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Subject: FPSC Docket 090079 - PCS Phosphate Post-hearing Statement of Positions and Brief

Attachments: PCS Post Hearing Brief and Position Statement.pdf

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BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for Rate Increase by Progress Energy Florida	)	**Docket No. 090079-EI** **Filed: October 16, 2009**

POST-HEARING BRIEF AND STATEMENT OF ISSUES AND POSITIONS OF WHITE SPRINGS AGRICULTURAL CHEMICALS, INC. d/b/a PCS PHOSPHATE – WHITE SPRINGS

Pursuant to the Florida Public Service Commission's March 27, 2009 *Order Establishing Procedure*, Order No. PSC-09-0190-PCO-EI, White Springs Agricultural Chemicals, Inc. d/b/a PCS Phosphate – White Springs ("PCS Phosphate" or "PCS") files its Post-Hearing Brief and Statement of Issues and Positions.

I. STATEMENT OF BASIC POSITION

Most elements of Florida's economy have been adversely affected by the global recession. This is certainly true for manufacturing operations in the state, and particularly for anyone participating in globally competitive commodity markets, such as those operated by PCS Phosphate in the service territory of Progress Energy Florida ("Progress" or "PEF"). The cost of electric energy is a significant factor that affects every aspect of the economy, and, in this very challenging environment, supporting Florida's economic recovery must be a core consideration in all state actions concerning energy costs and services.

Other states have responded to the economic crisis in varying ways to support economic recovery or to prevent further deterioration in local economic conditions. In May 2009, for example, the New York Public Service Commission issued a Notice requiring all utilities to develop, file and implement austerity plans limiting or otherwise "holding the line" on spending and overall rate levels. The New York Commission succinctly noted:

> When utility customers are experiencing the extraordinary economic realities we see today, these customers look to their utility service providers to demonstrate the same frugality as the customers themselves experience daily so that the ultimate costs that customers must bear are minimized.[1]

Set, as it must be, in the context of today's economic environment, the $499 million rate increase requested by Progress using a "business as usual" template is not simply disappointing. It lies directly at odds with the fundamental imperative Florida faces to improve economic circumstances. Each of the core elements of PEF's rate filing, including an inflated requested return on equity, proposed changes to depreciation schedules to further increase depreciation rates despite an excessive depreciation reserve surplus, and increases for highly compensated executives, indicate a general PEF indifference to the current plight of Florida consumers and businesses. PEF is, in fact, quite open about its goal to continue to grow Progress Energy's earnings per share irrespective of economic conditions in its service territory.[2] It is incumbent upon the Commission to exercise the restraint that eludes PEF, and to re-connect PEF's requested rate increase and profit expectations with today's economic reality.

Revenue Requirement

The record in this proceeding actually establishes not only that the existing revenue requirement is sufficient, but that a slight reduction in PEF's revenue requirement is warranted. PCS Phosphate did not offer pre-filed testimony on PEF's revenue requirement, but strongly supports the adjustments and proposed findings filed by the Office of Public Counsel ("OPC") and the Florida Industrial Power Users Group's

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[1] Case 09-M-0435, *Notice Requiring the Filing of Utility Austerity Plans,* issued May 15, 2009 at 1.
[2] See e.g., TR. 2674-2677.

("FIPUG"). In particular, PEF should be required to amortize its excess depreciation reserve (compared to the theoretical reserve) over the time frame recommended by OPC and to incorporate the other adjustments to PEF's depreciation expense identified by OPC's witnesses.

Cost Allocation and Rate Design

PEF's proposed allocation of production plant costs using the "12CP and 50% AD" methodology must be rejected as inappropriate and inconsistent with cost causation principles as well as Florida's express policies to manage peak load growth. By placing heavy reliance on total energy use by customer classes whenever and wherever consumed, PEF's proposed allocation method disregards the importance of peak demand in driving PEF's need for infrastructure investment and undercuts Florida's peak load management policies.

Also, there is no record basis for reducing the level of demand charge credits that PEF provides for interruptible service, including the existing IST-1 rate, or for ratably reducing the otherwise applicable interruptible credit based on a customer's load factor. The record demonstrates to the contrary that the existing interruptible credit is stale and fails to reflect PEF's current assessment of the costs it avoids by interruptible service, or the other system reliability, economic and environmental benefits associated with interruptible service. The credit should be increased substantially, as is demonstrated in FIPUG witness Jeffrey Pollock's testimony. In all other respects PCS Phosphate supports the cost allocation and rate design recommendations of FIPUG.

II. STATEMENT OF ISSUES AND POSITIONS

TEST PERIOD AND FORECASTING

ISSUES 1-5: No longer disputed.

QUALITY OF SERVICE

ISSUE 6: Is the quality and reliability of electric service provided by PEF adequate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

DEPRECIATION STUDY

ISSUE 7: Should the current-approved depreciation rates, capital recovery schedules, and amortization schedules be revised?

