BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NOS. 050045-EI AND 050188-EI FLORIDA POWER & LIGHT COMPANY

JULY 28, 2005

IN RE: PETITION FOR RATE INCREASE BY FLORIDA POWER & LIGHT COMPANY AND IN RE: 2005 COMPREHENSIVE DEPRECIATION STUDY BY FLORIDA POWER & LIGHT COMPANY

REBUTTAL TESTIMONY & EXHIBIT OF:

K. MICHAEL DAVIS

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6

7 Q. **Please state your name and business address.**

8 A. My name is K. Michael Davis, my business address is 9250 West Flagler Street,

9 Miami, Florida 33174.

10 Q. **Are you the same K. Michael Davis who submitted direct testimony and**

11 **supplemental direct testimony in this proceeding?**

12 A. Yes.

13 Q. **Are you sponsoring an exhibit to your rebuttal testimony?**

14 A. Yes. I am sponsoring an exhibit consisting of 11 Documents, KMD-10 through

15 KMD-20, which are attached to my rebuttal testimony.

16 Q. **What is the purpose of your rebuttal testimony?**

17 A. The purpose of my testimony is to rebut positions taken in this case by the

18 following witnesses for the intervenors and the FPSC Staff:

19 • Office of Public Counsel (OPC) witnesses Donna DeRonne, Kimberly

20 H. Dismukes, Hugh Larkin, and Michael Majoros

21 • South Florida Hospital and Healthcare Association (SFHHA) witness

22 Lane Kollen

23 • Florida Retail Federation (FRF) witness Sheree L. Brown

24 • Commercial Group witness James T. Selecky

1 • FPSC Staff witness Kathy Welch

2

3 My rebuttal testimony covers the following areas where issues have been raised:

4 • Capital Structure

5 • Rate Case Expenses

6 • Automated Meter Reading Project

7 • CWIP in Rate Base

8 • Working Capital

9 • GridFlorida

10 • Nuclear Fuel Last Core and End-of-Life Materials and Supplies

11 Accruals

12 • Nuclear Maintenance Reserve

13 • 2007 Turkey Point Unit 5 Adjustment

14 • Depreciation

15 • Dismantlement Costs on New Plants

16 • FPSC Staff Audit Reports

17 • Affiliate Transactions

18

19 Additionally, my rebuttal testimony sponsors Document KMD-10, Identified

20 Adjustments, which summarizes the adjustments FPL has identified as

21 appropriate during the course of this proceeding. Further, my testimony sponsors

22 Document KMD-13 which shows the effects of FPL's updated Depreciation

23 Study, and Document KMD-15 which shows the adjustments necessary to reflect

1 the Commission's decision on our storm damage cost recovery petition in Docket
2 No. 041291-EI.
3
4 **Capital Structure**

5 Q. **Mr. Larkin asserts it is inappropriate to offset deferred income tax assets**
6 **against deferred income tax liabilities because the customers are paying the**
7 **tax represented by the deferred income tax assets in most instances. Do you**
8 **agree?**

9 A. No. The Commission's policy on capital structure has been to include the net
10 amount of deferred income taxes in the capital structure as a cost free source of
11 capital. To the extent that taxes are not immediately paid to the state or Federal
12 government, deferred income tax liabilities are created. To the extent taxes are
13 paid earlier, deferred income tax assets are created. There is no fundamental
14 difference between the two. Rates paid represent the ultimate source of funds in
15 both cases. As such, the Commission should continue to follow its long standing
16 policy of treating the net amount of deferred income taxes (i.e., deferred income
17 tax liabilities less deferred income tax assets) as a cost free source of capital.
18
19 Commission orders support this position. For example, Order No. 13537, Docket
20 No. 830465-EI, page 26, states: "Because, as a general rule, sources of capital
21 cannot be clearly associated with specific utility property, the Commission has
22 traditionally considered all sources of capital (with appropriate adjustments) in
23 establishing a fair rate of return." Whenever FPL makes a cash payment for any
24 type of expenditure — whether it is for income taxes, payroll, construction or

1 whatever — it does so from a pool of funds generated from operations and all
2 sources of capital. When FPL records an accrual to reflect the excess of the tax
3 depreciation over book depreciation on a particular asset, it has additional funds
4 available in that period due to reduced current income tax payments. The
5 additional funds aren't put into a restricted bank account to be used only when
6 the tax-over-book differences turn around and the tax payments increase. Instead,
7 the increased operating cash flow in that period becomes a source of funds that is
8 used to pay current costs and expenses.
9
10 In contrast to the situation described above for deferred income tax liabilities,
11 where the deferral of income tax payments makes cash available to FPL, deferred
12 income tax assets arise where FPL has paid income taxes to the government. As a
13 result, FPL no longer has the cash available to use for other purposes. This
14 reduces the cost-free capital provided by deferred income tax liabilities and,
15 accordingly, it is natural and appropriate to offset the deferred income tax assets
16 against the deferred income tax liabilities when determining the funds FPL
17 actually has available to it as a cost-free source of capital.
18
19 Examples of situations that result in recognition of deferred income tax assets
20 include reserves (liabilities) for injuries and damages and for environmental
21 cleanup. Because FPL does not get a tax deduction for the accruals that build up
22 the reserve, a deferred income tax asset (prepaid tax asset) is created which will
23 reverse when actual payments associated with the injuries and damages are
24 made. Because the Commission requires deferred income taxes to be included in

1 the capital structure at zero cost, the inclusion of the prepaid tax asset is
2 necessary to offset the reduction to rate base. As an alternative, the Commission
3 could allow the deferred income tax asset in rate base which would accomplish
4 the same objective of getting the reserve (reduction to rate base) to a level
5 representative of the actual funds the Company has available. However, that is
6 not the Commission's policy.

7 Q. **Do you agree with Ms. Brown's assertion that FPL has improperly allocated**
8 **the removal of the accumulated deferred income taxes associated with the**
9 **storm damage fund on a prorata basis across all capital structure**
10 **components and that FPL should instead specifically eliminate the deferred**
11 **taxes from the deferred income tax capital structure component?**

12 A. No. The principles described in the immediately preceding answer apply equally
13 for the deferred income taxes associated with accruals to the Storm Damage
14 Reserve. Trying to track book accounting accruals that occur in different time
15 periods to actual cash payments and then attempting to track those cash payments
16 to a specific capital structure source is a futile exercise. Although it may be
17 possible to track the income tax effects of an item, doing so would result in
18 inconsistent treatment of like items. I believe this is why the Commission has
19 traditionally allocated rate base adjustments over all capital structure
20 components.

21

1 **Rate Case Expenses**

2 Q. **Ms. Brown observes that FPL included rate case expenses of $10.8 million in**
3 **Docket No. 001148-EI, which were amortized over a two year period**
4 **resulting in an annual rate case expense of $5.4 million. She goes on to state**
5 **that actual rate case expenses in that docket were only $4.5 million resulting**
6 **in an overrecovery and therefore asserts the currently requested rate case**
7 **expenses should be denied. Also, Ms. Brown states that: "While the**
8 **Commission has allowed utilities to defer rate case expenses in the past, FPL**
9 **is already recovering its rate case expense and its request for deferral and**
10 **amortization of rate case expenses should be denied." She alleges that, since**
11 **FPL included $5.4 million of rate case expenses in Docket No. 001148-EI and**
12 **since FPL was earning a return on equity in excess of its requested midpoint,**
13 **in effect the rate case expenses included in the 2006 test year have already**
14 **been recovered. Ms. DeRonne makes similar assertions. Do you agree with**
15 **these witnesses that the recovery of rate case expenses for this case could or**
16 **should be measured by the extent to which FPL recovered its 2002 rate case**
17 **expense?**

18 A. No. FPL's last rate case was in 2002 and was settled through a negotiated
19 agreement, obviating the need to incur the additional costs. That negotiated
20 settlement resulted in a $250 million base rate reduction and did not address
21 either the amount or disposition of rate case expenses. It would be inappropriate
22 and infeasible to trace recovery of the 2002 rate case expenses into the
23 subsequent years and reach conclusions about whether the precise amount of the
24 test year rate case expenses were or were not fully reimbursed to FPL, or were

1 part of the $250 million reduction. Moreover, such an exercise would run directly
2 counter to the concept of prospective, test year ratemaking.
3
4 Rate case expenses are a legitimate cost of doing business and should be fully
5 recognized. If these costs are not reflected in base rates to be set in January 2006,
6 FPL will be unfairly denied an opportunity to recover them.
7 **Q. Ms. DeRonne asserts that FPL is requesting rate case expenses in the 2006**
8 **test year that are out of period costs. Do you agree that recovery of rate case**
9 **expenses should be restricted to those incurred in the test year?**
10 A. No. As to the rate case expenses being out of period, this is a natural fallout of
11 the use of a projected test year. FPL must prepare in advance to file a projected
12 test year to set rates in a future period. In FPL's current case, we started the
13 preparation of MFRs and witness testimony in the last half of 2004, filed them in
14 the first quarter of 2005, and will be spending the rest of 2005 responding to
15 discovery requests, participating in the hearings and implementing the
16 Commission's final order. Inevitably, only a small portion of the rate case
17 expenses will be spent in the 2006 test year, because that's when the rates are
18 supposed to be approved and in effect. Adopting Ms. Brown's proposal to deny
19 recovery of rate case expenses incurred outside the test year would effectively
20 result in forbidding a utility recovery of such rate case expenses in cases based
21 on a projected test year. This would be unfair and inconsistent with the
22 Commission's well-established practice of allowing recovery of reasonable rate
23 case expenses.

1 **Q. Ms. DeRonne asserts that a two-year amortization period for rate case**
2 **expenses is unreasonable since it has been 20 years since FPL's last fully**
3 **litigated base rate case. Ms. Brown asserts that it is inappropriate to include**
4 **the unamortized portion of rate case expenses in working capital. Do you**
5 **agree with these assertions?**
6 A. No. The Commission used a two-year amortization in FPL's last rate case, with
7 no more certainty than there is today as to when the next rate case would occur. A
8 general rate proceeding could be initiated at any time. Rate case expenses
9 represent actual costs incurred by FPL and have a definite relationship to the
10 provision of electric service to FPL's customers. As such they are no different
11 than any other regulatory asset or prepaid expense.
12
13 Contrary to Ms. Brown's assertion, it is entirely appropriate to include the 2006
14 unamortized rate case expense in working capital and earn a return on these
15 unrecovered expenses until they are fully recovered. This approach is
16 consistently applied for other prepaid expenses and there is no reason to deviate
17 from that practice.
18 **Q. Finally, Ms. DeRonne asserts that the $550,000 of rate case expenses**
19 **projected to be incurred in 2006 is unreasonable since rates will be**
20 **implemented on January 1, 2006. Do you agree?**
21 A. No. What matters is whether the rate case expenses in total are reasonable and
22 are expected to be incurred. Whether they are incurred in 2004, 2005 or 2006 is
23 not relevant.
24

1 **Automated Meter Reading Project**

2 Q. **Ms. DeRonne asserts that $4.6 million of project costs related to the**
3 **Automated Meter Reading project (AMR) should be removed from rate**
4 **base in the test year. Do you agree?**

5 A. No. As explained in Ms. Santos' rebuttal testimony, the $4.6 million underrun
6 referred to by Ms. DeRonne will be incurred in 2005 in conjunction with the first
7 phase scheduled deployment of 50,000 meters. Therefore, the projected test year
8 amounts of $15.4 million in plant in service and $1.6 million in accumulated
9 depreciation are appropriate components of rate base.

10 Q. **Ms. DeRonne further proposes that the amount projected in plant in service**
11 **for the AMR project should be transferred to CWIP and accrue AFUDC**
12 **until system-wide deployment is implemented. Also, she recommends**
13 **removal of the related depreciation expense of $768,000, and O&M expense**
14 **of $1.6 million, from 2006 operating expenses. Do you agree?**

15 A. No. Ms. DeRonne is apparently unfamiliar with this Commission's policy
16 regarding the pre-capitalization of meters. The Commission has a long-standing
17 policy of recognizing meters as "reserve items" and as such has allowed utilities
18 to pre-capitalize them (i.e., place the meters directly into plant in service at the
19 time of purchase). In Docket No. 990529-EI, Petition for 1999 Depreciation
20 Study by Tampa Electric Company, Order No. PSC-00-0603-PAA-EI, the
21 Commission stated: "The accounting treatment utilized for meters, Account 370,
22 is cradle-to-grave in which a meter is capitalized upon purchase and not retired
23 until the meter can no longer be refurbished and is finally junked." Ms.
24 DeRonne's suggestion to place these costs in CWIP and accrue AFUDC goes

against Commission policy. The Commission's policy recognizes that meters are immediately used and useful in direct contrast to the concept of AFUDC for large projects that are typically placed in service at the end of construction when they become used and useful. To wait until system-wide deployment is completed would ignore this fact.

Because the AMR meters will be used and useful as soon as they are acquired, the associated depreciation expense of $768,000, and O&M expenses of $1.6 million, should be allowed.

CWIP in Rate Base

Q. Mr. Larkin proposes to remove CWIP from FPL's test year rate base. Would such an adjustment be consistent with the Commission's policy on CWIP?

A. No. The amount of CWIP included in rate base was determined in accordance with Commission Rule 25-6.0141. CWIP should be allowed to accrue AFUDC or be included in rate base. To do otherwise would result in confiscatory treatment.

The Commission historically has recognized that utilities are entitled to a return on CWIP either through AFUDC or via inclusion in rate base. For example, in Order No. 11437, Docket No. 820097-EU, the Commission states that:

> "The Company's investment in plant under construction can be accounted for by either of two methods. An Allowance for Funds Used During Construction (AFUDC) may be applied to the balance to be capitalized and later

1 recovered through depreciation charges once the plant is
2 placed in service. When this method is chosen, the
3 financial statements of the Company reflect paper income
4 "credits" associated with AFUDC, but the utility realizes
5 no current cash earnings from the investment in CWIP.
6 Alternatively, CWIP may be included as a portion of rate
7 base. Where this treatment is allowed, CWIP generates
8 cash earnings, which provide cash flow and increase
9 coverage ratios. Of course, no AFUDC is taken on that
10 portion of CWIP which is included in rate base."
11
12 Based on this excerpt, it is clear that the Commission's policy is to allow AFUDC
13 or rate base treatment of CWIP. Therefore, the only question should be whether
14 the CWIP included in rate base has been determined in accordance with the
15 Commission's rules and Mr. Larkin does not dispute this fact.
16 Q. **Did the modification of Rule 25-6.0141 for AFUDC change the Commission's**
17 **historic practice of allowing a return on CWIP either through the accrual of**
18 **AFUDC or inclusion in rate base?**
19 A. No. The modification of Rule 25-6.0141 (AFUDC Rule) in 1997, only changed
20 the basis for determining whether CWIP will accrue AFUDC or will be included
21 in rate base. Under the Rule, the CWIP associated with projects that will cost
22 greater than 0.5% of the total balance of Accounts 101 and 106 are eligible to
23 accrue AFUDC. Smaller projects do not accrue AFUDC and, accordingly, are to
24 be included in rate base. The transcript of the Agenda Conference at which the

1 Rule modifications were approved contain several discussions between the
2 Commissioners and Staff that clearly indicate the Commission was focused on
3 determining whether CWIP would accrue AFUDC or instead earn a current
4 return as rate base. There is no suggestion in the transcript that prudently incurred
5 CWIP would be denied a return as alleged by Mr. Larkin. My Document KMD-
6 11 contains excerpts from the relevant portion of that transcript.

7 **Q. How has FPL treated CWIP in its 2006 test year MFRs?**

8 A. FPL has accounted for CWIP consistent with the Commission's rule. That is, FPL
9 has excluded from rate base that portion of CWIP that is eligible for AFUDC
10 under Rule 25-6.0141 and has included in rate base the remaining CWIP that,
11 under the Rule, is not earning an AFUDC return. This is clearly the treatment that
12 is envisioned by the Commission and is consistent with how FPL has accounted
13 for CWIP in all of its monthly Earnings Surveillance Reports since the AFUDC
14 Rule was changed in 1997 and in the reports and schedules used to support the
15 1999 and 2002 Settlement Agreements.

