

BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

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In re: Fuel and purchased power cost recovery clause with generating performance incentive factor.

DOCKET NO. 110001-EI

DATED: October 5, 2011

COMMISSION CLERK

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Direct Testimony of Kathy L. Welch has been served by U.S. Mail this 5th day of October, 2011, to the following:

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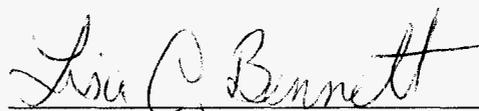
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Docket No. 110001-EI: Fuel and Purchased Power Cost Recovery Clause. Florida Power & Light Company's Hedging Activities

Witness: **Direct Testimony of KATHY L. WELCH**, Appearing on Behalf of the staff of the Florida Public Service Commission

Date Filed: October 5, 2011

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DIRECT TESTIMONY OF KATHY L. WELCH

1
2 **Q. Please state your name and business address.**

3 **A.** My name is Kathy L. Welch, and my business address is 3625 N.W. 82nd Ave.,
4 Suite 400, Miami, Florida, 33166.

5 **Q. By whom are you presently employed and in what capacity?**

6 **A.** I am employed by the Florida Public Service Commission as a Public Utilities
7 Supervisor in the Office of Auditing and Performance Analysis.

8 **Q. How long have you been employed by the Commission?**

9 **A.** I have been employed by the Florida Public Service Commission since June, 1979.

10 **Q. Briefly review your educational and professional background.**

11 **A.** I have a Bachelor of Business Administration degree with a major in accounting
12 from Florida Atlantic University and a Masters of Adult Education and Human Resource
13 Development from Florida International University. I have a Certified Public Manager
14 certificate from Florida State University. I am also a Certified Public Accountant licensed
15 in the State of Florida, and I am a member of the American and Florida Institutes of
16 Certified Public Accountants. I was hired as a Public Utilities Analyst I by the Florida
17 Public Service Commission in June of 1979. I was promoted to Public Utilities
18 Supervisor on June 1, 2001.

19 **Q. Please describe your current responsibilities.**

20 **A.** Currently, I am a Public Utilities Supervisor with the responsibilities of
21 administering the District Office and reviewing work load and allocating resources to
22 complete field work and issue audit reports when due. I also supervise, plan, and conduct
23 utility audits of manual and automated accounting systems for historical and forecasted
24 data.

25 **Q. Have you presented testimony before this Commission or any other**

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1 **regulatory agency?**

2 A. Yes. I have testified in several cases before the Florida Public Service
3 Commission. Exhibit KLW-1 lists these cases.

4 **Q. What is the purpose of your testimony today?**

5 A. The purpose of my testimony is to sponsor the staff audit report of Florida Power
6 & Light Company (FPL or Utility) which addresses the Utility's filing in Docket No.
7 110001-EI Fuel and purchased power cost recovery clause for costs associated with its
8 hedging activities. We issued an audit report in this docket for the hedging activities on
9 September 15, 2011. This audit report is filed with my testimony and is identified as
10 Exhibit KLW-2.

11 **Q. Was this audit prepared by you or under your direction?**

12 A. Yes, it was prepared under my direction.

13 **Q. Please describe the work you performed in these audits.**

14 A. Accounting Treatment

15 We obtained a summary schedule of all financial futures, options and swaps that
16 were executed by the utility for the 12-month period ended July 31, 2011. We reconciled
17 the monthly gain or loss to the company's filing. We traced these gains and losses to the
18 calculation of the average unit cost of gas and oil and to FPL's books and records. FPL's
19 accounting treatment of hedging gains and losses was verified to be in compliance with
20 Commission Order PSC-02-1484-FOF-EI, issued October 30, 2002 in Docket No.
21 011605-EI and as clarified by FPSC Order No. PSC 08-0316-PAA-EI, issued May 14,
22 2008 and FPSC Order No. PSC-08-0667-PAA-EI, issued October 8, 2008 in Docket
23 No.080001-EI.

24 We obtained the monthly level of hedging gains/losses and verified that they are
25 consistent with the requirements of Commission Order in Docket No. 011605-EI and

1 FPL's Hedging Plans. We also reviewed the company's external auditor's reports and
2 workpapers on derivative activity for the 12-month period ended July 31, 2011.

3 Contracts

4 We sampled two contracts, one for natural gas and one for heavy oil, and reviewed
5 the contracts to ensure that they were in compliance with the Company's hedging plans.