POSITION: *Yes, pursuant to the stipulation set forth in Section X of the Prehearing Order.*

ISSUE 8: What are the appropriate capital recovery schedules?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 9: Is PEF's calculation of the average remaining life appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 10: What are the appropriate depreciation parameters (remaining life, net salvage percent, and reserve percent), amortizations, and resulting rates for each production unit, including but not limited to coal, steam, combined cycle, etc.?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 11: What life spans should be used for PEF's coal plants?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 12: What life spans should be used for PEF's combined cycle plants?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 13: What are the appropriate depreciation parameters (remaining life, net salvage percent, and reserve percent), amortizations, and resulting rates for each transmission, distribution, and general plant account?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 14: Based on the application of the depreciation parameters that the Commission has deemed appropriate to PEF's data, and a comparison of the calculated theoretical reserves to the book reserves, what are the resulting differences?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 15: What, if any, corrective reserve measures should be taken with respect to the differences identified in the Issue 14?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 16: What should be the implementation date for revised depreciation rates, capital recovery schedules, and amortization schedules?

POSITION: *Yes, pursuant to the stipulation set forth in Section X of the Prehearing Order.*

FOSSIL DISMANTLEMENT COST STUDY

ISSUE 17: Should the current-approved annual dismantlement provision be revised?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 18: What, if any, corrective reserve measures should be approved?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 19: What is the appropriate annual provision for dismantlement?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 20: Are PEF's assumptions in the fossil dismantlement study with regard to site restoration reasonable?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 21: In future dismantlement studies filed with the Commission, should PEF consider alternative demolition approaches?

POSITION: **ISSUE DROPPED**

NUCLEAR DECOMMISSIONING COST STUDY

ISSUE 22: Should the currently approved annual nuclear decommissioning accruals be revised?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 23: What is the appropriate annual decommissioning accrual in equal dollar amounts necessary to recover future decommissioning costs over the remaining life Crystal River Unit 3 (CR3)?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

RATE BASE

ISSUE 24: Has the company removed all non-utility activities from rate base?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 25: Should any adjustments be made to rate base related to the Bartow Repowering Project?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 26: Should an adjustment be made to reflect any test year or post test year revenue requirement impacts of "The American Recovery and Reinvestment Act" signed into law by the President on February 17, 2009?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 27: Is PEF's requested level of Plant in Service for the projected 2010 test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 28: What adjustments, if any, should be made to accumulated depreciation to reflect revised depreciation rates, capital recovery schedules, and amortization schedules resulting from PEF's depreciation study?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 29: Is PEF's requested level of Accumulated Depreciation and Amortization in the amount of $4,437,117,000 for the 2010 projected test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 30: Is PEF's requested level of CWIP – No AFUDC in the amount of $151,145,000 for the projected 2010 test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 31: Is PEF's requested level of Plant Held for Future Use in the amount of $25,723,000 for the projected 2010 test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 32: Is PEF's requested level of Nuclear Fuel – No AFUDC (net) in the amount of $126,566,000 for the projected 2010 test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*
ISSUE 33: Should an adjustment be made to PEF's requested storm damage reserve, annual accrual of $14.9 million, and target level of $150 million?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 34: Should any adjustments be made to PEF's fuel inventories?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 35: Should unamortized rate case expense be included in Working Capital?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 36: Has PEF appropriately reflected the impact of SFAS 143 (Asset Retirement Obligations) in its proposed working capital calculation?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 37: Is PEF's requested level of Working Capital Allowance in the amount of ($9,041,000) for the projected test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 38: Is PEF's requested level of Rate Base in the amount of $6,238,617,000 for the 2010 projected test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

COST OF CAPITAL

ISSUE 39: What is the appropriate amount of accumulated deferred taxes to include in the capital structure for the projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 40: What is the appropriate amount and cost rate of the unamortized investment tax credits to include in the capital structure for the projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 41: Should PEF's requested pro forma adjustment to equity to offset off-balance sheet purchased power obligations be approved?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 42: What is the appropriate equity ratio that should be used for PEF for purposes of setting rates in this proceeding?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 43: Have rate base and capital structure been reconciled appropriately?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 44: What is the appropriate capital structure for the projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 45: What is the appropriate cost rate for short-term debt for the projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 46: What is the appropriate cost rate for long-term debt for the projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 47: What is the appropriate return on equity (ROE) for the projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 48: What is the appropriate weighted average cost of capital including the proper components, amounts, and cost rates associated with the projected capital structure?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

NET OPERATING INCOME

ISSUE 49: Is PEF's projected level of total operating revenues in the amount of $1,517,918,000 for the 2010 projected test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 50: What are the appropriate adjustments to reflect the base rate increase for the Bartow Repowering Project authorized in Order No. PSC-09-0415-PAA-EI?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 51: Has PEF made the appropriate test year adjustments to remove conservation revenues and expenses recoverable through the Conservation Cost Recovery Clause?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 52: Has PEF made the appropriate test year adjustments to remove fuel and purchased power revenues and expenses recoverable through the Fuel and Purchased Power Cost Recovery Clause?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 53: Has PEF made the appropriate test year adjustments to remove capacity revenues and expenses recoverable through the Capacity Cost Recovery Clause?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 54: Has PEF made the appropriate test year adjustments to remove environmental revenues and expenses recoverable through the Environmental Cost Recovery Clause?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 55: Has PEF made the appropriate adjustments to remove charitable contributions?

