BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 041393-EI

In the Matter of

PETITION FOR APPROVAL OF TWO UNIT POWER SALES AGREEMENTS WITH SOUTHERN COMPANY SERVICES, INC. FOR PURPOSES OF COST RECOVERY THROUGH CAPACITY AND FUEL COST RECOVERY CLAUSES, BY PROGRESS ENERGY FLORIDA, INC.

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VOLUME 3

Page 138 through 243

PROCEEDINGS:	HEARING
BEFORE:	CHAIRMAN BRAULIO L. BAEZ COMMISSIONER J. TERRY DEASON COMMISSIONER RUDOLPH "RUDY" BRADLEY
DATE:	Thursday, June 2, 2005
TIME:	Commenced at 9:30 a.m.
PLACE:	Betty Easley Conference Center Hearing Room 148 4075 Esplanade Way Tallahassee, Florida
REPORTED BY:	JANE FAUROT, RPR Official Commission Reporter (850) 413-6732
APPEARANCES:	(As heretofore noted.)

INDEX

WITNESSES

EXHIBITS

NUMBER:	ID.	ADMTD.
4-8		165
17-25		165
9-14		217

P R O C E E D I N G S

(Transcript follows in sequence from Volume 2.

SAMUEL S. WATERS

continues his testimony under oath from Volume 2:

CONTINUED CROSS EXAMINATION

BY MR. BUSHEE:

Q Would you please turn to Page 13 of your direct testimony?

A Okay.

Q And specifically Lines 12 through 15?

A Yes.

Q And you discuss rollover rights. Isn't it true that the rollover rights under the existing UPS agreement don't expire until 60 days before the contract termination date?

A Yes, I believe that's correct.

Q And those rollover rights are not created under the existing UPS agreement, are they?

A They are not created under the agreement, they are really created by the fact that the agreement predates the FERC orders establishing unbundling of the service, and the fact that we had an existing contract at that time which, in a sense, is grandfathered in and provides rollover rights as long as we continue those purchases.

MR. BUSHEE: Mr. Chairman, if I could just take a minute, I think I can significantly shorten the time I will need.

CHAIRMAN BAEZ: Go ahead.

Commissioner Deason, you had a question?

COMMISSIONER DEASON: Yes. I'm trying to understand what you mean by the term rollover transmission rights. Could you explain that further?

THE WITNESS: The rollover rights applies to certain contracts that predated the FERC orders that established it, basically our new scheme of things. What it says is that if you were purchasing through a certain transmission path prior to those orders, provided that you continue those purchases, you have rollover rights to unbundled transmission. In other words, you are first in line. It has to do with the queuing process.

COMMISSIONER DEASON: Let me interrupt you. The contracts that are the question in this docket, do they qualify as rollover?

THE WITNESS: Yes. In fact, Southern has already affirmed our rollover. We asked for rollover. They have already affirmed the paths from Miller to Progress and from Scherer to Progress.

COMMISSIONER DEASON: Okay. Now, you have to clarify for me then. If they qualify as rollover, why then does there have to be a system impact study? And the question arises about availability of transmission, cost of potential upgrades to facilitate a transaction; can you explain that?

THE WITNESS: That's a good question. If we were continuing to buy from Miller and purchase, I don't think we would have any of those questions, because the FERC rulings I have seen says that Southern has an obligation to continue planning as if we will continue purchasing from those sites.

However, since we are buying from Franklin, the next step after rollover is we need to ask for redirection of the point-to-point transmission from Miller to Franklin. So we are asking for a new path from Franklin to Progress Energy, in effect. So we are still holding our same place in the transmission queue, but now a system impact study has to be done because it is a new source delivering to Progress Energy. If we were still buying from Miller, it wouldn't be a question. But because we are buying from Franklin, we need to go through the system impact study.

COMMISSIONER DEASON: Okay.

CHAIRMAN BAEZ: And just to understand a little bit, and I may have missed the answer, so what you just described there is technically a rollover, or is there some further concession that has taken place in order to classify a redirection or a request for a new path as a rollover?

THE WITNESS: It is a rollover. There are a complicated set of rules here. But when we have a firm transmission path, such as from Miller to Progress Energy, we ave the right then to ask for a redirection of the service. 'e have that path, but now we can ask for a redirection of the ath from Franklin to Progress Energy. But any redirections re always subject to availability and, in the case of a ong-term firm contract, subject to a system exact study. So y moving it, that's what triggers the system impact study. ut it is related to the rollover, because that is how the rocess started.

CHAIRMAN BAEZ: Okay. Thank you.

I'm sorry, Mr. Bushee, go ahead.

Y MR. BUSHEE:

Q And just to follow up on that question. The concern ith the system impact study is that there could be congestion etween where you had the transmission path to where you want o move it?

A Well, that's right. The purpose is to see if there is any impact to the system.

Q And if there is congestion or the system simply can't accommodate that, then one option may be to build new facilities?

A That's correct.

Q Or it may not be possible to solve that problem by building new facilities economically?

A Right, that's possible.

Q Would you please turn -- I believe you have Mr.

Brubaker's confidential testimony with you?

A Yes.

Q And I'm just corrected and told that the questions I'm going to ask are not on a confidential matter. I would like you to look at Mr. Brubaker's Exhibit MEB-3, and I would say that is about three-quarters of the way towards the back.

A Okay. I have it.

Q And the chart you have before you shows the percentage of energy for Progress from oil and natural gas, does it not?

A That is what it purports to show, yes.

Q And at the bottom of that chart it says that the source is the ten-year Progress site plans for April 2001 and April 2005, do you see that?

A Yes.

Q I'll ask you to look at the percentages here and see if they strike you as correct?

A Yes. I'll say subject to check, I think they are correct, if they were transcribed from the site plans correctly. And they look to be correct.

Q So in the year 2000, according to this chart, the percentage of Progress' energy from natural gas is what?

A In 2000?

Q Yes.

A Roughly 15 percent for gas.

Q And by 2010 it raises to 30 percent?
A Yes.
Q And by 2014 it raises to roughly 45 percent?
A Roughly, that's correct.
Q And in the year 2000 the total oil and natural gas energy is what percentage?
A In 2000, I'm sorry?
Q 2000, yes.
A The total from oil and gas is probably around 28 percent or so.
Q And in 2010 the figure raises to about 42 percent?
A Roughly, yes.
Q And 2014 raises --
A It looks like maybe 53, 54, somewhere in that vicinity.
Q Now, Progress is a member of FRCC, is it not?
A Yes.
Q And what is FRCC?
A The Florida Regional Coordinating Council or Reliability Council. Florida Reliability Coordinating Council. I'll get the acronym right eventually.
CHAIRMAN BAEZ: I can never get it right, either.
THE WITNESS: I forget.
MR. BUSHEE: We don't deduct points for spelling.
BY MR. BUSHEE:

Q Would you agree with me that fuel diversity is an issue in FRCC?

A Yes.

Q And would you also agree with me that there are concerns that increased reliance on natural gas-fired generation could cause reliability problems?

A Yes. Hypothetically speaking, I think that has been addressed by the number of pipelines coming into the state. We have just taken actions to add a third pipeline in the state. So I think reliability concerns is probably not the main concern over diversity. I suspect it is more of a pricing concern.

Q Would you turn back to your direct testimony at Page 11?

A Yes.

Q And if you look at Page 11, Line 4, you talk about contributions to economy energy availability?

A Yes.

Q Now, the proposed UPS agreements themselves don't provide access to economy energy, do they?

A No.

Q That would be done through the rollover transmission rights, correct?

A Ultimately it is a function of transmission, yes.

Q And isn't it true that Progress gets to keep 20 percent of the benefit of its economy energy transactions?

A That has historically been the case, yes.

Q And that benefit would go to the Progress shareholders?

A Yes, with 80 percent going to the customers.

COMMISSIONER DEASON: Let me ask a question about that. Isn't there a threshold that has to be exceeded before there is a sharing?

THE WITNESS: Yes. And I'm not sure what the threshold is, but under the current terms there is a threshold.

COMMISSIONER DEASON: And it is based upon some type a moving average, is it not?

THE WITNESS: Yes.

MR. BUSHEE: I have no further questions at this time. I understand that Mr. Waters will take the stand again for his rebuttal testimony, is that correct?

CHAIRMAN BAEZ: Since we didn't -- I had assumed that that was correct. Okay.

Ms. Vining.

CROSS EXAMINATION

BY MS. VINING:

Q Good afternoon, Mr. Waters.

A Good afternoon.

Q I just have a few questions. Progress' expansion plan with these proposed UPS agreements show a potential coal

unit in 2015, is that correct?
A That's correct.
Q And at what point would Progress have to make the decision to move forward with the coal unit in order to meet that 2015 in-service date?
A It's difficult to point to one decision point. We are in the process of siting now as if we will proceed with that, and that is part of the overall process. So in a sense you could say we are on a course now to do that. There are subsequent decision points after design is done, after the final siting is done, and so on, that will -- I'll call them checkpoints along the way. But right now I would say we are on course.
I will add, though, that one of the concerns with coal has always been environmental. And now we have to think about how this plays off of the recently enacted clean air interstate rule, and how that might impact the plant. I don't have an answer for that today, but it will be a factor in what we do in the coal unit. So that is another checkpoint we will have to go through.
Q So will that potentially delay the 2015 in-service date?
A Well, I can't address anything specific right now. We don't have an answer. I can tell you that if you look at the clean air interstate rule, there is a 2009/2010 set of

limits, and then it drops in 2015. And if you think about how that plays off the timing we are talking about here, in the extreme it could potentially eliminate coal as an option, depending on how your system matches up to the overall limits. I think at the very least it will make coal a more limited option. It may not be that we can add a whole series of coal units, you know, year after year. That will have to be given some consideration.

Q To meet this 2015 in-service date, when do you anticipate you would issue an RFP for the unit?

A For the purposes here, I will take a rough guess. I would say it would have to be within the next year and a half or so that we would have to issue an RFP, keeping that in sequence with the licensing activities and so on.

Q Will Progress have the scheduling flexibility under the proposed UPS agreements to make economy sales from Southern's generating units?

A From the ones that we are buying from, yes, we will. As long as we schedule under the normal provisions of the contract, we could either take the energy into our system or sell it.

Q So this would only be from Scherer and Franklin?

A Right. Just the units we are buying from.

Q And how do the transmission rights work with the UPS agreements to get that benefit of making economy sales?

A I don't way to imply that they are part of the agreements. I want to be very clear it is a separate agreement. But just as we are asking for redirect at the long-term firm service, what we can do is ask for a redirect of transmission service which is provided on an as-available basis. So let's say we want to sell from one of these units, you know, back into North Carolina, for example. We can request a redirect of the transmission to accommodate that, and then Southern will tell us, Southern Transmission would tell us whether or not they have the transmission to accommodate it. So it would -- basically it's a flexible system.

Q Now, can Progress and its ratepayers benefit from these transmission rights in the cases when Progress is not receiving energy from the generating units that are covered by the UPS agreements?

A Yes, if I understand your question. If we don't schedule it for our own use because it is not economic in our system, we could go ahead and look at the market and say we will schedule it, and then sell to, you know, whomever might have higher energy costs at that point, and there would be a benefit from that, I think.

Q I'm wondering with these transmission rights, can you purchase from someone else other than Southern and use that transmission to bring it into Progress' system?

A Yes. I'm sorry, I thought we were still on the selling side. If we are purchasing, yes, we can do that. We can also redirect transmission to buy. And that is one of the benefits we have quantified in the analysis was to quantify buying economy from Southern itself. But the flexibility in this agreement would allow us to buy economy energy from outside the Southern system. We basically have an access to a much broader market, and we haven't tried to quantify that.

Q From a reliability perspective, how would Progress and its customers be impacted if Progress is not able to maintain these transmission rights on Southern's system?

A My opinion is that if we are not able to maintain the rights, and basically we have to forgo our rollover rights, I believe at that point the interface becomes fair game, and that there will be other players in the market to purchase across the interface. If that interface gets tied up, then I think we are harmed by the overall loss of the transaction. Because at that point we no longer have access into the Southern system if someone else has got it tied up.

Q If Progress --

COMMISSIONER DEASON: I'm sorry, I have a question. I thought in answer to a previous question you indicated that the Florida/Georgia interface, that you have a contractual right to a certain portion of that interface regardless of whether you continue purchasing from Southern or not.

THE WITNESS: Right. If we are purchasing, I think that is correct. The situation I'm talking about, and I think it is unclear as to what would happen, but I'm speculating a little here. If that interface was sitting idle, if we have not made purchases across that interface and it is sitting there idle, others will make a claim to it.

COMMISSIONER DEASON: Do you get compensation for that, or is it just a right if you use it; if you don't use it, you lose it?

THE WITNESS: I don't think there is compensation other than whatever wheeling charges might be associated with transactions through our system. The interface itself, there is not an interface charge, per se. But if they use our transmission lines, there would be charges associated with that. But I think others would demand and probably, in my opinion, given FERC's mind-set, would probably get access to that. We can't just sit on it. We have to be doing something with it and making purchases. So I think the interface by itself is not an asset that you can just hold.

BY MS. VINING:

Q Now, if Progress were to opt out of the Franklin contract for whatever reason, would Progress be able to maintain the contract for the capacity from the Scherer unit?

A I haven't really thought about that combination, but I think the way the contracts are written we could, because each of them has this same language about transmission availability and so on. So assume for the moment that the Franklin capacity was not deliverable and that Scherer was, I think we have the option of taking Scherer, but I'm not certain. I would have to go back and look at how the agreements interplay. But that is sort of my cursory review. I think that's the way it works.

Q Is it true that one of the benefits of the UPS agreements is deferring two combined cycle plants during the contract term?

A Yes.

Q And one of those would be deferred from 2010 to 2011, and the other from 2012 to 2018, is that correct?

A That's correct.

Q Now, is that deferral reflected in the 2005 ten-year site plan that was filed by Progress?

A Well, of course, one -- it's difficult to answer. The site plan is updated with a more current forecast. So if I were to go back and use the more current forecast and repeat the analysis, I would see deferrals of combined cycles. But I can't match the analysis we are discussing here with the site plan because it is a different load forecast. So you won't be able to see it, I guess, is the bottom line in the site plan because the load forecast has changed. It would be difficult to pick up. But by buying 400 megawatts of capacity, you are obviously displacing a need for 400 megawatts in your system, so there would be unit movement.

Q Okay. So even though in your 2005 ten-year site plan you indicate that takes into account the UPS purchases, it is not clearly reflected in what you filed?

