BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition by Progress Energy Florida, Inc. for approval to recover modular cooling tower costs through environmental cost recovery clause.	)	DOCKET NO. 060162-EI
	)	Filed: May 31, 2007

CITIZENS' POST HEARING BRIEF AND STATEMENT OF POSITIONS

INTRODUCTION AND OVERVIEW

In an industry in which numerous firms compete for the consumer's business, the competitive market "regulates" instances in which a provider of goods or services attempts to charge unreasonably high prices. Whether the unreasonably high price is due to inefficiency or an effort to gouge, the consumer can elect to obtain the product from a different provider who is anxious to compete based on price.

In Florida, electric service is provided by a monopoly enterprise. A single regulated electric utility serves 100% of the retail customers in its service area. Customers can wield no discipline to motivate a utility to keep its prices reasonable by availing themselves of alternatives (other than generating their own power or moving away from the service area). For this reason, the Legislature gave the Commission the task of ensuring that a monopoly utility subject to its jurisdiction charges rates that are fair and reasonable. Sections 366.05 and 366.06, Florida Statutes.

In this case, PEF asks for permission to flow an initial installation cost of $516,000 and $4.6 million of other O&M costs incurred during 2006, and approximately $3-4 million of ongoing rent and other O&M costs annually, through either the fuel cost recovery clause (PEF's initial choice, which was initially discouraged by the Commission Staff) or the environmental cost recovery clause. To gauge whether the request is fair and reasonable, or

alternatively, whether granting the request would result in an unwarranted, unfair and unreasonable rate increase, it is necessary to analyze PEF's petition in the context of the bigger ratemaking picture.

The testimony of OPC witness Patricia Merchant, a certified public accountant who has extensive knowledge of utility ratemaking in Florida, provided this needed perspective. She testified that the base rate mechanism is the principal regulatory tool that the Commission uses to carry out its principal oversight function. Generally, a regulated utility is entitled to charge rates that generate revenues sufficient to reimburse the utility for its prudent, reasonable costs of providing service, plus an opportunity to earn a fair return on its investment. To quantify the revenues that correspond to this formula, the Commission isolates and reviews operations of a period of time (test year) to identify the costs that will be representative of the future periods during which the rates will be in effect. (TR 51) The Commission quantifies the levels of the many categories of costs (including taxes and debt service) and the appropriate return on capital investment to arrive at the utility's total annual revenue requirements. The Commission then fashions rates which, when applied to anticipated consumption, will generate the targeted revenues.

Regulators understand, and ratemaking principles contemplate, that once rates become effective, the environment in which they function will not be static. (TR 52) Instead, all of the components of the ratemaking "formula"—types and levels of costs, the numbers of customers on the system, consumption patterns and sales-- will vary from the assumptions underlying the test year exercise. The Commission assigns a "range of reasonableness" to the authorized rate of return. While the actual cost patterns and revenue levels will vary from those assumed at the time of the rate case, as long as the relationship

between total costs and total revenues results in an earned return that falls within the range established by the Commission, the return is deemed to be fair. (TR 53) (A corollary of this observation is that as long as the utility's revenues exceed its costs and provide positive earnings, it is recovering all of its costs, whether or not the specific costs were explicitly built into test year assumptions.) (TR 53) A change in the level of an individual cost will not necessarily cause the return to fall below the range set by the Commission, because it may be more than offset by changes in other factors that result in decreases in other costs, or in an increase in revenues. Accordingly, absent a proceeding in which the utility's circumstances are reviewed, the base rates do not change as a result of fluctuations (up or down) in base rate revenues, costs, or earnings.