POSITION: **ISSUE DROPPED**

ISSUE 56: Has PEF made the appropriate adjustments to remove Aviation cost for the test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 57: Should an adjustment be made to advertising expenses?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 58: Has PEF made the appropriate adjustments to remove lobbying expenses?

POSITION: **ISSUE DROPPED**

ISSUE 59: Is PEF's proposed allowance of $2,412,100 for directors and officers liability insurance appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 60: Is PEF's proposed allowance of $3,669,000 for 2010 injuries and damages expense appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 61: Is PEF's proposed allowance of $23,228,000 for 2010 A&G office supplies and expenses appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 62: Should an adjustment be made to PEF's proposed 2010 allowance for O&M expense to reflect productivity improvements, if any?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 63: Should an adjustment be made to PEF's requested level of salaries and employee benefits for the 2010 projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 64: Are PEF's proposed increases to average salaries for 2010 appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 65: Are PEF's proposed increases in employee positions for 2010 appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 66: Should the proposed 2010 allowance for incentive compensation be adjusted?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 67: Should the Company's proposed 2010 allowance for employee benefit expense be adjusted?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 68: Should an adjustment be made to the accrual for property damage for the 2010 projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 69: Should an adjustment be made to PEF's 2010 generation O&M expense?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 70: Should an adjustment be made to PEF's 2010 transmission O&M expense?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 71: Should an adjustment be made to PEF's 2010 distribution O&M expense?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 72: Should an adjustment be made to Operating and Maintenance (O&M) expenses to normalize the number of outages PEF has projected for the 2010 projected test year?

POSITION: **ISSUE DROPPED**

ISSUE 73: What is the appropriate amount and amortization period for PEF's rate case expense for the 2010 projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 74: Should an adjustment be made to bad debt expense for the 2010 projected test year?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 75: What adjustments, if any, should be made to the 2010 projected test year depreciation expense to reflect revised depreciation rates, capital recovery schedules, and amortization schedules resulting from PEF's depreciation study?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 76: What is the appropriate amount of depreciation and fossil dismantlement expense for the 2010 projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 77: What is the appropriate amount of nuclear decommissioning expense for the 2010 projected test year?

POSITION: *Yes, pursuant to the stipulation set forth in Section X of the Prehearing Order.*

ISSUE 78: What adjustments, if any, should be made to the amortization of End of Life Material and Supplies inventories?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 79: What adjustments, if any, should be made to the amortization of the costs associated with the last core of nuclear fuel?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 80: Should an adjustment be made to taxes other than income taxes for the 2010 projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 81: Is it appropriate to make a parent debt adjustment as per Rule 25-14.004, Florida Administrative Code?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 82: Should an adjustment be made to Income Tax expense for the 2010 projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 83: Is PEF's requested level of O&M expense in the amount of $713,371,000 for the 2010 projected test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 84: Is PEF's projected net operating income in the amount of $268,546,000 for the 2010 projected test year appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 85: Has PEF appropriately accounted for affiliated transactions? If not, what adjustment, if any, should be made?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

REVENUE REQUIREMENTS

ISSUE 86: What is the appropriate projected test year revenue expansion factor and the appropriate net operating income multiplier, including the appropriate elements and rates for PEF?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 87: Is PEF's requested annual operating revenue increase of $499,997,000 for the 2010 projected test year appropriate?

POSITION: *No. PCS Phosphate agrees with and adopts the position of the OPC that required retail revenues for the 2010 projected test year should be a reduction of $35,038,000 and that rates should be reduced accordingly.*

COST OF SERVICE AND RATE DESIGN

ISSUE 88: Has PEF correctly calculated revenues at current rates for the projected test year?

POSITION: *PCS Phosphate agrees with and adopts the position of the FIPUG.*

ISSUE 89: Is PEF's proposed separation of costs and revenues between the wholesale and retail jurisdictions appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the FIPUG.*

ISSUE 90: What is the appropriate Cost of Service Methodology to be used to allocate base rate and cost recovery costs to the rate classes?

POSITION: *PCS Phosphate agrees with and adopts the position of FIPUG. The Commission should require PEF to continue to use the 12CP and 1/13th AD ("average demand" or "energy") cost allocation method. *

DISCUSSION

The Commission should require PEF to continue to use the 12CP and 1/13th AD cost allocation method. This method is more consistent with cost causation for production plant investment on the PEF system than the energy-oriented method that PEF now proposes. PEF's proposed allocation method for production plant (12CP and 50% AD) improperly disregards alignment of cost allocation with cost causation as a fundamental objective, and inappropriately assigns cost responsibility among customer classes as a result.