A What it defers is not clearly reflected. In the site plan we basically give you the end result, the final plan. What we don't show is what we were calling before the base plan would be without the Southern purchases, that is not reflected in the site plan itself.

Q I'm also curious because in the 2004 ten-year site plan, it appears to not include UPS purchases?

A It does not.

Q But yet they appear to be the same in terms of what you're predicting your combined cycle units would be?

A Yes.

Q Can you explain why there appears to be a similarity in what combined cycle units would be there?

A I guess you could say it is somewhat coincidental. If you were to check the difference in load forecasts and the peak demands, there is about a three to 400 megawatt increase in load, which basically says you take Southern -- I mean, one way to look at it is I take Southern to meet that load increase and everything else stays the same. So if you were to look at the combined cycle schedule between the two plans, they would look very similar. But we have additional load we are meeting, and Southern is taking the place of that. It is basically offsetting that.

MS. VINING: Those are all the questions we have.

CHAIRMAN BAEZ: Commissioners, do you have questions?

COMMISSIONER DEASON: I have a question.

CHAIRMAN BAEZ: Commissioner Deason.

COMMISSIONER DEASON: I think you briefly addressed in your testimony the fact that -- well, you acknowledged that there was not an RFP issued and that there were some reasons for that.

THE WITNESS: Yes.

COMMISSIONER DEASON: I assume one of those was the -- I guess time was of the essence when you were negotiating the contracts with Southern. But can you explain further why Progress decided to not avail itself of an RFP process?

THE WITNESS: I think there are a number of reasons. Part of it may come to mind-set on existing contracts. It is not uncommon to look at extending existing contracts. And I think the rationale for not looking at an RFP and potentially building new units to displace something you have already got is part of that. But I think one of the main drivers is we are under the distinct impression from dealing with Southern that if we don't take advantage of this, that they will just sell it elsewhere, and there is a market there.

If we go out with an RFP, they're certainly not obligated to hold it, they might, and bid into the RFP. But I think given the nature of their business, they would be looking to sell it as quickly as possible, get a commitment and not have any uncovered capacity in that time frame. I think it's just in their best interest.

COMMISSIONER DEASON: Let me interrupt for just a second. But we are talking about contracts that don't expire for some period of time. What, 2010 time frame, as I recall?

THE WITNESS: Yes, sir. But the potential buyers would be looking at displacing something they had to build. So from Southern's point of view you could say, well, they may not be rushed, they don't have to deal with it until 2010 when it becomes uncovered. But the market that they are selling into, they are going to be looking for people who have capacity needs in that time frame and are looking to build and have to take action today.

COMMISSIONER DEASON: And the people that would be buying it don't have to go through an RFP, either?

THE WITNESS: I don't think every -- well, I don't know that they would. Or if they sign a contract, the RFP requirement is tied to the Power Plant Siting Act, assuming Florida, for the moment. If I were to go and buy this and the only issue is cost-recovery, if I don't need approval of cost-recovery, and I'm not looking to license a new unit, there is no RFP requirement. So I could do this, if I'm one of those utilities that is not building a new unit, doesn't need approval for cost-recovery, I could do this without, basically, any review. I don't see the tie, necessarily, to an RFP because nobody is looking to license or build a unit here, it is just a contract.

COMMISSIONER DEASON: But you do agree that an RFP process gives greater assurance to you, your management, this Commission, and customers that whatever is the result is the lowest cost option?

THE WITNESS: Yes, I do. The only counter I would have to that is I think we don't want to be handcuffed by an RFP process if opportunities present themselves and we feel those are appropriate to pursue.

COMMISSIONER DEASON: And how should we judge that as regulators?

THE WITNESS: I think that the way the process is set up is the proper approach. It's tied tightly to the environmental licensing to make sure that whatever gets built in this state is absolutely necessary and is the best alternative. When it comes to contracts, I think you are in a whole different area. As I said, we are talking about extending -- not extending, I don't want to use that term, because contractually we are not extending, we are replacing the contract, but we are continuing a purchase of a resource.

There will be no impact here as far as building new resources, adding new resources in our system.

I think that is a situation where there ought to be the flexibility to be able to proceed with that. And we have a number of contracts where that is true, it is not just Southern. You could extend this on down to any of the contracts that we have. And, yes, the burden is on us to make the case that it is a good deal, but I don't think an RFP should be required in that case.

COMMISSIONER DEASON: Are these contracts contingent upon Public Service Commission approval?

THE WITNESS: Yes, they are.

COMMISSIONER DEASON: And when is the deadline for that approval?

THE WITNESS: I would have to refer to the contracts.

COMMISSIONER DEASON: Just generally, if you can say. And here, again, that is not confidential, I hope.

THE WITNESS: Well, I don't think so. I think it was 180 days from the November contract date, roughly. That is my recollection. That would us in -- not too far from now.

COMMISSIONER DEASON: If this Commission chooses not to grant approval, are you still free to go forward with the contract?

THE WITNESS: I think we would proceed at our own risk at that point. We can, but I think there is an obvious risk there if we proceed on that basis.

CHAIRMAN BAEZ: Mr. Perko, redirect.

REDIRECT EXAMINATION

BY MR. PERKO:

Q Mr. Waters, I believe you answered some questions from Mr. Bushee about the Burns and McDonnell report. Could you explain what role the Burns and McDonnell report played in Progress Energy's evaluation of solid fuel options?

A Yes. The Burns and McDonnell report was really commissioned to develop the cost parameters for solid fuel options, specifically the pulverized coal and fluidized bed options, and so on. It was not commissioned to be an economic analysis of the alternatives to PEF. In other words, while they did some graphs in the back and did some comparisons, that was never intended to be indicative of what the economics would look like on the PEF system.

We took the inputs from the Burns and McDonnell study as a source, ran detailed analyses, and used the models with our own assumptions, our own forecasts, and our own comparisons to develop what we thought was the most economic option. So it was really, I would say comparable, to what we used the EPRI Technology Assessment Guide for, and that is to provide inputs to the process.

Q I would like to refer you back to what has been marked as Exhibit Number 19, which Mr. Bushee also questioned you about.

A Yes.

Q And I believe it is an e-mail from Mr. Roger Kramer to Dan Roeder.

A Yes.

Q I believe you testified that Mr. Kramer works in the treasury department at Progress Energy, is that correct?

A That's correct.

Q What is treasury's role with respect to agreements of this nature?

A They have a limited role. In fact, if you were to look at all the names on this e-mail, each person has a narrow role to, in a sense, represent their department's or their group's interests in the overall analysis. So each person has a limited perspective. Treasury is going to take a strict net present value approach to everything. I mean, that is sort of their role in things. So they are going to look at a bottom line number and not look at any of the other factors associated with the deal.

Mr. Roeder, as the analyst, is going to look at the analysis and the system impacts and so on and do an analysis and only look at that piece. Everyone is looking at just their piece. Looked at from that perspective, any individual might say, well, I don't like this deal, but collectively the deal still represents a good deal for the customers. And I would also point out that the vice-president of treasury, the vice-president over planning, all the vice-presidents approved this transaction with these comments notwithstanding.

All this shows to me is there was a good healthy debate as we were going through the process, and it was certainly animated at times. But all the issues got laid out all the way up the chain, and this was approved through all the levels that I mentioned earlier of the approval process.

Q What, if any, additional analyses were performed after July 1st when this e-mail was sent out?

A Well, one additional analysis which was done was the transmission. It is referred to by several names in the process, transmission utilization, in other words, the economy energy transactions. That was not part of this analysis. This was just straight resource plan changes. And we did look at economy energy and all the -- what I have listed as the strategic concerns after this time.

Q Mr. Waters, I wanted to refer your attention back to some questions that Ms. Vining asked you about, and I believe it was in the event that there were transmission problems with Franklin, you could -- or perhaps it was the other way around, you could opt out of the Franklin contract. I would like to refer you specifically to Page 31, Section 7.4.7 of the -- excuse me, I've got the exhibits mixed up here. That would be the Scherer contract.

A Okay. That's what I thought.

Q Does that refresh your recollection?

A Could you refer me to the section again?

Q 7.4.7.

A Okay. This says that both are subject to termination in the event that one is not, or one has to be terminated due to the transmission provisions. So at that point it would probably be a matter of no transactions taking place in your example of Franklin not being available.

Q I would also like to refer you to the Franklin contract on Page 37, also Section 7.4.7.

A Yes. It's the same language, same provision.

Q Thank you. Now, Mr. Waters, if a municipality or a cooperative were interested in buying the Southern Power, assuming Southern put it back on the market, would they be required to conduct an RFP?

A I don't believe so. Since there is no tie to the Power Plant Siting Act, no requirement exists as far as I know to do an RFP.

Q And would they have to get Commission approval for any cost-recovery?

A I don't believe so, no.

MR. PERKO: If I could have one second, Your Honor, look over my notes. (Pause.)

Nothing further.

CHAIRMAN BAEZ: Exhibits.

MR. PERKO: Yes, Your Honor. If Progress Energy could move its Exhibits SSW-1, SSW-2, SSW-3, SSW-4R, SSW-5, and SSW-6 into the record. I believe they are marked as Exhibits 4 --

CHAIRMAN BAEZ: Well, let me -- hold off on it a second. I'll give you the numbers. I have 4, 5, 6, 7 and 8. Mr. Waters is still set to appear on rebuttal, so we are going to hold off 15 and 16 until we are finished with his rebuttal. Does that sound all right to you?

MR. PERKO: You have properly corrected me. Thank you.

CHAIRMAN BAEZ: I finally got one in.

Mr. Bushee, for you I have 17, 18, 19, 20, 21, 22, 23, 24, and 25.

MR. BUSHEE: That is correct, although I would note that Exhibit 18 will be a late-filed.

CHAIRMAN BAEZ: And I do have Late-filed Exhibit 18, as well. If there are no objections, 17 through 25 will also be admitted into the record and the late-filed exhibit would be -- I want to say subject to check, but I don't know if Mr. Perko even needs to reserve his right to object to the late-filed.

MR. PERKO: I would ask Mr. Waters if he expects any confidential information to be in it.

THE WITNESS: Obviously -- well, to do the numbers, there will be confidential information in the exhibit as it is laid out, because I will have to do the formulas per the contract.

CHAIRMAN BAEZ: All right. So then what we can do is we can label it as Confidential 18. You had mentioned that you could turn it around in a day or two?

THE WITNESS: I'm going to try and do that.

CHAIRMAN BAEZ: Would Monday be all right?

THE WITNESS: Monday is fine.

CHAIRMAN BAEZ: Okay. Monday okay with you, Mr Bushee?

MR. BUSHEE: Yes.

CHAIRMAN BAEZ: Very well. Without objection, show 17 through 25 admitted into the record.

(Exhibits 4 through 8 and 17 through 25 admitted into the record.)

MR. PERKO: Mr. Chairman, one final matter. We had discussed substituting the full copy of, I believe it is Exhibit 21, and my assistant has copies for everyone.

CHAIRMAN BAEZ: For the record, show that we are, with the agreement of all parties, substituting the Burns and McDonnell report in Confidential Exhibit 21 to reflect the complete report.

MR. PERKO: And, Mr. Chairman, unfortunately the copies are not stamped confidential, but they are confidential.

CHAIRMAN BAEZ: We'll make sure that that is reflected. And if at some point when we break, and I suspect we'll break after we get done excusing Mr. Waters, if you can make sure and collect the Burns and McDonnell reports that are incomplete, because they still remain confidential, you all can dispose of them as you need to. Is there anything else at this point?

We are going to break for ten minutes, and then we will take up Mr. Brubaker. We're in recess.

(Recess.)

CHAIRMAN BAEZ: Let's go back on the record.

Go ahead, Mr. Bushee.

MAURICE E. BRUBAKER

was called as a witness on behalf of White Springs Agricultural Chemicals, Inc., and having been previously duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. BUSHEE:

Q Mr. Brubaker, you have already been sworn?
A Yes, I have.
Q And you have before you Exhibits 9 through 14?
A Yes.
Q And those consist of your testimony and the attached exhibits?

A That is correct.

Q Do you have any changes to your testimony?

A I do not.

MR. BUSHEE: With that, the witness is available for cross-examination.

CHAIRMAN BAEZ: In the meantime, we will show the direct testimony of Witness Brubaker entered into the record as though read, and also let the record show that his exhibits, including the confidential version of his direct testimony are numbered Exhibits 9 through 14.

BEFORE THE
PUBLIC SERVICE COMMISSION OF FLORIDA

In re: Petition for approval of two unit power sales agreements with Southern Company Services, Inc. for purposes of cost recovery through capacity and fuel cost recovery clauses, by Progress Energy Florida, Inc.	**Docket No. 041393-EI**

Direct Testimony of Maurice Brubaker

Q **PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

A Maurice Brubaker. My business address is 1215 Fern Ridge Parkway, Suite 208, St. Louis, Missouri 63141-2000.

Q **WHAT IS YOUR OCCUPATION?**

A I am a consultant in the field of public utility regulation and president of Brubaker & Associates, Inc., energy, economic and regulatory consultants.

Q **PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.**

A I have been involved in the regulation of electric utilities, competitive issues and related matters over the last three decades. Additional information is provided in Appendix A, attached to this testimony.

INTRODUCTION AND SUMMARY

Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

A I am appearing on behalf of White Springs Agricultural Chemicals, Inc. d/b/a PCS Phosphate – White Springs (White Springs). White Springs is a manufacturer of fertilizer products with plants and operations located within Progress Energy Florida Inc.'s (PEF) service territory at White Springs, and receives service under numerous rate schedules. During calendar year 2004, White Springs purchased approximately $20 million of power from PEF.

Q WHAT IS THE PURPOSE OF THE TESTIMONY YOU ARE SUBMITTING?

A This testimony will address the request of PEF that the Commission approve as reasonable and prudent for cost recovery purposes two Unit Power Sales agreements (UPS) with one or more subsidiaries of the Southern Company (Southern). The proposed agreements provide for the sale to PEF of 74 megawatts of coal-fired power from Scherer Unit 3 in Georgia, which is owned by Georgia Power Company and Gulf Power Company, and 350 megawatts from a gas-fired combined cycle facility known as Franklin Unit No. 1, which is owned by an unregulated affiliate of Southern, known as Southern Power.

Q PLEASE SUMMARIZE YOUR FINDINGS AND RECOMMENDATIONS?

