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Subject: Electronic Filing for Docket No. 041291-EI/ FPL's Post-Hearing Brief

Attachments: Storm Post Hearing Brief.5.10.05.doc

Storm Post
ring Brief.5.1

Electronic Filing

a. Person responsible for this electronic filing:

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b. Docket No. 041291-EI

In re: 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.

c. Document being filed on behalf of Florida Power & Light Company.

d. There are a total of 50 pages.

e. The document attached for electronic filing is Florida Power & Light Company's Post-Hearing Brief

(See attached file: Storm Post Hearing Brief.5.10.05.doc)

Thank you for your attention and cooperation to this request.

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BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: 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.	))))	Docket No. 041291-EI Filed: May 10, 2005

FLORIDA POWER & LIGHT COMPANY'S POST-HEARING BRIEF

Florida Power & Light Company ("FPL" or the "Company") files with the Florida Public Service Commission (the "PSC" or the "Commission") its Post-Hearing Brief in the above-referenced docket, and states:

ISSUE 1: What is the legal effect, if any, of FPL's 1993 storm cost study and Order No. PSC-95-0264-FOF-EI entered in Docket No. 930045-EI on the decisions to be made in this docket?

The Commission approved accounting standards submitted by FPL pursuant to Commission order. FPL must adhere to Commission orders and has relied upon the Commission's order. Storm restoration costs were booked in accordance with the approved standards and were included in the Storm Damage Reserve deficit that was reported as an asset in the Company's 2004 financial statements. Changing the standards retroactively would undermine the basis for financial reporting. Nothing has occurred that alters the propriety of using the approved standards.

In 1993 following Hurricane Andrew, as a result of the diminishing availability of commercial property insurance covering transmission and distribution system assets, FPL petitioned the Commission to implement a self-insurance mechanism. By Order No. PSC-93-0918-FOF-EI, Docket No. 930405-EI (issued June 17, 1993) (the "1993 Order"), the Commission "permitted [FPL] to implement a self-insurance approach for the costs of repairing and restoring its transmission and distribution system in the event of a hurricane, storm damage or other natural disaster." Details on implementing the self-insurance approach remained to be ironed out, however. The Commission noted in the 1993 Order that "it is unclear what storm related expenses FPL intends [to] draw from the [self-insurance storm] reserve fund" and

directed FPL to "submit a study indicating ... the types of costs [FPL] intends to charge to the reserve ...." Tr. 92 (Davis).

As directed by the Commission, FPL filed its Storm Study on October 1, 1993 ("1993 Study"). Id. The study described three alternative approaches for determining the amounts to be charged to the Storm Damage Reserve (sometimes hereinafter "Reserve"): Actual Restoration Cost, Actual Restoration Cost with Net Book Value Adjustment, and Incremental Cost. It provided a detailed illustrative list of what would be charged to the Reserve under each approach, summarized the accounting entries that each approach would entail, and discussed the relative merits of each approach. The 1993 Study then expressly recommended using the Actual Restoration Cost approach. Ex. 24, p. 9. In 1995, the Commission entered Order No. PSC-95-0264-FOF-EI (the "1995 Order"), which was entitled "NOTICE OF PROPOSED AGENCY ACTION APPROVING STORM DAMAGE STUDY AND ADJUSTMENTS TO SELF INSURANCE MECHANISM." Ex. 25, p. 1 (emphasis added); Tr. 94 (Davis). By approving the 1993 Study, the Commission necessarily approved FPL's recommendation that the Actual Restoration Cost approach be used for charging storm costs to the Reserve.[1] The Commission has issued several orders subsequently that deal with the Reserve, but none of them has questioned or changed the Actual Restoration Cost approach that was approved in the 1995

[1] The 1995 Order clearly approved the approach set forth in the 1993 Study. The 1995 Order contains the following discussion concerning the basis for charging storm costs to the Reserve: "In addition, the study addresses the issues raised in the [1993 Order] concerning the types of expenses that would be charged to the reserve. However, we have the authority to review any expenses charged to the reserve for reasonableness and prudence. FPL stated that it would use the actual restoration cost approach for determining the appropriate amounts to be charged to the reserve." Ex. 25, p. 4. Read as a whole, this passage shows the Commission's intent to approve the *categories* of costs that should be charged to the Reserve, such that future proceedings would not have to address that question again, while retaining authority to review the reasonableness and prudence of specific charges that FPL makes in the future within the approved categories. As discussed in Issue 17 below, there is no dispute in the record of this proceeding that the 2004 storm costs FPL has charged to the Reserve are reasonable and prudent. Mr. Majoros testified that the 1995 Order only found adequate the level of the annual accrual proposed in the 1993 Study (Tr. 446) – a plainly impossible interpretation of the 1995 Order given that the 1993 Study proposed an annual accrual of $7.1 million, Ex. 24, p. 6, and the 1995 Order actually approved $10.1 million, Ex. 25, 6.

Order. Tr. 95-96 (Davis). Between 1993 and 2003, FPL consistently applied the Actual Restoration Cost approach in accounting for the costs of eight storms totaling $152 million in restoration costs, with no challenge from the PSC, Staff or any party. Tr. 96-97 (Davis).

Based on the Commission's approval of the Actual Restoration Cost approach in the 1995 Order and the Commission's consistent acceptance of it thereafter, FPL reasonably and appropriately used that approach to charge 2004 storm costs to the Reserve. Tr. 84 (Davis). Requiring FPL to use a different approach at this time would be unreasonable and inappropriate, because it would ignore ten years of precedent and retroactively change the applicable principles. Tr. 143 (Davis); 722-23 (Dewhurst). Retroactive application of new standards could significantly undermine the basis for FPL's financial reporting and the financial community's confidence in FPL's accounting for the effects of regulatory actions in its financial statements.[2]

As discussed in Issue 2 below, the 1995 Order approving the 1993 Study has served FPL and its customers well as demonstrated by FPL's performance in the aftermath of the 2004 storm season. Neither OPC nor other Intervenors have provided evidence demonstrating that circumstances have changed warranting a departure from or modification of the Actual Restoration Cost approach embodied in the Storm Study approved in the 1995 Order. See, e.g., Cleveland Clinic v. Agency for Hlth. Care, 679 So. 2d 1237, 1241-42 (Fla. 1st DCA 1996) (reversing AHCA decision "to simply 'change its mind' [with] no good reason why the agency's abrupt change of established policy, practice and procedure should be sanctioned"); Peoples Gas

[2] If the approach on which FPL has relied is retroactively changed, FPL will have relied on this approach to its detriment contrary to principals of law. See, e.g., Dolphin Outdoor Advertising v. Dept. of Transp., 582 So. 2d 709, 710-11 (Fla. 1st DCA 1991) (the essential requirements of equitable estoppel are: (1) a representation as to a material fact that is contrary to a later-asserted position; (2) reliance upon that representation; (3) a change in position caused by the representation and reliance). It would be unlawful for the Commission to retroactively apply a different methodology than that announced in the 1995 Order and applied by FPL since then. It could only be done prospectively through rulemaking as the Commission had previously contemplated or through administrative hearing if Ch. 120 rulemaking provisions would not require rulemaking procedures.

System, Inc. v. Mason, 187 So. 2d 335, 339-40 (Fla. 1966) (reversing a Commission order that modified an earlier final order because there was not a finding based on adequate proof that modification was necessary in the public interest because of changed conditions or other circumstances that were not present in the earlier proceedings); Order No. PSC-95-1319-FOF-WS, Docket No. 921237-WS (issued Oct. 30, 1995) (while "[a] change in circumstances or great public interest may lead an agency to revisit an order" ... "there must be a terminal point where parties and the public may rely on an order as being final and dispositive.")

ISSUE 2: Is the methodology in Order No. PSC-95-0264-FOF-EI, issued in Docket No. 930405-EI, for booking costs to the Storm Damage Reserve the appropriate methodology to be used in this docket?

Yes. Nothing has occurred that would alter the propriety of using the standards approved in Docket No. 930405-EI.

Notwithstanding the Commission's approval of the 1993 Study and FPL's subsequent reliance on it, OPC has argued that the Commission should disregard its prior practice and require FPL to charge storm costs in accordance with the "OPC Storm Damage Guidelines" that appear in OPC witness Majoros' testimony. Tr. 390-91. But Mr. Majoros offers no sound reason why the Commission should do so. He has no prior experience in accounting for storm cost recovery and has never participated in any form of storm restoration activities. Tr. 445. He acknowledges that the Commission has never before directed FPL to use anything other than the Actual Restoration Cost approach. Tr. 448. And apart from one unpersuasive contention, he openly acknowledges that there is nothing in the 1995 Order that would question FPL's use of the Actual Restoration Cost approach.[3]

[3] Mr. Majoros argues that the 1995 Order did not approve FPL's recommendation to use the Actual Restoration Cost approach because the Commission was "considering the appropriateness of opening a rulemaking proceeding to establish uniform guidelines for determining when the storm damage reserve should be charged and what costs should be charged to it." Ex. 10, p. 5. But he acknowledged that this rulemaking has never taken place and, if it ever does, its application should be prospective. Tr. 448-49.

Nor does Mr. Majoros point to any compelling advantages to using the "OPC Storm Damage Guidelines." Basically the OPC Guidelines differ from FPL's Actual Restoration Cost approach in two ways, neither of which would constitute an improvement.

First, implementation of the OPC Guidelines would increase FPL's rate base above the pre-storm level by the "normal" amount of capital costs that would be incurred to restore its transmission and distribution system, rather than charging those capital costs to the Reserve as FPL has done. This would have the effect of reducing the amount of the Reserve deficit that FPL needs to recover from customers through the proposed surcharge, but at the expense of creating a decades-long legacy of increased base-rate revenue requirements that ultimately would cost customers more and leave them paying for 2004 storm costs at the same time that they face exposure to the costs of future storms. Tr. 112-17 (Davis); 724 (Dewhurst).

Second, the OPC Guidelines would look past what FPL actually spent on 2004 storm restoration work and instead focus on a comparison of FPL's actual restoration costs to the pre-storm budgeted activity levels in an effort to calculate "incremental" restoration costs. FPL specifically addressed the incremental cost approach in its 1993 Study and recommended against it for three reasons: calculating what is "incremental" would be complicated, storm-specific and likely to engender extensive debate; an incremental approach would be inconsistent with the determination of restoration costs recoverable under replacement-cost insurance policies; and, when one takes into account all of the incremental impacts of storms on FPL's income, the cost to customers under the incremental approach would be as much or more as under the Actual Restoration Cost approach. Ex. 24, pp. 11-12. Each of those reasons is as applicable today as it was in 1993, and there is nothing in the record to the contrary.[4]

[4] OPC argues that there is no longer any need to account for storm costs consistently with the way that replacement-cost insurance claims are documented because FPL does not have and has no immediate prospects for obtaining

In an attempt to shore up his flawed incremental approach, Mr. Majoros resorts to unfounded invective. He characterizes FPL's Actual Restoration Cost approach as "double dipping" because FPL supposedly would recover certain costs both in its base rates and through the storm surcharge. This is simply wrong. If one were to use an incremental approach, then it could be applied fairly only by looking at *all* of the incremental storm-related impacts on a utility's income in the affected period. FPL experienced storm-related revenue losses in 2004 that are almost exactly equal to the amount of storm costs that Mr. Majoros would disallow as "double dipping" (approximately $38 million in both instances) Ex. 26; Ex. 19; Tr. 452-53 (Majoros). Mr. Majoros agreed that, if a utility's base revenues and base expenses both dropped by $38 million for a particular year as a result of storms, then the storms would have had no impact on the utility's net income for that year. Tr. 453. This effectively concedes that there was no "double dipping" for FPL in 2004, before one even considers the incremental "backfill" and "catch-up" costs and additional uncollectible accounts receivable write-offs that resulted from the 2004 storms. Tr. 104-09 (Davis).[5]

Simply put, the record contains abundant support for using the Actual Restoration Cost approach to charge FPL's 2004 storm costs to the Reserve, and it contains no competent evidence to the contrary.