The purpose of any cost of service study is to apportion responsibility for a utility's plant costs among customer classes in relation to how the usage characteristics of each class causes a utility to incur those costs. A customer class should be allocated its share of costs that it causes Progress to incur and should not be allocated costs that are not caused by serving that load. A simple example is that the costs of the distribution network are not allocated to customers taking service at transmission voltages because they do not use distribution equipment and PEF does not incur distribution costs in serving those loads. There is no argument between PEF witness Slusser and FIPUG witness Pollock that cost causation should form the basic premise for cost allocation. (TR. 3163; 1523).

Progress Energy has a system load shape characterized by pronounced morning and evening winter peaks and afternoon summer peaks. (TR. 3160; 3496; 3499). This pattern is driven principally by the usage behavior of PEF's residential load. (TR. 1604-05). The system demands required to serve this system load shape drives PEF's need for capacity. (TR. 1605). It also has a profound effect on the mix of generation resources that PEF must maintain in its fleet. Operationally, this peak demand pattern necessitates regular starts of PEF's peaking combustion turbines (thousands of starts for brief periods annually) (see TR. 490; 3490, 3496; 3499), including its older, more inefficient units that require very close operational scrutiny (because PEF fears an impending "catastrophic failure" each time they start up). (TR. 3495; 3499). PEF wants to retire several of these older units as soon as is feasible (see Exh. 216), but must continue to rely on those units to meet peaking requirements.

For system planning purposes, PEF must own or secure sufficient capacity or purchased power to meet its forecasted annual system firm peak demand plus a reserve margin of 20%. (TR. 989). Non-firm loads are subtracted from PEF's planning requirements. (TR. 988-89.) Consequently, PEF does not build or purchase capacity to serve its interruptible or curtailable loads. (TR. 1592). Progress plans resource additions to satisfy its peak capacity and reserve obligations according to various economic and reliability criteria that are discussed annually in its updated Ten Year Site Plan filings. (TR. 3430; 3492). PEF's selection of resources (i.e., base load, intermediate, or peaking and demand side resources) reflects the capabilities of existing resources, system load characteristics, state energy prerogatives and a least cost energy stratagem (i.e., one designed to produce lowest overall revenue requirements for consumers in the long run). The current Progress Energy Ten Year Site Plan shows a combustion turbine peaking unit as its next generation resource, a desire to retire the older peaking units as soon as is feasible, and a "bet the company" generation construction program tied to construction of the delayed Levy Nuclear Project. In sum, over the next 5-8 years, both PEF's resource planning and operational priorities are centered on improving its peaking resources while attempting to make progress with its nuclear construction program.

For some time, PEF has applied a 12CP and 1/13th AD method for allocating the cost of production plant. This method, as FIPUG witness Pollock discussed, properly aligns production plant cost allocation with peak-oriented consumption. The method is consistent with fundamental rate-making principles (TR. 3221) (i.e., cost allocation follows cost causation and peak demands determine the need for production capacity) while recognizing that all generation affects system average energy costs. This method supports the express Florida state energy policy stressing the particular importance of controlling the growth of weather sensitive peak

Loads. (See section 366.81 F.S.). It also is consistent with PEF's immediate system planning needs (i.e., managing its peak loads and the use of its aging peaking resources).

In this case, PEF proposes to employ a radically different method for allocating the cost of production plant using a 12CP and 50% energy method. PEF maintains that allocating half of the costs of production plant on the basis of energy provides a "better matching of the allocation of costs and benefits to customer rate classes." (TR. 1485). In short, rather than allocating costs to match cost causation, PEF proposes to allocate costs based on the benefits to all loads of system average fuel costs that are lower than the fuel costs of peaking generation.

Abandoning cost causation as the underlying principle for cost allocation in favor of an ill-defined fuel costs benefits criterion that is utterly indifferent to when, where or how energy is consumed has multiple flaws, but the fundamental error lies in the fact that when energy is consumed on the PEF system is the ultimate driver for utility investment in that system. As FIPUG witness Pollock correctly explained, PEF's proposed method severely under-values capacity and the significance of peak demands. (TR. 3160; 3167).

Progress asserts that generation investment strategies are somehow different today from traditional utility resource planning because there is a greater emphasis on providing clean and efficient generation as well as meeting reliability criteria. (TR. 1498-99). There is no basis for that assertion. Insofar as PCS can tell, PEF and its predecessor, Florida Power Corp., have historically considered a mix of resource options that include base load, intermediate and peaking facilities. The utility has considered, and built, nuclear, coal-fired, and oil and natural gas burning generation plant (Crystal River 3 alone entered commercial service in 1977). In every case, presumably, capital costs, fuel costs, maintenance requirements, system reliability, environmental and siting considerations, location on the grid and other factors were taken into account. One hopes that overall revenue requirements for utility consumers were considered as well (that being a bedrock objective of utility least cost planning). PEF does not point to any meaningful change in its planning process, or the investments it plans to make, that would support a basic change in cost allocation methods. In fact, the contrary appears to be true (i.e., managing its peaking resources and needs continues to grow in importance).

