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BEFORE THE
FLORIDA PUBLIC SERVICE COMMISSION

DOCKET NO. 120015-EI

In the Matter of:

PETITION FOR INCREASE IN RATES
BY FLORIDA POWER & LIGHT COMPANY.

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VOLUME 19

Pages 2483 through 2738

PROCEEDINGS: HEARING

COMMISSIONERS
PARTICIPATING: CHAIRMAN RONALD A. BRISÉ
COMMISSIONER LISA POLAK EDGAR
COMMISSIONER ART GRAHAM
COMMISSIONER EDUARDO E. BALBIS
COMMISSIONER JULIE I. BROWN

DATE: Monday, August 27, 2012

PLACE: Betty Easley Conference Center
Room 148
4075 Esplanade Way
Tallahassee, Florida

REPORTED BY: MICHELLE SUBIA, RPR

APPEARANCES: (As heretofore noted.)

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P R O C E E D I N G S

(Transcript follows in sequence from
Volume 18.)

Thereupon,

KEVIN W. O'DONNELL

was called as a witness, having been first duly sworn,
was examined and testified as follows:

CONTINUED CROSS-EXAMINATION

BY MR. GUYTON:

**Q Mr. O'Donnell, let's start with what's been
identified as Exhibit 572. That's a Value Line report,
correct?**

A Yes, sir, it is.

**Q And Value Line is a widely available
investment service available to investors, correct?**

A Absolutely.

**Q And indeed you rely on Value Line for some of
your exhibits, correct?**

A Yes, sir, I do.

**Q And you've seen this Value Line assessment,
correct, for FPL Group, haven't you?**

A Yes.

**Q And it was issued following FPL's last rate
case decision, correct?**

A Yes.

1 **Q Would you read for the Commission the portion**
2 **of the discussion that's highlighted from this Value**
3 **Line report?**

4 A "FPL was hit with a harsh rate order earlier
5 this year. The utility had requested rate increases of
6 \$1 billion in 2010 and \$250 million in 2011 based on a
7 return on equity of 12.5 percent. Utilities almost
8 never get everything they request, but it came as a
9 shock when the Florida Commission granted FPL a tariff
10 hike of just 75.4 million this year based on an ROE in
11 a range of 9 percent to 11 percent."

12 **Q Now, is it your position that the analyst**
13 **that wrote this assessment of the rate order was**
14 **unaware of the capital structure employed by the**
15 **Commission in that rate order?**

16 A No. I think I just testified, I believe,
17 that they do review those. But at the end of the day,
18 what you're mostly concerned with is what the actual
19 capital structure is and primarily that of the
20 consolidated holding company.

21 **Q Would you turn to what's been identified as**
22 **Exhibit 573, please, the S&P report. This report**
23 **explains the downgrade by S&P to FPL Group, correct?**

24 A Yes, sir, that's correct.

25 **Q And like the Value Line assessment, this**

1 **report was issued after FPL's last rate case?**

2 A Yes, sir, it was.

3 **Q And you've seen this report as well, haven't**
4 **you?**

5 A Yes, sir. And I'm digging for it right now,
6 and I can't seem to place my hands on it, at least my
7 marked-up copy, so I'll have to go with this one.

8 **Q I can give you another minute, if you need**
9 **it.**

10 A If you would be so kind as to give me about
11 one minute.

12 **Q I'd be happy to.**

13 A Just to look through it real quickly.

14 Okay. I'm ready, sir.

15 **Q All right. If you would turn to page 2 and**
16 **read the highlighted material under "Rationale,"**
17 **please.**

18 A "FPL's credit fundamentals on its regulated
19 utility side have been among the strongest in the U.S.,
20 due primarily to low regulatory risk and an attractive
21 service territory with healthy economic growth and a
22 sound business environment. Both of those pillars have
23 been weakened in the past year as Florida and FPL's
24 service territory in particular have suffered during
25 the recession and regulators have responded with

1 decisions that reflect more intense political influence
2 over the regulatory environment."

3 **Q And would you turn to page 3, please.**

4 A Yes.

5 **Q And would you read the highlighted passage on**
6 **page 3 on Exhibit 573.**

7 A "Regulatory risk, the most important risk a
8 utility faces, has been well-managed at FPL but has
9 risen of late as regulators have reacted to weak
10 economic conditions and keener attention in the
11 political arena with a series of decisions for FP&L
12 that fall short of the very sound record of past
13 support for credit quality."