ISSUE 3: Were the costs that FPL has booked to the Storm Damage Reserve consistent with the methodology in the study filed on October 1, 1993 by the Company in Docket No. 930405-EI?

Yes. Costs booked to the Storm Damage Reserve were recorded consistent with the methodology in the 1993 Study approved by the Commission in the 1995 Order.

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such insurance for its transmission and distribution system assets. This argument ignores the fact that FPL does indeed have replacement cost insurance for other types of assets. Using separate and inconsistent accounting approaches for the restoration costs associated with different types of assets would be inappropriate and difficult to administer in the field. Tr. 235 (Davis).

[5] In this regard, it is interesting to note that FPL's calculation in the 1993 Study of the total incremental costs associated with Hurricane Andrew were $299 million, versus Actual Restoration Costs for that storm of $270 million. Ex. 24, p. 15.

There is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach approved by the Commission in the 1995 Order. Mr. Davis testified that the costs were so recorded. Tr. 83-84. The Staff's audit concurred. Ex. 23, p. 12. Even OPC's Mr. Majoros acknowledged that he was aware of no instances in which FPL deviated from the Actual Restoration Cost approach. Tr. 446.

ISSUE 4: Has FPL quantified the appropriate amount of non-management employee labor payroll expense that should be charged to the storm reserve? If not, what adjustments should be made?

Yes. FPL has booked payroll costs to the Storm Damage Reserve consistent with the methodology in the 1993 Study approved by the Commission in the 1995 Order. No adjustment is necessary.

As discussed in Issue 3 above, there is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach. Storm-related payroll costs -- regular, overtime and temporary relieving pay -- are specifically identified as properly chargeable to the Reserve under the Actual Restoration Cost approach. Tr. 106 (Davis); Ex. 24, pp. 8, 16.

OPC's position in the Prehearing Order is that $10,906,236 of non-management employee labor payroll expense should be removed because it is "already included in the budgeted amounts supported by base rates."[6] There is no record support for the amount of OPC's proposed non-management payroll adjustment.[7]

OPC's incremental approach to payroll costs would introduce undesirable incentives. In meeting the objective of safe and rapid restoration, FPL mobilizes virtually the entire

[6] OPC's incremental approach to payroll costs (and Intervenors' allegations of so-called "double dipping") ignores the other side of the base rate equation – revenues, and also ignores that a portion of the regular payroll would have been charged to cost recovery clauses and to capital. Also, there is an inconsistency between Mr. Majoros' proposed adjustment for regular salaries and OPC's guidelines which propose adjusting only bargaining unit payroll. Tr. 107-08 (Davis).

[7] OPC's proposed adjustment of $10,906,236 is larger than the $9,483,684 of "regular" payroll for "bargaining" employees that FPL identified in its response to Twomeys' Interrogatory No. 43, which is part of Ex. 34.

organization in the restoration effort in one way or another. The normal work of those who are assigned directly to storm support either is performed by others "doubling down," or is done later, usually with overtime. If regular base compensation is disallowed against the Reserve, clearly the incentive is not to utilize available FPL resources but instead to leave them to perform their regular work and increase the utilization of contractors and foreign utilities. This would not only slow overall restoration efforts (since FPL resources can be mobilized more quickly than third parties can be brought in), but would also be more costly for customers because the unit costs of outside resources is significantly higher, on average, than FPL's costs, as the data from Hurricanes Charley, Frances and Jeanne clearly show. Tr. 725 (Dewhurst).

ISSUE 5: Has FPL properly treated payroll expense associated with managerial employees when determining the costs that should be charged to the storm reserve? If not, what adjustments should be made?

Yes. FPL has booked payroll costs to the Storm Damage Reserve consistent with the methodology in the 1993 Study approved by the Commission in the 1995 Order. No adjustment is necessary.

As discussed in Issue 3 above, there is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach. Storm-related payroll costs -- regular, overtime and temporary relieving pay -- are specifically identified as properly chargeable to the Reserve under the Actual Restoration Cost approach. Tr. 106 (Davis); Ex. 24, pp. 8, 16.

OPC asserts in the Prehearing Order that $18,300,983 of managerial payroll expense "should be removed from the amount charged to the storm reserve." OPC gives no rationale in the Prehearing Order for this position, but FPL assumes that it is based on the use of OPC's "incremental" approach. There is no record support for the amount of OPC's proposed

management payroll adjustment.[8] As discussed in Issue 4 above, OPC's incremental approach to payroll costs would introduce undesirable incentives. Moreover, even if Mr. Majoros' adjustment were appropriate, he has overstated it substantially because he failed to take into account the approximately 6% of regular payroll that is charged to adjustment clauses and approximately 22% that is charged to capital on an annual basis. Tr. 107 (Davis).

ISSUE 6: At what point in time should FPL stop charging costs related to the 2004 storm season to the storm damage reserve?

Application of PSC Rule 25-6.0143, Florida Administrative Code, provides that all costs determined to be the result of storm damages should be charged to the Storm Damage Reserve.

Rule 25-6.0143(4)(b), F.A.C., provides that if a utility elects to use a Storm Damage Reserve, "each and every loss or cost which is covered by the [Reserve] shall be charged to [the Reserve] and shall not be charged directly to expenses. Charges shall be made to [the Reserve] regardless of the balance in [the Reserve]." The 1993 Study, which was approved by the 1995 Order, stated that under the Actual Restoration Cost approach, the Reserve should be charged for all "costs incurred as the result of a storm to return plant and equipment to its original operating condition, safely restore service to customers, or costs that are clearly attributable to the storm and are reasonably quantifiable." Ex. 24, p. 16. Neither the 1993 Study nor the 1995 Order mentions any time limits on when such costs might be incurred, but the Commission has sanctioned charging follow-up work to the Reserve subsequent to the issuance of the 1995 Order. Tr. 110 (Davis). Consistent with the direction given by Rule 25-6.0143(4)(b) and the 1993 Study, FPL has charged and intends to continue charging all of its 2004 storm costs to the Reserve regardless of when they are incurred. The appropriate criterion for determining whether

[8] OPC's proposed adjustment of $18,300,983 is close, but not identical, to the total of $18,302,983 in "regular" payroll for "non-bargaining exempt," and "non-bargaining non-exempt" employees that FPL identified in its response to Twomeys' Interrogatory No. 43, which is part of Ex. 34.

work should be charged to the Reserve is the root cause of needed repair and restoration of the system to pre-storm status, not the timing of the work. Tr. 109-10 (Davis).

OPC would arbitrarily cut off charges to the Reserve on the departure date for the foreign utility crews that assisted FPL with its storm restoration activities. This approach is simply unworkable. First of all, it would directly contravene Rule 25-6.0143(4)(b), which *requires* that all storm-related costs be charged to the Reserve, with no provision for a cut-off date. It would likewise be inconsistent with the Actual Restoration Cost approach described in the 1993 Study and approved in the 1995 Order. But even if OPC's approach were permissible under the Rule and not inconsistent with the 1993 Study, it would inappropriately result in adverse incentives to rush completion of restoration work before the cut-off date. Specifically, imposing an arbitrary cut-off date for charging follow-up costs to the Reserve would run counter to FPL's approach of restoring customers quickly, which often involves taking temporary measures that require follow-up work to render such repairs permanent. Further, FPL could be required to incur substantially increased costs for enormous amounts of overtime and securing, on an expedited and cost-inefficient basis, substantial numbers of third-party contractors, to complete the follow-up work prior to the cut-off date. Such an approach would not be in the best interests of FPL's customers and would be inconsistent with the measured, cost-efficient approach currently utilized by FPL for follow-up work which includes requests for bids for specific work orders to ensure that only storm-related work is performed on the most cost-effective basis. Tr. 531 (Williams).

The record demonstrates that the notion of imposing an arbitrary cut-off date for charging costs to the Reserve has no substantive merit, violates Rule 25-6.0143(4)(b) and is inconsistent

with the 1993 Study, and would likely result in increased costs to the detriment of FPL's customers. Accordingly, it should be rejected.

ISSUE 7: Has FPL charged to the storm reserve appropriate amounts relating to employee training for storm restoration work? If not, what adjustments should be made?

Yes. No pre-storm training costs have been charged to the Storm Damage Reserve. No adjustments should be made.

Neither the record nor the parties' positions in the Prehearing Order reveals any disagreement with FPL's position that pre-storm training costs have not been charged to the Reserve and that, accordingly, no adjustments should be made. Tr. 104 (Davis).

ISSUE 8: Has FPL properly quantified the costs of tree trimming that should be charged to the storm reserve? If not, what adjustments should be made?

Yes. Only tree trimming costs incurred in conjunction with storm restoration have been charged to the Storm Damage Reserve. No adjustments should be made.

As explained by FPL's Vice President of Distribution, Geisha J. Williams, who also serves as Emergency Operations Officer during storm restorations (Tr. 507), the only costs charged to the Reserve were the costs caused by the storms. These costs arise from two phases of work - - initial, expedited and safe restoration of service and the follow-up work necessary to return the damaged infrastructure to its pre-storm state. Tr. 545 (Williams). Thus, FPL's 2004 charges to the Reserve for tree trimming relate directly to the cost of storm restoration and are properly charged to the Reserve pursuant to the Commission-approved Actual Restoration Cost approach. Tr. 111 (Davis). As discussed in Issue 3 above, there is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach.

OPC witness Majoros speculated in his prefiled testimony that the project entitled "3rd Party Assessment of Dangerous/Hazardous Vegetation Conditions" was an "... assessment to determine the relative state of vegetative conditions post-storm." **Tr. 402.** Mr. Majoros

advanced this theory despite his admitted lack of any personal involvement in managing storm restoration activities. Tr. 445. When asked about this particular adjustment, he agreed that if FPL provided sufficient detail to show that this study was performed to address problems related to the 2004 storms, then his adjustment would not be appropriate and the cost of the study should be charged to the Reserve. Tr. 454. Ms. Williams provided that detail and justification. As she explained at the hearing, "the purpose of this project was not to conduct a broad general survey of post-storm vegetation conditions but rather to assess those specific areas where vegetation removal was required as a result of the storm to identify any remaining hazardous conditions to be addressed." Tr. 514. Thus, the testimony of Ms. Williams confirmed that the cost of this project was properly charged to the Reserve and was not, by implication, a project reflecting normal, on-going tree trimming and vegetation management activities of FPL.

OPC proposes that FPL should be permitted to charge storm-related tree trimming expenses to the Reserve only to the extent that they cause FPL to exceed its budget for that activity. This adjustment is based on the "incremental" approach recommended in the OPC Storm Damage Guidelines, which should be rejected for the reasons discussed in Issue 2 above. However, even if one were to use OPC's proposed incremental approach, FPL spent all but approximately $1 million on regular (*i.e.,* non-storm) tree trimming activities in 2004, so the adjustment to remove "non-incremental" tree trimming expenses from the Reserve would be only $1 million instead of $4,220,000 as proposed by OPC.[9]

[9] Tr. 111-12 (Davis). OPC tries to avoid this conclusion by pointing out that FPL was under its budget for regular tree trimming activities by a larger amount for the 5-month period from August 2004 to January 2005. Ex. 36. However, comparing only segments of an annual budget improperly ignores any cyclical or variable impacts reflected in the full budget cycle. In fact, Mr. Majoros made his comparisons on an annual basis for the other "incremental" adjustments he has proposed. For example, he proposed to compare FPL's base salaries to what is in the "Company's *annual* budget." Tr. 402 (emphasis added). And he likewise objects to recovering vehicle expenses where, "[a]lthough Company vehicles have been used in the storm recovery effort, these vehicles have already been included in the *annual* budget." Tr. 403 (emphasis added).

ISSUE 9: Has FPL properly quantified the costs of company-owned fleet vehicles that should be charged to the storm reserve? If not, what adjustments should be made?

Yes. FPL has charged vehicle costs to the Storm Damage Reserve consistent with the methodology in the 1993 Study approved by the Commission in the 1995 Order. No adjustment should be made.

Pursuant to the Commission-approved Actual Restoration Cost approach, FPL has charged to the Reserve its 2004 vehicle costs that relate to storm restoration activities. As discussed in Issue 3 above, there is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach.