A My findings and recommendations may be summarized as follows:

1. The short-term cost effectiveness analysis submitted by PEF was grossly overstated, and should not be relied upon.

2. PEF has significantly overstated the claimed economic benefits associated with proposed UPS transactions. By PEF's own numbers,

they are uneconomic over the long-term evaluation period, and any "front end" savings are marginal, at best.

3. PEF should have given serious consideration to replacement of the UPS agreements with constructed or purchased solid fuel capacity well in advance of the expiration of those agreements, but apparently did not do so.

4. PEF has not demonstrated that the "base" plan which it uses to measure the impacts of the two proposed new UPS agreements is a least cost plan. It therefore cannot be claimed as an appropriate benchmark for this purpose.

5. Given the significant amount of capacity at issue with the expiration of the UPS agreements, PEF should have solicited the market in a comprehensive manner, such as through an RFP, for alternative products to compare to the UPS proposal.

6. PEF's projections indicate a sharply increasing reliance upon natural gas-fired generation, and a significantly reduced degree of diversity in its resource portfolio.

7. PEF has indicated that construction of a new coal-fired facility in the 2013 timeframe may be doable. Rather than pursue the proposed UPS agreements at this time, PEF should actively consider installation of a solid fuel facility as early as possible.

8. The existing UPS agreements do not expire until May of 2010, fully five years from now. There is no rush to enter into new agreements for the 2010-2015 time period.

9. There are many uncertainties with respect to the transmission service required to implement the proposed UPS contracts.

10. Various "non-price" factors that PEF cites in support of the UPS agreements are not sufficiently important or quantified to be given any significant weight by the Commission.

11. The Commission should not approve the proposed UPS agreements. Rather, PEF should be required to more fully analyze alternatives prior to any decision being made.

12. Because of the problems with how PEF has approached the capacity expansion issue, and evaluation of the proposed UPS agreements, the Commission should reserve for the pending rate case the question of whether a downward adjustment should be applied to PEF's return on equity.

 171

13. Should the Commission decide to allow PEF to enter into the UPS agreements in this case, it should make them subject to a prudency challenge whenever PEF would seek cost recovery.

PEF'S ECONOMIC ANALYSIS

Q WHAT ECONOMIC JUSTIFICATION HAS PEF SUBMITTED IN SUPPORT OF ITS PROPOSAL THAT THE COMMISSION APPROVE THE UPS AGREEMENTS?

A PEF provided a summary of its economics justification on Exhibit SSW-3 and also on Exhibit SSW-4.

Exhibit SSW-3 shows that over a 45-year period, consisting of the approximately five-year term of the proposed UPS agreements, followed by a 40-year term to capture end effects, the proposed transaction is not beneficial to consumers, relative to what PEF describes as its alternative base plan. On a net present value basis, Exhibit SSW-3 shows that PEF expects the result of entering into the UPS agreements, as compared to pursuing its base plan, would be a net detriment to consumers in the range of $5 million to $11 million. Thus, on its face, and by PEF's own admission, the proposed transactions are not as favorable to consumers as what PEF describes as its base plan.

Q WHAT DOES EXHIBIT SSW-4 PURPORT TO SHOW?

A It purports to show savings under the UPS contracts on an annual and a cumulative present value revenue requirement basis over the same time horizon. PEF's original exhibit claimed cumulative present value savings of $133 million during the five-year term of the proposed UPS contracts. PEF just recently requested permission to file supplemental testimony which acknowledges that it overstated the savings by $89 million, such that it now claims benefits of $44 million.

Q HAVE YOU EXAMINED PEF'S ORIGINAL AND REVISED CLAIMS?

A Yes. We have made an alternate analysis, using the costs associated with deferring or advanced generation units. However, since we had no way to check the claimed production cost differentials, we have used PEF's claimed production cost savings and other costs. The calculations are summarized on Exhibit MEB-1 ( ). This exhibit has been marked confidential. It shows the annual revenue requirements associated with the comparison of the UPS units to the Company's base case, and calculates the difference each year in revenue requirements. The results are significantly different than what PEF initially calculated. They show smaller front-end benefits than PEF's proposed revised calculations. They are graphed and presented on Exhibit MEB-2 ( ), which is in a format similar to Exhibit SSW-4, and therefore has not been marked confidential.

Q WHAT IF PEF'S CLAIMS FOR SAVINGS DURING THIS INITIAL PERIOD WERE ACCEPTED AT FACE VALUE?

A With respect to the claim that the front-end benefits are substantial, amounting to $133 million (revised to $44 million) over the five-year term of the contracts, even if we accept all of PEF's calculations as appropriate and relevant, extending the time horizon one more year (i.e., to one year beyond the end of the contact term) the same information and calculations demonstrate that these claimed benefits

contains some of the units that were included in the Ten-Year Site Plan as of December 31, 2004, it also includes several units (namely four coal units) which were not included in the previous Ten-Year Site Plan.

Furthermore, no information has been provided in connection either with this base plan or with what was provided in the Ten-Year Site Plans to demonstrate that any of these expansion plans are the least cost expansion plans and appropriate for meeting PEF's expected load obligations in an economical and reliable manner.

Q YOU SAY THAT PEF STARTED WITH THIS BASE PLAN. HOW DID IT THEN VIEW OR TEST THE IMPACT OF THE UPS AGREEMENTS?

A It simply introduced the UPS agreements into the resource portfolio for the period June 2010 through December 2015, and then adjusted the resources in the base plan in a manner that it says it would do were it to enter into these UPS agreements. The net effect, according to PEF, was to defer the installation of two generic combined cycle units, and to advance the installation date of one combustion turbine unit and one pulverized coal unit.

Having adjusted the resource expansion plan in this manner, PEF then ran an economic analysis of the fixed and variable costs, including purchased power and generation variable costs, and compared the revenue requirements under the two plans. This was the source for the numbers displayed on Exhibits SSW-3 and SSW-4, on which I have previously commented.

Q DID PEF SUPPLY ANY ANALYSIS DEMONSTRATING THAT THE BASE PLAN WHICH IT USED AS A BENCHMARK FOR COMPARISON WAS THE LEAST COST PLAN?

A No, as I indicated above, it did not. Thus, even assuming that all of the economic calculations were performed correctly, all the comparison tells us is that the proposed UPS transaction is between $5 million and $11 million less desirable from the customers' perspective than this plan, which has been called the base plan, but which has not been shown to be the least cost or best plan in the first place.

Q DO THE PROPOSED UPS AGREEMENTS MERELY EXTEND OR MODIFY THE EXISTING UPS AGREEMENTS?

A No, they do not. Whereas presently there is one UPS agreement, the proposal is to have two agreements. More fundamentally, however, the current agreement provides for roughly 80 megawatts of coal-fired power from the Scherer plant and 320 megawatts of coal-fired power from the Miller plant. As noted above, the Scherer plant is jointly owned by Georgia Power Company and Gulf Power Company. The Miller plant is owned by Alabama Power Company. The proposed new UPS agreements continue to provide some (reduced to 74 MW) amount of power from Scherer Unit 3, but the pricing is different. The second contract provides 350 MW gas-fired power from the combined cycle Franklin units, and is an entirely new agreement with a different party.

In addition, the present UPS agreement bundles generation and transmission service together, while the proposed agreements require PEF to seek and contract for transmission service separately from the UPS generating supply.

Thus, instead of being extensions or minor changes to existing agreements, these are entirely new agreements that are materially different.

Q **WHERE ARE THESE PLANTS LOCATED?**

A The Scherer plant is located in Monroe County, Georgia. The Miller plant is located in Jefferson County, Alabama, and the Franklin plant is located near Smiths, Alabama.

Q **ARE THE MILLER AND FRANKLIN PLANTS CLOSE TO EACH OTHER?**

A No, they are not. They are over 100 miles apart and connected to different portions of the Southern Company transmission system. This adds complexity to the transaction because of the need to separately secure transmission service from a facility not involved in the current transaction.

Q **WHY IS THIS AN ISSUE?**

A If the source of the power is changed from the Miller plant to the Franklin plant, the load flows on the Southern system will change. Whether or not the change in load flows adversely affects the transmission system from a thermal or stability point of view must be studied. I will address this in more detail later in this testimony.

Q **HOW LONG HAS PEF KNOWN THAT THE EXISTING UPS AGREEMENT WOULD EXPIRE IN MID-YEAR 2010?**

A This has been a known fact since 1988, when the contract was initially executed. Thus, PEF has had more than adequate time to seriously consider and evaluate appropriate alternatives to these contracts upon their expiration. As explained later in the testimony, it has not done so.

Q **HAVE YOU REVIEWED PEF'S RECENT TEN-YEAR SITE PLANS?**

A Yes. In response to Production of Documents (POD) No. 5, PEF produced copies of the Ten-Year Site Plans filed in the spring of 2001 through 2005. Little or no supporting data was supplied for the 2001 and 2002 site plans. For the more recent plans, there is some discussion of coal-fired alternatives, but the only analysis presented is rather simplistic "screening curves" which examine the theoretical crossover points that show where one technology becomes more economical than another. No economic analyses of coal-fired alternatives were presented as a part of the supporting documentation for the Ten-Year Site Plans, and the resource selections from those plans were exclusively gas-fired combined cycle units (and combustion turbine units). In none of these plans did coal apparently receive a serious analysis by PEF.

Q **IS THERE ANY EVIDENCE THAT PEF GAVE SERIOUS CONSIDERATION TO REPLACING THE UPS AGREEMENTS, UPON THEIR EXPIRATION IN 2010, WITH COAL-BASED POWER?**

A No, quite to the contrary. In POD No. 8, White Springs made the following request:

> "Please provide a copy of any and all documents and communications related to Progress's consideration, evaluation or study of building or acquiring coal-fired generating capacity to replace the coal-fired capacity purchased under Progress's existing unit power sales agreement with SCS."

In response thereto, PEF replied:

> "There are no documents responsive to this request."

This makes it perfectly clear that PEF did not give serious consideration to replacing the expiring coal-based purchased power agreements with either coal-based purchased power contracts or with a constructed facility.

Q SHOULD PEF HAVE CONSIDERED THIS APPROACH TO REPLACING THE CAPACITY FROM THE EXPIRING UPS AGREEMENTS?

A Yes. I believe it was particularly important that PEF undertake these considerations after the gas price spikes that occurred beginning in 2000. That event, coupled with subsequent spikes and escalating price levels, and the continued construction of gas-fired electric generation capacity (by merchants and others) certainly gave rise to concerns that natural gas prices would be both high and volatile. I believe PEF should have devoted more attention to analyzing the comparative risks and economics of natural gas and coal-fired generation.

Q IN ADDITION TO THIS FACTOR, ARE THERE OTHER REASONS WHY PEF SHOULD HAVE BEEN ACTIVELY CONSIDERING ACQUIRING COAL-FIRED POWER?

A Yes. From a resource diversity standpoint, PEF's current projections indicate a significantly increasing dependency on natural gas. For example, the Ten-Year Site Plans show an increase in the percentage of generation from oil and gas-fired resources from 28% in the year 2000, to a projected 34% in 2005, 42% in 2010, and 54% in 2014. This factor also should have led PEF to more actively consider adding coal-fired generation to the system, not only to replace the expiring UPS agreements, but also to meet part of the load growth requirements and maintain closer to an historic fuel diversity. Exhibit MEB-3 ( ) shows this pattern.

Q **HAS THE FLORIDA PSC STAFF COMMENTED ON THIS TREND IN DEPENDENCY ON NATURAL GAS?**

A Yes. The Commission's Division of Economic Regulation issued a report in December of 2004 entitled "A Review of Florida Electric Utility 2004 Ten-Year Site Plans." At Page 6 of that report, in a section entitled "**AREAS OF CONCERN** – *IMPACT OF PLANS ON FUEL DIVERSITY*", the Staff commented as follows:

> "Over the past several years, utilities across the nation and within Florida have selected natural gas-fired generation as the predominant source of new capacity. If this trend continues, natural gas usage will approach the levels of oil usage that Florida was experiencing just prior to the oil embargoes of the 1970's. Recent past experience has shown that natural gas prices can be volatile. Further, Florida's utilities project a wide range of prices for natural gas. These facts, coupled with the Florida utilities' historic under-forecasting of natural gas price and consumption, could further strain Florida's economy. In the 1970's, the Commission took action to encourage the utilities to diversify their fuel mix in an effort to mitigate volatile fuel prices. Based on current fuel mix and fuel price projections, Florida's utilities should

> explore the feasibility of adding solid fuel generation as part of future capacity additions."

Later in the report, at Page 21, in a section entitled "**GENERATING UNIT SELECTION**" Staff commented as follows

> "According to the utilities' *Ten-Year Site Plans*, natural gas is forecasted to play an even more dominant role in electric power generation in Florida over the next ten years. To minimize price and supply volatility, electric power generation must rely on multiple fuel sources. As a result, Florida's utilities should evaluate potential sites for coal capability. To lessen the capital cost impact of building coal-fired units, utilities should look at the possibility of joint ownership of future coal units. Florida's municipal utilities have a successful history of sharing investment costs associated with coal units. Finally, utilities should investigate the possibility of receiving financial assistance through the DOE's CCT Program. As emerging research and development in coal-fired generation reduces high capital costs, emissions, permitting lead times, and investment risk, coal could again play a critical role in electric power generation in Florida."

I believe Staff's comments are right on point, and merit serious consideration. Additional coal-fired capacity in Florida brings many benefits that are not available from gas-fired combined cycle facilities located in Alabama.

Q **IS THERE ANY RECENT EVIDENCE THAT PEF IS NOW LOOKING MORE CLOSELY AT INSTALLING COAL-FIRED UNITS?**

A Yes. As I indicated earlier, the so-called "base" plan, which PEF has advanced as what it would do absent the proposed UPS agreements, contains four pulverized coal units beginning in the year 2015. Also, in 2004 we begin to see more serious studies, including some conducted by outside parties, of the comparative economics of various types of solid fuel units. These studies indicate the increasing attractiveness of these types of units in light of changes in fuel markets.

In response to Interrogatory No. 15, PEF claims that it would take at least eight years to do the necessary development and construction for a coal-fired generating station, and if one accepts that claim, 2013 would be the earliest feasible in-service date.

In light of these circumstances and other factors noted above, PEF should intensify its efforts in regard to the analysis and development of coal-fired resources, and their expeditious construction if such analysis reveals them to be appropriate choices. So far, it appears that PEF has not undertaken this analysis.