14 **Q Do you agree with S&P's statement that**
15 **regulatory risk is the most important risk that a**
16 **utility faces?**

17 A I certainly won't argue with that. Yes, sir.
18 I guess what I'm a little bit confused about on this
19 particular report is that I've got a bunch of other
20 reports over here that indicated that economic
21 conditions were also part of the reason for the
22 downgrade, and that's I was trying to find in this
23 document.

24 **Q Would you turn to what's been identified as**
25 **574, please. Now, this is the report issued by Moody's**

1 for explanation of their downgrade of FPL after FPL's
2 last rate case, correct?

3 A Yes, sir.

4 Q And at the bottom of page 1 and the top of
5 page 2, Moody's explains its downgrade rationale for
6 FPL, correct?

7 A Yes, sir.

8 Q And in the interest of time, if you would
9 just look at the last bullet point highlighted on
10 page 2. Would you please read that into the record.

11 A The second or the bullet highlighted?

12 Q The second highlighted, the one that begins
13 "Historically strong."

14 A "Historically strong financial metrics and
15 cash flow coverage methods that may decline somewhat
16 following the recent rate case decision; although,
17 Moody's expects any decline to be modest, as a high
18 percentage of FP&L's revenues are recovered through
19 riders or other cost recovery provisions that remain
20 strong.

21 "In addition, FP&L's recently awarded
22 10 percent ROE is consistent with those granted to some
23 utilities in other parts of the country. And its
24 59.1 percent equity ratio remains one of the highest in
25 the U.S., mitigating the negative effect of the

1 relatively low base rate increase."

2 **Q So Moody's explicitly noted in its downgrade**
3 **that FPL's capital structure mitigated the negative**
4 **impact of the relatively low base rate increase,**
5 **correct?**

6 A Oh, I'm sorry. I didn't know if that was a
7 question.

8 That is what it -- that is what it does say.
9 But, again, I think it also says 59.1 percent is one of
10 the highest equity ratios in the industry. And based
11 upon my experience in the industry, I think that is
12 definitely an accurate statement.

13 **Q So without that strong capital structure, the**
14 **downgrade could have been worse?**

15 A I don't know if that were the case or not,
16 because there are other credit agency reports that I've
17 got over here where they talk about the poor economy in
18 the state of Florida at the time of the downgrade, so
19 it had definitely to do with more than just the rate
20 case order; it had to do with the poor economic
21 conditions that were going on at the same time.

22 **Q Well, let me get this straight. As a result**
23 **of the last rate case decision which granted FPL a**
24 **return on equity of 10 percent and used a regulatory**
25 **capital structure of 59.6 percent, S&P and Moody's both**

1 **downgraded FPL, correct?**

2 A No, sir, I'm not willing to go that far,
3 because I think I've just seen -- what I've just stated
4 is that the downgrade occurred for other reasons other
5 than just because of the rate case order. I think
6 we've seen poor economic conditions were also part of
7 the reason why the downgrade occurred. It was not
8 simply due to the rate case order, from what I'm seeing
9 in these other credit reports.

10 **Q And in this case, FPL's witnesses recommend a**
11 **return on equity not of 10 percent but 8.5 to**
12 **9 percent, and a reduction of the equity ratio from**
13 **59.6 to 50 percent, and you all maintain there won't be**
14 **an effect on the company's credit rating?**

15 A No, sir, I don't believe so, because I think
16 what we have seen, as Dr. Woolridge pointed out, is
17 that you've got -- interest rates have come down since
18 the last rate case. And I think that my recommended
19 equity ratio is going to be contemplated by the market.
20 I mean, we just read the statement you had me read
21 talking about 59.1 percent equity ratio is one of the
22 highest in the United States.

23 I think the market is very well aware that
24 that 59.6 percent equity ratio may not stand forever,
25 particularly given the fact that most other utilities

1 have somewhere in the neighborhood of 50 percent equity
2 ratio or so.

3 **Q Mr. O'Donnell, are you familiar with the**
4 **statement "Those who cannot remember the past are**
5 **condemned to repeat it"?**

6 A Absolutely.

7 MR. GUYTON: That's all I have. Thank you.

8 CHAIRMAN BRISE: Staff.

9 MR. HARRIS: Mr. Chairman, in lieu of
10 cross-examination, staff would like to introduce
11 the deposition of Mr. O'Donnell. I think it's
12 been identified in the comprehensive exhibit list
13 as Exhibit No. 114. We also exhibited an errata
14 sheet with it. I don't see that it's marked in
15 any way, but it does have the witness's signature
16 for the deposition.

