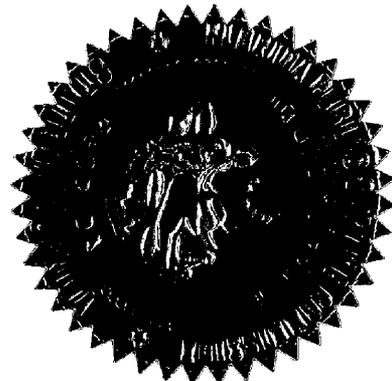


BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 060038-EI

In the Matter of:

PETITION FOR ISSUANCE OF A STORM
RECOVERY FINANCING ORDER, BY FLORIDA
POWER & LIGHT COMPANY.



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VOLUME 5

Pages 348 through 481

PROCEEDINGS: HEARING

BEFORE: CHAIRMAN LISA POLAK EDGAR
COMMISSIONER J. TERRY DEASON
COMMISSIONER ISILIO ARRIAGA
COMMISSIONER MATTHEW M. CARTER, II
COMMISSIONER KATRINA J. TEW

DATE: Thursday, April 20, 2006

TIME: Commenced at 9:00 a.m.

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

REPORTED BY: JANE FAUROT, RPR
Official Commission Reporter

PARTICIPATING: (As heretofore noted.)

DOCUMENT NUMBER-DATE

FLORIDA PUBLIC SERVICE COMMISSION

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FPSC-COMMISSION CLERK

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P R O C E E D I N G S

(Transcript follows in sequence from Volume 4.)

CHAIRMAN EDGAR: Good morning. We will go back on the record.

Welcome back. I'll begin by saying that we have, as we all know, a lot of ground to cover over the next two days. I know that we are all aware, but I do feel compelled to say that we are finishing with our third witness, and we have a total of 25. So, as with yesterday, I look forward to all of the questions, and I look forward to all of the answers, as I know my colleagues do, but I would ask both the attorneys and the witnesses to try to keep their questions and their answers focused.

And with that, I believe where we left off was with staff ready to ask some cross of the witness.

MS. GERVASI: Thank you.

DR. RICHARD E. BROWN

continues his testimony under oath from Volume 4:

CROSS EXAMINATION

BY MS. GERVASI:

Q Doctor Brown, let me turn your attention briefly to your testimony on Page 8. Starting on Line 5, you testify that distribution pole performance during Wilma is known to be acceptable since FPL gathered extensive forensic data on Wilma pole failures, correct?

1 A Correct.

2 Q Would you agree that as a general proposition data
3 collection can be skewed or biased so as to favor a particular
4 outcome?

5 A As a general proposition?

6 Q Yes, sir.

7 A Yes, as a general proposition.

8 Q Thank you.

9 Did KEMA examine or perform any analysis
10 independently to determine whether FPL's forensic efforts were
11 skewed or biased in any way favorable to FPL?

12 A Yes.

13 Q Can you explain?

14 A We looked at the forensic data that was gathered, we
15 examined the approach that they took to gather the data, and we
16 examined the pole retention yard to see if the poles that were
17 in the pole retention yard were consistent with the forensic
18 data that was gathered. And we found no evidence of bias in
19 the data collection.

20 MS. GERVASI: Thank you.

21 That's all we have.

22 CHAIRMAN EDGAR: That was a little quicker than I was
23 expecting, but it's a good start.

24 Commissioners, any questions for this witness? No.

25 Okay.

1 Mr. Butler.

2 MR. BUTLER: Thank you. I will try to keep this
3 brief.

4 REDIRECT EXAMINATION

5 BY MR. BUTLER:

6 Q Doctor Brown, Mr. McGlothlin asked you about pinging
7 the bolt threads or using locknuts after the loose and missing
8 bolts were discovered in 1998 on the Conservation Corbitt
9 (phonetic) line. Based on FPL's evaluation of the conductor
10 vibration conditions on that line, the corrective measures that
11 were taken to address the conductor vibration, and the results
12 of the subsequent inspections of the line, do you believe that
13 FPL had any reason to expect that pinging the threads or the
14 use of locknuts would have been necessary?

15 A No.

16 Q Mr. McGlothlin asked you about KEMA's utility
17 experience. Have any members of the team that prepared the
18 KEMA report previously worked for electric utilities?

19 A Yes. When I assembled the project team, I
20 specifically included people that had extensive utility
21 experience. Two of the members on the team had more than 15
22 years working for investor-owned utilities.

23 Q Would you please describe the consulting work that
24 you personally have done for electric utilities?

25 A Yes. I have worked for more than 50 utilities in a

1 consulting context, most of the large investor-owned utilities
2 in the U.S., and other large utilities around the world.

3 MR. KISE: Madam Chair.

4 CHAIRMAN EDGAR: Mr. Kise.

5 MR. KISE: I need to interpose an objection. I think
6 this question is beyond the scope of cross. We didn't
7 challenge the witness' credibility or qualifications. I don't
8 think any of us asked any questions about that, and redirect
9 is, of course, limited to what we asked. I don't see any
10 reason -- there wasn't any dispute over this witness'
11 experience, I don't know why we are spending any time on it. I
12 think it is improper.

13 CHAIRMAN EDGAR: Mr. Butler.

14 MR. BUTLER: In fact, there was. Mr. Kise -- they
15 weren't your questions, but they were Mr. McGlothlin's
16 questions, as I indicated, and Mr. McGlothlin had asked Doctor
17 Brown about whether he had worked for an electric utility. I
18 took the purpose of that question to be suggesting that
19 therefore, perhaps, the work that was done by KEMA didn't have
20 a lot of background behind it in electric utility operations.
21 I'm simply wanting to respond to that suggestion.

22 MR. KISE: Same objection. I disagree.

23 MR. MCGLOTHLIN: And I will add one other objection.
24 I asked Doctor Brown if he had ever been in the role of working
25 for the owner of a utility system and charged with the

1 responsibility of maintaining it, and that should be the scope
2 of the permitted redirect.

3 MR. KISE: Mr. McGlothlin and Mr. Kise's objections
4 are noted. I will note that the parties did spend with this
5 witness a great deal of time discussing this subject, and so
6 I'm going to allow Mr. Butler, but I think we can probably do
7 it quickly.

8 MR. BUTLER: When he finishes answering this
9 question, that is the only one on that subject.

10 Please continue, Doctor Brown.

11 A Yes, all of my consulting work for a large number of
12 utilities has been specifically for the transmission and
13 distribution infrastructure, including design, engineering,
14 maintenance, and operations.

15 BY MR. BUTLER:

16 Q Mr. McGlothlin asked you about FPL's asset management
17 system and Orion system. Did FPL's inspection of the
18 Conservation Corbitt line effectively confirm that FPL had
19 replaced and retightened the missing and loose bolts that were
20 discovered in 1998?

21 MR. WRIGHT: Madam Chair, I object, that is as
22 leading as it can be.

23 MR. BUTLER: I can make these question less so, if
24 that is the Chair's pleasure. I'm trying to move the
25 proceeding along and do this as efficiently as possible.

1 I would note that by the standard Mr. Kise is
2 raising, probably the vast majority of the questions asked on
3 redirect here routinely would fail the test. As I say, I'm
4 simply trying to move it along. If that's not the Commission's
5 preference, I will certainly ask more neutral questions.

6 CHAIRMAN EDGAR: I will note that this is an
7 administrative hearing, and we are here to hear from the
8 witnesses. However, I appreciate all of the parties taking my
9 words a few moments ago to heart.

10 Mr. Butler, please continue.

11 MR. BUTLER: Thank you.

12 BY MR. BUTLER:

13 Q Would you answer the question, Doctor Brown.

14 A Please restate the question.

15 Q What is your opinion as to whether the inspections of
16 the Conservation Corbitt line were able to confirm that FPL had
17 replaced and retightened the missing and loose bolts that were
18 discovered in 1998?

19 A The inspections were sufficient to conclude that this
20 had been done.

21 Q What is your opinion as to whether those same
22 inspections would have been able to confirm that over the
23 period 1999 to 2003 the bolts did not reloosen?

24 A Based on the number and types of inspections that
25 were done after 2003, it is unlikely that there were any

1 substantial number of loose and/or missing bolts.

2 Q Do you have an opinion as to whether the loose and
3 missing bolts that were discovered post-Wilma in 2005 were
4 loose or missing as of 2003?

5 A Yes.

6 Q And what is that opinion?

7 A My opinion is that the loose and missing bolts found
8 after Wilma were not loose and/or missing after 2003.

9 Q Mr. Wright asked you about the National Hurricane
10 Center's final report for Hurricane Wilma dated January 12,
11 2006, that was identified as Exhibit 143.

12 Do you have a copy of that report?

13 A Yes.

14 Q When KEMA evaluated the performance of FPL's
15 transmission and distribution system in Hurricane Wilma, would
16 you describe how it performed that evaluation?

17 A Yes. We measured the damage that occurred on the
18 system based on two factors. One, the number of poles that
19 were exposed to hurricane force winds, those are winds greater
20 than 75 miles per hour sustained wind speed, and, second, the
21 hurricane category.

22 And the hurricane category numbers used in the KEMA
23 analysis are fully consistent with the National Hurricane
24 Center tropical cyclone report on Wilma.

25 Q In your opinion, therefore, does the categorization

1 of Hurricane Wilma in the National Hurricane Center effect any
2 of the conclusions that you reached in the KEMA report?

3 A Yes.

4 Q It effects those conclusions?

5 A Oh, it does not effect those conclusions. It is
6 consistent with those conclusions.

7 Q Mr. McGlothlin asked you about the effectiveness of
8 FPL's pole inspection program. Do you consider nonhurricane
9 pole failure rates due to deterioration to be a good measure of
10 the effectiveness of a pole inspection program?

11 A Yes.

12 Q Would you explain why.

13 A Ultimately, the pole failure mechanism is the same
14 during nonhurricane and hurricane conditions. It is a function
15 of the strength of the pole versus the forces that are imposed
16 on a pole. And so looking at the pole performance in
17 nonhurricane conditions is a very good indication of how the
18 poles are going to perform under extreme loads. The number of
19 failures is going to be fewer, but the data that you collect is
20 much better. You have a lot -- a very much larger data set, it
21 is more controlled conditions, the data collection process is
22 much better, and so looking at nonstorm pole performance is a
23 very good indication of pole performance, expected pole
24 performance during extreme weather conditions.

25 Q Did KEMA compare FPL's nonhurricane pole failure rate

1 due to deterioration with rates for comparable utilities?

2 A Yes.

3 Q And what were the results of that comparison?

4 A In the benchmark survey that we did for the
5 engagement, nine utilities responded, and of those utilities,
6 five of those utilities kept statistics on nonstorm pole
7 failure rate due to deterioration. Of the five utilities that
8 responded, FPL had lower nonstorm pole failure rates due to
9 deterioration than each of these five utilities. Each of these
10 five utilities are subject to hurricane force winds, are in the
11 southern U.S. hot, humid climates. And of the average of the
12 five responses, FPL's number failure rate is 75 percent lower
13 than the average response.

14 Q Thank you.

15 Mr. Kise asked you whether FPL had transmission
16 structures that met the standards, construction standards that
17 were applicable at the time they were installed, but would not
18 meet today's standards. Are you aware of any utility that
19 upgrades all of its existing transmission structures when there
20 has been a change to the construction standards that would
21 apply to new construction.

22 A No, I'm aware of no utility that does this. This
23 would be extremely extensive, impractical, it would take a long
24 time to do this. And, in fact, in the process of doing this,
25 over many years, your standards would change, so you would be

1 shooting at a moving target, and it would be an imprudent
2 expense, in my opinion.

3 Q Mr. Kise asked you about the statistics on Page 31 of
4 the KEMA report concerning the percentage of Osmose inspected
5 poles in the Brevard area during 2005. Was the Osmose program
6 in Brevard focused on old creosote poles?

7 A Yes.

8 Q What is your opinion as to whether one would expect
9 to see an inspection program focused on old creosote poles to
10 identify a higher than average percentage of poles requiring
11 repair?

12 A The results of this particular inspection showed
13 higher failure rates. This is an indication to me that FPL did
14 a good job in targeting these inspections. So it shows that
15 they had a good feel for where potential old pole populations
16 with potentially higher reject rates would be.

17 MR. BUTLER: Thank you, Doctor Brown.

18 That's all the redirect that I have.

19 MR. KISE: Madam Chair, I want to note two things for
20 the record, if I may.

21 One, we have entered into an agreement with FPL
22 whereby we are going to obtain the notes that Doctor Brown has
23 that he referred to yesterday that relate to this new
24 information that only Doctor Brown and FPL had possession of,
25 and we are going to obtain that information, and then as I

1 understand it, this witness is going to be back for rebuttal
2 testimony; we will cover those subjects then.

3 I also have several recross questions. However, in
4 the interest of time, if the Chair will give me the latitude to
5 ask those questions when the witness returns for rebuttal, that
6 would be satisfactory.

7 CHAIRMAN EDGAR: Mr. Butler.

8 MR. BUTLER: If the questions relate to his rebuttal
9 testimony, it's certainly fine with me. If they don't, I think
10 they ought to be raised now.

11 CHAIRMAN EDGAR: Mr. Kise.

12 MR. KISE: Then I will simply ask them now. If the
13 Chair so desires, and FPL thinks that I need to ask them now as
14 opposed to then, that's fine, I can ask them now. They're only
15 a few questions.

16 CHAIRMAN EDGAR: Let's proceed. Mr. Kise.

17 RECCROSS EXAMINATION

18 BY MR. KISE:

19 Q Doctor Brown, did you meet with FPL counsel last
20 night or this morning?

21 A Yes.

22 Q Did you discuss the subject matter of your testimony
23 at that time?

24 A Yes.

25 Q What specifically did you discuss?

1 A We discussed some of the questions that potentially
2 could be asked on redirect.

3 Q Did you discuss the questions that you were asked
4 this morning?

5 A Yes.

6 Q Did you discuss your answers to those questions?

7 A Yes.

8 Q In responding to Mr. Butler, I think it was his first
9 question, and bear with me because I may butcher this question,
10 I'm paraphrasing, because there was a lot in it.

11 I believe the question related to whether you would
12 have had any reason to expect that these ping-pong threads or the
13 use of locknuts would have been required. Do you recall that
14 question that he asked you?

15 A Yes.

16 Q And I believe your answer was that there would be no
17 reason to expect that the use of locknuts would be required or
18 ping-pong threads, et cetera, would be required, is that right?

19 A Yes.

20 Q And that was based on FPL data, right?

21 A Yes.

22 Q That was not based on your individual inspection
23 prior to the start of the 2004 hurricane season, right?

24 A Correct.

25 Q And that was not based on your individual inspection

1 prior to the start of the 2005 hurricane season, right?

2 A Correct.

3 Q That was not based on your individual inspection
4 prior to Hurricane Wilma, right?

5 A Correct.

6 Q Okay. With respect to the question that Mr. Butler
7 asked you about targeting old pole populations, I believe you
8 indicated that -- well, strike that.

9 Is it fair to say that a program that targets for
10 inspection older pole populations is a sound idea for any
11 utility to undertake?

12 A Yes.

13 Q And as we covered yesterday, obviously FPL has the
14 ability to determine which pole populations are older, right?

15 A This particular activity did target a population that
16 had higher reject rates. I'm not certain if they would be able
17 to repeat that or not, but the one time that they tried it they
18 were successful.

19 Q Well, in your report on Page 31, you did say that in
20 this particular instance they were targeting areas with older
21 pole populations, right?

22 A Correct.

23 Q Then it would be reasonable to conclude, in your
24 opinion, that they must have some way of identifying older pole
25 populations, right?

1 A Yes.

2 MR. KISE: Thank you. That's all I have. Thank you.

3 CHAIRMAN EDGAR: I show that we have two exhibits
4 that we need to --

5 MR. KISE: Madam Chair, one other point on this
6 witness. With respect to the recross, I appreciate Mr. Butler
7 and FPL's position about the limitation on my questions.
8 However, with respect to the information that he provides by
9 his notes, I would not agree to that same limitation. If, in
10 fact, we discover things through a review of this witness'
11 notes, and we discover things as to which we were previously
12 unaware, then we would request the latitude to examine the
13 witness based on that information.

14 Additionally, I would ask that we be allowed to
15 reserve the right to call any additional witness necessary to
16 rebut this new information. FPL is coming before this
17 Commission asking for a billion and a half dollars of the
18 people's money out of the people's pocket, they ought to have
19 given us this information a long time ago. They had it, they
20 certainly had a chance to talk with this witness about the
21 substance of his testimony before two days ago.

22 CHAIRMAN EDGAR: Mr. Kise, this Commission is aware
23 of what the issues are that are before us, and we will take up
24 issues, motions, requests, at the time that they need to be
25 made. And let's see what it leads to, rather than guessing

1 what it may lead to.

2 MR. KISE: Fair enough.

3 CHAIRMAN EDGAR: Exhibits.

4 MR. WRIGHT: I move 143, Madam Chairman.

5 CHAIRMAN EDGAR: Any objections?

6 MR. McGLOTHLIN: I believe mine was 142.

7 CHAIRMAN EDGAR: It was. Any objections to 142?

8 MR. BUTLER: No.

9 CHAIRMAN EDGAR: Seeing none, please show Exhibits
10 142 and 143 moved into the record as evidence.

11 (Exhibits 142 and 143 admitted into the record.)

12 CHAIRMAN EDGAR: And, Doctor Brown, you are excused.

13 We look forward to seeing you, hopefully, tomorrow.

14 THE WITNESS: Thank you.

15 MS. SMITH: FPL calls Mr. Mark Warner.

16 **MARK WARNER**

17 **was called as a witness on behalf of FPL, and having been duly**
18 **sworn, testified as follows:**

19 **DIRECT EXAMINATION**

20 BY MS. SMITH:

21 Q Mr. Warner, were you present and sworn yesterday
22 morning?

23 A Yes, I was.

24 Q Would you please state your name and business
25 address.

1 A Yes. My name is Mark Warner. My business address is
2 700 Universe Boulevard, Juno Beach, Florida.

3 Q By whom are you employed and in what capacity?

4 A I'm employed by Florida Power and Light. My capacity
5 is the Vice-President of Nuclear Operation Support.

6 Q Have you prepared and caused to be filed 15 pages of
7 Prefiled Direct Testimony in this proceeding?

8 A I have.

9 Q Do you have any changes or revisions to your Prefiled
10 Direct Testimony?

11 A No, I do not.

12 Q If I asked you the same questions contained in your
13 Prefiled Direct Testimony today, would your answers be the
14 same?

15 A Yes, they would.

16 MS. SMITH: I would ask that Mr. Warner's Prefiled
17 Direct Testimony be inserted into the record as though read.

18 CHAIRMAN EDGAR: The prefiled testimony will be
19 entered into the record as though read.

20 BY MS. SMITH:

21 Q Mr. Warner, are you also sponsoring Exhibit MW-1 to
22 your Direct Testimony?

23 A Yes, I am.

24 MS. SMITH: And this has been identified as Exhibit
25 Number 16 and moved into the record yesterday.

REPORTER NOTE: Page 367 was inadvertently omitted from the record.

1 **BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**

2 **FLORIDA POWER & LIGHT COMPANY**

3 **DIRECT TESTIMONY OF MARK WARNER**

4 **DOCKET NO. XXXXXX-EI**

5 **JANUARY 13, 2006**

6

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

8 A. My name is Mark Warner. My business address is 700 Universe Blvd., Juno
9 Beach, FL 33408.

10 **Q. By whom are you employed and what is your position?**

11 A. I am employed by Florida Power & Light Company (FPL or the Company) as
12 Vice President, Nuclear Operations Support.

13 **Q. Please describe your duties and responsibilities in that position.**

14 A. As Vice President of Nuclear Operations Support, I am responsible for the
15 following functional areas: business services, information technology, emergency
16 preparedness, training, security, nuclear regulatory affairs and turbine generator
17 overhauls. I oversee the integration and standardization of the operational
18 programs and processes for FPL's nuclear plant sites.