Q OTHER THAN THE ECONOMIC ANALYSIS ATTACHED TO MR. WATERS' TESTIMONY (SSW-3 AND SSW-4) IS THERE ANY EVIDENCE THAT PEF COMPARED THE PROPOSED NEW UPS AGREEMENTS TO ANY OTHER ALTERNATIVE SOURCE OF POWER – EITHER FROM A CONSTRUCTED FACILITY, OR FROM ALTERNATIVES AVAILABLE FROM THIRD PARTIES IN THE MARKET?

A There is no such indication. PEF did not conduct any Requests for Proposals (RFPs) or take any other steps to ascertain the possible availability of substitutes for part or all of the expiring UPS agreement. In fact, White Springs asked the following as Interrogatory No. 5:

> "(a) Were any of "recent Requests for Proposals (RFPs)" referred to in line 10 of page 6 of the Direct Testimony of Samuel S. Waters undertaken in connection with the expiration and/or replacement of Progress's existing unit power sales agreement with SCS? (b) If your response to Interrogatory No. 5(a) is anything other than an unqualified "no," please identify each such Request for Proposals that was undertaken in connection with the

expiration and/or replacement of Progress's existing unit power sales agreement with SCS.

In response thereto, PEF stated: "(a) No."

Q WOULD IT HAVE BEEN PRUDENT FOR PEF TO CONDUCT AN RFP FOR THIS PURPOSE?

A Yes, it would have been appropriate and prudent for PEF to do so. Good practice when considering entering into transactions of this magnitude, representing over 400 megawatts of capacity and with a cost (estimated by PEF) over the five-year term of the contract of nearly [redacted] in fixed costs, plus fuel, would be to conduct a thorough review of the market to ascertain if there are any other options available which should be considered.

An RFP process is an organized and comprehensive way to approach the market and to solicit input. It is used quite frequently, and in fact PEF uses an RFP approach when it is testing the construction of new facilities. If a comprehensive search is not conducted, PEF may miss economical opportunities available in the marketplace. Furthermore, without this search, PEF cannot demonstrate that its chosen course of action is the appropriate one.

TRANSMISSION ISSUES

Q HAS PEF SECURED THE TRANSMISSION RIGHTS ON THE SOUTHERN SYSTEM THAT ARE NECESSARY TO DELIVER THE POWER FROM THE PROPOSED UPS AGREEMENTS?

A No, it has not.

Q PLEASE DESCRIBE THE TRANSMISSION SERVICE ARRANGEMENTS IN CONNECTION WITH THE UPS AGREEMENTS.

A In his Direct Testimony at Page 12, Mr. Waters summarizes the transmission requirements under the UPS Agreements:

> "The agreements call for PEF to submit a request for sufficient transmission Capacity to Southern Company Transmission within 30 days of the effective date of the agreement, November 24, 2004. The agreements further call for PEF to make commercially reasonable efforts to obtain an offer for transmission service by February 16, 2006, a date which may be extended by mutual consent. If any or all of the required transmission service cannot be provided, PEF will notify Southern Company, as seller, of the unavailability. The contracts also provide for PEF notification to Southern Company of the circumstances where transmission may be offered at a total cost greater than the embedded rate for Long Term Firm Transmission Service under Southern Company Transmission's Open Access Transmission Tariff (OATT). Upon notification, Southern Company has the option of offering to sell, including by reassignment, up to the required amount of transmission service, and/or offsetting any transmission costs above the OATT rate.
>
> If the amount of available transmission is less than [redacted] for the Franklin agreement, or if the transmission available at the OATT rate is below [redacted] PEF may terminate the agreement. The similar threshold in the Scherer agreement is [redacted]."

Q WHAT IS THE STATUS OF PEF'S TRANSMISSION REQUESTS?

A Again, in his Direct Testimony at Page 13, Mr. Waters summarizes the status of PEF's transmission service requests:

> "PEF submitted its requests for transmission on November 30, 2004, within the 30 day period required by the agreements. These requests were submitted to Southern Company Transmission as "rollover" requests of the existing transmission paths from Southern Company's Scherer plant and Miller plant under PEF's current UPS agreement. On March 8, 2005, these requests for transmission were accepted and conditionally

confirmed in a letter agreement signed by the parties. The letter agreement stated that Southern Transmission would accept the requests for transmission, and on March 15, the transmission requests were confirmed by PEF. The transmission agreements were contingent on PEF's ability to redirect the Miller transmission path to the Franklin plant, which PEF requested on March 15.

The next step in the process will be a System Impact Study ("SIS") and Southern Company Transmission has already sent notification of this study to PEF. PEF must respond with a deposit towards the study in the immediate future. Once PEF has submitted the deposit, Southern Company Transmission will begin the SIS to either confirm the transmission path for the Franklin purchase, or notify PEF of any system impacts that need to be addressed. If there are system impacts, an additional Facilities Study would follow. However, if no impacts are identified, the transmission request would be confirmed, in effect making PEF the owner of the Scherer and Franklin transmission paths at that time. This could occur any time after our submittal of the SIS deposit."

Q **DO YOU HAVE ANY DOCUMENTATION CONCERNING THE STATUS OF PEF'S TRANSMISSION SERVICE REQUESTS?**

A Yes. In discovery, White Springs asked PEF to explain what it had done to obtain transmission to implement the terms of the UPS Agreements. PEF's response to Interrogatory No. 8 is consistent with Mr. Waters's testimony noted above, and states:

"Please describe Progress's efforts and activities undertaken to obtain transmission to implement the terms of the UPS Agreements.

A. Section 7.4 of the UPS Agreements discusses the Parties requirements for obtaining transmission. Specifically, 7.4.1 required PEF to submit a request for transmission on Southern Company's OASIS within thirty days following the Effective Date of the Agreements. The Effective Date of the Agreements is November 24, 2004.

PEF initiated transmission requests on November 30, 2004 (see Southern OASIS Reference Numbers 519354, 519355),

> requesting rollover of PEF's existing service for Plant Scherer to the Southern-Florida Interface and for Plant Miller to the Southern Florida Interface.
>
> Southern Company then requested PEF to submit two documents: (1) Application for Firm Point-to-Point Transmission Service; and (2) Southern Company Transmission Deposit Information Sheet PEF submitted these documents, along with the Company's deposit, on December 15, 2004.
>
> Southern Company then wrote a Letter Agreement that detailed the study that they would perform, and mailed it to PEF on March 7, 2005. The Parties agreed to terms of the Letter Agreement on March 8, 2005. This Letter Agreement states that Southern would conditionally confirm both of PEF's transmission requests.
>
> On April 12, 2005, Southern Company sent PEF a notice stating that a System Impact Study would be required to determine available transmission capacity. On or before April 18, 2005, PEF submitted a signed original of the System Impact Study agreement. Payment in the amount of $10,000 was wire transferred to Southern Company on April 21, 2005 for the System Impact Study to be performed. Southern Company has acknowledged receipt of PEF's payment."

White Springs also requested a copy of any and all documents related to PEF's response to Interrogatory No. 8, and PEF produced a series of e-mails and agreements concerning the transmission service requested by PEF in response to POD No. 13. I have attached this as Exhibit No. MEB-4 (   ).

Q WHAT IS PEF'S APPARENT BELIEF CONCERNING WHETHER ITS TRANSMISSION SERVICE REQUEST WILL BE GRANTED?

A PEF appears confident that the request it has submitted for redirecting its point of receipt for transmission service from Plant Miller to Plant Franklin will be granted. For example, in response to White Springs's Interrogatory No. 9, PEF stated that it is not aware of any transmission constraints that could impede the implementation of the contract. Mr. Waters also testified at Page 14 of his Direct

Testimony that he had no "reason to believe that PEF will not be able to obtain sufficient transmission service to deliver the proposed purchases from Scherer and Franklin." He based his conclusion on his observation that the magnitude of the purchases is basically the same as is currently being purchased, and that, although a different point of receipt was involved for the Franklin purchase, he said that he had no reason to believe that delivery from the new source will be a problem.

Q WHAT ABOUT TRANSMISSION CAPACITY AT THE FLORIDA-GEORGIA BORDER?

A White Springs also asked in discovery about PEF's transmission rights at the Florida-Georgia interface. In response to Interrogatory No. 7, PEF explained:

> "With respect to the transmission capacity at the Georgia-Florida Interface, please (a) identify each owner of such capacity; and (b) identify and describe Progress's rights to such capacity, including but not limited to the amount of such capacity (in MW), the quality (firmness) of such rights, the duration of such rights, and any rollover rights concerning such rights.
>
> A. a) Based upon the 1990 "Florida-Southern Interface Allocation Agreement", the owners of the Florida – Southern interface are Florida Power and Light Company (FPL), Florida Power Corporation (CORP), Jacksonville Electric Authority (JEA) and the City of Tallahassee (TAL). For purposes of allocation, the Joint Ownership Party (JOP) means Florida Power and Light Company (FPL) and Jacksonville Electric Authority (JEA) collectively.
>
> b) **Subject to check, PEF believes the following information highlighted in yellow is CONFIDENTIAL PROPRIETARY INFORMATION and therefore subject to the Confidentiality agreement between PEF and White Springs.** The Firm allocated Import capability, based on current conditions, is as follows:
>
> [redacted]

> [redacted] Southern to Florida The allocation agreement was effective June 1, 1990 and automatically renews each year. As this agreement predates FERC Order 888 and subsequent orders, rollover rights for purchases existing at the time of the order are grandfathered in."

Mr. Waters also testified at Page 14 of his Direct Testimony that the interface allocation that currently accommodates the UPS purchases from Southern is sufficient to accommodate the proposed purchases.

Q DO YOU SHARE MR. WATERS'S OPTIMISM ABOUT THE AVAILABILITY OF TRANSMISSION?

A Notwithstanding PEF's confidence, it seems speculative at this point to try to determine whether the proposed transmission arrangements are sufficient from a reliability and economics standpoint. Southern has not yet completed its System Impact Study of the rollover and redirected transmission requests.

Q HAS PEF EXERCISED ITS ROLLOVER RIGHTS WITH RESPECT TO THE TRANSMISSION SERVICE TO IMPLEMENT THE UPS AGREEMENTS?

A It appears so. PEF's response to White Springs's Interrogatory No. 8 indicate that PEF submitted its transmission service requests in connection with the UPS Agreements using PEF's rollover rights under the current UPS agreement. Mr. Waters's testimony also states at Page 13 that the transmission requests were submitted as rollover requests.

Q PLEASE EXPLAIN FERC'S ELECTRIC TRANSMISSION ROLLOVER RIGHTS POLICIES.

A Section 2.2 of FERC's *pro forma* open access transmission tariff provides that existing long-term firm transmission service customers (including bundled wholesale requirements customers) have the right to continue to take transmission service from the transmission provider when the contract expires, rolls over, or is renewed. This transmission reservation priority is independent of whether the customer continues to purchase capacity and energy from the transmission provider or selects a different supplier, and it is an ongoing right that may be exercised at the end of all firm contract terms of one year or longer, unless the renewal period expires for a given customer to exercise its rollover right. Section 2.2 of Southern's OATT is no different than the section 2.2 of the *pro forma* open access transmission tariff. I have included a copy of section 2.2 of Southern's OATT in Exhibit No. MEB-5 ( ).

Q WHAT IS THE PURPOSE OF THIS ROLLOVER RIGHTS POLICY?

A FERC concluded in its open access rule (Order No. 888) that once a transmission provider evaluates the impacts on its system of providing transmission service to a customer and decides to grant a request for service, the rollover rights policy obligates the transmission provider to plan and operate its system with the expectation that it will continue to provide service to that customer, should the customer request rollover of its contract term within 60 days of the initial term's expiration. That policy applies to existing customers under long-term bundled wholesale contracts. If the transmission system becomes constrained such that the transmission provider cannot satisfy existing customers, then the obligation is on the transmission provider to either curtail service pursuant to the provisions of its OATT or to build more capacity to relieve the constraint.

Q **WHAT IS THE DEADLINE FOR SUBMITTING A REQUEST FOR TRANSMISSION SERVICE USING ROLLOVER RIGHTS?**

A Under FERC's current policies, a transmission customer seeking to exercise its rollover rights under section 2.2 of the OATT must submit its request by no later than 60 days before the customer's existing transmission service agreement expires. The transmission customer does not need to submit its request before that time, even if other customers or eligible customers have submitted requests for transmission service that would conflict with the rollover customer's transmission rights. Indeed, PEF seems to recognize this point. In response to White Springs's Interrogatory No. 10, PEF states:

> "Please identify the person(s) in the Southern Company transmission queue with a priority higher than that of Progress with respect to Progress's request for transmission capacity intended to be used to implement the UPS Agreements.
>
> A. Since the transmission associated with the UPS Agreements is subject to rollover rights associated with the existing agreements, there are no entities with a priority higher than Progress."

Q **WHAT DOES THAT MEAN FOR PEF'S ROLLOVER RIGHTS?**

A PEF's rollover rights under Southern's OATT's for transmission service under the existing UPS agreement do not expire until 60 days before the current UPS agreement expires on May 31, 2010. So, PEF has until April 2, 2010 to exercise its rollover rights.

Accordingly, I do not believe there is any merit to PEF's claim in its April 15, 2005 Answer to White Spring's Petition for Hearing that "To maintain the rollover rights, PEF must submit a System Impact Study Agreement for the redirection request in the immediate future, at which point Southern can act on the request at any time." (Answer at 3.)

There are at least three reasons for this belief. First, it is important for the Commission to understand that PEF will not lose its rollover rights until April 2, 2010 – the date that is 60 days before the expiration of the current UPS agreement. That is what Southern's OATT and FERC's rollover rights policy provides. Stated differently, PEF's rollover rights are independent of the UPS Agreements. Nothing in the current UPS agreement, the Southern OATT or FERC's rollover rights policy jeopardizes PEF's rollover rights if it fails to act at this time.

Second, documents and information provided to White Springs in discovery indicate that PEF already has submitted its SIS deposit and signed the SIS Agreement. (See POD No. 13 in Exhibit No. MEB-4 ( ); and PEF's response to Interrogatory No. 8.) That means that PEF has already put the wheels in motion for its transmission request – it will be acted on whether or not this Commission approves the UPS Agreements. There is therefore no need to rush to judgment here.