16

17 **Working Capital**

18 **Q. Mr. Larkin recommends exclusion of items from working capital,**
19 **apparently because the assets do not involve current cash receipts and the**
20 **liabilities do not result from current cash payments. Do you agree with his**
21 **approach?**

22 A. No. Mr. Larkin acknowledges on page 52, lines 11 through 13 of his testimony
23 that the basis for his proposed adjustments hinges on the outflow, or lack of
24 outflow, of dollars (cash). What Mr. Larkin proposes is a transparent attempt to

1 use the discredited lead-lag study or "formula" approach in determining working
2 capital. FPL's books and records are kept using accrual accounting, which results
3 in both assets and liabilities being recognized when economic events take place,
4 not at the time of cash receipt or disbursement. For example, as meters are read,
5 revenues are recorded; as goods and services are received, expenses are recorded.
6 The offsets to the recording of these profit and loss items before cash is received
7 or paid are corresponding balance sheet items, i.e., accounts receivable and
8 accounts payable. These assets and liabilities, recorded on the balance sheet,
9 recognize that no cash flow has occurred.
10
11 For the 2006 test year, FPL calculated its working capital using the balance sheet
12 method, which has been consistently applied by this Commission since the early
13 1980s. Order No. 13537, Docket No. 830465-EI, page 15 states: "In recent cases
14 we have applied the balance sheet approach to determine the working capital
15 allowance." Order No. 11437 in Docket No. 820097-EU, states: "A traditional
16 component of rate base is the value of the working capital committed to utility
17 operations. In recent cases we have applied the balance sheet approach to
18 determine the working capital allowance, as opposed to the 'formula' approach
19 previously utilized." This same Order goes on to define working capital: "...as
20 current assets and deferred debits that are utility related and do not already earn a
21 return, less current liabilities, and deferred credits and operating reserves that are
22 utility related and upon which the Company does not already pay a return." In
23 summary, whether a working capital item generates a cash transaction
24 immediately or there is a timing difference associated with the working capital

1 item are not the criteria used by this Commission for inclusion in working
2 capital. Focusing on the cash transactions would be clearly inconsistent with the
3 Commission-approved balance sheet approach. A logical extension of Mr.
4 Larkin's philosophy would be that FPL should not reduce rate base for any of its
5 accounts payable. Were FPL to take this approach, it would result in a substantial
6 increase in working capital thereby increasing rate base and resulting in increased
7 revenue requirements. In fact, this increase in working capital would
8 significantly exceed the sum of all Mr. Larkin's recommended working capital
9 adjustments.

10 **Q. Mr. Larkin's testimony is that: "Mr. Davis is wrong when he states FPL is**
11 **paying a return on these amounts to customers twice, once as a return on the**
12 **reduction of working capital included in rate base through base rates and, a**
13 **second time through interest expense paid to customers on the overrecovery**
14 **at the commercial paper rate through the cost recovery clause." He then**
15 **asserts that underrecoveries should be excluded from rate base because if**
16 **they were included the Company would receive a double return on the**
17 **underrecovery. Do you agree with his statements?**

18 A. No. His statements are incorrect and inconsistent. As I discussed in my direct
19 testimony, a return is paid on overrecoveries and received on underrecoveries
20 through the appropriate cost recovery clause. Overrecoveries should be removed
21 from rate base in the same manner that underrecoveries are removed from rate
22 base since both pay or earn a return through the appropriate cost recovery clause.
23 To include the overrecovery in rate base is to provide customers a double return

1 ***because it reduces rate base and the associated return.*** These are similar items
2 that should be treated the same.

3 Q. **Do you agree with Mr. Larkin's proposals to (1) record the Other Deferred**
4 **Credit associated with SJRPP accelerated recovery as a reduction to**
5 **working capital unless FPL can show that the liability to SJRPP is not a**
6 **source of funds to the Company and (2) to restore the $1 million regulatory**
7 **liability the Company has removed from working capital for the gain on the**
8 **sale of emission allowances because the Company has the use of the funds**
9 **during the period they have not been flowed back to ratepayers?**

10 A. No. Both items are properly included in a cost recovery clause.

11

12 Mr. Larkin acknowledges that the credit associated with this SJRPP liability is
13 collected through the capacity clause, yet he still wants to leave it in working
14 capital (reversing the adjustment in MFR B-2). This would result in customers'
15 receiving a double return on this liability—once through a current return on the
16 balance of the SJRPP liability paid to customers through the capacity clause and
17 again through the reduction in rate base by leaving the liability as a reduction to
18 rate base. Also, such treatment is inconsistent with the definition of working
19 capital provided in Order No. 11437 in Docket No. 820097-EI, that I quoted
20 earlier in my testimony. Specifically, because FPL pays a return on the SJRPP
21 liability through a clause, it does not meet the Commission's definition of a
22 liability includable in working capital.

23

1 Mr. Larkin raises this same argument with respect to the $1 million regulatory
2 liability for the gain on the sale of emission allowances which is wrong for the
3 same reasons as above since a return on this credit is paid to customers through
4 the environmental clause.

5 **Q. Do you agree with Mr. Larkin's proposed adjustment to remove from**
6 **working capital items related to derivative assets and liabilities?**

7 A. No. All balance sheet entries related to derivatives zero out except for the cost of
8 option premiums.
9
10 What Mr. Larkin did not recognize is that, except for option premiums, an
11 offsetting regulatory asset or liability is recorded at the same time and in the
12 same amount as the derivative liability or asset is recorded. This has the effect of
13 directly and completely offsetting the derivative transactions such that they have
14 no impact on rate base.
15
16 The options relate directly to the hedging program approved by the Commission
17 in Docket No. 011605-EI, Order No. PSC-02-1484-FOF-EI, issued October 30,
18 2002. In that Order, the Commission stated: "Further, the Proposed Resolution
19 of Issues appears to remove disincentives that may currently exist for IOUs to
20 engage in hedging transactions that may create customer benefits by providing a
21 cost recovery mechanism for prudently incurred hedging transaction costs, gains
22 and losses, and incremental operating and maintenance expenses associated with
23 new and expanded hedging programs." The option premiums are legitimate and
24 necessary cash outlays made as part of the hedging program. Option premiums

1 are included in rate base exactly as is the cost of fuel inventory. When the fuel is
2 burned, the cost of the options and the related fuel are expensed in tandem
3 through the fuel clause. If the options are removed from working capital, FPL
4 would not have an opportunity to recover the time value of money associated
5 with the option premiums over the period between FPL's purchase of the options
6 and their recovery through the clause. This would provide a disincentive to FPL
7 which is contrary to the provision contained in The Proposed Resolution of
8 Issues, attached to the Order in Docket No. 011605-EI as Attachment A and
9 incorporated in the Order by reference. Also, removal of the cost of the options
10 from working capital would result in their being treated differently than the fuel
11 to which they relate.

12 Q. **Do you agree with Mr. Larkin's proposal to include the payable to the**
13 **Nuclear Decommissioning Fund in the calculation of working capital and**
14 **thus decrease working capital by $5.7 million because it represents a source**
15 **of funds between the time the revenues are collected and when the funds are**
16 **deposited in the nuclear decommissioning trust fund?**

17 A. No. The Commission has previously determined that the nuclear
18 decommissioning reserve should be excluded from rate base because it earns a
19 return, and that related accounts should also be excluded from rate base including
20 the nuclear decommissioning accounts payable. Also, it is important to note, that
21 the amount due to the nuclear decommissioning trust fund is paid in the next
22 month so the liability only exists for a few days.
23

1 **<u>GridFlorida</u>**

2 Q. **Various witnesses have criticized the inclusion of the $45 million Company**
3 **adjustment and other costs budgeted for GridFlorida RTO costs in the 2006**
4 **test year. Would you like to comment?**

5 A. As discussed by Mr. Mennes in his direct testimony, GridFlorida is a real activity
6 looming on the horizon. FPL needs to recover the costs associated with this RTO
7 and my adjustment brings the level of GridFlorida costs to an annual average of
8 what FPL expects to incur for these types of costs over a five year period.
9 Additionally, as Mr. Mennes stated in his direct testimony, the costs included in
10 our test year compare favorably to actual costs incurred by similar RTOs
11 currently in operation. Without this adjustment, the level of GridFlorida costs
12 included in the test year would not be representative of the costs FPL can expect
13 to incur for this type of RTO and our base rates would not provide for recovery of
14 those costs. The Commission should not ignore a cost which is outside of FPL's
15 control, unless an alternative means of recovery is provided.

16

17 **<u>Nuclear Fuel Last Core and End-of-Life Materials and Supplies Accruals</u>**

18 Q. **Ms. Brown states that the Commission should suspend Last Core Nuclear**
19 **Fuel and End-of-Life Materials and Supplies Accruals until FPL files its**
20 **decommissioning studies and justifies continued accruals to the reserves. Do**
21 **you agree with this proposal?**

22 A. No. Both items have already been approved for recovery by the Commission.
23 FPL's test year expense is based on the amounts approved by the Commission in
24 Order No. PSC-02-0055-PAA-EI. As I stated in my direct testimony, FPL will

1 file updated studies later this year. Until a determination is made by the
2 Commission to change those accruals, the amount included is appropriate.
3
4 **Nuclear Maintenance Reserve**

5 Q. **Ms. Brown has proposed an adjustment to the Nuclear Maintenance Reserve**
6 **of $61.6 million for 2006. Her basis for this adjustment is that the Company**
7 **has debited the Nuclear Maintenance Reserve with anticipated costs of the**
8 **next outage at the time the accruals began instead of when the actual**
9 **expenditures are made. Do you agree with her proposed adjustment and**
10 **conclusion?**

11 A. Not entirely. Ms. Brown's adjustment to FPL's regulatory liability associated
12 with the Nuclear Maintenance Reserve is partially correct, but she has neglected
13 to consider corresponding adjustments to correct pre-test year balances that
14 actually reduce the regulatory liabilities and increase rate base. The comment that
15 the Company has debited the Nuclear Maintenance Reserve with anticipated
16 costs of the next outage at the time the accruals begin instead of when the actual
17 expenditures are made is true. However, Ms. Brown's recalculation neglected to
18 include the 2004 and 2005 outage reversals which impact the 2006 beginning
19 balance of the reserve. My Document KMD-12 recalculates the balance of the
20 regulatory liability based on Ms. Brown's recommended adjustment for the
21 timing of expenditures, and corrects her omission of the 2004 and 2005 outage
22 reversals. This Document shows that the resulting jurisdictional 13-month
23 average regulatory liability should be $53.1 million instead of the $58.9 million

1 currently included in rate base. Because regulatory liabilities reduce rate base,

2 this means that the test year rate base is actually understated by $5.8 million.

3

4 **2007 Turkey Point Unit 5 Adjustment**

5 Q. **Mr. Larkin and Mr. Selecky recommend the removal of the Turkey Point**

6 **Unit 5 Adjustment as it is outside the test period and would be better**

7 **addressed within a base rate proceeding closer to the actual in service date.**

8 **Do you agree with their recommendations?**

9 A. No. The in-service date of Turkey Point Unit 5 and the revenue requirements

10 associated with placing the unit in service are determinable with a high degree of

11 certainty. As such, it is entirely appropriate to consider them in this proceeding.

12 The Commission has approved similar limited scope requests in previous

13 proceedings such as FPL's St. Lucie Unit 2 Plant in Order Nos. 11437 and 12348,

14 Docket No. 820097-EU and for Progress Energy Florida's Crystal River Unit 5

15 Plant in Order No. 13771, Docket No. 830470-EI. In Docket No. 820097-EU,

16 FPL presented costs associated with St. Lucie Unit 2 in its rate case. In Order No.

17 11437, the Commission stated:

18 "With some modification, we are in favor of the general

19 concept proposed by FPL. Failure to recognize in rates the

20 investment in a plant as expensive as this could have

21 disastrous financial consequences for FPL in a short period

22 of time. On the other hand, requiring the utility to initiate

23 another full revenue requirements case merely to place this

24 plant in rate base would involve significant regulatory lag

1 detrimental to the utility and substantial amounts of
2 unnecessary rate case expense to be borne by the
3 customers. Notwithstanding our approval of the concept,
4 we believe we would be premature in approving the costs
5 and expenses associated with the plant at this juncture.
6 FPL's latest projection is that it will place St. Lucie Unit
7 No. 2 in commercial service in mid-June, 1983, while the
8 cost data available on the plant was prepared and filed
9 with testimony in April, 1982. We believe that more
10 current cost data will be required to make an informed
11 decision as to the revenue requirements of this plant.
12 Additionally, we believe that the methodology for
13 allocating the increased revenues associated with this plant
14 deserves closer examination."
15
16 While in the case of St. Lucie Unit 2, the Commission subsequently conducted a
17 limited scope hearing because of uncertainty about the cost data, no such follow-
18 up hearing is warranted in this case. The Commission has previously reviewed
19 the cost information for Turkey Point Unit 5 in FPL's need docket and the
20 operating costs of this type of plant are highly estimable because we already have
21 similar plants in operation. Mr. Yeager discusses the reliability of the Turkey
22 Point Unit 5 costs in more detail in his rebuttal testimony. Therefore, there is no
23 corresponding need for a subsequent update of the Turkey Point Unit 5 cost data.
24

1 **Depreciation**

2 **General**

3 Q. **After having reviewed the issues raised by Mr. Majoros and others, would**
4 **you please provide some background on this Commission's practices for**
5 **recovery of plant in service and cost of removal?**

6 A. Yes. The Commission provides the following three separate mechanisms which
7 FPL uses to recover the costs associated with its ownership, use and disposition
8 of property, plant and equipment:

9 - Depreciation addresses recovery of FPL's investment in plant in service.
10 Also, depreciation addresses the cost of removing specific units of
11 property that have reached the end of their useful life before the facility,
12 of which it is a part, reaches the end of its useful life (cost of removal).
13 - Nuclear Decommissioning addresses the cost of removing both
14 contaminated and non-contaminated property when an entire nuclear unit
15 reaches the end of its useful life.
16 - Fossil Dismantlement addresses the cost of removing complete fossil-
17 fueled generating units when they reach the end of their useful life, or
18 when a unit or units at a site are repowered, (i.e., the original steam
19 turbine is retained and a new combined cycle steam supply is
20 constructed).

21

22 Each of these mechanisms is governed by numerous Commission rules and
23 precedents, which FPL follows in keeping its books and records and in preparing
24 the very detailed studies required to support recovery under each of the

mechanisms. The studies are subject to Commission review and approval. As part of this process, the Commission Staff and interested parties are given an opportunity to review and comment on the studies. Ultimately, the Commission determines any adjustments to these studies arising out of this review. These studies are filed every four or five years depending on the Commission's rules.

Q. Have FPL's current and previous depreciation studies been prepared and filed in compliance with Commission requirements?

A. Yes. FPL's current depreciation study and its predecessors were prepared and filed in compliance with all of the Commission's requirements. Thus, the issues raised by Mr. Majoros and others represent an attempt to convince the Commission to rework its rules and practices on depreciation in order to achieve the particular base rate results sought by the intervenors. Specifically, Mr. Majoros is recommending that the Commission change a limited number of depreciable lives and implement his ideas regarding the measurement and recognition of removal costs. Also, the intervenors are proposing alternative ways to deal with the calculated theoretical reserve surplus.

I will address the issues raised by Mr. Majoros and others in the following subsections:

- Depreciable Lives,
- Theoretical Reserve Surplus, and
- Cost of Removal.

1 **Q. Mr. Majoros has recast the depreciation study filed by FPL on March 17,**
2 **2005, and has included it as his Exhibit MJM-7. Do you agree with the**
3 **changes he is recommending in his study?**
4 A. No. The principal differences reflected in his study are changes to the depreciable
5 lives for certain transmission, distribution and general property, the use of a net
6 present value (NPV) approach to providing for cost removal, and accelerated
7 amortization of the theoretical reserve surplus.
8
9 FPL rebuttal witness, Mr. Stout, addresses the changes in depreciable lives and
10 the approach to cost of removal in his testimony. Based on the conclusions
11 expressed by Mr. Stout and my own conclusions regarding the theoretical reserve
12 surplus, which I discuss later in my testimony, Mr. Majoros' study should be
13 rejected by this Commission.
14 **Q. Has FPL updated the Depreciation Study it filed on March 17, 2005?**
15 A. Yes. Consistent with normal practice, FPL filed an updated depreciation study on
16 July 1, 2005.
17 **Q. What were the changes between the studies filed on March 17, 2005 and July**
18 **1, 2005?**
19 A. The July 1, 2005 study updated the earlier study to include all actual results for
20 2004. The updated study also reflects the effects of FPL completing the
21 unitization of the Sanford and Fort Myers combined cycle units (placed in
22 service in prior years). In addition, the updated study includes the effects of
23 revised retirement units for nuclear and fossil plants (as I discussed in my cross
24 examination in Docket No. 041291-EI), and a separate capital recovery schedule

1 for the replacement of approximately 2.6 million meters related to the AMR
2 project. Finally, the updated study reflects allocation of all of the bottom line
3 reserve deficit to the nuclear function, instead of the nuclear, transmission and
4 distribution functions.

5 **Q. Would you please summarize the impact of these changes on the**
6 **depreciation expense that FPL is requesting in its test year?**

7 A. My Document KMD-13 summarizes all of the updates I mention above. The total
8 effect on depreciation expense in 2006 is $64.7 million.

9 **Q. At the time FPL filed its initial depreciation study in this docket did it advise**
10 **the Commission and other parties that it would be updating this study?**

11 A. Yes. In the transmittal letter attached to the March 17, 2005 filing, FPL advised
12 all the parties that it would be updating this initial filing for actuals for 2004 and
13 other known changes.