17 CHAIRMAN BRISE: Okay.

18 MR. GUYTON: No objection.

19 CHAIRMAN BRISE: We'll include that as part
20 of 114.

21 MR. HARRIS: Yes, sir.

22 CHAIRMAN BRISE: Okay.

23 MR. HARRIS: That's all we had. And I don't
24 believe I heard any objections from anyone.

25 MR. GUYTON: No objection.

1 CHAIRMAN BRISE: Any objections?

2 (No response.)

3 (Exhibit No. 114 marked for identification.)

4 CHAIRMAN BRISE: Commissioners.

5 Commissioner Balbis.

6 COMMISSIONER BALBIS: Thank you. I do have
7 one question, and it's a follow-up on -- well, let
8 me ask you this: Did you hear the testimony of
9 Mr. Dewhurst?

10 THE WITNESS: No, sir, I'm sorry, I was not
11 here for that. And I couldn't stream it on -- I
12 was traveling last week, I couldn't stream it.

13 COMMISSIONER BALBIS: Okay. Well, I'll ask
14 you the same question, because him and I had a
15 discussion about the capital structure. And one
16 of the comments he made was that FPL has had a
17 similar capital structure for several years and
18 has served the customers well. And then I had
19 asked what detrimental effects, if any, would
20 occur if that capital structure were changed.

21 And your testimony, you're recommending a
22 significant shift in their capital structure.
23 What are some negative impacts, if any, to the
24 customers if that occurs?

25 THE WITNESS: I don't believe that there are

1 going to be the negative impacts. Let me start
2 off by answering it this way: Right now I believe
3 that the ratepayers of FPL are paying a higher
4 interest rate than they would have otherwise --
5 and this is in my testimony so I'm not going
6 outside the bounds -- I think that they are paying
7 a higher interest rate today than they would have
8 if they were a standalone entity.

9 So to that degree, I think that they were
10 already being penalized. And the reason being is
11 because S&P links the utility credit rating to
12 that of a consolidated. And they are looking at a
13 39 percent equity ratio in the consolidated;
14 whereas, FPL is 59.6.

15 So we're paying substantially higher revenue
16 requirements to offset the possibility that there
17 will be a credit downgrade. And when you look at
18 the numbers of that, they're staggering.

19 In essence, we're being asked to pay an extra
20 \$214 million in the higher revenue requirements
21 for the possibility of not getting downgraded,
22 which may -- and if you'll assume the CAPEX next
23 year are \$3 billion and you assume 100 percent
24 equity, you may pay higher interest costs in the
25 neighborhood of \$20 million or so. So it doesn't

1 make a whole lot of sense to me.

2 And all I'm saying is let the ratepayers of
3 Florida get some of the benefits. The negative
4 aspect of what you've asked me, I don't believe
5 that the bond rating will be downgraded because of
6 it. And beyond that, with all of the other
7 regulatory factors that are involved, the fuel
8 adjustment clause, hurricane recovery factors and
9 conditions like that, I don't see the negative
10 implications.

11 COMMISSIONER BALBIS: Okay. And I have one
12 other question. Mr. Guyton had asked you to read
13 from an excerpt which indicated that, I believe,
14 it was due to the strong equity ratio that it
15 mitigated the effects of the rate request where
16 this Commission approved 75 million versus the
17 \$1 billion.

18 So would it be true then that if FPL received
19 an adequate revenue requirement, it would mitigate
20 the need for a higher equity ratio?

21 THE WITNESS: I'm sorry, let me see if I can
22 understand what you're asking me. You're saying
23 if they received a certain revenue requirement, it
24 would offset the need for a different equity
25 ratio?

1 COMMISSIONER BALBIS: Right, because his line
2 of questioning was, okay, we'll -- and I'm going
3 to paraphrase -- but luckily FPL's capital
4 structure had a high equity ratio which mitigated
5 the detrimental effects of not receiving the
6 revenue requirements it needed or it asked for.

7 So in this case, if FPL receives adequate
8 revenue requirements, then FPL would not need that
9 high equity ratio?

10 THE WITNESS: I don't know if -- I'm sorry
11 for being a little dense. I'm not certain if I'm
12 fully getting it.

13 But if this Commission grants a higher
14 revenue requirement and FPL chooses on its own
15 part to reduce its equity ratio, I think that that
16 would be a good thing for ratepayers in the longer
17 term because maybe instead of debating a
18 59 percent equity ratio, next time around they may
19 be debating a 55 percent equity ratio.