Third, PEF's real concern seems to be its position in the Southern transmission request queue with respect to its redirect request. That redirect request would change the point of receipt for transmission service in connection with the Franklin UPS Agreement from Plant Miller to Plant Franklin. Apparently, Southern and PEF are treating the transmission arrangements under the existing UPS agreements as point-to-point transmission service in which Plant Miller and Plant Scherer are the points of receipt (and the Florida-Georgia interface as the point of delivery). Under the rollover rights policy, Plant Miller and Plant Scherer are guaranteed as points of receipt. Under section 22.2 of the Southern OATT, redirecting Plant Miller to Plant Franklin on a firm basis would require a new study, and would be subject to any requests with a higher priority (a copy of section 22.2 of Southern's OATT is included in my Exhibit No. MEB-5 ( )). However, moving quickly to "lock in" Plant Franklin as a point of receipt begs the question of whether Plant Franklin is the best source.

Q **DO THE UPS AGREEMENTS HAVE ANY EFFECT ON THE CAPACITY AT THE FLORIDA-GEORGIA INTERFACE?**

A No. The allocation of the transmission capacity at the Florida-Georgia interface is governed by separate agreements among the owners of the interface capacity. That allocation should not be affected by the power supply arrangements of the parties who are allocated and use the capacity. In addition, Mr. Waters states at Page 14 of his direct testimony that the interface allocation that currently accommodates the UPS purchases from Southern is sufficient to accommodate the proposed purchases. But, nowhere does he state that the interface allocation may be used ***only*** for the delivery of the power under a UPS agreement with Southern.

Q WHAT DOES MR. WATERS CONCLUDE REGARDING THE TIMING OF THE COMMISSION'S DECISION IN THIS PROCEEDING AS IT RELATES TO TRANSMISSION?

A Mr. Water claims at Page 15 of his direct testimony that there is a chance that PEF could be committed to transmission without approval of the corresponding purchases. His conclusion is based on his observation that transmission service could be offered at any time after PEF submits the SIS deposit. He goes on to note that the date by which PEF must obtain Commission approval of the UPS Agreements is tied to the notices related to transmission service. According to Mr. Waters, a delayed decision by the Commission may put the agreements at "risk."

Q WHAT DO YOU MAKE OF THESE CONCLUSIONS?

A Mr. Waters has put the cart before the horse. In effect, Mr. Waters is arguing that the Commission should approve the UPS Agreements because PEF will have obtained transmission service to implement the contracts' terms.

Moreover, the jam that PEF apparently finds itself in is entirely of its own making. If the Commission approved PEF's approach here, it would mean that regulated utilities could agree upon compressed schedules for approval in their agreements, and then use those schedules to rush the Commission into approval. This is especially problematic in light of the overstated economic benefits of the UPS Agreements.

Q WHAT ABOUT PEF'S CLAIM THAT IT WOULD BE REQUIRED TO TAKE THE TRANSMISSION CAPACITY IMMEDIATELY IF SOUTHERN'S SYSTEM IMPACT STUDY SHOWS THE REQUEST TO REDIRECT MILLER TO FRANKLIN CAN BE ACCOMMODATED?

A PEF made the decision to enter into the UPS Agreements and to agree to the clauses requiring it to obtain transmission without first having obtained Commission approval. PEF made the decision to agree to and submit a conditional firm transmission service request in which it would be deemed to have accepted the transmission upon completion of the SIS. It is difficult to see why PEF's decisions in these matters should force the Commission to approve the UPS Agreements.

More important, the [redacted]

[redacted]

There is absolutely nothing automatic about PEF acquiring the redirected transmission, even if it is available. Moreover, there is nothing in the signed SIS agreement (also included at Pages 43 and 44 in Exhibit No. MEB-4 ( ), and also marked as confidential) [redacted]

Under the OATT, a transmission customer (PEF) can decide whether to proceed with its transmission service request after the transmission provider (Southern) issues its SIS report. (Section 19.3 of Southern's OATT, which is included in my Exhibit No. MEB-5 ( ).) Finally, [redacted]" Quite simply, PEF is not locked into any redirected transmission arrangements at this time. Indeed, if PEF should find itself in the position of having committed to transmission without Commission approval of the UPS agreements it will be as a result of its own actions and the Commission should find that PEF's shareholders, not its customers, are responsible for all transmission related costs.

Q ARE THERE ANY FACTORS THAT WOULD MITIGATE SUCH AN OUTCOME HERE?

A Yes. PEF completely ignores its ability to remarket the transmission capacity if it is unable to use it. Section 23.1 of the Southern OATT permits a transmission customer to release its firm reserved capacity on a short-term basis, subject to recall. (A copy of section 23.1 of Southern's OATT is included in my Exhibit No. MEB-5 ( ).) If PEF finds itself locked into a transmission contract that it is unable to use, it can mitigate its damages by reassigning its capacity, either permanently or until it is able to make use of it.

In addition, PEF could request deferral of the commencement of service under its transmission service agreement. Section 17.7 of Southern's OATT permits up to five one-year deferrals of the service commencement date, upon payment of one month's transmission service charges. (A copy of section 17.7 of Southern's OATT is included in my Exhibit No. MEB-5 ( ).) If PEF is unable to use the transmission capacity that it reserves as a result of its pending request, then it can exercise its rights to defer commencement of service by paying one month's transmission charges. That procedure, which could not be used until the June 1, 2010 service commencement date, may be helpful at that time if the capacity is not needed by PEF and there is not a market for reassignment.

Neither Mr. Waters nor PEF makes any mention of these procedures that would allow PEF to mitigate its exposure to costs resulting from its acquisition of transmission pending the Commission's review of the UPS Agreements.

Finally, even if the SIS report shows that the redirect transmission request can be accommodated, nothing in the Southern OATT would prevent PEF from asking for an extension from Southern to determine whether to act on its request.

Q GIVEN THE STATUS OF THE TRANSMISSION REQUEST, CAN IT BE SAID THAT THE ECONOMICS PRESENTED BY PEF WILL NOT CHANGE?

196

A No. It is entirely possible that Southern will require certain system modifications to be made before it will agree to approve the transmission necessary to accomplish the proposed UPS transactions. Depending upon the amount of any capital contribution that might be required from PEF, the economics of the proposed UPS transactions could become even more negative. Without knowing what the transmission will cost, it is not possible to know whether or not it is feasible or even marginally economic to enter into the proposed UPS agreements.

Q SHOULD THE COMMISSION REQUIRE THE SIS RESULTS BEFORE CONSIDERING THE UPS AGREEMENTS?

A Yes. The results of the SIS study should be known in approximately 60 days from the submission date. At that point the Commission will know whether transmission will be available and whether PEF's customers would be saddled with substantial system improvement costs.

<u>OTHER BENEFITS CLAIMED BY PEF</u>

Q BEGINNING AT PAGE 10 OF HIS DIRECT TESTIMONY, AND CONTINUING TO PAGE 12, PEF WITNESS WATERS DISCUSSES WHAT HE REFERS TO AS SEVERAL "OTHER" BENEFITS OF THE PROPOSED UPS AGREEMENTS. DO YOU HAVE ANY COMMENTS ON THESE CLAIMED NON-ECONOMIC RELATED BENEFITS?

A Yes, I do. The first factor he mentions is that the proposed UPS agreements would contribute to fuel diversity. By this he means that PEF would have the rights to 74 megawatts of Southern coal-based generation, which is more than it says it would have when the existing UPS agreement expires. Actually, for this to be true, the assumption must be made that there are no other sources of coal-fired power during this period of time, and/or that absent the UPS agreements PEF would not be able to construct or otherwise acquire a coal-based facility prior to 2015. PEF has not established this to be the case, and in fact has indicated that development of a new coal-fired generating facility might be possible by 2013. (See response to Interrogatory No. 15.)

The second factor mentioned by Mr. Waters is contribution to the availability of economy energy. He bases this on the asserted superior access to transmission facilities provided the UPS agreements are executed. As discussed elsewhere, PEF's opportunities are not so limited. Interestingly, he specifically references the ability to acquire energy during hours when the combined-cycle units available under the UPS agreement are not scheduled. This is effectively an admission that during these hours the output of the combined-cycle unit will be out of market and not economic.

The third factor he mentions is increased reliability. The argument he makes here is that PEF will maintain the transmission path to Southern for supplies when Scherer or Franklin are unavailable, and he also points out that the Franklin unit will be served from a gas supply system separate from those that serve other PEF units. There is more to this issue than he discusses. With respect first to the transmission path to the Southern system, PEF will continue to have import rights at the Florida-Georgia border, irrespective of any UPS agreements. Thus, imports to maintain reliability would not be diminished in the absence of the UPS agreements, and in fact to the extent that capacity were built in Florida, rather than acquired from Georgia, there would be a greater amount of import capability for reliability purposes.

The next factor he mentions is cost certainty, stating that purchases from existing units provide greater assurance of cost and performance than might be obtained from units that would need to be constructed. This may or may not be the case, depending upon what would be acquired or constructed, and the nature of the contractual arrangements. Furthermore, if there are credible non-gas fired resources, the UPS Agreements actually increase price risk.

He then mentions the right of first refusal if additional coal capacity on the Southern system should be offered to the wholesale market. There is no analysis of the probability of this being the case, and thus it is not possible to evaluate the benefits associated with this right.

The last factor mentioned is planning flexibility. Mr. Waters indicates that the agreements provide for extension of the combined cycle contract for two years at PEF's option. While there may be some benefit here, there is no analysis or demonstration that similar benefits would not be available absent the UPS agreements.

Q WHAT SHOULD BE DONE?

A The Commission should decline to approve the UPS agreements until FERC has completed its investigation of the credible allegations concerning the Southern Companies. At a minimum, the Commission should protect Progress' customers by declining to approve the agreements for cost recovery until FERC completes its investigation.

OTHER ISSUES CONCERNING UPS AGREEMENTS

Q ARE THERE ADDITIONAL REASONS TO BE CONCERNED ABOUT THE REASONABLENESS OF THE TWO UPS AGREEMENTS?

A Yes. Given that PEF is asking for approval of these contracts five years before the end of the current contract term, the Commission should be concerned by the considerable uncertainty that exists concerning potential federal regulatory impacts on the Southern Companies' wholesale activities. Specifically, FERC recently initiated multiple investigations of the Southern Companies that could significantly affect whether additional competitive alternatives to the UPS agreements may be available during the 2010-2015 term of the contracts.

Q PLEASE DESCRIBE THE SOUTHERN COMPANY ENTITIES INVOLVED IN THE PROPOSED UPS AGREEMENTS.

A As noted earlier, several Southern Company entities are involved in the UPS agreements. Southern Power Company ("Southern Power") owns the Plant Franklin gas-fired combined cycle facility, and is the Seller with respect to the Unit Power Sales Agreement for 350 MW from that facility. Georgia Power Company and Gulf Power Company own the Plant Scherer Unit No. 3, and are the Sellers with respect to the Unit Power Sales Agreement for 74 MW from that facility. In each case Southern Company Services ("SCS") acts as agent for the Seller. SCS is also the Southern Company entity responsible for administering transmission services on the Southern Company system, and as such will act on the PEF transmission requests that are a condition precedent to the UPS agreements. Each of these Southern entities is subject to the ongoing FERC investigations.

Q PLEASE BRIEFLY DESCRIBE THE FERC INVESTIGATIONS OF THE SOUTHERN COMPANIES.

A There are three ongoing FERC investigations concerning the exercise of market power by the Southern Companies. First, on December 17, 2004 FERC instituted an investigation under section 206 of the Federal Power Act concerning the justness and reasonableness of the Southern Companies'[1] market-based rates, based on the Southern Companies failure of FERC's generation market power screen.[2] That investigation involves Southern's generation market power within its control area. Second, on May 5, 2005 FERC initiated a separate Section 206 investigation to determine whether the Southern Companies failed the remaining three prongs of FERC's market based rate analysis: transmission market power, barriers to entry, and affiliate abuse or reciprocal dealing ("Rehearing Order").[3] Third, in a concurrent order, FERC also initiated an investigation concerning allegations concerning the Southern Companies

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[1] The Southern Companies include Southern Company Services, Alabama Power Company, Georgia Power Company, Gulf Power Company, Mississippi Power Company, Savannah Electric and Power Company and Southern Power Company.

[2] *Southern Companies Energy Marketing Inc. and Southern Companies Services, Inc.*, 109 FERC 61,275 (2004).

[3] Order on Rehearing, *Southern Companies Energy Marketing Inc. and Southern Companies Services, Inc.*, 111 FERC 61,144 (2005).

Intercompany Interchange Contract ("IIC") ("IIC Order").[4] The IIC is an agreement among the six Southern operating companies, including Southern Power, that establishes a closed power pool (the "Southern Pool").

Q PLEASE EXPLAIN WHAT CONCERNS FERC HAS EXPRESSED ABOUT THE SOUTHERN COMPANIES' ACTIONS.

A FERC has determined that there are credible concerns that the Southern Companies, including the Southern entities involved in the UPS agreements, have exercised market power to the detriment of wholesale competition and wholesale customers in the Southeast. For example, in the IIC Order at Paragraph 35 FERC observed that:

> "The participants have raised credible allegations . . . that the relationship between Southern Power and other Southern Companies, including Southern Services and the inclusion of Southern Power in the IIC and Southern pool, as well as the conduct of several of the Southern Companies may have resulted in unduly preferential or unduly discriminatory conduct in violation of the FPA and/or in violations of Part 37 of the Commission's regulations, to the detriment of wholesale competition and customers in the southeast. It is appropriate to allow the participants to continue to investigate these allegations in a hearing. We are also concerned that the IIC (including how ratepayers are impacted by the sharing of costs and revenues under the IIC and whether native load wholesale customers are receiving a proper share of revenue credits from off-system sales) may not be just and reasonable, may allow Southern Power to enjoy an undue preference by virtue of its pool membership that adversely impacts wholesale competition and wholesale customers, and may lack sufficient clarity and transparency to ensure its justness and reasonableness. These issues should be addressed in the hearing."

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[4] Order Establishing Hearing Procedures, *Southern Company Services, et al., 111* FERC 61,146 (2005).

Q **WHAT IMPACT MIGHT FERC'S INVESTIGATIONS HAVE ON THE UPS AGREEMENTS?**

A While I am not testifying as a legal expert, a plain reading of the orders reveals that the FERC investigations may have several significant impacts on the UPS agreements. First, FERC could decide that the Southern Companies do not meet FERC's test for market-based rates and presumably could revoke Southern's market-based rate authority.

Second, should FERC decide to open the closed Southern Pool to other competitors, Progress could have access to additional competitive options during the time frame of the UPS agreements. By approving the UPS agreements now, notwithstanding that the term of the agreements is 2010-2015, the Commission could foreclose the possibility of Progress' customers benefiting from such competitive options.

