

State of Florida



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DATE: November 15, 2011

TO: Office of Commission Clerk (Cole)

FROM: Division of Economic Regulation (Wu, A. Roberts, Dowds, Draper) *SW*
Office of the General Counsel (Brown, Murphy) *ALM*
MCB *mcg from* *Mad for AT* *(M)*

RE: Docket No. 110007-EI – Environmental cost recovery clause.

AGENDA: 11/22/11 – Regular Agenda – Post-Hearing Decision - Participation is Limited to Commissioners and Staff

COMMISSIONERS ASSIGNED: All Commissioners

PREHEARING OFFICER: Brisé

CRITICAL DATES: 12/01/2011

SPECIAL INSTRUCTIONS: Decision must be rendered before 12/01/2011 in order to implement factors for 01/01/2012. This recommendation should be considered after the recommendation for Docket No. 110001-EI.

FILE NAME AND LOCATION: S:\PSC\ECR\WP\110007.RCM.DOC

Case Background

As part of the Commission’s continuing environmental cost recovery clause (ECRC) proceedings, the Commission held a hearing in this docket on November 1-2, 2011. Most of the issues presented at the hearing were stipulated and approved by the Commission at the hearing. There is one issue, raised by the Florida Industrial Power Users Group (FIPUG) and identified as Issue 10G during the hearing, that is contested. This issue addresses whether Progress Energy Florida, Inc. (PEF) should be permitted to recover any environmental costs related to its purchases of replacement power due to the Crystal River Unit 3 (CR3) extended outage. The Commission deferred its decision on this issue, as well as certain fall-out issues (identified as

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Docket No. 110007-EI
Date: November 15, 2011

Issues 1 – 4, and 7) regarding the appropriate amounts that PEF should be allowed to recover through the ECRC and the corresponding ECRC factors, until the November 22, 2011, Commission Agenda Conference. On November 8, 2011, PEF filed its Post-Hearing Brief in this docket, and the Office of Public Council (OPC), FIPUG, and the Federal Executive Agencies (FEA) (collectively, Consumer Intervenors) filed a Joint Post-Hearing Brief of Intervenors (Consumers Brief) in this docket and Docket No. 110001-EI, In re: Fuel and purchased power cost recovery clause with generating performance incentive factor.

This post-hearing recommendation addresses the aforementioned primary issue and its fall-out issues. The Commission has jurisdiction over these subject matters pursuant to the provisions of Section 366.8255, Florida Statutes, (F.S.).

Discussion of Issues

Issue 1 (10G): Should PEF be permitted to recover any environmental costs related to its purchases of replacement power due to the Crystal River Unit 3 extended outage?

Recommendation: The evidence in the record shows that PEF did not incur any environmental costs - specifically allowance purchases - associated with purchases of replacement power due to the CR3 extended outage; therefore, there are no costs to recover. Staff recommends that the amounts shown on Table 1 should be included in PEF's 2012 ECRC factors. (Wu, Brown, Dowds, Murphy)

Positions of the Parties:

PEF: Yes. Last year, the Commission held that PEF should recover CR3 replacement power costs, subject to refund. This includes costs incurred to ensure that emissions from replacement generation comply with CAIR. PEF demonstrated the reasonableness of these costs and should recover them, subject to refund, pending resolution of Docket 100437-EI.¹ (PEF BR 8)

Consumer Intervenors: No. Ratepayers should not be responsible for replacement power costs, capacity costs, environmental costs, recovery costs or any other charges resulting from the continued extended outage of Crystal River 3. No determination has yet been made regarding the prudence of PEF's actions that led to the CR3 outage. Until such a determination is made, it is unfair and inequitable to require ratepayers to carry the burden of PEF's costs related to the outage. (Consumers BR 5)

Staff Analysis: PEF is experiencing an unplanned extended outage at its Crystal River Nuclear Unit 3 (CR3) that started in mid-December 2009. FIPUG raised as an issue in this proceeding whether PEF should be permitted to recover any environmental costs related to its purchases of replacement power due to the CR3 extended outage. The environmental costs in question are emission allowances. PEF stated that no allowance purchases have been made associated with replacement power due to the CR3 extended outage. PEF has made no allowance purchases since May of 2009. (EXH 2, Bates No. 00000339) Therefore, the actual dollar amount associated with this issue, which is the costs of the emission allowances related to the purchases of replacement power due to the CR3 extended outage, is zero.