14 **Depreciable Lives**

15 **Q. Do you agree with Mr. Majoros' comments that the 2005 depreciation study**
16 **filed in this docket results in "excessive depreciation" expense?**

17 A. Absolutely not. First of all Mr. Majoros' characterization of "excessive
18 depreciation" is telling in itself. He says that: "An ***excessive depreciation rate*** is
19 one that produces more depreciation expense than necessary to recover the cost
20 of a company's capital asset over the life of the asset." (Emphasis in original).
21 Thus, he acknowledges that the measure of the adequacy of a depreciation rate is
22 its effect over the life of an asset, not just the rate's effect during a portion of the
23 life of an asset. Despite acknowledging the appropriateness of this long-term
24 view, he proposes to adjust depreciation expense over a period much shorter than

1 the life of the assets primarily by amortizing the theoretical reserve surplus over
2 10 years.
3
4 Because FPL's proposed depreciation rates are designed to produce only the
5 amount of depreciation necessary to recover the remaining net book value of the
6 assets over the remaining useful life plus the cost of removal, they are not
7 excessive.

8 Q. **Mr. Majoros alleges that FPL's depreciable lives are too short. He cites the**
9 **existence of FPL's fossil units that are almost fully depreciated as an**
10 **example. Specifically, on page 7, lines 6 through 8 he makes the following**
11 **statement: "The impact of past excessive depreciation rates can be**
12 **demonstrated by looking at the current status of several of the company's**
13 **fossil plants. Several of these plants are almost totally depreciated today and**
14 **they are still producing power. That means that the rates paid by past**
15 **customers were higher than needed." Do you agree with Mr. Majoros'**
16 **conclusion?**

17 A. No, I do not. Mr. Majoros' conclusion is simplistic and misses the point. The
18 mere fact that a generating unit is mostly depreciated but still capable of
19 producing power should not cause a reasonable person to conclude that past
20 depreciation rates have been excessive. One should look instead to the remaining
21 net book value of the plant and consider that in relation to the ongoing utility of
22 the plant.
23

1 The fossil units cited by Mr. Majoros are presumably the steam units which are
2 older and are dispatched less often because they are less efficient. The weighted
3 average 2004 capacity factor for these units was about 40% with several in the
4 teens. Nevertheless, customers benefit from these units because they are
5 available to meet load when necessary. The lower net book value and the lower
6 resulting depreciation expense are entirely appropriate given the manner in which
7 the plants are utilized.
8
9 **Q. Mr. Majoros contends that FPL's theoretical reserve surplus was caused**
10 **primarily by the use of nuclear and steam production depreciation rates**
11 **based on life assumptions that were too short. Do you agree with his**
12 **statements?**
13 A. No. When a depreciation study is done, FPL uses known or expected lives
14 believed to be accurate at the time the study is prepared. Prior to the NRC license
15 extensions, FPL reasonably and appropriately calculated the depreciation
16 expense for its nuclear plants over their original operating license periods. This
17 approach yielded a deficiency in the reserve for the nuclear function that was
18 reflected in FPL's 1997 depreciation study. FPL's 2005 depreciation study, filed
19 in this proceeding, used the known or expected lives for those units, which
20 includes the newly approved license extensions for the nuclear generating
21 facilities. Thus, in both instances, FPL properly used the plant lives that were
22 known or expected at the time. The change between 1997 and 2005 in what was
23 "known or expected" about the lives of these units is the primary cause of the
24 theoretical reserve surplus in depreciation. The possibility of such changes is one

of the reasons the Commission requires electric utilities to file new depreciation studies every 4 years.

Q. What is the proper accounting for changes in the useful lives of depreciable assets?

A. Changes in the estimated useful lives of depreciable assets should be reflected as prospective changes to depreciation rates over the remaining lives of the related assets. This accounting policy has been recognized by the FPSC and FERC. Also, Generally Accepted Accounting Principles (GAAP) require that changes in estimates (specifically service lives of depreciable assets) be accounted for in the current period if the change affects that period only or the period of change and future periods if the change affects both. FERC states that utilities must use a method of depreciation that allocates in a systematic and rational manner the service value of depreciable property over the service life of the property. FPL's use of the "remaining life method" which reflects the recovery of the net book value of the assets over their remaining life is consistent with all of this guidance. This Commission has consistently approved the application of the remaining life method for FPL in Docket Nos. 910081-EI, 931231-EI, and 971660-EI, the last three times new depreciation rates were established based on comprehensive depreciation studies as well as for individual plant studies filed by FPL.

I think it is interesting to note that SFHHA witness Lane Kollen's filed Surrebuttal testimony in a 2001 Entergy Gulf States case (Louisiana Public Service Commission Docket No. U-24993) supports FPL's position by recognizing that:

1 "…once the twenty-year life extension is considered, the
2 existing accumulated depreciation reserve is higher than it
3 would have been if the unit had originally been
4 depreciated over a 60-year life rather than a 40-year life.
5 This difference is termed a "reserve surplus". If the useful
6 life of an asset is shortened from its original estimate, then
7 the accumulated depreciation reserve is lower than it
8 would have been if the asset had been depreciated over a
9 shorter life. This latter difference is termed a "reserve
10 deficiency". ***Such reserve surpluses and reserve
11 deficiencies inherently are recovered (amortized) over the
12 remaining estimated life of an asset every time a new
13 depreciation study is developed.*** Such adjustments are
14 considered to be changes in estimates and do not constitute
15 retroactive ratemaking. This methodology historically has
16 been utilized by the [Louisiana] Commission, and just
17 three years ago in the Docket No. U-22092 depreciation
18 proceeding, was proposed again by the Company … and
19 again approved by the Commission." (Emphasis added).

20 **<u>Theoretical Reserve Surplus</u>**

21 **Q. What is a theoretical depreciation reserve?**

22 A. A theoretical depreciation reserve is a calculated rather than an actual
23 depreciation reserve which is used as a guide in analyzing the actual reserve
24 condition. It is not an exact measurement for determining the condition of the

1 actual reserve. It is a reference point calculated at a point in time based on
2 current or proposed depreciation parameters. Also, it gives no consideration to
3 the manner in which the asset is being utilized.

4 **Q. How is a theoretical reserve surplus determined?**

5 A. The theoretical depreciation reserve is a snapshot look at where the accumulated
6 provision for depreciation should be at a specific point in time based on specific
7 assumptions about the future. This is compared with the accumulated provision
8 actually reflected in the books and records. The difference between these
9 amounts is the theoretical reserve surplus or deficit.
10
11 If you lived in a world of perfect information and knew precisely the exact lives,
12 retirements, cost of removal, salvage and other recoveries of all plant in service
13 the accumulated provision for depreciation would be identical to the theoretical
14 reserve. However, because this is not a perfect world, you may have more or less
15 accumulated depreciation resulting in either a theoretical reserve deficit or
16 surplus. However, as future events change, the theoretical reserve deficit or
17 surplus will change.

18 **Q. Did the depreciation study filed on March 17, 2005 and the July 1, 2005**
19 **update reflect a theoretical reserve surplus?**

20 A. Yes, both the original study and the update reflect a theoretical reserve surplus.
21 The theoretical reserve surplus in the March study was $1.5 billion. The
22 theoretical reserve surplus in the July update was $1.3 billion.

1 **Q. Please explain why the theoretical reserve surplus changed.**

2 A. The items causing the change in the theoretical reserve surplus are shown on my
3 Document KMD-13.

4 **Q. Mr. Majoros says that the theoretical reserve surplus is $2.4 billion. Do you**
5 **agree?**

6 A. No. His theoretical reserve surplus is based on his depreciation study which I
7 recommend be rejected by the Commission.

8 **Q. Mr. Majoros says that FPL is not paying a return to customers on the**
9 **surplus. Does this mean that customers receive no benefit from the existence**
10 **of the theoretical reserve surplus?**

11 A. Absolutely not. Revenue requirements for the 2006 test year in this proceeding
12 are $265.4 million lower than they would have been without the theoretical
13 reserve surplus. This reduction has two components: lower return requirements
14 due to lower rate base, and lower depreciation expense due to lower unrecovered
15 balances of plant in service.

16

17 Mr. Majoros' statement is misleading and more than a little disingenuous. The
18 theoretical reserve surplus relates to the recovery of funds (capital investments)
19 paid by FPL when the plant in service items were acquired or constructed. The
20 only time it would be appropriate for FPL to actually pay a return would be when
21 it collects funds from customers ***before*** it expends them. Nevertheless, as I stated
22 above, FPL's customers are receiving a very real and tangible benefit from the
23 existence of the theoretical reserve surplus.

24

1 The benefit is a direct result of accumulated depreciation reducing rate base.
2 Because rate base has been reduced, the return requirements associated with rate
3 base are lower. Based on the theoretical reserve surplus shown in the depreciation
4 study filed July 1, 2005, the lower rate base reduced revenue requirements by
5 $169.3 million.
6
7 In addition, because the theoretical reserve surplus reduces the net book value of
8 the associated plant in service, depreciation expense in the test year and future
9 years will be lower. This is because there is less investment in plant remaining to
10 be recovered. The reduction in test year depreciation expense reduced revenue
11 requirements by $96.1 million.
12 **Q. Mr. Majoros states that: "...based solely on the Company's depreciation**
13 **study as filed...the FPSC should amortize FPL's calculated reserve excess**
14 **back to rate payers." Do you agree?**
15 A. No. In the first place, I disagree with the implication that amounts have
16 inappropriately been collected from our customers. Second, the proper way to
17 address the theoretical reserve surplus is through lower depreciation expense
18 over the remaining lives of the assets, reflecting the lower net book value
19 remaining to be recovered. Under Commission rules, FPL can only recover its
20 investment in plant plus the cost of removing that plant at the end of its useful
21 life. As such, there is an absolute ceiling on FPL's recovery. To the extent a dollar
22 has been recovered in the past, future recoveries are reduced. That is precisely
23 why depreciation expense is lower than it would have been if the theoretical
24 reserve surplus did not exist.

1 FPL has properly included the effects of the theoretical reserve surplus in the
2 development of prospective depreciation rates in its 2005 depreciation study. As
3 a result, those rates, and the resulting depreciation expense that is included in our
4 2006 test year, are lower than they would have been without the surplus. This has
5 the dual effect of reducing the depreciation expense that customers will pay
6 through base rates and of eliminating the theoretical reserve surplus over the
7 remaining life of the affected assets. Additionally, the accumulated provision for
8 depreciation which is the cumulative effect of the recovery of plant in service
9 reduces plant in service included in rate base.

10 **Q. Do you agree with Mr. Majoros' proposal for dealing with the theoretical**
11 **reserve surplus?**

12 A. No. Mr. Majoros is proposing to flow the surplus back to customers over a 10
13 year period. He also said a 4 year period could be justified. Using his
14 amortization periods has the effect of providing current customers a windfall at
15 the expense of future customers. My Document KMD-14 shows the rate shock
16 impact on FPL customers in the fifth year under Mr. Majoros' proposed four-
17 year flowback or in the eleventh year under his proposed ten-year flowback.
18 When coupled with the approximately $858 million in planned capital
19 expenditures for the nuclear plants and the additional depreciation of these
20 nuclear additions, the flowback would result in an increase in revenue
21 requirements of $616 million in the case of the four-year flowback or of $415
22 million in the case of the ten-year flowback. These large rate shocks illustrate
23 why Mr. Majoros' "borrow against the future" approach to depreciation should be
24 rejected.

1 Q. **Messrs. Majoros and Larkin assert that, since the Commission has**
2 **previously permitted accelerated recovery of a deficiency in the reserve for**
3 **depreciation it would only be appropriate that the Commission follow that**
4 **same policy regarding reserve surpluses (or what Mr. Larkin refers to as**
5 **reserve sufficiencies). Do you agree?**

6 A. No. The Commission has allowed reserve deficiencies to be recovered over
7 periods that are shorter than the remaining useful lives of the affected assets
8 where specific events supported the recovery. Neither OPC witness cites any
9 instance where any public service commission has flowed back what they refer to
10 as a depreciation reserve surplus over a period shorter than the remaining life of
11 the affected assets. Also, neither of them has cited any specific event or
12 circumstance, other than the mere existence of the theoretical reserve surplus to
13 support their recommendation of a period shorter than the remaining useful life
14 of the related asset.

15 Q. **Mr. Larkin states that FPL has advocated the elimination of reserve**
16 **deficiencies as soon as possible when a reserve deficiency existed in the past.**
17 **Would you like to comment on this?**

18 A. Yes. FPL has done this: (1) to recover potentially stranded assets at a time when
19 deregulation seemed imminent; and (2) to establish, pursuant to the
20 Commission's Depreciation Rule 25-6.0436: "capital recovery schedules to
21 correct associated calculated [reserve] deficiencies" prior to retirement of major
22 installations where: "(1) replacement of an installation or group of installations
23 is prudent and (2) the associated investment will not be recovered by the time of
24 retirement through the normal depreciation process." Both of these exceptions

1 relate to very specific circumstances and do not apply generally to theoretical
2 depreciation reserve deficiencies as Mr. Larkin implies.
3 Q. **Mr. Larkin cites FPL witness Mr. Gower's statements in Docket No. 970410-**
4 **EI regarding amortization of reserve deficiencies. Mr. Larkin states: "Mr.**
5 **Gower, as stated above, thought it important to return underrecoveries to**
6 **investors over a short period of time and that the return of these funds will**
7 **result in lower future costs...By amortizing overrecoveries back to**
8 **ratepayers' rates will also be reduced. Lower rates will stimulate sales and**
9 **thus increase returns to stockholders." Do you agree with Mr. Larkin's**
10 **conclusion?**
11 A. No. Mr. Larkin ignores two obvious facts in his analysis. The first is that as the
12 theoretical reserve surplus is flowed back, rate base will increase, causing an
13 increase in revenue requirements. The second is that any reduction in base rates
14 will have an adverse effect on cash flow requiring FPL to seek replacement funds
15 through increases in capitalization. The combination of the two will result in an
16 increase, not a decrease, in requirements and rates. As such, Mr. Larkin's
17 assertions regarding sales and stockholder returns will be short lived if they occur
18 at all.
19 <u>Cost of Removal</u>
20 Q. **What approach has the Commission taken regarding the cost of removing**
21 **plant in service at the end of its useful life?**
22 A. The Commission requires that the depreciation rates used by companies it
23 regulates include a provision for cost of removal. That provision is reflected as an
24 addition to the depreciation rate associated with the recovery of the cost of the

1 item of plant in service or through the separate mechanisms described earlier in
2 my rebuttal testimony.

3 **Q. Does FPL have a legal obligation to remove these items?**

4 A. Not in every case. As a general rule, a legal liability only exists where
5 transmission and distribution assets are located on leased property or where there
6 are environmental issues. In addition, a legal liability exists for removal of
7 significant portions of our nuclear facilities; however, that is addressed through a
8 separate mechanism outside of depreciation rates. In any case, whether a legal
9 liability exists is irrelevant. The relevant question is whether FPL intends to
10 remove those assets at the end of their useful lives and the Commission's policies
11 and practices regarding removal of such property.

12 **Q. Mr. Majoros suggests that the Company is collecting funds through cost of**
13 **removal that will never be spent. His implication is that the Company will**
14 **keep those funds. Do you agree?**

15 A. No. I strongly disagree with Mr. Majoros' allegation that the Company could
16 collect money for cost of removal and be able to take it into income simply
17 because there is no legal obligation for FPL to remove the assets. I cannot
18 understand how anyone with integrity who understands rate regulation could
19 believe that a regulated entity could act unilaterally to seize and dispose of funds
20 collected from customers for a specific purpose.

21

22 Even the premise for Mr. Majoros' statement is faulty. If an entity was not rate
23 regulated, they would not be able to accrue cost of removal unless a legal liability
24 existed. If a rate regulated entity was being deregulated, it would be highly

1 unlikely that a commission could fail to ensure that cost of removal dollars were
2 not restricted.

3 Q. **What are the Commission's policies and practices regarding the cost of**
4 **removal of assets at the end of their useful lives?**

5 A. In accordance with Commission Rule 25-6.0436, Depreciation, FPL accrues the
6 original cost of the assets and the estimated net salvage cost for each asset over
7 its useful life. This method of accounting for cost of removal matches the costs
8 with the revenues and charges paid by the customers benefiting from the
9 consumption of the asset. The National Association of Regulatory
10 Commissioners endorses the accrual method as described in their Public Utility
11 Depreciation Practices, page 18:

12 "Net salvage is expressed as a percentage of plant retired
13 by dividing the dollars of net salvage by the dollars of
14 original cost of plant retired. The goal of accounting for
15 net salvage is to allocate the net cost of an asset to
16 accounting periods, making due allowance for the net
17 salvage, positive or negative, that will be obtained when
18 the asset is retired. This concept carries with it the premise
19 that property ownership includes the responsibility for the
20 property's ultimate abandonment or removal. Hence, if
21 current users benefit from its use, they should pay their pro
22 rata share of the costs involved in the abandonment or
23 removal of the property and also receive their pro rata
24 share of the benefits of the proceeds realized."

