

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

**In re: Nuclear Cost Recovery
Clause**

**DOCKET NO. 090009
Submitted for filing:
August 10, 2009**

REDACTED

REBUTTAL TESTIMONY OF GARY R. DOUGHTY

**ON BEHALF OF
PROGRESS ENERGY FLORIDA**

**IN RE: NUCLEAR COST RECOVERY CLAUSE
FPSC DOCKET NO. 090009**

REBUTTAL TESTIMONY OF GARY R. DOUGHTY

1 **Q. Please state your name, occupation, and address.**

2 A. My name is Gary R. Doughty. I am President of Janus Management
3 Associates, Inc. My business address is 412 White Columns Way,
4 Wilmington, North Carolina 28411.

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6 **Q. What is the purpose of your testimony in this proceeding?**

7 A. I provided direct testimony on March 1, 2009, regarding my assessment of
8 the prudence of Progress Energy Florida's (PEF's) project management
9 and project controls for the Levy Nuclear Project (LNP). I am submitting
10 this testimony to rebut assertions made by Dr. William R. Jacobs, Jr.
11 ("Jacobs"), witness for the Florida Office of Public Counsel, of "issues and
12 concerns" he raised regarding PEF's execution of an Engineering,
13 Procurement and Construction (EPC) contract with Westinghouse Electric
14 Corporation and Shaw, Stone & Webster on December 31, 2008.

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1 **Q. Please describe your prior testimony in these proceedings.**

2 A. My direct testimony presented my expert opinion with respect to the
3 reasonableness and prudence of PEF's management decision processes
4 and project management and controls as they relate to the LNP. I found
5 that PEF's LNP decision processes, project management and controls are
6 reasonable and prudent. I also found that the LNP has a sophisticated
7 risk management process in place that is consistent with industry best
8 practices.

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10 **Q. What standard should be followed in assessing prudence?**

11 A. There are several elements to an appropriate prudence standard:

12 * Any determination of the prudence of a management decision must be
13 based on what was known or reasonably should have been known by the
14 utility managers at the time the decision was made, and not based on the
15 outcome or result of the decision.

16 * Hindsight review is impermissible.

17 * One's own judgment should not be substituted for that of management.

18 The prudence standard recognizes that reasonable persons can have
19 honest differences of opinion and there may be more than one prudent
20 decision under the circumstances.

21 * There is a presumption of management prudence.

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1 * The decision must be evaluated on the basis of actual facts. The
2 review must be based on facts, not merely on opinions.

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4 **Q. What criticism does Jacobs make regarding the EPC contract?**

5 **A.** Jacobs argues that PEF should not have signed the EPC contract on
6 December 31, 2008 because: (1) PEF had not received a schedule from
7 the NRC for the review and approval of a requested Limited Work
8 Authorization (LWA); and (2) Joint Owners had not yet committed to the
9 project. As I will discuss, both of these contentions are without merit.

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11 **Q. Did Jacobs follow the appropriate prudence evaluation standard in
12 his criticism of the signing of the EPC contract?**

13 **A.** No. Jacobs has used hindsight to evaluate PEF management prudence
14 in signing the EPC contract in December 2008. Based on what was
15 known at the time, PEF acted prudently in signing the contract when it did.
16 As I will discuss below, there were compelling reasons for PEF to sign the
17 EPC contract by December 31, 2008, which included [REDACTED]

18 [REDACTED]

19 [REDACTED]

20 [REDACTED]

21 Jacobs ignores these benefits to signing the EPC contract -- he
22 does not even acknowledge them in his testimony -- and instead bases his

1 criticism on an event that took place in late January 2009. On January
2 23, 2009, well after the signing of the EPC contract, the NRC informed
3 PEF that it had decided to review the applications for the LWA and the
4 Combined Operating License (COL) for LNP on the same schedule. This
5 effectively eliminated the benefits of seeking the LWA and resulted in a
6 change in the overall LNP schedule. Jacobs asserts that PEF
7 management should have foreseen this action by the NRC and hence not
8 signed the EPC contract. A fair reading of the documents and what was
9 known by PEF management in 2008 do not support his allegations.

