that are
19 in, that would be allowed even via the Office of Public
20 Counsel's proposal are not in the operating budget. So that is
21 not specifically a double count as I'm describing it here.

22 Q Okay. Yes. Well, as I understood your, your
23 description of the phenomenon that you called double-dipping,
24 it was referring to O&M costs only.

25 A O&M expenses.

1 COMMISSIONER BAEZ: Mr. Majoros, can you get a little
2 closer to the mike, if you can?

3 THE WITNESS: Yes, sir.

4 BY MR. WRIGHT:

5 Q At Page 15 of your testimony, Mr. Majoros, you make
6 this statement, "In my opinion as an accountant the proposal,"
7 FPL's proposal that is, "would abuse the storm reserve and
8 mistreat customers." And I would like to ask you to explain to
9 the Commissioners how it would abuse the storm reserve and how
10 it would mistreat customers.

11 A I believe charging normal expenses to the storm
12 reserve and then in turn collecting them as surcharges over
13 and -- within base rates is an abuse of -- it's an exploitation
14 of an extraordinary problem that occurred this year, and I
15 think that is an abuse.

16 Furthermore, I believe that this company well knows
17 that it has accumulated over a billion dollars for the sole
18 purpose of the removal of assets. And in particular, the
19 billion dollars that I have identified relates primarily to
20 transmission and distribution assets, primarily. And to not
21 even acknowledge that in its proposal seems to me in my
22 personal opinion to be an abuse. It's a serious problem. The
23 company incurred a lot of costs, it did a good job in restoring
24 service. Ratepayers, some ratepayers, I understand, are still
25 trying to get their homes fixed. You know, it just seems to me

1 that the way this company did this as opposed to what we might
2 consider to be, you know, a worse storm -- a less worse -- a
3 less bad storm system is an abuse. There are plenty of
4 mechanisms the company could have used to, to soften the impact
5 of this storm season on ratepayers. And I think it was an
6 abuse.

7 COMMISSIONER BAEZ: Commissioner Davidson.

8 COMMISSIONER DAVIDSON: On this issue, Mr. Majoros,
9 as sort of an accounting issue, where there is, say, some type
10 of surplus, is there an accounting principle that would suggest
11 that is applied prospectively, retroactively? I mean, what
12 sort of governs how a reserve is dealt with?

13 And I understand, you know, the Commission has
14 discretion and ratemaking is not quite accounting. But from
15 just an accounting standpoint, if you had a client and there
16 was sort of this reserve and it had to be dealt with somehow,
17 what, what would you look to to determine how to deal with
18 that, if that question makes sense?

19 THE WITNESS: The question makes sense. You're
20 asking me what I would say to a client of mine after the fact,
21 after the storms hit?

22 COMMISSIONER DAVIDSON: Well, from trying to, trying,
23 if you can, to sort of divorce your, your opinion as to what's
24 right and what sort of should occur given the whole context and
25 trying to limit it to are there, are there sort of accounting

1 guidelines or principles that would address this type of
2 reserve and how to deal with it?

3 THE WITNESS: Well, I think that the, the, the
4 accrual and reserve method that the Commission has approved and
5 is being used is a reasonable method to anticipate the costs
6 for storms. Unfortunately, nobody has perfect foresight and
7 who would have known that you were going to have -- there were
8 actually four hurricanes here and would have incurred this much
9 damage?

10 But I think that the reasonable way to move forward
11 with this is to consider how much, given now what we know and
12 the probabilities of it potentially happening again, look at
13 the level of the accrual that goes to the storm reserve. I
14 think that's what -- on a going-forward basis.

15 Now as far as this, you know, the damages from this
16 storm, if I had a client who was an unregulated client --

17 COMMISSIONER DAVIDSON: Well, let me sort of jump in
18 there. I didn't mean to cut you off, but I probably was
19 unclear in my answer (sic.) I was trying to -- or in my
20 question. I was trying to ask specifically about the
21 depreciation reserve that you just talked about, not the storm
22 charge reserve. But the -- if -- maybe I misunderstood. Did
23 you just reference the depreciation reserve?

24 THE WITNESS: There's a couple of reserves that I've
25 mentioned.

1 COMMISSIONER DAVIDSON: Okay. Well, I was talking
2 about that depreciation reserve specifically. Are there
3 accounting principles or guidelines that would sort of tell
4 you, outside the context of this case just, or in the context
5 of this case but in general, okay, here's this client that's
6 got this huge depreciation reserve, we know that, everybody
7 sort of agrees this reserve is there, are there accounting
8 principles or guidelines that would tell you how to deal with
9 that?

10 THE WITNESS: I'm going to, I'm going to, I'm going
11 to try to answer. Are there accounting principals and
12 guidelines? In my opinion, yes. And the guideline, I'm going
13 to try and articulate it. I can't point to a special rule.
14 But if the company accrues and charges its customers, and we're
15 talking about regulated utilities here, charges its customers
16 an amount for future cost of removal and then in the future
17 incurs costs of removal, it ought to charge that cost of
18 removal that it incurred to the reserve that it built up for
19 cost of removal.

20 FPL has a reserve for cost of removal of
21 \$1.1 billion, and yet it doesn't want to charge a penny of the
22 cost of removal it incurred during the storms to that reserve.
23 It would rather charge it to ratepayers via an incremental
24 surcharge over two years.

25 To me, when I -- when we were talking about abuse

1 earlier, I -- to me that's an abuse and it flies in the face of
2 why this Commission, why this company has in the past asked
3 this Commission to approve depreciation rates which include a
4 specific component for cost of removal, and then when it needs
5 to use that money, it wants to charge, instead of using it, it
6 wants to charge ratepayers. I think that flies in the face of
7 good sound regulatory GAAP and every other kind of accounting
8 principle.

9 COMMISSIONER BAEZ: Commissioner Davidson.

10 COMMISSIONER DAVIDSON: That's all.

11 COMMISSIONER BAEZ: Commissioner Deason, you had a
12 question.

13 COMMISSIONER DEASON: Yes. Mr. Majoros, I had a
14 question on cost of removal, and now seems to be a good time to
15 ask it.

16 As I understand your testimony, it's your position
17 that there is a reserve that has been accumulated over time
18 based upon depreciation rates to allow there to be a reserve
19 for a cost of removal. Is that correct?

20 THE WITNESS: Your use of the word "position," I
21 think it misrepresents what I'm saying.

22 The -- this company has identified in its 10K, Form
23 10K and its Form 1 a reserve for cost of removal of
24 \$1.1 billion as a regulatory liability, an amount owed to
25 ratepayers.

1 COMMISSIONER DEASON: You must be reading something
2 into my question. I'm just trying to understand.

3 THE WITNESS: No, but that's not my position. It's
4 not a number -- I'm not taking a position. I'm stating a fact.

5 COMMISSIONER DEASON: All right. Your testimony says
6 that there is a reserve for cost of removal.

7 THE WITNESS: Yes.

8 COMMISSIONER DEASON: And it should be utilized.

9 THE WITNESS: That's correct.

10 COMMISSIONER DEASON: That's all I'm trying to
11 establish.

12 THE WITNESS: I'm sorry. I --

13 COMMISSIONER DEASON: I'm not cross-examining you,
14 sir. I'm trying to understand the issue because I'm going to
15 be the one to have to make the vote.

16 THE WITNESS: I was just trying to clarify that, that
17 it's not a position.

18 COMMISSIONER DEASON: Yes, sir. Just don't be so
19 defensive. I'm just trying to get the facts out here. Okay?

20 THE WITNESS: I get scared up here.

21 COMMISSIONER DEASON: Okay. Are you familiar with
22 the methodology this Commission uses in establishing
23 depreciation rates, which by definition include a component for
24 cost of removal?

25 THE WITNESS: Yes.

1 COMMISSIONER DEASON: And you're familiar that we
2 review that every four years.

3 THE WITNESS: I, I know that you review that on a
4 regular basis or you try to.

5 COMMISSIONER DEASON: Okay. Do you know if in
6 determining depreciation rates every four years, which include
7 a component for cost of removal, whether the information we use
8 to make that determination includes the cost of removals
9 associated with named tropical storms and hurricanes or ignores
10 those costs and assumes that those costs will be recovered
11 through the Storm Damage Reserve?

12 THE WITNESS: I am not -- I haven't delved deep
13 enough into any of your past, any of this company's past
14 depreciation studies to know whether you've excluded hurricane,
15 hurricanes from those cost of removal charges.

16 On the other hand -- so I don't know. But to me
17 that, that's an irrelevant -- it's irrelevant.

18 COMMISSIONER DEASON: Okay. And why is that
19 irrelevant?

20 THE WITNESS: Because I will be able to demonstrate
21 in the future that the amounts, the \$1.1 billion, first of all,
22 they don't have an obligation to spend that money. Second of
23 all, even if they did have an obligation, they don't have an
24 obligation to spend that money on cost of removal. And I don't
25 know what they've done with it. But even if they did have an

1 obligation, the amount is overstated as a result of how those
2 estimates were made.

3 And, and, third, I think in, around the Year 2000 I
4 was reading a transcript of something, and there was a
5 Mr. Evanson on behalf of FP&L who pointedly told this
6 Commission that they had a serious, serious problem with excess
7 of depreciation reserves, and I think that one of the reasons
8 is this.

9 Now one thing you didn't know when he told you that
10 was that there was a regulatory liability for this amount
11 because that was first recognized at the end of 2002. So this
12 is all new information that has come about since the last time
13 that I'm aware that you even considered or discussed FPL's
14 depreciation situation and rates.

15 COMMISSIONER DEASON: Okay. Let me ask you a
16 question on a, on a going-forward basis as a matter of
17 principle, good accounting.

18 Would you -- would it be your belief that the cost of
19 removal of assets damaged by a named tropical storm or
20 hurricane, that those costs should be recovered either through
21 depreciation rates which include that as a cost component in
22 looking forward in a depreciation study, or else include that
23 cost in trying to establish an adequate Storm Damage Reserve on
24 a going-forward basis; that it should be one or the other and
25 we should be clear as to whether -- where we're going to look

1 do to account for those anticipated costs? Do you understand
2 the question? I'm just trying to understand on a going-forward
3 basis what's your belief as to how we should account for costs
4 associated with removal of assets damaged in a hurricane.

5 THE WITNESS: I think you should account -- this is
6 my opinion. I think you should account for them, cost of
7 removal as, as being -- you should charge them to the cost of
8 removal reserve.

9 COMMISSIONER DEASON: Now if that reserve that you
10 recommend we charge against, if, if we determine that that
11 reserve is inadequate because it has failed to consider
12 anticipated cost of removal from hurricane damaged assets,
13 would it be your position then you would recommend that we
14 increase depreciation rates to provide an adequate reserve for
15 cost of removal?