19 **Q. Please describe your educational background and professional experience.**

20 A. I earned my Bachelor of Science degree in Mechanical Engineering from
21 Villanova University in 1986. In 1991, I received a Senior Reactor Operator
22 Certification. I attended the Advanced Management Program at Duke University's
23 Fuqua School of Business in 1996.

1 Prior to working in the electric power industry, I served in the U.S. Marine Corps
2 from 1974 to 1981. I am an 18-year veteran in the electric power industry,
3 serving in positions of increasing responsibility in operations, maintenance, work
4 control outage management, and engineering. Before becoming Vice President of
5 Nuclear Operations Support I was the site vice president of FPL Energy's
6 Seabrook nuclear power plant. Before that I served as site vice president of
7 Nuclear Management Company's Point Beach and Kewaunee nuclear power
8 plants. From June 2000 to January 2002, I was vice president of Three Mile Island
9 Nuclear Plant for Exelon Corp.

10 **Q. Are you sponsoring an exhibit in this case?**

11 A. Yes, I am sponsoring an exhibit consisting of one document, Document No. MW-
12 1, 2005 Nuclear Storm Costs, which is attached to my direct testimony.

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

14 A. The purpose of my testimony is to discuss the impact of the 2005 storm season on
15 FPL's St. Lucie and Turkey Point nuclear plant sites. I address the preparation
16 required for the potential onset of hurricanes and tropical storms at the St. Lucie
17 and Turkey Point nuclear sites, and the damage sustained from Hurricane Wilma
18 at these two nuclear sites. I also discuss the cost and expected insurance recovery
19 associated with the hurricane-related damage.

20

21

STORM PREPARATION

22 **Q. Please provide an overview of FPL's nuclear operations in Florida.**

23 A. FPL has four nuclear units in Florida – two at the Turkey Point Nuclear Plant
24 (1,386 MW) and two at the St. Lucie Nuclear Plant (1,677 MW). The Turkey

1 Point site is located on the shore of Biscayne Bay, east of Florida City in Dade
2 County. The St. Lucie site is located near Jensen Beach on the east coast of
3 Florida in St. Lucie County.

4 **Q. What procedures does the Nuclear Division have in place to ensure that it is**
5 **prepared for hurricanes or tropical storms that may affect its plant sites in**
6 **Florida?**

7 A. Our nuclear units begin preparing for hurricanes and tropical storms at the
8 beginning of hurricane season each June. The sites perform walk-downs to
9 identify areas and equipment that are vulnerable to storm damage, and take
10 necessary steps to secure material that is stored outside. In addition, during the
11 walk down, the employees verify operability of emergency communication
12 equipment. This is important because the plant must be able to communicate its
13 status in the event of an emergency and be able to notify state and local
14 government officials. Also, the employees prepare an inventory of necessary
15 hurricane supplies and secure needed equipment and material. These preparation
16 activities are not charged to the Reserve.

17 **Q. Does the nuclear division train its employees to respond to storms?**

18 A. Yes. Under federal regulations, nuclear plants are required to periodically train
19 individuals who are expected to respond to emergencies which include natural
20 disasters such as hurricanes. FPL trains responders once each calendar year. In
21 addition, the emergency response organization conducts periodic drills and
22 exercises throughout the year to maintain proficiency. These activities also are
23 not charged to the Reserve.

1 **Q. What procedures are in place when a tropical storm or hurricane threatens a**
2 **nuclear plant site?**

3 Each of the plants has an emergency plan that is used as the basis of the storm
4 response. A key to execution of the emergency plan is that an emergency crew is
5 stationed to ride out a storm, recognizing that staffing an emergency organization
6 that would travel to the plant site during a storm would not be safe. During the
7 storm, crews (emergency personnel and other station staff) are housed in safe
8 areas throughout the plant including a team in the Emergency Diesel Generator
9 building. If the storm impacts the station, to the extent it is safe to do so,
10 emergency crews would respond to start, repair or troubleshoot any plant
11 equipment. However, emergency crews would not be placed in unsafe conditions.
12 More extensive repairs would be deferred until after the wind subsides, when
13 outside travel would be possible.

14 **Q. What other actions are taken when there is an imminent threat of hurricane**
15 **force winds at a nuclear site?**

16 A. When a hurricane watch or warning is given by the National Hurricane Center,
17 the nuclear plant site fills all necessary fuel and water tanks, completes all
18 scheduled maintenance activities and conducts any necessary training for the
19 operating crew to ensure they are prepared for potential circumstances they could
20 face in a hurricane. All these actions are designed to support the placement of the
21 nuclear unit in a safe condition prior to being impacted by hurricane force winds.

22

1 Pursuant to its Station Blackout requirements, the Nuclear Regulatory
2 Commission (NRC) requires FPL to commence a shutdown of its nuclear units
3 two hours prior to the onset of hurricane force winds at the site. FPL has
4 procedures at the nuclear sites that start implementing plant shutdown activities as
5 early as 72 hours prior to projected landfall and require the nuclear units to
6 actually be shutdown two hours prior to the onset of hurricane force winds at the
7 site.

8
9 **2005 STORM SEASON**

10 **Q. Which storms impacted the operation of FPL's nuclear sites during the 2005**
11 **storm season?**

12 **A.** Hurricane Wilma affected the operation of both the St. Lucie and Turkey Point
13 nuclear plant sites resulting in Turkey Point nuclear units 3 and 4 and St. Lucie
14 nuclear Unit 2 being taken off line. St. Lucie nuclear Unit 1 was already off line
15 for a planned refueling outage when Hurricane Wilma threatened the plant site.

16
17 Hurricanes Katrina and Rita impacted the Turkey Point nuclear plant site, but the
18 units at the site were not required to be taken off line during the storm. The
19 Turkey Point nuclear plant site performed storm preparation and restoration
20 activities in response to Hurricanes Katrina and Rita.

21
22

1 **Q. What was the intensity of Hurricane Wilma when it reached the Turkey**
2 **Point plant site?**

3 A. As addressed in the testimony of Ms. Williams, Hurricane Wilma made landfall
4 on the southwest coast of Florida on October 24, 2005, as a Category 3 hurricane.
5 Based on the track of Hurricane Wilma, the Turkey Point nuclear plant site began
6 to experience tropical storm force winds from Hurricane Wilma in the early
7 morning of October 24 and began to experience hurricane force winds early in the
8 day. Due to the speed of Hurricane Wilma, hurricane winds were only on the site
9 for a brief period of time (less than 1 hour). The winds subsided to tropical storm
10 force winds that morning and below tropical storm force by the early afternoon.
11 The most intense winds recorded at the Turkey Point nuclear plant site were 76
12 mph, which rates as Category 1 force winds on the Saffir-Simpson Intensity Scale
13 (SSI Scale). Category 1 force winds are between 74 and 95 miles per hour (mph)
14 sustained for one minute.

15 **Q. What was the intensity of Hurricane Wilma when it reached the St. Lucie**
16 **nuclear plant site?**

17 A. The St. Lucie nuclear plant site began to experience tropical storm force winds on
18 the morning of October 24 and hurricane force winds that afternoon. The most
19 intense winds at the St. Lucie nuclear plant site were experienced at
20 approximately noon. The onsite meteorological tower failed but the National
21 Hurricane Center reported St. Lucie experiencing Category 2 force winds on the
22 SSI Scale. Category 2 force winds are winds between 96 and 110 mph sustained
23 for at least 1-minute.

1 **Q. Please describe the shutdown of FPL's nuclear units due to Hurricane**
2 **Wilma.**

3 A. St. Lucie Unit 2 and Turkey Point Units 3 and 4 were brought off-line in the early
4 morning on October 24 before the sites began experiencing hurricane-force
5 winds.

6 **Q. Were there any circumstances that extended the time to prepare for**
7 **Hurricane Wilma?**

8 A. Yes. Due to a refueling outage at St. Lucie Unit 1, additional time was necessary
9 to demobilize plant equipment and material staged for outage support to safely
10 secure the unit before the storm made landfall. For example, large cranes were
11 dismantled and heavy equipment was required to be moved and secured.
12 Numerous site personnel were involved in completing these tasks in the short-
13 time frame before the storm arrived.

14 **Q. Please explain the regulatory requirement for the restart of a nuclear unit**
15 **following a natural disaster.**

16 A. The criteria for restarting the nuclear units following a hurricane are based on
17 reviews performed by the NRC and the Federal Emergency Management Agency
18 (FEMA) regarding the ability of FPL, the State of Florida, and local governments
19 to effectively implement their emergency plans. The standard used by the NRC
20 and FEMA to evaluate the ability to restart the plant following an event such as a
21 hurricane is whether there is reasonable assurance that both FPL and the state and
22 local government can protect the health and welfare of the public in the event of a
23 nuclear power plant accident.

1 **Q. Please provide examples of necessary preconditions to restart the nuclear**
2 **units.**

3 A. The plant systems required for operation must be able to perform their intended
4 function; the plant has technical specifications that describe what equipment must
5 be operable. In the community surrounding the plant site, the Alert and
6 Notification System (sirens) must be operable and the local government must be
7 able to support the implementation of public protective actions such as shelter,
8 evacuation and monitoring of evacuees. Additionally, the local government must
9 have the essential personnel and equipment in place for emergency operations.

10 **Q. Did the effects of Hurricane Wilma delay the restart of any of the nuclear**
11 **units?**

12 A. Yes. Turkey Point Unit 4 did not return to service until November 13. The unit
13 restart delays were due to grid instability issues, grass intrusion into secondary
14 plant systems, salt water intrusion due to a tube sheet plug failure as an indirect
15 result of grass removal and loss of offsite power due to salt contamination in the
16 plant switch yard. The other nuclear units returned to service within 4-9 days
17 after Hurricane Wilma struck.

18

19

STORM-RELATED COSTS

20 **Q. Did the St. Lucie and Turkey Point sites incur costs resulting from the 2005**
21 **Hurricanes?**

22 A. Yes. Both the St. Lucie and Turkey Point plant sites incurred costs from the 2005
23 Hurricanes.

1 **Q. Please describe the type of costs incurred due to the 2005 Hurricanes.**

2 A. The costs incurred by the nuclear sites due to the 2005 Hurricanes are primarily in
3 two categories: 1) storm preparation and unit restoration costs; and 2) storm
4 damage costs. Storm preparation and unit restoration costs are primarily labor
5 costs associated with demobilizing the plant to safely secure the site before the
6 storms made landfall and to restart the unit back to full power. Storm damage
7 costs are physical damage to the plant infrastructure and surrounding property.

8 **Q. What is the estimated total cost for the nuclear division storm preparation
9 and unit restoration and storm damage to the nuclear sites?**

10 A. The estimated total cost for hurricane-related unit preparation/restoration and
11 damage is \$40.9 million for the St. Lucie and Turkey Point nuclear sites.

12 **Q. Please quantify the storm preparation and unit restoration costs for the St.
13 Lucie and Turkey Point plant sites.**

14 A. FPL estimates storm preparation and unit restart costs for the St. Lucie of \$6.8
15 million and the Turkey Point Site of \$2.8 million.

16 **Q. Why are the storm preparation and unit restart costs for the St. Lucie site
17 substantially greater than that for the Turkey Point site?**

18 A. As addressed above, because St. Lucie Unit 1 was in the middle of its refueling
19 outage prior to Hurricane Wilma, additional time and labor costs were required to
20 secure the site before the storm made landfall.

1 **Q. Please describe the storm damage from Hurricane Wilma sustained at the St.**
2 **Lucie nuclear site.**

3 A. St. Lucie performed a preliminary inspection and assessment of the site and
4 identified damage to various buildings, several power block systems, the intake
5 canal and dunes and inventory. There was roof, ceiling and wall damage to
6 several buildings due to water intrusion. Also, the Quality Control Test Facility
7 was completely demolished and the South Service Building, which is the primary
8 work location for site departments, sustained roof damage. The power block
9 damage consists of water intrusion to motors and air conditioning units, wind and
10 water damage to protective insulation, and damage to corrosion protective plant
11 coatings on the power block structure. The dunes adjacent to the plant site
12 suffered substantial beach erosion, and the intake and discharge canals sustained
13 damage to the side walls.

14 **Q. What is the estimated total cost for Hurricane Wilma storm damage**
15 **sustained at the St. Lucie site?**

16 A. The estimated total cost for storm damage to the St. Lucie site is \$10.6 million.
17 Document No. MW-1 includes a breakdown of St. Lucie storm damage by
18 category of cost.

19 **Q. What effect did Hurricane Wilma have on the St. Lucie Unit 1 refueling**
20 **outage?**

21 A. A refueling outage commenced at St. Lucie Unit 1 on October 16. On October
22 20, the refueling outage was suspended to prepare the site for Hurricane Wilma.

1 Due to preparations for and the effects of Hurricane Wilma, the refueling outage
2 was delayed approximately one week.

3 **Q. How was storm activity for St. Lucie Unit 1 segregated from outage activity?**

4 A. Each functional area was instructed to segregate storm-related preparation from
5 outage-related activity. The storm preparation activities were captured under
6 storm work orders and outage-related work was captured under the outage O&M
7 work orders.

8 **Q. You mentioned that there was damage to the dunes. Could you please**
9 **describe what you mean by the dunes and how they affect the operation of**
10 **the St. Lucie Nuclear Plant?**

11 A. The dunes are a berm of natural sand and foliage at the beachfront that protect the
12 plant from hurricane force waves and storm surge. Without the protection
13 afforded by the dunes, FPL's infrastructure, canal dikes, head walls, access roads
14 and bridges would absorb the main force of the waves, causing significant
15 damage. If the dunes are not in place, the restart of the St. Lucie Nuclear Plant
16 may be substantially delayed due to increased damage to the plant and its
17 infrastructure.

18 **Q. Did the dunes serve their purpose during Hurricane Wilma?**

19 A. Yes. The dunes absorbed the brunt of the wave and storm surge from Hurricane
20 Wilma, which helped the St. Lucie Nuclear Plant to return to operation in a timely
21 manner.

22

1 **Q. Please describe the effect of Hurricane Wilma on the dunes and the need to**
2 **repair damage to the dunes.**

3 A. The wave and storm surge from Hurricane Wilma significantly eroded the height
4 and width of the dunes and damaged the vegetation that protects the dunes. The
5 dunes must be repaired for the St. Lucie Nuclear Plant to be protected during
6 future storms and to comply with the site licensing requirements. The ability of
7 the dune line to absorb the force of hurricane force waves is credited in the NRC
8 evaluation of the hurricane and associated flood protection for the St. Lucie Plant.
9 The configuration of the dunes at the time of the NRC evaluation is described in
10 our plant design basis and plant licensing documents. In order to maintain the
11 design assumptions, the topographic features credited for protection of the plant
12 are required to be maintained by FPL as part of FPL's license to operate the St.
13 Lucie Nuclear Plant. Technical Specifications have been issued to ensure that
14 plant design requirements are not violated. These Technical Specifications
15 require, as a minimum, that after each hurricane, a visual inspection of the dunes
16 be performed to ensure the dunes are not breeched, potentially violating the basis
17 for the design of the plant.

18 **Q. Is the damage to the dunes covered by insurance?**

19 A. No. The beach dunes at the St. Lucie site are outside the insurance coverage
20 boundary.

21 **Q. Approximately how much will it cost to repair the dunes?**

22 A. FPL estimates it will cost approximately \$3.2 million to restore the dunes to their
23 original configuration.

1 **Q. Please describe the storm damage sustained at the Turkey Point nuclear site.**

2 A. There was damage to various buildings, power block systems, security lighting
3 and fencing at the Turkey Point site. The power block damage consists of water
4 intrusion to motors and air conditioning units, as well as damage to corrosion
5 protective plant coatings on the power block structure.

6 **Q. What is the estimated cost for storm damage sustained at the Turkey Point
7 nuclear site?**

8 A. The estimated cost for storm damage to the Turkey Point nuclear site is \$20.8
9 million. Document No. MW-1 includes a summary of Turkey Point storm
10 damage by category of cost.

11

12

NUCLEAR INSURANCE

13 **Q. Does FPL have insurance coverage to pay for damage to the nuclear sites?**

14 A. Yes, but the insurance will not pay for all the storm damage.

15 **Q. Please describe FPL's insurance coverage for its nuclear plant sites.**

16 A. The nuclear plants are insured by Nuclear Electric Insurance Limited (NEIL).
17 NEIL insures domestic and international nuclear utilities for the costs associated
18 with interruptions, damages, decontaminations and related nuclear risks.

19

1 NEIL established an insurable property boundary that includes the plant and
2 surrounding facilities. This boundary is not the same as FPL property line, so
3 there are facilities and property outside of the line that are not covered by NEIL.

4 **Q. What costs does FPL expect to recover from NEIL?**

5 A. As stated above, FPL has estimated \$40.9 million in total storm-related costs for
6 the nuclear plant sites affected by the 2005 Hurricane Season. The majority of the
7 costs are attributed to Hurricane Wilma with the exception of \$538,000 in storm
8 preparation costs at the Turkey Point nuclear plant site for Hurricanes Katrina and
9 Rita. Of this, FPL expects to recover \$23 million from insurance, but this
10 number may be adjusted as additional inspections or work is performed.

11 **Q. What types of costs are not covered by the NEIL policy?**

12 A. In addition to the insurance deductible of \$1 million per site, FPL anticipates the
13 storm preparation and unit restoration costs and any property damages outside the
14 NEIL boundary line will not be recovered by insurance. This property would
15 include the dunes. FPL expects that through the NEIL review process, additional
16 costs will be determined to not be covered by the insurance policy.

17 **Q. What is the total amount of nuclear storm-related costs that FPL seeks to
18 recover in this proceeding?**

19 A. The total net of insurance nuclear storm-related costs being requested is \$17.9
20 million. This includes a deductible of \$1 million per site, and \$15.9 million of
21 estimated uninsured costs. To the extent more costs are recovered from insurance
22 than FPL anticipates, FPL would contribute that amount to the balance of the
23 reserve to pay for future storm costs. If fewer costs are recovered from insurance

1 than anticipated, or FPL's costs are underestimated, FPL would charge the
2 additional costs to the Reserve.

3
4 **SUMMARY**

5 **Q. Please summarize your testimony.**

6 A. FPL's Turkey Point and St. Lucie nuclear power plant sites incurred
7 approximately \$40.9 million in total costs from the 2005 Hurricane Season,
8 approximately \$23 million of which FPL expects to recover from its NEIL
9 insurance policy. The majority of the costs are attributed to Hurricane Wilma,
10 with the exception of \$538,000 in storm preparation costs at the Turkey Point
11 nuclear plant site for Hurricanes Katrina and Rita. The total amount of costs FPL
12 seeks to recover in this proceeding is \$17.9 million. Nuclear storm-related costs
13 were exacerbated because St. Lucie Unit 1 was in the middle of a refueling outage
14 when Hurricane Wilma threatened that site. Therefore, FPL had to take extensive
15 measures to secure the Unit in anticipation of the hurricane. In addition, there
16 was damage to the beach dunes that are critical to the safe operation of the St.
17 Lucie plant site, which also increased the amount of storm-related costs.

18 **Q. Does this conclude your direct testimony?**

19 A. Yes.

1 BY MS. SMITH:

2 Q Mr. Warner, would you please provide a summary of
3 your Direct Testimony to the Commission?

4 A Yes. Good morning.

5 My testimony provides an explanation of the impact
6 the 2005 storm season had on the St. Lucie and Turkey Point
7 nuclear facilities. It also describes the preparation required
8 for the potential onset of hurricanes and tropical storms and
9 the damaged sustained from Hurricane Wilma at the two
10 facilities.

11 Hurricane Wilma affected the operations of both
12 St. Lucie and Turkey Point nuclear sites. This resulted in
13 Turkey Point Units 3 and 4 and St. Lucie Unit 2 being taken
14 off-line prior to the onset of hurricane force winds at the
15 sites. This is required by the Nuclear Regulatory Commission
16 to comply with our license and to meet the station blackout
17 requirements. St. Lucie Unit 1 was already off-line for a
18 planned refueling outage when Hurricane Wilma threatened the
19 site.