In the event its earned return falls below a reasonable range, the utility may request an increase, in which case the Commission and affected parties will examine the request in light of the totality of the utility's circumstances. In the event the return becomes excessive, the Commission can initiate proceedings to reduce rates.[1]

While the base rate mechanism is the primary ratemaking tool, Florida utilities are also allowed to implement special cost recovery mechanisms that operate separately from base rates. Two of them are involved in this docket. The fuel cost recovery clause is intended to enable the utility to respond to volatile changes in fuel costs without having to experience the delays of a base rate proceeding. The Legislature directed the Commission to establish the environmental cost recovery clause to enable the utilities to collect the costs of complying with the terms of environmental permits outside of base rates. (TR 54) Unlike

[1] Currently, PEF's rates are governed by the terms of a stipulation in which the authorized rate of return is replaced by an agreed range of revenues. However, the discussion of general ratemaking remains pertinent. The stipulation is consistent with this treatment, in that it provides that during the term of the stipulation base rates will function without change, even though PEF's costs and revenues will fluctuate, unless PEF's earned rate of return on equity falls below 10%, at which time it may seek an increase in base rates.

the utility's base rates, which are designed to recover a myriad of fluctuating costs without themselves changing, each of the fuel and environmental cost recovery factors is intended to track changes in a specific, narrowly defined set of costs. (TR 54)

When a utility incurs a new cost that is deemed to be related to base rates, its total costs increase but base rates and base revenues do not change; customers' bills will remain the same and earnings (profits) are lower than they would be absent the new cost.[2] If instead the utility places the same new base rate-related cost with those that flow through either the fuel cost recovery clause or the environmental clause, the customers' bills collectively go up by the amount of the new cost and the utility's earnings (profits) are insulated and preserved. (TR 55) In other words, utilities have a powerful incentive to pass as many such costs as possible through a cost recovery clause. (TR 56)

However, a special cost recovery clause was intended to be, and is, a limited departure from the base rate mechanism, which is characterized by the ability to take into account the entire enterprise and the dynamics that affect it, and to regulate based on an analysis of the utility's overall circumstances. To ensure the utility does not circumvent this holistic regulation by exceeding the legimate scope of the special cost recovery clause, each of these clauses has eligibility criteria. To protect customers from unwarranted increases in the size of their bills, which is the Commission's primary reason for being, the Commission must police requests to pass costs through the cost recovery mechanisms carefully. To fail to do so, and to allow an ineligible cost to flow through the clause, would increase customers' bills to protect corporate profits from the effects of costs that base rate revenues are intended to fund, and would by definition render the utility's charges unfair and unreasonable. It

[2] Concomitantly, if a utility experiences a reduction in a cost, or if costs remain constant while revenues increase, base rates do not change and the utility's earnings (profits) increase

would enable the utility to circumvent the review of the totality of its circumstances, including those factors (customer growth, for instance) that serve to offset cost increases and maintain the overall relationship between costs and revenues adequate to yield a fair return, and to implement what would effectively be a base rate increase through the "back door" of the special cost recovery clause. (TR 63)

To filter certain items from the costs nominated by the utility for a special cost recovery clause does not mean the utility will not recover the cost; it means the cost will be recovered through base rates. (TR 63) Again, as long as base rate revenues exceed the costs that base rates are intended to collect, a utility recovers all of those costs, whether or not they were explicitly built into test year assumptions when the rates were designed. Any purported claim by a utility or utility's witness to the contrary must succumb to this immutable and irrefutable mathematical truism.

For the reasons that follow, the costs of the modular cooling towers do not satisfy the eligibility criteria of either the environmental cost recovery clause or the fuel cost recovery clause.[3] To prevent unwarranted increases to customers' bills, the Commission should deny PEF's request.

STATEMENT OF FACTS

The pertinent facts are largely undisputed. However, Citizens believe an exposition of facts will assist in the analysis of clause eligibility criteria that follows. Progress Energy Florida, Inc. ("PEF") owns and operates Crystal River Units 1 and 2, which are coal-fired,

[3] Citizens do not challenge the prudence of the decision to install the modular cooling towers; rather, Citizens believe that for PEF to fail to address the condition requiring it to derate base load units would be *im*prudent. Citizens submit that the measure is necessitated by PEF's obligation to customers to operate prudently and efficiently, and the costs are among those O&M costs that base rates are designed and intended to recover. The fact that an expense is prudent does not qualify it for a special cost recovery mechanism.

base-loaded generating units located at PEF's Crystal River plant site. The units burn coal to produce steam, which drives a turbine/generator set to produce electricity. After it exits the turbine, the steam must be cooled and condensed to water form so that it can be returned to the boilers in an ongoing cycle. To accomplish this, PEF draws water from the Gulf of Mexico and uses it in a form of heat exchangers called "cooling towers" to condense the steam. In this process, heat is transferred from the boiler steam to the cooling tower water, which is discharged into a canal leading back to the Gulf.