6 Gains and Losses

7 We traced the monthly hedging gains and losses to the supporting documents that
8 were used to prepare FPL's filing. FPL provided the "Derivative Settlements-All
9 Instruments" report that shows the calculation of all gains and losses by deal options and
10 swaps made by each counter party. This report was traced to the filing. A sample of the
11 October 2010 natural gas and September 2010 heavy oil transactions were selected for
12 testing. The deals sampled were traced to confirmation letters, bank invoices, deal forms,
13 and purchase statements. In addition, the settle price was traced to Platt's and NYMEX
14 market data. In order to trace the September and October 2010 gains and losses to the
15 general ledger, account 151 Fuel Inventory, we first reconciled the gain and losses to the
16 "Monthly Gas Closing Report" and "Allocation of Oil Financing Instrument" report,
17 which, in turn, were reconciled to the general ledger.

18 Quantity of Gas and Residual Oil

19 We obtained the 2010 Risk Management Plan and the Planned Position Strategy
20 (PPS) procedures, which show the hedged targets by months. The natural gas and the
21 heavy oil actual percentage hedged were compared to the target hedged and verified to the
22 specified tolerance bands. If the actual percent hedged of a particular month was not
23 within the tolerance band, then a rebalance would be required. The rebalancing was
24 implemented by either purchasing or selling the swaps to meet the established targets.
25 We verified and recalculated the percent of hedge amounts and the rebalancing by month.

1 No exceptions were noted.

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3 Value At Risk (VaR)

4 We verified that the Value At Risk (VaR) Activities were within the transaction
5 limits and authorization as stated in the Risk Management Plans.

6 Segregation of Duties

7 We reviewed the procedures for separating duties and had no exceptions.

8 **Q. Please review the audit findings in this audit report, Exhibit KLW-2.**

9 **A.** There were no findings in this audit related to hedging activities.

10 **Q. Does that conclude your testimony?**

11 **A.** Yes.

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**History of Testimony
Provided by Kathy L. Welch**

- In re: Application for approval of rate increase in Lee County by Tamiami Village Utility, Inc., Docket No. 910560-WS
- In re: Application for transfer of territory served by Tamiami Village Utility, Inc. in Lee County to North Fort Myers Utility, Inc., cancellation of Certificate No. 332-S and amendment of Certificate 247-S; and for a limited proceeding to impose current rates, charges, classifications, rules and regulations, and service availability policies, Docket No. 940963-SU
- In re: Application for a rate increase by General Development Utilities, Inc. (Port Malabar Division) in Brevard County, Docket No. 911030-WS
- In re: Dade County Circuit Court referral of certain issues in Case No. 92-11654 (Transcall America, Inc. d/b/a ATC Long Distance vs. Telecommunications Services, Inc., and Telecommunications Services, Inc. vs. Transcall America, Inc. d/b/a ATC Long Distance) that are within the Commission's jurisdiction, Docket No. 951232-TI
- In re: Application for transfer of Certificates Nos. 404-W and 341-S in Orange County from Econ Utilities Corporation to Wedgefield Utilities, Inc., Docket No. 960235-WS
- In re: Application for increase in rates and service availability charges in Lee County by Gulf Utility Company, Docket No. 960329-WS
- In re: Fuel and purchased power cost recovery clause and generating performance incentive factor, Docket No. 010001-EI
- In re: Application for staff-assisted rate case in Highlands County by The Woodlands of Lake Placid, L.P., Docket No. 020010-WS
- In re: Application for rate increase in Marion, Orange, Pasco, Pinellas, and Seminole Counties by Utilities, Inc. of Florida, Docket No. 020071-WS
- In re: Petition for rate increase by Florida Power & Light Company, Docket No. 050045-EI
- In re: Petition for issuance of a storm recovery financing order, by Florida Power & Light Company, Docket No. 060038-EI
- In re: Application for increase in wastewater rates in Monroe County by K W Resort Utilities Corp., Docket No. 070293-SU

- In re: Petition for rate increase by Florida Public Utilities Company, Docket No. 070304-EI
- In re: Natural gas conservation cost recovery, Docket No. 080004-GU
- In re: Nuclear cost recovery clause, Docket No. 080009-EI
- In re: Petition for rate increase by Florida Public Utilities Company, Docket No. 080366-GU
- In re: Petition for increase in rates by Florida Power & Light Company, Docket No. 080677-EI
- In re: Natural Gas Conservation Cost Recovery Clause for Florida City Gas, Docket No. 090004-GU
- In re: Nuclear cost recovery clause, Docket No.090009-EI, Florida Power & Light Company, Nuclear Uprate
- In re: Fuel and purchased power cost recovery clause with generating performance incentive factor, Docket No. 100001-EI, Florida Power & Light Company, Hedging
- In re: In re: Fuel and purchased power cost recovery clause with generating performance incentive factor, Docket No. 100001-EI, Florida Public Utilities Company, Fuel

State of Florida



Public Service Commission

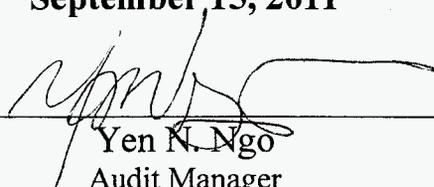
Office of Auditing and Performance Analysis
Bureau of Auditing
Miami District Office