20 But I would also indicate that I think OPC
21 has taken that factor into consideration because
22 Dr. Woolridge has assigned a lower ROE if you use
23 the 59.6 percent equity ratio and a higher ROE if
24 you use my 50/50 capital structure. So I think
25 that OPC has taken that into account.

1 And what FPL does moving forward, yes, I hope
2 they do come off the 59.6 percent because I
3 haven't seen it like that other places. But I do
4 believe that whatever revenue requirement you
5 give, it may give the company the ability to lower
6 that equity ratio if they so choose.

7 COMMISSIONER BALBIS: Okay. Thank you.
8 That's all I had.

9 CHAIRMAN BRISE: Commissioner Brown.

10 COMMISSIONER BROWN: Thank you. And
11 Commissioner Balbis actually asked my question,
12 but I think I have one more for you.

13 You said in your testimony that the requested
14 capital structure does not reflect -- of what FPL
15 is requesting -- does not effect the true risk for
16 a return relationship inherent in an investment.
17 But then you also say that NextEra's consolidated
18 equity ratio would be too onerous for FPL.

19 So I'm trying to understand then how an
20 average of what FPL is requesting versus -- or the
21 average between what FPL is requesting from what
22 NextEra's equity ratio is, is truly reflective of
23 the risk return relationship.

24 THE WITNESS: When an investor goes into the
25 marketplace -- if you were to go back home tonight

1 and you pull your Value Line out and you decide
2 that you wanted to invest in a utility, what
3 you're going to see from that equity investment is
4 going to be the consolidated equity ratio. In
5 this case for NextEra, it's going to be 39.6.

6 From a pure financial theory standpoint, I've
7 always preferred to use that consolidated equity
8 ratio. In this case, the gulf was too big, it's
9 too wide, 39.6 to 59.6 on a revenue requirement
10 basis that accounted for over \$400 million in a
11 case that's worth \$690 million.

12 We decided to be fair to FPL and to
13 ratepayers to basically split that difference.
14 \$400 million was a little bit too hard, so we went
15 on the conservative side and went 50/50 is halfway
16 between consolidated and halfway between FPL.

17 COMMISSIONER BROWN: But is that
18 contradicting your testimony that -- is that
19 reflective of the true risk return relationship?

20 THE WITNESS: I see your point. To some
21 extent, yes. But this is a regulatory market that
22 we deal with. In regulation you don't have
23 market-driven forces. If we had purely
24 market-driven forces, and if this Commission
25 were -- if I felt like you-all would be okay with

1 using a 39 percent equity ratio, I would have
2 recommended it. But when we put our case
3 together, I looked at that and said that's a
4 little bit too harsh. So to your point, yes.

5 But I would also argue that the same is true
6 for NextEra and FPL. They used an operating
7 company capital structure but a
8 stock-market-driven return on equity, so you've
9 got two inconsistencies here. And the only way to
10 be 100 percent consistent would be to use the
11 consolidated capital structure. And we felt like
12 that was a little bit too harsh on the revenue
13 requirement side.

14 COMMISSIONER BROWN: Okay. Thanks.

15 CHAIRMAN BRISE: All right. Any further
16 questions, Commissioners?

17 (No response.)

18 CHAIRMAN BRISE: Seeing none, Mr. McGlothlin,
19 you may redirect.

20 REDIRECT EXAMINATION

21 BY MR. MCGLOTHLIN:

22 **Q Mr. O'Donnell, Mr. Guyton asked you some**
23 **questions that related to the impact on investors of**
24 **modified -- of low ranging equity ratio for rate-making**
25 **purposes. Do you remember that question and answer?**

1 A Yes.

2 **Q What would be the implications for customers**
3 **of keeping 59.6 percent equity ratio for rate-making**
4 **purposes in this case?**

5 A They would be overpaying by at least
6 \$214 million and, in my view, not getting any of the
7 benefits of lower interest costs that would have --
8 that would accrue to them had they been a standalone
9 company.