The terms of an environmental permit – specifically, the permit issued under the federal National Pollution Discharge Elimination System ("NPDES") program – require PEF to ensure that the cooling tower water does not exceed 96.5° Fahrenheit, as measured by a three hour rolling average, when PEF discharges it into the return canal. The NPDES permit was issued to PEF in 1988. (TR 44) Since 1988, the permit imposing the 96.5° Fahrenheit limitation has been in effect continuously.

The cooling towers that PEF installed to serve Crystal River Units 1 and 2 have a finite capacity to condense steam without exceeding the temperature limit placed on exiting cooling water. The capability is affected by the temperature of the cooling water at the time it is drawn from the Gulf - - the higher the initial temperature, the smaller the quantities of water that can accept heat from process of steam and remain below 96.5° Fahrenheit. Sufficient process water for steam in the boiler is necessary for operations at maximum electrical output. A mechanism to cool and condense steam to water in those needed quantities is necessary to support operations at that level.

In recent periods, and especially in 2005, the temperature of "intake" cooling water has been elevated as compared to the past norm. (TR 25) To compensate for the reduced

cooling capacity created by the higher intake temperature, PEF has lessened steam production, and therefore necessarily reduced ("derated") the electrical output of Crystal River Units 1 and 2, when necessary to remain in compliance with the terms of the NPDES permit. When PEF cannot operate these base load units at full capacity when they are needed to meet demand, PEF must generate or purchase more expensive power to replace it. The more expensive replacement power necessitated by the inability to operate the most economical base load plant at full output, as they are intended to operate under normal conditions, increases fuel costs and raises customers' bills.

To contend with the recent elevation in the temperature of incoming cooling water, PEF rented and installed "modular cooling towers." The modular cooling towers augment the cooling capacity of the existing system, reduce the need for "derates," and enable PEF to operate the base load units at higher levels of output than is possible when cooling capacity is constrained. The costs associated with the cooling towers include mobilization and set-up costs, rental fees, and demobilization costs, and costs to replace fill. These costs are in the nature of operations and maintenance (O&M costs). O&M costs are "base rate-related," meaning they normally form part of the overall costs of providing service that base rate revenues are intended to defray.

The test period for PEF's most recent base rate, revenue requirements case was 2005. That case ended with the Commission's approval of a stipulated settlement reached by the parties.

For the year ending December 31, 2006, PEF reported an earned return of 8.53%, including 11.00% return on equity.

STATEMENT OF THE CASE

On February 24, 2006, PEF filed a petition seeking permission to pass the costs of the modular cooling towers through the fuel cost recovery clause. On July 13, 2006 PEF resubmitted its petition, this time requesting permission to pass the costs of the modular cooling tower through the environmental cost recovery clause.

Originally, the case was slated to be processed via an order on Proposed Agency Action ("PAA"). When the Citizens expressed their opposition to the PEF's reformulated petition, during the agenda conference of August 29, 2006, the Commission decided to set the matter for an evidentiary hearing. The Commission directed that the hearing encompass whether the costs of the modular cooling towers are eligible for either the environmental cost recovery clause or the fuel cost recovery clause. The hearing was convened on May 1, 2007. At that time, by stipulation the prefiled testimony of witnesses for PEF and Citizens was entered into the record.

ARGUMENT

ISSUE 1: What is the appropriate mechanism to recover the prudently incurred costs of Progress Energy's temporary cooling tower project?

(A) Should PEF recover costs for the Crystal River Units 1 and 2 cooling tower project through the Environmental Cost Recovery Clause?