1 **Q. Does FPL remove assets when it retires them even though they do not have a**
2 **legal obligation to do so?**
3 A. Yes. FPL continually replaces poles, conductors, and other equipment and
4 removes old poles, conductors and equipment when it does. In fact, there have
5 been instances where FPL did not immediately remove the existing facilities and
6 has been cited by the Commission and instructed to remove the facilities.
7 **Q. Mr. Majoros asserts that FPL's cost of removal included in depreciation**
8 **rates is overstated. Do you agree?**
9 A. No. This assertion is based on Mr. Majoros' alternative ways to determine cost of
10 removal which are refuted by Mr. Stout in his testimony and by me later in my
11 rebuttal testimony.
12 **Q. Mr. Majoros discusses three alternative ways to determine the annual**
13 **provision for cost of removal: the Expensing Method, the Normalized Net**
14 **Salvage Allowance Method and the Net Present Value Method. Do you agree**
15 **with any of these methods?**
16 A. No. Mr. Stout discusses a number of concerns he has with these approaches and
17 recommends that all of them be rejected. I agree with Mr. Stout and have a few
18 additional observations I would like to make.
19
20 Both the Expensing Method and the Normalized Net Salvage Allowance Method
21 look to actual retirements and ignore any cost of removal associated with plant
22 that is still in service. As such, they leave the cost of removal on remaining plant
23 in service to be paid by future customers who derived no benefit from them.
24

1 Mr. Majoros' description of the Net Present Value Method fails to point out that
2 whenever a cost is discounted, the resulting discount must then be accreted,
3 increasing future accruals. The accretion together with future increases in the
4 actual cost of removal would result either in significant increases in the accrual in
5 future years, or the accumulated amounts of the accrual will turn out to be
6 inadequate to cover the actual cost of removal.

7 **Q. Is Mr. Majoros' assertion that the cost of removal should match what**
8 **actually occurs on a yearly basis correct?**

9 A. No. Mr. Majoros' assertion that the Company is accruing more removal cost than
10 is being incurred each year ***is a thinly veiled attempt by OPC to steer the***
11 ***Company and the Commission once again to cash basis accounting.*** The cost
12 of removal percentage included in the depreciation rates is designed to recover
13 the removal costs associated with the surviving plant investment over a ratable
14 period of time (i.e., the average remaining life), not just to recover what removal
15 costs actually occurred on an annual basis. Mr. Majoros would have today's
16 customer pay for only what retires today, leaving future customers to pay the
17 removal costs of equipment from which current customers are receiving a
18 benefit.

19 **Q. Mr. Majoros asserts that where old items of property are removed and new**
20 **items of property are installed, FPL could allocate 100% of the costs it**
21 **incurs in removing old items of plant in service to the new items of plant in**
22 **service. Do you agree?**

23 A. No. Either Mr. Majoros is not familiar with the FERC rules or he has little regard
24 for them. Mr. Stout addresses these rules in his testimony. In addition, the

1 purposeful misallocation of costs as advocated by Mr. Majoros would result in a
2 clear misstatement of gross plant with potentially significant ramifications under
3 the Sarbanes-Oxley Act of 2002.
4
5 **Dismantlement Costs on New Plants**

6 Q. **Mr. Larkin is recommending that the Commission exclude the Company**
7 **adjustment for the accumulated provision and dismantling costs for Ft.**
8 **Myers Unit No. 3 which went into service after 2001 and Martin Unit No. 8**
9 **and Manatee Unit 3 which went into service in June 2005. He contends that**
10 **since each of these plants have or will be placed in service after the period**
11 **used in FPL's last dismantlement study and that an adjustment downward**
12 **in total depreciation expense and dismantlement cost is justified, these**
13 **should be removed. Do you agree?**

14 A. No. The plants Mr. Larkin mentions above are producing power and providing
15 service to customers. Since they are generating revenues which are included in
16 our base rate request, it is only appropriate to include the expenses related to
17 running the plants in base rates as well. The dismantlement accruals requested for
18 these units by FPL are based on accruals for similar units that are supported by
19 detailed dismantlement studies which have been approved by the Commission.
20 FPSC Order No. PSC-04-0086-PAA-EI approved the current dismantlement
21 accrual for FPL's fossil and other production plants, including the units (Sanford
22 Unit 4 and Martin Units 8A and 8B) whose accruals serve as proxies for the
23 estimated accrual of $880,000 for the new units at Fort Myers, Manatee and
24 Martin. They are reasonable estimates. The Commission should not deny FPL

1 recovery of a valid cost. Additionally, failure to begin accruing dismantlement
2 costs will create a deficiency in the dismantlement reserve that will have to be
3 recovered at a later time.
4
5 **FPSC Staff Audit Reports**

6 **Q. Have you read the testimony of Staff witness Ms. Welch, dated July 8, 2005?**
7 A. Yes. For the purposes of my comments I will refer to two exhibits in Ms.
8 Welch's testimony: Exhibit KLW-2, the Audit Report and Exhibit KLW-3, the
9 Supplemental Audit Report.
10 **Q. What time period was covered by the audit that is discussed in the two audit**
11 **reports?**
12 A. The audit applied only to historic 2004 results. Attached as my Document KMD-
13 16 is FPL's response to the Audit Report and Supplemental Audit Report as filed
14 in this docket.
15 **Q. Did the auditors suggest that FPL's 2006 test year be reviewed to determine**
16 **whether any of the adjustments recommended in the audit for 2004 would**
17 **also apply to 2006?**
18 A. Yes.
19 **Q. Has FPL reviewed the 2006 test year results to determine if any such**
20 **adjustments need to be made?**
21 A. Yes. FPL has confirmed that only Supplemental Audit Exception No. 1, Item 3
22 and Supplemental Audit Exception No. 3 (includes Audit Exception No. 2)
23 applies to 2006. FPL identifies the effect of these exceptions on my Document
24 KMD-17.

1 **Q. Please explain the effect of these exceptions.**

2 A. The Affiliate Management Fee (AMF) charged to affiliates by FPL was increased
3 by $2,261,927 which corrected the treatment of FPLE-OSI and Seabrook-OSI
4 (Supplemental Audit Exception No. 1, Item 3). The AMF was also increased by
5 $981,721 to correct for the budget activities that should have been included in the
6 AMF (Supplemental Audit Exception No. 3).
7
8 In addition, my Document KMD-17 describes two other necessary corrections to
9 the AMF found during our subsequent review. The total effect of these items is
10 $3,454,534.
11
12 **Affiliate Transactions**

13 **Q. Ms. Dismukes raises several points criticizing some of FPL's cost allocations**
14 **and transactions with respect to its affiliates. Do you have any general**
15 **comments about Ms. Dismukes' criticisms?**

16 A. Yes. FPL is committed to ensuring that its affiliate transactions and related cost
17 allocations are correct, reasonable and comply fully with Commission policy
18 including all applicable laws and regulations. My testimony explains why the
19 Commission and our customers should have confidence that costs are properly
20 allocated among FPL and its affiliates, consistent with the Commission's
21 regulations and sound accounting practices.
22
23 Ms. Dismukes' criticisms begin by imputing improper motivations to FPL
24 concerning its incentives to comply with regulations. She goes on to make

1 recommendations which are factually incorrect, contrary to sound principles of
2 affiliate cost allocation, and seek to arbitrarily shift and disallow properly
3 allocated costs. Ms. Dismukes' testimony also overlooks the benefits to FPL
4 customers of FPL's affiliate relationships.
5
6 Ms. Dismukes' testimony falsely accuses FPL of failing to comply with a
7 regulatory rule, recommending a punitive $25 million ratebase disallowance
8 relating to the purchase of a turbine. This accusation, which is based on a
9 misreading of the Commission's regulations, lacks factual basis and should be
10 rejected. It also demonstrates a disturbingly cavalier approach for someone
11 making such a serious accusation.
12 Q. **Please describe FPL's overall approach to ensuring that affiliate**
13 **transactions and related cost allocations are correct, reasonable and comply**
14 **fully with Commission policy.**
15 A. FPL uses three primary accounting concepts, each of which is carefully aligned
16 with the Commission's requirements for correct affiliate cost allocations:
17 - Costs of resources used exclusively to provide service for the benefit of
18 one company are directly charged to that company. For example, FPL had
19 $27,221,684 of direct charges in 2004 (projected 2006 - $26,397,520);
20 - Where distinct cost "drivers" exist, the cost of resources used jointly to
21 support utility and affiliate operations are allocated using specific factors.
22 The drivers are carefully selected in order to best and most fairly allocate
23 costs. Examples of commonly used drivers include megawatts (MW) of
24 capacity, headcount and number of personal computers. In 2004, FPL

1 allocated to FPLE or its affiliates $1,682,810 through its Nuclear
2 Management Fee (projected 2006 - $2,425,669); $3,299,654 through its
3 Energy, Marketing and Trading Management Fee (projected 2006 -
4 $3,631,050); $3,742,722 through its Power Generation Management Fee
5 (projected 2006 - $3,004,020, which reflects a 2005 transfer of 10
6 employees to FPLE, previously included in the management fee); and
7 $668,939 through its Integrated Supply Chain Management Fees
8 (projected 2006 - $717,848).

9 • Corporate staff infrastructure and governance costs that benefit affiliates
10 and which do not have specific drivers are allocated using the
11 Massachusetts Formula, a methodology widely accepted as a fair and
12 reasonable way to allocate common costs among affiliates. The results of
13 application of the Massachusetts Formula, the Human Resource drivers
14 and the Information Management drivers are included in the Affiliate
15 Management Fee. During 2004, $17,346,303 was allocated to affiliates
16 through the Affiliate Management Fee (projected 2006 - $22,254,534).

17 **Q. Please explain how FPL implements these accounting concepts, through its**
18 **business practices, to ensure correct affiliate cost allocations.**

19 A. Each of the accounting concepts is implemented in a systematic way using the
20 most reliable and accurate business information reasonably available to the
21 Company. Our commitment to proper cost allocation is embodied in written
22 corporate policies, as well as practices and procedures, which are a daily part of
23 our business lives and are built into our information management and cost
24 accounting systems. These policies, practices and procedures are rigorously

1 carried out with attentive management supervision in order to ensure appropriate
2 affiliate cost allocations, and that all of the affiliated transaction regulations and
3 policies of the Commission are consistently carried out.

4 Q. **Ms. Dismukes starts her discussion of affiliate matters by saying that**
5 **"whether or not FPL explicitly establishes a methodology for the allocation**
6 **and distribution of affiliate costs, there is an incentive to misallocate or shift**
7 **costs to regulated companies so that the unregulated companies can reap the**
8 **benefits." Do you agree?**

9 A. No. Ms. Dismukes is engaging in abstract economic theorizing and ignores the
10 realities of the incentives guiding FPL's affiliate relations. FPL is a regulated
11 company providing public utility service to millions of customers. We are subject
12 to the close oversight and scrutiny of the Commission and numerous other
13 governmental and regulatory bodies at the federal, state and local levels. Our
14 incentive is to ensure that at all times we are in full compliance with applicable
15 laws, regulations and Commission policies, including those dealing with affiliate
16 transactions and cost allocation. This is not only the right thing to do, and the
17 legally proper thing to do, it is good business practice.
18
19 FPL works hard to earn the trust of its customers and regulators. Good affiliate
20 cost allocation practices are part of earning and keeping that trust. In order to
21 achieve those good practices, FPL commits a large amount of time and other
22 resources to ensuring that costs are appropriately allocated among affiliates.

1 **Q. Please describe the Company's policies concerning integrity, compliance**
2 **with laws and regulations, record keeping, and information provided to**
3 **regulators.**
4 A. All employees of FPL and its affiliates are subject to the Company's Code of
5 Business Conduct and Ethics (the "FPL Code"). The FPL Code in relevant part
6 requires all representatives of the Company and its affiliates to: (i) act in
7 accordance with the highest standards of personal and professional integrity and
8 to comply with all applicable laws, regulations and Company policies; (ii)
9 maintain all records accurately and completely; and (iii) ensure that the
10 information provided to regulators is accurate and not misleading. All employees
11 of FPL and its affiliates are required to review and commit to abide by the FPL
12 Code.
13 **Q. Is FPL subject to reporting requirements with respect to its affiliate**
14 **transactions?**
15 A. Yes. FPL's affiliate reporting provides a high degree of transparency concerning
16 all of its dealings with its affiliates. FPL complies with strict affiliate accounting
17 and reporting requirements mandated by the Commission.
18 **Q. Will you describe some of the Commission's affiliate reporting**
19 **requirements?**
20 A. Yes. These reports include, but are not limited to, the Commission's requirement
21 that FPL file a detailed and comprehensive Diversification Report each year
22 providing extensive information concerning FPL and its affiliate relationships.
23

1 Matters reported to the Commission in the Diversification Report include: (i) a
2 statement of any changes in corporate structure, including partnerships, minority
3 interests and joint ventures, including an updated organizational chart; (ii) a
4 detailed analysis of diversification activity which reports each new or amended
5 contract or other business arrangement with affiliate companies for the purchase,
6 lease or sale of land, goods or services (excluding tariffed items) (report includes
7 terms, price, quantity, amount and duration of the contracts); (iii) a schedule of
8 transaction-specific data concerning all affiliate transactions in excess of
9 $500,000; (iv) a summary of affiliate transfers, and cost allocations, for each
10 transaction with affiliates exceeding the very low threshold of $300; (v) a
11 summary of all affiliated transactions involving asset transfers or the right to use
12 assets; and (vi) a position-by-position listing of every employee earning more
13 than $30,000 annually who is transferred between FPL and an affiliate company.
14 **Q. Do you have personal knowledge of FPL's preparation of the annual**
15 **Diversification Report?**
16 A. Yes. The Diversification Report is prepared under my direction, and I personally
17 certify to the Commission in each such report that the information contained in
18 the report is true to the best of my knowledge, information and belief.
19 **Q. Ms. Dismukes, referring to Schedule 1 attached to her testimony, states that**
20 **several affiliates owned by FPL Group, Inc. are not allocated any costs from**
21 **FPL or FPL Group, and asserts that this is a "problem." Do you agree?**
22 A. No. FPL's affiliate cost allocations reflect correct application of the three basic
23 cost allocation principles discussed above. No "problem," as Ms. Dismukes puts
24 it, exists. FPL and its major affiliates -- which are operating companies with

1 many employees, substantial revenues and/or property, plant and equipment --
2 bear most of the costs. This flows logically from application of the three affiliate
3 accounting principles. Just as logically, some of FPL's affiliates which are non-
4 operating and have few or no employees, little or no revenues and little or no
5 property, plant and equipment, are allocated few and sometimes no costs.

6 Q. **Please provide some examples of "no cost" affiliates from those listed on**
7 **Schedule 1 to Ms. Dismukes' testimony.**

8 A. FPL Group Trust I and II, FPL Group Capital Trust II and III, and FPL Group
9 Holdings 1, Inc. and 2 Inc. shown on Ms. Dismukes' Schedule 1 were created
10 with the intention of holding assets or conducting business, but were never used.
11 Several of the companies shown on Ms. Dismukes' Schedule 1 do no more than
12 hold certain financial instruments. FPL's Delaware investment companies are
13 examples. The basic cost allocation principles I have discussed in my testimony
14 have been applied to these and all other FPL affiliates. Where, as with the
15 Delaware investment companies, affiliates do not incur or cause costs to be
16 incurred, no costs are allocated to those entities. Document KMD-18 attached to
17 my rebuttal testimony shows all companies including those not receiving costs,
18 and the reasons why this is proper.
19
20 Several of the companies shown on Ms. Dismukes' Schedule 1 were established
21 to explore opportunities in liquefied natural gas. FPL Group Resources, LLC is
22 one of those companies and Ms. Dismukes specifically takes exception to its
23 exclusion from the allocation process. However, she acknowledges that FPL
24 Group Resources "...does not have any revenues or property, plant and

1 equipment...and currently it has six employees." Clearly, FPL Group Resources
2 would have no impact if included in the allocation process under the
3 Massachusetts Formula or any other method. However, any support provided by
4 FPL to FPL Group Resources is directly charged together with associated
5 administrative and general expenses (as well as pension, welfare, insurance and
6 payroll taxes), which are included in the intercompany billings.

7 **Q. Please comment on FPL's cost allocation treatment for the FPLE**
8 **subsidiaries shown on Ms. Dismukes' Schedule 1.**

9 A. The cost allocations and affiliate management fee for all of the FPLE subsidiaries
10 shown on Ms. Dismukes' Schedule 1 are included in the allocation to their parent
11 company (FPLE). Accordingly, her assertion that FPLE subsidiaries are not
12 allocated costs properly is incorrect.