10 **Q Assume for purposes of the question that a**
11 **utility is employing an equity ratio that all parties**
12 **and Commission agree is unreasonably high for the**
13 **purpose of the question.**

14 **In that situation, would equity investors be**
15 **entitled or have a justified expectation of the**
16 **continuation of that for rate-making purposes?**

17 A No.

18 **Q Commissioner Balbis asked you a question that**
19 **involved the setting of an equity ratio in light of a**
20 **particular revenue award to the utility. Do you recall**
21 **that question?**

22 A Yes.

23 **Q What is the relationship between equity ratio**
24 **and return on equity?**

25 A They're linked. The higher the -- and that

1 goes to the point we made in this case. If you go with
2 the 59.6 percent equity ratio, that's lower financial
3 risk, therefore, Dr. Woolridge recommends 8 and a half
4 percent. If you go with the 50/50 equity ratio --
5 excuse me -- 50 percent equity ratio, then that means
6 slightly more financial risk and therefore slightly
7 higher ROE.

8 And if you look at these numbers right here,
9 you can see the cases that I'm referring to. They work
10 out relatively close in terms of the revenue
11 requirement impact between the different capital
12 structures and associated ROEs.

13 **Q If you will turn to what was marked as 573 on**
14 **page 2, which is captioned "FPL Group, Inc. Downgraded**
15 **to A minus from A." Do you have that?**

16 A Is that the S&P document?

17 **Q Yes.**

18 A Okay. Yes, sir.

19 **Q Mr. Guyton asked you to read the highlighted**
20 **paragraph directly under "Rationale." Do you see that?**

21 A Yes.

22 **Q There's another sentence that I would like**
23 **for you to read, and it begins below that beginning**
24 **with the words "In addition." Would you read that to**
25 **the Commissioners.**

1 A Yes. "In addition, the balance between
2 regulated utility operations and unregulated businesses
3 is projected to trend in favor of the riskier merchant
4 generation, marketing and trading activities, as lower
5 returns and higher regulatory risk in Florida lead to
6 changes in capital allocation decisions. This will
7 erode FPL's business risk profile, which we now deem to
8 be strong instead of excellent."

9 **Q Does it appear to you that the credit**
10 **agencies regard capital allocation decisions as**
11 **something that's going to be changing over time?**

12 MR. GUYTON: Objection, leading. He can
13 restate the question.

14 BY MR. McGLOTHLIN:

15 **Q What does this sentence indicate to you with**
16 **respect to the view of credit agencies on capital**
17 **allocation decisions?**

18 A It indicates to me that as NextEra moves more
19 towards unregulated operations, that its business risk
20 profile is going to be increasing.

21 MR. McGLOTHLIN: Those are all of my
22 questions.

23 CHAIRMAN BRISE: Thank you.

24 Exhibits.

25 MR. McGLOTHLIN: OPC moves 225 through 235

1 inclusive.

2 CHAIRMAN BRISE: Okay. 225 through 235. Are
3 there any objections?

4 MR. GUYTON: No objection.

5 CHAIRMAN BRISE: Okay. Seeing no objections,
6 we will move 225 to 235 into the record.

7 (Exhibit Nos. 225 through 235 received in
8 evidence.)

9 MR. GUYTON: FPL moves Exhibit 572, 573, and
10 574.

11 CHAIRMAN BRISE: Okay. Are there any
12 objections to --

13 MR. MOYLE: FIPUG would like to be heard on
14 these at the right time.

15 CHAIRMAN BRISE: Okay. Are there any
16 objections on 572, 573, and 574?

17 MR. McGLOTHLIN: No.

18 MR. SAPORITO: Mr. Chairman, I have an
19 objection on 574 because my page 3 and 4 of that
20 exhibit are kind of obliterated and I can't read
21 it.

22 MR. GUYTON: We'll be happy to provide
23 Mr. Saporito with a more legible copy.

24 CHAIRMAN BRISE: Okay. So your objection
25 isn't to the document, it's just you just want a

1 clean copy?

2 MR. SAPORITO: Yes, sir.

3 MS. HELTON: Mr. Chairman, mine is also, so
4 I'm not sure if all of them are in that state.

5 CHAIRMAN BRISE: Mine isn't clear either.

6 MR. GUYTON: We will endeavor to get that
7 back to the Commission later today.

8 CHAIRMAN BRISE: Thank you.

9 Mr. Moyle.

10 MR. MOYLE: So the FIPUG objection, I
11 guess -- and it may prompt a question -- but to
12 the extent that these documents are offered for
13 the truth of the matter asserted, you know, we
14 would object. To the extent that they are offered
15 with respect to informing an expert's opinion and
16 the expert is offering the opinion based on these
17 reports, then we are okay.