Mr. Majoros proposes to remove from the Reserve that portion of the storm-related vehicle costs that were included in FPL's 2004 budget ($5,261,887). This adjustment is based on the "incremental" approach recommended in the OPC Storm Damage Guidelines, which should be rejected for the reasons discussed in Issue 2 above. However, even if one were to use OPC's proposed incremental approach, approximately 47 percent of FPL's budgeted vehicle expenses relate to capital projects. Tr. 111 (Davis). Mr. Majoros did not dispute this calculation and agreed that it would reduce his proposed adjustment by $2.4 million. Tr. 454.

ISSUE 10: Has FPL properly determined the costs of call center activities that should be charged to the storm damage reserve? If not, what adjustments should be made?

Yes. FPL has charged incremental costs of the call center operation to the Storm Damage Reserve consistent with the methodology in the 1993 Study approved by the Commission in the 1995 Order. No adjustment should be made.

Consistent with the Commission-approved Actual Restoration Cost approach, FPL charged only incremental call center costs to the Reserve; it did not charge the normal costs of call center operations. Tr. 101, 112 (Davis); Ex. 24, p. 16. Mr. Majoros acknowledged that he has no evidence to the contrary. Tr. 470. As discussed in Issue 3 above, there is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach.

ISSUE 11: Has FPL appropriately charged to the storm reserve any amounts related to advertising expense or public relations expense for the storms? If not, what adjustments should be made?

Yes. Consistent with the methodology in the 1993 Study approved by the PSC in the 1995 Order, the only advertising or public relations expenses that were charged to the Storm Damage Reserve are safety and storm-related public service advertising. No adjustment should be made.

Consistent with the Commission-approved Actual Restoration Cost approach, FPL charged safety and storm-related public service advertising and media costs to the Reserve. Ex. 24, p. 16. As discussed in Issue 3 above, there is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach. OPC's position in the Prehearing Order is that $1,700,000 should be removed from the Reserve for advertising and media costs. However, there is no support in the record for OPC's position, and it must be rejected.

ISSUE 12: Has uncollectible expense been appropriately charged to the storm damage reserve? If not, what adjustments should be made?

FPL has not charged the Storm Damage Reserve with uncollectible accounts expense. If the Commission follows the methodology in the 1993 Study approved by the Commission in the 1995 Order, no adjustment should be made.

There is no dispute over this issue. FPL has not charged any uncollectible accounts receivable write-off expense to the Reserve. Tr. 144 (Davis). Mr. Majoros acknowledged that he has no evidence to the contrary. Tr. 471.

ISSUE 13: Of the costs that FPL has charged or proposes to charge to the storm reserve, should any portion(s) instead be booked as capital costs associated with its retirement (including cost of removal) and replacement of plant items affected by the 2004 storms? If so, what adjustments should be made?

No. FPL has appropriately accounted for additions, retirements and removal costs in accordance with the methodology in the 1993 Study approved by the Commission in the 1995 Order.

Consistent with the Commission-approved Actual Restoration Cost approach, FPL has accounted for capital costs associated with storm-related additions, retirements and removal costs

in a manner that leaves plant in service and the depreciation reserve at the pre-storm levels. Tr. 113 (Davis); Ex. 24, p. 22 (illustrates intended effect of Actual Restoration Cost approach on Plant In Service (A/C 101) and Depreciation Reserve (A/C 108)). This treatment recognizes that the reason for replacing the assets is not to improve the system, but simply to restore it to pre-storm conditions. Tr. 113 (Davis). As discussed in Issue 3 above, there is no dispute in the record that FPL recorded costs consistent with the Actual Restoration Cost approach.

As discussed in Issue 2 above, OPC would have FPL increase rate base over the pre-storm level by the amount of normal capital costs that would be incurred to restore its transmission and distribution system, rather than charging those capital costs to the Reserve. This would yield a short-term benefit to customers, by reducing the amount FPL would recover through the storm surcharge. However, customers would be harmed in the long run because base-rate revenue requirements would be increased for many years to come, ultimately costing customers more and leaving them responsible for 2004 storm costs at the same time that they face exposure to the costs of future storms. Tr. 112-17 (Davis). Further, not all of the cost of removal for the items retired will have been accrued as of the date the storm strikes. As a result, charging the storm-related cost of removal against the accumulated removal cost in depreciation would create a deficit that will have to be recognized through higher depreciation in the future. Tr. 114 (Davis).

Consistent with the Actual Restoration Cost approach, FPL has charged the Reserve for storm-related removal costs, which it estimates to be $12.2 million. Tr. 117 (Davis). In contrast, OPC proposes to reduce FPL's depreciation reserve by not just the $12.2 million in removal costs that FPL has estimated, but by a total of $36.4 million in what OPC describes as "normal"

costs of removal. OPC's proposal is wrong for three reasons: one theoretical; one practical; and another that could be described as "computational."

The theoretical flaw in OPC's proposal is that it would misuse the removal cost component of the depreciation reserve. Those removal costs are designed to recover normal end-of-service-life retirements, not premature retirement of property as a result of catastrophic events such as hurricanes. Tr. 116 (Davis). Stated another way, FPL will have the same obligation to remove the replacement equipment that was installed as part of the 2004 storm restoration work as it did with respect to the equipment that was replaced, and FPL will need the accumulated depreciation reserve to fund that removal. Tr. 236 (Davis).

The practical flaw in OPC's proposal is that there is no free lunch: the proposal would increase base-rate revenue requirements as discussed above. Customers currently benefit from the accumulated costs of removal via a decrease in net plant in service and hence rate base. If the accumulated removal costs were reduced as OPC proposes, rate base would inevitably and commensurately increase. Tr. 114 (Davis).

Finally, even if one were to use OPC's approach for handling removal costs, there is no legitimate support for its position that the "normal" level of such costs is $36.4 million. FPL reasonably estimated the removal costs as $12.2 million based on the application of its work management system. Tr. 167-68 (Davis). The relationship that the estimated removal costs bear to the original cost of the removed (retired) property (about 1:3) is similar to the relationship between the current cost of a 35-foot pole and the work management system's estimate for the cost of removing such a pole. Tr. 164-65 (Davis). OPC would substitute a roughly 1:1 relationship between removal costs and retirement costs based on nothing more than an excerpt from FPL's recently-filed depreciation study showing removal costs and retirement costs

recorded in 2003. Ex. 37. There is no information in the record to indicate the specific nature or the age of the retired plant, or the circumstances of the removals that are reflected in those 2003 figures. Tr. 164-67 (Davis). Without such information, it is impossible to draw inferences from Exhibit 37 about what "normal" removal costs might be for the equipment that was replaced as a result of the 2004 storms.[10]

ISSUE 14: Has FPL appropriately quantified the costs of materials and supplies used during storm restoration that should be charged to the storm reserve? If not, what adjustments should be made?

Yes. Materials and supplies inventory costs directly related to storm restoration activities were appropriately charged to the Storm Damage Reserve in accordance with the 1993 Study approved by the Commission in the 1995 Order. No adjustments should be made.

There is no dispute over this issue. OPC's position in the Prehearing Order is that "FPL should charge only the costs of the materials and supplies used during restoration activities to the storm reserve. It should not charge the costs of replenishing supplies and inventories to the reserve." Mr. Majoros acknowledged that he has no evidence that FPL has charged materials and supplies inventory costs to the Reserve in a manner inconsistent with OPC's position. Tr. 471. Moreover, Mr. Davis testified that virtually the entire 2004 budget for materials and supplies was spent without regard to the amounts charged to the Reserve. Tr. 112.

ISSUE 15: If the Commission does not apply in this docket the methodology applied by FPL for charging expenses to the storm reserve pursuant to the study filed on October 1, 1993 by the Company and addressed by the Commission in Order No. PSC-95-0264-FOF-EI in Docket No. 930405-EI, should the Commission take the following items into account and, if so, what adjustments should be made?

a. Revenues lost by the Company due to the disruption of customer service during the 2004 storm season or the absence of customers after the storms;

[10] Id. The debate over the proper level of "normal" removal costs illustrates nicely one of the real problems with OPC's "incremental" approach. In contrast to the Actual Restoration Cost approach, OPC's approach requires one to calculate with precision removal costs in order to determine how much of the storm restoration cost should be charged to the Reserve versus the amount charged to the depreciation reserve. The need to make this distinction invites -- in fact, virtually ensures -- the sort of "extensive debate" over the calculation and the resulting "unnecessary delays" against which the 1993 Study warned. Ex. 24, p. 12.

b. Overtime incurred by Company personnel in work areas not directly affected by the storm due to loss of some personnel to storm assignments (backfill work);

c. Costs associated with work which must be postponed due to the urgency of the storm restoration and accomplished after the restoration was completed (catch-up work);

d. Uncollectible accounts receivable write-offs directly related to the storms; and

e. Incremental contractor, outside professional services and temporary labor costs due to work postponed due to the urgency of the storm restoration and accomplished after the restoration was completed.

* Yes. If the Commission departs from the methodology in the approved study, it should take into account impacts on the Company and expenses incurred that were directly caused by the hurricanes, but not charged to the Reserve. Such impacts and adjustments would include $38.2 million in lost base rate revenues, $9.0 million in overtime (catch-up work), $6 million in uncollectible accounts receivable write-offs directly related to the storms, and $7.0 million in incremental expenses associated with contractors and outside services.*

If the Commission were to depart from the Commission-approved Actual Restoration Cost approach and utilize an "incremental" approach of the sort espoused by OPC, the record would support the following adjustments to take into account impacts on FPL and expenses incurred that were directly caused by the hurricanes, but that FPL has not charged to the Reserve:

- Lost base revenues of $38.2 million. Ex. 26; Tr. 452-53 (Mr. Majoros acknowledges that he has no reason to dispute FPL's calculation of lost base revenues);
- Backfill and catch-up work totaling $16 million. Tr. 105 (Davis) (FPL incrementally spent $7 million on contractors and outside professionals and incurred $9 million of incremental overtime during the last two months of 2004); and
- Uncollectible accounts receivable write-offs of approximately $6 million. Tr. 109 (Davis).[11]

[11] In addition to the above-referenced adjustments, as Mr. Davis testified, there should be additional adjustments based on the fact that Mr. Majoros did not account for payroll charged to cost recovery clauses or capital. Further,

Backfill work[12] and catch-up work[13] are unavoidable consequences of how FPL staffs its storm restoration. FPL operates under two different modes - - a "normal mode" and a "storm mode" of operation. Tr. 570-71 (Williams). Work done as part of normal operations and maintenance is generally not undertaken and not completed when FPL's personnel and resources are engaged in storm restoration activities. This planned, normal and on-going operations and maintenance work does not go away and is not eliminated as a result of the diversion of resources to the storm restoration efforts. Tr. 105 (Davis). Such "catch-up" work - - postponed due to the urgency of the storm restoration and repairs - - still must be performed and accomplished after the restoration was completed. Tr. 568 (Williams). Backfill work and catch-up work represent real costs of business charged to normal operating accounts (not the Reserve) and absorbed in FPL's base rates. Tr. 105-06 (Davis). Completing the backfill and catch-up work impacts normal on-going operations until the backlog is completed either through additional overtime or engaging additional contractors. Tr. 105-06 (Davis), 579-80 (Williams).

If the Commission were to abandon the methodology applied by FPL for charging expenses to the Reserve, and FPL maintains that any such action can only be implemented prospectively, then the record clearly supports consideration of the above-referenced amounts for lost base revenues, backfill and catch-up work, and uncollectible accounts receivable write-offs, in calculating the amount to be charged to the Reserve.

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there is an inconsistency between Mr. Majoros' proposed adjustment for regular salaries and OPC's guidelines which propose adjusting only bargaining unit payroll. Bargaining unit regular payroll charged to the Reserve aggregated only $9.5 million. Other adjustments would need to be made for costs normally charged to capital work and cost recovery clauses. Therefore, it is clear, even if it were appropriate to revisit the storm accounting standards in this proceeding, there are numerous issues that would have to be factored into any decision to move to the approach advocated by Mr. Majoros. Of course, these are the same types of issues that were addressed in connection with the 1993 Study that was approved in 1995. Tr. 107-08 (Davis).