16 THE WITNESS: No, I -- you know, the premise of your
17 question is, is the direct opposite of what I believe to be
18 true. I believe that the cost of removal reserve is
19 exorbitantly excessive. So to, to say even if it's possible
20 that in the past you may have excluded retirements relating to
21 storms from the life studies and, ergo, you excluded them from
22 the cost of removal analyses, the reserve for cost of removal
23 is still excessive, highly excessive. And so I, I recommend
24 you don't -- that's not -- I wouldn't -- I don't think that's
25 good logic.

1 COMMISSIONER DEASON: But you would agree there needs
2 to be a mechanism -- cost of removal of assets from hurricane,
3 is that a, a cost of doing business in the state of Florida?

4 THE WITNESS: What's that?

5 COMMISSIONER DEASON: Cost of removal of assets
6 damaged in a hurricane, is that a legitimate cost of doing
7 business within the state of Florida?

8 THE WITNESS: And I'm not proposing that it not be
9 recovered. I'm just saying assign that to the cost -- there is
10 a reserve, a \$1.1 billion reserve set aside that could be used
11 for that.

12 COMMISSIONER DEASON: And my question is which is the
13 preferred alternative: To recover those costs through
14 depreciation rates or to recover those costs through a Storm
15 Damage Reserve?

16 THE WITNESS: Well, if there were no cost of removal
17 reflected in depreciation rates at all and if there were no
18 cost of removal reserve as a result of that, then obviously
19 they should be collected through the Storm Damage Reserve.

20 COMMISSIONER DEASON: Thank you, sir.

21 COMMISSIONER BAEZ: Go ahead, Mr. Wright.

22 MR. WRIGHT: Thank you, Mr. Chairman.

23 BY MR. WRIGHT:

24 Q Just one more question along this line, Mr. Majoros.

25 Do you have -- did you prepare an estimate of how

1 much of FPL's claimed storm costs ought to be charged against
2 the removal reserve?

3 A I did not. And as -- as I stated earlier in my
4 summary, Footnote 2 to my Exhibit MJM-7 updated said that those
5 adjustments should be made. Mr. Davis provided an estimate in
6 his rebuttal testimony of \$12.2 million. However, I think
7 that's an understated estimate, the reason being that it's

8 30 percent of the retirements that he estimates. And when I go
9 back and look at his historical, you know, actual historical
10 activity, the ratio is much higher than that. So I think that
11 the \$12.2 million, Mr. Davis's \$12.2 million cost estimate
12 appears to be understated.

13 Q Are you in a position to tell us by how much so that
14 the Commissioners would have a number they could use if they
15 decided to follow your, your proposal here?

16 A Based upon a look at the actual cost of removal
17 experienced in 2003 to the retirements in 2003 for the primary
18 plant accounts involved in the storm, which were poles -- I
19 could give you a list. I don't have it right here. The ones
20 that were impacted, the accounts impacted. I think that the
21 ratio is somewhere between 78 and over 100 percent. Between 78
22 and 100 percent.

23 Q So would I be correct to understand that you think
24 that the ratio is approximately three times that that Mr. Davis
25 used?

1 A Yes, at least.

2 Q And so for, for working purposes, would Mr. Davis's
3 adjustment, if it were to be adopted, would be something like
4 \$12 million, do you think the number should be something like
5 \$30 to \$40 million?

6 A When I -- if you divide -- I didn't -- I haven't made
7 that actual quantification, but --

8 Q I was just going from the ratio.

9 A Between 78 and 100 percent of \$36.4 million, which is
10 his estimate of retirements.

11 Q Okay. So between about \$28 million and \$36 million?

12 A Yes.

13 Q Okay. Thank you. Toward the end of your primary
14 testimony you talk about some calculations that you performed
15 demonstrating how much the storm restoration costs the company
16 could absorb from earnings before hitting the 10 percent ROE
17 threshold. In doing that calculation you used FPL's earnings
18 surveillance reports?

19 A Yes.

20 MR. WRIGHT: Okay. I'm going to ask Mr. Perry to
21 hand out an exhibit that consists of certified copies of FPL's
22 earnings surveillance reports for 2002, 2003, 2004, and ask
23 that they be marked. The original with the raised seal will be
24 given to the court reporter.

25 COMMISSIONER BAEZ: Show the composite exhibit marked

1 as 43.

2 (Exhibit Number 43 marked for identification.)

3 BY MR. WRIGHT:

4 Q These appear to be the kind of documents you're
5 familiar with, I guess, Mr. Majoros?

6 A Yes.

7 MR. WRIGHT: Okay. Thanks. That's all the questions

8 I have for Mr. Majoros. Thank you, Mr. Chairman.

9 COMMISSIONER BAEZ: Mr. Twomey.

10 MR. TWOMEY: Thank you, Mr. Chairman.

11 CROSS EXAMINATION

12 BY MR. TWOMEY:

13 Q Good morning, sir.

14 A Good morning.

15 Q I'd like to ask you to turn to Page 4 of your
16 additional supplemental testimony, please. Additional
17 supplemental.

18 A Yes.

19 Q Okay. I'd like to read the question starting at Line
20 9 of Page 4 and ask you to read the answer, please.

21 The question is, excuse me, "From the standpoint of
22 proper regulatory accounting, is it appropriate to use the
23 surplus in the depreciation accounts to reduce or eliminate the
24 negative balance in the Storm Damage Reserve?"

25 Would you read the answer, please?

1 A "Yes. FPL's \$1.24 billion book depreciation reserve
2 excess represents, by FPL's own definition, excessive charges
3 that it has collected from its customers. The principles of
4 regulatory accounting enable FPL to apply the excess in
5 depreciation reserves to reduce whatever negative balance in
6 its Storm Damage Reserve that the Commission identifies in this
7 case. I recommend that the Commission consider this option."

8 Q Okay. Do you stand by that answer?

9 A Yes.

10 Q Now the, the -- you say that the \$1.24 billion book
11 depreciation reserve excess represents, by FPL's own
12 definition. That's their number; is that correct?

13 A Yes.

14 Q Do you necessarily agree with the, the size of the
15 number?

16 A No.

17 Q Do you, do you suggest that it could be larger?

18 A I am pretty certain that the excess is much larger
19 than that.

20 Q Okay. Now, so the -- in your opinion, would it be --
21 would you agree with me that the number is not theoretical,
22 that number is not theoretical?

23 A When -- from the company's perspective it is not
24 theoretical. The company quantified it and called it an
25 excess. Not, not a theoretical excess, they called it a

1 reserve excess.

2 Q Okay. And you're saying that whatever -- you believe
3 that it would be consistent with, with GAAP and other
4 principles of regulatory accounting if the Commission in this
5 case found that the appropriate storm restoration costs for
6 this company were \$300 million, so they could take \$300 million
7 and offset it by \$300 million of the depreciation surplus;

8 correct?

9 A That's correct.

10 Q Now if, if that's correct and is consistent with the
11 principles of regulatory accounting, let me ask you this.
12 Would it be appropriate to use a portion of that depreciation
13 surplus to recharge the Storm Reserve Fund, if you know?

14 A That's -- mechanically that could be done, but that's
15 not what I'm recommending here. I'm offsetting one excess
16 against a deficiency.

17 Q Okay. Now the, the -- Commissioner Deason asked
18 you -- no, I'm sorry. In response to Commissioner Davidson's
19 question, I believe, you spoke to the \$1.1 billion of recovery,
20 I mean, cost of removal monies; correct?

21 A Yes.

22 Q That is distinct from the \$1.24 billion you're
23 speaking to.

24 A That is correct.

25 Q And I take it that it's your position that there is

1 that much money in there and that cost of removal, particularly
2 if they're associated with these hurricane seasons and these
3 restoration costs should come from that reserve, not be charged
4 a second time to customers through a surcharge; is that
5 correct?

6 A Yes.

7 MR. TWOMEY: That's all I have. Thank you.

THE WITNESS: Thank you.

9 COMMISSIONER BAEZ: Mr. Butler.

10 MR. BUTLER: Thank you, Mr. Chairman.

11 CROSS EXAMINATION

12 BY MR. BUTLER:

13 Q Good morning, Mr. Majoros.

14 A Good morning, Mr. Butler.

15 Q Before I go into what I had scripted here, I'd like
16 to ask you a question about this Exhibit 43 that was identified
17 by Mr. Wright on the composite of FPL earning surveillance
18 reports. Do you have a copy of that there?

19 A Is this what we're talking about?

20 Q I think so. My eyesight is --

21 A I'm sorry. I didn't write the number.

22 Q Composite Exhibit FPL's Earning Surveillance Reports
23 for 2002, 2003 and 2004.

24 A Yes.

25 Q Okay. And would you agree that starting on Page 50

1 to the end of this is the FPL surveillance report, including
2 the cover letter transmitting it to the Commission for
3 December 2004?

4 A Yes.

5 Q Okay. Now in preparing your Exhibit MJM, excuse me,
6 MJM-7 and MJM-8 you relied on information from the
7 November 2004 surveillance report; correct?

8 A Yes

9 Q Would you agree that the information contained in the
10 December 2004 report would be more appropriate for assessing
11 FPL's earnings in 2004 than the November report was?

12 A Yes.

13 Q Okay. So you wouldn't have any objection to using it
14 for that purpose?

15 A No, sir.

16 Q Okay. In your calculation of what you say is the
17 pretax system expense that FPL could absorb and still produce a
18 10 percent ROE, one of the inputs to that was FPL's pro forma
19 return on common equity, wasn't it?

20 A Yes.

21 Q Okay. Do you know what adjustments are made to get
22 from the FPSC adjusted ROE to the pro forma ROE in the
23 surveillance reports?

24 A Several adjustments are made.

25 Q What are your understanding of those adjustments?

1 A They're listed in the surveillance report. I -- you
2 know, we can look at them. I'm not intimately familiar with
3 all of them.

4 Q Would you agree that weather normalization is an
5 adjustment?

6 A Yes, I believe it is.

7 Q Okay. So in using the pro forma ROE, what you're
8 looking at is what FPL would have earned if it had had normal
9 weather conditions instead of what it actually earned in the
10 year in question; correct?

11 A I guess so, yes.

12 Q And tell me what, if any, other adjustments besides
13 weather normalization you're aware of that were made to the
14 December 2004 pro forma ROE.

15 A Well, I think several adjustments were made to rate
16 base as well as earnings, and both of those impact ROE.
17 They're all in there. Is there any particular one you would
18 like me to focus on?

19 Q I'd just be interested to know what adjustments you
20 understood were made.

21 A The ones that are in the surveillance report. I
22 didn't identify and I didn't review all of the adjustments.

23 Q Okay. So are you aware -- can you point me to
24 anything showing an adjustment other than for weather
25 normalization in the December 2004 surveillance report?