13 **Q. Ms. Dismukes criticizes FPL's determination of cost allocation factors,**
14 **claiming that (i) using the Massachusetts Formula means that the allocation**
15 **factors are "largely size based"; (ii) some allocation factors are allegedly**
16 **"stale"; and (iii) FPL was "unable to provide the amount of costs charged to**
17 **FPL from FPL Group for the projected test year". First, please respond to**
18 **Ms. Dismukes' criticism that FPL's allocation factors are "largely size**
19 **based." Do you agree with her criticism?**

20 A. No. First, Ms. Dismukes fails to mention that companies across the industry use
21 sized-based allocations such as assets, employees and/or number of customers.
22 Therefore, Ms. Dismukes' complaint amounts to an indirect attack on FPL's use
23 of the Massachusetts Formula. Her attack is unwarranted and unfounded. The
24 Massachusetts Formula is a widely-accepted methodology for allocating

1 common costs, which is generally recognized as resulting in fair allocations. The
2 Commission's Staff has reviewed FPL's Massachusetts Formula calculations
3 during recent regulatory audit activities and has never objected to its use. FPL's
4 Cost Allocation Manual, which describes the Affiliate Management Fee and the
5 Massachusetts Formula, is on file with the Commission.
6
7 The Massachusetts Formula is accepted by the FERC, and has been used for
8 many years for electric and other utility affiliate cost allocation matters. In fact,
9 the factors used in this methodology are commonly accepted as a fair way to
10 allocate costs. Therefore, they are also used in a number of non-utility
11 applications, including apportionment of federal income taxes by states for multi-
12 state business operations.
13
14 As a further example of this methodology, the Cost Accounting Standards
15 contained in the Federal Acquisition Regulation, Section 9904.403-50 (attached
16 as Document KMD-19 to my rebuttal testimony) provides that residual expenses,
17 which are of the type FPL allocates through the Massachusetts Formula, are
18 required to be allocated using the three-factor approach contained in the
19 Massachusetts Formula.
20
21 The Massachusetts Formula is widely accepted and regarded for good reason. Its
22 use of a weighted average of assets, revenues and payroll appropriately considers
23 the various factors affecting the use of common services. This is demonstrated by
24 the fact that if a company has only a minimal amount of one factor but more of

1 others, it still receives a significant allocation. In this way, the Massachusetts
2 Formula factors appropriately measure the likely benefit, or lack of benefit, to
3 each affiliate.
4
5 In the face of this broad support and acceptance of the Massachusetts Formula
6 and its clear logical appeal, Ms. Dismukes offers nothing but blanket criticism,
7 suggesting that the methodology should be rejected merely because it is "size
8 based." Her suggestion runs contrary to long-established regulatory and
9 accounting practice, and should be rejected.

10 **Q. Ms. Dismukes compares the allocations resulting from the Massachusetts**
11 **Formula with a single-factor "costs per employee" factor. Is this a useful**
12 **comparison?**

13 A. No. Ms. Dismukes suggests this alternative but makes no recommendations
14 based on it. Her reticence is easy to understand: Ms. Dismukes' "costs per
15 employee" factor disregards (i) the property, plant and equipment of the affiliate;
16 and (ii) the revenues of the affiliate, which are two of the three key factors relied
17 upon by utilities, regulators and others in properly allocating costs for affiliates.
18 It is interesting to note that Ms. Dismukes does not point to a single utility,
19 regulatory commission or other governmental agency that uses a "costs per
20 employee" factor for allocating costs to affiliates.

21 **Q. Please address Ms. Dismukes assertion that for several of the Management**
22 **Fees the allocation factors used during the test year are "stale." Is she**
23 **correct?**

1 A. No. A simple comparison of 2004 factors versus 2006 factors for FPLE indicates
2 significant growth in (1) revenues (30%), (2) property, plant and equipment
3 (24%) and (3) payroll (8%). Using stale factors would not have produced these
4 results. This information was included in data used by Ms. Dismukes.
5
6 FPL's proposed rates are based upon projected 2006 revenues and expenses
7 prepared with the best information available at the time all of the projections
8 were made. The data FPL used for its allocation factors is reasonably
9 representative data. By the very nature of the ratemaking process, as time
10 passes from the time the projection was made, positive and negative variances
11 occur in actual results compared with the projections. Moreover, the actual
12 charges that will be made to affiliates in any year will reflect the actual affiliate
13 transactions that occur in that year.
14
15 The megawatts (MW), revenues, payroll, and property, plant and equipment
16 amounts used by FPL in its computations reflected all of FPL's reasonably
17 expected changes, and for FPLE and its subsidiaries all their confirmed
18 contracted projects at the time the forecasts were prepared. Projected growth for
19 certain recent additions to the portfolio at FPLE during 2004, 2005 and 2006 is
20 not reflected in the factors because at the time of the development of the 2005
21 and 2006 forecasts, some new projects were unknown.
22
23 For example, the GEXA Corp. and Solar Energy Generating System ("SEGS")
24 acquisitions and the construction of the Horse Hollow Wind Energy Center,

1 referred to by Ms. Dismukes, were certainly unknown. It would have been
2 literally impossible to include the investment, revenues and payroll associated
3 with such facilities and companies in the planned 2006 activity. In fact, it will
4 likely take months before this type of information is developed due to the
5 numerous business decisions that have to be made based on various analyses.
6 However, project additions are included in the factors to the extent that the
7 additions are identified and certain, such as construction of the Weatherford
8 Energy Center. In addition, although unidentified as to specific projects, growth
9 in FPLE's MWs was included in the forecast data.
10
11 It would be inappropriate and impractical to include speculative revenues, payroll
12 and MWs from projects which may never come to fruition. Unlike FPL's projects
13 which are primarily need-based and approved by the Commission, FPLE projects
14 are transaction-based and may or may not occur. The same would hold true if
15 FPLE announced that it was selling a project. The factors would not be adjusted
16 until a transaction was completed.
17 **Q. Ms. Dismukes claims that FPL "failed to provide adequate workpapers to**
18 **support some of the allocation factors that it used." Is this correct?**
19 A. No. She is simply wrong. FPL complied fully with the Commission's MFR
20 requirements, and provided information responsive to OPC's and others' data
21 requests concerning affiliate matters and many other issues. FPL's documentation
22 is proper, and her claim should be rejected.

1 **Q. Ms. Dismukes claims that "the inability to separately identify and examine**
2 **the amount of FPL Group costs that are charged to FPL makes it difficult, if**
3 **not impossible, to evaluate the reasonableness of these charges." Do you**
4 **agree?**
5 A. No. FPL's overall approach is to budget 100% of shared costs to FPL in order to
6 provide for control over the budgeting process. From this budget, amounts are
7 allocated to each affiliate based upon the accounting principles, rules and
8 procedures described in my testimony.
9
10 FPL provided a detailed breakdown of the governance cost components (which
11 include FPL and FPL Group costs) with allocation factors for each type of cost in
12 its response to OPC's 10th Request for Production, request number 273. FPL
13 believes that this provides sufficient information for the Commission to
14 determine whether the governance costs are reasonable.
15
16 Moreover, through numerous detailed discovery responses, FPL has thoroughly
17 explained how affiliate transactions are priced. Together, the combination of the
18 data in the referenced MFR and in response to discovery requests provides the
19 Commission with all of the information needed in order to consider and assess
20 the correctness of charges.
21 **Q. Ms. Dismukes asserts that FPL's methodology for allocating the costs**
22 **associated with its executives is incorrect because "more senior executives ...**
23 **are shared than non-senior executives" and that the "presumably higher**
24 **costs" of the senior executives "tends to under-allocate costs to the affiliates**

1 **and over-allocate costs to FPL. Please comment.**

2 A. Cost allocation is the process of assigning a single cost to more than one cost
3 object. The basic goals of cost allocation methods should be to ensure proper
4 distribution of costs and to minimize the time and expense necessary to record
5 and audit transactions. FPL's methodology is a fair, reasonable and
6 administratively workable method of providing for cost allocation. Ms.
7 Dismukes' approach is not reasonably administrable because it would require
8 cost allocation at an individual or near-individual level of detail rather than in a
9 cost pool. It should also be pointed out that, even if FPL had no affiliates, the
10 same corporate governance positions would need to be staffed for FPL, meaning
11 that the substantial allocation of governance costs to affiliates is a clear benefit to
12 customers using any reasonable method of allocation.

13 **Q. Ms. Dismukes claims that due to what she calls "the problems associated**
14 **with the size-based nature of the allocation factor, the fact that several**
15 **affiliates are not allocated any of the management fees, and the problems**
16 **associated with the added projects and acquisitions of FPLE that may not be**
17 **included in the allocation factors," that the Commission should "assign an**
18 **additional 5% allocation factor to this group of non-regulated affiliates." Do**
19 **you agree?**

20 A. No. Ms. Dismukes' claim is contrary to the sound cost accounting principles and
21 data relied upon in FPL's careful and reasonable assignment of costs, and would
22 arbitrarily and unfairly shift costs that have been properly allocated among FPL's
23 affiliates. I have previously responded to her "stale data," "size based formula"
24 and "no-fee subsidiary" claims, and will not repeat those detailed responses here.

1 Her 5% allocation factor is plucked from the air, with no analytical basis
2 provided whatsoever. Moreover, she fails to point to a single utility, Commission
3 or any other entity that has ever adopted such a speculative and arbitrary factor.
4 This arbitrary 5% penalty ($6 million) represents 41.2% of the $14 million AMF
5 adjustment Ms. Dismukes proposes in her Schedule 5 and should be rejected.
6 Q. **Ms. Dismukes claims that the allocation of the affiliate management fee**
7 **should be changed because (i) administrative and general services provided**
8 **by FPL and FPL Group are "extremely valuable to the affiliates"; (ii)**
9 **"within the AMF there are several accounts which FPL claims do not benefit**
10 **certain segments of FPLE"; and (iii) the "allocation factors used to**
11 **distribute costs for the Human Resource department and Information**
12 **Management are outdated and not supported by source documentation."**
13 **Based upon these assertions she claims that changes should be made to**
14 **FPL's proposed cost allocations. Do you agree that administrative and**
15 **general services are valuable to the affiliates and therefore the allocations to**
16 **affiliates should be changed?**
17 A. No. Ms. Dismukes claims that FPL's affiliates should pay more than their
18 allocation of the cost of administrative and general services because the services
19 are "valuable to the affiliates." Her point is an illogical non-sequitur. All agree
20 that administrative and general services have value to affiliates. However, the
21 correct question is whether the affiliates have been allocated the proper amount
22 of costs of the services that they use, under applicable regulations and cost
23 allocation principles. FPL has provided for and charged such proper costs.
24 Accordingly, there is no basis under cost allocation principles or regulations for

1 allocating extra costs to affiliates above and beyond their properly allocated
2 costs. The services affiliates use are already charged to them and no additional
3 charges should be allocated due to the fact that the services they obtain are
4 useful.
5
6 Ms. Dismukes assumes that the level of administrative and general expenses
7 would be the same for affiliates as it is for the utility. This is not so. Because of
8 FPL's size and other factors, its infrastructure is much greater than what would be
9 needed by the affiliates. Contrary to Ms. Dismukes claims, FPL's customers are
10 benefited, not burdened, by the affiliates. Even Ms. Dismukes' Schedule 4, after
11 correcting for her error of using $18,000,000 instead of $18,800,000 for the
12 amount "Allocated to Affiliates," shows that 12.8% of the administrative and
13 general services are borne by affiliates in 2006. Her schedule would actually
14 indicate that the percentage allocated to affiliates is growing (i.e., 2004 – 11.8%
15 and 2005 – 12.3%). My Document KMD-17 would indicate that the composite
16 percentage allocated to affiliates for 2006 is 14.3%. Interestingly, included in that
17 composite rate are costs allocated to affiliates at 20.7% (results of the
18 Massachusetts Formula).
19 **Q. Should the AMF be changed because FPL does not allocate certain activities**
20 **to one or more affiliates?**
21 A. No. There are sound reasons for FPL's treatment of certain activities. FPLE, for
22 example, has its own accounts payable department. They do not use FPL's
23 department in this area and therefore do not cause any costs to FPL in this
24 respect. Nor does FPLE benefit in any way from FPL's expenditures in this area.

1 Accordingly, FPL's exclusion of such costs from fees due from FPLE is based
2 upon solid business facts.
3
4 Likewise, only FPL and FPLE use and benefit from FPL's environmental services
5 and natural resources business functions. Other affiliates do not use or rely upon
6 these functions. Another example is FPL's community relations programs
7 focused on educating communities in FPL's service territory (i.e. school energy
8 and electrical safety awareness programs). Such costs only benefit FPL and not
9 FPLE, and such costs are not allocated to FPLE.
10
11 It is this kind of detailed understanding and assessment of the functions and
12 activities of FPL and its affiliates, applied using a careful and systematic method,
13 which is the basis for FPL's decisions to include or exclude from cost allocation
14 specific charges of the kind complained of by Ms. Dismukes. Her suggestion that
15 FPL arbitrarily includes or excludes costs between affiliates, or that FPL's
16 allocations are illogical, is incorrect and should be rejected as well as the
17 $139,727 adjustment in her Schedule 5.
18 **Q. Should the AMF be changed due to the allocation factors FPL used to**
19 **allocate its Human Resources and Information Management costs?**
20 A. No. Information used by FPL in its allocation factors relating to Human
21 Resources and Information Management represented the latest and most reliable
22 information available at the time of its preparation of the filing. There were and
23 are no compelling reasons to believe that the percentages would materially
24 change since the time the forecasts were prepared. It would be incorrect to base

1 allocations and percentages based on speculation as to future affiliate growth, or
2 affiliate divestiture for that matter, rather than the best available actual data of the
3 Company.
4
5 Accordingly, Ms. Dismukes' suggestion that the allocation factors used to
6 distribute costs for Human Resources and Information Management are
7 "outdated and not supported by source documentation," that an alternative
8 "composite allocation factor" mixing the Massachusetts Formula with other
9 weightings, and that the AMF charges to the affiliates in the projected year 2006
10 should be increased by $5,666,219 are unfounded and should be rejected.
11
12 Ms. Dismukes spends a substantial amount of time in her testimony arguing that
13 the Massachusetts Formula is inappropriate. Then, in order to recommend an
14 increase in the allocations to affiliates, she factors in the results of the
15 Massachusetts Formula, which yields the single largest allocation percentage to
16 affiliates. Her recommendation fails to reflect the fact that affiliates have
17 proportionally fewer employees than FPL. This notion alone represents
18 approximately 40% of the $14 million adjustment recommended by Ms.
19 Dismukes. This recommendation is unfounded and should be rejected.
20 **Q. Do you have any additional comments regarding Ms. Dismuke's proposed**
21 **changes to the AMF?**
22 A. Yes. Ms. Dismukes carelessly proposes adjustments to FPL's property, plant and
23 equipment and payroll used in the Massachusetts Formula based on other OPC
24 witnesses' testimony. Adjustments proposed by those witnesses have absolutely

1 nothing to do with proper allocation of costs. For example, OPC witness Larkin
2 recommends that the Commission disallow approximately $523 million of CWIP
3 in rate base because he claims it is not needed to maintain FPL's financial
4 integrity. Mr. Larkin is not challenging the prudence of the CWIP. This is $523
5 million FPL will expend on capital additions and it is appropriately reflected in
6 FPL's property, plant and equipment in the Massachusetts Formula regardless of
7 how FPL earns a return on the CWIP. However, Ms. Dismukes totally disregards
8 the principles of proper allocation and proposes a regulatory adjustment in her
9 allocation methodology that would remove $523 million from the numerator of
10 FPL. It is this type of illogical reasoning, together with the concerns I have
11 addressed above, that should convince the Commission to reject Ms. Dismukes'
12 proposed $14 million adjustment to the AMF. My Document KMD-17 reflects all
13 appropriate adjustments to the AMF and therefore Ms. Dismukes' Schedule 5
14 should be rejected in total.

15 **Q. You stated that Ms. Dismukes' testimony overlooks real and tangible**
16 **financial benefits to customers arising from FPL's affiliate relationships.**
17 **Please describe some of these benefits.**

18 A. Ms. Dismukes fails to point out that the Commission's affiliate rules are intended
19 to protect utility customers and therefore, by design, FPL's non-regulated
20 affiliates are often charged more than the incremental cost FPL would pay for
21 certain services. This can be seen by considering the benefits to customers of
22 affiliate billings for certain specific services. One such service is for Operations
23 and Mainframe Software maintenance. It costs FPL approximately $10 million
24 for this support. Through FPL's Affiliate Management Fee, FPL charges

1 affiliates approximately $1 million of the Operations and Mainframe Software
2 expenses, effectively reducing the cost to FPL to $9 million. If the affiliates did
3 not exist, FPL would still incur $9.7 million in costs, thereby increasing costs to
4 FPL customers by $700,000. This is only one example of how FPL customers
5 benefit from its affiliates.
6
7 Another example is that if FPL Group's only subsidiary was FPL, the full cost of
8 the investor relations program (including the cost of the annual report) would be
9 borne by FPL customers. Instead, FPL Group's other subsidiaries are allocated
10 approximately 20% of the costs. I strongly urge the Commission to consider fully
11 the benefits of FPL's affiliates and not to be misguided by isolated
12 unsubstantiated representations.
13 Q. **Ms. Dismukes claims that FiberNet charges to FPL should be reduced by**
14 **$1,343,816. Do you agree?**
15 A. No. Ms. Dismukes is incorrect in suggesting a reduction to the charges for the
16 2006 test year of $1,343,816 related to fiber services provided by FiberNet. First,
17 her cost of capital is based on her reliance on Dr. Woolridge's recommended pre-
18 tax overall cost of capital of 8.56% which is based on costs and a capital
19 structure for a regulated electric utility and applying that to a telecommunications
20 company which has a completely different risk profile. Dr. Avera addresses the
21 appropriate cost of capital in his rebuttal testimony filed in this docket.
22
23 Ms. Dismukes ignores the benefit the relationship with FiberNet provides to FPL
24 and its customers. FPL relies on FiberNet's dedicated fiber service to run its

1 systems such as Supervisory Control and Data Acquisition (SCADA), internal
2 voice and data networks, and nightly back ups of all the servers to the redundant
3 computer centers in Juno Beach and the General Offices. Additionally, FiberNet
4 allows outflow (interflow) calling between the two call centers via tielines,
5 allows care center personnel access to outbound toll access (ITN) at a lower cost
6 and FiberNet provides dedicated personnel services. Furthermore, if FPL were to
7 transfer these services to another provider it would be very expensive and the
8 current dedicated service to FPL might suffer. This would not be in the best
9 interest of our customers and therefore Ms. Dismukes adjustment should be
10 rejected in its entirety.