20 Additional time was necessary to demobilize equipment
21 and material that was staged for outage work and to safely
22 secure the unit before the storm made landfall. For example,
23 large cranes were dismantled and heavy equipment was required
24 to be moved and secured. Numerous site personnel were involved
25 in completing these tasks in a short time frame before the

1 storm arrived.

2 Hurricane Wilma damaged numerous structures and
3 facilities at the St. Lucie site, including damaging several
4 power block systems and the intake and discharge canals. In
5 addition, the wave and the storm surge from Hurricane Wilma
6 significantly eroded the height and the width of the dunes
7 adjacent to the St. Lucie plant and damaged the vegetation that
8 protects the dunes. The dunes must be repaired to ensure flood
9 protection during future storms and to comply with our site
10 licensing requirements. Damage at Turkey Point included damage
11 to our power block systems, critical plant equipment such as
12 water intrusion in motors, electrical switch gear, fire
13 protection seals, and numerous buildings and other facilities.

14 St. Lucie and Turkey Point facilities incurred \$17.4
15 million and \$23.5 million worth of damage respectively,
16 totalling \$40.9 million. FPL expects to recover approximately
17 23 million from its Nuclear Electric Insurance Limited
18 insurance policy. The storm-related cost request is
19 17.9 million net insurance. If more costs are recovered from
20 insurance, then FPL would contribute that amount to the reserve
21 to pay for future storm costs.

22 This concludes my summary.

23 BY MS. SMITH:

24 Q Mr. Warner, have you also prepared and caused to be
25 filed eight pages of Prefiled Rebuttal Testimony in this

1 proceeding?

2 A I have.

3 Q Do you have any changes or revisions to your Prefiled
4 Rebuttal Testimony?

5 A I do not.

6 Q If I asked you the same questions contained in your
7 Prefiled Rebuttal Testimony today, would your answers be the
8 same?

9 A Yes, they would.

10 MS. SMITH: Madam Chairman, I would ask that Mr.
11 Warner's Prefiled Rebuttal Testimony be inserted into the
12 record as though read.

13 CHAIRMAN EDGAR: The Prefiled Rebuttal Testimony from
14 this witness will be entered into the record as though read.

15 BY MS. SMITH:

16 Q Mr. Warner, are you also sponsoring Exhibits MW-2 and
17 MW-3 to your rebuttal testimony?

18 A I am.

19 MS. SMITH: And these have been identified as Exhibit
20 Numbers 109 and 110 and moved into the record yesterday. We
21 have distributed a confidential version of MW-2, and this needs
22 to be marked. The confidential version still needs to be
23 entered into the record.

24 CHAIRMAN EDGAR: This will be marked as Exhibit 144.

25 Ms. Smith, a title.

1 MS. SMITH: Confidential 2004 Nuclear Estimate of
2 Noninsured Storm Damage.

3 CHAIRMAN EDGAR: Thank you.

4 (Exhibit 144 marked for identification.)

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1 **BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**
2 **FLORIDA POWER & LIGHT COMPANY**
3 **REBUTTAL TESTIMONY OF MARK WARNER**
4 **DOCKET NO. 060038-EI**
5 **APRIL 10, 2006**

6
7 **Q. Please state your name and business address.**

8 A. My name is Mark Warner. My business address is 700 Universe Boulevard,
9 Juno Beach, Florida 33408-0420.

10 **Q. Did you previously submit direct testimony in this proceeding?**

11 A. Yes.

12 **Q. Are you sponsoring an exhibit in this case?**

13 A. Yes. I am sponsoring an exhibit consisting of two documents, Document Nos.
14 MW-2, and MW-3, which is attached to my rebuttal testimony.

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

16 A. The purpose of my testimony is to rebut certain positions taken in this case by
17 Donna DeRonne for the Office of Public Counsel related to the following
18 issues she raised in her testimony:

- 19 • The removal of \$21.5 million of 2004 storm recovery costs for damage
20 to the St. Lucie nuclear plant site;
- 21 • The removal of \$2,490,800 of 2005 storm recovery costs associated
22 with nuclear employee base salaries; and

- 1 • Imposing a cut-off date of December 31, 2006 for charging 2005 storm
2 restoration costs to the Reserve.

3 I also respond to the Florida Public Service Commission Staff (Staff) Audit
4 Finding Number 6: Nuclear Storm Preparation Costs sponsored by Staff
5 witness Kathy Welch.

6

7

2004 Nuclear Storm Costs

8 **Q. Ms. DeRonne asserts the estimated 2004 storm recovery costs for**
9 **“Various Nuclear Storm Damages” should be removed since it is an**
10 **estimate and may be offset by insurance recoveries. Do you agree?**

11 **A.** No. A \$21.5 million disallowance is inappropriate for two reasons. First, the
12 accrual for the remaining nuclear division costs from 2004 represents the
13 amount FPL expects will not be covered by insurance. Based on experience
14 and work with our insurer, Nuclear Electric Insurance Limited (NEIL) related
15 to FPL’s storm losses, it is reasonable to expect that NEIL will not cover all of
16 FPL’s loss for a number of reasons. These reasons include differences in
17 scope of work to be completed, property outside the NEIL insurance boundary
18 and policy limits. Second, a \$21.5 million disallowance is inappropriate
19 because FPL adjusted the amount of its accrual for 2004 remaining work in
20 March 2006 as a result of meetings with NEIL regarding its 2004 claim. The
21 accrual amount has been reduced to \$15.35 million.

22

1 Q. Ms. DeRonne asserts the estimated 2004 storm recovery costs for
2 “Various Nuclear Storm Damages” should be removed since work for the
3 St. Lucie nuclear plant intake canal restoration “appear to be costs
4 beyond those that were presented in the prior case after July 31, 2005.”
5 Do you agree?

6 A. No. The estimated 2004 storm recovery costs for nuclear storm damages is a
7 function of the amount of insurance that FPL expects to receive for the 2004
8 storm season. It was comprehended within FPL’s filing that uninsured
9 amounts would be charged to the Reserve.

10 Q. Could FPL have made all of the repairs to the St. Lucie nuclear plant site
11 prior to July 31, 2005?

12 A. No. Refueling outages only occur once in approximately every 18 months,
13 and only one of the two units at the St. Lucie plant site had a refueling outage
14 prior to July 2005. Refueling outages are required in order to do detailed
15 inspections of the storm damage to our power block. The repairs are then
16 made in subsequent refueling outages.

17

18 Second, over fifty buildings sustained some measure of hurricane damage. It
19 was not possible to repair this magnitude of damage to all the structures prior
20 to July 31, 2005.

21

1 Third, there was substantial damage to the intake and discharge canals. We
2 had to ensure that FPL and NEIL agreed on the scope of damage prior to
3 commencing work due to the significant costs involved.

4

5 **Q. Why did FPL adjust the accrual for 2004 nuclear division repairs related**
6 **to the 2004 storm season?**

7 A. FPL met with NEIL's adjuster and NEIL's subject matter experts on March 9,
8 2006 at which time the NEIL adjuster agreed that NEIL would cover the
9 repair of the damaged intake and discharge canals at the St. Lucie Plant Site
10 all the way to the bottom of the canals. Previously, the NEIL subject matter
11 experts had indicated that they would only recommend coverage for repairs
12 down to approximately eleven feet below the surface. This change in NEIL's
13 position resulted in a \$5 million increase in the estimated insurance recovery
14 and a corresponding \$5 million reduction in FPL's estimate of uninsured
15 repairs. FPL has also made a \$1 million downward adjustment in the
16 estimated uninsured cost for dredging the canals based upon the March 9,
17 2006 meeting.

18 **Q. What types of repairs make up the remaining accrual of \$15.35 million at**
19 **the St. Lucie plant site related to the 2004 storm season?**

20 A. As shown on Document MW-2, the remaining repairs are associated with
21 repairs to the intake and discharge canals, repair of coatings in various areas
22 of the plant, canal dredging, supervision costs over the two percent insurance
23 cap and damage to facilities outside the NEIL insurance boundary. These

1 repairs are necessary to restore the nuclear units back to pre-storm condition
2 and to ensure the long term reliability of plant operations. For example, if
3 FPL does not repair the intake and discharge canals, the unit may not be able
4 to operate due to inadequate cooling. The repair of coatings is necessary to
5 prevent degradation of the equipment.

6

7 The \$15.35 million is a reasonable estimate of the amounts FPL expects NEIL
8 will not cover based on extensive internal review, as well as discussions with
9 NEIL and third-party contractors and vendors. To the extent FPL recovers
10 more from NEIL than it expects, we will credit the Reserve accordingly.

11

12

2005 Nuclear Storm Costs

13 **Q. Ms. DeRonne asserts that \$2,490,800 of nuclear employee base salaries**
14 **should be removed from FPL's requested recovery amount since FPL**
15 **expects to recover this amount from insurance. Do you agree?**

16 **A. No.** The \$2,490,800 is not part of the \$17.9 million of nuclear division storm
17 costs requested for recovery in this proceeding. Therefore, this amount should
18 not reduce FPL's storm costs since it is not a part of those costs.

19 **Q. Ms. DeRonne argues in favor of a cut-off date of December 31, 2006 for**
20 **charging the 2005 storm restoration costs to the reserve. Is this feasible**
21 **or appropriate for the nuclear storm repairs?**

22 **A. No.** FPL should be able to charge storm expenses through 2008 when it is
23 anticipated all repairs for storm related damage will be completed. After a

1 storm strikes, FPL's priority is to return the low cost nuclear units back to
2 service as safely and quickly as possible. The units can sometimes be brought
3 back online without repairing all storm-related damage. However, these
4 repairs are still critical to ensure the long term reliability of plant operations
5 and must be made at the earliest possible opportunity. Again, due to the
6 nature of nuclear operations, it may take several years to restore the nuclear
7 plants to pre-storm condition. Damage assessment and repairs to certain
8 equipment can only be performed during refueling outages which occur
9 approximately every 18 months. For example, certain motors can only be
10 inspected when the unit is shut down, then the work would have to be planned
11 for and completed in the subsequent refueling outages. Furthermore, the
12 NEIL insurance process is a long process that involves FPL and NEIL jointly
13 working to identify the damage scope and cost, repairing the equipment,
14 submitting the claim and the NEIL audit of the claim. It is not feasible to
15 complete all of these tasks prior to December 31, 2006.

16 **Q. Document No. GJW-10 in Geisha J. Williams' rebuttal testimony**
17 **addresses remaining work to be completed. Please discuss the Nuclear**
18 **Division items included in this exhibit.**

19 A. First, FPL estimates \$3.2 million to restore the dunes that are adjacent to the
20 St. Lucie Plant site. As addressed in my direct testimony, FPL is required to
21 maintain the dunes as part of its plant license. This \$3.2 million amount was
22 derived from a bid proposal from a third party. The restoration work on the
23 dunes could not be completed until after turtle nesting season as required by

1 federal and state governments. Turtle nesting season ends October 31, 2006
2 and FPL plans to begin work in November 2006. In addition, there are
3 amounts included in the exhibit which may not be covered by the NEIL
4 insurance policy for various reasons (e.g. storm damage outside the NEIL
5 boundary line, NEIL limitations on payment for certain costs such as
6 supervision, insurance deductible, etc.). FPL will continue with the claim
7 process as restoration work is completed until the NEIL insurance claim is
8 completely resolved. FPL expects to have all of the 2005 nuclear site damage
9 repaired by 2008. Once the claim process is complete, FPL will credit the
10 Reserve to the extent it recovers more from insurance than it expects.

11 **Q. How much of the Nuclear Division 2005 storm restoration costs charged**
12 **to the reserve are based on actual costs or third party proposals?**

13 A. Over 80 percent of 2005 storm expenses requested for recovery are based on
14 actual costs or third party proposals. Only \$3.1 million of the \$17.9 million
15 requested for recovery relates to estimated amounts FPL expects the NEIL
16 insurance policy will not cover. The rest of the \$17.9 million – related to
17 storm preparation costs, deductibles, and the dunes – are actual or known
18 amounts.

19

20

21

22

23

2005 Nuclear Storm Preparation Costs

1

2 **Q. Ms. Welch asserts “if the Commission decides that storm preparation**
3 **costs should be excluded, the nuclear storm preparation costs of**
4 **\$10,052,336.46 should be excluded.” Do you believe that the nuclear**
5 **storm preparation costs should be excluded?**

6 A. No. Storm preparation activities are necessary to safeguard nuclear power
7 plants and facilities. This is an extraordinary expense and is necessary in order
8 to minimize damage resulting from the storm. For example, if FPL had not
9 taken steps to prepare St. Lucie for the onset of the hurricane force winds,
10 scaffolding and cranes used for the Unit 1 refueling outage could have
11 severely damaged the power plant. This could have resulted in a substantial
12 delay of the refueling outage and the subsequent restart of the unit back to
13 service.

14 **Q. Do you have any concerns regarding Ms. Welch’s calculation of storm**
15 **preparation costs?**

16 A. Yes. As shown in Document No. MW-3, the \$10,052,336.46 in nuclear storm
17 preparation costs includes approximately \$1.7 million of regular payroll. This
18 \$1.7 million in regular payroll is also counted in Audit Finding No. 1,
19 addressing regular payroll. It should not be counted twice.

20 **Q. Does this conclude your rebuttal testimony?**

21 A. Yes.

1 BY MS. SMITH:

2 Q Mr. Warner, would you please provide a summary of
3 your rebuttal testimony to the Commission.

4 A I will, thank you.

5 My rebuttal testimony rebuts certain positions taken
6 in this case by Donna DeRonne for the Office of Public Counsel.
7 Specifically, I rebut the removal of 21.5 million of 2004 storm
8 recovery costs for damage to the St. Lucie Nuclear Plant site,
9 the removal of \$2,490,800 of the 2005 storm recovery costs
10 associated with nuclear employee-based salaries, and imposing a
11 cut-off date of December 31st, 2006, for charging the 2005
12 storm restorations cost to the reserve. I also rebut the
13 Florida Public Service Commission Staff Audit Finding Number 6
14 related to nuclear storm preparation costs sponsored by Staff
15 Witness Kathy Welch.

16 The \$21.5 million accrual for the remaining nuclear
17 division costs from the 2004 storms have been reduced to
18 15.35 million in March of 2006 as a result of meeting with
19 Nuclear Electric Insurance Limited, or NEIL, regarding FPL's
20 2004 insurance claim. This amount represents what FPL expects
21 will not be covered by insurance, and should be recovered
22 through the storm charge. The 2004 repairs are necessary to
23 restore the units back to prestorm conditions and to ensure the
24 long-term reliability of plant operations.

25 It was not feasible to complete the nuclear repairs

1 prior to July 31st, 2005. After a storm strikes, FPL's
2 priority is to return the low-cost nuclear units back to
3 service as safely and quickly as possible. The units can
4 sometimes be brought back online without repairing all
5 storm-related damage. However, these repairs are still
6 critical to ensure the long-term reliability of plant
7 operations and must be made at the earliest possible
8 opportunity.

9 Damage assessment and repairs to certain equipment
10 can only be performed during refueling outages which occur
11 approximately every 18 months. Furthermore, the NEIL insurance
12 process is a long process that involves FPL and NEIL jointly
13 working to identify the damage scope and cost, repairing the
14 equipment, preparing the claim, and the NEIL audit of the
15 claim.

16 Further, the \$2,490,800 of nuclear employee-based
17 salaries that the Office of Public Counsel proposes to disallow
18 because FPL expects to recover these amounts from insurance
19 should not be removed from FPL's requested storm costs, since
20 this amount has not been charged to the reserve and therefore
21 is not included in FPL's requested storm costs.

22 In regard to the December 31st, 2006, cut-off date
23 for the 2005 storm costs proposed by the Office of Public
24 Counsel, it is not feasible for FPL to complete all necessary
25 storm repairs by this date for the reasons previously

1 discussed. FPL should be able to charge storm expenses through
2 2008 when it is anticipated all repairs for storm-related
3 damage will be completed. Also, storm preparation activities
4 should not be excluded from the storm reserve. Storm
5 preparation activities are necessary to safeguard the nuclear
6 power plants and facilities.

7 This is an extraordinary expense, and is necessary in
8 order to minimize damage resulting from the storm. Additional
9 damage resulting from unsecured equipment could have resulted
10 in a substantial delay of the refueling outage, and the
11 subsequent restart of the unit back to service.

12 This concludes my rebuttal summary.

13 MS. SMITH: The witness is available for
14 cross-examination.

15 CHAIRMAN EDGAR: Thank you.

16 Mr. Beck.

17 MR. BECK: Thank you, Madam Chairman.

18 CROSS EXAMINATION

19 BY MR. BECK:

20 Q Hello, Mr. Warner. I'm Charlie Beck with the Office
21 of Public Counsel.

22 A Good morning.

23 Q Mr. Warner, could you turn to Page 10 of your
24 testimony, please.

25 A Yes.

1 Q And I'm referring to your direct testimony.

2 A Yes.

3 Q At the top of Page 10 you are asked to describe the
4 storm damage from Hurricane Wilma sustained at the St. Lucie
5 nuclear site. Do you see that?

6 A Yes.

7 Q And at Lines 12 and 13 as part of your answer you
8 describe that the intake and discharge canal sustained damage
9 to the side walls?

10 A Correct.

11 Q And that is as a result of Hurricane Wilma?

12 A That's correct.

13 Q And Hurricane Wilma was in October of 2005, is that
14 right?

15 A That is correct.

16 Q Could you describe whether the intake and discharge
17 canals had any structures or reinforcements in place to help it
18 withstand the winds from a hurricane?

19 A No, they did not. They had the -- the actual intake
20 and discharge canals are a culvert which is excavated at the
21 start of construction and they are reinforced with rock and
22 various, I'll call it riprap (phonetic). And those things are
23 which line the edges of the canal. And those are the
24 protection that we have for the canal itself, excuse me, for
25 the discharge, yes.

1 Q What was the damage, then, that was sustained to the
2 side walls?

3 A What actually has occurred is when the storm comes
4 through, it actually evacuates, if you will, it takes the water
5 and then also it takes the actual rock and so forth and
6 displaces it and either will remove it totally, or move it down
7 into the center of the canal itself. And then the problem with
8 that is then it limits the amount of intake cooling water that
9 we have to the structure, so therefore it requires dredging
10 of those intake and discharge canals. And in addition to that,
11 then you would have the erosion that would take place where the
12 rock has been displaced.

13 Q And has FPL started or engaged in the dredging that
14 you just described to fix --

15 A We have done some dredging, but the actual repairs
16 themselves have not taken place yet due to the extensive damage
17 and the costs associated, and also us working closely with NEIL
18 to determine the scope and the actual cost of the repair.

19 Q I have an exhibit I would like to show you. I'm
20 going to ask that that be passed out.

21 MR. BECK: Madam Chair, I would like to ask that this
22 exhibit be marked as an exhibit for identification.

23 CHAIRMAN EDGAR: Thank you. This will be Exhibit
24 145. Mr. Beck, a title?

25 MR. BECK: Port St. Lucie intake canal analysis.

1 CHAIRMAN EDGAR: Thank you.

2 (Exhibit 145 marked for identification.)

3 BY MR. BECK:

4 Q Mr. Warner, do you recognize the exhibit I have just
5 passed out?

6 A No, I do not.

7 Q You have never seen this document before?

8 A No, I have not. But that's okay.

9 Q Let me ask you to see if you are knowledgeable about
10 any of the things that are in there, if I could?

11 A Okay.

12 Q Are you familiar with an analysis that was done by
13 Austin AECOM?

14 A No, I'm not.

15 Q Are you familiar with any analysis that had been done
16 about the work that would be required to repair the canals?

17 A Yes, I'm familiar with the discussions that we have
18 had with NEIL around the scope and cost of the repairs for the
19 intake and discharge canals.