Third, the Commission should be hesitant to approve, far in advance, transactions that may be tainted by Southern Companies' market power. As FERC has recognized, there are credible allegations that the Southern Companies have used their market power to harm wholesale competition, and wholesale customers, in the Southeastern United States. Such a result would harm both Progress and its customers. For example, if Southern has used its market power to deprive PEF of competitive alternatives, PEF's customers would bear the burden of higher prices.

RECOMMENDATION

Q WHAT IS YOUR RECOMMENDATION?

A For the reasons indicated above, I recommend that the Commission deny PEF the authority to enter into the proposed UPS contracts until and unless it provides a more thorough analysis of options available to it, including accelerated pursuit of solid fuel resources.

Q DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A Yes, it does.

Qualifications of Maurice Brubaker

Q **PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

A Maurice Brubaker. My business address is 1215 Fern Ridge Parkway, Suite 208, St. Louis, Missouri 63141.

Q **PLEASE STATE YOUR OCCUPATION.**

A I am a consultant in the field of public utility regulation and President of the firm of Brubaker & Associates, Inc., energy, economic and regulatory consultants.

Q **PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.**

A I was graduated from the University of Missouri in 1965, with a Bachelor's Degree in Electrical Engineering. Subsequent to graduation I was employed by the Utilities Section of the Engineering and Technology Division of Esso Research and Engineering Corporation of Morristown, New Jersey, a subsidiary of Standard Oil of New Jersey.

In the Fall of 1965, I enrolled in the Graduate School of Business at Washington University in St. Louis, Missouri. I was graduated in June of 1967 with the Degree of Master of Business Administration. My major field was finance.

From March of 1966 until March of 1970, I was employed by Emerson Electric Company in St. Louis. During this time I pursued the Degree of Master of Science in Engineering at Washington University, which I received in June, 1970.

In March of 1970, I joined the firm of Drazen Associates, Inc., of St. Louis, Missouri. Since that time I have been engaged in the preparation of numerous studies relating to electric, gas, and water utilities. These studies have included analyses of the cost to serve various types of customers, the design of rates for utility services, cost forecasts, cogeneration rates and determinations of rate base and operating income. I have also addressed utility resource planning principles and plans, reviewed capacity additions to determine whether or not they were used and useful, addressed demand-side management issues independently and as part of least cost planning, and have reviewed utility determinations of the need for capacity additions and/or purchased power to determine the consistency of such plans with least cost planning principles. I have also testified about the prudency of the actions undertaken by utilities to meet the needs of their customers in the wholesale power markets and have recommended disallowances of costs where such actions were deemed imprudent.

I have testified before the Federal Energy Regulatory Commission (FERC), various courts and legislatures, and the state regulatory commissions of Alabama, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, Florida, Georgia, Guam, Hawaii, Illinois, Indiana, Iowa, Kentucky, Louisiana, Michigan, Missouri, Nevada, New Jersey, New Mexico, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, South Dakota, Texas, Utah, Virginia, West Virginia, Wisconsin and Wyoming.

The firm of Drazen-Brubaker & Associates, Inc. was incorporated in 1972 and assumed the utility rate and economic consulting activities of Drazen Associates, Inc., founded in 1937. In April, 1995 the firm of Brubaker & Associates, Inc. was formed. It includes most of the former DBA principals and staff. Our staff includes consultants with backgrounds in accounting, engineering, economics, mathematics, computer science and business.

During the past ten years, Brubaker & Associates, Inc. and its predecessor firm has participated in over 700 major utility rate and other cases and statewide generic investigations before utility regulatory commissions in 40 states, involving electric, gas, water, and steam rates and other issues. Cases in which the firm has been involved have included more than 80 of the 100 largest electric utilities and over 30 gas distribution companies and pipelines.

An increasing portion of the firm's activities is concentrated in the areas of competitive procurement. While the firm has always assisted its clients in negotiating contracts for utility services in the regulated environment, increasingly there are opportunities for certain customers to acquire power on a competitive basis from a supplier other than its traditional electric utility. The firm assists clients in identifying and evaluating purchased power options, conducts RFPs and negotiates with suppliers for the acquisition and delivery of supplies. We have prepared option studies and/or conducted RFPs for competitive acquisition of power supply for industrial and other end-use customers throughout the Unites States and in Canada, involving total needs in excess of 3,000 megawatts. The firm is also an associate member of the Electric Reliability Council of Texas and a licensed electricity aggregator in the State of Texas.

In addition to our main office in St. Louis, the firm has branch offices in Phoenix, Arizona; Chicago, Illinois; Corpus Christi, Texas; and Plano, Texas.

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CHAIRMAN BAEZ: Mr. Brubaker, do you have comments, sir?

THE WITNESS: Yes, sir, I would like to make some brief comments?

CHAIRMAN BAEZ: Go ahead and summarize your testimony.

THE WITNESS: Thank you.

Mr. Chairman, members of the Commission, I have filed testimony in this proceeding in which I recommend that the Commission not approve PEF's entry into the proposed UPS agreements, but rather find that PEF should be required to more fully analyze alternatives available to it prior to making a decision on the contract or choosing some other course of action.

Now, let me just touch on some of the more important reasons why I come to that recommendation. First of all, a critical aspect of the analysis that is done is the selection of the base plan. And the base plan is the portfolio of resources that the utility would undertake to execute if it didn't do the UPS agreements. It takes that base plan and then it compares the UPS agreement to that and moves resources in the portfolio to adjust for the fact that it would have capacity from these UPS agreements over some interval of time, maintaining roughly the same reserve margin with those two different portfolios. And I think, in general, conceptually that is a proper approach.

What I have trouble with is it is not clear to me that what has been characterized or developed as the base plan is, in fact, the best choice, and what PEF should be doing in the absence of the UPS agreements or some other set of resources. And some of the reasons for that, I cannot tell from the information provided, for example, what constraints may have been placed on the availability of solid fuel technologies in a timing sense, or the size of units that could be considered, or the effect of higher gas prices on the resources that belong in the base plan in the first instance.

This is particularly problematic in light of the much higher gas prices that PEF has forecasted subsequent to March of '04 when it formulated the base plan, including higher gas prices forecasted in the fall of 2004 prior to the time that it decided to enter into the UPS agreements with Southern.

Now, if the base plan that is selected is not really the best plan that the utility should be trying to execute, then all the analysis that has been done shows is how the UPS agreement or a plan with the UPS agreement and some adjustments compares to a base plan which may not be the right base plan.

The second major issue I have is that in deciding to go with the UPS agreements, the utility did not conduct an RFP to determine what other kinds of assets might have been available to it in either the 2010/2015 time frame or some part f that time frame. That means that they may have overlooked ther opportunities that they may not even know about and would ot know about because they didn't address the market in an rganized and comprehensive fashion to test what actually is vailable.

Third, based on my review, there was no consideration iven to accelerating the coal units, or considering ccelerating the coal units to an earlier date than 2015. I elieve there was an indication this morning that from an conomic standpoint on a life-cycle basis, coal in 2013, I elieve, had a lower cost to the consumers than what the base lan was. I find that problematic that more attention wasn't iven to those options, especially in light of the Burns and IcDonnell study in early 2004 and, again, the escalating gas rices.

The transmission issue, I think, is important, too. ecause at this point we don't know what the availability of ransmission will be to implement these agreements, nor do we now that if there is transmission available what the upgrade osts would be that would have to be incurred in order to actually secure the transmission contract path from Southern to deliver power from the Franklin gas-fired unit to the Florida/Georgia interface. It simply is not known and could increase the potential costs that PEF would be asking the Florida consumers to bear in a scenario where already, by its own calculations, the economics of the transaction are somewhat negative over the time period considered.

I was also troubled that in my review we did find a significant overstatement of claimed savings on the front end of this deal in the first five years. That leads me to wonder if there might be other aspects of the studies that could benefit from further scrutiny and vetting in a more suitable time frame than what was available to me, at least, in this proceeding.

In any event, the front-end savings in the first five years at 37, or 44, or whatever the number is, are not near as compelling to me as the initial number. And if you look two or three years out beyond 2015 to, I think, 2017 or 2018, those cumulative net present value benefits actually disappear, and it becomes effectively a wash at zero. So there might be some short-term benefits there available, but they don't last very long. And given the gas prices, what they have done, what the company's new forecast is compared to what they assumed in the base plan, it is not even clear to me that those numbers would be there.

I also need to indicate that the exhibit I presented, which recalculated the deferral savings, only addressed the capital costs associated with the deferred units. We did not have the time or ability to look into the production cost models and determine if we had any issues with respect to those ıatters. And the production cost models, as I recall, the lollar amounts at issue there are many, many, many times in ıagnitude what the deferral cost numbers are. So I find that lifficult for me to buy into the conclusions of the study.

For those reasons, my recommendation is to reject ;iving permission to PEF to enter into these agreements and, .nstead, suggest that they could benefit from more analysis of ılternatives.

Thank you.

CHAIRMAN BAEZ: Thank you, sir.

Mr. Perko, you can cross.

MR. PERKO: Thank you, Mr. Chairman.

CROSS EXAMINATION

3Y MR. PERKO:

Q Good afternoon, Mr. Brubaker.

A Good afternoon, Mr. Perko.

Q Can you tell me when you were first retained to work on this case?

A It was a time frame approximately when the Commission issued its procedural order, which if memory serves was around the 20th of April.

Q Thank you. Now, have you ever worked for an electric utility?

A Not as an employee of an electric utility, I have not.

Q You mentioned the company's base plan. Have you ever developed a resource plan for an electric utility?

A Not on an engagement where I was working for an electric utility. I have looked at a lot of utility base plans and suggested alternative plans in the course of participating in proceedings like this in long-term resource planning dockets.

Q Ny question is have you ever developed a utility resource plan?

A Not for a utility. Not from scratch, if that is where you are going. My role typically is to take a look at what utilities are proposing to do and see if I have any issues with it.

Q Would you agree that development of an electric utility resource plan involves the exercise of professional judgment?

A I would.

Q Now, you talked a little bit about the production cost models that Progress Energy used, and I assume you were talking about the PROSYM and/or Strategist model?

A Correct.

Q Do you have any training with either the PROSYM or Strategist models?

A Not to run them. I am very familiar with production cost models and what they turn out and what the basic workings, internal workings is of them.

Q But you have never run it?

A I have never run it. Never had a need to.

Q Now, you mentioned that you, I believe, in your testimony performed an alternative analysis of the costs associated with the agreements, is that correct?

A Yes. Just limited to the fixed costs associated with the units that were potentially deferred.

Q And as I understand it, the results of those costs at year 2015, at the end of the term of the agreement, showed $37 million in savings, is that correct?

A Correct. Subject to the previous caveats that I expressed.

Q And would you agree that the difference between 37 and $44 million in savings is relatively immaterial?

A I would.

Q Your alternative analysis also showed that over a long-term period of 45 years the agreements would result in the net cost of approximately 11 million, is that correct?

A Correct. Again, subject to the caveats that that is derived by just assuming that the company's production cost analysis was correct and without having had an opportunity to look at it and see if I agreed with it.

Q Now, you mentioned you had some questions about how Progress Energy's analysis was performed, is that correct?

A Yes.

Q To your knowledge, did White Springs ever attempt to depose Mr. Waters or anyone at Progress Energy?

A I don't believe -- well, I don't know. I don't think so. I'm not aware if they did.

Q Wouldn't you think you would aware if they did?

A Probably.

Q Would you agree that price is not the only factor that should be considered in connection with approval or disapproval of power purchase agreements?

A I would. There are other factors that are important, as well.

Q Would you agree that at least to the extent that it includes 74 megawatts of coal capacity from Plant Scherer, that the UPS agreements increase fuel diversity on Progress Energy's system as compared to the self-build?

A If you compare the UPS agreements to what the company represents as its base case, that would be true. Since I'm not comfortable with the base case as having been fully -- been the product of fully vetting all the options, I don't know whether that would produce more coal-fired energy than some other opportunity or some other option would.

MR. BUSHEE: Mr. Chairman, during this brief break, might I ask my own witness to speak closer to the microphone so we could hear him better.

THE WITNESS: I'm sorry. People don't usually have trouble hearing me. Sometimes understanding me, but not hearing me. So I will try to be conscious of that.

BY MR. PERKO:

Q Do you recall being deposed on May 18th of this year?

A I think that is the date, yes.

Q Do you recall me asking you the question would you agree that when compared to the self-build alternative that the new UPS agreements would increase fuel diversity on PEF's system?

A I do.

Q And would you agree that at that time you stated, "Only to the extent of the relative modest amount of coal for the duration"?

A I gave that answer. I don't recall if I amplified it or not.

Q Was it correct when you stated it?

A Yes. It is probably not as complete as I just gave.

MR. PERKO: Nothing further, Mr. Chairman.

CHAIRMAN BAEZ: Ms. Vining.

MS. VINING: Staff doesn't have any questions.

CHAIRMAN BAEZ: Commissioners, any questions of Mr. Brubaker?

Mr. Bushee, you can redirect.

REDIRECT EXAMINATION

BY MR. BUSHEE:

Q Mr. Brubaker, just one question for you on redirect. A couple of times in response to Mr. Perko's questions you mentioned subject to the caveats that you have. **Would you** just make sure that the record reflects what your caveats are?

A Yes. They were the fact that I had not had an opportunity to go through the production cost model or its results and determine whether or not I had any issues with respect to that part of the analysis. **Plus, any other aspect** other than just the pure deferral analysis on the capital costs was not able to look at.

MR. BUSHEE: I have no further questions.

MR. PERKO: I know this is unusual. May I ask one follow-up question?

CHAIRMAN BAEZ: Subject to redirect, go ahead.

RECROSS EXAMINATION

BY MR. PERKO:

Q Mr. Brubaker, did you ever attempt to get access to the Strategist or PROSYM models?

A No, sir, because by the time that I got anything that even looked like the output results of the PROSYM, it was four or five days after I had filed my direct testimony, and I just knew there was no point from a time standpoint of even trying to ask for that.

MR. PERKO: Nothing further.

CHAIRMAN BAEZ: Mr. Bushee, you have an opportunity o redirect on the question, sir.

MR. BUSHEE: I have no further questions.

CHAIRMAN BAEZ: Very well. We will take exhibits. ınd I am showing 9 through 14 inclusive.

MR. BUSHEE: That is what my records reflect, Your Ionor.