1 A Schedule 2, Page 1 of 3, shows the average rate of
2 return rate base. The second line is a series of
3 jurisdictional per books, and then FPSC adjustment, see
4 Schedule 2 Page 3 of 3 and Schedule 2 Page 3B of 3. That's
5 where I guess the rate base adjustments are.

6 Q That's the FPSC level adjustment, isn't it? If you
7 look on down that page, you'll see the pro forma adjustments.

8 MR. MCGLOTHLIN: Mr. Butler, I'm not clear what
9 you're referring to. Would you give us a --

10 MR. BUTLER: I'm sorry. Yeah. We are referring to,
11 it's Exhibit 43, and Mr. Majoros and I are on Page 52 of 73.

12 COMMISSIONER BAEZ: Is that 52 or 32?

13 MR. BUTLER: 52. Schedule 2, Page 1 of 3 of the
14 December 2004.

15 MR. MCGLOTHLIN: Thank you. Now could I hear the
16 question again?

17 BY MR. WRIGHT:

18 Q Mr. Majoros, you were referencing some FPSC
19 adjustments in sort of the top half of this document, and I was
20 pointing you instead to there's a heading that says "Pro Forma
21 Adjustments." And would you agree that the two shown on, two
22 categories of adjustments shown on this page, special deferred
23 fuel adjustment, total pro forma adjustments, have zeros across
24 the, across the columns for those entries?

25 A Yes, I agree with that. And the note also says, "The

1 pro forma adjustments are not necessarily all of the pro forma
2 adjustments that would be made in a base rate filing."

3 Q Okay. Would you turn --

4 A So then we go to the next page.

5 Q I'm sorry. Would you turn to Page 54?

6 A 54? I'm sorry. I'm sorry. 54 of November?

7 Q No. Page 54 of 73. I don't think November is in

8 this exhibit.

9 A Okay.

10 Q I think this exhibit consists of the December 2002,
11 2003 and 2004 surveillance reports. Are you there, Page 54?

12 A Yes.

13 Q Okay. Now this shows a weather normalization
14 adjustment, doesn't it.

15 A Yes.

16 Q And then you'll see total pro forma adjustments.

17 A Yes.

18 Q And, in fact, the totals are the same as the weather
19 normalization amounts; right?

20 A Yes.

21 Q So would that lead you to conclude that the only
22 normalization, or, I'm sorry, the only pro forma adjustment for
23 this particular schedule is a weather normalization adjustment?

24 A Yes.

25 Q Okay. Thank you. One other question for you,

1 please, about your Exhibit MJM-7. Do you have a copy of that
2 available to you?

3 A I have an Exhibit MJM-7 and an Exhibit MJM-7 update,
4 so.

5 Q Fair enough. Yes. The updated one.

6 A Okay. Yes, I'm there.

7 Q Okay. Now you propose what you call disallowed
8 expenses totalling \$38.62 million; right?

9 A Yes.

10 Q Okay. And your point there is that FPL should absorb
11 those as a normal operating cost in the sort of base O&M
12 expenses rather than recovering them through the storm
13 surcharge; correct?

14 A Correct.

15 Q Okay. So if FPL were to have done that in 2004, that
16 would have reduced its ROE compared to what it has reported in
17 the surveillance reports, wouldn't it?

18 A Yes.

19 Q Okay. So, in fact, the amount available for reducing
20 the ROE down to 10 percent would be less by that amount,
21 wouldn't it?

22 A Roughly, yes.

23 Q Okay. Thank you.

24 Mr. Majoros, other than in the Progress Energy
25 Florida storm docket and this docket, have you ever testified

1 on the subject of accounting for storm costs?

2 A No.

3 Q Do you have any personal experience in accounting for
4 the cost of storm recovery?

5 A No.

6 Q Okay. Do you have any personal experience in
7 budgeting for the cost of maintaining or repairing transmission
8 and distribution systems?

9 A No.

10 Q Okay. Have you ever been responsible for living
11 within a budget for the repair or maintenance of a transmission
12 and distribution system?

13 A No.

14 Q Okay. Have you ever been personally involved in
15 managing storm restoration activities?

16 A No.

17 Q Switch to what I think is going to be a yes answer.
18 Are you familiar with FPL's 1993 storm study, which was
19 attached as Exhibit KMD-3 to Mr. Davis's rebuttal testimony?

20 A Yes.

21 Q Okay. Do you have a copy of that available with you?

22 A Yes, I do.

23 Q Would you please turn to Attachment 2 in the study,
24 and then Page 1 of Attachment 2.

25 COMMISSIONER DEASON: Mr. Butler, what page is that

1 of the exhibit?

2 MR. BUTLER: Oh, gosh. Hold on. You caught me out,
3 Mr. McGlothlin.

4 It would be Page 22 of 51.

5 COMMISSIONER DEASON: Thank you.

6 BY MR. WRIGHT:

7 Q Do you have that, Mr. Majoros?

8 A Yes.

9 Q Would you agree that this provides illustrative
10 accounting entries for what is referred to as the actual
11 restoration cost approach?

12 A Yes.

13 Q And it's your understanding that FPL's storm study
14 recommended use of the actual restoration cost approach?

15 A Yes.

16 Q Okay. Are you aware from your review of FPL's filing
17 in this docket of any deviation from the accounting treatment
18 that is outlined on Page 1 of Attachment 2?

19 A No.

20 Q And would you agree that the Commission found FPL's
21 storm study to be adequate in Order Number PSC-95-0264-FOF-EI
22 dated February 27, 1995?

23 A Yes. But as you know, my opinion is they found it
24 adequate to set the level of the accrual to the reserve.

25 Q Okay. But does anything in that order -- I'm going

1 to call it Order 95-0264. Is that okay? Is there anything in
2 Order 95-0264 that disputes FPL's recommendation to use the
3 actual cost, excuse me, actual restoration cost approach?

4 A And this is, this is the February 27th order?

5 Q Yes. The February 27, 1995, order. Right.

6 A Yes. I don't -- first of all, I'm not an attorney.

7 I don't think that this order specifically precludes that

8 accounting, but, on the other hand, it certainly doesn't

9 endorse it. At Page 5 --

10 Q Excuse me, Mr. Majoros. What I asked you is whether
11 there is anything in the order you're aware of that disputes
12 FPL's recommendation to use the actual restoration cost
13 approach. Are you aware of anything in the order that disputes
14 their use of that approach?

15 A In that case or this case?

16 Q In the order. Is there anything in the order that
17 says, going forward, FPL, we disagree with your recommendation
18 to use the actual restoration cost approach?

19 A Well, you know, that's what I was trying to explain
20 before. I'm not saying -- disputes is, is a, a judgment,
21 judgmental concept. But when the Commission said at Page 5,
22 "We are considering the appropriateness of opening a rulemaking
23 proceeding to establish uniform guidelines for determining when
24 the Storm Damage Reserve should be charged and what costs
25 should be charged to it," and that follows just a few

1 paragraphs after its explanation of the replacement cost
2 approach, I don't know if that is a dispute, but it's certainly
3 not an endorsement.

4 Q We'll get to that in a minute. But other than that,
5 anything else in the order you're aware of that disputes the
6 use of the actual cost recovery approach?

7 A No.

8 Q Okay. Is there anything in the order that directs
9 FPL to use something other than the actual restoration cost
10 approach?

11 A No.

12 Q Are you aware of any Commission order since
13 February 1995 that has directed FPL to account for storm costs
14 in any manner different than the actual restoration cost
15 approach?

16 A No.

17 Q You mentioned the paragraph about the possibility of
18 conducting rulemaking. Do you know whether that rulemaking
19 ever occurred?

20 A It's my understanding that it did not.

21 Q Okay. I think in your deposition you agreed that
22 rulemaking is by its nature prospective in application?

23 A Generally, yes.

24 Q So would you agree that if the Commission were to
25 initiate rulemaking today on storm cost accounting, any rule

1 resulting from the rulemaking would apply only to accounting
2 for storm costs after the rule became effective?

3 A Well, that depends on what the Commission decides.

4 Q Well, if it's going to apply the rule prospectively
5 in application, that would be the result, wouldn't it?

6 A Yes. If that's what the decision was, then that
7 would be true.

8 Q Okay. Are you aware of any generally accepted
9 accounting principles that would require FPL to account for
10 storm costs in any manner different than the actual restoration
11 cost approach?

12 A Just to get our concepts straight, when you say
13 generally accepted accounting principles, what are you talking
14 about?

15 Q GAAP, sort of the --

16 A Financial accounting standards that emanate from the
17 Financial Accounting Standards Board, is that what you mean?

18 Q Yes.

19 A I'm not aware of any that precluded and I'm not
20 specifically aware of any that address the issue.

21 Q Let me ask you about the FPL 2002 rate stipulation
22 that was approved by the Commission in Order Number
23 PSC-02-0501-AS-EI. Are you familiar with that, with that
24 document?

25 A I have seen it. I'm not sure I even have a copy of

1 .t here. I'm not intimately familiar with it.

2 Q Well, let me just ask you this. You say you have
3 seen it; right?

4 A Yes.

5 Q When did you first see it?

6 A I don't recall. I'm sure it was before I prepared my
7 direct testimony in this case.

8 COMMISSIONER BAEZ: Mr., Mr. Butler, are you
9 referring to the stipulation and settlement?

10 MR. BUTLER: That's right, yes.

11 COMMISSIONER BAEZ: I think it's part of
12 Mr. Dewhurst's -- it's MPD-1.

13 MR. WRIGHT: You're right.

14 COMMISSIONER BAEZ: Mr. Majoros, if you have it
15 there.

16 MR. BUTLER: You're right. I was so advised Thank
17 you, Mr. Chairman.

18 THE WITNESS: MPD-1?

19 COMMISSIONER BAEZ: It's Exhibit 1 to Mr. Dewhurst's
20 testimony, MPD-1.

21 MR. BUTLER: We'll provide him a copy of
22 Mr. Dewhurst's testimony. Thank you, Mr. Chairman.

23 BY MR. WRIGHT:

24 Q Mr. Majoros, did you have any involvement in drafting
25 the stipulation that was approved in this order?

1 MR. MCGLOTHLIN: I'm going to object to this line of
2 questions as beyond the scope of the witness's testimony. He's
3 testifying as to the account he believes should be applied to
4 the storm costs. It's unrelated to the stipulation.

5 COMMISSIONER BAEZ: Mr. Butler, can you point out in,
6 in Mr. Majoros's testimony where he either comments or
7 testifies on the settlement?

8 MR. BUTLER: I will. Hold on just a second, please.

9 On Page 24 of Mr. Majoros's testimony he has a series
10 of questions and answers that discuss the 2002 settlement and
11 the consequences of that to what he considers to be the
12 appropriate amount that should be allowed for recovery in this
13 docket.

14 COMMISSIONER BAEZ: Mr. McGlothlin, I see the
15 reference, and it seems like he does have some testimony in
16 terms of the 10 percent.