20 Q It's your testimony, is it not, that the canals were
21 damaged by Hurricane Wilma in 2005?

22 A That is correct. And also by hurricanes in 2004,
23 also, that's correct.

24 Q In your direct testimony, let me go back to that if I
25 could for a second, on Page 10 where we were discussing it

1 before --

2 A Yes.

3 Q -- on Line 16 you say that the estimated total costs
4 for storm damage at the St. Lucie site is \$10.6 million, do you
5 see that?

6 A Yes, I do see that.

7 Q And does that include your estimates for repairing
8 the intake and discharge canals at Port St. Lucie?

9 A No, it does not. And let me expand on that. When we
10 sat down with the NEIL insurers, because it was very difficult
11 to differentiate between the storm damage in '04 and the storm
12 damage in '05, what we worked through with NEIL is that we
13 would do the total repairs for the canals for the intake and
14 discharge structures, because it was very hard to differentiate
15 what was storm damage that occurred in '04 versus what was
16 storm damage that occurred in '05.

17 Q I thought earlier you told me that the damage was
18 done in 2005 to the side walls?

19 A Continuation of the damage had occurred, that is
20 correct, in '05.

21 Q Well, explain to me what occurred in '04 and what
22 occurred in '05 --

23 A It was very hard to differentiate between the damage
24 between '04 and '05. And, again, we had the most knowledgeable
25 people out there, and it was their conclusion, also, that in

1 order to try to differentiate between this is the claim for '04
2 and this is the claim for '05 would be very difficult.
3 However, we do know that prior to the '04 season this was the
4 condition of the canals, intake and discharge, and the fact
5 that these two hurricanes have, in fact, caused this damage
6 that needs to be restored to bring it back to the pre-storm
7 conditions, and for us to be able to ensure continued long,
8 reliable operation of the unit.

9 Q So part of the damage to the canals was done in 2004
10 and part was done in 2005, is that your testimony?

11 A Correct.

12 Q And in your estimate you give in your testimony for
13 the total -- I guess you say the estimated total cost for storm
14 damage to the St. Lucie site is \$10.6 million. You have not
15 included any of the damage that was done to the canals in 2005?

16 A That is correct, that is my understanding.

17 Q What work did Florida Power and Light do after the
18 2004 storms and before the 2005 season to repair the canals?

19 A We did no work due to the extensive damage and the
20 particular cost that was going to be involved, and we worked
21 closely with NEIL to expeditiously work through the NEIL
22 process, which I described earlier as a very long process in
23 order to say, okay, what are the things we need to do to return
24 it back to pre-storm conditions.

25 Q Did you have any contractors come in before the 2005

1 storm season to provide you estimates of what if it would cost
2 to repair the canals?

3 A We had our people do -- the process, the way it works
4 is we go forth and put together what our estimates are, then we
5 bring NEIL out and they go through their damage assessment
6 looking at scope and cost, and we then agree upon what the
7 scope should be, and then we go out for third-party estimates.

8 Q And did you do the third-party estimates before the
9 2005 season?

10 A No.

11 Q So whatever damage that was done during the 2004
12 season, it wasn't sufficient damage to cause Florida Power and
13 Light to get a contractor to come in and give an estimate of
14 the repairs?

15 A We actually did some dredging prior to the '05
16 season. But to your point, we did not have somebody come in
17 and do a third-party estimate as to what it would take to
18 repair the intake and discharge canal. Again, the damage was
19 so extensive that we needed to engage NEIL to understand what
20 the actual cost and scope was going to be of the repairs.

21 Q Did it effect the operation of the plant after the
22 2004 storms, but before the 2005 storm season?

23 A No, we did some dredging to allow us to ensure we
24 weren't going have any issues with the cooling at that time.
25 But, again, when we talk about storm damage, as I stated

1 earlier, when we first go through the initial storm assessments
2 following a hurricane, we ensure that we can restart the unit
3 and we do the necessary repairs to get the unit back on line.
4 More extensive damages that are not an immediate threat to the
5 unit are then planned and executed, going through a detailed
6 analysis of what needs to be done. So, clearly, you know, we
7 ensure that the unit is ready for restart, and then we want to
8 make sure that we do the right thing in terms of detailed
9 planning and analysis to ensure that we are doing a
10 cost-effective repair for the damage that occurred as a result
11 of the hurricanes.

12 Q But, in any event, you were able to operate the plant
13 after the 2004 storms up to the 2005 season without even
14 bringing in a contractor to give you an estimate for the
15 damage?

16 A That is correct.

17 Q Is the plant operating now?

18 A Yes, both plants are operating now. One will be
19 coming down for a refueling outage this weekend.

20 Q So you are able to operate the plants with the canals
21 even in their current state?

22 A Correct. And I just want to add, again, I think the
23 point I want to make is after the storms we turn around and we
24 ensure that we can safely restart the units, and we do the
25 immediate repairs that are necessary. The repairs that we are

1 talking about are to ensure the long-term reliability of the
2 units. And that has been our approach. There is no reason for
3 us to hold the unit down for an extended period of time to do
4 extensive inspections and damage assessment. It is not in the
5 best interest of our customers to go ahead and do that. It is
6 more advantageous for us to plan it out, perform the work
7 during the refueling outage, and then also to make sure that we
8 have good third-party bids before we execute the work.

9 Q FPL is requesting that all of the costs associated
10 with repairing the intake canal that haven't even been incurred
11 yet be charged against the 2004 storm season, is that right?

12 A No, that is not correct.

13 Q Would you correct it for me, please.

14 A Yes. If you take a look at the exhibit -- I guess it
15 would be best for us to go to the rebuttal testimony, and I
16 guess it would be best to look at the confidential version, not
17 the redacted version. For clarity, we're talking about the '04
18 storm damage, is that correct?

19 Q Right.

20 A I just wanted to be sure.

21 Q Go ahead.

22 A And if you take a look in there you will see that
23 there is a portion of the amount that we are asking for
24 recovery of the 15.35 million which is associated with repairs
25 to the intake and discharge canal embankments that will not be

1 covered by insurance.

2 Q I didn't ask the question correctly.

3 A I'm sorry.

4 Q Part of the cost is being reimbursed by insurance to
5 repair the canals?

6 A A large portion of it is being reimbursed by NEIL
7 insurance, that's correct.

8 Q And you show the portion that is not covered by
9 insurance in your Exhibit MW-2?

10 A That is correct.

11 Q Of the portion that is not being covered by
12 insurance, what portion is being charged to 2004, and what
13 portion is being charged to 2005?

14 A All of it is being charged to the 2004.

15 Q And in your testimony you state and you have
16 testified today that part of the damage was caused by the 2005
17 storm?

18 A That is correct.

19 Q I want to know why you haven't allocated a portion of
20 it to 2005?

21 A Again, I think we talk about the complexity of trying
22 to differentiate between the damage that occurred in '04 and
23 '05. The damage in '04 was much more extensive. But trying to
24 be able to segregate thousands and thousands and thousands of
25 feet of the discharge canal under the water and saying this is

1 '04 damage, this is '05 damages, it would be very difficult to
2 do that. And, quite frankly, I think that it probably wouldn't
3 be a good use of anyone's time.

4 Q Mr. Warner, let me ask you about a few statements
5 that are contained in the document that has been labeled
6 Exhibit 145 for identification.

7 A Which one?

8 Q I guess it's by your right hand.

9 A Thank you.

10 Q I want to ask if you have any personal knowledge of
11 some of the matters discussed in there. Do you see the section
12 under intake canal, the first page after the cover?

13 A Yes.

14 Q And in the second paragraph it states that the
15 eastern end of the canal has been armored with filter point,
16 fabric formed concrete matting. Do you see where it says that?

17 A I see that, uh-huh.

18 Q Do you know whether that statement is true or not?
19 Has there been concrete matting on the canal?

20 A I do not have personal knowledge of that, but that is
21 my understanding of what the design is, that's correct.

22 Q Do you know whether there has been any kind of
23 armoring or refortification on the canal prior to the
24 hurricanes?

25 A No, not that I am aware of.

1 Q What you are proposing to do is to add some sort of
2 protection along the sides of the canal, is that not right?

3 A What we are proposing to do is to restore the canals
4 to the prestorm condition. Now, one of the difficulties we
5 have is to be able to bring repairs in to make the damaged
6 portion match up with the existing portions that hasn't been
7 damaged. So what I mean by that is there is going to be a
8 transition where certain portions of the canals are not
9 required to be repaired, and then you are going to have to
10 repair another section. So what is going to happen is you have
11 this linear section that is going to be damaged, and is going
12 to go from damaged to moderately damaged to no damage, and the
13 transition piece is going to be difficult in terms of
14 understanding what the repair is going to be.

15 Q Again, referring to that section of the document on
16 intake canal, but this time the last paragraph.

17 A Yes.

18 Q It says that Florida Power and Light proposed
19 repairing the canal by dredging it and restoring the banks to
20 their initial dimensions and revetting the sides with concrete
21 mat. Do you see that?

22 A Yes.

23 Q Could you describe what it thens to revet the sides
24 with concrete mat?

25 A Yes. This would be a portion of putting down rebar

1 over the existing structure and then going ahead and putting a
2 concrete filler between the rebar to reinforce the sides of the
3 canal and to make sure that they are repaired back to prestorm
4 conditions.

5 Q Well, I thought you told me earlier that there was no
6 sort of concrete or mats in the canal previously?

7 A True. But this is a repair method which we are going
8 to undertake which NEIL agrees with.

9 Q So will this be an improvement over the way the
10 canals were previously?

11 A No, it wouldn't be an improvement, it is the repair
12 technique that we need to do to ensure that the structural
13 sides of the canal are sound.

14 Q So before you just had rocks along the side of the
15 canal?

16 A That's correct. There was a culvert with layers of
17 rock, that's correct.

18 Q And your repairs proposed to -- instead of having
19 just rocks, you're going to have concrete mats placed along the
20 sides of the canal?

21 A That's correct, over portions -- that's correct.

22 Q How long do you think that -- replacing the concrete
23 mats, how long will that last, how long will it be good for?

24 A How long will they last?

25 Q Yes.

1 A They should last for the life of the plant.

2 Q And how many years would that be?

3 A Presently we just filed for license renewal, so let
4 me quickly do the math. About another thirty years.

5 Q So you would expect the work that is going to be done
6 will benefit the plant over the next thirty years, is that
7 right? Will be a benefit to the plant --

8 A It would be a benefit to bring the plant back to its
9 pre-storm conditions, correct.

10 MR. BECK: Thank you, Mr. Warner, that's all I have.

11 THE WITNESS: Thank you.

12 CHAIRMAN EDGAR: Mr. Wright.

13 MR. WRIGHT: Thank you, Madam Chairman, I just have a
14 few questions for this witness.

15 CROSS EXAMINATION

16 BY MR. WRIGHT:

17 Q Good morning, Mr. Warner.

18 A Good morning.

19 Q I have just a few questions for you about your
20 Exhibit 144 and about your rebuttal testimony at the bottom of
21 Page 4. My questions, generally speaking, relate to the total
22 costs and the supervision costs and how the insurance cap
23 works. So with that in mind, I'll proceed.

24 A Okay.

25 Q Did I get it right, in your summary you said that you

1 expect NEIL to pay something like 17.9 million in insurance
2 proceeds?

3 A For which storm? If we are talking for -- I'm sorry.

4 Q Help me out. I just heard the number, and I wasn't
5 sure which was which?

6 A In my direct testimony I was talking about 2005,
7 which would be 17.9 million.

8 Q Right. How about for 2004 as it would relate to the
9 nonconfidential number of 15.35 million that is shown on your
10 Exhibit 144?

11 A Your question is what portion -- please rephrase your
12 question to make sure I'm answering your question.

13 Q I understand the \$15.35 million number there to be
14 net of insurance proceeds, is that accurate?

15 A That's correct.

16 Q What is the corresponding insurance payment that
17 would be added to that to get an idea of the total charges to
18 the storm reserve absent the insurance proceeds?

19 A Total to the storm reserve?

20 Q Right.

21 A Right now it would be this 15.35 million that we see
22 in Exhibit MW-2, and we have already booked an additional 15
23 million previous to this. So it would be a total of
24 approximately 30 million.

25 Q And would I correctly infer then that you expect NEIL

1 to pay or NEIL has paid something like that other 15 million?

2 A No, I think I just need to back up a second. The
3 actual NEIL -- the actual portion of the NEIL claim that we
4 expect to file will be in the vicinity of \$108 million.

5 Q For 2004?

6 A For 2004, that's correct.

7 Q Thank you.

8 A And we believe that 15.35 million will not be covered
9 by NEIL.

10 Q Thank you. That is helpful. Understanding that the
11 supervision cost number shown there is confidential, what I
12 wanted to ask you is what the total supervision costs were, and
13 understanding that that number is also probably confidential,
14 if you could perhaps give it in terms of a multiple of the
15 value that is shown in your table, that would be a help to us?

16 A Instead of trying to give you a number, let me try it
17 this way, because I think when we get into insurance it gets a
18 little bit complicated.

19 MR. WRIGHT: Madam Chairman, if I could, what I was
20 trying to get at right now is just what the total supervision
21 cost is, and then I want to go on and ask you about --

22 A (Continuing) Okay. The total supervision cost that
23 is part of this insurance cap is exactly the number you see
24 here in MW-2.

25 Q Okay. So there is no part of the supervision costs

1 that is covered by the insurance the way you have accounted for
2 it?

3 A Correct. That is why I wanted to elaborate. Let me
4 do that. Anything that is a directly related cost with the
5 repair of the facilities is covered under the NEIL insurance
6 claim. NEIL restricts the amount of what I'll call indirect
7 costs which is associated with things like certain layers of
8 supervision, levels of supervision, people who are involved in
9 the budgeting and the scheduling and so forth. Things that do
10 not directly perform the repairs, they put a two percent cap on
11 it. This number reflects what we expect that NEIL will not
12 cover to do these repairs for '04, and they are called indirect
13 or supervision costs.

14 Q Thank you. And the two percent is two percent of
15 what?

16 A It's two percent of the total direct cost.

17 Q Thank you. How was the confidential number shown
18 there as the supervision costs calculated? For example, is
19 that actual booked costs; is it a number that is calculated by
20 an FPL corporate overhead computer program or -- help me out.
21 Help us out.

22 A You're talking about this supervision cost over two
23 percent insurance cap?

24 Q Yes, sir.

25 A We take a look at the total cost of the claim and

1 what portion of that would be attributable to these people's
2 salaries, you know, and so forth, and that is how we calculate
3 it. And that is done by us and also then would also be vetted
4 with NEIL. Again, this would all be part of the negotiation
5 process about what is actually covered and what is not.

6 Q I understand.

7 A And I will just add that we will, we always do
8 present it as we want it to be recovered under insurance, and
9 then we ask, and then NEIL would then turn around and tell us
10 what would not be covered, and we negotiate with them.

11 Q I think I just have one or two more clarifying
12 questions, Mr. Warner.

13 You just made reference to looking at the supervisory
14 personnel's actual salaries. Would I be correct to understand
15 that you look at their salaries and allocate part of their
16 salaries to the supervision function and then book that to
17 here?

18 A Yes.

19 Q I'm really trying to ask the next question just as a
20 factual question, not in any manner to be argumentative. But
21 do you make any adjustment along the lines of trying to
22 identify incremental salary costs, or do you just book part of
23 their actually salary cost to the activity?

24 A This is actually -- this dollar value that you see
25 here is associated -- we go out and do the damage assessment

1 and what it will actually cost to perform the repairs. And
2 from that we know what type of supervision will need to be
3 involved, whether it be the budgeting people, the second line
4 supervisor, whatever. And we know what that cost is, and then
5 we back it out, and this is the number that you see here. So,
6 it is the actual estimate of what it is going to take to repair
7 the units and bring them back to prestorm condition.

8 Q Just to be clear, if you have got a supervising
9 engineer who is paid an annual salary of \$125,000, do you take
10 part of that \$125,000 based on how many hours his or her time
11 is going to be spent working on the job and book that into that
12 number?

13 A Not being a total accountant, I can only tell you how
14 we fix stuff at the plant. So I will try it the other way. We
15 know that if we are going to do a particular job and it is
16 going to require 40 hours of this particular supervisor or
17 budget person's time, then that time is then calculated and put
18 against this number.

19 MR. WRIGHT: Thank you very much.

20 That's all I have. Thanks.

21 CHAIRMAN EDGAR: Nothing from FIPUG.

22 Captain Williams. No.

23 Mr. Kise?

24 MR. KISE: No questions.

25 CHAIRMAN EDGAR: Mr. Twomey?

1 MR. TWOMEY: No, ma'am.

2 CHAIRMAN EDGAR: Thank you. Questions from staff?

3 MR. KEATING: Yes, just a couple of questions.

4 CROSS EXAMINATION

5 BY MR. KEATING:

6 Q Good morning, Mr. Warner.

7 A Good morning.

8 Q Does FPL periodically dredge the intake canals at St.
9 Lucie?

10 A I'm not sure. I know we dredged it recently. I
11 don't have the history of whether we periodically dredge.

12 Q Do you know when FPL dredges, what the cost of that
13 dredging would be?

14 A In this particular case, the most recent dredging we
15 did, I believe, was in the tune of approximately one and a half
16 million dollars.

17 Q Do you know how those dredging expenses are recovered
18 by FPL?

19 A In this particular case, when we did the dredging for
20 '04, it was included in the actual -- the estimate that you see
21 here for the repair and the dredging of the canals. And at
22 this point it is my understanding that that particular amount
23 was charged against the 2004 storm reserves.

24 Q And just to be clear, you don't know if FPL
25 periodically dredges those canals?

1 A I know we do routine maintenance at the plant. I
2 just can't tell you from a first-hand knowledge when the last
3 time that we actually dredged those intake and discharge
4 canals.

5 MR. KEATING: Thank you.

6 CHAIRMAN EDGAR: Commissioners? Mr. Keating, I did
7 understand that that was your last question?

8 MR. KEATING: Yes. Thank you.

9 CHAIRMAN EDGAR: Ms. Smith.

10 MS. SMITH: Just a few. Thank you.

11 REDIRECT EXAMINATION

12 BY MS. SMITH:

13 Q Mr. Warner, why did you not do the work to repair the
14 damage to the intake and discharge canals between the 2004 and
15 2005 storm seasons?

16 A The reason that we did not undertake the repairs at
17 that point was that the damage was so extensive that we needed
18 to go through and do the -- we needed to confer with NEIL on
19 the actual cost and scope, if you will, of the repairs.

20 Q Has FPL met with NEIL recently regarding damage to
21 the intake and discharge canals as a result of the 2004 storms?

22 A Yes. We met with the NEIL insurers in March of 2006
23 of this year and actually went through some details. And as a
24 result of that, you'll see that the actual amount that we were
25 requesting for the noninsured storm damage went from

1 approximately 21.5 million to 15.3 million. And that was,
2 again, a result of us getting an understanding of how much
3 damage was done in the canal.

4 So, for example, prior to this meeting there was a
5 concern about how far down under the water line there was
6 actual damage, because that is where a majority of the repairs
7 are going to take place. And NEIL agreed that the damage
8 sustained from the hurricanes was, in fact, would go all the
9 way down to the bottom of the canal, and agreed that they would
10 pay for that.

11 Q And prior to that time, was there disagreement with
12 respect to how much NEIL would cover?

13 A Yes.

14 Q And you said that -- in speaking with Mr. Beck you
15 said that repairs to intake and discharge canals would last
16 thirty years. Is that the case if storms occur?

17 A No.

18 Q And why is dredging of the canals needed as a result
19 of storms?

20 A Yes. The dredging is necessary to ensure that we
21 don't fill the canals with silt which would then be carried
22 into our cooling systems at the plant. And if that were to
23 occur, we could actually either have to shut the unit down
24 because we don't meet our licensing requirement for cooling our
25 emergency systems, or it could delay the restart of the unit

1 coming out of a refueling outage due to inadequate condensor
2 vacuum.