The one notable change of significance in resource planning in recent years has involved legislative direction concerning energy policy. As noted above, Florida policy clearly has targeted management of the growth of weather sensitive peak loads as a special concern. (Sec. 366.81 F.S.). Florida's interest in reducing reliance on oil and natural gas (the primary fuels for peaking units) is also served by mitigating peak load growth. (See also sec. 366.92(1) F.S.).

Peaking generation contributes disproportionately to the system average cost of fuel relative to the energy it supplies. (TR. 4099; Exh. 204). Thus, for the immediately foreseeable future, a key way for PEF to manage its fuel costs (apart from effective hedging strategies) is to focus on managing its peak loads. Continuing to allocate production plans primarily based on customer class contributions to the system peaks using the 12CP and 1/13th method, supports this objective. Relying heavily on total usage, regardless of system impacts, serves to undercut that basic objective. Further, almost all discussion of grid modernization and a clean energy strategy (smart grid, demand response, integration of plug-in vehicles, etc.) begins by better reconciling how electric rates are developed and designed with how energy use affects system reliability and the need for new power plants.

Notwithstanding all of the above, PEF proposes to adopt a 12CP and 50% AD cost allocation methodology for production plant. Notably, PEF does not consistently apply this methodology to variable (primarily fuel) costs. The 12CP and 50% AD method allocates production cost plant based half on the monthly peaks year round and half based on average demand (i.e., energy use). This method is indifferent to the impact of the sharp PEF system seasonal peaks (winter and summer) that actually drive PEF's system requirements. PEF's heavy reliance on total class energy use also ignores the basic physical realities of an electrical system. (Because electric energy currently cannot be stored in meaningful quantities, production capacity must be available at all times to serve the continually varying demand on the system even if much of that capacity is utilized for very brief periods).

The utility's testimony in support of allocating production capacity costs significantly on an energy basis suffers from murky logic. Essentially, it presumes that more capital intensive base load units lower system average fuel costs to the benefit of all consumers, but the linkage between this self-evident benefit and cost causation is missing. PEF argued that it is spending twice as much on base load units than it would for peaking only combustion turbines. See Exh. 113. This claim, however seriously understates the capital cost of peaking units according to other PEF exhibits. See Exh. 113 (which shows cost current cost of peaking capacity to be $329 per kW while PEF assumed $209 per kW; see also TR. 3171).

Similarly, in rebuttal, PEF witness Slusser offered an exhibit intended to show that building a peaker-only generation fleet would produce substantially higher system fuel costs than PEF's actual fuel costs.[3] (Exh. 250). Mr. Slusser, however, agreed that the planning scenario underlying this hypothetical was implausible and rested on the impractical premise that lowest capital costs was the only relevant generation planning criterion. (TR. 1498). Least cost resource planning, however, is never limited to lowest capital costs, but reflects a desire to achieve lowest overall revenue requirements and a host of reliability, operational and other factors.

Finally, PEF's proposed 12CP and 50% method is simply a renamed version of the Equivalent Peaker method that the Commission previously has considered and rejected. (TR. 1530).

<u>ISSUE 91</u>: If the Commission approves a cost allocation methodology other than the 12 CP and 1/13th Average Demand, should all cost recovery factors be adjusted to reflect the new cost of service methodology?

<u>POSITION</u>: *Yes, provided that the interruptible credit is adjusted to reflect its full value (PCS Phosphate agrees with FIPUG).*

<u>ISSUE 92</u>: How should any change in revenue requirements approved by the Commission be allocated among the customer classes?

<u>POSITION</u>: *PCS Phosphate agrees with and adopts the position of FIPUG. No rate schedule should receive an increase greater than 150% of the system average increase.*

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[3] PEF also asserted that its energy –weighted method would affect all customer classes equally, but it became apparent that the exhibit simply assigned the same percentage amounts to all classes. Thus, PEF established only that the exhibit was algebraically correct. It did not demonstrate, and did not actually attempt to demonstrate, that customer classes possessing different load shapes and load factors would see comparable impacts from a 50% energy weighting of production plant. (See TR. 4094-4095).

DISCUSSION

The essential purpose of the Commission's long standing policy limiting rate increases to 150% of the system average increase is to prevent rate shock to any group of existing customers. This policy is particularly important where the utility is proposing a very large base rate increase and all consumers are bearing the brunt of difficult economic circumstances. The rate increases PEF proposes patently contravene this practice, and appropriate adjustments are necessary.