18 But I don't think it's appropriate for these
19 documents to be used in effect for the statements
20 in here as to the truth of what's in these
21 statements, whether -- you know, there's a whole
22 bunch of factual statements. So that's the basis
23 of the objection.

24 CHAIRMAN BRISE: Okay. We'll move it into
25 the record and we'll give it the weight that is

1 due.

2 (Exhibit Nos. 572, 573 and 574 received in
3 evidence.)

4 MR. HARRIS: Staff would move 114.

5 CHAIRMAN BRISE: Okay. 114. Any objections
6 to 114?

7 (No response.)

8 CHAIRMAN BRISE: All right. Seeing no
9 objections to 114.

10 (Exhibit No. 114 received in evidence.)

11 CHAIRMAN BRISE: So we have dealt with these
12 exhibits, and we will get a copy of -- a clean
13 copy of Exhibit 574, okay.

14 Thank you, Mr. O'Donnell.

15 THE WITNESS: Thank you. It's good to be
16 back in Tallahassee.

17 CHAIRMAN BRISE: All right. Mr. McGlothlin.

18 MR. MCGLOTHLIN: OPC calls Jacob Pous.

19 Mr. Chairman, may we excuse the first two
20 witnesses from further attendance of the hearing?

21 CHAIRMAN BRISE: Sure. Mr. O'Donnell, you
22 are excused.

23 MR. MCGLOTHLIN: And Dr. Woolridge.

24 CHAIRMAN BRISE: And Dr. Woolridge, you are
25 excused as well. Thank you.

1 Thereupon,

2 JACOB POUS

3 was called as a witness, having been first duly sworn,

4 was examined and testified as follows:

5 DIRECT EXAMINATION

6 DIRECT EXAMINATION

7 BY MR. MCGLOTHLIN:

8 **Q Were you sworn earlier today?**

9 A Yes, I was.

10 **Q Would you state your full name and business**
11 **address for the record.**

12 A My name is Jacob Pous, that's P-o-u-s. I go
13 by Jack. My business address is 1912 West Anderson
14 Lane, Austin, Texas.

15 **Q Mr. Pous, on behalf of the Office of Public**
16 **Counsel, did you prepare and submit prefiled testimony**
17 **in the docket?**

18 A Yes, I did.

19 **Q Do you have that document with you?**

20 A Yes, I do.

21 **Q Do you have any changes or corrections to**
22 **make to your prefiled testimony?**

23 A No.

24 **Q Do you adopt the questions and answers**
25 **contained in this prefiled document as your testimony**

1 **today?**

2 A Yes.

3 MR. McGLOTHLIN: I request that the prefiled
4 testimony of Mr. Pous be inserted into the record
5 at this point.

6 CHAIRMAN BRISE: All right. We will enter
7 Mr. Pous' prefiled testimony as though read into
8 the record, seeing no objections.

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DIRECT TESTIMONY

OF

Jacob Pous

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

Docket No. 120015-EI

SECTION I: STATEMENT OF QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Jacob Pous. My business address is 1912 W Anderson Lane, Suite 202, Austin, Texas 78757.

Q. WHAT IS YOUR OCCUPATION?

A. I am a principal in the firm of Diversified Utility Consultants, Inc. (“DUCI”). A description of my qualifications appears as Exhibit No.__(JP-Appendix A).

Q. PLEASE DESCRIBE DIVERSIFIED UTILITY CONSULTANTS, INC.

A. DUCI is a consulting firm located in Austin, Texas. DUCI has an international client base. DUCI provides engineering, accounting, and financial services to clients. DUCI provides utility consulting services to municipal governments with utility systems, to end-users of utility services and to regulatory bodies such as state public service commissions. DUCI provides complete rate case analyses, expert testimony, negotiation

1 services and litigation support in electric, gas, telephone, water, and sewer utility
2 matters.

3
4 **Q. HAVE YOU PREVIOUSLY TESTIFIED IN PUBLIC UTILITY**
5 **PROCEEDINGS?**

6 A. Yes. Exhibit No. ___(JP-Appendix A) also includes a list of proceedings in which I have
7 previously presented testimony. In addition, I have been involved in numerous utility
8 rate proceedings that resulted in settlements before testimony was filed. In total, I have
9 participated in well over 400 utility rate proceedings in the United States and Canada. I
10 have testified on behalf of the staff of five different United States regulatory
11 commissions, and one Canadian regulatory body on subjects relating to appropriate
12 depreciation rates.