3 Q And would there be costs associated with that delay?

4 A Yes, there would be costs associated with that delay.
5 Quite substantial, in my opinion.

6 Q Could you elaborate?

7 A Well, our low-cost nuclear units, the fuel
8 differential is approximately a million dollars in fuel costs.
9 So if we were to actually plan a 30-day outage, or if we were
10 to actually have to take the unit off-line prematurely because
11 of an unforeseen degradation in the cooling system and we had
12 to be down approximately a week or ten days, it would be quite
13 expensive for our customers.

14 Q And the silt that you mentioned needs to be dredged
15 as a result of storms, does that occur in the normal course of
16 business?

17 A Yes and no. With the extensive damage and things
18 that have taken place as a result of the '04 and '05 storm,
19 once you remove the protective layers from the banks on the
20 sides of the actual canals themselves, then obviously the silt
21 build up will be much more accelerated because the canals are
22 not in their original design configuration. So, therefore, you
23 would have an accelerated build-up, and therefore that would
24 cause us problems in our cooling systems.

25 MS. SMITH: Thank you.

1 I would move Number 145 into the record. Actually,
2 it's 144.

3 CHAIRMAN EDGAR: Yes, 144. Any objections? Seeing
4 none, show Exhibit 144 moved in as evidence.

5 (Exhibit 144 admitted into the record.)

6 Mr. Beck.

7 MR. BECK: I don't object to Ms. Smith moving in 145,
8 but I'm not going to offer it because the witness wasn't
9 familiar with it.

10 CHAIRMAN EDGAR: 145, any objections? Oh, you're not
11 moving it. I'm sorry, I misunderstood you. Thank you,
12 Commissioner Deason.

13 MR. BECK: No, I'm not going to offer it into
14 evidence because the witness wasn't familiar with the document.

15 CHAIRMAN EDGAR: All right. The witness is excused.
16 Thank you very much.

17 MR. ANDERSON: Good morning, Chairman Edgar. Good
18 morning, Commissioners. Florida Power and Light Company would
19 call as its next witness Mr. K. Michael Davis.

20 **K. MICHAEL DAVIS**

21 **was called as a witness on behalf of FPL, and having been duly**
22 **sworn, testified as follows:**

23 **DIRECT EXAMINATION**

24 BY MR. ANDERSON:

25 Q Good morning, Mr. Davis. Can you hear me down there?

1 A Yes, sir, I can.

2 Q Will you please state your name and business address?

3 A My name is K. Michael, it's initial K, Michael Davis.

4 The business address is 9250 West Flagler Street, Miami,

5 Florida.

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

7 A I am the Vice President, Controller, and Chief

8 Accounting Officer of Florida Power and Light Company.

9 Q Have you already been sworn as a witness in this
10 proceeding?

11 A Yes, I have.

12 Q Have you prepared and caused to be filed 43 pages of
13 Prefiled Direct Testimony in this proceeding?

14 A Yes, I have.

15 Q Do you have any changes or revisions to your Prefiled
16 Direct Testimony today?

17 A Yes, I do. I have two changes.

18 Q Could you tell us about those, please?

19 A The first change is on Page 17, Line 2. It is to
20 insert the word "unsubstantiated" between the words "using
21 estimates". So it would read, "Using unsubstantiated
22 estimates." The second change is on Page 42 of my testimony,
23 Line 14. The word "liability" should be changed to the word
24 "asset." So it would read, "deferred income tax asset." Those
25 are the only two changes.

1 Q With the two changes you just told us about, if I
2 asked you the same questions contained in your Prefiled Direct
3 Testimony, would your answers be the same?

4 A Yes, sir, they would.

5 MR. ANDERSON: Madam Chair, we would ask that Mr.
6 Davis' Prefiled Direct Testimony be inserted into the record as
7 though read.

8 CHAIRMAN EDGAR: The prefiled testimony will be
9 entered into the record as though read with the changes noted
10 by the witness.

11 BY MR. ANDERSON:

12 Q You are also sponsoring some exhibits to your
13 testimony?

14 A Yes, I am.

15 Q Have those been prenumbered as KMD-1 through KMD-9?

16 A That is correct.

17 MR. ANDERSON: Mr. Davis' exhibits have already been
18 marked and admitted as Exhibits 17 through 25 in staff's master
19 exhibit list.

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1 **BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION**
2 **FLORIDA POWER & LIGHT COMPANY**
3 **TESTIMONY OF K. MICHAEL DAVIS**
4 **DOCKET NO. XXXXX-EI**
5 **JANUARY 13, 2006**

6
7 **Q. Please state your name and business address.**

8 A. My name is K. Michael Davis and my business address is 9250 West Flagler
9 Street, Miami, Florida 33174.

10 **Q. By whom are you employed and what is your position?**

11 A. I am employed by Florida Power & Light Company (FPL or the Company) as
12 Vice President, Controller and Chief Accounting Officer.

13 **Q. Please describe your duties and responsibilities in that position.**

14 A. As Vice President, Controller and Chief Accounting Officer, I am responsible for
15 the development, interpretation and implementation of FPL's accounting policies,
16 procedures and related internal accounting controls, and for maintaining the
17 accounting records in compliance with financial and regulatory accounting
18 requirements.

19 **Q. Please describe your educational background and professional experience.**

20 A. I graduated from the University of Florida in 1968 with a Bachelor of Science
21 degree in Business Administration, with a major in Accounting. In that same year
22 I was employed by Deloitte Haskins & Sells (DH&S), Independent Public
23 Accountants, (presently Deloitte & Touche). I was promoted to manager in 1976

1 and was elected a Partner in 1981. During my tenure with DH&S I participated in
2 engagements involving services to a number of diverse industry groups including
3 the utility industry. In addition, I was responsible for handling accounting
4 questions concerning the utility industry during a three-year assignment in the
5 DH&S executive office in New York. In December 1988, I was employed by FPL
6 as comptroller. On July 1, 1991, I accepted my current position as Vice President,
7 Controller and Chief Accounting Officer. I am a Certified Public Accountant in
8 the State of Florida, and a member of the American Institute of Certified Public
9 Accountants and the Florida Institute of Certified Public Accountants. I am a
10 member and past chairman of the Accounting Executive Advisory Committee of
11 the Edison Electric Institute (EEI) which is composed of Chief Accounting
12 Officers from utilities that are members of EEI. The Committee oversees the
13 activities of the various accounting committees of EEI and advises senior EEI
14 committees on accounting issues. It meets annually with the Financial
15 Accounting Standards Board to discuss accounting issues of interest to the
16 membership and approves all comment letters issued by EEI on accounting
17 matters.

18 **Q. Are you sponsoring an exhibit in this case?**

19 A. Yes, I am sponsoring an exhibit consisting of nine documents, KMD-1 through
20 KMD-9 which is attached to my direct testimony.

21

22

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

2 A. The purpose of my testimony is to:

- 3 • Provide the revenue requirement calculations for FPL's primary and
4 alternative recommendations for storm cost recovery;
- 5 • Identify the total costs incurred for the 2004 and 2005 storms;
- 6 • Present the estimated amount of storm-recovery costs proposed for storm-
7 recovery financing as of July 31, 2006;
- 8 • Discuss the amount of 2005 storm costs to be recovered for the Power
9 Generation Division (FPL's fossil plant sites), and Other FPL Facilities
10 (Corporate facilities and the Indiantown Central Distribution Facility);
- 11 • Discuss the methodology the Company recommends be used in
12 determining the amount of 2005 storm-recovery costs to be recovered;
- 13 • Discuss the accounting processes and controls in place for capturing and
14 recording the costs related to storm restoration activities;
- 15 • Propose a form to be used for the Storm Charge true-up mechanism; and
- 16 • Present the accounting entries that will be required for the proposed storm-
17 recovery financing.
- 18

19 **BACKGROUND**

20 **Q. What is the history of FPL's Storm Damage Reserve (the Reserve)?**

21 A. The Reserve was created in 1946, and became a funded Reserve in 1958. The
22 Reserve (Account 228.1) was established pursuant to Rule 25-6.0143, Florida
23 Administrative Code. FPL has increased the Reserve by the amounts authorized

1 by the Florida Public Service Commission (the Commission). In addition, the
2 Reserve has been increased by the earnings from investments held in the related
3 fund. The Reserve has been reduced by amounts associated with repairing
4 damage caused by hurricanes and other named storms. Accordingly, FPL's
5 customers have benefited from the existence of the Reserve. It was the
6 catastrophic nature of the three hurricanes experienced in 2004 that depleted the
7 entire Reserve and created a deficit.

8 **Q. How did FPL address the Reserve deficit resulting from the 2004 storm**
9 **season?**

10 A. The Company petitioned the Commission for recovery of its prudently incurred
11 storm costs that exceeded the then existing Reserve balance. The Commission
12 approved the recovery of the deficit balance resulting from the 2004 storm season
13 through the current storm restoration surcharge in Order No. PSC-05-0937-FOF-
14 EI, Docket No. 041291-EI (the 2004 Storm Cost Recovery Order).

15 **Q. Since the 2004 storm season, have any other methods become available for**
16 **recovering and financing storm costs?**

17 A. Yes. Effective June 1, 2005, the Florida Legislature enacted a comprehensive
18 storm-recovery financing statute, Section 366.8260, Florida Statutes (2005),
19 which provides another option for storm cost recovery through the issuance of
20 storm-recovery bonds, as defined in Section 366.8260.

1 **Q. Has any recent Commission decision addressed FPL's Reserve and recovery**
2 **of storm costs?**

3 A. Yes. The Stipulation and Settlement Agreement (the Agreement) approved in
4 Docket Nos. 050045-EI and 050188-EI by the Commission in Order No. PSC-05-
5 0902-S-EI issued on September 14, 2005, suspended FPL's annual accrual of
6 \$20.3 million to the Reserve effective January 1, 2006. The Agreement permits
7 FPL to petition the Commission for recovery of prudently incurred storm costs
8 and replenishment of the Reserve through Section 366.8260, Florida Statutes
9 (2005), and/or through a separate surcharge that is independent of and incremental
10 to retail base rates. In addition, FPL committed to address replenishment of its
11 Reserve within six months of the Order.

12 **Q. Has the company incurred storm costs subsequent to the 2004 storm season?**

13 A. Yes. FPL has incurred costs as a result of four storms that affected FPL's service
14 territory in 2005. The nature of these storms is discussed further in Ms. Williams'
15 testimony.

16

17 **PROPOSED METHOD OF STORM COST RECOVERY**

18 **Q. What method of storm cost recovery is FPL requesting in this proceeding?**

19 A. As Mr. Dewhurst discusses in his testimony, FPL is requesting to issue bonds to
20 reimburse the Company for storm costs incurred as a result of the 2004 and 2005
21 storm seasons in accordance with Section 366.8260, Florida Statutes (2005). As
22 discussed further in Dr. Morley's and Mr. Olson's testimonies, these bonds will be
23 structured to result in a projected stable cents/kWh factor. The proceeds of the
24 storm-recovery financing will be used to provide recovery of all unrecovered

1 2004 and 2005 storm-recovery costs and replenish the Reserve to a level of
2 approximately \$650.0 million.

3

4 In order to implement this recovery method, FPL proposes to establish a Special
5 Purpose Entity (SPE), a wholly-owned subsidiary of FPL, to issue the bonds. The
6 SPE will have a servicing agreement with FPL under which FPL will act as a
7 collection agent and will forward certain revenues collected from customers to the
8 SPE. Further details of these transactions are discussed later in my testimony and
9 in Mr. Olson's testimony.

10 **Q. Mr. Dewhurst's testimony discusses FPL's primary and alternative**
11 **recommendations for storm cost recovery. Would you please describe the**
12 **revenue requirements for FPL's primary recommendation?**

13 **A. Yes. FPL is proposing to securitize the costs incurred for the 2004 and 2005**
14 **storms through storm-recovery bonds. Page 1 of my Document No. KMD-1**
15 **shows the annual revenues required to repay these bonds, including interest,**
16 **income taxes, and ongoing costs, over the expected bond life of approximately**
17 **twelve years. These revenue requirements will be updated to reflect the outcome**
18 **of the Financing Order, and the actual costs associated with the issuance of bonds.**

19 The proceeds from the bonds will be applied to the following:

- 20 • Jurisdictionalized Unrecovered 2004 Storm-Recovery Costs;
- 21 • Jurisdictionalized Unrecovered 2005 Storm-Recovery Costs;
- 22 • Replenishment of the Reserve to approximately \$650.0 million; and
- 23 • Upfront Bond Issuance Costs.

1 The unrecovered storm-recovery costs are discussed later in my testimony, and
2 the replenishment of the Reserve and details of the upfront bond issuance costs
3 are further discussed in Mr. Dewhurst's testimony.

4 **Q. What are the revenue requirements for the recovery of costs through the**
5 **Company's alternative recommendation?**

6 A. Page 2 of my Document No. KMD-1 shows the annual revenues required for the
7 Company's alternative recommendation over a three-year period. The revenue
8 requirements are comprised of the following:

- 9 • Continuation of the 2004 storm cost recovery over the remaining two
10 years through the existing storm restoration surcharge authorized in the
11 2004 Storm Cost Recovery Order, including an interest charge;
- 12 • Recovery of the 2005 storm costs, including an interest charge, over a
13 three-year period starting in year one; and
- 14 • Approximately \$650.0 million to replenish the Reserve over a three-year
15 period starting in year one.

16 **Q. How were the interest charges calculated on the 2004 and 2005 storm costs**
17 **in the alternative recommendation?**

18 A. The interest charges included in the recovery of the 2004 and 2005 storm costs
19 were calculated by multiplying the average monthly unrecovered balance by the
20 current estimated after-tax commercial paper rate. Therefore, these charges
21 represent the interest expense associated with the debt the Company would incur
22 or has incurred to cover the net-of-tax storm costs.

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STORM CHARGE

Q. Please describe the Storm Charge the Company is proposing.

A. As discussed in Mr. Dewhurst's testimony, FPL is seeking approval from this Commission to establish a per kWh storm charge (the Storm Charge) to be collected on customer bills over the expected twelve-year life of the bonds. The Storm Charge is comprised of two components:

- The Storm Bond Repayment Charge, and
- The Storm Bond Tax Charge.

Q. What is the Storm Bond Repayment Charge?

A. The Storm Bond Repayment Charge is the portion of the Storm Charge collected from customers to make the necessary payments to service the bonds. These amounts will be remitted to the SPE and are defined as a storm-recovery charge in Section 366.8260(1)(m), Florida Statutes (2005). The accounting entries associated with these transactions are further detailed in my Document No. KMD-9.

Q. What is the Storm Bond Tax Charge?

A. The Storm Bond Tax Charge, which is also a storm-recovery charge under the statute, covers the income taxes associated with the revenues collected to repay the storm-recovery bonds and will be collected and retained by the Company.

Although the SPE will be structured to be a separate bankruptcy-remote entity, it will be treated as a division of FPL for tax purposes. Therefore, FPL will be responsible for the payment of all income taxes due on the Storm Bond

1 Repayment Charge. As such, FPL will need to collect from its customers an
2 amount that after payment of income taxes is sufficient to yield an amount equal
3 to the Storm Bond Repayment Charge. In addition, FPL will be required to
4 collect and remit amounts sufficient to pay gross receipts taxes, sales taxes, and
5 regulatory assessment fees as well as pay the franchise fees and revenue taxes
6 imposed by the cities and counties in which its customers receive service. The
7 entries associated with these transactions are further detailed in my Document No.
8 KMD-9.

9 **Q. Has the U.S. Treasury Department issued any guidance on accounting for**
10 **storm-recovery financing and related income taxes?**

11 A. Yes. Revenue Procedure 2005-62 provides a safe harbor for public utility
12 companies that, pursuant to specified cost recovery legislation, receive an
13 irrevocable Financing Order permitting the utility to recover certain specified
14 costs through a qualifying securitization. Under the revenue procedure, FPL will
15 not recognize taxable income upon 1) the receipt of the Financing Order; 2) the
16 transfer of FPL's rights under the Financing Order to the SPE; or 3) the issuance
17 of the storm-recovery bonds.

18 **Q. Does the storm-recovery financing FPL is proposing meet the requirements**
19 **of this revenue procedure?**

20 A. Yes.

21 **Q. What storm-related costs are proposed for storm-recovery financing?**

22 A. As shown on Document No. KMD-2, the following storm-related costs are
23 proposed for storm-recovery financing:

- 1 • Jurisdictionalized Unrecovered 2004 Storm-Recovery Costs;
- 2 • Jurisdictionalized Unrecovered 2005 Storm-Recovery Costs; and
- 3 • Replenishment of the Reserve to approximately \$650.0 million.

4 The above-referenced costs are estimated as of July 31, 2006, as allowed by
5 Section 366.8260(2)(a)2., Florida Statutes (2005), and are net of insurance
6 proceeds, normal capital replacement costs, including cost of removal, and costs
7 that have already been recovered through the existing storm restoration surcharge.
8 These storm-related costs plus upfront bond issuance costs represent the total
9 amount of costs subject to storm-recovery financing.

10 **Q. Why did FPL use July 31, 2006 to estimate the amount of storm-recovery**
11 **costs to be financed?**

12 A. If the proposed storm-recovery financing is approved by the Commission, the
13 Company intends to conduct the storm-recovery financing in 2006 as soon as
14 practicable following the issuance of a Financing Order and will work to do so
15 prior to August 1, 2006 to ensure funding is in place during the next storm season.
16 Thus, the Company believes a date of July 31, 2006 is reasonable.

17 **Q. If the actual issuance date of the storm-recovery bonds is different than what**
18 **is estimated, does FPL propose to adjust the amount of storm-recovery costs**
19 **to be financed?**

20 A. No. If the actual issuance date is not on or about August 1, 2006, FPL proposes to
21 charge or credit any difference in the amount of storm-recovery costs to be
22 financed to the Reserve.

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STORM-RECOVERY COSTS

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Q. What is the definition of storm-recovery costs?

A. As defined in Florida Statute (2005) §366.8260(1)(n):

“‘Storm-recovery costs’ means, at the option and request of the electric utility, and as approved by the commission pursuant to sub-subparagraph (2)(b)1.b., costs incurred or to be incurred by an electric utility in undertaking a storm-recovery activity. Such costs shall be net of applicable insurance proceeds and, where determined appropriate by the commission, shall include adjustments for normal capital replacement and operating costs, lost revenues, or other potential offsetting adjustments. Storm-recovery costs shall include the costs to finance any deficiency or deficiencies in storm-recovery reserves until such time as storm-recovery bonds are issued, and costs of retiring any existing indebtedness relating to storm-recovery activities.”

Q. Do the amounts for 2004 and 2005 storm-recovery costs FPL is proposing to finance meet this criteria?

A. Yes, for the reasons explained below.

Q. What is the jurisdictional amount of unrecovered pre-tax 2004 storm-recovery costs to be included in the amount of storm-recovery financing?

A. As shown on Document No. KMD-3, FPL’s jurisdictional unrecovered pre-tax 2004 storm-recovery costs as of July 31, 2006 are estimated to total \$213.3 million.

1 **Q. Please describe how the amount of unrecovered pre-tax 2004 storm-recovery**
2 **costs was determined.**

3 A. The total amount incurred for the 2004 storms after deducting insurance proceeds
4 was approximately \$890.0 million. In the 2004 Storm Cost Recovery Order, the
5 Commission approved collection of \$442.0 million in 2004 storm cost by FPL
6 from its retail customers. The \$442.0 million represents the total amount less the
7 then existing Reserve balance, normal capital replacement costs and the \$21.7
8 million that I discuss below. FPL has been collecting the current restoration
9 surcharge for these costs since February 2005 and as shown on my Document No.
10 KMD-3, FPL estimates \$212.0 million of this amount will remain to be collected
11 as of July 31, 2006. This amount was calculated by adding monthly interest at the
12 commercial paper rate to the unrecovered balance (as allowed in the 2004 Storm
13 Cost Recovery Order) and subtracting the estimated billed revenues based on the
14 average retail surcharge factor approved by the Commission times forecasted
15 kWh sales detailed in Dr. Green's testimony.