[12] Backfill work is similar to catch-up work except that it is performed by a limited number of employees who remain behind during the storm restoration activities to address only the most pressing distribution related issues such as a thunderstorm caused outage.

[13] Ms. Williams provided numerous examples of catch-up work, including customer-required road widenings; and pole inspection, repair, removal and replacement. Tr. 516, 568, 572-73.

ISSUE 16: Taking into account any adjustments identified in the preceding issues, what is the appropriate amount of storm-related costs to be charged against the storm damage reserve?

$890 million.

The accounting principles adopted in the 1995 Order make sense. Pursuant to Rule 25-6.0143(4)(b) and the Commission's direction in the 1995 Order, FPL should charge all 2004 storm-related costs, as determined by the Actual Restoration Cost approach, to the Reserve. FPL commits that the storm-related costs will not exceed $890 million, which is the estimate of total storm costs. Tr. 122 (Davis); Ex. 7. Over 90% of those costs have already been paid or invoiced to FPL. Tr. 142 (Davis); Ex. 8 (approximately 93% of the $890 million was paid or invoiced as of January 19, 2005).

ISSUE 17: Were the costs FPL has booked to the storm reserve reasonable and prudently incurred?

Yes. The $890 million in costs FPL has incurred and booked to the Storm Damage Reserve were necessary, reasonable and prudent in safely and rapidly restoring service to more than 5.35 million customers (cumulative) during the most active hurricane season on record in the State of Florida. Over 90% of those costs have already been paid or invoiced to FPL.

No one has challenged the reasonableness and prudence of the costs incurred by FPL. The record overwhelmingly supports a determination that FPL acted prudently in providing a superior level of performance in responding to the three hurricanes which impacted FPL's service territory over a six-week period. FPL's prudent planning, preparedness and implementation of its storm response and service restoration procedures during the most extreme and adverse conditions, underscore not only the prudence of FPL's actions but the prudence of the costs of such actions.[14]

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[14] No party even questioned the reasonableness or prudence of the phase one storm restoration costs. While protests initially were raised by OPC concerning two projects included in the phase two follow-up costs outlined in Exhibit 27, the concerns raised by OPC witness Majoros concerning these two projects were effectively withdrawn in light

Ms. Whalin, FPL's Director of Distribution Operations Support (Tr. 11), detailed the unrebutted facts regarding the effects of the three hurricanes on FPL's infrastructure (Tr. 22-24) and FPL's performance in restoring service. Never before have three hurricanes made landfall in FPL's service territory in a single year. Despite the punishing circumstances and monumental challenges presented by these three back-to-back hurricanes, within three days following each of the three storms, FPL was successful in restoring power to more than 75% of the customers who had lost power. Tr. 35 (Whalin); Ex. 5. As Ms. Williams explained:

> the primary objective that we have is to restore power to our customers as safely and as quickly as possible. And we will bring additional resources on the property, we will open up staging sites, we will get additional contractors, we will do everything that is humanly possible to bring resources to bear to get the lights back on as quickly as possible because as a matter of principle that is what we have got to do. Our customers are counting on it, the community is counting on it. And from my perspective these costs that make that happen are reasonable and prudent, because we know that our customers are expecting it from us, we also know that government officials are expecting it from us, we expect it from ourselves. So if it speeds up the restoration... it is reasonable and prudent, because it is all about getting the customers' lights back on.

Tr. 547-48.

FPL's performance was reviewed in detail by an independent consultant, Davies Consulting, Inc. ("DCI"). DCI concluded that FPL met or exceeded standard industry practices in virtually every facet of the restoration, particularly in the areas of infrastructure performance, crew and logistics mobilization, restoration planning and implementation, and FPL's ability to restore a large percentage of customers within the first few days. In DCI's opinion, no utility

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of his acknowledgment that the costs for these projects should be charged to the Storm Reserve if they reflect work performed to address problems related to the 2004 storms. Tr. 454. Ms. Williams confirmed that all of the projects detailed in Exhibit 27: "are all associated with assessing and repairing storm damage to our facilities, including our generating plants, corporate offices, distribution and transmission facilities, and communication towers. As such, these expenses are clearly appropriate to charge to the Reserve." Tr. 521.

could have addressed the restoration effort in a six-week period as successfully as FPL. Tr. 512 (Williams); Ex. 28, p. 8 of 16.[15]

OPC and supporting Intervenors implied that FPL failed to maintain its facilities properly and speculated that two specific follow-up projects identified in Exhibit 27 were for normal maintenance activities and not directly caused by the storms.[16] OPC witness Majoros alleged without any factual basis or foundation that FPL's facilities were "old and worn out" (Tr. 402) and, by extension, inadequately maintained. Tr. 517 (Williams). The record belies that accusation. Over the past several years FPL has invested about $150 million annually for reliability enhancement projects,[17] and its average annual outage times were the best in Florida in 2003 and 2004. Tr. 517 (Williams).

FPL's investment in reliability and performance and its achievements in that area proved to be particularly important in 2004 when the three back-to-back hurricanes hit FPL's service territory. As confirmed by Ms. Williams, FPL's maintenance practices played a substantial role in the resiliency displayed by FPL's infrastructure in withstanding the impact of the hurricanes. The results speak for themselves: only 1% of FPL's million plus poles required replacement while only 1.5% of FPL's transformers required replacement, most of which was due to physical damage such as the impact of debris, not electrical failures. Tr. 517-18, 577-78 (Williams).

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[15] The Edison Electric Institute award for emergency response received earlier this year by FPL further validated the Company's industry leading expertise and superior performance during the storm season. Tr. 511-12 (Williams).

[16] As Ms. Williams explained, there are two phases to hurricane restoration. The first phase involves restoring customers' electric service as safely and quickly as possible, even if accomplishing that goal requires necessary increases in cost that would not typically be incurred under normal operations. Tr. 509-10. The second phase involves the follow-up work necessary to restore the infrastructure to its pre-storm or pre-failure state. Tr. 545.

[17] Contrary to the unsupported allegations of Mr. Cline at the Melbourne service hearing, over the past 15 years, FPL has substantially increased its maintenance activities with regard to its infrastructure including increased levels of vegetation management and conducting thermovision. These increased levels of maintenance and service quality have been achieved despite substantial reductions in employee levels, confirming that FPL has succeeded in improving service quality and reliability on a cost-effective basis. Tr. 559-60 (Williams).

Finally, FPL has no incentive to engage in the type of maintenance deferral suggested by the Intervenors. The deferral of system maintenance would only result in increased costs and associated risks with not conducting maintenance in a timely manner. Tr. 517, 553 (Williams).

In sum, the unrefuted evidence demonstrates that FPL's facilities performed exceedingly well in withstanding the impact of the three major hurricanes. Mr. Davis' and Ms. Williams' testimony confirm that only costs directly arising from the storms were charged to the Reserve.

Though Intervenors may suggest otherwise, now is the time to conclude that the costs charged to the Reserve relative to the 2004 storm season are reasonable and prudently incurred. Although the initial request for recovery filed in November 2004 necessarily was based on estimated costs at the time, the description of activities and the nature and categories of costs were fully documented, audited and addressed through discovery conducted by Intervenors in this proceeding. More importantly, over time, as more invoices were received, it became possible to provide a firmer estimate. That estimate, net of insurance proceeds, is $890 million, over 90% of which already has been paid by FPL or invoiced to FPL. Tr. 142 (Davis); Ex. 8.

Parties to this Docket have been provided, or have had access to every piece of paper in the Company's possession that underlies this request. While there will be a true-up of the surcharge at the end of the recovery period to ensure only that no more than the authorized amount of storm damage costs in fact are collected, that should be limited to the simple mathematical computation – not an excuse to reopen and re-litigate matters that were or could have been properly raised and addressed under Issue 17.

ISSUE 18: Is FPL's objective of safe and rapid restoration of electric service following tropical storms and hurricanes appropriate? (Policy issue)

*Yes. FPL's efforts and its approach to restoration were consistent with the overarching public policy favoring prompt and safe restoration of electric service, consistent with the unwavering

and oft-repeated expectations of state and local government, and consistent with the regulatory framework instituted by the Florida Public Service Commission following Hurricane Andrew.*

As emphasized by Ms. Whalin, "[t]he primary objective of FPL's emergency preparedness plan and restoration process is to safely restore the greatness number of customers in the least amount of time." Tr. 14 (Whalin). FPL's objective is matched by the objectives and expectations of state policymakers, the Governor, Secretary Castille, legislators, local government officials and regulators who continually focused on the need to restore power as quickly as possible during the 2004 storm season, and facilitated the Company's ability to do so through such actions as granting weigh station waivers, providing law enforcement escorts, mapping routes around damaged bridges, and expediting necessary permits. Tr. 25 (Whalin), 713 (Dewhurst). Simply put, FPL and government officials from all levels including the Governor, did whatever it took to restore service as quickly and safely as possible. FPL's actions and the expectations of government officials were reinforced at the hearing by Ms. Williams. Tr. 545-46. The expectations of government officials and emergency operations coordinators are real. As the Commission repeatedly heard at the customer service hearings, their expectations were met or exceeded by FPL's commitment, dedication and performance.

ISSUE 19: Does the stipulation of the parties that the Commission approved in Order No. PSC-02-0501-AS-EI affect the amount or timing of storm-related costs that FPL can collect from customers through the proposed surcharge? If so, what is the impact? (Legal issue)

* FPL's request is consistent with, and expressly contemplated by, the Stipulation and Settlement that was executed by all parties to this proceeding, including OPC, in Docket No. 001148-EI, and approved by the Commission in Order No. PSC-02-0501-AS-EI. The Stipulation and Settlement establishes a regulatory mechanism that constitutes the "appropriate and exclusive mechanism to address earnings levels" and expressly contemplates that FPL would have the opportunity to recover expenditures incurred in the event of an extraordinary storm season.*

Intervenors contend that the Company's shareholders should "share" some portion of the reasonable and prudently incurred costs of storm restoration based, in part, on an incorrect and

untenable interpretation of the Stipulation and Settlement that was negotiated by OPC and FPL, signed by OPC, FPL and all but one party to FPL's last rate proceeding, including FIPUG, FRF and Twomeys, and approved by the Commission in Order No. PSC-02-0501-AS-EI, Docket Nos. 001148-EI and 020001-EI (issued April 11, 2002) (hereinafter "Stipulation and Settlement").[18] Tr. 693 (Dewhurst); Ex. 30. They assert that the provision in paragraph 8 of the Stipulation and Settlement, which provides a mechanism for general base rate relief if FPL's return on equity ("ROE") drops below 10%, requires that FPL absorb the negative balance in the Reserve through earnings to the extent that 2004 earnings exceed 10% ROE. Tr. 260-61 (Rothschild), 320-21, 326, 335; Ex. 30, ¶ 8. This interpretation is wrong.

OPC's interpretation, adopted by the other Intervenors, is inconsistent with the plain language of the Stipulation and Settlement and ignores key provisions of the document, effectively depriving the Company of a significant portion of the protections and benefits the Company was to receive in exchange for agreeing to a $250 million annual reduction in base rates. Tr. 693, 695-702 (Dewhurst); Ex. 2 (FPL's supplemental response to OPC's Sixth Request for Production of Documents No. 43). The Stipulation and Settlement establishes a regulatory mechanism that constitutes the "appropriate and exclusive mechanism to address earnings levels" and expressly contemplates that FPL would have the opportunity to recover expenditures incurred in the event of an extraordinary storm season. Tr. 695 (Dewhurst); Ex. 30, ¶¶ 5, 13 (emphasis supplied).

A. OPC's interpretation contradicts the unambiguous language of the Stipulation

OPC and the other Intervenors' contention that FPL should expense storm costs down to a 10% earned return for 2004 ignores the plain language of the Stipulation and Settlement.

[18] The Stipulation and Settlement is effective from April 15, 2002 through December 31, 2005. Ex. 30.