11 Q. **Ms. Dismukes claims that $2,746,000 in revenue should be attributed to FPL**
12 **with respect to unregulated gas margin revenues. Do you agree?**

13 A. No. As discussed in Mr. Brandt's testimony, the correct net revenues for natural
14 gas are $1,734,000. As Mr. Brandt addresses, this is a business that originated in
15 FPLES. FPLES has been transferring net revenues to FPL and will continue to do
16 so through the end of 2005 under the stipulation and settlement agreement. The
17 contracts that were entered into by FPL and are being transferred to FPLES
18 effective January 1, 2006 have been valued and FPL is proposing to amortize this
19 amount of $835,318 over a five year period as is shown in my Document KMD-
20 10 as an Identified Adjustment.

21 Q. **Ms. Dismukes claims that FPL should be credited with revenue of $78,000**
22 **representing "an administrative fee of 10%" representing what she says is**
23 **the value of FPL's Energy Marketing and Trading (EMT) department**
24 **setting up over-the-counter swaps on behalf of FPLES. Do you agree with**

1 **her claim?**

2 A. No. I do not. There is no logic in Ms. Dismukes' conclusion. The settlement
3 results of financial instruments are driven by markets and have no correlation
4 with costs at EMT. However, EMT direct charges fully loaded payroll and other
5 costs to FPLES when any EMT employee from the front office, risk management
6 or accounting works on a FPLES transaction. The direct charges to FPLES are
7 reflected as credits to FPL's expense accounts. In addition, the volume of
8 transactions is small (FPL executed 55 trades for FPLES in 2003, 27 trades in
9 2004, and 11 trades for the first six months of 2005).

10 **Q. Ms. Dismukes asserts that FPL did not properly allocate expenses to FPL's**
11 **New England Division (FPL-NED), and recommends a $2,571,061 reduction**
12 **in test year expenses. Do you agree?**

13 A. No. Ms. Dismukes adjustment is incorrect. FPL-NED was budgeted as a separate
14 entity and was not included as an allocated portion of the FPL budget. All
15 applicable costs of FPL-NED were considered in the 2006 budget forecast but
16 were not presented by FERC account for budget purposes. These expenses were
17 treated as a one-line item of $6.905 million charged to FERC account 562,
18 Station Expense. Because FPL-NED receives a zero jurisdictional separation
19 factor, FPL-NED is not included in the revenue requirements for this proceeding
20 in any way. The detailed O&M expenses applicable to FPL-NED in my
21 Document KMD-20 shows a breakdown of all costs which were accounted for
22 separately for both budget and MFR purposes. Thus, the allocation process on
23 Ms. Dismukes Schedule 15 resulting in an adjustment of $2,571,061 is both
24 arbitrary and unnecessary and should be rejected.

1 **Q. Ms. Dismukes claims that FPL violated the Commission's affiliate**
2 **transaction rules concerning its purchase of a turbine and that FPL's plant**
3 **in service should therefore be reduced by $25,088,783. Do you agree?**
4 A. No. FPL complied with all applicable regulations, procured the subject turbine
5 for utility purposes using reasonable business practices, and the subject turbine is
6 vitally necessary for FPL to have readily available in order to permit FPL to
7 swiftly repair any one of the other six sibling turbines that FPL needs and relies
8 upon in providing service to customers. FPL witness, William L. Yeager,
9 provides detailed information on the turbine in his rebuttal testimony.
10
11 Ms. Dismukes relies on an inapplicable section of the Commission's regulations
12 as the basis for her regulatory violation claim. Citing Commission Rule 25-
13 6.1351, she claims that "an independent appraiser must verify the market value
14 of assets transferred with a net book value greater than $1,000,000." She claims
15 that, because FPL did not have such an appraisal performed, it is in violation of
16 the Commission's rule.
17
18 However, Ms. Dismukes has misread the Commission's regulations. There is no
19 requirement for an independent appraisal in the circumstances of FPL's purchase
20 of the turbine. Because the turbine was purchased by FPL from GE, and not
21 transferred by FPL to a non-regulated affiliate, no appraisal requirement applies.
22 It is only where "an asset used in regulated operations is transferred from a utility
23 to a non-regulated affiliate" that an appraisal requirement applies. Rule 25-

1 6.1351(d). Accordingly, Ms. Dismukes' claim for a disallowance should be

2 rejected.

3

4 **Identified Adjustments**

5 Q. **Please describe your Document KMD-10 summarizing adjustments to net**

6 **operating income and rate base.**

7 A. My Document KMD-10 summarizes the adjustments FPL has identified as

8 appropriate during the course of this proceeding. As you can see, the net effect on

9 revenue requirements of these adjustments is only about $7 million,

10 demonstrating the continued integrity of FPL's test year results for rate-setting

11 purposes.

12 Q. **Have you determined the effects of the Commission's decision in FPL's**

13 **petition for storm damage recovery in Docket No. 041291?**

14 A. Yes. My Document KMD-15 shows the effects of the Commission's decision in

15 the above referenced docket.

16 Q. **Does this conclude your testimony?**

17 A. Yes it does.

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
SUMMARY OF 2006 TEST YEAR ADJUSTMENTS

RB or NOI	Item No.	Description	Impact on 2006 Retail Revenue Requirements Increase/(Decrease) ($000)
RB	1	Correction of error in the original forecast of the reserve account for post retirement benefits other than pension (account 228.370) results in a decrease in the working capital liability and a corresponding increase in per book rate base of $39,966,000	$4,782
RB	2	CWIP eligible for a return through the environmental clause was inadvertently not removed from rate base. Removal of this CWIP from rate base results in a decrease in per book rate base of $26,473,000.	($3,134)
RB	3	Correction of error in the original forecast of the nuclear maintenance reserve accounts (accounts 228.410 - .413) results in a decrease in working capital liability and a corresponding increase in the 13 month average rate base of $5,869,000.	$702
RB	4	Correction of error in the original forecast of the Accrued Pension asset reduces per book rate base by $20,416,000.	($2,443)
RB	5	Correction of error in the original forecast of Retiree Medical Account # 143.126 including correction of allocation to non-regulated affiliates identified in the MFR Audit Report, Disclosure #14. Adjustment reduces per book rate base by $4,513,000.	($540)
RB	6	Charitable expenses capitalized in error to the Manatee Combined Cycle project. Adjustment reduces 2006 per book rate base by $35,000.	($5)
NOI	7	Revenues were overstated due to inadvertent double-up of certain thermal scan and power monitoring revenues which were included in both Account 456 Other Electric Revenues, Misc. and in Account 451 Misc. Service Revenues. Adjustment reduces 2006 Misc. Revenues by $332,000.	$330
NOI	8	State deferred income tax expense associated with AFUDC debt was input with the wrong sign in the original interest synchronization calculation. Correction reduces jurisdictional income tax expense by $1,016,000.	($1,644)
NOI	9	Allocation of certain costs with affiliate benefits were not properly allocated to non-regulated entities through the affiliate management fee. Adjustment reduces 2006 O&M expense by $3,454,000.	($3,418)
NOI	10	ECRC O&M expenses were inadvertently included in base O&M expenses. Adjustment reduces 2006 O&M expenses by $560,000.	($553)
NOI	11	The adjustment to Miscellaneous Operating Revenues represents the amortization of a transfer of assets to an affiliate. The adjustment reduces Misc. Other Operating revenues in 2006 by $167,000.	$166
NOI	12	Operating revenues associated with the bill statement advertising program was understated in error in the forecast. Adjustment reduces Misc. Other Operating revenues in 2006 by $1,012,000.	($1,007)
NOI	13	NOI Multiplier - should be adjusted for the tax impact of the American Jobs Creation Act of 2004	($325)

TOTAL ADJUSTMENT IMPACT - NET INCREASE IN REVENUE REQUIREMENTS	($7,089)

1 BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION
TALLAHASSEE, FLORIDA
2
3
4 IN RE: Proposed revisions to Rule 25-6.0141, F.A.C.,
Allowance for Funds Used During Construction
5 (AFUDC). (Deferred from the April 30, 1996
Commission conference.)
6
DOCKET NO. 951535-EI
7
8
9
10
BEFORE: CHAIRMAN SUSAN F. CLARK
11 COMMISSIONER J. TERRY DEASON
COMMISSIONER JULIA L. JOHNSON
12 COMMISSIONER DIANE K. KIESLING
COMMISSIONER JOE GARCIA
13
PROCEEDING: AGENDA CONFERENCE
14
ITEM NUMBER: 4**
15
DATE: Tuesday, June 11, 1996
16
PLACE: 4075 Esplanade Way, Room 148
17 Tallahassee, Florida
18 REPORTED BY: JANE FAUROT, RPR
Notary Public in and for the
19 State of Florida at Large
20
21
JANE FAUROT, RPR
22 P.O. BOX 10751
TALLAHASSEE, FLORIDA 32302
23 (904) 379-8669
24
25

1 sense, I think that our rule is stricter than what is
2 in the generally accepted accounting world. So I don't
3 think that we are -- I don't think we are far-afield,
4 personally
5 COMMISSIONER JOHNSON: Okay.
6 CHAIRMAN CLARK: Do I understand the
7 recommendation on the rule that's under the primary
8 recommendation that allows -- even if we set a
9 materiality threshold, that if a company wants to
10 include it in rate base they can petition to do that?
11 MS. SALAK: The way the rule will work, if it is
12 under the half percent?
13 CHAIRMAN CLARK: Yes.
14 MS. SALAK: Then that will go into rate base.
15 It's not a petition, but if they want -- if it is over
16 a half a percent -- under half a percent, if a company
17 like Gulf wants to accrue AFUDC -- or not accrue AFUDC
18 at that point, then they can come in and get a waiver
19 and not accrue AFUDC.
20 CHAIRMAN CLARK: Right. Under the rule it would
21 be material for them.
22 MS. SALAK: Yes.
23 CHAIRMAN CLARK: And they would, therefore, accrue
24 AFUDC under the rule.
25 MS. SALAK: At half a percent, they would accrue

1 guidelines and the accounting rules. It's a
2 convenience that there is a Commission here that sets
3 flat amounts, but when we really go to -- if full
4 competition comes to pass and everyone is following
5 generally accepted accounting principles, what you're
6 going to have is a different interpretation of rules in
7 different -- you will not have a flat amount set by
8 anyone. I think this is a step in that direction and
9 that getting them prepared if that should happen, is
10 that they will be facing the real world, real world in
11 the sense of outside accountants. If you talk to a CPA
12 auditor, for example, when they look at their books and
13 records they are not going to say, "Take it off for
14 every dollar in flat amount." They are going to look
15 at materiality and that is the threshold that they use
16 whether or not they pass that on an item or not. And
17 materiality will become more and more important as we
18 transition.
19 CHAIRMAN CLARK: What is the purpose of accruing
20 AFUDC as opposed to putting it in rate base as soon as
21 the money is expended? CWIP, I guess that's CWIP.
22 MS. SALAK: Yes. There is an argument that as a
23 plant is being constructed, that the company should not
24 be --
25 CHAIRMAN CLARK: Recovering those costs from the

1 a rate case. It just means it's still pending a
2 review.
3 COMMISSIONER DEASON: In other words, rates would
4 not be impacted in the short therm by their inclusion
5 of an item in rate base as opposed to accruing AFUDC.
6 If there were a rate proceeding where there would be a
7 rate case or an overearnings investigation, at that
8 point there could be a determination made of the
9 prudency of those dollars. And at that point a
10 determination would be made as to whether ratepayers
11 should continue to pay a return --
12 MS. SALAK: Yes.
13 COMMISSIONER DEASON: -- on all or a portion of
14 those dollars.
15 MS. SALAK: Yes. We did have some additional
16 provisions in the original rule, that one was that if
17 the Commission -- just to clarify, that if the
18 Commission chooses that a project under the 5-l/2
19 percent to each point's threshold should accrue AFUDC
20 as opposed to going straight into rate base, there is a
21 provision that the Commission can choose to do that on
22 a prospective basis. And the second thing we added
23 were reporting requirements for any project that was
24 $10 million. So it would be on a projected basis we
25 would know what projects existed over $10 million so we

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
2006 RECALCULATED NUCLEAR MAINTENANCE RESERVE BALANCES (1)

Line No.		St. Lucie 1 (1)	St. Lucie 2 (2)	Turkey Pt 3 (3)	Turkey Pt 4 (4)	Total (5)	As Reported on MFR B-6 (6)
1							
2	**Actual Balance as of 8/31/2004**	**($7,050,457)**	**($24,392,090)**	**($28,934,073)**	**($18,301,633)**	**($78,678,252)**	**($78,678,252)**
3							
4	Forecasted Outage Accruals	(6,788,834)	(6,530,548)	(6,571,294)	(7,162,298)	(27,052,974)	(27,052,974)
5	Forecasted Outage Reversals (2)	0	30,780,075	32,920,402	0	63,700,477	58,856,070
6	**Forecasted Balance as of 12/31/2004**	**(13,839,291)**	**(142,562)**	**(2,584,965)**	**(25,463,931)**	**(42,030,749)**	**(46,875,156)**
7							
8	Forecasted Outage Accruals (3)	(20,077,684)	(20,250,600)	(18,536,496)	(19,112,033)	(77,976,813)	(77,976,813)
9	Forecasted Outage Reversals (4)	30,783,530	0	0	31,878,000	62,661,530	55,054,934
10	**Forecasted Balance as of 12/31/2005**	**(3,133,445)**	**(20,393,163)**	**(21,121,461)**	**(12,697,963)**	**(57,346,032)**	**(69,797,035)**
11							
12	Forecasted Outage Accruals (3)	(18,631,525)	(21,013,719)	(19,315,225)	(18,224,033)	(77,184,501)	(77,184,501)
13	Forecasted Outage Reversals (4)	0	28,802,668	26,368,000	27,311,324	82,481,992	93,431,587
14	**Forecasted Balance as of 12/31/2006**	**(21,764,970)**	**(12,604,213)**	**(14,068,686)**	**(3,610,672)**	**(52,048,541)**	**(53,549,948)**
15							
16							
17							
18	**13-Month Average as of 12/31/06**	**($12,449,208)**	**($13,040,593)**	**($12,434,349)**	**($15,423,402)**	**($53,347,550)**	**($59,216,537)**
19							
20							
21	**Jurisdictional 13-Month Average as of 12/31/06**					**($53,082,253)**	**($58,922,053)**
22							
23							
24							

25 (1) FPL's nuclear maintenance reserve included in FPL's MFR filing was forecasted incorrectly. The outage costs that
26 should have been reversed out of the reserve at the time of the outage was reversed out at the time the accruals began.
27
28 (2) Forecasted outage reversals used in the recalculation of the 12/31/04 balance tie to FPL's response to Staff's Third Set of
29 Interrogatories, Question No. 93, Attachment 1 page 3, under the Current Actual Data section for the Fall 2004 outages.
30
31 (3) Total forecasted outage accruals used in the recalculation of the 12/31/05 and 12/31/06 balances tie to FPL's response to
32 OPC's First Set of Interrogatories, Question No. 40, Attachment 2, pages 1 and 2.
33
34 (4) Forecasted outage reversals used in the recalculation of the 12/31/05 and 12/31/06 balances tie to FPL's response to Staff's
35 Third Set of Interrogatories, Question No. 93, Attachment 1 pages 1 and 2.