16

17 In addition to the costs to be recovered, as a result of the 2004 Storm Cost
18 Recovery Order, the Commission also approved an adjustment to the 2004 storm
19 costs of \$21.7 million (jurisdictional amount of \$21.6 million) which was
20 included in the Reserve. My Document No. KMD-3 shows that the net
21 jurisdictional amount remaining after considering FPL's jurisdictional 2005 storm
22 accrual of \$20.2 million (total system amount of \$20.3 million) and fund earnings
23 from January through September 2005 of \$0.1 million, is \$1.3 million. This

1 amount has been included in the amount of unrecovered 2004 storm-recovery
2 costs.

3

4 The sum of the 2004 storm cost deficiency as of July 31, 2006 of \$212.0 million,
5 plus the net adjustment of \$1.3 million, totals \$213.3 million of unrecovered 2004
6 storm-recovery costs.

7 **Q. Does the Company propose to true-up the estimate of unrecovered 2004**
8 **storm-recovery costs?**

9 A. Yes. FPL included in the existing restoration surcharge an estimate for identified
10 projects that were not yet completed. However, the actual costs for such projects
11 may be more or less than what was estimated. An example of this type of work
12 was described in detail in Commission Order No. PSC-95-1588-FOF-EI on page
13 4:

14 “FPL suffered extensive salt water damage to underground facilities as a
15 result of Hurricane Andrew and the March 1993 Storm. It is the
16 Company's intent to repair these facilities as they fail, or during any
17 normal upgrading of the facilities. Certain of these facilities are expected
18 to fail in the near future. Based on engineering estimates of anticipated
19 future repair costs, an insurance settlement of \$6.7 million was reached.
20 This is a final settlement; if the repairs exceed this amount the Company
21 will not be able to file for additional insurance reimbursement.

22

1 It appears from FPL's petition that the Company wishes to establish a
2 separate liability for the \$6.7 million, rather than placing it in the reserve.
3 The \$6.7 million received by the Company represents a settlement of
4 claims for which neither the actual total amount nor the timing of the
5 replacement can be accurately determined. This is exactly the situation a
6 storm reserve is designed to cover. Therefore, we find that this amount
7 shall be added to the reserve and the after tax amount added to the fund.
8 By doing so, the amount can be invested and accrue interest. This will
9 help to mitigate any costs for repairs should they exceed the Company's
10 original estimates. As the repairs are actually completed, the reserve shall
11 be charged for the cost of the repairs.” (emphasis added)

12 Therefore, FPL proposes that once these projects are completed, if the actual
13 amount is lower than the estimated amount, the difference would be credited to
14 the Reserve. If the actual amount is higher than the estimated amount, FPL
15 proposes to charge the difference to the Reserve.

16 **Q. What is the jurisdictional amount of unrecovered pre-tax 2005 storm-**
17 **recovery costs to be included in the amount of storm-recovery financing?**

18 **A. As shown on Document No. KMD-4, FPL's total system amount of unrecovered**
19 **2005 storm-recovery costs is estimated at \$827.5 million and the jurisdictional**
20 **unrecovered pre-tax 2005 storm-recovery costs is estimated to total \$826.9**
21 **million. These amounts are after deducting capital and insurance proceeds from**
22 **the total estimated amount of costs incurred and include interest incurred prior to**
23 **July 31, 2006.**

1 **Q. Has the Commission established a specific methodology with regards to**
2 **storm cost recovery as a result of its decision in Docket No. 041291-EI?**

3 A. No. The Commission made it very clear in that docket that it has the latitude to
4 determine what costs are to be recovered on a case-by-case basis. My Document
5 No. KMD-5 contains excerpts from the discussion at the agenda conference held
6 on July 19, 2005 during which Commissioners Deason and Baez clearly
7 articulated this position.

8 **Q. What methodology does FPL recommend the Commission adopt to**
9 **determine the amount of unrecovered 2005 storm-recovery costs?**

10 A. FPL recommends that the Commission adopt the Actual Restoration Cost Method
11 addressed in Docket No. 930405-EI with an adjustment to remove normal capital
12 costs. This method, excluding an adjustment to capital costs, was utilized by the
13 Company between 1993 and 2003 to determine the storm restoration costs to be
14 charged against the Reserve. For this proceeding, FPL's proposed method
15 includes all costs which are incurred to safely restore electric service or return
16 plant and equipment to its pre-storm condition. The adjustment to remove capital
17 costs will be at "normal cost" and recorded to rate base. What is left after
18 adjusting for insurance recoveries represents the operations and maintenance
19 expenses the Company has incurred to restore service to its customers. This
20 amount plus interest incurred as of the expected date of securitization, as allowed
21 in Section 366.8260, Florida Statutes (2005), results in the amount proposed for
22 storm-recovery financing.

1 **Q. Please explain why the methodology FPL is recommending this Commission**
2 **adopt is appropriate.**

3 A. FPL believes that its proposed method should be adopted for several reasons.
4 First and foremost, this method is by far the most accurate way to account for
5 storm restoration costs. Also, it is totally consistent with sound and commonly
6 accepted cost accounting principles, procedures and practices. Accordingly, it
7 results in accounting and recovery of the actual costs incurred to restore electric
8 service.

9 **Q. Why is FPL's proposed method the most accurate way to account for storm**
10 **restoration costs?**

11 A. FPL's proposed method is the most accurate way to account for all of FPL's
12 storm restoration costs because it properly utilizes the normal cost accounting
13 practices, processes and procedures that are relied upon by the Company in the
14 ordinary course of its business. Also, it avoids the necessity of making estimates
15 for year-end budget variances that are inconsistent with the stringent financial
16 reporting requirements imposed on public companies by the Sarbanes-Oxley Act
17 of 2002.

18 **Q. Can you please elaborate why these estimates are a financial reporting**
19 **concern?**

20 A. To apply the incremental cost approach to interim financial statements, FPL will
21 have to estimate the amount of year-end variances and deduct that amount from
22 the amounts determined using the Company's proposed method. There is simply
23 no basis for making such an estimate until the actual variance is known.

1 FPL is a public company and must publicly report its financial information on a
2 quarterly basis. Using ^{unsubstantiated} estimates in preparing those financial statements is not
3 permitted. At the same time, making no adjustment shrouds FPL's financial
4 statements with uncertainties that can create disadvantages for FPL as it competes
5 for capital.

6 **Q. Why should the Commission and the public have confidence that adopting**
7 **FPL's proposed method will ensure that the right amount of storm**
8 **restoration costs are properly recorded, reported and recovered?**

9 A. While I discuss this in detail elsewhere in my testimony, in summary, all of FPL's
10 storm restoration costs are charged to specific storm work orders and account
11 numbers, which FPL's employees are trained and experienced in using. The work
12 orders and account numbers are opened up at the time that storm-related work
13 begins, and closed out when it ends. Simply put, the amounts that end up
14 recorded under these work orders and in these accounts fairly and accurately state
15 FPL's total costs of storm restoration.

16 **Q. Are there other reasons supporting adoption of FPL's proposed method?**

17 A. Yes. FPL's proposed method also has the advantage of replicating the cost
18 recovery that FPL would receive under a hypothetical third party replacement cost
19 insurance policy, were such coverage to be available in the insurance
20 marketplace. This is consistent with the regulatory policy established by the
21 Commission in its rules, such as Rule 25-6.0143, Accumulated Provision for
22 Property Insurance, as well as discussed in prior Commission orders. For
23 example, the express function of Rule 25-6.0143 is to facilitate provision of self-

1 insurance under the direction of the Commission for losses caused by risks, such
2 as storm restoration costs not covered by insurance.

3 **Q. How does the “modified incremental cost method” of accounting for storm**
4 **costs provided for in the 2004 Storm Cost Recovery Order compare with**
5 **FPL’s proposed method?**

6 A. First, it should be noted that FPL believes that the method provided in the 2004
7 Storm Cost Recovery Order and FPL’s proposed method in this proceeding,
8 would result in the same total amount of storm restoration costs for the 2005
9 storm season. FPL believes that as a policy matter, the Commission, customers
10 and FPL would all be better served by using FPL’s proposed method which relies
11 upon cost accounting data, rather than the incremental cost approach’s indirect
12 and judgmental assessment of budget-related documents, as the measure for storm
13 restoration costs. FPL notes that year-end financial data is only now beginning to
14 become available that would enable performance of a final comparison of 2005
15 budgeted and actual figures, demonstrating an additional practical limitation on
16 the usefulness of the incremental cost approach during the year when storm
17 restoration costs are incurred.

18 **Q. Please compare the incremental cost approach and FPL’s proposed method**
19 **from the perspective of accounting theory.**

20 A. FPL’s proposed method correctly applies cost accounting principles and data for
21 capturing and measuring storm restoration costs. The incremental cost approach,
22 in contrast, contaminates the results achieved through the Company’s proposed
23 method by improperly using managerial accounting tools for a purpose for which

1 they are not intended. Moreover, instead of relying on readily available and
2 accurate storm restoration cost data, the incremental cost approach relies upon
3 measuring or estimating variances between budgeted and actual expenditures in
4 the numerous budget line items making up the Company's budgeting and cost
5 management process. The incremental cost approach's use of managerial
6 accounting principles of budget variance analysis for cost accounting purposes
7 uses the wrong set of accounting tools for the job of determining storm restoration
8 costs.

9 **Q. Why is a comparison of budgeted and actual expenditures, used in the**
10 **incremental cost approach, the wrong financial and accounting tool for the**
11 **job of computing storm restoration costs?**

12 A. Quite simply, FPL's budgets are set for the purposes of allocating overall
13 resources. This is a basic management process aided by the budgeting tools of
14 managerial accounting. Budgets are monitored, and adjustments in expenditures
15 are made over the course of the year, in order to help FPL's management measure
16 and assess actual business resource requirements in the course of the year in
17 comparison with the resources that were estimated to be needed in the budgeting
18 process. This is a valid and indeed essential business process for FPL to use and
19 follow. However, it is not a typical, common or even accepted accounting
20 method for cost accounting. It is also an unnecessarily complicated and indirect
21 method for measuring storm costs, especially when the Company already has in
22 place accurate cost accounting methods for capturing and recording storm
23 restoration costs directly.

1 **Q. Why isn't using differences between budgeted and actual cost performance,**
2 **as is involved in the incremental cost approach, as good a method as using**
3 **accurate cost accounting records of actual storm restoration costs?**

4 A. Using the managerial accounting tool of budget variance analysis is not nearly as
5 good as using storm cost accounting records because budgeted and actual cost
6 performance for individual line items, and for the Company as a whole, varies
7 widely for a host of reasons having nothing to do with storm restoration costs.
8 Unanticipated but necessary expenses continually arise, and other expenses are
9 mitigated or avoided, in the course of routine business operations. Trying to
10 gauge storm restoration costs indirectly by looking at budget variances is a
11 difficult and highly judgmental process at best. It is also unwieldy because final
12 variances are never known until the year's end, making use of the incremental
13 cost approach for measuring storm costs exceedingly difficult in the course of the
14 ordinary business year. Moreover, using such an indirect and unwieldy process is
15 simply unnecessary when accurate, direct, measures of storm restoration costs are
16 available through reference to the actual expenditure data that FPL routinely
17 compiles in the course of its storm restoration work. Using the incremental cost
18 approach results in laboriously improvising an imperfect cost measurement tool,
19 instead of using well-established and existing cost accounting tools and data.

20 **Q. Does using FPL's proposed method result in recovery of expenses through**
21 **base rates and through a storm-recovery mechanism?**

22 A. No. It results in only a proper single recovery of the correct amount of storm
23 restoration costs.

1 **Q. Please explain why FPL's proposed method results in only a single recovery**
2 **of storm restoration costs.**

3 A. In prior storm restoration cost recovery proceedings, others have urged the use of
4 a so-called incremental cost approach instead of an actual restoration cost
5 approach in order to avoid what they contend would be a recovery of storm costs
6 through base rates and through a storm recovery mechanism. This theory claims
7 that reimbursing FPL its actual costs for storm restoration is excessive because,
8 the argument goes, such costs are already accounted for in the Company's base
9 rates. One fatal weakness of this theory is that there is no provision for
10 extraordinary storm restoration costs in base rates. In other words, even if, for
11 example, a certain level of normal O&M expense is deemed to be implied in base
12 rates, that level of expense neither includes nor contemplates any amount of cost
13 contingency associated with the impact of a hurricane, which, among other things,
14 results in normally scheduled work and the related costs being deferred or delayed
15 to a subsequent period, not to mention widespread outages during which such
16 costs are not recovered through sales of electricity. Therefore, FPL receives only
17 a single recovery for its storm restoration costs when its proposed method is used.

18 **Q. Please summarize your points supporting use of FPL's proposed method for**
19 **determining storm restoration costs.**

20 A. FPL urges the Commission to rely upon FPL's actual cost accounting data with
21 respect to storm recovery costs, rather than trying to indirectly infer storm costs
22 through use of the budget variance-based incremental cost approach. FPL's
23 proposed method represents a correct use of accurate accounting data as a basis

1 for achieving a single proper recovery of storm restoration costs. In addition, any
2 method that only adjusts the expense side of the ratemaking equation, violates the
3 basic concept of ratemaking. Therefore, there is no analytical, financial, rate or
4 other logical basis for any assertion that reimbursing FPL for its actual costs of
5 storm restoration constitutes double recovery and the alternative incremental cost
6 approach should not be used.

7 **Q. Please describe how the amount of unrecovered pre-tax 2005 storm-recovery**
8 **costs was determined.**

9 A. As allowed in Section 366.8260(2)(a)2., Florida Statutes (2005), FPL's total
10 estimated amount of 2005 storm-recovery costs represents the sum of the
11 following:

- 12 • Known storm-recovery costs;
- 13 • An estimate for storm restoration activities not yet completed; and
- 14 • An estimate for completed activities where the final costs are not yet
15 known.

16 FPL's total estimated amount is based on a financial close date as of November
17 30, 2005 except for certain estimate updates received on or about December 15,
18 2005 (the final cut-off). Therefore, for purposes of determining the estimated
19 amount of unrecovered pre-tax 2005 storm-recovery costs, I have utilized FPL's
20 total system number provided in Ms. Williams' testimony as a starting point.
21 This amount represents a reliable estimate of the costs incurred to restore service
22 following the damages sustained from Hurricanes Dennis, Katrina, Rita, and

1 Wilma. These costs are consistent with the storm-recovery activities defined in
2 Section 366.8260(1)(k), Florida Statutes (2005):

3 “‘Storm-recovery activity’ means any activity or activities by or on behalf
4 of an electric utility in connection with the restoration of service
5 associated with electric power outages affecting customers of an electric
6 utility as the result of a storm or storms, including, but not limited to,
7 mobilization, staging, and construction, reconstruction, replacement, or
8 repair of electric generation, transmission, or distribution facilities.”

9 My Document No. KMD-4 details \$90.4 million in adjustments to this amount in
10 accordance with the Company’s proposed method as well as an addition of \$11.5
11 million for interest incurred through July 31, 2006, as allowed by Section
12 366.8260(1)(n), Florida Statutes (2005), to determine the total unrecovered pre-
13 tax 2005 storm-recovery costs. This adjusted amount was then multiplied by a
14 jurisdictional factor of 99.921% to come to a jurisdictional amount of \$826.9
15 million. The jurisdictional factor applied is further detailed on page 2 of
16 Document No. RM-1 in Dr. Morley’s testimony.

17 **Q. Does the Company propose to true-up the estimate of unrecovered 2005**
18 **storm-recovery costs?**

19 **A.** Yes. Even though FPL is able to provide an estimate of the costs incurred to
20 restore service for the 2005 storms, in accordance with Section 366.8260(2)(a)2.,
21 a portion of these costs are not yet finalized. Therefore, once all of the costs for
22 the 2005 storms are finalized, any difference between the estimated amount and
23 the actual amount of costs incurred, or due to the outcome of a staff audit or any

1 Commission proceeding, would be charged or credited to the Reserve. Thus, if
2 the actual costs are lower than anticipated, the resulting balance in the Reserve
3 will be higher and vice versa.

4 **Q. What specific 2005 storm costs are you addressing in your testimony?**

5 A. As indicated in Ms. Williams' testimony, I will be addressing the 2005 storm costs
6 for the Power Generation Division (FPL's fossil plant sites) and Other FPL
7 Facilities (Corporate facilities and the Indiantown Central Distribution Facility).

8 **Q. What are the estimated 2005 storm costs eligible for recovery for the Power
9 Generation Division (FPL's fossil plant sites)?**

10 A. The total estimated 2005 storm costs for the Power Generation Division (FPL's
11 fossil plant sites) are \$19.4 million. The details for this amount are illustrated on
12 my Document No. KMD-6 and represent the following types of activities: storm
13 preparation and repairs to buildings and grounds, cooling ponds, cooling towers
14 and basins, chimneys, electrical equipment, boilers, intake system, instruments
15 and controls, insulation and lagging, mold remediation, and tanks. These
16 activities are necessary to bring the Power Generation Division (FPL's fossil plant
17 sites) facilities to their pre-storm condition.

18

19 Also, included in the total amount for the Power Generation Division (FPL's fossil
20 plant sites) is \$0.9 million of storm damage costs related to the fossil units at
21 FPL's Turkey Point site. That site is insured under a Nuclear policy, NEIL, that is
22 described by Mr. Warner in his testimony.

23

1 As illustrated on my Document No. KMD-6, the total estimated 2005 storm costs
2 of \$19.4 million for the Power Generation Division (FPL's fossil plant sites) less
3 estimated capital costs of \$2.1 million and estimated insurance proceeds of \$2.4
4 million is \$15.0 million. This amount represents the Power Generation Division
5 (FPL's fossil plant sites) storm costs eligible for recovery. Later in my testimony,
6 I will address the process FPL goes through to determine capital costs and
7 insurance recoveries.

8 **Q. What are the estimated 2005 storm costs eligible for recovery for Other FPL**
9 **Facilities (Corporate facilities and the Indiantown Central Distribution**
10 **Facility)?**

11 **A.** The total estimated 2005 storm costs for Other FPL Facilities (Corporate facilities
12 and the Indiantown Central Distribution Facility) are \$13.5 million. The details
13 for this amount are illustrated on my Document No. KMD-7 and represent the
14 following types of activities: repairs to roofing, fencing and gates, landscaping,
15 Heating, Ventilating, and Air Conditioning (HVAC), and rollup doors. These
16 activities are necessary to bring these facilities to their pre-storm condition. As
17 illustrated on my Document No. KMD-7, this amount less estimated capital costs
18 of \$5.7 million and estimated insurance proceeds of \$0.6 million results in \$7.1
19 million of storm costs eligible for recovery for Other FPL Facilities (Corporate
20 facilities and the Indiantown Central Distribution Facility). As previously
21 mentioned, I will address the process FPL goes through to determine capital costs
22 and insurance recoveries later in my testimony.

1 **Q. As previously mentioned, FPL proposes to make adjustments to the total**
2 **amount of unrecovered 2005 storm-recovery costs. What adjustments would**
3 **be made using FPL's proposed methodology?**

4 A. As shown on Document No. KMD-4, the proposed adjustments to be made to the
5 2005 storm-recovery costs for Hurricanes Dennis, Katrina, Rita, and Wilma
6 consistent with this approach would be as follows:

- 7 1. Remove estimated capital costs of \$63.9 million and include them in rate
8 base;
- 9 2. Remove estimated insurance proceeds received or expected to be received
10 of \$26.5 million for Hurricane Wilma. The Company has not removed any
11 insurance proceeds for Hurricanes Dennis, Katrina, or Rita as none have
12 been received or are expected to be received; and
- 13 3. Add interest incurred through July 31, 2006, which is estimated to be \$11.5
14 million, as allowed in Section 366.8260(1)(n), Florida Statutes (2005).