OPC: *No. These costs do not qualify as ECRC costs pursuant to the Commission's policy defined in Order No. PSC-94-0044-FOF-EI. To qualify costs for recovery through the ECRC, a utility must demonstrate that the costs were the activity is legally required to comply with a government-imposed environmental regulation that was enacted or became effective, or whose effect was triggered after the company's last test year upon which rates are based. The cooling towers are intended to help PEF comply with a requirement that predated the passage of the ECRC statute and the company's last rate case. Accordingly, the effect of the requirement was not "triggered" after PEF's last rate case. The "triggering event" language in the Commission's policy refers to changes in

> regulatory requirements, not operating conditions. The "triggering event" provision would be applicable, for instance, to a regulation that was enacted in 2003 but imposed requirements that take effect in 2009 and require money to be spent in 2008 to comply with the 2009 requirement. Thus, the costs do not satisfy the Commission's eligibility criteria and are ineligible for the ECRC.
>
> This result does not mistreat PEF, as it will recover the costs, as it recovers all costs other than those that qualify for the exceptional treatment of a specific recovery mechanism, through base rate earnings. The effect will be negligible--the stand-alone impact on the company's earned rate of return during the first, highest-cost year is less than 9/10 of 1%--and may be offset by growth in revenues or declines in other costs.*

Citizens and PEF agree that, to qualify for the environmental cost recovery clause, the activity must be "legally required to comply with a government imposed environmental regulation that was enacted or became effective, or whose effect was triggered after the company's last test year upon which rates are based . . ."

Citizens and PEF also agree that the government imposed environmental regulation that imposes the temperature condition on water discharged from the cooling towers was enacted and became effective in 1988, well prior to the last test year (2005) on which PEF's rates are based.

PEF's assertion that the costs of the modular cooling tower qualifies for the environmental cost recovery clause is based on the argument that the effect of the regulation was "triggered" after the company's last test year upon which rates are based. PEF's argument fails.

The first reason why the Commission should reject PEF's argument is that it conflicts with the language of the order in which the Commission articulated the criterion. Within the criterion, the references to "became effective" (after the most recent test period) and the alternative possibility, which is that the "effect was triggered after" (the test period) are

separated by the disjunctive "or" : the conditions purposely are separate and distinct. The proper construction of the criterion—the only one that gives effect to its careful delineation of concepts-- is that, with respect to those costs that qualify for inclusion, *either* a regulatory requirement becomes effective after the utility's most recent test year, *or* its effect is triggered after the test year. Straightorward logic says that it would be impossible for the same regulatory requirement—in this instance, the 96.5° ceiling-- to take effect prior to the test year *and* have its effect triggered after the test year. It is undisputed that the NPDES permit containing the 96.5° temperature limitation took effect in 1988. It is therefore impossible for its effect to have been "triggered" after 2005.

PEF argues that the increase in the temperature of the intake water was the "triggering" effect. Citizens' witness Tom Hewson refuted this notion. Mr. Hewson is by training a civil engineer. He has been involved as an expert with environmental permits and environmental equipment pertaining to the electric industry for some thirty years. Mr. Hewson showed that the increase in temperature is merely a change in an operating condition that affects the measures necessary to comply with a requirement already long in effect. The temperature requirement was 96.5° Fahrenheit in 1988, 1989, 1990, 1991, 1992, 1993, 1994, 1995, 1996, 1997, 1998, and in every other year prior to, during, and following the 2005 test year. PEF incurred costs to comply with the requirement in each of those years prior to 2005. The fact that the temperature differential in 2005 and subsequent years requires a level of compliance activity greater than was necessary in prior years does not "trigger" the effect of the 1988 regulation.

Mr. Hewson illustrated a far more reasonable and plausible meaning of "triggered." (TR 44) Some environmental regulations, including the recent Clean Air Interstate Rule and

the Clean Air Mercury Rule, have requirements that are phased in over time following the date of enactment. For example, a regulation may be enacted in the year 2004, but may specify increasingly stringent conditions that do not come into being until 2007 and 2011. In that instance, the regulation's enactment date differs from the date the measure becomes a requirement for those to whom it is applicable. That is not the situation here. There has been no change to the 96.5° requirement since the 2005 test year.