Auditor's Report

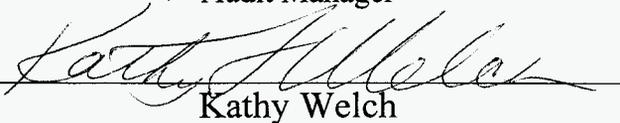
Florida Power & Light Company
Hedging Activities

Twelve Months Ended July 31, 2011

Docket No. 110001-EI
Audit Control No. 11-129-4-2
September 15, 2011



Yen N. Ngo
Audit Manager



Kathy Welch
Reviewer

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Purpose

To: Florida Public Service Commission

We have performed the procedures described later in this report to meet the agreed-upon objectives set forth by the Division of Economic Regulation in its audit service request dated May 9, 2011. We have applied these procedures to the schedules prepared by Florida Power & Light Company (FPL or Utility) in support of its filing for its Hedging Activities in Docket No. 110001-EI.

This audit was performed following General Standards and Fieldwork Standards found in the AICPA Statements on Standards for Attestation Engagements. Our report is based on agreed-upon procedures. The report is intended only for internal Commission use.

Objectives and Procedures

Accounting Treatment

Objectives: The objective was to verify that the accounting treatment for future option and swap contracts between the utility and its counter parties are in compliance with the Commission Order PSC-02-1484-FOF-EI, issued October 30, 2002 in Docket No. 011605-EI.

Procedures: We obtained a summary schedule of all financial futures, options and swaps that were executed by the utility for the 12-month period ended July 31, 2011. We reconciled the monthly gain or loss to the company's filing. We traced these gains and losses to the calculation of the average unit cost of gas and oil and to FPL's books and records. FPL's accounting treatment of hedging gains and losses was verified to be in compliance with Commission Order in Docket No. 011605-EI.

Objectives: The objectives were to verify that the level of hedging gains and losses associated with FPL's financial activities from August 2010 through July 2011 are consistent with the requirements of Commission Order in Docket No. 011605-EI and FPL's 2010 and 2011 Hedging Plans.

Procedures: We obtained the monthly level of hedging gains/losses and verified that they are consistent with the requirements of Commission Order in Docket No. 011605-EI and FPL's Hedging Plans. We also reviewed the company's external auditor's reports and workpapers on derivative activity for the 12-month period ended July 31, 2011.

Contracts

Objectives: The objective was to verify that the hedging contracts are in compliance with the Utility's stated objectives in its Hedging Plans.

Procedures: We sampled two contracts, one for natural gas and one for heavy oil, and reviewed the contracts to ensure that they were in compliance with the company's hedging plan.

Gains and Losses

Objectives: The objective was to reconcile the hedging results reported in the Utility's final July 31, 2011 filing to FPL's books and records.

Procedures: We traced the monthly hedging gains and losses to the supporting documents that were used to prepare FPL's filing. FPL provided the "Derivative Settlements-All Instruments" report that shows the calculation of all gains and losses by deal options and swaps made by each counter party. This report was traced to the filing. A sample of the October 2010 natural gas and September 2010 heavy oil transactions were selected for testing. The deals sampled were traced to confirmation letters, bank invoices, deal forms, and purchase statements. In addition, the settle price was traced to Platt's and NYMEX market data. In order to trace the September

and October 2010 gains and losses to the general ledger, account 151 Fuel Inventory, we first reconciled the gain and losses to the “Monthly Gas Closing Report” and “Allocation of Oil Financing Instrument” report, which, in turn, were reconciled to the general ledger.

Quantity of Gas and Residual Oil

Objectives: The objective was to verify that the quantities of gas, residual oil, and purchased power hedged are within the limits, i.e. the percentage range, specified in FPL’s risk management plans.

Procedures: We obtained the 2010 Risk Management Plan and the Planned Position Strategy (PPS) procedures, which show the hedged targets by months. The natural gas and the heavy oil actual percentage hedged were compared to the target hedged and verified to the specified tolerance bands. If the actual percent hedged of a particular month was not within the tolerance band, then a rebalance would be required. The rebalancing was implemented by either purchasing or selling the swaps to meet the established targets. We verified and recalculated the percent of hedge amounts and the rebalancing by month. No exceptions were noted.

Value At Risk (VaR)

Objectives: The objective was to verify that the individual and group transaction limits and authorizations set forth in FPL’s 2010 and 2011 Risk Management Plans have been followed.

Procedures: We verified that the VaR Activities were within the transaction limits and authorization as stated in the Risk Management Plans.

Segregation of Duties

Objectives: The objective was to verify that FPL has followed the procedures for separating duties related to the front office, middle office and back office.

Procedures: We reviewed the procedures for separating duties and had no exceptions.

Audit Findings

None