During the hearings, PEF and the intervenors – ancillary to the issue as framed - discussed whether PEF should be permitted to recover the environmental costs related to its replacement power costs incurred due to the CR3 extended outage, rather than the cost of any purchased emission allowances due to the CR3 extended outage, as Issue 10G stated. The replacement power costs due to the CR3 extended outage consist of two portions: the purchased replacement power and self-generated replacement power. Although there were no environmental costs incurred associated with purchases of replacement power due to the CR3 extended outage, there were environmental costs, namely the costs of the emission allowances, associated with the self-generated portion of the replacement power. Table 1 shows the

¹ Docket No. 100437-EI, In re: Examination of the outage and replacement fuel/power costs associated with the CR3 steam generator replacement project, by Progress Energy Florida, Inc.

estimated system expense associated with previously purchased emission allowances that were used for the purpose of generating replacement power due to the CR3 extended outage and included in PEF's projected 2012 factor. (EXH 41) Intervenors have not contested the amounts shown in Table 1.

2010	\$2,453,542
2011	\$1,191,999
2012	\$(957,130)
Total	\$2,688,411

The Consumer Intervenors oppose the recovery of the emission allowances related to the replacement power due to the CR3 extended outage. They asserted that PEF should not be permitted to recover any further costs related to the CR3 extended outage until the prudence issues in Docket No. 100437-EI are resolved. They argued that the Commission should deny PEF's request to recover any costs resulting from the outage of the CR3 nuclear power plant until it determines in Docket No. 100437-EI whether the events or actions leading to the CR3 outage were reasonable and prudent. (TR 234-238; Consumers BR 15)

PEF asserted that PEF's emission allowance costs are reasonable and recoverable. PEF stated that the Commission has determined that the evidence in this docket indicates that PEF followed a prudent NOx emission allowance strategy. (Order No. PSC-11-0505-PHO-EI,² at 21-22) PEF asserted that allowing CR3 extended outage-related environmental cost recovery prior to a determination of prudence is constitutional. PEF further asserted that deferral of recovery of emission allowance costs associated with the CR3 replacement power would contravene established Commission precedent and policy. (PEF BR 2-3) Moreover, PEF argued in its brief:

. . . by approving the stipulation of Issue 10E in this docket, the Commission established a regulatory asset to allow PEF to recover the cost of surplus NOx allowances in its inventory over a 3 year period. . . . The establishment of the regulatory asset effectively moots any issue in this proceeding regarding NOx allowance costs because had PEF not utilized the NOx allowances associated with the CR3 replacement power, they would have remained in inventory and been recovered through the regulatory asset. (PEF BR 4)

Staff notes that the Commission's practice in the environmental clause proceedings, as well as the Commission's other clause proceedings, has been to allow recovery of projected costs, which are then subject to true-up adjustments based on actual costs incurred.

² Order No. PSC-11-0505-PHO-EI, issued October 28, 2011, in Docket No. 110007-EI, In re: Environmental Cost Recovery.

Subsequently, the Commission may disallow costs if a finding of imprudence is made. (Order No. PSC-10-0734-EI,³ at 17) This practice allows cost recovery in a timely manner while protecting ratepayers by conducting a separate review for potential disallowance. Each year the Commission determines the next year's ECRC factor based on three types of costs: (1) final true-up amounts which are known to have been incurred during the prior year; (2) current period true-up amounts which consist of a half-year's actual and a half-year's estimated costs; and (3) projected amounts which are, of course, completely estimated costs. Thus, ECRC revenues, as well as those of all the other clauses, are collected from customers on a projected basis and subject to refund. The Commission approves cost recovery amounts for the next calendar year based upon estimates of the costs that will be incurred during that year. Estimates are never exact, so it is to be expected that there will be some variance between a utility's initial cost estimates and its actual costs. Accordingly, the cost recovery amounts approved for developing rates for the projected year will not only include the initial cost estimates for that year, but also a true-up of costs previously approved for recovery during the current year. The true-up process addresses the variances which occur between initial cost estimates and actual costs over a moving three-year period. (Order No. PSC-11-0505-PHO-EI, at 6-9)