17 MR. MCGLOTHLIN: He says he is advised that OPC's
18 position is that the stipulation requires a 10 percent. That
19 was a given for his purposes. He, he took that as a given and
20 then applied the accounting principles.

21 COMMISSIONER BAEZ: Well, the only problem that I see
22 in that, Mr. McGlothlin, is that he adopted, he adopted your
23 position, I think he said.

24 MR. BUTLER: Let me, let me ask him a question, Mr.
25 Chairman, to see if I can clarify that somehow.

1 COMMISSIONER BAEZ: If you can, if you can shortcut
2 .t. I mean, I understand Mr. McGlothlin's point. We don't
3 want to get too far abroad of it, but.

4 BY MR. BUTLER:

5 Q Mr. Majoros, would you agree that you have no
6 independent views to offer this Commission on the effect of the
7 2002 FPL rate settlement beyond what you've been told by Public
8 Counsel and have repeated in your testimony?

9 A Yes.

10 Q Okay. I'll accept that, and I don't need to go
11 through this set of questions. Thank you.

12 Mr. Majoros, do you believe that any of FPL's 2004
13 storm costs were imprudently incurred?

14 A No.

15 Q Do you have any reason to dispute the calculation of
16 \$38.2 million in base revenue loss that is shown in Mr. Davis's
17 Exhibit KMD-5?

18 A No. But I might add, as I said when you deposed me,
19 that that doesn't tell the entire story there. There are fuel
20 savings that go along with that number.

21 Q And I believe you indicated at your deposition you
22 don't know where and how the fuel cost savings and fuel cost
23 related revenues are accounted for with respect to base rates,
24 do you?

25 A Well, I think I said they're accounted for in a fuel

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10 A Yes.

11 Q Okay. And would you agree that if as a result of
12 storms in a particular year a utility's expenses went down by

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16 A Yes.

17 Q You've proposed an adjustment of \$5.26 million for
18 vehicle expenses on Exhibit MJM-7. In Mr. Davis's rebuttal
19 testimony he states that, quote, on an annual basis

20

21 charged to capital projects. Assuming the same split is
22 applied to the vehicle costs charged to the Storm Damage
23 Reserve, that would yield approximately \$2.4 million.

24 Do you have any basis to disagree with this

25 calculation by Mr. Davis?

1 A No.

2 Q And would you agree that if his calculation is
3 correct, then the amount of the vehicle expense adjustment to
4 O&M costs you've shown would be reduced by \$2.4 million?

5 A Yes.

6 Q You've proposed an adjustment of \$1.38 million for
7 salt spray and vegetation studies on Exhibit MJM-7. Would you

8 agree that if FPL provided sufficient detail to show that those
9 studies were performed to address problems related to the 2004
10 storms, then your adjustment would not be appropriate and the
11 cost of the study should be chargeable to the storm reserve?

12 A Yes.

13 Q Okay. Would you agree that the goal during the
14 hurricane restoration process is to get service restored as
15 quickly and safely as possible?

16 A Yes.

17 Q Okay. And would you agree that this might mean that
18 a utility would put up poles and lines and not fix everything
19 that was on the poles and lines in order to move along and get
20 additional poles and lines in place to restore as much service
21 as possible as quickly as possible?

22 A That might be the case.

23 Q Okay. As a result of that process, would you agree
24 that there would be some facilities or equipment that was
25 damaged by the hurricanes that would still have to require

1 final repairs after service was restored?

2 A Again, that might be the case.

3 Q And you don't dispute that FPL has had to go out
4 after service was restored and make sure all of its equipment
5 is working properly, do you?

6 A No.

7 Q Do you have any factual basis to conclude that none
8 of that sort of work would have been required on FPL's system
9 after December 31, 2004?

10 A I guess, you know, I believe it, it was required, but
11 I also believe a lot of that was probably anticipated in normal
12 operations.

13 Q You believe that FPL's normal operations anticipate
14 having to go back and make sort of follow-on repairs to
15 extraordinary hurricane loss damages to the system?

16 A I believe that FPL has a pole inspection program and
17 outside plant personnel whose job it is to maintain outside
18 plant.

19 Q Have you reviewed FPL's budgets for, I guess it would
20 be for 2005?

21 A No, I haven't.

22 Q Okay. So other than just suspecting that may be the
23 case, you don't have any factual basis to know that FPL has
24 budgeted for those sorts of follow-on activities, do you?

25 A Well, I'm fairly convinced that they've budgeted for

1 maintaining outside plant.

2 Q For ordinary maintenance of outside plant; correct?

3 A But I told you earlier that I don't have any
4 knowledge of specifically how FPL develops those budgets, or I
5 thought I told you that.

6 Q Okay. Mr. Majoros, isn't it true that you propose --
7 change subjects here. Isn't it true that you propose to

8 include in your original testimony a position that the cost of
9 removal reserve in the accumulated depreciation should be used
10 to absorb a portion of FPL's storm damage costs, but the Office
11 of Public Counsel told you to take that position out of your
12 testimony?

13 A Yes. Yes. That's correct.

14 Q Okay. But then subsequently you filed additional
15 supplemental testimony where you're proposing to use a
16 depreciation reserve surplus to absorb not only a portion of
17 but all of FPL's Storm Damage Reserve deficit; correct?

18 A Yes.

19 Q And you proposed to do this as a one-time lump sum
20 adjustment; is that right?

21 A Yes.

22 Q Prior to filing your additional supplemental
23 testimony, did you conduct any review of the Commission's rules
24 and orders concerning depreciation practices to confirm whether
25 your proposal was consistent with those rules or orders?

1 A No. And let me -- I would like to clarify about the
2 one-time. I recommended that the Commission consider this
3 option. So when you say, when you asked me if I'm proposing a
4 one-time lump sum adjustment, at this point I am. But I
5 recognize that it could be spread over some other period.

6 Q Okay. Did you conduct any review of FERC rules or
7 orders prior to filing your additional supplemental testimony?

8 A No, I didn't.

9 Q Did you conduct any review of SEC guidance on
10 depreciation for financial reporting purposes before filing
11 your additional supplemental testimony?

12 A No.

13 Q Are you aware of any instance in which the Commission
14 has approved a one-time lump sum adjustment of the sort you
15 propose in your additional, excuse me, your additional
16 supplemental testimony?

17 A I'm aware that the Commission has in the past on many
18 occasions quantified the amount of a theoretical, of an
19 accumulated reserve deficiency and separated that from
20 accumulated depreciation and allowed an accelerated
21 amortization of that amount.

22 Q I don't think you answered my question.

23 Are you aware of any instance in which the Commission
24 has previously approved a one-time lump sum adjustment of the
25 sort you've proposed in your additional supplemental testimony?

1 A Well, I'm not sure the Commission has been confronted
2 specifically with the recommendation that I'm making. So I
3 can't say that I'm aware of any instance where the Commission
4 specifically approved such a recommendation.

5 Q Is your answer, no, with explanation?

6 A Yes.

7 Q Okay. Would you agree that FPL's calculated

8 depreciation reserve surplus is predominantly in the nuclear
9 function?

10 A Yes.

11 Q And would you agree that the costs accumulated in the
12 Storm Damage Reserve predominantly relate to the transmission
13 and distribution function?

14 A Yes.

15 Q And, further, would you agree that the majority of
16 the costs in the Storm Damage Reserve are O&M expenses rather
17 than capital?

18 A Yes. Based on the company's estimates, that appears
19 to be correct, yes.

20 Q Okay. So isn't it true that your proposal would
21 offset depreciation reserves that are predominantly in the
22 nuclear function against storm costs that are primarily in the
23 T&D function?

24 A The source of the numbers are as you've described.
25 But as I said earlier, the Commission has in the past separated

1 reserve imbalances from accumulated depreciation and allowed
2 accelerated amortizations of those amounts to be charged to
3 ratepayers. Trying to earmark this money is, is, is, in my
4 opinion, sort of a red herring in this whole thing. The fact
5 is that the company has quantified a 1.2 -- 24 -- \$1.24 billion
6 excess in accumulated depreciation regardless of where that is.
7 And that represents money that has been charged to and
8 ~~collected from ratepayers, and it's over and above what the~~
9 company believes is necessary. And, in fact, based upon that
10 transcript I read, about three years ago Mr. Evanson on behalf
11 of the company was discussing a distorted rate base as a result
12 of excessive depreciation that was charged.

13 Another thing that I said this morning is that the
14 depreciation study proceeding isn't over yet. I hadn't said
15 that. But I did say that in my opinion the \$1.24 billion
16 excess that your client has calculated is vastly understated.
17 And it is understated because your client has understated the
18 amount of the excess relating to transmission and distribution.
19 So there's more. And trying to -- the game you're trying to
20 play here doesn't fly as far as I'm concerned.

21 Q Putting aside the editorial though, you would agree
22 that your proposal would offset depreciation reserves that are
23 predominantly in the nuclear function against storm costs that
24 are primarily in the T&D function, wouldn't you?

25 A Well, it would offset accumulated depreciation

1 excesses against Storm Damage Reserve deficiencies, both of
2 which are rate base items.

3 Q I'm sorry. Most of which are rate base items?

4 A That's correct.

5 Q I thought you just agreed a moment ago that the
6 majority of the costs in the Storm Damage Reserve are O&M
7 expenses rather than rate base items?

A If you recall, FP&L's first application to this
9 Commission in this regard asked that its storm damage costs be
10 established as a regulatory asset. The Commission decided that
11 treatment was not necessary, you could just go ahead and charge
12 the costs to the reserve, which was already reflected as a
13 regulatory liability. And by virtue -- if you were deficient
14 in that, those charges would create a negative regulatory
15 liability, which was the same as, as I'm paraphrasing the
16 Commission's decision, a regulatory asset. So that deficiency
17 is, as we speak, in addition to rate base.

18 Q But you would agree it's comprised predominantly of
19 costs that are of an O&M nature rather than capital costs,
20 would you not?

21 A Well, I mean, that's irrelevant. Once it -- what
22 we're talking about now are two rate base items, a rate base
23 addition and a rate -- which is the storm damage deficiency,
24 and a rate base reduction, which is accumulated depreciation.
25 What I'm recommending is that you just merge the two and it's

1 gone.

2 Q Okay. Do you know the function to which the
3 regulatory asset that you are describing is allocated?

4 A Pardon me?

5 Q Do you know the function or functions to which the
6 regulatory asset you're describing is allocated?

7 A No.

8 Q Okay. In preparing your additional supplemental
9 testimony, you've examined the depreciation study that FPL
10 recently filed; correct?

11 A I went through it one time. And I reviewed it, as I
12 told you, I think it took about four to six hours because it is
13 six volumes. But I am not intimately familiar with everything
14 that's included in that study.