15 **Q. How are capital costs related to storm restoration activities determined?**

16 A. Each Business Unit is responsible for preparing an estimate of capital work as a
17 result of storm damage to its assets. FPL estimates storm damages related to its
18 Transmission and Distribution assets at normal cost utilizing the Company's
19 estimating systems. Storm damages to all other assets are estimated individually
20 by each Business Unit. These estimates are then reviewed by FPL's Accounting
21 Department (Accounting) to ensure these costs are capital costs, not operating or
22 maintenance costs. Accounting also ensures the correct amount of additions,
23 retirements, removal, and salvage will be recorded on the Company's books.

1 Based on the estimates developed, the capital costs are adjusted out of storm-
2 recovery costs and are charged to rate base.

3 **Q. Do you expect the capital estimates to change?**

4 A. Yes. The capital estimates may change for various reasons, including but not
5 limited to, true-up of material issuances/returns, true-up of actual costs for assets
6 other than Transmission and Distribution, and/or true-up arising from subsequent
7 processing required to allocate the capital costs at the county level for property
8 tax purposes. Any difference between what was estimated and the actual capital
9 costs will be charged or credited to the Reserve.

10 **Q. How are insurance recoveries and deductibles related to storm damages**
11 **handled?**

12 A. Each Business Unit is responsible for estimating the damages to its infrastructure
13 caused by storms. This estimate is then reviewed with the Risk Management
14 organization to determine what portion of the estimated damages may be
15 recoverable under the applicable insurance policies. Once this is determined, the
16 appropriate deductibles for each insurance policy are charged to the Reserve as
17 are any estimated storm damages which are excluded from coverage under the
18 various insurance policies. The estimated insurance recoveries are not included
19 in the total amount of storm-recovery costs charged to the Reserve.

20 **Q. Do you expect the estimated insurance recoveries to change?**

21 A. Yes. After a storm, our Risk Management department meets with the insurance
22 adjusters who visit the damaged property to evaluate the extent and type of the
23 damages. Following the inspection process, there is a review and finalizing

1 process between our Risk Management personnel and representatives of the
2 insurance companies to determine which damage elements are covered by
3 insurance and the ultimate actual cost to complete repair or replacement. This
4 results in an agreed to amount of insurance recovery. This process can take a
5 prolonged period of time before the final amount covered by insurance is
6 determined. Once a claim is finalized and the insurance adjuster makes a final
7 determination as to the eligibility of the damaged facilities, the estimated
8 insurance recoveries may change from the initial estimates. Therefore, at the time
9 insurance recovery is finalized, any difference between the original estimate and
10 the actual insurance recovery will be charged or credited to the Reserve. In
11 addition, if any amount is recovered from third parties, adjustments to the Reserve
12 would also be made.

13 **Q. Can you please explain FPL's insurance recoveries and deductibles for the**
14 **2005 storm damages in more detail?**

15 **A.** Yes. I will discuss the insurance recoveries related to the non-nuclear damages of
16 \$4.5 million and Mr. Warner will discuss the nuclear insurance recoveries of
17 \$23.0 million in his testimony. For 2005, FPL has estimated total storm damage
18 which might be insured to be \$29.5 million for its non-nuclear property with a
19 deductible of \$25.0 million, which yields an estimated insurance recovery of \$4.5
20 million (\$29.5 million less \$25.0 million). Of this estimated insurance recovery,
21 \$1.0 million relates to capital expenditures and \$3.5 million relates to recovery of
22 operations and maintenance costs. The addition of the \$3.5 million to estimated
23 nuclear insurance recoveries of \$23.0 million results in the \$26.5 million

1 insurance recovery adjustment shown on my Document No. KMD-4. I would like
2 to point out that the recovery amount is determined using a “good faith” effort
3 between the parties but as additional inspections or work is performed this
4 number may be adjusted. The Company will charge or credit the Reserve with
5 any true-up of the estimated amount.

6 **Q. Did FPL derive tax benefits from the storm-recovery costs?**

7 A. Yes. The Company has either received or will receive federal and state income
8 tax benefits for the storm restoration costs incurred.

9 **Q. How have these tax benefits been reflected in the proposed storm-recovery
10 financing?**

11 A. The Company has reduced the storm-recovery financing amount for the federal
12 and state benefits at the statutory tax rate of 38.575% to reflect all tax benefits
13 related to the storm-recovery costs.

14 **Q. What is the total amount of storm-related costs proposed for storm-recovery
15 financing?**

16 A. As shown on my Document No. KMD-2, the aggregate storm costs incurred for
17 2004 and 2005 is \$1.8 billion. Also shown on my Document No. KMD-2, the
18 amount of storm-related costs proposed for storm-recovery financing is \$1.7
19 billion, which includes replenishment of the Reserve. This amount less income
20 tax benefits plus upfront bond issuance costs represents the aggregate amount of
21 bonds FPL is proposing to issue. As the Storm Charge is collected from
22 customers, that income tax benefit will reverse and income taxes will become

1 payable as revenues are recorded. Therefore, the amounts ultimately paid by
2 customers will include those taxes.

3

4

STORM ACCOUNTING AND CONTROLS

5 **Q. Can you please explain the accounting process and controls that exist to**
6 **ensure that storm-recovery costs are accurate?**

7 A. Yes. When a storm is approaching and the Company activates the General Office
8 Command Center, Accounting issues a unique storm work order to capture all
9 costs for storm restoration activities related to the storm. Upon Business Unit
10 request, additional work orders may be issued to further segregate costs.
11 However, all storm-related work orders are accumulated in Account 186,
12 Miscellaneous Deferred Debits, to facilitate reporting of the storm's total costs.
13 Along with the set up of these work orders, Accounting also issues guidance to
14 the organization on what costs are appropriate to charge to the storm work order.
15 The use of work orders to capture costs is part of the Company's normal process
16 for recording transactions and is supported by normal internal controls and
17 processes. In Ms. Williams' testimony, she discusses the controls over the
18 appropriate levels of resources, procurement, and logistical support, which are
19 charged to the storm work order, and controls surrounding the procurement
20 process. She also discusses Restoration Management's approval process relating
21 to employee time sheets, contractor time sheets, receipt logs, and invoice
22 processing. In addition to issuing the storm work orders, Accounting
23 representatives (Site Controllers) will field questions during storm restoration

1 efforts as to whether a particular cost can be charged to the storm work order.
2 Because these individuals are trained on the costs eligible for storm and required
3 supporting documentation, this provides an additional level of control. If
4 uncertainty exists regarding a cost, Site Controllers or Accounting would review
5 the specified cost with Site Management or Business Unit management to ensure
6 the appropriate linkage between the expenditure and its reasonableness.

7 **Q. Do you have any additional comments regarding the accounting process**
8 **and/or controls that exist to record the Company's storm costs?**

9 A. Yes. First of all, let me state that the accuracy of our financial records is very
10 important to us. As I have already discussed, Accounting issues unique work
11 orders and guidance on how to capture the storm costs. Also, in addition to the
12 supervisory approvals required as part of our normal control environment, Site
13 Controllers are deployed to the staging sites to further support Site Management
14 in promoting effective internal controls during storm restoration. The Site
15 Controllers are an integral part of the logistics team and provide guidance on
16 eligible costs and record-keeping. Additionally, the Site Controllers observe the
17 critical control processes, as discussed in Ms. Williams' testimony, to obtain
18 confirmation that the control processes are working as intended. Some of the
19 important functions the Site Controller performs are as follows:

- 20 • Ensure FPL personnel at staging sites understand the nature of their
21 control activities and comply with the applicable control and
22 documentation requirements;

- 1 • Review contractor time sheets for compliance with FPL approval
2 procedures;
- 3 • Review expense reports approved by Site Management;
- 4 • Randomly sample FPL employee time sheets for approvals and accuracy;
- 5 • Prepare receipt documents for materials and services received on site, and
6 forward contractor time sheets to a central location for further review and
7 processing;
- 8 • Review account distribution on samples of FPL time sheets, expense
9 reports, and procurement card purchases; and
- 10 • Provide guidance as questions arise in the field and seek any additional
11 clarification from the General Office Command Center and/or Accounting
12 as required.

13 **Q. Can you please explain the accounting process used to record the 2005 storm**
14 **costs?**

15 A. Yes. Accounting sent a standard template to each Business Unit to estimate each
16 Business Unit's storm costs. The template displays the actual storm costs
17 recorded in the general ledger and requests each Business Unit to estimate the
18 storm costs they have incurred that are not yet recorded on the Company's books.
19 The templates and related supporting schedules are reviewed by each Business
20 Unit's Management who evidences the review by signing the template. Once
21 these schedules are returned to Accounting, the templates and supporting
22 schedules are reviewed to determine whether the estimate is based on supporting
23 documentation (i.e., storm purchase orders and receipt documentation, contractor

1 time sheet summaries, payroll recorded, third party confirmations, vendor bids,
2 engineering estimates or other supporting documentation.) Once the final
3 estimates are prepared and reviewed, Accounting works with the Business Units
4 to ensure they accrue for their portion of costs incurred but not yet actualized.

5 **Q. Do you expect material changes in the estimate of 2005 storm-recovery costs?**

6 A. No. The Business Units review their estimates each month following the original
7 estimate until all actual costs have been recorded on the Company's books. As
8 part of this process, they check for payments and updated information received
9 during the month (i.e., additional invoices, foreign utility confirmations/invoices,
10 contractor time sheets/invoices) which would impact their estimate. In addition,
11 FPL will continuously monitor the estimates and internally reclassify line items
12 within the estimates as needed. Therefore, if the estimate needs to be revised, the
13 Business Unit will provide a new estimate and work with Accounting to ensure
14 the appropriate accrual has been recorded. However, in any event, we do not
15 expect to change the amount of costs included in the storm-recovery financing, as
16 I have previously discussed.

17 18 **TRUE-UP MECHANISM**

19 **Q. Will FPL be required to true-up its Storm Charge?**

20 A. Yes. According to Section 366.8260(2)(b)2.e., Florida Statutes (2005), if the
21 Commission issues a Financing Order to FPL, the Commission will;

22 "Include a formula-based mechanism for making expeditious periodic
23 adjustments in the storm-recovery charges that customers are required to

1 pay under the financing order and for making any adjustments that are
2 necessary to correct for any overcollection or undercollection of the
3 charges or to otherwise ensure the timely payment of storm-recovery
4 bonds and financing costs and other required amounts and charges payable
5 in connection with the storm-recovery bonds.”

6 This true-up mechanism helps to ensure that customers pay no more or less than
7 what is required under storm-recovery financing. It also helps mitigate
8 bondholders’ exposure to differences in actual and estimated sales forecasts,
9 uncollectible accounts receivable, and cash flow variability.

10 **Q. How often will FPL file a true-up adjustment?**

11 A. In accordance with Section 366.8260(2)(b)4., Florida Statutes (2005), FPL will
12 file a petition or a letter applying the formula-based mechanism with the
13 Commission at least every six months.

14 **Q. How quickly will a requested true up adjustment to the Storm Bond
15 Repayment Charge and Storm Bond Tax Charge become effective?**

16 A. The Company requests that the Commission either approve the request or inform
17 the Company of any mathematical error in its calculation within thirty days.

18 **Q. Apart from the six month true-ups, does the Company seek authority to file a
19 true-up at any other time?**

20 A. Yes. FPL seeks authority to file for a true up as frequently as quarterly, if
21 required by the rating agencies to achieve the highest possible rating, or at any
22 time if necessary to more quickly accommodate changes resulting from regulatory
23 actions. FPL would seek approval of such a true-up filing on the same basis as

1 the six month true up (i.e., within thirty days of filing).

2 **Q. What is FPL required to include in the true-up adjustment?**

3 A. Section 366.8260(2)(b)4., Florida Statutes (2005) requires FPL to detail in its
4 filing any adjustments made for the undercollection or overcollection of revenues
5 as follows;

6 “Such adjustments shall ensure the recovery of revenues sufficient to
7 provide for the payment of principal, interest, acquisition, defeasance,
8 financing costs, or redemption premium and other fees, costs, and charges
9 in respect of storm-recovery bonds approved under the financing order.”

10 In summary, the Storm Bond Repayment Charge will be reset to a level intended
11 to recover the sum of the following costs:

- 12 • Principal of (in accordance with the Expected Amortization Schedule),
13 and interest on the Storm Recovery Bonds;
- 14 • Costs of the Servicer for the Storm Recovery Bonds;
- 15 • Ongoing costs of administering the SPE and servicing the Storm Recovery
16 Bonds, including, without limitation, trustee fees, expenses and
17 indemnities and rating agency expenses. Details of these costs are
18 illustrated on Document No. MPD-3 in Mr. Dewhurst’s testimony;
- 19 • Amounts required to replenish any amounts drawn from the capital
20 subaccount; and
- 21 • Other ongoing expenses of any other credit enhancement agreement,
22 including any amount or termination payment that might become due and

1 payable by the SPE as a result of any interest rate swap agreement entered
2 into in connection with floating rate Storm Recovery Bonds, if issued.

3 **Q. How will the true-up mechanism work?**

4 A. Document No. KMD-8 demonstrates how FPL proposes the true-up mechanism
5 would work to address the overcollection or undercollection of the Storm Bond
6 Repayment Charges or Storm Bond Tax Charges for the prior period. Once the
7 total average retail Storm Charge per kWh is calculated for the upcoming
8 remittance period, it is broken down to specific charges per rate class. This
9 breakdown is addressed by Dr. Morley in her testimony.

10 **Q. Will over or under recoveries of the Storm Charge be tracked on a class-by-**
11 **class basis for determining future charges?**

12 A. No. Any over or under recoveries for any prior period will simply be added to the
13 periodic revenue requirement for the next period and such cost will be spread over
14 all customers classes. This "cross collateralization" will strengthen the security
15 for the bonds.

16 **Q. Will FPL ever amend the true-up mechanism?**

17 A. FPL will file an amendment to the true-up mechanism with the Commission if it
18 deems it necessary or appropriate to address any material deviations between
19 Storm Charge collections and periodic payment requirements. Any such change
20 could not adversely affect the credit ratings on the Storm Bonds.

1 **Q. How long will the Storm Charge be imposed and collected?**

2 A. The Storm Charge will be imposed and collected until the Storm Bonds have been
3 paid in full or legally discharged and the other financing costs, including the tax
4 liabilities associated with such charges, have been paid in full or fully recovered.

5 **Q. Will FPL reconcile Storm Bond Recovery Bond Collections and estimated**
6 **remittances?**

7 A. Yes. On or before March 1 of each year, the Company will reconcile Storm Bond
8 Repayment Charge collections during the prior calendar year with amounts
9 remitted. If Storm Bond Repayment Charges have been under-remitted, the
10 Company will remit the shortfall to the bond trustee on the next servicer business
11 day. If the Storm Bond Repayment Charges have been over-remitted, then the
12 Company will reduce the next succeeding remittance(s) by the amount of the
13 over-remittance. FPL will also update the data underlying the weighted average
14 days outstanding and delinquency factors.

15 **Q. What will happen with Storm Bond Repayment Charge collections following**
16 **repayment of the Storm Bonds and any related financing costs?**

17 A. Upon payment in full of the Storm Bonds and all related financing costs, any
18 remaining amounts held by the SPE (exclusive of the amounts in the capital
19 subaccount, representing the equity contribution, and any interest earnings
20 thereon) will be remitted to FPL and added to the Reserve, or in the alternative,
21 applied as a credit to customer rates.

22

ACCOUNTING FOR STORM-RECOVERY FINANCING

1
2 **Q. Please describe the overall accounting treatment for storm-recovery**
3 **financing.**

4 A. As explained in Mr. Dewhurst's direct testimony, FPL will conduct storm-
5 recovery financing through an SPE. The SPE will be created solely to facilitate
6 storm-recovery financing and will be a subsidiary of FPL. The SPE and FPL will
7 maintain separate accounting records. The accounting entries necessary to record
8 storm-recovery financing activities, along with an explanation of each, are
9 illustrated in my Document No. KMD-9.

10 **Q. Is FPL requesting Commission approval for any specific accounting**
11 **treatment associated with the proposed storm-recovery financing?**

12 A. Yes. FPL is requesting that the Commission authorize replenishment of the
13 Reserve to approximately \$650.0 million to support future storm restoration and
14 the establishment of a related regulatory asset. In addition, FPL is requesting that
15 the Commission authorize the establishment of a regulatory asset for the 2005
16 storm-recovery costs and the remaining jurisdictional \$1.3 million of 2004 storm-
17 recovery costs charged to the Reserve as previously discussed. Finally, FPL is
18 requesting authorization to sell these regulatory assets together with the remaining
19 amount of unrecovered 2004 storm-recovery costs, which is already a regulatory
20 asset, net-of-tax to the SPE. These regulatory assets on the SPE's books are to be
21 classified as storm-recovery property as defined in Florida Statute (2005)
22 §366.8260 (1)(o).

23

1 **Q. Are the LLC Agreement, Administration Agreement, Storm-Recovery**
2 **Property Sale Agreement, and Storm-Recovery Servicing Agreement**
3 **considered affiliate transactions?**

4 A. Yes. FPL has attached these agreements to Mr. Olson's testimony and requests
5 that the Commission approve FPL entering into these agreements in substantially
6 the form as they are being submitted to the Commission.

7 **Q. What amount of regulatory assets is FPL proposing to sell to the SPE?**

8 A. FPL is proposing to sell regulatory assets net-of-tax in the amount of
9 approximately \$1.0 billion to the SPE. FPL will assume responsibility for the
10 income taxes payable when the Storm Charges are collected from the customer.
11 As such, the deferred income taxes associated with the regulatory assets will
12 remain on FPL's books along with an equivalent regulatory asset amount.

13 **Q. How will the SPE amortize this storm-recovery property?**

14 A. The SPE will amortize the storm -recovery property to expense based on the
15 principal amount required for the repayment of the bonds over the expected life of
16 the bonds.

17 **Q. How will FPL amortize its regulatory assets?**

18 A. FPL will amortize its regulatory assets to expense over the life of the bonds. As it
19 is amortized, FPL will incur current tax obligations related to the revenues
20 collected and will reverse the deferred tax liability related to it.

21 **Q. What are the anticipated accounting entries to be recorded at the SPE?**

22 A. As illustrated on pages 1 and 2 of my Document No. KMD-9, the accounting
23 entries to be recorded by the SPE are as follows: (1) recording of capital

1 subaccount from FPL's equity investment; (2) recording of proceeds from the
2 issuance of bonds; (3) purchase of storm-recovery property net-of-tax from FPL;
3 (4) receipt of cash from FPL for the Storm Bond Repayment Charges collected;
4 (5) amortization of the storm-recovery property; (6) accrual of interest expense;
5 (7) amortization of upfront bond issuance costs; (8) payment of bond principal
6 and interest; (9) recording of on-going operating costs and servicing fees payable;
7 (10) replenishment of capital subaccount, if needed; and (11) transfer of cash to
8 the excess funds account in the event of excess Storm Bond Repayment Charges
9 collected, if any.

10 **Q. What are the anticipated accounting entries to be recorded at FPL?**

11 **A.** As illustrated on pages 3 and 4 of my Document No. KMD-9, the accounting
12 entries to be recorded by FPL are as follows: (1) recording of expenditure of cash
13 to fund the capital subaccount at the SPE and a related investment; (2)
14 establishment of regulatory assets consisting of unrecovered 2004 and 2005
15 storm-recovery costs, and the replenishment of the Reserve with related deferred
16 income tax assets; (3) sale of regulatory assets net-of-tax to the SPE; (4) use of
17 proceeds FPL receives from the sale of its regulatory assets to replenish the
18 Reserve's related fund and to reimburse FPL for previously expended storm-
19 recovery costs; (5) recognition and collection of Storm Charges; (6) amortization
20 of the remaining regulatory assets; (7) reversal of deferred income taxes and
21 payment of current income taxes; (8) earnings on the fund; and (9) payment of
22 revenue taxes.

1 **Q. How will Storm Charges collected from customers be recorded?**

2 A. The Storm Bond Repayment Charge collections will be remitted to and recorded
3 as revenues at the SPE. The collections of the Storm Bond Tax Charge (i.e. the
4 component of the Storm Charge imposed to cover the associated income taxes)
5 will be recorded at FPL.