PEF's Method of Accounting and Expensing of Emission Allowances

As part of its Clean Air Interstate Rule (CAIR) compliance program, PEF has maintained emission allowance inventories. (EXH 2, Bates No. 00000321; TR 254, 256) Some of these allowances were allocated by the Environmental Protection Agency (EPA) to PEF at no cost, and the rest were purchased by PEF in the market. (EXH 2, Bates No. 00000337) PEF confirmed that it booked to inventory at zero cost the allowances the EPA gave to PEF at no charge, and it did not impute a value for any allowances based on market conditions. (EXH 2, Bates No. 00000338) PEF values its overall pool of allowances at average cost, and expenses these allowances to meet emission compliance requirements using an average cost method. (EXH 2, Bates No. 00000337; TR 258)

During the hearing, FIPUG questioned the appropriateness of PEF using the average cost inventory valuation method, rather than a First In First Out (FIFO) method, for the accounting and expensing of its emission allowances. (TR 258-261, 325-330) PEF witness Garrett explained that the average cost method is recognized by the FERC and GAAP as an acceptable method of valuing inventories, and PEF uses this method not only for its emission allowance inventory, but also for its fuel inventories. (TR 259) Witness Garrett indicated that PEF has employed the average cost approach for its emission allowance accounting and expensing since the beginning of the emission compliance program (TR 263), and has not implemented any accounting changes related to emission allowances due to the CR3 extended outage. (TR 264)

In their Joint Post-Hearing Brief, the Consumer Intervenors asserted that PEF had sufficient zero-cost allowances to offset all emissions related to the CR3 extended outage. They argued that use of FIFO would result in no charge to ratepayers for these credits. The Consumer Intervenors do not believe it is appropriate for PEF to use the average market approach and allocate additional costs to ratepayers when no amount was paid for the CR3-related emission

³ Order No. PSC-10-0734-FOF-EI, issued December 20, 2010, in Docket No. 100001-EI, In re: Fuel and purchased power cost recovery clause with generating performance incentive factor.

allowances. The Consumer Intervenors argued that the Commission should reject the average cost accounting approach PEF requests in favor of the first in, first out approach. (Consumers BR 16)

PEF argued that it would be inappropriate to pick and choose an accounting methodology just to obtain a desired result as advocated by the Intervenors. Further, PEF argued that

... even if one accepts Intervenors' [sic] argument that the allowances attributed to the CR3 extended outage should be expensed at zero, there is an impact of increased cost on PEF's other allowances which must be taken into account. This impact to the cost of the other allowances that PEF expensed during this time period is unknown and not part of the record evidence. Thus, the Commission cannot base any decision on a FIFO methodology, even assuming that such a change in methodology could somehow be warranted.

PEF asserted that the Commission should not arbitrarily change the established methodology used to account for its emission allowance costs. (PEF BR 6)

In its brief, PEF mentioned that at the final hearing in this proceeding the Intervenors argued for the first time that the accounting methodology used for PEF's emission allowance inventory should be changed from an average cost basis to a FIFO basis. PEF pointed out that under the terms of the Order Establishing Procedure; the Intervenors waived this issue because they failed to raise it before the Prehearing Conference. (PEF BR 5) Staff notes that in Section C, Waiver of Issues, at page 6 of Order No. PSC-11-0150-PCO-EI,⁴ the Prehearing Officer ruled:

Any issue not raised by a party either before or during the Prehearing Conference shall be waived by that party, except for good cause shown. A party seeking to raise a new issue after the Prehearing Conference shall demonstrate each of the following:

- (1) The party was unable to identify the issue because of the complexity of the matter.
- (2) Discovery or other prehearing procedures were not adequate to fully develop the issue.
- (3) Due diligence was exercised to obtain facts touching on the issue.
- (4) Information obtained subsequent to the Prehearing Conference was not previously available to enable the party to identify the issue.
- (5) Introduction of the issue would not be to the prejudice or surprise of any party.