15 Q Have you spent any more time reviewing it since we
16 had our deposition?

17 A No, sir.

18 Q Okay. Well, based on the review you have done -- so
19 at this point you're saying you've spent four to six hours
20 reviewing FPL's depreciation study in total?

21 A Four to six hours.

22 Q Right. Four dash six?

23 A That's correct.

24 Q Based on the review you've performed, would you agree
25 that FPL applied the remaining life technique in preparing that

1 depreciation study?

2 A Yes, I would. And certainly it was not 426 hours.

3 Q That would have kept you up late at night.

4 (Laughter.)

5 Do you have any reason to believe that FPL applied
6 the remaining life technique improperly in preparing the
7 depreciation study?

8 A No.

9 Q Do you have any reason to believe that FPL's
10 depreciation study does not comply with the requirements of
11 GAAP?

12 A No. You know, that's a, that's -- that question --
13 first of all, GAAP doesn't control ratemaking. But let me, let
14 me -- you asked me that question and you asked me before and it
15 just struck me as you asked me again, here's -- there is a big
16 difference today which has occurred since the last time that
17 this Commission discussed FP&L's depreciation rates, and, and
18 it relates to SFAS Number 143, which is GAAP, accounting for
19 long-term assets.

20 For an unregulated -- Mr. Deason and I were talking
21 about the inclusion of net salvage ratios in depreciation rates
22 earlier today. And I guess what I was saying was that they're
23 in there and that they're excessive, and that's what resulted
24 in this \$1.1 billion regulatory liability.

25 But for an unregulated company, SFAS 143 does not

1 allow the inclusion of a negative net salvage ratio in a
2 depreciation rate, period.

3 What SFAS, which is GAAP, what SFAS 143 does, it says
4 these are all, you know, hypothetical numbers. And the
5 magnitude of them are demonstrated by the \$1.1 billion. Nobody
6 knew before, before this how much money was involved in, in
7 using negative net salvage and depreciation rates.

8 ~~143 highlighted this amount. And it just -- it came out -- the~~
9 first year it was ever implemented, I think, was at the end of
10 2002 or the beginning of 2003.

11 But what SFA -- what the public accounting profession
12 requires is if you're going to try and charge operating,
13 operating income today for some cost you speculate may be
14 incurred in the future, you have to go to the attorneys and
15 establish that you have a legal obligation to spend that money.
16 And if you do, then that, the net present value of that, not
17 the future inflated value, but the net present value of that
18 becomes a part of the cost of the asset and is depreciated. So
19 the depreciation rate under GAAP is a rate which does not
20 include net salvage in the calculation of the rate. Now
21 SFAS -- so that is GAAP and that is different than FPL's
22 current depreciation rates.

23 Q But SFAS allows you to, allows FPL to do what it has
24 done in its depreciation study, does it not?

25 A SFAS 143 contains an exception for regulated

1 utilities and allows them to include negative net salvage
2 ratios in depreciation rates, continue to do that. On the
3 other hand, the quid pro quo for that exception is that you
4 must identify -- if you don't have a legal liability to spend
5 that money, you must identify the amount that you have already
6 charged so far, plus what you are collecting on a going-forward
7 basis as a regulatory liability, that is an amount owed to
8 ratepayers, and that's the \$1.1 billion.

9 Q Do you have any reason to believe that FPL has
10 performed its depreciation study or reflected in MFRs in its
11 rate case filing or otherwise inconsistently with what you just
12 described regarding the asset retirement obligations?

13 A No. But your question was, did they, were those
14 depreciation rates developed in accordance with GAAP, and in
15 general terms the answer is no.

16 Q But you would agree that it is, it has been done
17 consistently with the exception contained in SFAS 143, would
18 you not?

19 A Well, that's just an exception. SFAS 143 doesn't say
20 include net salvage ratios in the rates. It says, if you do,
21 you must report these amounts as regulatory liabilities.

22 Q I'm asking you whether to the best of your knowledge
23 FPL has reported the obligations consistent with the exception
24 in SFAS 143?

25 A And you're saying it incorrectly. There is an

1 exception. There is an exception in SFAS 143 which requires
2 them -- if, if FPL does what it is doing, it must report a
3 regulatory liability.

4 Q I'm asking you whether it's your understanding that
5 FPL has properly reported consistent with that exception?

6 A It has properly reported the regulatory liability. I
7 agree with that.

8 Q Okay. Do you have any reason to believe that FPL's
9 depreciation study does not comply with any FPSC rules for
10 depreciation studies?

11 A No.

12 Q Would you agree that using the remaining life
13 depreciation technique, any depreciation reserve surplus that
14 has been calculated currently should be eliminated over the
15 remaining lives of the affected assets via reduced depreciation
16 rates?

17 A That is the intent and the reason for using the
18 remaining life method. Correct.

19 Q And do you have any reason to believe that that's not
20 what FPL has done in its recent depreciation study?

21 A I agreed earlier that FPL has used the remaining life
22 technique.

23 Q And its study has been performed consistently with
24 that technique?

25 A Yes.

1 Q Have you reviewed Mr. Davis's Exhibit KMD-6?

2 A Is that the discounted cash flow study?

3 Q It is.

4 A I've, I've looked at it.

5 Q Do you have any reason to disagree with the
6 calculations that are reflected in it?

7 A Absolutely. I disagree with everything about that
8 exhibit.

9 Q Okay. Tell me -- okay. Tell me -- and understand
10 the question. I'm simply asking you the calculations that are
11 performed, do you disagree mathematically with any of the
12 calculations that are shown in his --

13 A I haven't checked the calculations mathematically,
14 no.

15 Q So you don't have an opinion one way or the other on
16 whether the calculations are done correctly?

17 A The premise of the exhibit is incorrect in my
18 opinion, and it is -- even if the premise were correct, it is
19 misleading, and so I disagree with everything about it.

20 Q But you don't know whether it's been performed
21 mathematically correctly because you haven't checked?

22 A I would be willing to accept, subject to check, that
23 Mr. Davis, Mr. Davis's arithmetic is correct.

24 Q And would you agree that if his arithmetic is
25 correct, what it shows on Page 1 is that at any customer

1 discount rate below approximately 15 percent, the net present
2 value of your proposal to make the one-time lump sum offset of
3 depreciation surplus reserve against Storm Damage Reserve
4 deficiency will have a net present value for customers that's
5 higher than what FPL proposes?

6 MR. MCGLOTHLIN: I'm going to object because the
7 witness stated earlier that while he would accept arithmetic
8 ~~subject to check, he disagreed with the premise. Mr. Butler~~
9 has now changed from arithmetic to premise.

10 COMMISSIONER BAEZ: I'll sustain.

11 MR. BUTLER: Well, I'm simply asking him as a
12 question whether he agrees with it. I mean, he can disagree
13 with it.

14 COMMISSIONER BAEZ: You can ask him to read the
15 number, but --

16 MR. BUTLER: So I can't ask him whether he agrees
17 with what it shows?

18 COMMISSIONER BAEZ: Well, I think, I think if he
19 originally disagreed the premise, you should probably know the
20 answer to that.

21 BY MR. BUTLER:

22 Q Well, Mr. Majoros, would you agree that Page 1 of
23 Mr. Davis's document KMD-6 or Exhibit KMD-6 shows or has a
24 calculation showing that at in a customer discount rate less
25 than approximately 15 percent the cumulative net present value

1 to customers would be lower under FPL's proposed storm
2 surcharge than under your proposal to offset that storm
3 surcharge with a one-time lump sum transfer from the
4 depreciation reserve surplus?

5 MR. MCGLOTHLIN: Same objection.

6 COMMISSIONER BAEZ: Sustained again. Mr. Butler, I
7 think what you're going to have to ask him is to look, look at
8 the numbers and ask him if that is higher than one number or
9 another. I think -- see, the problem is you're, how you're
10 presenting it.

11 MR. BUTLER: Okay.

12 BY MR. BUTLER:

13 Q Mr. Majoros, would you look at Page 1 of KMD-6.

14 A Could I have a moment? I'm having a hard time
15 finding that exhibit in my notebook here.

16 Q It should be attached at the back of the supplemental
17 rebuttal testimony of Mr. Davis.

18 Do you have it?

19 A Yes, I have it. I'm just -- oh, I know where it is.

20 COMMISSIONER BAEZ: Mr. Butler, while we're letting,
21 while we're letting Mr. Majoros locate it, we want to break
22 for, recess for five minutes. Okay?

23 MR. BUTLER: Okay. That's fine. Thank you.

24 (Recess taken.)

25 COMMISSIONER BAEZ: We'll go back on the record.

1 Mr. Majoros, did you get a chance to locate
2 everything that, that you needed?

3 THE WITNESS: I have copies. I haven't located.

4 COMMISSIONER BAEZ: I hesitate to say that. You've
5 got a stack a foot high there. Mr. Butler, go ahead with your
6 questioning.

7 MR. BUTLER: Thank you.

8 BY MR. BUTLER:

9 Q I'm going to save you, me and the Commission some
10 wear and tear here though and we'll just let Exhibit
11 KMD-6 speak for itself.

12 Let me ask you, Mr. Majoros, just a -- I don't have
13 very many more questions. I'd like to ask you though about
14 some positions that your client, Office of Public Counsel, has
15 expressed in the prehearing order. Do you have a copy of the
16 prehearing order available?

17 A If you have one --

18 Q We'll bring you one.

19 A I'm not having much success rooting through piles of
20 paper today. I apologize.

21 Q Okay. Do you have a copy of it now?

22 A Yes.

23 Q Okay. Would you turn to Page 26 of the order and
24 look at Issue 10. And do you have that?

25 A Yes.

1 Q Okay. And this issue is, "Has FPL properly
2 determined the cost of call center activities that should be
3 charged to the storm reserve? If not, what adjustments should
4 be made?"

5 There isn't any Office of Public Counsel position
6 shown or it's shown as no position at this time.

7 The FPL position, I'm just going to read it to you,

8 say, "Yes. FPL has charged incremental costs of the call
9 center operation to the Storm Damage Reserve consistent with
10 the methodology in the study filed on October 1, 1993, in
11 Docket 930405-EI and approved by the Commission in Order Number
12 PSC-95-0264-FOF-EI issued February 27, 1995. No adjustment is
13 necessary."

14 Do you have any evidence that FPL is doing anything
15 other than charging incremental storm, incremental call center
16 costs?

17 A No. No.

18 Q And let me ask you on Issue 12, this concerns
19 uncollectible expenses. The issue is, "Has uncollectible
20 expense been appropriately charged to the storm reserve? If
21 not, what adjustment should be made?"

22 And here there is an Office of Public Counsel
23 position. I would ask you to read that position. You don't
24 need to read it out loud. Just read it to yourself.

25 You'll see the last sentence there, it says, "It is

1 inappropriate to charge any portion of uncollectible expense to
2 the Storm Damage Reserve." Do you see that?