PEF's witness Javier Portuondo cited Rule 62-62-761, Florida Administrative Code in support of PEF's "triggering" argument. *The rule cited by Mr. Portuondo supports Citizens' position, not PEF's.* At page 71, he states: "As shown on Table AST of page 5 of the exhibit, although the rule amendments were in place since 1998 (before the test year upon which PEF's then-current rates were based), PEF was not required to undertake any compliance activities to meet with the specific requirements for the storage tanks at issue . . . until 2005 and 2010. In other words, the full effect of the pre-existing environmental requirement was not triggered until after PEF's last base rate proceeding. (Exactly so!! The triggering factor in each of the rules cited by Mr. Hewson and in the rule cited by Mr. Portuondo is the operative date specified within the regulation on which the requirement kicks in. It has nothing to do with changes in activity levels needed to comply with a continuously effective requirement.)

However, Mr. Portuondo then claims, "The same logic applies to the Modular Cooling Tower Project because the full effect of the NPDES permit limit was not triggered until after PEF's base rates were established." Mr. Portuondo is wrong: his argument is *illogical*. The "full effect" of the NPDES permit is simply the requirement that exiting water not exceed a temperature of 96.5° Fahrenheit. Had the NPDES permit imposed a

requirement of 96.5° during 1988-2005, and then mandated additional cooling to a standard not to exceed 94° beginning in 2006, Mr. Portuondo would have an argument. If the NPDES permit had said in 1988 that the original 96.5°requirement would not become effective until 2006, Mr. Portuondo would have an argument. Instead, however, the NPDES permit became "fully effective" in 1988, 17 years prior to the utility's most recent test year. PEF is simply trying to stretch the definition of the eligibility criterion to encompass a change in operating conditions and measures needed to comply with this "fully effective" regulation in order to avoid having to absorb the costs of the modular cooling towers through base rate earnings. However, the change in the cost to adhere to an established requirement is an example– indeed, a textbook example--of the type of fluctuations in O&M cost levels that base rates are designed and intended to accommodate. As stated earlier, to allow PEF to pass an ineligible cost through the clause would be, plainly and simply, to permit an unwarranted increase to customers' bills "through the back door." The resulting factor would be by definition unfair and unreasonable.

NOTE: Citizens contend that costs should be recovered through base rates unless they meet the strict eligibility criteria of a special cost recovery mechanism. Citizens believe a more orderly presentation of argument would be to consider the eligibility criteria of each of the cost recovery mechanisms before addressing the base rate alternative. Accordingly, Citizens will present argument on (C) before (B).

C) Should PEF recover costs for the Crystal River Units 1 and 2 cooling tower project through the Fuel Cost Recovery Clause?

CITIZENS: *No. Order No. 14546, containing eligibility criteria, lists generating plant O&M (of which these costs are examples) in the section identifying *ineligible*

> costs. Further, the modular cooling tower costs are not fossil-fuel related and are well removed from the fuel process. In addition, when the utility cannot operate base load units at full capacity, costs borne by customers are increased above the norm. Measures designed to enable the utility to correct abnormally expensive operations and revert to normal, economic operations do not accomplish "savings" as contemplated by the Commission in Order No. 14546. Finally, if one accepts PEF's open-ended fuel savings argument, then by extension all costs incurred in planned or unplanned outages of any lower-fuel cost plant would qualify for the fuel clause—an absurd proposition. These costs belong in base rates.*

PEF largely bases its (alternative) request for authority to pass the costs of the modular cooling towers through the fuel cost recovery clause on the eligibility criteria contained in Commission Order No. 14546. Item 10 of the list of eligible costs states that, on a case-by-case basis, the Commission will consider requests by utilities for approval to pass costs that ordinarily would be treated as related to base rates through the fuel cost recovery clause where the utility can show the costs enable it to lower fossil fuel costs. *However*, the beginning point of the analysis is not Item 10, because Order No. 14546 delineates – not only the costs deemed eligible – but the costs that are *ineligible*. Only costs other than those deemed ineligible are potential candidates for case-by-case consideration under Item 10. Generating plant O&M, such as the costs associated with the modular cooling towers, don't make the first cut. Following the list of eligible costs, including the "case-by-case" Item 10, at page 5 the Commission stated:

> The following types of fossil fuel-related costs are more appropriately considered in the computation of these rates:
>
> 1. Operations and maintenance expenses at generating plants or system storage facilities.