As a result of negotiations with OPC, and as reflected in Order No. PSC-02-0501-AS-EI and the Stipulation and Settlement, FPL agreed to a base rate reduction of $250 million annually and sharing of revenues with its customers in the form of a refund when revenues reached a specified threshold. Ex. 30 at ¶¶ 2, 6-7. Further, FPL agreed to withdraw its request for an increase in the annual accrual to its Reserve that would have increased the Reserve and further protected its customers against having to seek a special assessment in the event of extraordinary losses in excess of the Reserve.[19] Tr. 695-696 (Dewhurst); Ex. 2 (FPL's supplemental response to OPC's Sixth Request for Production of Documents No. 43).

In exchange for FPL's agreement to reduce base rates annually, share revenues above a certain threshold, and withdraw its request for increased accruals to the Reserve, FIPUG, OPC and the other parties to the Stipulation and Settlement agreed that FPL would "no longer have an authorized Return on Equity (ROE) range for the purpose of addressing earnings levels." Ex. 30, ¶ 3. "[T]he revenue mechanism herein described will be the appropriate and exclusive mechanism to address earnings levels." Id. (emphasis added). Regarding the Reserve, the parties, including OPC and FIPUG, specifically agreed as follows:

> In the event there are insufficient funds in the Storm Damage Reserve and through insurance, FPL may petition the FPSC for recovery of prudently incurred costs not recovered from those sources. The fact that insufficient funds have been accumulated in the Storm Damage Reserve to cover costs associated with a storm event or events shall not be evidence of imprudence or the basis of a disallowance. Parties to this Stipulation and Settlement are not precluded from participating in such a proceeding.

Ex. 30, ¶ 13 (emphasis added). The Commission found that "the Stipulation and Settlement is in the best interests of FPL's ratepayers, the parties, and FPL, and is therefore approved." See Order No. PSC-02-0501-AS-EI, p. 5, Docket No. 001148-EI (issued April 11, 2002).

[19] See Order No. PSC-02-1850-PAA-EI, p. 2, Docket No. 021164-EI (issued Dec. 27, 2002) (noting that "In Paragraph 13 of the Stipulation and Settlement, FPL withdrew its request for an increase in the annual accrual to the

Intervenors' position would render meaningless, or at least superfluous, paragraph 13 of the Stipulation and Settlement. Neither the 10% condition in paragraph 8 nor paragraph 13 refers to one another in the Stipulation and Settlement. Tr. 699 (Dewhurst); Ex. 30, ¶¶ 8, 13. The 10% condition is quite general: it encompasses all factors that might cause the Company's earned return to drop below 10%. Id. Thus, even in the absence of paragraph 13, FPL would have the right to petition for relief in the event that the storm fund balance becomes negative and FPL's ROE falls below 10%. If the specific language in paragraph 13 addressing the right to seek rate relief is to be given any meaning, it must be capable of applying even if the 10% condition is not met. Tr. 699 (Dewhurst); Ex. 30. A contrary interpretation would violate well-established principles of contract law. See, e.g., City of Homestead v. Johnson, 760 So. 2d 80, 84 (Fla. 2000) (courts are required to read provisions of a contract harmoniously in order to give effect to all portions thereof); Aucilla Area Solid Waste v. Madison County, 890 So. 2d 415, 416-17 (Fla. 1st DCA 2004); Peoples Gas System v. City Gas Co., 147 So. 2d 334, 336 (Fla. 3d DCA 1962) ("No word or part of an agreement should be treated as a redundancy or surplusage if any meaning reasonable and consistent with other parts can be given to it").[20]

In addition to ignoring substantial language that does exist in the Stipulation and Settlement, OPC's position reads language into paragraph 8 that simply does not exist. Nowhere in the text of paragraph 8 does it state that FPL's request would only be granted to the extent necessary to bring its earnings back to 10%. Ex. 30; Tr. 302 (Rothschild). Yet, such a clause appears to be the gravamen of OPC's position that would cap FPL's recovery of storm costs.

Reserve for Storm Damage).

[20] It defies logic that Mr. Rothschild, although testifying in two separate dockets on substantively identical matters, involving two separate settlement agreements that were largely similar but for the existence of paragraph 13 in FPL's Stipulation and Settlement, would not have bothered to ask anyone about paragraph 13. Tr. 305-306.

FPL's petition for authority to recover the prudently incurred storm restoration costs related to the 2004 storm season that exceed the Storm Reserve balance is expressly permitted by the plain language of the Stipulation and Settlement. Tr. 695 (Dewhurst); Ex. 30.

B. OPC's interpretation contradicts the intent of the parties regarding the Stipulation

OPC's interpretation not only conflicts with the plain language of the Stipulation and Settlement, but is contrary to what the parties intended as clearly evidenced by the circumstances surrounding the negotiation and adoption of the Stipulation and Settlement. FPL witness Moray P. Dewhurst was the Company's Chief Financial Officer at the time FPL negotiated and received management approval to sign the Stipulation and Settlement, and he was responsible for evaluating the financial and risk management consequences of the agreement. Tr. 693-94 (Dewhurst). In that role, Mr. Dewhurst was fully aware of, and approved, the exchange of concessions or quid pro quo by which the Stipulation and Settlement was reached, which included FPL's agreement to a $250 million annual base rate reduction that involved the Company's agreement to withdraw its prior request for an increase in the annual storm accrual in order to offer the magnitude of base rate decrease sought by OPC. Tr. 693-94 (Dewhurst).[21]

Pursuant to the Stipulation and Settlement, OPC and its constituents, including the other Intervenors in this proceeding, have received annual base rate decreases of $250 million, and an opportunity for refunds should FPL's revenues exceed certain threshold amounts. As a result of these concessions, FPL's customers will have realized approximately $1 billion in savings and refunds through calendar year 2005, the end of the Stipulation and Settlement. Tr. 695-96 (Dewhurst). In exchange for these benefits, FPL sought and obtained certain protections in the

[21] No attorney representing OPC in this proceeding or witness appearing on OPC's behalf was involved in negotiating the Stipulation and Settlement on OPC's behalf, and no such witness asked anyone who actually negotiated the agreement on OPC's behalf about the intent or effect of paragraph 13. Tr. 305-06, 452, 694

form of conditions. First, as noted above, FPL was to "no longer have an authorized Return on Equity (ROE) range for the purpose of addressing earnings levels." Tr. 294, Ex. 30, ¶ 3. In fact, it was clearly agreed that "the revenue mechanism ... [was to] be the appropriate and exclusive mechanism to address earnings levels." Tr. 292-93; Ex. 30, ¶ 3 (emphasis added).[22] Second, FPL sought a general level of protection by reserving the right to petition the Commission for rate relief due to earnings falling below 10%. Ex. 30, ¶ 8. Third, FPL needed specific assurance that excess storm costs, to the extent reasonably and prudently incurred, could be recovered during the term of the Stipulation and Settlement. Ex. 30, ¶ 13.

To support its position, OPC focuses only on the second condition, ignoring the purpose and effect of the other two. Tr. 696 (Dewhurst). Each of the three conditions identified above was essential to FPL's willingness to agree to a $250 million annual base rate reduction. As Mr. Dewhurst testifies, the third condition was added late in the negotiations as part of the final quid pro quo that enabled an agreement to be struck. OPC was insistent that there be a large base rate reduction. To help fund the large base rate reduction required to obtain a settlement, FPL had to agree to withdraw its then pending request to increase the annual storm accrual by $30 million. Tr. 696-97 (Dewhurst).[23] But, FPL was not willing to accept the specific risk of excess storm

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(Dewhurst); Ex. 33 (OPC's responses to FPL's First Requests for Admissions). The witnesses merely relied on the advice of OPC attorney McGlothlin. Tr. 307. There is no record evidence of OPC's intent relative to paragraph 13.

[22] Mr. Rothschild incorrectly testified that the Stipulation and Settlement provided the Company with the opportunity for unlimited earnings, but subsequently acknowledged the existence of a revenue cap and sharing thresholds in paragraph 3 of the Stipulation and Settlement –something that he had not focused on --, agreeing that the mechanism operated as a practical ceiling on FPL's earnings during the term of the agreement. Tr. 292-93.

[23] Mr. Dewhurst's testimony regarding withdrawal of the request to increase the annual Reserve accrual by $30 million in exchange for the protection in paragraph 13 and the language in paragraph 3 is confirmed by FPL's response to OPC's Sixth Request for Production of Documents No. 43, included in Ex. 2. The request asked for documents evidencing the "quid pro quo" discussed in Mr. Dewhurst's testimony. The document produced was a settlement document dated January 14, 2002, which clearly shows in item 8 of that document that FPL was still seeking an increase in the accrual of $30 million. In addition, the document includes an authorized return on equity in item 2, including a 10% floor, but does not include the protection related to recovery of deficiencies in the Reserve that is in Paragraph 13 of the Stipulation and Settlement. Ex. 2 (FPL's supplemental response to OPC's Sixth Request for Production of Documents No. 43).

restoration costs while under a fixed base rate agreement, -- even under a draft agreement that already contained a general mechanism for relief if ROE dropped below 10%. Tr. 697 (Dewhurst); Ex. 2. Therefore, FPL proposed, and OPC accepted, adding the third condition reflected in paragraph 13. Id.; Ex. 30. There is no record evidence contradicting or even challenging Mr. Dewhurst's testimony in this regard.

If OPC's contention is correct that the 10% threshold applies also to extraordinary storm losses, then the specific language reflected in paragraph 13 would have been totally unnecessary. But, Mr. Paul Evanson, then president of FPL and also involved in management approval of the terms of the Stipulation and Settlement, clearly emphasized the importance of paragraph 13 at the March 22, 2002, Special Agenda Conference where the Commission considered the Stipulation and Settlement.[24] Certainly, the intent was that FPL would have the right to petition for rate relief, even during a period of otherwise fixed base rates, if storm restoration costs

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[24] At that Agenda, the following exchange was held between Commissioners and Mr. Evanson:

> Commissioner Baez: ... [I]s Section 13 creating a right of recovery that didn't exist before? ... [I]s the agreement offering you the ability to come back and, [] recover prudently incurred costs in excess of whatever the storm reserve was that didn't exist before?
>
> Mr. Evanson: ... Well, no, it doesn't change, I think, what was there before. Actually, what makes the most economic sense, and I think what we came in and requested some time ago from the Commission after Hurricane Andrew was, was an agreement or a rule from the Commission that to the extent that there were losses, significant losses from the storm, that we would have the ability to recover them via a clause over a three-to-five year period. ... But the Commission at that time said that that logic made a lot of sense and, to the extent you are short, why don't you come in and we'll talk about it then? And I think what this is doing is continuing that same logic. So there's not a change in my mind in the substance of where we were before that provision.
> ...
>
> Commissioner Bradley: [S]o then the Commission should assume then that you have sufficient funds to cover a catastrophic event at this time in this particular reserve fund?
>
> Mr. Evanson: No. [W]e have what we think is adequate for most occurrences. But I could tell you surely if a storm like Hurricane Andrew hit Miami and came right up the east coast through Palm Beach, there would not be nearly enough assets in that fund in insurance and it would be a significant impact to the company, and there's no doubt I would be here before you asking for some kind of special relief on it because you could be talking about billions of dollars in that case.

Tr. 698 (Dewhurst).

caused the Reserve balance to become negative, regardless of the then-prevailing ROE level. Tr. 699 (Dewhurst).

Mr. Shreve, Public Counsel at the time who negotiated the Stipulation and Settlement and recommended it for approval by the Commission, concurred in the discussion relative to paragraph 13. Immediately following the exchange with Mr. Evanson relative to paragraph 13, the Chairman asked: "Mr. Shreve, we've had some discussion this morning. Is there anything that you've heard this morning that changes your opinion or your involvement in this settlement being, in your opinion, a good settlement?" Mr. Shreve replied, "No, Commissioner, there's not." Tr. 700 (Dewhurst).[25] Significantly, Mr. Shreve did not attempt to clarify that FPL's right to seek relief for extraordinary storm costs was limited or in any way conditioned by the 10% threshold, a point that would have been most obvious and appropriate for him to make at the time had it truly been OPC's understanding as OPC contends today.