CHAIRMAN BAEZ: Very well. Without objection, we vill show Exhibits 9, 10, 11, 12, 13, and 14 admitted into the record.

(Exhibits 9 through 14 admitted into the record.)

CHAIRMAN BAEZ: Mr. Brubaker, thank you. You are excused.

And, Mr. Waters, you are back in the box.

SAMUEL S. WATERS

was called as a rebuttal witness on behalf of Progress Energy Florida, and having been previously duly sworn, testified as follows:

DIRECT EXAMINATION

BY MR. PERKO:

Q Good afternoon, Mr. Waters.

A Good afternoon.

Q Do you have your rebuttal testimony with you?

A Yes, I do.

Q Are there any changes or revisions that you need to ake to that testimony?

A No.

MR. PERKO: At this time, Mr. Chairman, I would like o move Mr. Waters' rebuttal testimony into the record.

CHAIRMAN BAEZ: Without objection, show the rebuttal .estimony of Samuel Waters moved into the record as though ·ead. And also for the record show his attached rebuttal :xhibits marked as 15 and 16.

PROGRESS ENERGY FLORIDA

DOCKET NO. 041393-EI

REBUTTAL TESTIMONY OF

SAMUEL S. WATERS

May 20, 2005

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

A. My name is Samuel S. Waters and I am employed by Progress Energy Carolinas (PEC). My business address is 410 S. Wilmington Street, Raleigh, North Carolina, 27601.

Q. Have you previously filed testimony in this docket?

A. Yes, I have.

Q. What is the purpose of your rebuttal testimony?

A. I wish to address several points raised by Mr. Maurice Brubaker on behalf of White Springs Agricultural Chemicals, Inc. d/b/a PCS Phosphate – White Springs (White Springs) regarding the proposed Unit Power Sales (UPS) Agreements between Progress Energy Florida (PEF) and Southern Company Services, Inc. Mr. Brubaker raises 13 points regarding the agreements and recommends that the Commission deny PEF the authority to enter into the proposed contracts. I will address each of the points in turn and discuss why Mr. Brubaker has not offered any credible reason why the contracts should not be approved.

Q. Please summarize what you believe to be Mr. Brubaker's main objections to approval of the contracts.

A. Mr. Brubaker takes issue with the cost effectiveness analysis, particularly the short-term calculations (Points 1, 2 and 4). He asserts that PEF should have taken various actions to replace the UPS agreements when they expire, or proceed now to add coal capacity, or just wait and do nothing (Points 3, 5, 7, 8 and 11). He states that fuel diversity will be reduced, but that "non-price" factors are not sufficiently important to be given any significant weight in the Commission's decision (points 6 and 10). He also offers an opinion that there are many uncertainties regarding transmission service required to implement the agreements (Point 9). His remaining points are not objections to the agreements themselves, but recommendations for Commission action, including a suggestion that the Commission consider a downward adjustment to PEF's return on equity in the pending rate case (Point 12), and, should the contracts be approved, that the Commission should make the UPS Agreements subject to a prudency challenge when cost recovery is sought (Point 13).

I would summarize Mr. Brubaker's issues into the following categories:

- Cost effectiveness of the UPS Agreements
- Non-price or strategic considerations associated with the agreements
- Transmission requirements
- Alternatives to pursuing the agreements

and,

- Proposed Commission actions

I will address each of his issues within these categories, and I have categorized in this order because I believe that this is the relative importance of the arguments he has made against the contracts, from my perspective.

Q. Please begin by addressing Mr. Brubaker's discussion of the cost-effectiveness analysis.

A. First, let me begin by acknowledging an error in the initial calculations submitted in my direct testimony. The error does not affect the overall analysis or conclusion it supported. The analysis illustrates the year-by-year economics of the UPS Agreements. It was performed after the initial cost-effectiveness analysis, which was based on a methodology that relied upon the use of economic carrying charges, also known to this Commission as a value-of-deferral analysis. This type of analysis calculates the costs and benefits associated with deferring or advancing generating units over their full expected life, but does not allow for the quantification of actual benefits or savings in any specific year of the analysis. Put in simple terms, the economic carrying charge or value of deferral analysis tells me that delaying a generating unit may save $20 million, net present value (NPV), over, say, 25 years, but it does not tell me how much will be saved in year 1, year 2, year 3, etc. This method was the basis for the quantification of the NPV $5 million to $11 million cost presented in my direct testimony, and this analysis was and remains correct.

In an attempt to identify the net cost or savings to customers during the five-year term of the proposed UPS Agreements, a simple revenue requirements analysis was performed. This analysis included an error which was revised in my supplemental testimony. The revised analysis shows an NPV savings of approximately $44 million during the contract term, 2010-2015. Mr. Brubaker has repeated the analysis and shown the results in his Exhibits MEB-1 ( ) and MEB-2 ( ).

Q. What do you make of Mr. Brubaker's analysis?

A. Mr. Brubaker suggests that "The results are significantly different than what PEF initially calculated" (Brubaker, page 5, line 12), apparently referring back to the analysis I originally submitted. However, examining his Exhibit MEB-2 ( ) against my revised Exhibit No. ___ (SSW-4), one would be hard pressed to see any significant difference. In other words, Mr. Brubaker has apparently obtained the same result, that there are savings to customers during the five year term of the contracts.

Q. But doesn't Mr. Brubaker contend that little or no weight be given to these front-end savings?

A. Yes. Mr. Brubaker would rely on later years' results, pointing to the period beginning three years after the contract and the next 20 years (Brubaker, page 6, lines 3-4).

Q. Do you agree that these front-end savings should not be considered?

A. No. Use of the "bottom line" number from the analysis alone would be inappropriate. The benefits in the near-term are more certain because the resource plan is more certain in those earlier years. If considered in isolation, the costs in the longer term, which are based on assumed resource plan additions to which PEF has not committed, may have an unduly large impact on the decision on whether or not to pursue the alternative under consideration. While we must make some assumptions about the resource plan to perform the analysis, planning judgment is appropriate in reviewing the results. This is not to say that the decision should be based solely on this near-term view, but it is certainly worthy of consideration, not dismissal. This consideration is not unique to this analysis. Timing of costs and benefits is a consideration in resource planning decisions. It is relevant to consider how long it takes to produce savings in the comparison of resource alternatives, just as it is relevant to look at the year-by-year savings provided by the UPS agreements.

Q. What other criticisms does Mr. Brubaker have regarding the cost effectiveness analysis?

A. Mr. Brubaker asserts that the base plan to which the UPS Agreements were compared has not been shown to be the least cost plan that PEF would execute in the absence of the Agreements. (Brubaker, page 6, lines 20-22). His belief is apparently based, at least in part, on the fact that the base plan includes four coal units that were not included in the PEF Ten Year Site Plan as of December 31, 2004. (Brubaker, page 7, lines 1-3) Of course, the obvious reason that the coal units were not included in the PEF Ten year Site Plan is that the document is just what it says, a 10 year plan which covers the period 2005-2014, and the coal units are not included in the base plan used in this analysis until 2015. However, PEF does determine optimal plans for a 20 year planning horizon, so the base plan used here was optimized for the period 2004 through 2023. It was determined in the same manner that PEF uses to determine its base plan for inclusion in the Ten Year Site Plan. The base resource plan used to determine the cost effectiveness and the alternative resource plan including the purchases from Southern are shown in my Exhibit ___(SSW-5).

I do want to make an important distinction between my use of the term optimal plan and Mr. Brubaker's use of the term "least cost" plan. The objective of the planning process is not simply to identify the plan that represents "least cost" over a given period. As has been presented many times to this Commission, there are many other factors which may influence the selection of resources to meet customer needs. I will not burden this proceeding with a discussion of the strategic factors that should be considered, but, needless to say, the Commission has considered factors beyond cost in previous decisions, including the recent approval of FPL's purchases from the Southern Companies. Even in the consideration of costs, the definition of "least cost" may depend on the time frame selected for the comparison, as I previously discussed. Therefore, I believe the standard for the base plan should be the most cost effective plan that PEF would pursue absent the purchases under the UPS Agreements. That was the plan that was used in this instance.

Q. Mr. Brubaker states that he has not been provided with the model or any of the inputs or outputs used in the economic analysis. Is this correct?

A. No. Mr. Brubaker has been provided the forecasts used in the analysis and the raw input data, as well as summary output files used in the analysis. He has not been provided the Strategist model, which PEF obtains under license, which prohibits distribution of the model and certain input files. PEF did provide saved output files that could be used in the model, should Mr. Brubaker decide to obtain access. The only capability that Mr. Brubaker may be missing is the ability to rerun the model himself. All relevant information was provided.

Q. How does Mr. Brubaker suggest that non-price factors be included in the analysis of the UPS Agreements?

A. In somewhat contradictory testimony, Mr. Brubaker cites various "non-price" factors in support of his findings and recommendations, while at the same time arguing that "'non-price' factors that PEF cites in support of the UPS agreements are not sufficiently important or quantified to be given any significant weight by the Commission." (Brubaker, page 3, lines 27-29). One of the non-price factors he refers to is, of course, that the UPS Agreements contribute to fuel diversity. Apparently, to Mr. Brubaker, this factor is only important in pursuing the construction of new coal units, an alternative I will address later in my testimony. Other non-price factors, such as maintaining "closer to an historic fuel diversity" are given as reasons to reject the UPS Agreements rather than approve them. I do not understand the distinction. Mr. Brubaker apparently weighs the "non-price" factors selectively, either dismissing or attaching significance to them depending upon which argument he is trying to support. One of the clear benefits of these agreements is the contribution to fuel diversity by making coal-fired energy available.

Q. What about Mr. Brubaker's criticisms of the other non-price factors you have presented?

A. His second criticism of non-price factors appears to be that "PEF's opportunities are not so limited" (Brubaker, page 30, line 12), referring to PEF's ability to access additional economy energy without the UPS Agreements. I take it from his discussion that he means that we could simply contract for the transmission, buy economy energy when available, and resell the transmission capacity when it is not needed. He offers no analysis that this would produce a net savings to customers, so I cannot address it quantitatively, but on the face of it, it does not appear to make sense. Economy purchases might somewhat offset the transmission costs, but they are not likely to completely pay for transmission access. Referring to my own original Exhibit No. ___(SSW-3), the NPV of the transmission costs was approximately $28 million, while the NPV of the economy savings was calculated to be $6 to $12 million. Thus, there would be a shortfall of $22 to $16 million and Mr. Brubaker provides no evidence that additional economy savings could make up the difference.

Mr. Brubaker's next point is that "...... in fact to the extent that capacity were built in Florida, rather than acquired from Georgia, there would be a greater amount of import capability for reliability purposes." (Brubaker, page 31, lines

1-3) This would be true only if the interface between Georgia and Florida sat idle. In other words, he apparently assumes that if PEF does not pursue the UPS Agreements, no other entity in Florida would be interested in buying power across the interface. This seems very unlikely in light of the fact that other entities have expressed interest in buying power from across the border.

Mr. Brubaker addresses the issues of cost certainty, the right of first refusal for additional coal capacity and planning flexibility by simply noting that either they may or may not be the case, or they haven't been quantified. This is not a sufficient reason to be totally dismissive of the potential for benefit they provide. They are non-price factors, and by definition, not quantifiable, at least in the same manner as the overall deal economics. However, as even Mr. Brubaker concedes regarding planning flexibility, "..... there may be some benefit here......" (Brubaker page 31, line 16). Non-quantifiable benefits are benefits nonetheless.

Q. What does Mr. Brubaker have to say with regard to the transmission requirements associated with the UPS Agreements?

A. Mr. Brubaker devotes a great deal of his testimony to transmission issues, nearly 14 of the 36 pages. The main points seem to boil down to 3 major issues:

- PEF will maintain its rollover transmission rights until 2010.
- The Commission should wait until the System Impact Study (SIS) is completed to make a decision on the UPS Agreements

- The costs of transmission may be higher than analyzed, resulting in increased costs to customers.

One factor ignored in these arguments is that Southern, as a marketer, has an interest in selling the designated capacity and consummating the deals. While it may be true that PEF could wait until 2010 to exercise its rollover rights, just what would we be expected to buy to exercise those rights at that time? There is no reason to believe that Southern will hold these assets for PEF to buy at a later date. Even buying from another source would involve exercising the right to rollover the transmission service far earlier than 2010. Transmission service would be required as a necessary precedent before the purchases could be completed, as it is in this case. The UPS Agreements specifically call for PEF to request transmission service within 60 days of the effective date of the agreements. PEF has until February, 2006 to make arrangements for service. This condition precedent protects PEF against the possibility of not being able to deliver the resources it is paying for, and it protects the Southern Companies from having to hold open an offer that may not be ultimately completed. It would not be desirable for either party to delay a decision until the brink of expiration of the current contract.

Regarding waiting until the System Impact Study is completed, Mr. Brubaker would like to wait and see if additional system upgrade costs will be incurred. This should not be a concern since the UPS Agreements specifically provide for mitigation should transmission costs be above the Southern Open Access Transmission Tariff (OATT) rates. PEF customers would not be ".... saddled with substantial system improvement costs" as Mr. Brubaker suggests. (Brubaker, page 29, lines 13-14) The mitigation measures in the contract include the potential for offsetting increased charges, provision of alternative transmission service, or even cancellation of the contract. Waiting until the SIS is completed is unnecessary if the concern is that additional costs may be incurred. The more appropriate concern is that the SIS will be completed with no system upgrades required. At that point, Southern will affirm the transmissions service, and PEF will own the transmission service. Since the transmission service request is currently in process, and a response could occur within the next 60 days, delaying the decision on the UPS Agreements does introduce the risk that PEF could have to decide on transmission without knowing whether the agreements themselves have been approved. The delay is simply not necessary or advisable.

I would also like to note that the SIS study does not address rollover rights, as Mr. Brubaker suggests in his testimony. Rollover of the existing transmission rights has already been confirmed by Southern. Mr. Brubaker's suggestion on page 20, line 14 of his testimony that these rights need to be studied, or the inference that any additional costs might be incurred as the result of such a study, is in direct opposition of his own description of the purpose of rollover rights on page 21.

Q. Do you believe that PEF has adequately identified the costs associated with the proposed UPS Agreements?

A. Yes. The costs associated with the agreements, such as the capacity, energy and O&M costs, as well as fuel transportation and transmission costs were included in the analysis. Mr. Brubaker's insinuation that transmission costs might be higher is not anything other than that, and even so, he ignores the mitigation measures provided by the agreements. The analysis I have presented gives the best available information, and is a true representation of the impact we would expect on PEF customers.