The record shows that while Counsel for FIPUG raised the question of a change in PEF's accounting practices with respect to emission allowances, there is no testimony or other evidence to support the appropriateness of such a change. Furthermore, FIPUG never raised this as an issue at the Prehearing Conference. Based on the record, staff recommends that it is appropriate

⁴ Order NO. PSC-11-0150-PCO-EI, issued March 4, 2011, In re: Order Establishing Procedure.

and reasonable for PEF to use the average cost valuation method to manage the accounting and expensing of its emission allowance inventories.

Constitutional Issues

As staff explains in its post-hearing recommendation in Docket No. 110001-EI, at pages 7-9, the Commission should decline to address the constitutional issues raised by the Consumer Intervenors. The staff notes, however, that the Consumer Intervenors have been given the opportunity to raise constitutional issues at the Florida Supreme Court, *de novo*, on appeal

Regulatory Asset for the Emission Allowances

As noted above, in its Post-Hearing Brief, PEF asserted that the establishment of the regulatory asset for NOx emission allowances effectively moots any issue in this proceeding regarding NOx allowance costs. If PEF had not utilized the NOx allowances associated with the CR3 replacement power, they would have remained in inventory and then been recovered through the regulatory asset. (PEF BR 4) As a result, the major portion of the CR3 extended outage-related environmental expenses shown in Table 1 will be recovered through the ECRC regardless of the Commission's decision in this issue. If the Commission approves staff's recommendation, the amounts shown in Table 1 should be included in the 2012 ECRC factors. If the Commission denies staff's recommendation, these expenses will be recovered through the ECRC over three years.

Conclusion

The evidence in the record shows that PEF did not incur any environmental costs - specifically allowance purchases - associated with purchases of replacement power due to the CR3 extended outage; therefore, there are no costs to recover. Staff recommends that the amounts shown on Table 1 should be included in PEF's 2012 ECRC factors.

Issue 2: What are the appropriate recovery amounts for PEF in the 2011 ECRC proceeding?

Recommendation: This is a fall-out issue. Staff shows below the amounts associated with staff's recommendation in Issue 1. (Wu, Brown)

Issue No. in ECRC Hearing	Description	Amounts
1	What are the final environmental cost recovery true-up amounts for the period ending December 31, 2010?	\$6,232,839 over-recovery
2	What are the estimated environmental cost recovery true-up amounts for the period January 2011 through December 2011?	\$2,552,337 over-recovery
3	What are the projected environmental cost recovery amounts for the period January 2012 through December 2012?	\$207,302,671
4	What are the environmental cost recovery amounts, including true-up amounts, for the period January 2012 through December 2012?	\$198,660,428

Positions of the Parties:

PEF: (BR 7)

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1	What are the final environmental cost recovery true-up amounts for the period ending December 31, 2010?	\$6,232,839 over-recovery
2	What are the estimated environmental cost recovery true-up amounts for the period January 2011 through December 2011?	\$2,552,337 over-recovery
3	What are the projected environmental cost recovery amounts for the period January 2012 through December 2012?	\$207,302,671
4	What are the environmental cost recovery amounts, including true-up amounts, for the period January 2012 through December 2012?	\$198,660,428

Consumer Intervenors: No position is provided for the fall-out issues in Consumer Intervenors's brief. At the Prehearing Conference, as memorialized in Order No. PSC-11-0505-PHO-EI, FIPUG took the following position:

FIPUG is opposed to ratepayers being charged now for replacement power costs, capacity costs, environmental cost recovery costs or any other charges resulting from the continued extended outage of Crystal River 3 until prudence issues related to this outage are determined by the Commission.