6 **Q. Please describe how the Company, as Servicer, proposes to remit Storm Bond
7 Repayment Charges to the SPE.**

8 A. As FPL does not track its customer charges on a daily basis, FPL will remit Storm
9 Bond Repayment Charges based on estimated daily collections using a weighted
10 average balance of days outstanding on FPL's retail bills. Collections remitted
11 daily will represent the estimated charges per the servicing agreement. For
12 example, if FPL's retail bills are outstanding, on a weighted average basis, for a
13 period of thirty days, then FPL will remit to the SPE the Storm Bond Repayment
14 Charges billed on a particular date, less an assumed delinquency rate, thirty days
15 thereafter.

16 **Q. How will FPL allocate partial payments on a bill to the Storm Bond
17 Repayment Charge?**

18 A. When doing the annual reconciliations, partial payments will be allocated to
19 Storm Bond Repayment Charges in the same proportion that such charges bear to
20 the total bill. The first dollars collected would be attributed to past due balances,
21 if any. Once those balances are paid in full, if cash collections are not sufficient
22 to pay a customer's current bill, then the cash would be prorated between the
23 different components of the bill.

1 **Q. Assuming the Commission approves the replenishment of FPL's Reserve**
2 **through the proposed Financing Order, what types of charges does FPL**
3 **expect to apply against?**

4 A. FPL requests that the Reserve be used for all of the purposes provided for in and
5 consistent with Rule 25-6.0143, Florida Administrative Code for Account No.
6 228.1, Accumulated Provision for Property Insurance. FPL also requests the
7 Company be allowed to adjust the Reserve for any differences in actual and
8 estimated costs as previously discussed in my testimony.

9 **Q. In the event of a storm loss, what would be the anticipated accounting entries**
10 **that would occur?**

11 A. Storm losses would continue to be recorded on FPL's books. FPL would charge
12 the pre-tax jurisdictionalized storm costs to the Reserve and would withdraw cash
13 from the fund on an after-tax basis. In addition, a proportional amount of the
14 deferred income tax ~~liability~~ ^{asset} associated with the Reserve will be reversed and a
15 current tax benefit for storm losses incurred will be established.

16

17

SUMMARY

18 **Q. Please summarize your testimony.**

19 A. I have presented and discussed the total amount of costs incurred for the 2004 and
20 2005 storms as well as the amounts of storm-recovery costs FPL is requesting the
21 Commission to approve for recovery through a Storm Charge to its customers. I
22 have presented the revenue requirements for the Company's primary and
23 alternative recommendations for storm cost recovery. I have also discussed the

1 controls in place for capturing and recording the costs related to storm restoration
2 activities. In addition, I have proposed a true-up mechanism to be filed at least
3 every six months to adjust the Storm Charge for any over or under recoveries.
4 Finally, I have presented and discussed the necessary accounting entries to record
5 the proposed storm-recovery financing, including special accounting treatment for
6 the set up and sale of regulatory assets which FPL is requesting the Commission
7 to authorize, and the types of charges FPL expects to charge against the
8 replenished Reserve.

9 **Q. Does this conclude your direct testimony?**

10 **A. Yes.**

1 BY MR. ANDERSON:

2 Q Mr. Davis, have you prepared a summary of your
3 testimony?

4 A Yes, I have.

5 Q Would you please provide your summary to the
6 Commission?

7 A Yes, I will, thank you.

8 Commissioners, in this docket FPL is asking for the
9 Commission to approve the issuance of storm-recovery bonds as
10 defined in Section 366.8260, of the Florida Statutes. In my
11 testimony I present the revenue requirements associated with
12 the use of the storm-recovery bonds which is FPL's recommended
13 approach as well as an alternative approach using a surcharge.

14 In my testimony, I describe the computation of the
15 remaining unrecovered 2004 storm costs. Also, I discuss the
16 2005 costs incurred at facilities managed by the power
17 generation division and by the corporate real estate
18 department. Those costs were incurred to restore those
19 facilities to their pre-storm condition.

20 The 2005 storm costs discussed by Ms. Williams have
21 been determined using the actual restoration cost approach with
22 adjustments to remove capital expenditures. FPL believes that
23 it is the appropriate methodology to use because it is the most
24 accurate means by which to measure the costs incurred in
25 repairing the damage caused by the 2005 hurricanes, and it is

1 consistent with the regulatory policy established by this
2 Commission in Rule 25-6.0143, the accumulated provision for
3 property insurance. It utilizes the normal cost accounting
4 practices, processes, and procedures that are relied upon by
5 FPL in the ordinary course of its business. Also, it avoids
6 the necessity of making unsubstantiated estimates in its
7 quarterly financial statements that are inconsistent with the
8 stringent financial reporting requirements imposed by the
9 Sarbanes-Oxley Act of 2002.

10 In the 2004 storm cost recovery order, the Commission
11 used the modified incremental cost method to account for storm
12 costs. Properly applied, the method produces the same results
13 as the actual restoration costs approach with a capital
14 adjustment. However, the incremental method requires the use
15 of indirect and judgmental assessments of budget related data
16 to effect adjustments to amounts determined using the actual
17 restoration cost approach.

18 Proponents of the incremental approach contend that
19 the adjustments are necessary to ensure that costs are not
20 recovered twice, once through base rates and again through the
21 storm-recovery mechanism. Base rates do not include any
22 provision for of the recovery of the activities associated with
23 recovering from a storm, so that contention is incorrect.

24 Also, the activities that would have been performed
25 but for the assignment of personnel to storm restoration do not

1 go away. They are performed by others on overtime or they are
2 delayed until the primary restoration effort has been
3 accomplished, and then they are completed, again using
4 overtime.

5 Finally, hurricane-related outages adversely effect
6 sales of electricity, thereby removing the only mean by which
7 recovery can occur. When these factors are properly
8 considered, the modified incremental cost approach produces the
9 same result as the actual restoration cost approach with
10 capital judgment.

11 The storm recovery bonds discussed by Mr. Dewhurst
12 will be issued by a Special Purpose Entity, or SPE. The SPE
13 will be a wholly-owned subsidiary of FPL, but will be treated
14 as a division of FPL for income tax purposes. Upon issuance of
15 the bonds, the SPE will purchase the storm-recovery regulatory
16 assets approved as a part of the financing order. The income
17 tax equivalent -- this means that only the after tax equivalent
18 of these regulatory assets will be financed. The income tax
19 equivalent of the regulatory assets will remain on Florida
20 Power and Light's books, since FPL will be responsible for
21 paying the income taxes as the amounts are collected from
22 customers.

23 Numerous accounting entries are required to properly
24 account for the issuance of the bonds, collections of storm
25 costs from customers, and the payment of the debt service

1 requirement on the bonds. They are reflected in an exhibit to
2 my testimony. This concludes my summary.

3 MR. ANDERSON: Mr. Davis is available for
4 cross-examination.

5 CHAIRMAN EDGAR: Thank you. Who would like to begin
6 for the cross? Mr. McWhirter.

7 MR. McWHIRTER: Yes, ma'am.

8 CROSS EXAMINATION

9 BY MR. McWHIRTER:

10 Q Good morning, Mr. Davis. My name is John McWhirter,
11 and I'm an attorney for some of your industrial consumers.

12 You were a certified public accountant with the
13 DeLoitte-Touche now known as DeLoitte, Haskins, and Sells?

14 A Yes.

15 Q And you came to Florida Power and Light in 1991?

16 A 1988. I joined Florida Power and Light in 1988 as --
17 at that time it was called the comptroller. In 1991, I became
18 the Vice-President and Controller, so a change in title.

19 Q You became comptroller in July and then Hurricane
20 Andrew came do visit Florida Power and Light. When was that?

21 A That would have been in August 1992.

22 Q So you're familiar with the circumstances that your
23 company utilized to deal with that catastrophic event, are you
24 not?

25 A I'm certainly familiar with the accounting. The

1 underlying restoration activities I would defer to
2 Ms. Williams.

3 Q At that point in time, under the Commission's
4 accounting rules, did you have a storm reserve account?

5 A Yes, sir, we did. We also had insurance that covered
6 a substantial portion of it. After Andrew there was no more
7 insurance.

8 Q And after Andrew the account went into deficit?

9 A No, it did not.

10 Q You had sufficient money in 1993 to pay all the
11 Hurricane Andrew damages?

12 A The answer is yes and no. Yes in the sense that we
13 had insurance. The only amount that was not covered by
14 insurance was approximately \$20 million, which was the
15 insurance deductible. We had the storm fund. The insurance
16 deductible was charged against the storm fund, and that is why
17 I have said several times in my testimony that the approach
18 that the company is sponsoring here produces basically the same
19 result as would be achieved using replacement cost insurance.
20 Because back in Andrew, the insurance company covered a certain
21 portion of the loss, the remainder of the loss was covered by
22 the storm insurance reserve.

23 Q Mr. Davis, I didn't ask you about insurance at this
24 juncture, I was just trying to find out about the storm damage
25 reserve. And in order to speed things along, if you would

1 restrict your responses to my questions, it would be helpful.

2 A Okay. But to get to the amount that is charged to
3 the reserve, in 1992 you have a total storm cost which would be
4 covered by insurance, and then there would be a portion which
5 was not covered by insurance which would be charged to the
6 storm reserve and would be borne by the customers.

7 Q All right, sir. You say borne by customers, how
8 was -- was that a fund of cash, the storm reserve at that time,
9 or was it an accounting entry?

10 A It is basically both. The storm reserve, if you look
11 at the liability side, the creation of the reserve that is
12 covered by -- I forget the rule number, but the self-insurance
13 reserve, storm insurance reserve that is on the books. That is
14 on the liability side. And it is, if you will, the measure of
15 the ability of the company to absorb a loss without going to
16 the income statement.

17 Over on the asset side, you have a storm reserve.
18 Basically the storm reserve, a cash account, if you will,
19 invested. All earnings from that went back into the storm
20 fund. That would be, basically, the after tax equivalent of
21 the storm reserve. Because the storm reserve was not
22 deductible for tax purposes, therefore, the sources of money to
23 pay for the storm losses which were absorbed by the reserve
24 would come from two places. One, the cash account,
25 representing about 61 percent of the storm reserve, and the

1 rest, roughly 38 or 39 percent, would come from a cash tax
2 savings.

3 Q All right. So the cash account that you are speaking
4 of, the source of that cash account, did the money come from a
5 surcharge on customers, or was it money that was taken out of
6 the money customers paid through their base revenue?

7 A It would have come from a storm accrual that had been
8 approved as a component of base rates, unlike today where we do
9 not have any storm dollars in base rates.

10 Q All right. And then that money was invested. What
11 kind of investments does Florida Power and Light put the money
12 into?

13 A Basically, the investments would be very highly rated
14 short-term investments, because we were attempting to deal with
15 an event which was, I'll say unpredictable, so the investments
16 were short-term. They may have been municipal bonds, they may
17 have been short-term investments. Not bonds, but short-term
18 municipal investments or short-term taxable investments so that
19 they could be liquidated quickly without significant loss of
20 principal.

21 Q And would you describe those investments? Were they
22 government bonds that you used, money market accounts, stocks
23 and bonds of corporations, or what were they?

24 A It would have been debt securities of some fashion.
25 It could be commercial paper, it could be very short-term

1 indebtedness of governmental agencies, municipal governments.
2 That's as far as I would go. I don't recall specifically what
3 they were invested in.

4 Q Are you allowed to invest in debt securities or other
5 securities issued by FPL Group subsidiaries?

6 A I do not know if there was a prohibition against it.
7 I can say that we did not do that.

8 Q Is it your intention to maintain a policy in which
9 you will not invest in your intercorporate transactions when
10 you have funds in a storm reserve?

11 A The investment policy does not fall within my
12 purview. I can't imagine us doing that, but I can't state
13 unequivocally. I would defer to the Commission. If that was a
14 concern of the Commission, I would suggest that they establish
15 that as a requirement.

16 Q After Hurricane Andrew, the storm fund -- you
17 concluded that it was inadequate for the type of catastrophic
18 storm that might come in the future, and the accrual amount was
19 increased. What was the annual accrual after the order issued
20 in connection with Hurricane Andrew?

21 A I am going to be a little uncertain on the precise
22 years, but ultimately the accrual was increased to 20.3 million
23 per year, and we accrued the 20.3 million until somewhere in
24 the 2000. Certainly we stopped -- well, until the most current
25 rate settlement, and at that point the 20.3 million was removed

1 from base rates.

2 Q All right. So annually from base rates you accrued
3 \$23 million, and by 2004 when we had that catastrophic
4 hurricane season, the amount of the fund had grown to what
5 amount?

6 A Approximately \$356 million.

7 Q And if you multiply 23 times 10, that's only
8 something like \$230 million. So you must have had fairly
9 substantial earnings on that account?

10 A We had earnings on the fund because all earnings that
11 were earned on the cash investments, it is a funded reserve on
12 the cash investments were added to the fund as well as there
13 were some additional monies that were left as a result of the
14 insurance recoveries associated with Andrew, which the company,
15 with the Commission's approval, put into the reserve. There
16 were also dollars that were put in there that were to be used
17 for subsequent repairs of underground lines. We also made a
18 special cash --

19 Q You don't need to go into that. I was just wondering
20 if the investments had brought it up by about \$100 million over
21 that 10-year period?

22 A It would have been, I think, less, because I was
23 going to say there is a \$35 million special contribution that
24 was made at one point.

25 Q I see.

1 A But it's a combination of dollars accrued through
2 base rates and earnings, suffice it to say.

3 Q Now, how is that fund of money you have that is -- I
4 guess it's set aside out of the general use of your cash funds.
5 How is that money treated in your rate base?

6 A The money is, one, it's included in a special fund
7 which is not available for use for general corporate purposes,
8 it's held specifically for the storm reserve. That would be
9 the same treatment that would be accorded to the monies if we
10 replenished the reserve. It is excluded from rate base. The
11 reason that the reserve is excluded from rate base is that it
12 is a funded reserve, and the assets of the fund are also
13 excluded from rate base because --

14 Q And how is it treated in your capital structure?

15 A Because it is excluded from rate base, it would come
16 out of -- there are two specific adjustments that are made as
17 part of the surveillance report process. You pull out the
18 reserve and you pull out the investment fund. There are two
19 different categories of investments or eliminations or
20 adjustments that are made.

21 Q All right. So it doesn't even show in your capital
22 structure that you show to the Commission?

23 A There would be one impact. You have the deferred
24 taxes, and the deferred taxes --

25 Q I'm going to get that in a minute. Just tell me

1 about the reserve fund?

2 A Well, the reserve fund is excluded, it is not a part
3 of rate base.

4 Q And it is not part of your capital structure, is that
5 correct?

6 A Well, capital structure supports rate base. If it's
7 not rate base, then by definition it is not in capital
8 structure.

9 Q All right. Now, when you collected that money from
10 your base rates, you had to pay current income taxes on it, or
11 did you have to pay current income taxes at that time?

12 A Yes, we would have paid income taxes on it, because
13 the 20.3 million accrual is not a deductible expense.

14 Q If you collected \$100, approximately \$40 of that
15 would be subject to income tax. So did the reserve reflect a
16 balance of \$100, or did the reserve reflect a balance of \$60?

17 A The reserve would reflect a balance of \$100
18 representing the capacity to absorb storm losses. Sixty
19 dollars, using your percentages, would be would go into the
20 special fund, the storm fund, investment fund. Forty dollars
21 would be paid as current taxes.

22 Q And you don't pay the taxes the moment that you get
23 them, you pay them at some future time. So you would put it in
24 a deferred tax account until the time the taxes are to be paid,
25 is that correct?

1 A No, sir, that is not correct. You pay the taxes
2 currently. However, what you do is set up a deferred tax asset
3 representing the fact that at a point in the future when that
4 reserve, the monies that were added to that reserve become
5 deductible, essentially you have an asset, a receivable from
6 the government.

7 Q I see. So how is the deferred tax account treated in
8 your capital structure?

9 A It is included along with all other deferred taxes.
10 Basically, it is undifferentiated deferred taxes that are added
11 together and treated as a zero cost component of capital.

12 Q And the deferred taxes are, as you say, cost-free
13 capital in your rate structure, and that tends to bring your
14 required return down?

15 A I don't believe -- it would not bring the return
16 down. What it would do would be -- you would still have a
17 return that is associated with the common equity. You would
18 have a return that is associated with the debt. That
19 particular component has a zero. If you blend them all
20 together and calculate a weighted average cost of capital, then
21 that overall return, yes, it would come down.

22 Q For instance, your return on equity has a range from
23 10 to 12, but equity is only part of your capital structure.
24 So when you come up with your combined weighted average cost of
25 capital, it only represents about 50 percent of the cost of

1 capital, and deferred taxes is something like 17 percent?

2 A Off the top of my head, I don't know the percentage.
3 Subject to check, 17 is fine.

4 Q Now, let's go to your Exhibit KMD-2. And that, I
5 believe, is Exhibit 17 in the record. It looks like what you
6 have done there is shown that the 2004 storm cost is
7 \$885,000,000, and the 2005 storm costs surprisingly is less
8 than your cost in 2004, but the total of those is \$1.7 billion.
9 And then you discount that sum by \$680 million. Is that
10 because -- well, I'm not going to ask you a question about it
11 yet now. But then there is a footnote down here that says the
12 objective of this schedule is to show the maximum amount of
13 cost eligible for financing under the IRS Safe Harbor
14 Provisions and the actual amount FPL proposes to finance.

15 Tell us what those Safe Harbor Provisions are?

16 A I believe that that is described in my direct
17 testimony. I won't go looking for it now, but it is basically
18 to comply with a revenue ruling that governs the issue of
19 whether or not the issuance, the receipt of proceeds from the
20 issuance of securitization bonds are taxable. And, basically,
21 one of those requirements are the costs relating it to an
22 amount of costs that have been approved by a Commission to be
23 recovered.

24 Q When you receive the proceeds of that bond sale, it
25 is not taxable to you, is that correct?

1 A That is the current assumption. That is certainly
2 our belief that they will not be taxable to us, and that was
3 the reason for putting the schedule together to provide that
4 information for the record.

5 Q Well, there is a revenue ruling to the effect that
6 it's not taxable, so you can rely pretty assuredly that it is
7 not going to be taxed when you get the bond proceeds because it
8 is like a debt, isn't it?

9 A Correct. I mean, the Internal Revenue Code does not
10 always follow logically along, but I think to bring that part
11 to a close, it is certainly our belief that it will not be --
12 the issuance of the securitization bonds will not be a taxable
13 event to Florida Power and Light Company.

14 Q Did the IRS give any reason why it would require you
15 to reduce the amount of the bond issue by 38.75 percent or 575
16 percent?

17 A The revenue ruling does not address the tax
18 deduction. What we are doing there is we are saying consistent
19 with what has occurred in the past, we are saying that these
20 costs will be deductible for tax purposes as most of the storm
21 costs are. We made an overall assumption that all of these
22 costs would be deductible, that we would receive a current tax
23 benefit for that. And that, therefore, there was not a need to
24 finance those dollars. So the tax deduction is there to
25 illustrate that purpose. That is why the financing --

1 Q I want you to go slower, because I've got a
2 fourth-grade mind when it comes to accounting. So let's go
3 slowly, if you don't mind.

4 A Okay. What we are asking for, I think it would be
5 better to look at the bottom half of the schedule starting on
6 Line 12.

7 Q All right, sir.

8 A And in Line 12, what we are specifically asking for
9 is \$1,690,160,000 of costs to be securitized. However, the
10 amount that will actually be issued in bonds will only be one
11 billion fifty, which is the 1.38 billion shown, it looks like
12 on Line 22, plus the issuance costs of about \$11 million. So
13 what is happening there is that we are providing the benefit to
14 the customer of having deducted the storm losses and received a
15 current cash benefit for those losses.

16 (Transcript continues in sequence with Volume 6.)
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STATE OF FLORIDA)

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CERTIFICATE OF REPORTER

COUNTY OF LEON)

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

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

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

DATED THIS 21st day of April, 2006.



JANE FAUROT, RPR
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