As structured within Order No. 14546, it is clear that O&M expenses at generating plants, of which the costs of the modular cooling towers are examples, fall outside the list of eligible costs – including those that may be justified for inclusion under the rationale of Item

10. (Citizens are attaching pages 4 and 5 of Order No. 14546 to the brief as Exhibit A for ease of reference.)

Even if, for the sake of argument, one considers the applicability of Item 10 to the modular cooling towers (which would not be proper to do in light of the explicit exclusion of generating plant O&M costs), these costs would not qualify. Order No. 14546 was issued in 1985 in a docket created specifically to consider the treatment of the costs of "fossil fuel." In fact, the word "fossil" appears in the order 23 different times. More importantly, the order contains an illustration of the *type* of expenditure the Commission had in mind at the time. The given example is a utility that leases an additional oil storage tank for a short period to enable it to purchase a shipment of oil on favorable terms: the rent paid to lease the oil tank makes possible the fuel savings, and would qualify for inclusion in the fuel cost recovery clause. The expenditure is directly related to the delivered cost of fossil fuel to be burned in the boilers to generate electricity.

By contrast, the modular cooling tower costs are not "fossil fuel related:" they are in the nature of plant operations and maintenance (O&M) expense. In fact, PEF witness Mr. Lawery said of the expenses, "The annual expenditures are expected to include O&M expenses for unit mobilization and setup, rental fees, de-mobilization, and fill replacement." (TR 37) Citizens' witness Tom Hewson observed that the purpose of the modular cooling towers is not to affect the delivered cost of fuel that will be burned, but to "improve station performance." (TR 46). In this respect, the modular cooling towers are no different from any other O&M expense incurred at power plants—they are incurred to enhance performance. (It is therefore for good reason that Order No. 14546 excluded such costs from the list of eligible costs.) To allow PEF to shunt these particular costs through the fuel cost

recovery clause would be to expand the clause beyond its intended purpose, and to invite utilities to seek to pass more routine O&M expenses designed to enhance performance through a cost recovery clause instead of collecting them through base rates, all to the detriment of customers, who would see their overall bills rise.

A separate reason, equally fundamental and equally compelling, argues against PEF's effort to flow the costs of the modular cooling towers through the fuel cost recovery clause: The costs cannot legitimately be regarded as leading to "savings" in the sense the Commission intended when it created the exception found in paragraph 10 of Order No. 14546. Crystal River Units 1 and 2 are base loaded, coal fired units. "Base loaded" means that they are among the most economical to operate relative to other units on the system, and are operated to the maximum extent before the more expensive units are called on, so as to minimize overall fuel costs. The "derating" of a base loaded unit—that is, the reduction of a coal-fired unit's output at a time when it is the most economical source on the system—is an anomaly; an unfortunate aberration; an unhappy and expensive departure from the norm. The derating creates an undesirable inefficiency in generation that increases costs borne by customers above what they are when PEF can operate Crystal River Units 1 and 2 without limitation. The modular cooling towers are, then, not a measure undertaken to improve on the normal status quo: they are a form of remedial action taken to patch an operational problem that is creating artificially high costs. To incur O&M costs necessary to restore Crystal River Units 1 and 2 to full service is not a program to save fuel costs in the usual sense—it is a measure that is necessary to rid the system of inordinately high costs and return to the lower system costs that PEF was experiencing prior to the problem caused by insufficient cooling capacity. A measure designed and needed to rectify abnormal operations

and associated high costs and restore the baseloaded unit to normal operation is not fairly characterized as accomplishing "fuel savings."