3 A Yes.

4 Q Do you have any evidence that FPL is charging any
5 portion of uncollectible expense to the Storm Damage Reserve?

6 A No, I do not.

7 Q Okay. And if you'll turn to Page 29, Issue 14, which
8 reads, "Has FPL appropriately quantified the costs of materials
9 and supplies used during storm restoration that should be
10 charged to the storm reserve? If not, what adjustment should
11 be made?"

12 And I'll just read because it's pretty short the OPC
13 position. "FPL should charge only the costs of the materials
14 and supplies used during restoration activities to the storm
15 reserve. It should not charge the cost of replenishing
16 supplies and inventories to the reserve."

17 Do you have any evidence that FPL is doing anything
18 inconsistent with the OPC position stated here?

19 A No, I do not.

20 MR. BUTLER: Thank you, Mr. Majoros. Those are all
21 the questions that I have.

22 THE WITNESS: Thank you.

23 COMMISSIONER BAEZ: Staff.

24 MS. FLEMING: We have no questions.

25 COMMISSIONER BAEZ: Commissioners, any questions for

1 Mr. Majoros? Okay. Exhibits.

2 MR. MCGLOTHLIN: I may have a few on redirect.

3 COMMISSIONER BAEZ: Oh, I'm sorry. Mr. McGlothlin,
4 go ahead and redirect.

5 REDIRECT EXAMINATION

6 BY MR. MCGLOTHLIN:

7 Q Mr. Majoros, during questioning Mr. Butler asked you

8 to agree that Mr. Davis's calculation of lost revenues, about
9 \$38 million of it, as I recall, is approximately the same value
10 as the O&M adjustments that you recommend be made in your
11 testimony.

12 Do you regard that lost figure, lost revenue figure
13 as somehow offsetting your adjustment?

14 A I don't think so. And when he asked me about it, I
15 didn't think they were specific, they were related. The
16 majority of my \$30 million adjustment is labor, and so the
17 answer is no.

18 Q The items that you've identified as the basis of
19 adjustments were in the category of costs incurred for
20 restoration activities; is that correct?

21 A Yes.

22 Q Is lost revenues a cost incurred to restore service?

23 A No.

24 Q Mr. Butler discussed with you that the depreciation
25 reserve excess which you address in your most recent testimony,

1 the source of that is largely the nuclear investment; whereas,
2 the storm damage deficiency relates primarily to transmission
3 and distribution assets. Do you recall that?

4 A Yes.

5 Q Do you think that difference presents a reason why
6 the Commission should not consider the offset that you've
7 described?

8 A No.

9 Q Would you explain why that's not a, not an obstacle
10 to your proposal?

11 A Well, first of all, let's make sure everybody
12 understands that the excess that we, that FPL has quantified
13 represents an amount of money that has been charged to and
14 collected from ratepayers. There's no, no debate about that.
15 And it's excessive; that's why they call it an excess.

16 So regardless of Mr. Butler trying to tag these to
17 different functions, the simple facts of life are that that is
18 money that has been charged to ratepayers for depreciation over
19 and above what should have been charged. And it's perfectly
20 acceptable.

21 Now it happens to be manifested right now in
22 accumulated depreciation, which is a deduction from rate base.
23 The Storm Damage Reserve deficiency, as I explained earlier, as
24 a result of your decision is a rate base addition.

25 All I'm recommending is a debit and credit. And you

1 will have -- use some of the excess that has been paid by
2 ratepayers to cover the storm damage costs, all of them,
3 whatever you decide is the deficiency in this case.

4 So I don't think it's precluded by anything. The
5 fact that the excess that FPL calculated relates to nuclear
6 plant is irrelevant because I know and I'm going to demonstrate
7 there's a bigger excess that relates to transmission and
8 distribution. It's one big excess that relates to all of FPL's
9 plant. And Mr. Evanson recognized a couple of years ago that
10 rate base is distorted as a result of all that excess
11 depreciation.

12 So you can consider this an attempt, beyond what I'm
13 saying, just take care of storm damages, the first step in
14 curing the, the rate base problem, the distorted rate base
15 problem.

16 Q Commissioner Deason explored with you the subject of
17 how cost of removal occasioned by a severe hurricane should be
18 accounted for on a going-forward basis, and I wanted to pose
19 this question to perhaps take that to the next step.

20 Assume you've got two poles and one pole is blown
21 over during a hurricane and is removed in that situation. The
22 other pole is in place with 30 years and is retired at the end
23 of its useful life. Does the reason that causes the need for
24 removal -- does the manner in which the cost of removal expense
25 is recognized, accounted for differ based on the reason that

1 causes the removal to occur?

2 A Not in my opinion. I think I've said that in my
3 testimony. The reason is irrelevant. There is a reserve for
4 cost of removal and it should be used.

5 Q With respect to the specific plant items that were
6 removed and replaced in the aftermath of the storms in 2004,
7 did the company receive from ratepayers any cost of removal
related revenues associated with those plant items?

9 A I'm sorry. I'm --

10 Q Okay. You described the existing cost of removal
11 reserve of about a billion dollars or so?

12 A Yes.

13 Q Is any portion of that present reserve related to the
14 plant items that were damaged and removed after the hurricane?

15 A Yes.

16 Q Would you explain why that's the case?

17 A Because depreciation rates were applied to all plant,
18 those poles as well as all the other poles that weren't damaged
19 by the storm. And the application of the depreciation rates
20 which included a component for cost of removal was to all
21 poles; ergo, cost of removal was collected for those specific
22 poles.

23 Q Mr. Butler asked you to agree that FPL had applied
24 the remaining life technique in designing the proposed
25 depreciation rates that are encompassed within the study. Do

1 you recall that question and answer?

2 A Yes.

3 Q Do you believe that the remaining life technique is
4 appropriate for the situation that the company faces presently?

5 A I'm, I'm not here to debate depreciation methods in
6 this case. But I will tell you that my personal opinion is
7 that when -- I said earlier that the reason that the remaining

life technique is normally used is to handle reserve

9 imbalances. One of -- I've never been crazy about the
10 remaining life technique, but it is -- a lot of commissions use
11 it.

12 My preferred approach is an approach that was used by
13 this Commission back in the mid-1980s for the telephone
14 industry where the reserve deficiency would be carved out as a
15 separate amount, and then whole life depreciation was used for
16 depreciation purposes with a separate amortization of the
17 reserve in balance.

18 The reason that that's a better approach particularly
19 for FPL today is because a remaining life rate is adjusted to
20 correct for a reserve imbalance. **If there is a deficiency, the**
21 remaining life is higher than the whole life rate. Therefore,
22 the next new asset that gets placed in service gets an
23 incorrect rate applied to it. **If the average service life is,**
24 say, ten years, the rate ought to be 10 percent. But if
25 there's a reserve deficiency, let's say the rate to correct for

1 that deficiency is 11 percent, but you put a new asset in next
2 year, you're hitting it with an 11 percent rate rather than
3 .0 percent. It's brand new and there's no deficiency
4 associated with that asset.

5 On the other hand, if there's an excess, which this
6 company has, the reverse happens and you wind up
7 underdepreciating the new assets. So most of the time those
8 ~~imbbalances are not of the magnitude that I think exists for~~
9 this company. And the application of the wrong rates to new
10 assets is merely going to perpetuate some kind of problem in
11 the future.

12 Q At one point Mr. Butler asked you whether there are
13 any standards or guidelines that, that direct the methodology
14 to be applied to depreciation, and you've already testified
15 that you're aware that in certain instances the Commission has
16 addressed reserve deficiencies with a time frame other than the
17 remaining life.

18 A That's correct.

19 Q What guidelines, what consideration would be taken
20 into account to, to arrive at the decision to use a life
21 shorter than the remaining life?

22 A Are you asking me what, what I recall was the
23 rationale for using a different? And I think it was
24 intergenerational equity.

25 Q Do you think that consideration or that guideline

1 would have application to the situation that you've addressed
2 in your testimony?

3 A Yes.

4 Q Mr. Butler asked you some questions about what has
5 been described as a discounted cash flow exercise, and you said
6 you disagreed with the premise of the, of the exhibit. Would
7 you explain what you meant by that?

8 A Well, there are two basic reasons. The first, my
9 first disagreement with the premise is that it assumes there
10 would be some sort of rate base increase resulting from my
11 recommendation, when that's not the case. There'll be no
12 change to rate base because we have a rate base reduction
13 offsetting a rate base addition. There's no change.

14 Second, you know, I think that Mr. Davis somehow
15 asserts that we're trying to finance storm damages in the
16 future as a result of my recommendation, and that's, that's
17 just a silly, that's a silly representation of what I'm
18 recommending. I disagree with it completely. It's not what
19 I'm recommending.

20 MR. MCGLOTHLIN: Those are all of my questions.

21 COMMISSIONER BAEZ: Exhibits?

22 MR. MCGLOTHLIN: We'll move Mr. Majoros's prefiled
23 exhibits I think 13 through 32.

24 COMMISSIONER BAEZ: 13 through 22 is what I have. Am
25 I --

1 MR. MCGLOTHLIN: I'm sorry. You're right. 13
2 through 22.

3 COMMISSIONER BAEZ: Just an accounting error; right?

4 (Laughter.)

5 Without objection, show Exhibits 13 through
6 22 entered into the record.

7 (Exhibits 13 through 22 admitted into the record.)

8 MR. WRIGHT: I'd move 43, Mr. Chairman.

9 COMMISSIONER BAEZ: Mr. Wright has 43. Are there any
10 objections? None showing, show Exhibit 43, composite Exhibit
11 43 entered into the record.

12 (Exhibit 43 admitted into the record.)

13 That's all the exhibits that I'm showing.

14 Mr. Majoros, thank you.

15 THE WITNESS: Thank you.

16 COMMISSIONER BAEZ: You're excused, sir.

17 Mr. Keating.

18 MR. KEATING: Staff calls Iliana Piedra. And I do
19 not believe that Ms. Piedra has been sworn.

20 COMMISSIONER BAEZ: We'll give Ms. Piedra a couple of
21 minutes so that Mr. Majoros can get out of her way.

22 (Pause.)

23 I'll swear you in, Ms. Piedra.

24 ILIANA H. PIEDRA

25 was called as a witness on behalf of Commission Staff and,

1 having been duly sworn, testified as follows:

2 DIRECT EXAMINATION

3 BY MR. KEATING:

4 Q Ms. Piedra, could you state your name and business
5 address for the record.

6 A Iliana Piedra, 3625 Northwest 82nd Avenue.

7 Q And by whom are you employed?

8 A The Miami District Office, Florida Public Service
9 Commission.

10 Q Okay. And in what capacity are you employed?

11 A I'm a Professional Accounting Specialist.

12 Q Have you brought -- have you prefiled testimony in
13 this docket?

14 A Yes, I have.

15 Q Do you have any changes or corrections to make to
16 that testimony at this time?

17 A No.

18 Q Staff asks that Ms. Piedra's prefiled testimony be
19 inserted into the record as though read.

20 COMMISSIONER BAEZ: Without objection, show the
21 prefiled direct testimony of Iliana Piedra entered into the
22 record as though read.