Docket No. 050045-EI
Docket No. 050188-EI
K. Michael Davis, Exhibit No. ___-
Document No. KMD-13, Page 1 of 1
Depreciation Filing Changes Summary

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
ANALYSIS OF CHANGES TO RESERVE AND ACCRUAL
ESTIMATED 12/31/05 PLANT AND RESERVE BALANCES
AS FILED ON JULY 1, 2005
($ millions)

		Increase/(Decrease)		
Line No.	**Description**	**Effect on Reserve Balance**	**Effect on Theoretical Reserve Surplus**	**Change in Expense for 2006 (A), (B)**
1				
2	Unitization of Ft. Myers and Sanford	$ -	$ (50.1)	$ 37.0
3				
4	Retirement Unit Changes:			
5	Steam	-	(11.2)	1.2
6	Nuclear	-	(131.1)	11.0
7	Other Production	-	(1.5)	3.4
8				
9	Allocation of Bottom Line Reserve 100% to Nuclear:			
10	Nuclear Function	(46.5)	(46.5)	4.0
11	Transmission, Distribution and General Plant	46.5	46.5	(1.3)
12				
13	Automated Meter Reading:			
14	Effect of Removing from Depreciable Account	(101.9)	101.9	(2.0)
15	Effect of Establishing Capital Recovery Schedule	101.9	(101.9)	4.6
16				
17				
18	Remaining Life Changes in Transmission, Distribution and General Plant	-	169.2	(6.0)
19				
20	Update Forecast for Plant and Retirement Activity	(47.6)	(21.8)	4.5
21				
22				
23	Adjustments to March Filing:			
24	Adjustment of Reserve Balance for Nuclear Capital Recovery Schedule	(100.0)	(94.0)	1.3
25	Adjustment of Production Plant Reserve for Projected Retirements in 2005	(44.7)	(44.7)	7.0
26				
27	Totals	**$ (192.3)**	**$ (185.2)**	**$ 64.7**
28				
29				
30				

Notes:
(A) Includes depreciation expense related to clauses and transportation.
(B) Revenue Requirements Effect of Depreciation ($000's):

Effect of Depreciation Expense, net of Clause	$65,940
Revenue Requirement Effect of Change in Rate Base	(4,180)
Total Revenue Requirement	$61,760

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
REVENUE REQUIREMENT IMPACT IN YEAR FIVE
(FOUR YEAR FLOWBACK)
($000's)

Line No.		2006	2007	2008	2009	2010
1						
2	Plant additions for Nuclear Plant (A)	$174,215	$443,094	$153,403	$87,387	$0
3						
4	Plant In Service	174,215	617,309	770,712	858,099	858,099
5						
6	Depreciation Expense based on Site Rate	1,572	6,928	12,367	14,498	15,276
7	Depreciation Rate on Nuclear Unit	1.8047%	1.7505%	1.7820%	1.7802%	1.7802%
8	Accumulated Reserve	1,572	8,500	20,867	35,365	50,641
9	Increase in Net Plant In Service	172,643	608,809	749,845	822,734	807,458
10						
11	Increase in Rate Base due To Additions	86,322	347,565	548,705	685,720	746,589
12	Jurisdictional Factor					0.995899
13	Jurisdictional Amount					743,527
14						
15	Amortization of the Theoretical Reserve Surplus over 4 years (B)	333,009	333,009	333,009	333,009	0
16						
17	Decrease in Accumulated Reserve/Reg Liability	333,009	666,018	999,027	1,332,036	1,332,036
18						
19	Increase in Rate Base due to Amortization	166,505	499,514	832,523	1,165,532	1,332,036
20	Jurisdictional Factor					0.991931
21	Jurisdictional Amount					1,321,288
22						
23	Increase in Rate Base	252,826	847,079	1,381,228	1,851,251	2,078,625
24	Jurisdictional Factor					0.993356
25	Jurisdictional Amount					2,064,815
26						
27	Return Requirement on Increased Rate Base (C)					8.2188%
28						169,703
28						
29	Revenue Expansion Factor (per current Filing) (D)					1.59219
31	Revenue Requirement on return on Rate Base Increase					270,199
32						
33	Effect on Revenue Requirements of Completing Amortization of Theoretical Reserve Surplus					330,322
34						
35	Increase in Depreciation Expense					15,213
36	**Total Increase in Revenue Requirement in year Five**					**$615,735**

Notes:
(A) Additions are only reflective of the Nuclear Function additions required to maintain the options for the license extension.
(B) Reflects the amortization of $1.332 billion of the theoretical reserve surplus over a four year period.
(C) Rate of Return based on the thirteen month average capital structure and requested return for the test year. The rate of return does not reflect the change in deferred taxes in the capital structure or the effects of risk associated with future cost rates.
(D) The revenue expansion factor is per the current filing and is adjusted for the Section 199, Manufactures deduction.

Docket No. 050045-EI
Docket No. 050188-EI
K. Michael Davis, Exhibit No. ___-
Document No. KMD-14, Page 2 of 2
Theoretical Reserve Rate Shock

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
REVENUE REQUIREMENT IMPACT IN YEAR ELEVEN
(TEN YEAR FLOWBACK)
($000's)

Line No.		2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
1												
2	Plant additions for Nuclear Plant	$174,215	$443,094	$153,403	$87,387	$0	$0	$0	$0	$0	$0	$0
3												
4	Plant In Service (A)	174,215	617,309	770,712	858,099	858,099	858,099	858,099	858,099	858,099	858,099	858,099
5												
6	Depreciation Expense based on Site Rate	1,572	6,928	12,367	14,498	15,276	15,276	15,276	15,276	15,276	15,276	15,276
7	Depreciation Rate on Nuclear Unit	1.8047%	1.7505%	1.7820%	1.7802%	1.7802%	1.7802%	1.7802%	1.7802%	1.7802%	1.7802%	1.7802%
8	Accumulated Reserve	1,572	8,500	20,867	35,365	50,641	65,917	81,192	96,468	111,744	127,020	142,296
9	Increase in Net Plant In Service	172,643	608,809	749,845	822,734	807,458	792,182	776,907	761,631	746,355	731,079	715,803
10												
11	Increase in Rate Base due To Additions	86,322	347,565	548,705	685,720	746,589	769,386	773,146	767,388	756,872	743,975	729,889
12	Jurisdictional Factor											0.995899
13	Jurisdictional Amount											726,896
14												
15	Amortization of the Theoretical Reserve Surplus over 10 years (B)	133,203	133,203	133,203	133,203	133,203	133,203	133,203	133,203	133,203	133,203	0
16												
17	Decrease in Accumulated Reserve/Reg Liability	133,203	266,406	399,609	532,812	666,015	799,218	932,421	1,065,624	1,198,827	1,332,030	1,332,030
18												
19	Increase in Rate Base due to Amortization	66,602	199,805	333,008	466,211	599,414	732,617	865,820	999,023	1,132,226	1,265,429	1,332,030
20	Jurisdictional Factor											0.991931
21	Jurisdictional Amount											1,321,282
22												
23	Increase in Rate Base	152,923	547,370	881,713	1,151,930	1,346,002	1,502,002	1,638,966	1,766,411	1,889,097	2,009,404	2,061,919
24	Jurisdictional Factor											0.993336
25	Jurisdictional Amount											2,048,178
26												
27	Return Requirement on Increased Rate Base (C)											8.2188%
28												168,336
28												
30	Revenue Expansion Factor (per current Filing) (D)											1.59219
31	Revenue Requirement on return on Rate Base Increase											268,022
32												
33	Effect on Revenue Requirements of Completing Amortization of Theoretical Reserve Surplus											132,128
34												
35	Increase in Depreciation Expense											15,213
36	**Total Increase in Revenue Requirement in year 11**											**$415,364**

Notes:

(A) Additions are only reflective of the Nuclear Function additions required to maintain the options for the license extension.
(B) Reflects the amortization of $1.332 billion of the theoretical reserve surplus over a ten year period.
(C) Rate of Return based on the thirteen month average capital structure and requested return for the test year. The rate of return does not reflect the change in deferred taxes in the capital structure or the effects of risk associated with future cost rates.
(D) The revenue expansion factor is per the current filing and is adjusted for the Section 199, Manufactures deduction.

Docket No. 050045-EI
Docket No. 050188-EI
K. Michael Davis, Exhibit No. ___-
Document No. KMD-15, Page 1 of 1
Rev Reqmt Impact on FPSC Storm
Recovery Docket Decision

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
REVENUE REQUIREMENT IMPACT ON FPSC STORM RECOVERY DOCKET DECISION
(DOCKET NO. 041291-EI)
($000's)

Line No.	Description	2006 Company Per Book Adjustment (1)		Jurisdictional Factor (2)	2006 Jurisdictional Adjustment (3)
1					
2	**RATE BASE (13 Month Average)**				
3					
4	PLANT IN SERVICE	$ 21,680	A	0.994930	$ 21,575
5	ACCUM PROVISION FOR DEPREC/AMORT	47,722	B	0.998356	47,667
6	NET PLANT IN SERVICE	$ 69,402			$ 69,242
7					
8					
9	EFFECT ON REVENUE REQUIREMENTS - INCREASE (DECREASE)				$ 8,326
10					
11					
12	**NET OPERATING INCOME**				
13					
19	DEPRECIATION & AMORTIZATION	$ 866	C	0.994203	$ 861
20	INCOME TAXES (38.575%)	(332)		1.000000	(332)
21	TOTAL OPERATING EXPENSES	$ 534			$ 529
22					
23	TOTAL OPERATING INCOME	$ (534)			$ (529)
24					
25					
26	EFFECT ON REVENUE REQUIREMENTS - INCREASE (DECREASE)				$ 856
27					
28					
29	TOTAL EFFECT ON REVENUE REQUIREMENTS - INCREASE (DECREASE)				$ 9,182
30					

Notes:
(A) Amount directed to be capitalized $58,024 less amount currently capitalized $36,344.
(B) Accumulated depreciation represents the 13 month average for the year end December 31, 2006 and reflects depreciation expense through that date. The amount consists of plant in service retired at an original cost of $36,344 and cost of removal of $12,171 partially offset by 17 months of depreciation expense.
(C) Depreciation is based on the original cost of the new assets less retirements.

STEEL
HECTOR
DAVIS
INTERNATIONAL

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July 1, 2005

- VIA ELECTRONIC FILING -

Blanca S. Bayó
Director, Commission Clerk and Administrative Services
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399-0850

Re: Docket No. 050045-EI

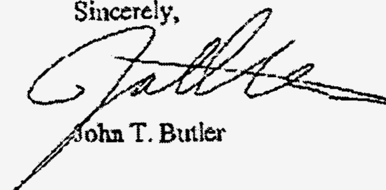
Dear Ms. Bayó:

On June 13, 2005, the Commission Staff filed a final audit report (Audit Control No. 05-094-4-1) for Florida Power & Light Company ("FPL") in this docket (the "Audit Report"). On June 30, 2005, the Staff filed a final supplemental audit report under the same Audit Control Number (the "Supplemental Audit Report"). Both the Audit Report and the Supplemental Audit Report concern an "audit [of] the rate base, net operating income, and cost of capital schedules for the historical 12-month period ending December 31, 2004" that were filed with FPL's petition for rate relief in this docket.

The Staff transmittal memoranda advised that, if FPL wished to respond to the Audit Report and Supplemental Audit Report, it should file the response with your office. I am therefore enclosing for filing FPL's response to the Audit Report and Supplemental Audit Report. Please be aware that, in accordance with the stated purpose of the audit as set forth above, FPL's response addresses the audit exceptions and disclosures only with respect to their effect on calendar year 2004.

If there are any questions regarding this transmittal, please contact me at 305-577-2939.

Sincerely,



John T. Butler

Enclosure
cc: Counsel for Parties of Record (w/encl.)

FLORIDA POWER & LIGHT COMPANY
RESPONSES TO FPSC AUDIT REPORTS
MFR AUDIT – 2004 HISTORICAL

SUPPLEMENTAL AUDIT EXCEPTION NO. 2 - JUNE 24 REPORT

SUBJECT: RENT TO AFFILIATES

FPL disagrees with the audit opinion on the following grounds:

1. Compliance with Rule 25-6.1351(3)(b), F.A.C.
FPL believes the market-based rental rates it charges its affiliates are appropriate and in compliance with Rule 25-6.1351(3)(b), F.A.C. The costs being charged to the affiliates are greater than incremental costs at both the General Office and Juno Beach facilities and thus result in a benefit to the customer.

2. FPL is charging the higher of cost or market at the General Office. The Statement of Facts in Audit Exception 2 acknowledges that FPL is charging more than fully allocated cost for rent at the General Office. Audit Exception 2 goes on to claim, however, that FPL's market-based rate understates the market in the area of the General Office. FPL disagrees with the conclusion that its measure of market rate is understated for the reasons identified below.

a.) 2002 is the appropriate timeframe for measuring market rates at the General Office
The rate being charged to affiliates leasing space in the General Office was established in late 2002. The lease terms were based on a presumed 5-year lease term because leases of the type of space involved here are typically of at least that duration. A lease rate of $17.50 per square foot was representative for 5-year leases in 2002. FPL will reevaluate the market rates at the end of this five year term.

b.) DMS Study is not necessarily relevant to our situation
It is difficult to assess the applicability of the DMS rent study without a complete review of the study. Many factors can affect lease rates including tenant size, quality of building, location, and lease terms and conditions.

FLORIDA POWER & LIGHT COMPANY
RESPONSES TO FPSC AUDIT REPORTS
MFR AUDIT – 2004 HISTORICAL

AUDIT DISCLOSURE NO. 3 - JUNE 10 REPORT

SUBJECT: EXPENSE FOR CANCELLED WORK ORDERS

The total charges associated with the five work orders referenced in the Audit Report are $90,505. After reviewing 50% of all costs charged to account 584.650 in 2004 (all work orders exceeding $5,000), FPL identified an additional $44,217 incorrectly charged to this account. Corrections for all identified errors are to be completed by July 2005.

FLORIDA POWER & LIGHT COMPANY
RESPONSES TO FPSC AUDIT REPORTS
MFR AUDIT – 2004 HISTORICAL

AUDIT DISCLOSURE NO. 5 - JUNE 10 REPORT

SUBJECT: AFFILIATE TRANSACTIONS

The market-based rental rates FPL charges its affiliates consist of a base rent component and an operating expense component. See Statement of Fact for Audit Exception No. 2, Supplemental Audit Report dated June 24, 2005.

The operating expense component of the market rate includes building maintenance. The costs identified in this Audit Disclosure are for general maintenance and repairs incurred by FPL, the lessor. FPL's affiliates are paying for building maintenance through the rental rate charged by FPL. These costs are therefore the responsibility of FPL as lessor and should not be incrementally passed on to its lessee affiliates.

FLORIDA POWER & LIGHT COMPANY
RESPONSES TO FPSC AUDIT REPORTS
MFR AUDIT – 2004 HISTORICAL

AUDIT DISCLOSURE NO. 6 - JUNE 10 REPORT

SUBJECT: PENSION

The information used by FPL to determine the annual pension allocation is derived primarily from a letter provided annually by Towers Perrin that summarizes the plan information and expenses for the upcoming year. The letter clearly states that Towers Perrin provides the breakdown of participant counts and service costs so that FPL can develop their allocations. Towers Perrin makes no allocation recommendation (Durose). The method of allocating pension expense based on payroll dollars has been consistently applied by FPL.

As stated in the audit disclosure, FPL allocates pension costs using payroll dollars. Pensions are a function of pension-eligible payroll earnings and are therefore directly related to payroll dollars. The auditor's suggestion to allocate these costs to affiliates based on head count is inappropriate and unfounded.

FPL would also like to note that the payment to Ernst and Young in the amount of $1,706,754 is the same charge identified by the auditors in Audit Exception No. 2, Audit Report dated June 10, 2005.

FLORIDA POWER & LIGHT COMPANY
RESPONSES TO FPSC AUDIT REPORTS
MFR AUDIT – 2004 HISTORICAL

AUDIT DISCLOSURE NO. 8 - JUNE 10 REPORT

SUBJECT: DUES

FPL disagrees with the audit finding. FPL included only the 2004 dues paid to EPRI in its 2004 expenses.

The 2003 EPRI dues of $240,000 were properly accrued (expensed) in December 2003. The accrual (and expense) of $240,000 was reversed in January 2004. The $240,000 invoice for the 2003 EPRI dues was paid in February 2004. The expense accrual reversal in January 2004 offsets the positive $240,000 expense recorded at the time of the February 2004 payment, resulting in a net impact of zero on 2004 for the 2003 EPRI dues. The 2004 EPRI dues of $240,000 were paid in December 2004, at which time an expense for 2004 was properly recorded.