Paragraphs 8 and 13 each was to provide FPL with certain rights under the Stipulation and Settlement in exchange for a large base rate reduction. It is fundamentally wrong for OPC to interpret these provisions in a way that uses one of the paragraphs to circumscribe the benefits of the other. In other words, OPC is using paragraph 8 to make FPL worse off than if paragraph 8 did not exist, even though paragraph 8 was intended only to protect FPL. Tr. 700 (Dewhurst).

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[25] That OPC developed its interpretation of the Stipulation and Settlement in a vacuum, unconstrained by extrinsic evidence contrary to its position, is evidenced by the fact that OPC's witness Rothschild did not even know whether OPC had advocated before the Commission or anyone whether the Stipulation and Settlement was a good deal. Tr. 287. Further, despite the Company's reliance on paragraph 13 and OPC's awareness that paragraph 13 forms the basis for FPL's petition to recover storm costs that exceed the Reserve balance, OPC's witness Rothschild used his testimony in the Progress Energy Florida ("PEF") storm docket as a template for his testimony in this proceeding and "most of the words [in the two testimonies – PEF and FPL] are the same." Tr. 303-05. However, the PEF and OPC settlement agreement that resolved PEF's last rate proceeding, though similar to FPL's Stipulation and Settlement, does not include paragraph 13. See Order No. PSC-02-0655-AS-EI, Ex. A, Docket No. 000824-EI (issued May 14, 2002). Despite this significant difference in the two dockets, Mr. Rothschild's testimony is "essentially identical" to that filed in the PEF proceeding and his recommendations are the same. Tr. 304-05.

The explicit agreement was that FPL would concede the $250 million per year rate reduction only on condition that: FPL would have the right to "petition the FPSC for recovery of prudently incurred costs not recovered from [the Storm Damage Reserve and insurance coverage]"; that "[t]he fact that insufficient funds have been accumulated in the Storm Damage Reserve to cover costs associated with a storm event or events shall not be ... the basis of a disallowance"; and that "the revenue mechanism herein described [--not excess storm restoration costs --] will be the appropriate and exclusive mechanism to address earnings levels." Tr. 701; Ex. 30, ¶¶ 3, 13. But if OPC's position is accepted, FPL would: (a) have no right to rate relief without reference to a 10% earnings level, (b) face a significant disallowance, the effective result of not having had sufficient funds accumulated in the Storm Damage Reserve, and (c) have its earnings levels "addressed," if not lowered, by reference to something other than the Stipulation and Settlement's revenue mechanism. These were key conditions to FPL's acceptance of the Stipulation and Settlement. Tr. 701-02 (Dewhurst).

Intervenors are asking the Commission to reinterpret the Stipulation and Settlement after they have enjoyed the benefits of the past two agreements (1999 and 2002) through rate reductions and refunds to customers totaling nearly $4 billion through the end 2005. This would be bad policy. Utilities will be naturally reluctant to enter into agreements if they feel they cannot rely on the plainly expressed terms being upheld. Intervenors' interpretation of the Stipulation and Settlement must be rejected to encourage future negotiated settlements. Tr. 727 (Dewhurst).[26]

ISSUE 20: **In the event that the Commission determines the stipulation approved in Order** No. PSC-02-0501-AS-EI does not affect the amount of costs that FPL can recover from ratepayers, should the responsibility for those costs be apportioned between

[26] **Mr. Rothschild agrees that settlement agreements should be adhered to and honored so as to engender the** necessary respect for the process among companies, the investment community, as well as customers. Tr. 316-17.

FPL and retail ratepayers? If so, how should the costs be apportioned? (Legal issue)

No. The recovery from customers of all reasonable and prudent costs associated with storm restoration is central to the cost-of-service approach to regulation followed in Florida. Storm restoration costs are a cost of providing electric service in Florida and, as such, are properly recoverable from customers. There should be no apportionment of costs between the Company and its customers. Customers are the direct beneficiaries of the Company's restoration efforts.

Irrespective of the Stipulation and Settlement, Intervenors' proposed application of an earnings test for storm recovery is inconsistent with the sound regulatory framework instituted by the Commission following Hurricane Andrew and the dissipation of commercially available insurance is inappropriate as a matter of cost-of-service regulation, and inconsistent with public policy favoring safe and rapid restoration of service. The PSC has established and consistently endorsed an overall framework that acknowledges that the costs associated with restoring service after tropical storms and hurricanes are a necessary cost of doing business in Florida and as such are properly recoverable from customers. Tr. 589-590 (Avera), 700-10 (Dewhurst).

A. OPC's earnings test is inconsistent with the Commission's regulatory framework

Prior to Hurricane Andrew FPL had a small storm damage reserve and maintained commercial insurance coverage for its T&D network in the amount of $350 million per occurrence. The costs of carrying this insurance, a bona fide cost of doing business, were recovered through base rates. The cost of storm restoration, therefore, was borne by customers through the cost of insurance. Tr. 703 (Dewhurst).

Following Andrew, commercial insurers recognized that they had fundamentally misunderstood the nature of utility windstorm coverage and effectively withdrew from the market. In the absence of commercial coverage, FPL, with the Commission's approval, instituted an approach that relied more heavily on the Reserve, the existence of which pre-dated Andrew. In 1993, the Commission rejected "at this time" FPL's proposal to implement an

automatic revolving storm clause, to operate in perpetuity addressing all future storm costs. See The 1993 Order, p. 5. Instead, the Commission approved a self-insurance mechanism for FPL as a means of addressing the need for comprehensive storm recovery. The Commission determined that the inclusion of an annual accrual amount in base rates, coupled with the ability to request a specific recovery mechanism in the event of a shortfall, should provide sufficient protection to the Company and its customers. Id.[27] The Commission instructed FPL, in part, as follows:

> If FPL experiences significant storm-related damage, it can petition the Commission for appropriate regulatory action. In the past, the Commission has acted appropriately to allow recovery for prudent expenses and has allowed amortization of storm damage expense. Extraordinary events such as hurricanes have not caused utilities to earn less than a fair rate of return, and FPL has shown no reason to believe that the Commission will require a utility to book exorbitant storm losses without recourse. ...
>
> The Commission will expeditiously review any petition for deferral, amortization or recovery of prudently incurred costs in excess of the reserve. Our vote today does not foreclose or prevent further consideration at a future date of some type of a cost recovery mechanism, either identical or similar to what has been proposed in this petition. The Commission could implement a cost recovery mechanism, or defer the costs, or begin amortization, or such other treatment as is appropriate, depending on what the circumstances are at that time.

Id.

Therefore, the Commission endorsed an approach, confirmed and clarified in subsequent orders, consisting of three parts: (1) an annual storm accrual, adjusted over time as circumstances change; (2) a funded Storm Damage Reserve adequate to accommodate most but not all storm years; and (3) a provision for utilities to seek recovery of costs that go beyond the balance in the Reserve. Tr. 704 (Dewhurst), 802-07, 812-19. These three parts act together to allow FPL over time to recover the full costs of storm restoration, while at the same time balancing potentially competing customer interests: as small an ongoing impact on customer bills as possible;

[27] In Docket No. 930405-EI, OPC agreed that "If a hurricane strikes, FPL can petition for appropriate regulatory treatment at that time." See Prehearing Statement of the Office of Public Counsel, at 1, Docket No. 930405-EI, filed

minimal volatility or "rate shock" in customer bills because the Reserve is insufficient; and intergenerational equity. Tr. 704.

Pointing to select provisions of the 1993 Order out of context, the Intervenors incorrectly contend that the 1993 Order controls the disposition of FPL's Petition. Yet, their position ignores a few key facts. First, in Docket No. 930405-EI, the Commission did not vote on the issue of whether earnings should be considered when ruling on a request for storm recovery because that issue was rendered moot. Tr. 684-85; Ex. 51, pp. 25-31. Second, by express language in the 1993 Order, the Commission did not preclude itself from considering a surcharge proposal such as the one proposed by FPL. Tr. 806. Third, the 1993 Order directed FPL to continue to try to locate some level of commercial insurance for T&D facilities on the premise that some reasonable amount of coverage might be available.[28] Fourth, the PSC issued several orders subsequent to 1993 Order relative to the Storm Damage Reserve and the self-insurance framework. Intervenors and their witnesses ignore all of that precedent. In fact Mr. Rothschild, the only witness in opposition to FPL on this issue was completely ignorant of other subsequent Commission orders addressing the Reserve or accrual. Tr. 319.[29]

In the same docket in the 1995 Order, the Commission considered a range of variations on the self-insurance framework and opted for one that was intended to maintain the overall framework, but reduce the reliance on special assessments. Significantly, two other options were considered but rejected. One would have increased the accrual to the amount of the expected annual loss with no dependence on special assessments. The other would have eliminated the annual accrual and relied exclusively on special assessments.

May 14, 1993.

[28] As indicated in PSC decisions subsequent to the 1993 Order, it has become clear since 1993 that commercial insurance is not reasonably available to FPL to insure against storm damage to T&D facilities. Tr. 794-96; 812-20.

Over the years, the Commission periodically has reviewed the levels of the target Reserve amount and the annual accrual and, in some instances, has increased those amounts.[30] In 1998, the Commission explicitly considered the adequacy of the $20.3 million accrual then (and still) in effect as well as the target amount of the Reserve. Weighing the types of interests described above, the Commission rejected the proposed increase in the accrual, concluding that no changes were needed at that time. However, consistent with the post-Andrew regulatory framework, the Commission acknowledged that:

> [i]n the event FPL experiences catastrophic losses, it is not unreasonable or unanticipated that the reserve could reach a negative balance. ... The December 1997 balance of $251.3 million, is, we believe, sufficient to protect against most emergencies. In cases of catastrophic loss, FPL continues to be able to petition the Commission for emergency relief, as reflected in Order No. PSC-95-1588-FOF."

See Order No. PSC-98-0953-FOF-EI, p. 3, Docket No. 971237-EI (issued July 14, 1998). In that decision the Commission also affirmed that:

> the costs of storm damage incurred over and above the balance in the reserve and the costs of the use of the lines of credit would still have to be recovered from ratepayers.

Id.; Tr. 812-20.[31]

Since Hurricane Andrew, this framework has operated to keep customer rates lower than they otherwise would have been, because the annual accrual has been significantly less than the expected annual costs of restoration. This concept was discussed at the hearing.[32]

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[29] Mr. Rothschild does not recall asking for or being given any order other than the 1993 Order to prepare his testimony in this proceeding. Tr. 319.

[30] Excerpts from several of those decisions were referenced by Mr. Dewhurst at the hearing. Tr. 802-19.

[31] Mr. Dewhurst was questioned about the 1995 Gulf Power Company ("Gulf") Order, Order No. PSC-96-0023-FOF-EI, issued January 8, 1996 in Docket No. 951433, in which the PSC approved Gulf's request to apply to Gulf's Storm Reserve all earnings that exceeded the then-existing 12.75% ROE cap governing Gulf's rates. As Mr. Dewhurst explained, within the context of the earnings cap governing Gulf's rates, the exact disposition of any excess earnings was left to the PSC's discretion. Under those company-specific circumstances, Gulf's request and the PSC's action was contemplated within Gulf's framework. Tr. 780-84. As discussed in detail in Issue 19 above,

FPL's lower than necessary annual accrual over the past decade has only been possible because of the very favorable storm experience. Until now, FPL has never had to call on the third part of the framework, the right to petition for emergency relief. Tr. 706 (Dewhurst).

B. OPC's earnings test is inappropriate under cost-of-service regulation

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the framework for FPL is that there is no ROE range and it is specifically contemplated that FPL will seek recovery of reasonable and prudently incurred storm costs that exceed the balance of the Reserve. Ex. 30, ¶¶ 3, 13.