23 BY MR. KEATING:

24 Q And, Ms. Piedra, did you have one exhibit attached to
25 your testimony --

1 A Yes I did.

2 Q -- identified as Exhibit IHP-1?

3 A Yes, I did.

4 Q And do you have any changes or corrections to that
5 exhibit at this time?

6 A No, I don't.

7 MR. KEATING: I believe that exhibit has already been
8 identified as hearing Exhibit 23.

9 COMMISSIONER BAEZ: That's correct.

10 MR. KEATING: Okay. And staff will waive a summary
11 for this witness and tender the witness for cross-examination.

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1 DIRECT TESTIMONY OF ILIANA H. PIEDRA

2 Q. Please state your name and business address.

3 A. My name is Iliana H. Piedra and my business address is 3625 N.W. 82nd Ave.,
4 Suite 400, Miami, Florida, 33166.

5

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

7 ~~A. I am employed by the Florida Public Service Commission as a Professional~~
8 Accountant Specialist in the Division of Regulatory Compliance and Consumer
9 Assistance.

10

11 Q. How long have you been employed by the Commission?

12 A. I have been employed by the Florida Public Service Commission since January,
13 1985.

14

15 Q. Briefly review your educational and professional background.

16 A. In 1983, I received a Bachelor of Business Administration from Florida
17 International University with a major in accounting. I am also a Certified Public
18 Accountant licensed in the State of Florida.

19

20 Q. Please describe your current responsibilities.

21 A. Currently, I am a Professional Accountant Specialist with the responsibilities of
22 planning and directing audits of regulated companies, and assisting in audits of
23 affiliated transactions. I am also responsible for creating audit work programs to meet
24 a specific audit purpose.

25

1 Q. Have you presented expert testimony before this Commission or any other
2 regulatory agency?

3 A. Yes. I testified in the City Gas Company of Florida rate case, Docket No.
4 940276-GU and the General Development Utilities, Inc. rate cases for the Silver
5 Springs Shores Division in Marion County and the Port LaBelle Division in Glades
6 and Hendry Counties in Docket Nos. 920733-WS and 920734-WS, respectively.

7

8 Q. What is the purpose of your testimony today?

9 A. The purpose of my testimony is to sponsor the staff audit report of Florida
10 Power & Light Company (Company) which addresses the Company's Petition for
11 authority to recover prudently incurred storm restoration costs related to the 2004
12 storm season that exceeded its storm reserve balance, Audit Control Number 04-343-4-
13 1. This audit report, with the exception of two detailed schedules associated with
14 Audit Disclosure No. 3, is filed with my testimony and is identified as Exhibit IHP-1.

15

16 Q. **Did you prepare** or cause to be prepared under your supervision, direction, and
17 control this audit report?

18 A. **Yes, I was the** audit manager in charge of the audit.

19

20 Q. Please describe the work performed in this audit.

21 A. We scanned and compiled all files provided with storm charges in Account
22 186.18, Storm Maintenance Deferred Debit, in order to select sample items for vehicle,
23 material and supplies, journal vouchers, cash vouchers, and payroll. We reconciled the
24 totals to the Company's general ledger. We verified sample items by reference to
25 supporting documentation. We also determined what portion of the Company's

1 property is insured and obtained information regarding any claims filed. We also read
2 the Commission-approved study, Transmission and Distribution Insurance
3 Replacement, dated October 1, 1993 and Order No. PSC-95-0264-FOF-EI, which
4 granted the request of Florida Power & Light Company to increase its annual storm
5 damage accrual and discussed the storm damage study.

6

7 ~~Please review the audit disclosures in the audit report.~~

8 A. Audit Disclosure No. 1 discusses the nuclear plant damages. The insurance
9 company is expected to reimburse FPL for all the St. Lucie nuclear plant damage
10 except for its deductible of \$2,000,000 and storm preparation expenses of \$9,280,311.
11 The deductible and storm preparation costs for St. Lucie nuclear plant are included in
12 the total amounts that the company is asking for as storm restoration costs in this
13 docket. The other costs were removed from the storm cost estimates and included in a
14 separate sub account consisting of all costs for nuclear. Also, the company received
15 \$20,000,000 in advances from its insurance company for the St. Lucie nuclear damage.
16 This amount was also removed from the storm cost estimates and included in a
17 separate sub account.

18 For Turkey Point nuclear, the company included a total of \$1,060,461.22 for
19 storm preparation charges. This total is for all three storms.

20

21 Audit Disclosure No. 2 discusses the insurance coverage for non-nuclear
22 property. FPL carries insurance on non-nuclear property which has a deductible of
23 \$25,000,000 for each named storm. The policy indicates that no coverage is provided
24 for transmission and distribution lines, except for lines situated within 1,000 feet of the
25 insured premises. We did not find items in our sample for credits for insurance

1 ayments or accrued insurance payments for non-nuclear property. The company has
2 ot applied to the insurance company for reimbursement. Company personnel
3 xplained that, as of mid-January, the damage to plants and buildings for each named
4 torm was approximately \$12 million for Charley, \$15 million for Jeanne, and \$18
5 illion for Frances. The Company periodically updates these estimates. FPL has not
6 identified damage estimates for the lines situated within 1,000 feet of the premises.
7 hould the damage to plant and building exceed the \$25,000,000 deductible for a
8 articular storm, then the insurance reimbursements should be credited to the
9 estoration costs.

10
11 Audit Disclosure No. 3 discusses bonuses paid to employees. FPL paid
12 pproximately \$2,043,600 in bonuses to various employees. Of this total, the company
13 eversed \$129,000 leaving a net amount of \$1,914,600 charged to the storm reserve.
14 These bonuses range from \$1,500 to \$35,000 per employee.

15 The company stated:

16 "The Approved study states that regular payroll, overtime payroll, and
17 temporary relieving pay are chargeable to the storm reserve fund.
18 These charges should be reasonable and attributable to the storm
19 restoration efforts. Management determined that in some cases certain
20 employees who performed beyond expectations deserved additional
21 compensation. Management, therefore, awarded bonuses to these
22 employees. In doing so, management developed loose guidelines in
23 order to determine the amount of the bonus based on the employee's
24 position held during storm restoration efforts. For example, a staging
25 site manager was eligible for an \$18,000 bonus for Charley, and the

1 manager's backup was eligible for a \$12,000 bonus. If they, of course,
2 exceeded management's expectations. Whether an employee received
3 overtime compensation also determined the amount of the bonus. For
4 instance, if management felt that a certain position deserved a \$10,000
5 bonus, but the person in that position also earned \$5,000 in overtime
6 compensation then that employee was only awarded a \$5,000 bonus.”
7

8 Audit Disclosure No. 4 discusses storm assignment records. We selected a
9 ample of payroll from the Company's Account 186.18-Storm Maintenance Deferred
10 Debit, which was later charged to the storm reserve Account 228, to determine if the
11 Company had adequate supporting documentation and that the employees were
12 actually working on storm related work. The sample was traced to supporting
13 documentation, but the documentation did not include any information about what
14 duties the employee performed. We requested additional information about the duties
15 performed by all employees in the sample and, for a small sample of those employees,
16 we asked for job tickets that the employee worked on. The Company explained that
17 they could not provide a job ticket or job record which shows the actual storm duties
18 assigned to each employee selected or a list of duties for the entire sample. The
19 Company contacted the individuals in the small sample for which we sought job tickets
20 to request their storm duties and locations and explained that:

21 “FPL maintains a storm restoration plan with initial assignments of
22 employees to restoration assignments. When the storm restoration efforts
23 actually are underway, the assignments become very fluid. Some
24 employees are not available for their assignment and others are
25 substituted. The goal is to track all assignments, however, during the

1 summer of 2004 the efforts were so long and so dynamic, centralized
2 daily records are not available. Employees are reassigned duties and
3 locations on a daily basis to meet the changing needs of the restoration
4 efforts.”

5 Since the records were not available, we were not able to verify storm duties for the
6 sample of payroll selected.
7

8 Audit Disclosure No. 5 discusses the revision of the storm reserve estimate to
9 \$890,000,000. On December 8, 2004, we requested all entries to Accounts 228-Storm
10 Reserve and 186.180-Storm Maintenance Deferred Debit for 2004. The Company
11 provided the information through November because the data for December was not
12 yet available. On January 10, 2005, we again requested detail of all December 2004
13 entries. We received this detail on January 14, 2005. The Company made a press
14 release on January 21, 2005, to announce it was increasing the costs charged to the
15 storm reserve from \$710,000,000 to \$890,000,000. The detail we received on January
16 14 did not include the journal entry accruing the additional amounts. On January 21,
17 we requested all supporting documents relating to the accrual. On January 25, we
18 received the journal entry but no supporting documents. We did not receive any
19 supporting documents until January 31. On that date we selected a sample of vendors
20 and asked the Company to provide the list of invoices for those vendors. We had
21 planned to select a sample of those invoices to trace to source documentation. We did
22 not receive the lists until February 5, 2005. Since our audit report was due February 8,
23 we could not follow up on these items and obtain the actual invoices.
24

25 Audit Disclosure No. 6 discusses items included in base rates. The Company

1 records regular and overtime payroll based on Expense Analysis Codes (EAC). In
2 1993, as part of Docket No. 930405-EI, FPL was required to file a study describing to
3 the Commission how it would record hurricane related costs to the reserve. The study
4 provided by FPL included three possible methods.

- 5 1. Actual restoration costs
- 6 2. Actual restoration cost with a net book value adjustment.
- 7 ~~3. Incremental costs.~~

8 The incremental cost method proposed reducing restoration costs by straight time
9 payroll, loadings, and vehicle charges. But, included in that proposal, the Company
10 included an increment for lost revenue, catch-up work, and back-fill work. Order No.
11 PSC-95-0264-FOF-EI, dated February 27, 1995, says:

12 "FPL stated that it would use the actual restoration cost approach for determining the
13 appropriate amounts to be charged to the reserve. This methodology is consistent with
14 the manner in which replacement cost insurance works." The order also states:
15 "However, we have the authority to review any expenses charged to the reserve for
16 reasonableness and prudence." The order also discusses that capital additions should
17 be recorded in the reserve at the gross cost of the replaced plant. FPL has recorded the
18 costs as proposed in its 1993 study and as discussed in the 1995 order, using the actual
19 costs.

20

21 Q. Does this conclude your testimony?

22 A. Yes, it does.

23

24

25

1 a complete verification of all the costs related to the
2 hurricanes back to those supporting documents; correct?