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11 **Q. On what does Jacobs rely for this criticism?**

12 A. Jacobs points to a letter from the NRC to PEF on October 6, 2008. He
13 alleges the letter should have been read by PEF as a clear sign that the
14 LWA would not be reviewed in a timely manner and implies the ultimate
15 decision by the NRC regarding the LWA was somehow foreshadowed by
16 this letter. These allegations are without merit.

17 Contrary to the testimony of Jacobs, a fair reading of the NRC's
18 October 6 letter would not have caused PEF management to assume that
19 a LWA would not be approved by the NRC. The NRC letter, in the first
20 paragraph, states their acceptance of the COL application for docketing.

"This letter informs you that the NRC staff has completed its
acceptance review and has determined that your application
is acceptable for docketing."

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Later in the letter, the NRC states:

“As discussed with your staff, the date that we intend to publish a schedule for review cannot be determined until additional information is provided by you. Although our acceptance review determined that the LNP COLA is complete and technically sufficient, the complex geotechnical characteristics of the Levy County site require additional information in order to develop a complete and integrated review schedule. Enclosure 1 contains this Request for Additional Information (RAI).

As necessary, other RAIs will be issued separately. Because of the scheduling uncertainty in the areas of geotechnical science and structural engineering, the NRC staff does not intend to commence a review of these areas until all associated RAIs are sufficiently answered.”

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This letter would not have been of particular concern to a utility manager because they were aware there were geotechnical issues to address as part of the site specific review process and were preparing to address those issues.

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Q. Should the receipt of Requests for Additional Information from the NRC have put PEF on notice there was a serious problem with the LWA application?

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A. No. RAIs are a normal part of the NRC licensing process – they are regularly used by the NRC to gather additional information. Receipt of RAIs would be appropriately viewed as a part of the process as it moved forward. In response to the NRC’s request for additional information, PEF immediately set about to respond to the RAIs. In fact, as indicated in

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1 Jacobs Exhibit WRJ (PEF)-3, PEF had begun responding to the NRC
2 RAIs by early October and completed its responses by November 20,
3 2008.

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5 **Q. Was it reasonable for PEF to expect NRC approval of an LWA review**
6 **schedule based on the response to the NRC geotechnical RAIs?**

7 A. Yes. After submitting its responses on November 20, 2008, PEF did not
8 receive any additional RAIs related to geotechnical issues. PEF offered to
9 meet with NRC technical representatives at the time of the geotechnical
10 RAI submittal, but the NRC declined to meet. PEF interpreted this as an
11 indication that there was nothing further needed at that time for the NRC
12 to process the LWA request. Based on industry experience, PEF
13 reasonably expected that providing responses to the NRC RAIs would
14 lead to a LWA review schedule. The NRC decision in late January 2009
15 to review the LWA on the same schedule as the COL was a complete
16 surprise not only to PEF, but also to the industry.

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18 **Q. Did the NRC make public statements after the October 6, 2008 letter**
19 **regarding their expectations for their review of the LWA?**

20 A. Yes. NRC leadership on December 4, 2008 made statements at an LNP
21 public meeting regarding their expectation for the time period for the NRC
22 to review the LWA request. The NRC Project Manager for Levy (Brian

1 Anderson) in response to a question from the public at the LNP EIS
2 Scoping meeting, stated:

3 "Just to give you a ballpark time frame, **we expect that
4 somewhere on the order of two years will be required to
5 complete our entire review process for the limited work
6 authorization.** And that's a ballpark time frame. The detailed
7 review schedule activities will be made publicly available once
8 we've completed the development of our schedule." [Transcript of
9 EIS public meeting held at Crystal River, FL on December 4, 2008,
10 www.nrc.gov, NRC ADAMS #ML083520102.]
11 [Emphasis added]

12 This response, which reinforced PEF's assumptions regarding the
13 NRC review of the LWA, clearly shows that Jacobs' strained
14 reading of the October 6 letter is without basis. This information
15 was not included in Jacobs' testimony.