Based on PEF's rate filing, the proposed rate increases for rates GSD-1, IS-1/IS-2, and SS-3 all would exceed 150% of the system average increase. (Exh. 317). PEF does not dispute this, but seeks to evade the policy by asserting that its proposed revenue allocation would not produce an excessive increase for any class of customer. Since the purpose of the policy is to mitigate excessive rate impacts, the analysis must necessarily start from existing rate schedules. (TR. 3185).

ISSUE 93: Is PEF's proposed treatment of unbilled revenue due to any recommended rate change appropriate?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 94: Is PEF's proposed charge for Investigation of Unauthorized Use appropriate?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 95: Should the Commission approve PEF's proposal to eliminate its IS-1, IST-1, CS-1, and CST-1 rate schedules and transfer the current customers to otherwise applicable rate schedules?

POSITION: *No. The Commission should direct PEF to retain the IS-1, IST-1, CS-1 and CST-1 rate schedules. Further, no existing customers should be transferred to any optional rate schedule. Customers should be allowed to elect among available rate options.*

DISCUSSION

As noted above, PEF does not plan to build or purchase capacity to serve its roughly 300 MWs of non-firm load. (TR. 988-89). That is but the beginning of the story in terms of the economic, reliability and environmental benefits provided to PEF and other PEF rate payers by interruptible loads. PEF certainly avoids the capital costs, land, property taxes, etc. of building a peaker. (TR. 1559-60). It also avoids the additional capacity requirement associated with the reserve margin required for a comparable amount of firm load. PEF of course avoids the fuel costs of running a peaking unit (which as discussed above are substantially higher than average fuel costs). (See Exh. 204). It also avoids the emissions produced by a peaking unit, O&M, spare parts inventory, labor and various other costs.

In addition, the purpose of PEF's interruptible service is to aid PEF in preserving system reliability to prevent service disruptions to firm loads. PEF can disrupt service to interruptible loads at no notice to the customer (PEF notifies curtailable loads of the need to reduce load but must wait for those loads to comply). PEF's ability to drop significant amounts of load on very short, or no, notice makes interruptible customers especially valuable for system reliability purposes because this load can serve as the functional equivalent of spinning generation reserves. In fact, since many of PEF's older combustion turbines require considerably more than 10 minutes to start up and connect to the grid, those units cannot serve that function. (TR. 3497).[4] In the event of a major system disturbance (i.e., tripping of a major generation source, power line or other contingency event), PEF's ability to shed load or add generation quickly is essential to

[4] PEF witness Crisp also acknowledged that the Texas system averted a system crash in early 2006 largely due to the performance of fast responding interruptible loads that helped maintain system stability under circumstances in which available peaking generation could not respond fast enough. (TR. 3502-3503.)

preserving system reliability. In short, PEF's interruptible load is a very valuable resource that provides a variety of economic, operational and reliability benefits. Further, a number of PEF's IST-1 customers are large loads. These customers allow PEF to shed significant amounts of load very easily.

In this case, PEF proposes to eliminate the grandfathered IS-1, IST-1, CS-1 and CST-1 rate schedules and transfer the loads currently served on those schedules to the companion IS-2, IST-2, CS-2 and CST-2 rate schedules on the basis that the grandfathered rates were considered not to be cost-effective some time ago. (TR. 1509-1510). There is no record evidence in this case, however, that the existing grandfathered demand credits are not cost-effective today. In fact, the only record evidence on this point is a study performed by PEF which demonstrates a) that PEF needs additional non-firm load, and b) that the existing demand charge credits provided by these schedules are far below what is economically justified. See Exh. 279.

The current IST-1 credit is $3.62 per kW-mo. According to PEF's updated cost-effectiveness analysis, based on PEF's current most recent calculation of costs and benefits using the Rate Impact Measurement ("RIM") test, that credit should be no less than $10.49 per kW-mo. (Exhs. 198 and 279; TR. 3192). Moreover, that analysis does not take into account the spinning reserve reliability benefits provided by existing interruptible loads. In sum, the Commission should require PEF to retain the existing 1-series interruptible and curtailable rate schedules and increase the demand credits under those schedules to the levels that have been shown to be cost-effective.

Finally, in the event that the Commission allows PEF to eliminate those rate schedules, PEF should not be permitted to simply transfer existing 1-series customers to the 2-series rate schedules. There are significant differences between, for example, the IST-1 and IST-2 rate schedules due in large part to the lower demand credit offered and the load factor adjustment applied to further diminish the customer credit. (TR. 1533-1534). It is important to recognize that interruptible customers receive a reduced rate (demand charge credit) because they receive a lesser quality of service than firm customers. (TR. 1538-1539). These customers are not compensated for the costs they incur as a result of such service disruptions (which may include lost production, increased maintenance and labor costs, and other inefficiencies). It is entirely possible that some (or all) 71 existing IST-1 customers[5] may determine that the diminished benefits associated with the IST-2 rate may no longer justify incurring the costs of participating in the interruptible program. PEF witness Slusser conceded that the substantial economic differences between the IST-1 and IST-2 rates may make a difference to those loads. (TR. 1553).