3 A We did an audit as of a certain amount, and the
4 company made a revision later on and we did not get to complete
5 the new charges that were revised

6 Q Okay. And even for those amounts that you did look
7 at, you were just verifying a sample of those charges; correct?

8 A Yes.

9 Q Okay. So you didn't do an actual full and complete
10 audit of every single charge that was made to the storm --

11 A No, we did not.

12 Q And attached to your direct testimony you contain an
13 audit report; am I correct?

14 A Yes.

15 Q And your audit report contains audit disclosures?

16 A Uh-huh.

17 Q I want to refer you to the audit disclosures referred
18 to in your report. Let me refer you first to Audit Disclosure
19 Number 3. And that discusses bonuses paid to employees; am I
20 correct?

21 A Yes.

22 Q And according to the audit disclosure, the amount of
23 employee bonuses that were originally charged to the storm
24 reserve was approximately \$1.9 million.

25 A Yes.

1 Q And is it my understanding or your understanding, I'm
2 sorry, is it your understanding that subsequent to your audit
3 report FPL decided that it was no longer going to charge the
4 \$1.9 billion worth of employee bonuses to the storm reserve but
5 charge those to normal operations?

6 A Yes. That was in their response.

7 Q Okay. Let me refer you to Audit Disclosure number 4.

8 ~~Am I correct that the supporting documentation provided by FP&L~~
9 did not include any documentation about the duties performed by
10 the employees who were supposedly working on these storms in
11 the sample that you received from FPL?

12 A Yes. That's correct.

13 Q Okay.

14 A The documentation we reviewed was coded to a work
15 order for a specific storm, but it didn't have a detail of what
16 the employees did. It was charged to the storm work order.

17 Q Okay. On Audit Disclosure Number 5, is that related
18 to the increased request for FP&L; correct?

19 A Yes.

20 Q And it's my understanding from your earlier testimony
21 today and from this audit disclosure that due to the timing of
22 that increase you were unable to select a sample and to verify
23 those samples against the invoices.

24 A Yes. We selected additional documentation and some
25 of it was provided, some of it was received, but we needed to

1 pick additional items and we were not able to verify.

2 Q Okay. So then would I be correct in saying that for
3 the additional cost there's no independent staff verification
4 for the sampling at this point?

5 A Uh-huh. Yes.

6 Q Referring to Audit Disclosure Number 6, you state in
7 your testimony that this item discusses things that were

8 included in rate base. Am I correct?

9 A Yes.

10 Q Okay. And as part of your disclosure you identify
11 several items that are part of rate base; correct?

12 A Yes.

13 Q Part of the costs that were included in rate base is
14 regular and overtime payroll based on expense analysis codes
15 which FPL charged to the storm account. Am I correct in that
16 understanding?

17 A Yes.

18 Q And you identify the amount of regular salaries as of
19 December 31st, 2004, as \$27 million approximately; am I
20 correct?

21 A Yes.

22 Q Okay. And you also identify vehicle costs which are
23 normally included as part of base rates; am I correct?

24 A Yes.

25 Q And you indicate that those were also charged to the

1 storm account.

2 A Yes.

3 Q Now would you agree that double-dipping is collecting
4 twice for the same work?

5 A In a general scenario, yes. The reason why we
6 explained this in the disclosure is because when we found the
7 items, we realized that some of the things were in rate base.

8 ~~But in the study that we were given throughout the audit there~~
9 ~~was an attachment that had listed some items, and vehicle and~~
10 ~~overtime pay were listed in that study.~~

11 Q Okay. But normally those are included in base rates;
12 correct?

13 A Yes, they are.

14 Q And if you collect once from base rates for those
15 items and collect then again from another source for those same
16 items, that would be classically double-dipping; is that
17 correct?

18 A It could be.

19 Q Okay. It could be.

20 And you would agree that catch-up work is work that
21 would be postponed until a later time; correct?

22 A Yes.

23 Q And would you agree with me that double-dipping and
24 catch-up work are not the same thing by definition?

25 A No. They don't appear to be.

1 Q Okay. And is it your understanding that it is
2 Commission policy not to allow double-dipping?

3 A I would imagine it is not allowed.

4 Q Okay. So you would agree -- well, so you would agree
5 that as a practical matter any double-dipping should be
6 disallowed as a cost?

7 A I would think so.

8 Q Okay. In Audit Disclosure Number 6 you also discuss
9 Order Number PSC-95-0264-FOF-EI; correct?

10 A Yes.

11 Q Okay. And in your order you select, quote -- well,
12 you quote select passages from that order. Am I correct in
13 that?

14 A Yes.

15 Q And The two quotes that you, you particularly
16 discussed is that "FPL stated that it would use the actual
17 restoration cost approach for determining the appropriate
18 amounts to be charged to the reserve. This methodology is
19 consistent with the manner in which replacement cost insurance
20 works." And the other select quote that you used was,
21 "However, we have the authority to review any expenses charged
22 to the reserve for reasonableness and prudence." Am I correct?

23 A Yes.

24 Q Okay. Do you have a copy of that order in front of
25 you?

1 A Yes.

2 Q If not, we can pass out a copy of that order just to
3 make sure everyone has a copy.

4 Okay. Let me refer you to Page 4 of that order. The
5 first paragraph under the storm, the section titled "Storm
6 Damage Study," am I correct in that, that it states "FPL's
7 study provided sufficient analysis to indicate the appropriate
8 annual amount that should be contributed to the Storm Damage
9 Reserve Fund at this time"? Is that correct?

10 A Yes.

11 Q And if you look at Page 5, the paragraph at the end
12 of that section, right above Tropical Storm Gordon --

13 A Uh-huh.

14 Q -- reads, "We are considering the appropriateness of
15 opening a rulemaking proceeding to establish uniform guidelines
16 for determining when Storm Damage Reserve should be charged and
17 what costs should be charged to it." Is that also a correct
18 reading of what's in this order?

19 A Yes.

20 Q And this is the same order where you took the other
21 quotes from?

22 A Uh-huh.

23 Q Okay. Would you agree with me that the, that by
24 selecting those particular passages you were not intending to,
25 to do a complete analysis of what the order said on FPL's

1 study; correct?

2 A Can you repeat the question? I'm sorry.

3 Q By choosing those two sections that you did, you
4 chose to quote in your audit disclosure, would I be correct in
5 saying that you weren't trying to do a complete analysis of
6 what that order meant, everything that the order said?

7 A No. I was simply trying to state something that
8 related to the disclosure I was writing.

9 Q Okay. And would you agree that in your, in the
10 opinion section of your Audit Disclosure Number 6 you only note
11 that FP&L recorded costs using the actual cost methodology as
12 it proposed to do in its 1993 study and discussed in that
13 order; is that correct?

14 A Yes.

15 Q Okay. And you were not intending to render a legal
16 opinion as to whether FPL's actual storm cost methodology is
17 the appropriate methodology to use for storm recovery. Am I
18 correct in that?

19 A No, I was not rendering a legal opinion. You're
20 right.

21 Q And you're not here today rendering an opinion as to
22 how, what appropriate storm cost methodology should be used by
23 the Commission; correct?

24 A Correct.

25 MS. CHRISTENSEN: Okay. I have no further questions.

1 MR. PERRY: I have no questions.

2 COMMISSIONER BAEZ: Mr. Wright?

3 MR. WRIGHT: No questions, Mr. Chairman.

4 COMMISSIONER BAEZ: Mr. Twomey has no questions.
5 Mr. Huntoon?

6 MR. HUNTOON: Yes. Thank you, Mr. Chairman.

7 CROSS EXAMINATION

8 BY MR. HUNTOON:

9 Q Is the use of sampling techniques standard in the
10 audit process?

11 A Yes, it is.

12 Q And did staff use sampling techniques that it
13 believed were consistent with its processes generally for the
14 audit that it performed in this case?

15 A Yes, we did.

16 Q Thank you. Is it -- on Page 7 of your testimony,
17 Lines 17 through 19, would you take a look at that? Could you
18 read that, the last sentence of your testimony?

19 A Okay. Line 16?

20 Q I'm sorry. 17 through 19.

21 A Okay. "The order discusses that capital additions
22 should be recorded in the reserve at the gross cost of the
23 replaced plant. FPL has recorded the costs as proposed in its
24 1993 study and as discussed in the 1995 order, using actual
25 costs."

1 Q And is that -- that's your testimony still today? Is
2 that testimony correct, I guess, is my, my question?

3 A Yes.

4 Q Do you know -- has, has the, has the company extended
5 the opportunity to staff to do any additional audit work that
6 it deems appropriate with respect to the additional costs that
7 have been booked to the storm reserve?

8 A Yes. In the response to the audit report the company
9 indicated that the records underlying the revised estimates
10 were available upon request.

11 Q Is that, is that a correct statement in your view?

12 A Yes. As far as us auditing the work, we would have
13 to get audit service requests from our Tallahassee personnel in
14 order for us to conduct additional testing. We don't do
15 that -- we don't make that decision.

16 Q But FPL has offered that; is that right?

17 A Yes, they have.

18 Q One moment, please.

19 Sorry. One more moment, please.

20 When you used the term "double-dipping" in response
21 to the question from counsel, could you explain what you meant
22 by that or what you understood that term to mean when you were
23 responding to the question?

24 A Well, what I think she meant is that there are things
25 that are included in base rates and would also be included in

1 the storm reserve. I never used that term in my work papers or
2 in my report.

3 MR. HUNTOON: Okay. Nothing further. Thank you very
4 much.

5 THE WITNESS: Thank you.

6 COMMISSIONER BAEZ: Commissioners, do you have any
7 questions? Redirect.

8 MR. KEATING: No redirect.

9 COMMISSIONER BAEZ: Exhibits?

10 MR. KEATING: Staff would move Exhibit 23.

11 COMMISSIONER BAEZ: Without objection, show Exhibit
12 23 entered into the record.

13 (Exhibit 23 admitted into the record.)

14 Thank you, Ms. Piedra. You're excused.

15 THE WITNESS: Thank you.

16 (Transcript continues in sequence with Volume 5.)

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1 STATE OF FLORIDA)
2 COUNTY OF LEON) : CERTIFICATE OF REPORTER

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I, LINDA BOLES, RPR, Official Commission Reporter, do hereby certify that the foregoing proceeding was heard at the time and place herein stated.

IT IS FURTHER CERTIFIED that I stenographically reported the said proceedings; that the same has been transcribed under my direct supervision; and that this transcript constitutes a true transcription of my notes of said proceedings.

I FURTHER CERTIFY that I am not a relative, employee, attorney or counsel of any of the parties, nor am I a relative or employee of any of the parties' attorneys or counsel connected with the action, nor am I financially interested in the action.

DATED THIS 22nd DAY OF APRIL, 2005.


LINDA BOLES, RPR
FPSC Official Commission Reporter
(850) 413-6734