[32]

> COMMISSIONER DEASON: [s]o it has been the Commission's position to establish the reserve, to fund it, to allow accruals, but those accruals historically have been conservative such that it does not place any unnecessary burden on customers.
>
> [Mr. Dewhurst] Generally. One of the other criteria that the Commission has clearly looked at, if you go through the old orders, and I think it makes a lot of sense, is to target a level in the storm reserve that will be enough to cover most years, but not the most extreme year. ... [T]hat number has changed over time. The definition of exactly what that constitutes, is an Andrew like storm or is it something else, has changed. But conceptually, the Commission has used that as another guidepost.
>
> COMMISSIONER DEASON: Well, one way to ensure that even catastrophic events are covered would be to obtain insurance, which was the previous policy, pre-Andrew policy; correct?
>
> [Mr. Dewhurst]: Yes, sir.
>
> COMMISSIONER DEASON: And the Commission reviewed that, with the help of the companies and the intervenors and made a decision that a self-insurance program with a reserve is better for customers and more cost-effective than to continue the old regime of paying insurance premiums.
>
> [Mr. Dewhurst]: Yes, that's correct. And as a practical matter, insurance for a while just totally disappeared. One of the other things the Commission has required is that we continue diligently to, you know, sound the market for commercially reasonable insurance, which we do. And I believe in the period '98 to 2001 we had a little slice of coverage. But the last number that I recall was a quote of about 35 million annual premium for 100 million of coverage, so that is obviously not a very attractive proposition. ... As a practical matter [insurance is] just not economically available today. ...
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> COMMISSIONER DEASON: If, and I emphasize if, if it were the decision of this Commission that we never wanted to see even the remote possibility of having a surcharge on customers again as a result of a catastrophic hurricane event, we would – insurance is not available, so we would have to fund the reserve at what you may term a high level, which potentially could be burdensome to customers or economically [in]efficient [sic]?
>
> [Mr. Dewhurst]: Yes, sir. ... If you literally had no commercial insurance ... you would need a surplus of – thinking of it from an insurance company perspective, you would need a surplus of a billion or $2 billion to support that kind of risk. That billion or $2 billion will be sitting on the balance sheet earning modest returns, because you've got to have the liquidity there, the funds available if there is a storm. That's just not a good proposition.

Tr. 793-96.

Apart from maintaining adequate utility service, the opportunity to recover reasonable and necessary expenditures, such as those associated with FPL's extraordinary storm restoration efforts, is central to the cost-of-service approach to regulation adopted in Florida and elsewhere in this country. Tr. 590 (Avera). The Intervenors' suggestion that there should be a "sharing" of reasonably and prudently incurred costs of service between FPL and its customers should be rejected as inconsistent with the regulatory **compact.**[33] Tr. 589-90 (Avera); Ex. 47, pp. 7-31. Intervenors suggest that OPC's approach allows the "recovery" of costs. But Mr. Rothschild conceded that there is no difference in the financial outcome of ordering a utility to expense an amount sufficient to reduce its earnings to a predetermined level and disallowing recovery of the same amount based on a finding of imprudence. Tr. 313-16.

OPC's witness Mr. Rothschild also incorrectly contends that FPL should be required to bear "a portion of the risk associated with extraordinary storm casualty losses" and that this is "fully consistent with the nature of business risks and investments." Tr. 263. As Mr. Dewhurst notes, Mr. Rothschild conflates two quite distinct concepts in his testimony: risk and cost. The entirely foreseeable costs of restoring power after a tropical storm are an integral part of the cost of providing electric service in Florida, a region susceptible to tropical storms and hurricanes. As such, they are legitimately recoverable from customers under the basic principles of regulation addressed above.[34] FPL does not now (and has not since Andrew) recovered through base rates the full expected costs of restoring service after storms, a fact that Mr. Rothschild and

[33] Mr. Dewhurst and Dr. Avera flatly rejected OPC's suggestion that FPL could be required to absorb all storm costs down to a 10% ROE for 2004, yet still recover all its costs. Tr. 754; Ex. 47, pp. 16-17. Tr. 589-592 (Avera); Ex. 47, pp. 7-31.

[34] Mr. Rothschild agrees that reasonable and prudently incurred storm costs are a cost of providing electric service. Tr. 327-29.

Intervenors simply ignore.[35] Nor does FPL recover through base rates the amounts that would be necessary to compensate for the risk capital that would need to be supplied were investors to assume an insurance function, which is what OPC and Mr. Rothschild are effectively proposing. But an integral part of that framework is the ability of the utility to recover prudently incurred costs in excess of the Reserve balance at the precise moment that hurricanes strike, for this balance is inevitably a matter of chance. Tr. 707-08, 715-24 (Dewhurst), 754.

Mr. Rothschild also glosses over the important question of whether investors have been compensated or are compensated to take on the specific risks that he proposes. In this case, the answer is clearly no. A reasonable reading of the history of Commission orders would clearly not lead a prudent investor to conclude that the Commission was employing the framework now proposed by OPC and the other Intervenors and endorsed by Mr. Rothschild. Tr. 708. Mr. Rothschild, not having reviewed any Commission orders other than the one OPC's counsel gave him, nor having reviewed any equity analyst reports prior to filing his testimony, is not in the best position to suggest anything to the contrary.[36] Tr. 317-21. Yet his recommendations, if accepted, would result in FPL having to restate its earnings for 2004,[37] clearly a result unintended by the Stipulation and Settlement and wholly unanticipated by investors.

Moreover, whereas risk and reward are rudiments of the same financial concept, even Mr. Rothschild acknowledges that there is no upside or profit potential for FPL's shareholders associated with the Reserve during non-storm years. Tr. 332-35. Intervenors' position would

[35] Yet Mr. Rothschild agrees that if the average annual expected loss due to storms were $70 million, and the annual accrual was only $20 million, the expected storm costs would not be built into base rates and "there would be a $50 million loss on average." Tr. 331-32.

[36] In fact, despite Mr. Rothschild not having done so himself, he agreed that an investor who wanted to assess a utility's regulatory risk with respect to a particular matter would review relevant Commission orders. Tr. 317-18.

[37] Tr. 309 (Rothschild). Although asserting that shareholders were compensated for the specific risks of potentially having to absorb the reasonable and prudently incurred costs of hurricane restoration above the amount in the Reserve, Mr. Rothschild did not know the amount of the annual accrual, and did not even know whether the Reserve

imply only risk, and no reward for shareholders. In contrast to general expenses, with respect to which utilities can improve their earnings through productivity and other efficiency enhancements, FPL realizes no profit or earnings increases due to an inactive hurricane season. Tr. 293-94, 332-35.[38]

Regulators and customers should be concerned about investors' perceptions because investors' assessment of regulatory support and risk has a direct impact on FPL's financial strength and ability to attract capital. Tr. 607, 611 (Avera). FPL expert witness Dr. Avera testified:

> OPC's proposal to engineer a backdoor reduction in FPL's ROE through a novel reinterpretation of the stipulation would send an alarming message to investors at the very time when FPL must attract the capital necessary to meet the needs of a growing service area.

Id. (emphasis added). FPL faces a number of potential challenges that might require the relatively swift commitment of considerable capital resources in order to maintain the high level of service to which its customers have become accustomed. Id.; Tr. 673-81.

C. OPC's earnings test is inconsistent with Commission rule

Further, OPC and the other Intervenors' suggestion that the Company be required to retroactively expense storm restoration costs down to a 10% earned return for 2004, irrespective of whether those costs were reasonably and prudently incurred, is inconsistent with Rule 25-6.0143, Florida Administrative Code. Pursuant to the rule, FPL has established an accumulated provision account for uninsured storm losses. Under Rule 25-6.0143(4), utilities that elect to use such an account shall charge to the account "each and every loss or cost which is covered by the account," and such losses or costs "shall not be charged directly to expenses ... regardless of the

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was funded, even though those were the types of questions that would be asked by someone being asked to determine the risks being imposed. Tr. 299, 330, 321-26.

balance in those accounts." Nevertheless, despite the fact that OPC's witnesses did not even remember reviewing Rule 25-6.0143, OPC and the Intervenors ask that the Commission require FPL to expense or absorb all costs to the extent necessary to bring FPL's ROE down to 10% for 2004 without regard to the Commission rule and irrespective of a determination of the reasonableness and prudence of FPL's costs. Tr. 295-96 (Rothschild), 419-21 (Majoros).

D. 10% ROE for 2004 is not a fair return

Apart from the legal infirmities with his suggestion, there is no legitimate record evidence on which a decision that a 10% ROE for 2004 is fair could reasonably be based. Mr. Rothschild's superficial analysis contains numerous errors that render it suspect. Tr. 592-605; Ex. 47, pp. 80-98. First, he does not in any way suggest that he intends or is able to demonstrate that 10% is the required rate of return by investors. To do so, his analysis at a minimum would have been supported by discounted cash flow and capital asset pricing model assessments. He did neither. Tr. 335, 354. To say that FPL's investors would be fairly compensated based not on their required return, but on what a group of holding companies actually earned in a prior period is a novel approach without precedent in Florida regulatory law.[39] But, even as to that approach, there is ample record support detailing the flaws in his analysis. As noted, the returns against which Mr. Rothschild compares the proposed 10% return for FPL are overall holding company returns, not actual utility company returns. In addition, Mr. Rothschild acknowledged that the returns he uses include variability due to structure of the holding company, the percent of non-regulated activity, write-downs, and variability in weather and performance, among other

[38] Not surprisingly, Mr. Rothschild could not point to any analyst reports that suggested any earnings upside or profit potential due to the Storm Damage Reserve. Tr. 334.

[39] In fact, the only investment report that he reviewed to determine what FPL's investors might be expecting to earn was a 2004 Value Line report that included only 3 months of projections. Tr. 319-320.

factors.[40] Indeed, upon closer scrutiny, it was disclosed that other investor-owned utilities in the Southeast earned returns in 2004 that were markedly above the 10% ROE suggested by Mr. Rothschild as fair. Tr. 345-53; Ex. 41, 42. Further, Dr. Avera rejected OPC's attempts to persuade him to agree that a 10% ROE or something close to it was fair on grounds that each of the analyses OPC asked him to conduct "start[ed] from a false premise." Ex. 47, pp. 80-98.

E. OPC's earnings test is inconsistent with public policy and produces absurd results

As described in Issue 18 above, the policy of state and local governments with respect to restoration of electric power was very clear. FPL was expected to take all necessary actions and deploy every available resource to restore power as quickly as possible in the interest of Floridians. This is uncontroverted in the record. Even if the PSC were to conclude that OPC's proposal was preferable to the existing framework, for a number of reasons, as a matter of public policy changes should be applied prospectively. Tr. 713-27 (Dewhurst).

Whatever framework is adopted should, as much as possible, be independent of normal utility operations – i.e., it should operate the same regardless of the current state of the utility or its financial situation. Customers have very different interests during normal operations than they do after major storm events. In the storm environment, customers want utilities to be highly focused on rapid restoration, almost to the exclusion of other considerations. In contrast, during normal operations customers have a far broader set of interests, and utilities have a far broader array of issues to manage. As a matter of policy, it is beneficial to have a framework that

[40] Tr. 335-51. Interestingly, while Mr. Rothschild believes that the group of entities he lists on Ex. 11 (with no significant distinction or detail in the analysis), offers a good proxy against which to assess a proposed 10% rate of return, he quickly asserts that he'd want to know much more about the circumstances of those companies and the numbers if the same group disclosed an average of 11%, 12% or 13% --that the analysis couldn't be "one-dimensional." Tr. 340-41. Further, the variability in reported results was no more evident than in the earnings reported for TECO Energy, Inc. by Value Line, which in the December 3, 2004 edition relied upon by Mr. Rothschild showed earnings of 0.51% for 2004, and just three months later in a report dated March 4, 2005 showed earnings of 12.7%. Mr. Rothschild's observation was telling: "So what happened in that interim I don't know, but for whatever reason, between those three months, Value Line changed the result for 2004." Ex. 11, 40; Tr. 343-44.

focuses utilities very tightly on rapid restoration after major storms even at the expense of some efficiency. The Commission should not want utilities' non-storm actions to be influenced by what situation they might find themselves in if a storm struck, and conversely the Commission should not want utilities' storm actions to be influenced by contemplation of whether or not a particular level of expenditure will be recoverable or not. Tr. 717 (Dewhurst). There is no record evidence contradicting or even opposing Mr. Dewhurst's testimony in this regard.