Under PEF's General Rules and Regulations governing electric service, a customer may elect to be billed under an optional rate schedule. (Section 1.03 Rate Applications; Second Revised Tariff Sheet 4.011). Thus, if an existing rate schedule is eliminated, it is the customer's choice as to which rate should apply if it is eligible for an optional rate schedule. This election is particularly important in this instance because the IST-2 rate schedule requires 36 months notice to terminate; a point that PEF witness Slusser acknowledged during the hearings. (TR. 1553-1556). No customer should be required to take service under an optional rate, and held on that rate for a minimum of three years, that the customer does not consider to be in its best interest. While, as discussed above, the 1-series rates should be continued, if they are eliminated PEF should

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[5] (See TR. 1551).

not be permitted to simply transfer customers to the comparable 2-series rate schedule. Customers should be permitted to elect among available rate schedules following an appropriate transition period.

ISSUE 96: Is PEF's proposal to grandfather certain terms and conditions for existing IS-1, IST-1, CS-1, and CST-1 customers under the combined IS and CS rate schedules appropriate?

POSITION: *Subject to PCS Phosphate's objections to the elimination of those rate schedules and the unauthorized transfer of existing customers to optional rate schedules discussed in response to Issue 95, PCS agrees with and adopts the position of the FIPUG.*

ISSUE 97: Should PEF's proposal to close the RST-1 rate to new customers be approved?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 98: Are PEF's proposed customer charges appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 99: Are PEF's proposed service charges appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 100: Is PEF's proposed charge for Temporary Service appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 101: Is PEF's proposed Premium Distribution Service charge appropriate?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 102: Are PEF's proposed tariffed LS-1 lighting rate schedule charges for standard equipment appropriate?

POSITION: **ISSUE DROPPED**

ISSUE 103: Are PEF's proposed monthly fixed charge carrying rates to be applied to the installed cost of customer-requested distribution equipment, lighting service fixtures, and lighting service poles, for which there are no tariffed charges, appropriate?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 104: Are PEF's proposed delivery voltage credits appropriate?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 105: Are PEF's power factor charges and credits appropriate?

POSITION: *PCS Phosphate accepts the stipulation reached on this issue.*

ISSUE 106: Is PEF's proposed lump sum payment for time-of-use metering costs appropriate?

POSITION: *No position.*

ISSUE 107: What is the appropriate method of designing time of use rates for PEF?

POSITION: *PCS Phosphate agrees with and adopts the position of the AFFIRM.*

ISSUE 108: What are the appropriate charges under the Firm, Interruptible, and Curtailable Standby Service rate schedules?

POSITION: *PCS Phosphate agrees with and adopts the position of the FIPUG.*

ISSUE 109: What is the appropriate level of the interruptible credit?

POSITION: *PCS Phosphate agrees with and adopts the position of the FIPUG. The interruptible credit should be $10.49/kW-mo. and should not be load factor adjusted. This credit level is justified based on PEF's most current cost-effectiveness study.*

ISSUE 110: Should the interruptible credit be load factor adjusted?

POSITION: *No. PCS Phosphate agrees with and adopts the position of the FIPUG.*

DISCUSSION OF ISSUES 109 AND 110

As is discussed above, interruptible service is a highly valuable demand side substitute for spinning generation. Issues 109 and 110 concern PEF's proposal to substantially reduce the credit for interruptible service. As discussed above, there is no record evidence that the demand credit currently provided to IS-1 and IST-1 customers is not cost effective. To the contrary, PEF's own analysis using the Rate Impact Measure test indicates that, based on PEF's current appraisal of costs and benefits, the credit should be increased to at least $10.49 per kW-month. (Exh. 279; TR. 3192).

PEF proposes to eliminate the IS-1 and IST-1 rates schedules and to transfer customers on those schedules to IS-2 and IST-2. The IS-1 credit currently is $3.62 per kW-month. The current IS-2 credit is $3.31 per kW-month applied to load factor adjusted demand. PEF concedes that no existing IST-1 customers would receive the full $3.31 per kW credit because none operate at a 100% load factor (nor would they be expected to operate in such a manner). (TR. 1556-59).

PEF does not attempt to justify elimination of the 1-series rate schedules other than to note that at one point they were not considered to be cost-effective. (TR. 1509-1510). PEF also does not attempt to update or economically justify the level of the IST-2 credit. Instead, PEF simply explained proposed changes to, or retention of, certain non-price tariff provisions. (TR. 1513-1514).