16 **Q. You mentioned earlier that Mr. Jacobs did not mention in his
17 testimony the benefits to PEF of executing the EPC contract in
18 December 2008. What were those benefits?**

19 **A.** The Office of Public Counsel requested information related to
20 PEF's basis for signing the EPC contract in its data request No. 63,
21 wherein they asked:

22 "The EPC contract for the Levy Nuclear Project was signed
23 on December 31, 2008. Please explain if there were any
24 commercial reasons or other benefits for signing on
25 December 31, 2008 rather than signing in January 2009.
26 For example, were the prices or terms and conditions only
27 guaranteed through December 31, 2008? Would signing in
28 January 2009 have required significant changes or
29 renegotiation of the contract?"

30 PEF's response stated:

"Yes, there were commercial reasons or other benefits for PEF signing the EPC agreement on December 31, 2008 rather than January 2009. Those reasons and benefits are stated below.

[REDACTED]

1 In response to Staff request DR 7, regarding cost benefits / risks
2 associated with signing the EPC contract prior to the NRC issuance
3 of COL/LWA schedule, PEF expanded on the benefits above,
4 including the following:

5 [REDACTED]

[REDACTED]

1 Q. In your opinion, were the reasons stated by PEF in its
2 responses reasonable?

3 A. Yes. The advantages to enter into the EPC contract by December 31,
4 2008, were substantial both in terms of cost and maintaining the LNP
5 schedule. Jacobs' testimony does not mention these reasons despite his
6 having been advised of this information.

7 Further, as I identified in my direct testimony, PEF had thoroughly
8 reviewed the EPC contract terms and conditions including engaging Price
9 Waterhouse Coopers to perform an independent review of the contract.

10 PEF's EPC contract strategy was to [REDACTED]
11 [REDACTED]
12 [REDACTED] designed to provide incentive
13 to the contractor to perform efficiently. [REDACTED]
14 [REDACTED].

15 From a licensing perspective, signing the EPC contract was
16 evidence of an active engineering, design and procurement program.
17 PEF reasonably anticipated that this posture would be reflected in

1 recognition of their increased sensitivity to the timeliness of NRC license
2 review activity. With a signed EPC contract PEF established that LNP
3 was in the first review tier along with the only other two plants (Vogtle and
4 Summer) that had signed EPC contracts.

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6 **Q. Jacobs implies there was a connection between the NRC's decision**
7 **with respect to the LWA and the stop work order PEF issued to**
8 **CH2MHill in 2007 for quality controls deficiencies identified by PEF.**
9 **Is he accurate?**

10 A. No. Jacobs points to certain QA issues with CH2MHill, and implies that
11 may have been a problem with respect to the NRC's review of the LWA
12 application. This is wrong for several reasons. First, it should be noted
13 that the issues he points to arose out of work performed by CH2MHill at
14 the Harris Nuclear Plant and not at LNP. In a March 2007 QA audit of
15 CH2MHill geotechnical work on Harris, Progress Energy identified a
16 number of QA programmatic deficiencies and issued a stop work order to
17 CH2MHill on COLA deliverables. Based on Progress Energy's
18 assessment of completed corrective actions, this stop work order was
19 lifted on May 1, 2007. The NRC in October and November 2007
20 conducted a selective audit of the implementation of the Harris QA
21 program related to the development of the Harris COLA deliverables. The
22 results of the NRC audit were provided to Progress Energy in February
23 2008 and identified issues were addressed in a Progress Energy response

1 the following month. In April 2008 the NRC indicated the Progress Energy
2 reply was responsive to all NRC concerns and that they had no further
3 questions or comments.

4 CH2MHill performed similar work on LNP's geotechnical studies
5 which were underway at the time Progress Energy was addressing the
6 Harris QA issues. The March 2007 Progress Energy QA audit of
7 CH2MHill addressed their work at both Shearon Harris and LNP, and the
8 March 12, 2007 stop work order applied to CH2MHill's work for both
9 plants. As of March 23, 2007 based on assessments and direct field
10 observations, CH2MHill was released to continue field work at the LNP
11 site, and the stop work order was fully lifted on May 1, 2007. Subsequent
12 Progress Energy audits in October 2007 and April 2008 showed progress
13 in addressing the identified QA programmatic issues. In particular the
14 April 2008 audit comments indicated effective implementation of the
15 CH2MHill quality program. The same QA programmatic corrective actions
16 that were taken for Harris work were implemented contemporaneously for
17 LNP, and the NRC's April 2008 statements were taken as an indication
18 that no uncorrected QA problems with CH2MHill's work existed at LNP.