Q. Mr. Brubaker offers a number of alternatives that he states PEF should, or should have pursued. How do you view these alternatives?

A. As with the non-price factors, I find Mr. Brubaker's suggestions to be all over the map, and somewhat contradictory. In the same list of issues, PEF should have:

- Added coal capacity in advance of the expiration (page 3, lines 3-6)
- Conducted an RFP (page 3, lines 11-14)
- Planned to add coal capacity in 2013 (page 3, lines 18-21)
- Wait to enter into agreements for 2010-2015 (page 3, lines 22-24)
- More fully analyze alternatives (page 3, lines 30-32)

I am reminded of the expression "hurry up and wait" in reviewing these suggestions as a whole. I will first address the suggestion that there is no rush to enter into agreements.

Mr. Brubaker does not really address when it would be appropriate to enter into an agreement. In his transmission discussion, Mr. Brubaker asserts that "PEF has until April 2, 2010 to exercise its rollover rights". (Brubaker, page 23, lines 1-2) Certainly, he does not mean to imply that PEF should take no action to replace the 414 MW of capacity currently purchased from Southern until approximately 2 months before it disappears, but he does not suggest when the appropriate time would be. For reasons I will discuss later, delaying the approval of the UPS Agreements does, I believe, put the deals at risk, without regard for transmission schedules or rollover rights.

I will return to the issue of an RFP, but first I would like to discuss the assertion that PEF should have planned to add coal capacity when the existing UPS contracts were going to expire. Mr. Brubaker does not appear to take issue with the fact that a new coal unit takes approximately 8 years to site, license, design and construct. Thus, to meet a June 1, 2010 in-service date, PEF would have had to commit to the siting and licensing process back in 2002. If PEF had made that commitment, that certainly would have made the company more prescient than any other utility I am aware of. As I review a PEF fuel forecast dated February of 2002, I see a natural gas price forecast for the year 2010 of \$3.48/MMBtu (Henry Hub price). Planning studies at that time indicated that combined cycle units were the most economic, as indicated by PEF's Ten Year Site Plan, and that was in general agreement with the plans of other utilities. Today, the forecast for the year 2010 is about \$7.10/MMBtu, more than double the view of only 3 years ago. I wish I could say we had the foresight to predict that steep climb, but we did not (nor am I aware that any other utilities did), and now we must make a decision on capacity for 2010, only five years from now.

Construction of a new coal unit to meet that need is not an option, but the UPS Agreements do allow us some measure of coal at a reasonable price. As compared to the existing agreements, we retained approximately the same relative amount of coal (17%) under the new agreements, as did FPL under the UPS agreements that this Commission approved in January of this year. We would like more, but that was not an option.

Mr. Brubaker suggests we should proceed with a new coal unit now, rather than take the UPS Agreements, because it might be possible to place a new coal unit in service by 2013. However, he has not offered a solution for what we might do from the time the current UPS contracts expire, May 31, 2010, to the in service date of the new unit. Obviously, the three year interim would have to be filled by some agreement, although according to Mr. Brubaker, it is premature to address that period.

Q. What does Mr. Brubaker suggest with respect to requiring a bidding process to demonstrate the cost effectiveness of the proposed power purchases from the Southern Companies?

A. Mr. Brubaker suggests that "Good practice when considering entering into transactions of this magnitude . . . would be to conduct a thorough review of the market to ascertain if there are any other options available which should be considered." (Brubaker, page 15, lines 6-11)

Q. Do you agree with that suggestion?

A. No. I believe that conducting an RFP would jeopardize PEF's ability to take advantage of this opportunity.

Q. Please explain.

A. Clearly, in the creation of the Commission's "Bid Rule", there was recognition that requiring an RFP process in all instances where the utility is acquiring capacity would restrict a utility's ability to plan its supply system in a flexible and cost-effective manner. For example, when a utility has identified combustion turbines as its most cost-effective alternative, there is no requirement for an RFP, allowing the utility to more quickly respond to needs in the near term. Repowering of existing units is also excluded, encouraging the efficient use of older generating units. These exemptions result from the clear linkage between the "Bid Rule" and the Power Plant Siting Act, but they also implicitly suggest that there are circumstances where bidding may not be appropriate. In this case, where we are dealing with a continuation of a contractual relationship with an existing party, rather than construction of a new unit, I believe that there is a great risk of losing the opportunity if PEF is required to proceed with an RFP.

Q. Why do you feel that the opportunity to make this purchase from the Southern Companies would be at risk?

A. There are two reasons. To put the risk in context, it is important to recognize that an RFP process would take on the order of six months to complete, followed by negotiations to complete a contract for the power to be purchased.

Based on this timeframe, the first reason I believe risk is increased is that Southern is under no obligation to either hold this offer or bid into an RFP and wait for the outcome to see if they are the winning bidder. There is every reason to believe that Southern will continue to search for a buyer if we back away from an agreement today. The assets they are seeking to sell are "uncovered" by any existing power sale or retail rate base once our current contracts with them end. It stands to reason that no owner of a capital intensive asset will take a passive approach to selling that asset. We have to ask ourselves, what incentive would Southern have to wait for us? If the argument is that there are no other potential buyers, it brings me to my second reason for believing that this deal is at risk by delaying.

Not only do I believe that there are potential buyers for this capacity simply looking at the overall growth in peninsular Florida, but I also believe that at least some of the potential buyers are not subject to Commission review of the contract for cost recovery, and would not have to delay a purchase by conducting an RFP process. This would be true for potential buyers both inside and outside Florida. The only reasonable conclusion is that, at the very least, there is an increased possibility of this deal being offered elsewhere, in whole or in part, while PEF goes through an RFP process. Loss of this sale would result in loss of the advantages I outlined in my previous testimony, the most important of which, in my mind, is access to coal energy.

Q. Do you believe that an RFP would produce any offers that would be more economic than the UPS Agreements?

A. No. I would not expect to see any coal capacity offered because, as I have previously discussed, a new coal unit takes roughly 8 years to bring into service, and we're looking only 5 years out. For the combined cycle portion of the agreements, I have compared the Franklin unit to offers received in PEF's most recent RFP solicitation for Hines 4. The results of my comparison are shown in Exhibit No.___ (SSW-6). While I have only compared fixed costs, this is a good indicator of relative cost since all bids were gas and oil units. If anything, I would expect to see new bids that are even higher in cost because of recent increases in materials costs.

In addition to these results, it is worth noting the PEF has a wholesale marketing group that is constantly testing the market, looking for both purchase and sale opportunities. We are not making these decisions in a vacuum.

Q. How then can the Commission address the cost effectiveness of this proposed purchase from the Southern Companies?

A. The Commission has sufficient information available to make an informed decision. We have presented the economics of the proposed agreements, and the assumptions upon which they are based, the relative costs of the agreements compared to the offers received in response to PEF's most recent RFP, as well as the strategic benefits associated with the purchases. There is sufficient information to make a judgment on whether or not the purchases are prudent and cost-effective. Waiting for additional information would put the offer at risk and potentially lose the benefits of this deal for PEF customers.

Q. Mr. Brubaker suggests that the Commission should not approve the UPS Agreements, but require PEF to more fully analyze alternatives. Do you agree with his recommendation?

A. No. Mr. Brubaker has not identified a single alternative that may be available, nor has he made a case that additional analysis will produce a different result. There is no reason to delay a decision, and PEF customers stand to lose potential benefits as a result of any delays. Furthermore, even with the UPS agreements, PEF plans to issue a request for proposals for its next combined cycle unit, identified in the 2005 PEF Ten Year Site Plan, and at that time the wholesale power market will have an opportunity to submit alternatives.

Q. Mr. Brubaker also suggests that, because of the <u>alleged</u> "problems" with how PEF has approached the capacity expansion issue and evaluation of the proposed UPS Agreements, the Commission should consider a downward adjustment to PEF's return on equity in the pending rate case. Is this issue appropriate in this case?

A. No. It appears to be a thinly disguised effort to tie this contract approval into the pending rate case (in which White Springs has intervened) and introduce an issue which is not at all relevant to the Commission's consideration of the contract. PEF does not make a return on purchased power contracts. Therefore, the only incentive PEF has to move forward with these agreements is to obtain the benefits the agreements provide for PEF customers.

Q. What is your opinion on Mr. Brubaker's suggestion that "Should the Commission decide to allow PEF to enter into the UPS agreements in this case, it should make them subject to a prudency challenge whenever PEF would seek cost recovery" (Brubaker, page 4, lines 1-3)?

A. I am not certain of what Mr. Brubaker is suggesting. However, I would say that if his intent is to reopen the issue of whether or not PEF should have entered into the agreements, then I would be adamantly opposed to such a "prudency challenge". There should not be a "second bite of the apple" regarding review of the prudence of these agreements. If his intent is to monitor PEF's administration of the agreements, and the expenses associated with the contracts, I believe that this would be done in the normal course of fuel cost recovery proceedings, as it is today.

Q. Would you please summarize your rebuttal testimony?

A. The testimony of Mr. Brubaker on behalf of White Springs raises a number of objections to the UPS Agreements between PEF and Southern which are contradictory, vague, and in some cases, immaterial to the question of approving the agreements. His own cost effectiveness analysis produces results similar to those I presented in my supplemental testimony, and his suggestion that non-price factors should be ignored is not consistent with planning practices with which the Commission is familiar. He broadly discusses transmission issues without demonstrating that any would require the Commission to delay a decision. Finally, his call for an RFP would add unnecessary delay to the process and most certainly puts the UPS Agreements at risk.

The proposed purchases from the Southern Companies offer a unique opportunity to obtain coal energy, access a broader southeastern market, and defer the need for new capacity in Florida. I continue to believe that approval of this purchase is in the best interest of PEF customers.

Q. Does this conclude your testimony?

A. Yes.

CHAIRMAN BAEZ: Mr. Waters, do you have a summary?

THE WITNESS: Yes, I do.

CHAIRMAN BAEZ: Okay.

THE WITNESS: Good afternoon, Commissioners. My rebuttal testimony addresses several issues raised by Mr. Maurice Brubaker on behalf of White Springs.

I've summarized Mr. Brubaker's points into five main categories, including the cost-effectiveness of the unit power sales agreements, the nonprice or strategic considerations associated with the UPS agreements, the transmission requirements, the alternatives to pursuing the agreements, and proposed Commission actions. I have placed these considerations in this order because I believe that that is their relative importance in dealing with these new agreements.

Regarding the cost-effectiveness of the UPS agreements, my revised short-term analysis has demonstrated a $44 million savings, net present value, to customers over the five-year term of the agreements. Mr. Brubaker's analysis does not significantly differ from that result. Mr. Brubaker does not provide an alternative analysis to the long-term results I have presented, and I disagree with his suggestion that the short-term analysis should be dismissed and only the results of the long-term analysis considered to judge the cost-effectiveness of these agreements. The short term analysis shows benefits in the period where the resource plan is more certain and is, therefore, very relevant in assessing the cost-effectiveness of these agreements.

Regarding nonprice or strategic considerations associated with the UPS agreements, Mr. Brubaker contends that we could access the Southern System without the UPS agreements and take advantage of economy transactions. My own economic analysis shows that if we were to take this approach the economy savings do not offset the transmission costs.

He also asserts that if capacity were built in Florida rather than acquired in Georgia there would be greater import capability for reliability purposes. This could only be true if the interface between Georgia and Florida sits idle, which I consider to be very unlikely.

Finally, Mr. Brubaker addresses a number of other nonprice issues saying that they may or may not happen and they haven't been quantified. Nonprice factors are, by definition, not quantifiable, at least not in the same manner as direct costs. But nonquantifiable benefits are still benefits.

Regarding transmission requirements, Mr. Brubaker makes three main points, all of which suggest delay or inaction. First of all, delay or inaction on the part of Progress Energy until the system impact study is complete or until rollover rights are about to expire would not necessarily correspond to inaction on the part of Southern Company in marketing its generating capacity. Waiting, as Mr. Brubaker suggests, is not a prudent course of action, given that Southern Company will have other markets for existing capacity.

Second, waiting until the system impact study is completed is an unnecessary step. The new agreements provide for remedies in the event that the system impact study identifies any necessary transmission upgrades. And the very possibility of system upgrade reinforces the need to proceed now rather than waiting.

The third point Mr. Brubaker makes is that Progress Energy has not adequately identified the costs associated with the agreements, implying that transmission costs might be higher. As I stated previously, the agreements contain mitigation measures in the event of system upgrade costs protecting Progress Energy's customers.

Regarding alternatives to pursuing these agreements, Mr. Brubaker makes several suggestions that focus on adding coal capacity to the Progress Energy system. First of all, there are no existing coal-fired resources currently available that would compete with these agreements. Prices offered by Southern Company in these agreements are consistent with the pricing we have seen in the recent request for proposals for capacity, and, therefore, we would not expect that any further solicitation of the market would provide a more favorable result.

Second, Mr. Brubaker contends that we should have taken action to replace the existing agreement with coal capacity, or, in the alternative, we should currently be planning to add coal capacity by 2013. His suggestion that we should have acted to add coal capacity more than three years ago is made with perfect 20/20 hindsight, and the suggestion that we should add coal capacity by 2013 ignores the fact that these agreement address a 2010 need.

Mr. Brubaker does not ever reach a bottom line on what the most appropriate course of action should be. In fact, in the course of his testimony he suggests we should have already proceeded, or we should wait until 2010, or we should proceed immediately. Mr. Brubaker does seem to feel that Progress should actively pursue coal-fired generation to replace the existing UPS agreement, and the new agreements present an opportunity to do just that.

Regarding proposed Commission actions, I would just say that a suggestion that the agreements be subject to a later prudency challenge is entirely inappropriate. Having the agreements subject to a prudency challenge when Progress Energy seeks cost-recovery would essentially make any action taken by the Commission in this proceeding meaningless.

That concludes my summary.

(Transcript continues in sequence with Volume 4.)

STATE OF FLORIDA)

: CERTIFICATE OF REPORTER

COUNTY OF LEON)

I, JANE FAUROT, RPR, Chief, Office of Hearing Reporter Services, FPSC Division of Commission Clerk and Administrative Services, do hereby certify that the foregoing proceeding was heard at the time and place herein stated.

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

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

DATED THIS 3rd day of June, 2005.

JANE FAUROT, RPR
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FPSC Division of Commission Clerk and
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