FIPUG's testimony by Jeffrey Pollock explained that applying a load factor adjustment to the IS-2 credit will reduce the credit to approximately $2.02 per kW-month on average when, in fact, the level of credit should be increased. (TR. 3192). Mr. Pollock further explained that a load factor adjustment, which PEF claims to have used as a proxy for coincidence with peak demand, is inappropriate in any event. First, PEF can interrupt IS customer loads at any time that system conditions require. (TR. 3190). Interruptions are not confined to peak periods. Second, as Mr. Pollock explained, load factor is not a reasonable measure of coincidence with monthly system peaks. (TR. 3193).[6] Mr. Pollock

[6] The interruptible class has an average coincidence factor of 68% but an average load factor of 61%. (TR. 3193).

suggested that a customer's average annual load on-peak might be a better measure of the level of interruptible load that PEF can rely upon. (TR. 3193-94).

More fundamentally, as described above, interruptible load serves as a resource substitute for fast responding peaking generation. PEF's rate recovery of the costs of its generation is not ratably apportioned based on the availability of those resources (which experience both planned and unplanned outages in the normal course of events). PEF's load factor adjustment thus is highly discriminatory toward demand side resources.

Ultimately, PEF carries the burden of proving its proposed rates. In this case, PEF has not justified its proposal with respect to interruptible service. PEF has:

- Not attempted to establish that the existing IS-1 and IST-1 credits are not cost-effective today.
- Not disputed that its own calculations demonstrate that an interruptible credit of $10.49/ kW-month is appropriate and cost-effective.
- Acknowledged that its load factor adjustment will reduce the interruptible credit for all existing IST-1 loads.
- Not disputed the record evidence that the expected credit under IST-2 is significantly less than a credit level that has been shown to be cost effective.
- Acknowledged that the substantially lowered credit may substantially affect the continued interest of existing IST-1 customers in remaining interruptible loads.

In sum, based on this record, all existing interruptible rate schedules, including IS-1 and IST-1, should be continued. The interruptible credit should be increased to reflect a current estimate of the level of credit that is cost-effective, and that credit should not be load factor adjusted.

ISSUE 111: What are the appropriate energy charges?

POSITION: *PCS Phosphate agrees with and adopts the position of the FIPUG.*

ISSUE 112: What are the appropriate demand charges?

POSITION: *PCS Phosphate agrees with and adopts the position of the FIPUG.*

ISSUE 113: What are the appropriate lighting charges?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 114: Should PEF's proposal to revise its Leave Service Active (LSA) provision (tariff sheet No. 6.110) be approved?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 115: What is the appropriate effective date for PEF's revised rates and charges?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

Issue 115A: Are the rates proposed by Progress Energy Florida fair, just, and reasonable, and compensatory as those terms are used in Chapter 366, Florida Statutes, including specifically Section 366.03, 366.041(1), 366.05(1), and 366.06(1), Florida Statutes?

POSITION: *No. Based on the other issues discussed above, the Commission should reduce PEF's rates.*

Issue 115B: In fulfilling its mandate under Section 366.01, Florida Statutes, to regulate public utilities in the public interest and for the protection of the public welfare, and its mandate under Section 366.041(1) to fix fair, just, reasonable, and compensatory rates that consider among other things the value of such service to the public and that do not deny the utility a reasonable return upon its rate base, should the Commission grant any part of PEF's proposal to increase its base rate in this docket?

POSITION: *No. Based on the other issues discussed above, the Commission should reduce PEF's rates.*

OTHER ISSUES

ISSUE 116: Should any of the $13,078,000 interim rate increase granted by Order No. PSC-09-0413-PCO-EI be refunded to the ratepayers?

POSITION: *Yes. PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 117: Should PEF be required to file, within 90 days after the date of the final order in this docket, a description of all entries or adjustments to its annual report, earnings surveillance reports, and books and records which will be required as a result of the Commissions findings in this proceeding?

POSITION: *Yes, pursuant to the stipulation set forth in Section X of the Prehearing Order.*

ISSUE 118: What are the appropriate guidelines for the pension fund regulatory asset?

POSITION: **ISSUE DROPPED**

ISSUE 119: Does the creation of a regulatory asset and the deferral of pension expenses from a period covered by the Stipulation approved by Order No. PSC-05-0945-S-EI to a future period violate the terms of the Stipulation and order?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 120: Does the creation of a regulatory asset and the deferral of pension expenses from a period covered by the Stipulation and order to a future period constitute retroactive ratemaking?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 121: Does the creation of a regulatory asset and the deferral of pension expenses from a period covered by the revenue sharing provisions of the Stipulation and order to a future period result in double recovery of those expenses?

POSITION: *PCS Phosphate agrees with and adopts the position of the OPC.*

ISSUE 122: Should this docket be closed?

POSITION: *Yes, once a final order has been issued in this matter.*

Respectfully submitted the 16th day of October, 2009.

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CERTIFICATE OF SERVICE

I hereby certify that a true copy of the foregoing has been furnished by electronic mail and/or U.S. Mail this 16th day of October 2009 to the following:

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