For the same reason, PEF is in error when it portrays a continuation of the derating of Crystal River Units 1 and 2 as an acceptable, alternative means of complying with the NPDES permit. (TR-70). (TR 70) Fundamentally, a regulated utility has an obligation to its customers to operate efficiently. Where a more cost-effective solution *from customers' perspective* is available, PEF has an obligation to pursue it. A decision to impose on customers the higher costs of more expensive generation in order to avoid incurring O&M costs that would return base load units to full service would conflict with that basic obligation. To continue to operate with a gross inefficiency that is artificially increasing costs to customers cannot, under any stretch of a prudent management's imagination, be considered as an acceptable, "co-equal" compliance alternative to steps that would return Crystal River Units 1 and 2 to economical, baseloaded status.

(B) Should PEF recover costs for the Crystal River Units 1 and 2 cooling tower project through current base rates?

OPC: *Yes. The costs are of the type that are properly considered costs of operation and/or maintenance normally recovered through base rates. They do not satisfy the eligibility criteria of separate cost recovery mechanisms. To include them in a cost recovery clause notwithstanding their ineligibility would impose an unwarranted rate increase on customers. Accordingly, they should be recovered in base rate revenues. To require PEF to collect the costs through base rate revenues is appropriate, because this specific increase in O&M is but one of a myriad of changing costs, revenues, investments, and other dynamics that affect earnings during the period following the conclusion of a rate case. The impact of the costs on rate of return is negligible, and may be offset by declines in other costs and/or increases in revenues in any event.

As explained by Citizens' witness Patricia Merchant, base rates are designed to recover costs of operation and maintenance. The costs associated with the modular cooling towers are not eligible for either the environmental cost recovery clause or the fuel cost

recovery clause. Therefore, PEF should recover them from base rate revenues. *This is normal. This is as it should be.* As long as base rate revenues exceed the sum of all related costs and provide a positive return, those costs have been recovered—regardless of whether they were explicitly made part of the test year. The utility is compensated for the risk of fluctuations in costs, revenues, and earnings through its rate of return. (TR 59) Said differently, the costs of doing those things necessary to operate efficiently are already reflected in the price tag for service that is the bill for the utility's base rates. In the event a utility's rate of return falls below the range deemed by the Commission to be fair, the remedy is not to abuse a cost recovery clause, but to address the adequacy or inadequacy of base rates.[4]

ISSUE 2: How should the Commission's decision on Issue 1 be implemented?

OPC: The estimated 2006 costs included in the ECRC clause should be removed in the 2007 ECRC docket true-up process with interest added. The 2006 actual costs incurred and any 2007 and other future costs associated with this project should be recorded as regular O&M expenses, to be absorbed in base rate revenues.

CONCLUSION

For the reasons developed in this brief, the Commission should require PEF to recover the costs of the modular cooling towers through base rates.

[4] Witness Merchant showed that if PEF is directed to collect the costs of the modular cooling towers through base rates, the impact on PEF's earnings will be *de minimis*. (TR 62) PEF complains that the Commission has never applied an "earnings test" to a request for inclusion of an item in a cost recovery clause. PEF misses Citizens' point, which is that the items are not eligible for the clauses, but a denial of PEF's request will have a negligible effect on its earnings. Citizens believe the principle at stake is more significant than the dollars involved, as is the possible precedental effect of a decision to grant PEF's request; if the Commission does not draw the line, it can expect PEF and other utilities to continue to attempt to shift baserate~~base-rate-~related costs to a cost recovery mechanism.

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DOCKET NO. 060162-EI
CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of foregoing Citizens' Post Hearing Brief and Statement of Positions has been furnished by electronic mail and U.S. Mail on this 31st day of May, 2007, to the following:

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Finally, the parties recognize that the Commission, during its most recent fuel adjustment hearing, voted to determine in a single proceeding which items of fossil fuel-related costs should be transferred from fuel adjustment recovery to base rate recovery and to effect such changes at one time. While recognizing that this was the vote of the Commission, Public Counsel disagrees with such approach.