19 There is no legitimate basis for Jacobs to suggest that the NRC
20 may have been unwilling to commit to developing the LNP LWA review
21 schedule based on the deficiencies of a contractor. There is nothing in the
22 NRC's October 6, 2008 LNP COLA docketing letter or any other

1 communication from the NRC that indicates any such linkage. As further
 2 evidence of the absence of any link between the NRC's LWA decision and
 3 the CH2MHill QA program, the NRC's acceptance of the QA corrective
 4 actions had occurred well prior to PEF's July 2008 filing for the LNP
 5 COLA.

6 Finally, it is important to note that PEF identified the deficiencies
 7 that CH2MHill had in their quality assurance program through its oversight
 8 and audit process, and that they were corrected. These corrective actions
 9 were fully accepted based on the audits conducted between March 2007
 10 and April 2008 that verified the implementation of the revised quality
 11 program.

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 13 **Q. Jacobs asserts that PEF, by signing the EPC contract, has placed**
 14 **itself in a very weak position to renegotiate the EPC contract. Do**
 15 **you agree?**

16 **A.** No. In my opinion, Jacobs is speculating with no facts to support his
 17 speculation. Contrary to Jacobs' implication, PEF may actually be in a
 18 stronger negotiating position because it signed the EPC contract on
 19 December 31, 2008, and confirmed the benefits of [REDACTED]
 20 [REDACTED]
 21 [REDACTED] The
 22 revised costs to accommodate the schedule of the LNP may be

1 comparable or lower than what they would have been had the EPC
2 contract not been signed in 2008.

3 Had PEF not signed the EPC contract by December 31, 2008, they
4 would have faced [REDACTED]

5 [REDACTED]

6 [REDACTED]

7 [REDACTED]

8 [REDACTED]

9 [REDACTED]

10 [REDACTED] In my opinion,
11 having locked in these cost and schedule savings by signing the EPC
12 contract, PEF was in a stronger position to renegotiate the contract than if
13 these terms were not previously secured.

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15 **Q. Jacobs states that PEF should have had joint owners in place prior**
16 **to signing the EPC contract. Do you agree?**

17 **A.** No. Jacobs mischaracterized the meaning of the statements found in the
18 LINC meeting minutes that "JO work and EPC are closely tied." Rather
19 than his implication that LNP joint owners were necessary before signing
20 the EPC, the statement has to do with the desire of potential joint owners
21 to have the EPC in place before they signed a joint owner agreement.

22 The sequence anticipated from PEF's early 2008 discussions with
23 the prospective joint owners was that the finalized joint owner agreements

1 would follow the LNP need determination from the Florida Public service
2 Commission and the signing of the EPC contract. This sequence was
3 reflected in LINC Weekly Updates at least through January 2009, when
4 joint owner negotiations were continuing after PEF signed the EPC
5 contract.

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7 **Q. Jacobs criticizes the PEF management of risks for the LNP. Do you**
8 **agree?**

9 A. No. Based on Jacobs' testimony, he seems to require all risks to be
10 eliminated, which is extremely difficult and is likely to be an unreasonable
11 expense. The elimination of all risk may take excessive funding and effort
12 that is better spent on other areas of the project. Indeed, the Project
13 Management Body of Knowledge (PMBOK), a primary reference for the
14 LNP Risk Management Process Document, states that "It is seldom
15 possible to eliminate all risk from a project."

16 As I testified in my direct testimony, the LNP risk management
17 process follows the best practices and procedures of the PMBOK; it has
18 defined processes for risk identification, risk analysis (qualitative analysis
19 and, where appropriate, quantitative analysis), risk response planning, and
20 risk monitoring and control. These processes provide PEF management
21 with a logical and coherent framework to evaluate, prioritize, and develop
22 courses of action to mitigate, transfer, or avoid major project risks. In my
23 opinion, the LNP risk management process in place is consistent with best

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practices for risk management in the industry and consistent with what I have observed on well-managed projects, including nuclear construction projects, of a similar scope and size to the LNP.

Q. Does this complete your testimony?

A. Yes.