OPC's proposed framework, which was endorsed by the other Intervenors, would distort utilities' incentives. Under OPC's proposal, utilities operating under normal ratemaking (i.e., in the absence of some rate agreement) would see odd incentives during restoration activity, depending upon the pre-existing level of the Reserve, the magnitude of the restoration effort, and their existing ROE. For restoration efforts modest in magnitude relative to the Reserve, the incentives would remain as today: to restore power as rapidly as practical, even at some cost in efficiency, which is consistent with customer interests. If the restoration effort were likely to be large enough to exceed the Reserve, though, there would be an incentive to keep costs from exceeding the Reserve. An illustrative example might be electing to wait two extra days for crews to travel a further distance if their overall cost was expected to be lower than crews originating from closer locations. Such an incentive is not in customers' interests, is not an acceptable position to a utility attempting to meet both customer and shareholder needs, and makes for poor public policy. Perversely, under OPC's framework, the better the utility performs in terms of rapidly restoring power, the greater the share of restoration costs imposed on shareholders. Tr. 719 (Dewhurst). In fact, Mr. Rothschild conceded that under OPC's approach, the financial outcome for FPL would be identical whether the Commission (a) ordered the Company to expense a certain amount of costs in order to reduce FPL's ROE for 2004 to

10%, or (b) found the same amount costs to have been unreasonable and imprudently incurred and, therefore, disallowed recovery. He also conceded that OPC's approach would produce the same financial outcome for two utilities, one of whom had produced better earnings results in the period due to productivity enhancements. Tr. 309-16.

ISSUE 21: What is the appropriate amount of storm-related costs to be recovered from the customers?

$533 million (jurisdictional) plus interest on the unrecovered balance. The Commission should reject OPC's proposal to use a theoretical depreciation reserve surplus to offset the deficit balance. The OPC proposal violates FPSC and FERC policy and orders, GAPP and SEC guidance, and would cost customers substantially more than FPL's proposed surcharge. The OPC proposal also would shift cost responsibility from wholesale to retail customers. FPL has properly addressed the theoretical depreciation reserve surplus by reducing depreciation expense in base rates.

FPL seeks to recover via its proposed surcharge the actual amount of the jurisdictional deficiency (but in no event more than $533 million), together with interest at the 30-day commercial paper rate on the unamortized balance. Tr. 85-87, 123-24 (Davis). As contemplated by the PSC's regulatory framework, and consistent with state policy, the special assessment or surcharge proposed is the appropriate mechanism to recover the Reserve deficit. Tr. 813-19.

Shortly before the hearing, OPC filed additional supplemental testimony of Mr. Majoros that proposed a one-time, lump-sum adjustment to offset the $533 million deficiency in the Reserve with a portion of the theoretical depreciation reserve surplus that FPL identified in its recently filed depreciation study. Mr. Majoros' proposal should be rejected for several reasons.

First, it would cost customers considerably more in the long run than FPL's proposal and would leave customers paying for all of the 2004 storm costs 20 years from now, when they also would be facing the risk of subsequent storms. Using the theoretical depreciation reserve surplus to offset the entire Reserve deficiency would have the effect of unnecessarily increasing rate base and depreciation expense in FPL's upcoming rate case, necessitating higher base rates to cover

the resulting revenue requirements for many years into the future. Tr. 139-40 (Davis). FPL would earn its overall authorized rate of return on the increased rate base, while it proposes to charge only the 30-day commercial paper rate on the unamortized balance of the Reserve deficiency. The cumulative impact of these two phenomena is a protracted recovery period and a higher return on the asset balance over that recovery period. Ex. 31. While Mr. Majoros clearly does not like the implications of FPL's position, his critique never rose above the puerile: he called it "silly" without offering a single substantive objection or correction. Tr. 478. In short, there is unrefuted record evidence that adopting Mr. Majoros' proposal would impose a significant additional financial burden on FPL's customers.

Mr. Majoros' proposal should be rejected for several other reasons as well. It would have the effect of increasing the level of nuclear plant in FPL's rate base, as well as the associated depreciation expense. Because nuclear plant is allocated almost entirely to the retail jurisdiction in FPL's separation studies, adopting Mr. Majoros' proposal in lieu of FPL's proposed storm surcharge would be the equivalent of increasing the percentage of the total Reserve deficiency for which retail customers are responsible. Tr. 134 (Davis), 255-56 (Morley). And within the retail jurisdiction, this same phenomenon would result in a shift of cost responsibility away from large industrial customers toward residential and smaller commercial/industrial customers. Tr. 256 (Morley). Moreover, Mr. Majoros' proposal would be inconsistent with GAAP and would violate stated depreciation policies of this Commission, the Federal Energy Regulatory Commission (FERC) and the Securities Exchange Commission (SEC). Tr. 132-39, 144 (Davis). Telling in this regard is Mr. Majoros' admission that he did not even bother to review the rules and orders of the Commission, the FERC or the SEC prior to filing his testimony and that he is

aware of no instance in which the Commission has ever approved a proposal such as his. Tr. 456-58.

Mr. Majoros' approach is unwarranted -- for two additional reasons: First, the calculation of theoretical depreciation reserve levels is ephemeral, in the sense that there can be large changes in the reserve level over time in response to changed circumstances. FPL's calculated depreciation reserve balance actually showed a *deficiency* in 1997, which switched to a surplus in 2001, which became a larger surplus in the current depreciation study. Tr. 131 (Davis). But now there are factors, including FPL's plans to incur substantial capital costs in the near future for its nuclear function, that will reduce the depreciation reserve surplus substantially. Id. Making such a substantial decision on the basis of the depreciation reserve balance at a single point in time would be like looking at a single motion-picture frame and assuming that you not only have seen the entire film but know how it ends. Tr. 132 (Davis). The Commission would be ill-advised to accept Mr. Majoros' call for precipitous action on the basis of one look at the current level of FPL's theoretical depreciation reserve.

Second, there is simply no need for the Commission to take extraordinary action of any sort because the remaining-life depreciation technique is by its very nature self-correcting and will appropriately address FPL's current theoretical depreciation reserve surplus without further intervention. **Mr. Majoros admitted as much.**[41] In short, OPC's proposal is an expensive solution in search of a problem, and it should be rejected.

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> Q. Would you agree that using the remaining life depreciation technique, any depreciation reserve surplus that has been calculated currently should be eliminated over the remaining lives of the affected assets via reduced depreciation rates?
>
> A. That is the intent and the reason for using the remaining life method. Correct.
>
> Q. And do you have any reason to believe that that's not what FPL has done in its recent depreciation study?

ISSUE 22: If recovery is allowed, what is the appropriate accounting treatment for the unamortized balance of the storm-related costs subject to future recovery?

The commission should authorize the transfer of the unamortized balance of the storm related costs subject to future recovery from the Storm Damage Reserve (Account 228.1) to a deferred Regulatory Asset (Account 182.3). The amount transferred should be amortized consistent with the amounts recovered as revenue through the authorized surcharge recovery factor.

There is no dispute in the record with FPL's position on this issue, and it should be adopted.

ISSUE 23: Should FPL be authorized to accrue and collect interest on the amount of storm-related costs permitted to be recovered from customers? If so, how should it be calculated?

Yes. Interest should be calculated monthly using the average commercial paper rate applied to the average unamortized balance for the month. In addition, if the tax benefit of the deduction resulting from storm expenses is used to reduce the balance on which carrying costs are applied, the amount associated with the tax benefit would need to be financed with other sources of capital. These funds would have a cost possibly as high as FPL's overall cost of capital.

FPL should be authorized to accrue interest on the unamortized balance of the Reserve deficiency at the 30-day commercial paper rate. Tr. 86 (Davis). Deferred taxes are used as a cost-free source of capital to finance FPL's capital requirements. Tr. 221 (Davis). The unamortized balance of the deferred taxes associated with the 2004 storm-related costs are included as a cost-free source of capital in the MFRs that FPL has filed in Docket No. 050045-EI, which has the effect of lowering FPL's overall cost of capital and hence its revenue requirements for the rate case test year. Id.; Ex. 39. Moreover, the base rates set in Docket No. 050045-EI are likely to remain in effect well after the deferred taxes have been fully amortized, resulting in a continuing benefit to customers. Id. If the Commission were to use deferred taxes associated with the 2004 storm-related costs to reduce or eliminate the accrual of interest on the

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

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

A. Yes.

unamortized balance of the Reserve deficiency, then those deferred taxes should be removed from the calculation of FPL's cost of capital in Docket No. 050045-EI. Tr. 226 (Davis).

ISSUE 25: If the Commission approves recovery of any storm-related costs, how should they be allocated to the rate classes?

The Storm Recovery Surcharge should be allocated to rate classes based on each rate class's share of gross plant divided by its kWh sales. The resulting calculation of the Storm Recovery Surcharge factors by rate class is reflected in Document No. RM-1 attached to the Direct Testimony of Rosemary Morley filed in this Docket.

Consistent with the treatment of Reserve accrual costs in base rates, the Storm Restoration Surcharge should be allocated to rate classes based on each rate class' share of gross plant. Tr. 249 (Morley). Each rate class' allocated cost is divided by its kWh sales during the same time period used to develop the allocation factors, and the resulting calculation of the factors by rate class is shown in Ex. 9. Tr. 252 (Morley). There is no testimony in the record opposing this allocation of costs or calculation of rate class charges. Nor has any party provided an alternative set of rates for the Commission's consideration.

ISSUE 26: What is the appropriate recovery period?

The jurisdictional portion of the Storm Reserve Deficit, $533 million, should be recovered over a three-year period, or such shorter period as is necessary to recover the Storm Reserve Deficit.

The appropriate recovery period is 36 months or such shorter period as may be needed to recover the Storm Deficiency. Tr. 249 (Morley). The Surcharge may be terminated in less than 36 months if the revenue requirements associated with the Storm Deficiency have been fully recovered. Ex. 10. FPL concurs with the Staff position that billings should end with cycle 12 so all customers are assessed the Surcharge for the same period of time.

ISSUE 27: If the Commission approves a storm cost recovery surcharge, should the approved surcharge factors be adjusted annually to reflect actual sales and revenues?

Tr. 465.

FPL does not believe such an exercise is necessary. The Storm Recovery Surcharge will be subject to true-up based on actual sales and revenues, and any over- or under-recovery will be subject to disposition as ordered by the Commission.

There should be a single cumulative true-up at the conclusion of the recovery period based on the actual sales and revenues recorded during the recovery period, with any over-recovery refunded to customers with interest as soon as feasible. Tr. 249-50 (Morley). A single cumulative true-up works hand-in-hand with termination of the Surcharge in less than 36 months if the applicable revenue requirements are recovered before that time. Id. Intermediate or annual true-ups before the end of the recovery period are not necessary and would not represent the best use of the Commission's time and resources. Id. There is no testimony in the record supporting an annual adjustment instead of a cumulative true-up.

ISSUE 28: If the Commission approves a mechanism for the recovery of storm-related costs from the ratepayers, on what date should it become effective?

It should be deemed effective the same date as the interim surcharge became effective (Feb. 17, 2005).

The Commission-approved surcharge should be deemed effective the same date as the interim surcharge became effective (February 17, 2005). Any difference between FPL's requested revenue requirement and the Commission-approved amount would be subject to the cumulative true-up at the end of the recovery period. There is no dispute in the record with FPL's position on this issue and it should be adopted.

ISSUE 29: What is the appropriate disposition of the revenue collected as an interim storm cost recovery surcharge?

Revenues collected on an interim basis, less revenue taxes, should be applied to the amount approved for recovery by the Commission.

Revenues collected on an interim basis, less revenue taxes, should be applied to the amount approved for recovery by the Commission. Total revenues would be subject to the

cumulative true-up at the end of the recovery period. There is no dispute in the record with FPL's position on this issue and it should be adopted.

ISSUE 30: Should the docket be closed?

Yes.

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of Florida Power & Light Company's Post-Hearing Brief, has been furnished electronically and by United States Mail this 10th day of May, 2005, to the following:

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