OPC took the following position:

OPC took the following position: Due to the changed circumstances caused by the subsequent discovery of a delamination in Bay 5-6 on or about March 14, 2011, due to the recent announcement by the Company that there may be other further possible delaminations or structural problems in other areas of containment building, and due to the fact that CR3 will not come online at any time during 2012, PEF should not be permitted to recover any costs for capacity or energy, including any capacity cost payments that would otherwise be recovered through the Capacity Cost Recovery Clause, that PEF incurred due to the extended outage at Crystal River 3 until after the conclusion of current pending prudence review in Docket No. 100437-EI.

Staff Analysis: This is a fall-out issue. Staff shows the amounts associated with staff's recommendation in Issue 1. (Wu, Brown)

Issue 3: What are the appropriate environmental cost recovery factors for the period January 2012 through December 2012 for each rate group for PEF?

Recommendation: This is a fall-out issue, which was identified as Issue 7 in the hearing. Staff shows below the factors associated with staff's recommendation in Issue 1. (Wu, A. Roberts, Draper, Brown)

Rate Class	ECRC Factors
Residential	0.545 cents/kWh
General Service Non-Demand	
@ Secondary Voltage	0.539 cents/kWh
@ Primary Voltage	0.534 cents/kWh
@ Transmission Voltage	0.528 cents/kWh
General Service 100% Load Factor	0.532 cents/kWh
General Service Demand	
@ Secondary Voltage	0.534 cents/kWh
@ Primary Voltage	0.529 cents/kWh
@ Transmission Voltage	0.523 cents/kWh
Curtailable	
@ Secondary Voltage	0.528 cents/kWh
@ Primary Voltage	0.523 cents/kWh
@ Transmission Voltage	0.517 cents/kWh
Interruptible	
@ Secondary Voltage	0.520 cents/kWh
@ Primary Voltage	0.515 cents/kWh
@ Transmission Voltage	0.510 cents/kWh
Lighting	0.529 cents/kWh

Positions of the Parties:

PEF: (BR 7)

Rate Class	ECRC Factors
Residential	0.545 cents/kWh
General Service Non-Demand	
@ Secondary Voltage	0.539 cents/kWh
@ Primary Voltage	0.534 cents/kWh
@ Transmission Voltage	0.528 cents/kWh

General Service 100% Load Factor	0.532 cents/kWh
General Service Demand	
@ Secondary Voltage	0.534 cents/kWh
@ Primary Voltage	0.529 cents/kWh
@ Transmission Voltage	0.523 cents/kWh
Curtailable	
@ Secondary Voltage	0.528 cents/kWh
@ Primary Voltage	0.523 cents/kWh
@ Transmission Voltage	0.517 cents/kWh
Interruptible	
@ Secondary Voltage	0.520 cents/kWh
@ Primary Voltage	0.515 cents/kWh
@ Transmission Voltage	0.510 cents/kWh
Lighting	0.529 cents/kWh

Consumer Intervenors: No position is provided for this fall-out issue in Consumer Intervenors's brief. In PSC-11-0505-PHO-EI, FIPUG took the following position:

FIPUG is opposed to ratepayers being charged now for replacement power costs, capacity costs, environmental cost recovery costs or any other charges resulting from the continued extended outage of Crystal River 3 until prudence issues related to this outage are determined by the Commission.

OPC took the following position:

OPC took the following position: Due to the changed circumstances caused by the subsequent discovery of a delamination in Bay 5-6 on or about March 14, 2011, due to the recent announcement by the Company that there may be other further possible delaminations or structural problems in other areas of containment building, and due to the fact that CR3 will not come online at any time during 2012, PEF should not be permitted to recover any costs for capacity or energy, including any capacity cost payments that would otherwise be recovered through the Capacity Cost Recovery Clause, that PEF incurred due to the extended outage at Crystal River 3 until after the conclusion of current pending prudence review in Docket No. 100437-EI.

Staff Analysis: This is a fall-out issue. Staff shows the factors associated with staff's recommendation in Issue 1. (Wu, A. Roberts, Draper, Brown)

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Issue 4: Should this docket be closed?

Recommendation: No. The Environmental Cost Recovery Clause docket is an on-going docket and should remain open. (Brown, Murphy)

Staff Analysis: The Environmental Cost Recovery Clause docket is an on-going docket and should remain open.