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
2006 REVISED AFFILIATE MANAGEMENT FEE (AMF)

Line No.		Cost Pool (1)	Fee (2)	Notes (3)
1				
2				
3	**2006 FPL Affiliate Allocation Basis - As Filed**			
4				
5	FPL Staff Groups - FIN, ISC, GC, IA, CC w/ affiliate benefit	$ 60,670,089	$ 6,796,350	
6	Power Gen Shared Executives using Rated Megawatts	740,458	288,779	
7	Corporate Communication BA's w/ no benefit to FPLE	1,023,609	12,776	
8	Accounts Payable without benefit to FPLE & Palms	710,288	8,865	
9	Environmental Services without benefit to FiberNet, FPLES, Palms	842,811	118,086	
10	FPLE OSI incl. Seabrook benefit using Mass Formula and Specific Drivers	0	4,446,595	C
11	IM SUBS Allocation (Using IM Driver)	66,364,876	4,858,346	
12	HR SUBS Allocation (Using HR Drivers)	16,269,629	2,171,359	
13		$ 146,621,760	$ 18,701,155	
14				
15	Rounded (As Filed)		$ 18,800,000	
16				
17				
18	**2006 FPL Affiliate Allocation Basis - Revised**			
19				
21	FPL Staff Groups - FIN, ISC, GC, IA, CC w/ affiliate benefit	$ 61,185,997	$ 12,684,115	A,C
22	Power Gen Shared Executives using Rated Megawatts	740,458	288,779	
23	Corporate Communication BA's w/ no benefit to FPLE	1,043,929	13,039	A
24	Accounts Payable without benefit to FPLE & Palms	719,752	8,990	A
25	Environmental Services without benefit to FiberNet, FPLES, Palms	862,429	171,414	A
26	FPLE OSI incl. Seabrook benefit using Mass Formula and Specific Drivers	0	0	
27	IM SUBS Allocation (Using IM Driver)	67,506,771	5,449,760	A
28	HR SUBS Allocation (Using HR Drivers)	23,172,674	3,638,437	A,B
29		$ 155,232,009	$ 22,254,534	
30				
31	**Increase in 2006 Affiliate Management Fee**		**$ 3,454,534**	
33				
34				
35				
36	**2006 FPL Affiliate Allocation Basis - Reconciliation from Filed to Revised**			
37				
38	**2006 FPL Affiliate Allocation Basis - As Filed**		**$ 18,800,000**	
39	Correction to Supplemental Audit Exception No. 1, Item 3.		2,261,927	C
40	Correction to Audit Exception No. 2, Supplemental Audit Exception No. 3		981,721	
41	Allocation to FPL- New England Division		44,340	
42	Correction of Aviation Cost Pool and Allocation % used in HR		166,546	
43	**2006 FPL Affiliate Allocation Basis - Revised**		**$ 22,254,534**	
44				
45				

Notes:

(A) Cost pool increased to reflect additional gross up for 2005 corporate budget assumptions.

(B) Cost pool increased to reflect Supplemental Audit Exception, No. 3 and inclusion of insurance costs related to aircraft.

(C) The inclusion of FPLE-OSI and Seabrook-OSI in the overall allocation of affiliate BA's, removing previous exceptions, caused the Fee on several line items to increase. The allocation amount shown on Line 10 of the As Filed AMF Fee is now included in Line 21 of the Revised AMF Fee.

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
FPL GROUP, INC. ORGANIZATIONAL CHART
EXPLANATIONS OF WHY ENTITIES ARE/ARE NOT ALLOCATED COSTS

Company	Nature of the Business
Florida Power & Light Company	
BXR, LLC	Created with the intention of entering potential land leases, but never used. No revenues, PP&E, and payroll.
Florida Power & Light Company Trust I	Formed as a statutory trust to issue trust securities, but never used. No revenues, PP&E and payroll.
Florida Power & Light Company Trust II	Formed as a statutory trust to issue trust securities, but never used. No revenues, PP&E and Payroll.
FPL Enersys, Inc.	Owns FPL Energy Services II and FPL Services LLC, and jointly owns FPL Services (GP); all transactions are recorded directly on FPL's books. No revenues, PP&E and payroll.
FPL Services (GP)	General Contractor; all transactions are recorded directly on FPL's books. No revenues, PP&E and payroll.
FPL Energy Services II, Inc.	Jointly owns FPL Services GP; all transactions are recorded directly on FPL's books. No revenues, PP&E and payroll.
FPL Services LLC	General Contractor; all transactions are recorded directly on FPL's books. No revenues, PP&E and payroll.
FPL Historical Museum, Inc.	Not-for-profit organization for collecting, storing and displaying historical artifacts. No revenues or payroll. Has net PP&E of $150k at year end of 2004.
GridFlorida LLC	Partnership to prepare for Regional Transmission Company. No revenues, PP&E and payroll.
JEA 500 KV Transmission Line (JV)	FPL and JEA jointly own the line; FPL performs the maintenance and bills JEA. No revenues, and PP&E and payroll are on the books of FPL & JEA.
KPB Financial Corp	Holds certain intangible assets for FPL to minimize FPL's intangible taxes. Consolidated with FPL for regulatory purposes.
Robert W. Scherer Electric Generating Plant - Unit #4 (JV)	FPL is part owner of this plant which is operated by Georgia Power. FPL has an ownership interest in the power plant, but they are not operated by FPL. FPL's ownership interest is recorded on FPL's books.

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
FPL GROUP, INC. ORGANIZATIONAL CHART
EXPLANATIONS OF WHY ENTITIES ARE/ARE NOT ALLOCATED COSTS

Company	Nature of the Business
Florida Power & Light Company (cont.)	
St. Johns River Power Park (JV)	FPL is part owner of this plant which is operated by Jacksonville Electric Authority. FPL has an ownership interest in the power plant, but they are not operated by FPL. FPL's ownership interest and prorata share of operating costs are recorded on FPL's books.
FPL Group, Inc.	
FPL Group Foundation, Inc	Not-for-profit corporation formed to financially assist charitable, scientific, and educational organizations. No revenues, PP&E and payroll.
FPL Group Trust I	Formed as a statutory trust to issue trust securities, but never used. No revenues, PP&E and payroll.
FPL Group Trust II	Formed as a statutory trust to issue trust securities, but never used. No revenues, PP&E and payroll.
FPL Group Capital Trust I	Formed as a statutory trust to issue trust securities; debentures issued in 2004. No revenues, PP&E and payroll.
FPL Group Capital Trust II	Formed as a statutory trust to issue trust securities, but never used. No revenues, PP&E and payroll.
FPL Group Capital Trust III	Formed as a statutory trust to issue trust securities, but never used. No revenues, PP&E and payroll.
FPL Group Capital, Inc.	
FPL Energy Services, Inc.	Operating Company, coordinating retail sales of natural gas and other miscellaneous products. Included in the calculation of the Affiliate Management Fee.
FPL Group Holdings 1, Inc	Formed with the intention of holding assets or conducting business, but never used. No revenues, PP&E and payroll.
FPL Group Holdings 2, Inc	Formed with the intention of holding assets or conducting business, but never used. No revenues, PP&E and payroll.
HJT Holdings, Inc	Delaware Investment Holding Company; jointly owns SRM Investments. No revenues, PP&E and payroll.
LCR Holdings, Inc	Delaware Investment Holding Company; jointly owns SRM Investments. No revenues, PP&E and payroll.

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
FPL GROUP, INC. ORGANIZATIONAL CHART
EXPLANATIONS OF WHY ENTITIES ARE/ARE NOT ALLOCATED COSTS

Company	Nature of the Business
FPL Group Capital, Inc. (cont.)	
SRM Investments, L.P.	Delaware Investment Holding Company; owns EMB Investments. No revenues, PP&E and payroll.
EMB Investments, Inc.	Delaware Investment Holding Company to hold intangible assets. No revenues, PP&E and payroll.
Palms Insurance Company, Limited	Captive Insurance Company providing insurance to FPL Group operating companies; operated by Aon. Included in the calculation of the Affiliate Management Fee.
Pipeline Financial, Inc	Created for the pipeline financing in Delaware; replaced by Pipeline Funding, LLC. No revenues, PP&E and payroll.
Pipeline Funding, LLC	Provided financing for Gulfstream Natural Gas System LLC's extension of its pipeline to FPL's Manatee and Martin power plants. No revenues, PP&E and payroll.
Turner Foods Corporation	Shell company that remains after citrus groves were sold. No revenues, PP&E and payroll.
Alandco Inc	Owned undeveloped land, no payroll, and has management fee income (less than $15K in 2004).
FPL Energy, LLC	Owns and operates power plants outside of Florida. Included in the calculation of the Affiliate Management Fee.
ESI Energy, LLC	Subsidiary of FPL Energy, LLC, factors included in FPLE.
FPL Energy Maine, Inc	Subsidiary of FPL Energy, LLC, factors included in FPLE.
FPL Group International, Inc	Subsidiary of FPL Energy, LLC, factors included in FPLE.
FPL Energy ATB, LLC	Created to hold intangible assets for FPL Energy, LLC, but never used. No revenues, PP&E and payroll.
FPL FiberNet, LLC	Owns and operates Fiber Optic Networks. Included in the calculation of the Affiliate Management Fee.
FPL Group Resources, LLC	Exploring opportunities in Liquified Natural Gas. No revenues, $8K of PP&E at end of 2004, and six employees in 2005.
FPL Group Interstate Pipeline Co, LLC	Exploring opportunities in Liquified Natural Gas. No revenues, PP&E and payroll.

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
FPL GROUP, INC. ORGANIZATIONAL CHART
EXPLANATIONS OF WHY ENTITIES ARE/ARE NOT ALLOCATED COSTS

Company	Nature of the Business
FPL Group Capital, Inc. (cont.)	
S-C Pipeline Holding, LLC	Exploring opportunities in Liquified Natural Gas. No revenues, PP&E and payroll.
Calypso U.S. Pipeline, LLC	Exploring opportunities in Liquified Natural Gas. No revenues, PP&E and payroll.
FPL Holdings Inc	Owns Colonial Penn Capital Holdings. No revenues, PP&E and payroll.
Colonial Penn Capital Holdings, Inc	Owns Bay Loan and Investment Bank. No revenues, PP&E and payroll.
Bay Loan and Investment Bank	Assets are being liquidated. No revenues, no PP&E, and has employees with annual payroll of $250,000.
FPL Investments Inc	Owns several leases. No revenues, PP&E, and has one employee as of 2005.
FPL-BT Ventures (JV)	Joint venture of FPL Investments. No revenues, PP&E and payroll.
Praxis Group, Inc	Shell company remaining after assets were sold. No revenues, PP&E and payroll.
West Boca Security, Inc	Delaware Investment Holding Company to hold intangible assets. No revenues, PP&E and payroll.

9904.403-50 -- Techniques for Application.

(a)

(1) Separate expense groupings will ordinarily be required to implement 9904.403-40. The number of groupings will depend primarily on the variety and significance of service and management functions performed by a particular home office. Ordinarily, each service or management function will have to be separately identified for allocation by means of an appropriate allocation technique. However, it is not necessary to identify and allocate different functions separately, if allocation in accordance with the relevant requirements of 9904.403-40(b) can be made using a common allocation base. For example, if the personnel department of a home office provides personnel services for some or all of the segments (a centralized service function) and also established personnel policies for the same segments (a staff management function), the expenses of both functions could be allocated over the same base, such as the number of personnel, and the separate functions do not have to be identified.

(2) Where the expense of a given function is to be allocated by means of a particular allocation base, all segments shall be included in the base unless:

(i) Any excluded segment did not receive significant benefits from, or contribute significantly to the cause of the expense to be allocated and,

(ii) Any included segment did receive significant benefits from or contribute significantly to the cause of the expense in question.

(b)

(1) Section 9904.403-60 illustrates various expense pools which may be used together with appropriate allocation bases. The allocation of centralized service functions shall be governed by a hierarchy of preferable allocation techniques which represent beneficial or casual relationships. The preferred representation of such relationships is a measure of the activity of the organization performing the function. Supporting functions are usually labor-oriented, machine-oriented, or space-oriented. Measures of the activities of such functions ordinarily can be expressed in terms of labor hours, machine hours, or square footage. Accordingly, costs of these functions shall be allocated by use of a rate, such as a rate per labor hour, rate per machine hour or cost per square foot, unless such measures are unavailable or impractical to ascertain. In these latter cases the basis for allocation shall be a measurement of the output of the supporting function. Output is measured in terms of units of end product produced by the supporting function, as for example, number of printed pages for a print shop, number of purchase orders processed by a purchasing department, number of hires by an employment office.

(2) Where neither activity nor output of the supporting function can be practically measured, a surrogate for the beneficial, or causal relationship must be selected. Surrogates used to represent the relationship are generally measures of the activity of the segments receiving the service; for example, for personnel services reasonable surrogates would be number of personnel, labor hours, or labor dollars of the segments receiving the service. Any surrogate used should be a reasonable measure of the services received and, logically, should vary in proportion to the services received.

(c)

(1) Where residual expenses are required to be allocated pursuant to 9904.403-40(c)(2), the three factor formula described below must be used. This formula is considered to result in appropriate allocations of the residual expenses of home offices. It takes into account three broad areas of management concern: The employees of the organization, the business volume, and the capital invested in the organization. The percentage of the residual expenses to be allocated to any segment pursuant to the three factor formula is the arithmetical average of the following three percentages for the same period:

(i) The percentage of the segment's payroll dollars to the total payroll dollars of all segments.

(ii) The percentage of the segment's operating revenue to the total operating revenue of all segments. For this purpose, the operating revenue of any segment shall include amounts charged to other segments and shall be reduced by amounts charged by other segments for purchases.

(iii) The percentage of the average net book value of the sum of the segment's tangible capital assets plus inventories to the total average net book value of such assets of all segments. Property held primarily for leasing to others shall be excluded from the computation. The average net book value shall be the average of the net book value at the beginning of the organization's fiscal year and the net book value at the end of the year.

(d) The following paragraphs provide guidance for implementing the requirements of 9904.403-40(c)(3).

(1) An indication that a segment received significantly less benefit in relation to other segments can arise if a segment, unlike all or most other segments, performs on its own many of the functions included in the residual expense. Another indication may be that, in relation to its size, comparatively little or no costs are allocable to a segment pursuant to 9904.403-40(b)(1) through (5). Evidence of comparatively little communi-cation or interpersonal relations between a home office and a segment, in relation to its size, may also indicate that the segment receives significantly less benefit from residual expenses. Conversely, if the opposite conditions prevail at any segment, a greater allocation than would result from the application of 9904.403-40(c)(1) or (2) may be indicated. This may be the case, for example, if a segment relies heavily on the home office for certain residual functions normally performed by other segments on their own.

(2) Segments which may require special allocations of residual expenses pursuant to 9904.403-40(c)(3) include, but are not limited to foreign subsidiaries, GOCO's, domestic subsidiaries with less than a majority ownership, and joint ventures.

(3) The portion of residual expenses to be allocated to a segment pursuant to 9904.403-40(c)(3) shall be the cost of estimated or recorded efforts devoted to the segments.

(e) Home office functions may be performed by an organization which for some purposes may not be a part of the legal entity with which the Government has contracted. This situation may arise, for example, in instances where the Government contracts directly with a corporation which is wholly or partly

Docket No. 050045-EI
Docket No. 050188-EI
K. Michael Davis, Exhibit No. ___-
Document No. KMD-19, Page 3 of 3
Cost Allocation Standard

owned by another corporation. In this case, the latter corporation serves as a "home office," and the corporation with which the contract is made is a "segment" as those terms are defined and used in this Standard. For purposes of contracts subject to this Standard, the contracting corporation may only accept allocations from the other corporation to the extent that such allocations meet the requirements set forth in this Standard for allocation of home office expenses to segments.

FLORIDA POWER & LIGHT COMPANY AND SUBSIDIARIES
FPL-NEW ENGLAND DIVISION (FPL-NED)
OPERATING EXPENSES OTHER THAN INCOME TAXES
($000's)

Line No.	Description	FERC Account (1)	System Amount as Forecasted (2)	System Amount as Shown on MFR C-4 (3)	MFR C-4 Reference (4)	Notes (5)
1	**Operating Expenses:**					
2	FPL Personnel and Consulting Costs	562	$0	$1,203		
3	Transmission Station Expenses	562	437	0		
4	Transmission Support Expenses	562	5,702	5,702		
5	Total Operating Expenses		6,139	6,905	page 5, line 13	A,B
6						
7	**Maintenance Expenses:**					
8	Maintenance of Station Equip	570	546	0	page 5, line 25	A
9						
10	**Admin & General Expenses:**					
11	Admin & General Salaries	920	62	0	page 7, line 17	A
12	Office Supplies & Expenses	921	20	0	page 7, line 19	A
13	A&G Overhead Loadings	922	104	0	page 7, line 21	A
14	Property Insurance	924	0	0	page 7, line 26	A
15	Workers Compensation Insurance	925	3	0	page 7, line 28	A
16	Pension & Welfare	926	18	0	page 7, line 33	A
17	Total Admin & General Expenses		208	0		
18						
19	**Taxes Other Than Income Taxes:**					
20	Payroll Taxes	408	12	0		
21	Property Taxes	408	138	138		
22	Total Taxes Other Than Income Taxes		150	138	page 11, line 28	A
23						
24	Depreciation Expense	403	957	957	page 9, line 16	A
25						
26						
27	**Total Operating Expenses Other Than Income Taxes**		**$8,000**	**$8,000**		
28						
29						
30						

31 **Notes**
32 (A) Corresponding jurisdictional amount reported on MFR C-4 is zero.
33
34 (B) Amount reported on MFR C-4 includes forecasted amounts for FPL Personnel and Consulting Costs.
35 This includes transmission station expenses, transmission maintenance expenses, administrative and general
36 expenses, and payroll taxes.
37
38
39
40