Commission's Findings

Having considered the stipulation of all the parties in this proceeding and recognizing the need for a further elaboration upon how fossil fuel-related costs should be treated for purposes of cost recovery, the Commission approves the stipulation of the parties and adopts the provisions therein, as its own. We find the policy outlined and specified in the stipulation to be an appropriate extension of the prior determinations regarding fuel costs to be recovered through fuel clauses made by the Commission in Order No. 6357.

In that earlier decision the Commission found that "the delivered cost of fuel to the generating plant site be used in determining a utility's fuel adjustment charge." That language has given rise to the recovery through the fuel adjustment clauses of unloading expenses, terminal operating expenses for terminals removed from plant sites, and transportation costs for moving oil from terminals to plant sites. While we recognize that the recovery of such costs through fuel clauses is consistent with the language in Order No. 6357, we feel further refinement is necessary since it is clear that these costs are not volatile.

Another expense which has come to be passed through the utilities' fuel clauses as a part of the cost of fuel is the cost of additives which are not added to fuel prior to burn or to boilers during burn. These additives are added after fuel is burned, generally to improve emissions control. We find that the cost of these "non-fuel additives" is more appropriately recovered through base rates.

As a result of our determinations in this proceeding, prospectively, the following charges are properly considered in the computation of the average inventory price of fuel used in the development of fuel expense in the utilities' fuel cost recovery clauses:

1. The invoice price of fuel.
2. Any revisions to the invoice price.
3. Any quality and/or quantity adjustments to the invoice price.
4. Transportation costs to the utility system, including detention or demurrage.
5. Federal and state taxes and purchasing agents' commissions.
6. Port charges.
7. All quantity and/or quality inspections performed by independent inspectors.
8. All additives blended with fuel prior to burning or injected into the boiler firing chamber along with fuel.

EXHIBIT A

9. Inventory adjustments due to volume and/or price adjustments.

10. Fossil fuel-related costs normally recovered through base rates but which were not recognized or anticipated in the cost levels used to determine current base rates and which, if expended, will result in fuel savings to customers. Recovery of such costs should be made on a case by case basis after Commission approval.

It is not the Commission's intent to require the restatement of the average cost of fossil fuel inventory computed prior to the revision of rates necessitated by this Order.

The following types of fossil fuel-related costs are more appropriately considered in the computation of base rates:

1. Operations and maintenance expenses at generating plants or system storage facilities. This includes unloading and fuel handling costs at the generating plant or storage facility.

2. Transportation charges between dedicated storage facilities and generating plants.

3. Fuel procurement administrative functions.

4. Fuel additives neither blended with fuel prior to burning nor injected into the boiler firing chamber along with fuel.

While it is the Commission's intent in this Order to establish comprehensive guidelines for the treatment of fossil fuel-related costs, it is recognized that certain unanticipated costs may have been overlooked. If any utility incurs or will incur a fossil fuel-related cost which is not addressed in this order and the utility seeks to recover such cost through its fuel adjustment clause, the utility should present testimony justifying such recovery in an appropriate fuel adjustment hearing.

Consistent with the determinations previously made herein, the Commission finds that the base rates and fuel and purchased power cost recovery factors for the following investor owned electric utilities in this state will require revisions. Tampa Electric Company is currently recovering unloading expenses through its fuel clause which should be recovered through base rates. Similarly, Florida Power & Light Company and Florida Power Corporation are recovering expenses of terminal operations and of transportation of fuel between terminals and plant sites through their fuel adjustment clauses which should be recovered through their base rates. Gulf Power Company is recovering the cost of a contract tugboat used to shift coal barges at a plant site through its fuel clause which expense is more appropriately recovered through its base rates. It is the Commission's intent that any revisions to fuel and purchased power cost recovery factors and base rates only reflect a change in the means of recovery of these items. So that the Commission can be assured of the accuracy and fairness of these necessary rate changes, they will be considered during the course of the August 1985 fuel adjustment hearings and become effective for billings on or after October 1, 1985.

Therefore, the stipulation of the parties to this proceeding is accepted, and it is,

ORDERED by the Florida Public Service Commission that the findings of fact and conclusions of law herein be and the same are hereby approved in every respect. It is further