13
14 **Q. WHAT IS YOUR PROFESSIONAL BACKGROUND?**

15 A. I am a registered professional engineer. I am registered to practice as a Professional
16 Engineer in numerous states.

17
18 **Q. ON WHOSE BEHALF ARE YOU PROVIDING THIS TESTIMONY?**

19 A. Florida's Office of Public Counsel ("OPC") engaged me to address the subject of the
20 amortization of excess depreciation reserve that is treated in Florida Power & Light
21 Company's ("FPL" or "the Company") filing before Florida Public Service Commission
22 (the "Commission" or "FSPC") in this proceeding.

1 **SECTION II: OVERVIEW**

2 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

3 A. The purpose of my testimony is to address the surplus depreciation amortization issue.
4 Specifically, FPL describes the decision of the Commission in Docket No. 080677-EI to
5 require FPL to return \$895 million of depreciation reserve surplus to customers over
6 four years as a \$104 million “driver” of its current request. Elsewhere in testimony, FPL
7 states that the decision to require FPL to amortize a portion of its depreciation reserve
8 surplus over four years was a “temporary” means of postponing an increase in base
9 rates. (See Mr. Barrett’s Direct Testimony at page 26). In my testimony, I will show
10 that both of these statements, which appear designed to criticize, albeit indirectly, the
11 policy decision made in Docket No. 080677-EI, are misplaced. In addition, I will
12 address how FPL’s claimed \$191 million amortization of excess depreciation reserve, or
13 other level proposed by other parties and ultimately adopted, for the 2013 test year
14 should be treated after the 2013 test year.

15
16 **SECTION III: TREATMENT OF AMORTIZATION OF SURPLUS**
17 **DEPRECIATION - PRIOR RATE CASE**

18 **Q. YOU SAID FPL’S STATEMENTS APPEAR TO BE CRITICAL OF A POLICY**
19 **DECISION THE COMMISSION MADE IN DOCKET NO. 080677-EI. PLEASE**
20 **BRIEFLY EXPLAIN THE MATTERS THE COMMISSION ADDRESSED AND**
21 **THE RATIONALE FOR ITS DECISION.**

22 A. A utility recovers costs of items or services that it “consumes” within one year by
23 ”expensing” the entire cost within that year. A utility accounts for capital investments in
24 plant differently. The objective relating to plant is to “depreciate,” or recover the total
25 cost of the plant item, during the full period during which it is in service, such that

1 customers who receive service from the plant pay their fair share of the cost of the plant
2 that serves them. This process of fair recovery over the useful life is called the
3 “matching principle.” The utility therefore recovers a portion of the cost of plant each
4 year. The Commission approves depreciation rates that are designed to result in the
5 appropriate amount of depreciation expense or capital recovery annually. Because the
6 service lives of plant items and their corresponding net salvage values are estimates, and
7 those estimates change over time, periodically the Commission requires utilities to
8 perform “depreciation studies” to ascertain: (1) whether the utility is “on course” to
9 recover the investment in plant ratably over the related service lives, and (2) if there is a
10 discrepancy (i.e., the utility is either ahead of schedule or behind schedule), the
11 adjustments necessary to rectify the imbalance. A severe imbalance between the amount
12 of depreciation that the utility has collected and the amount it *should* have collected at a
13 given point in time means that current and historical customers paid either too much or
14 too little of the overall cost of plant. This imbalance is frequently called an
15 “intergenerational inequity.” The corrective measure is to fashion depreciation rates that
16 have the effect of a mid-course correction. Typically, the correction takes place over the
17 currently estimated remaining lives of the plant items. However, in Docket No. 080677-
18 EI, which was consolidated with the concurrent docket involving FPL’s last depreciation
19 study and request for then current estimated service lives and depreciation rates, the
20 Commission determined the remaining life approach was inadequate to address FPL’s
21 specific circumstances.

22
23 **Q. WHAT WERE THOSE CIRCUMSTANCES?**

24 A. Very simply, the depreciation reserve imbalance created by FPL’s prior over collection
25 of depreciation expense was so extreme—meaning that current customers had paid such

1 an inordinately high portion of the costs of plant during the early part of the plant's
2 service lives—that to have flowed the excess amount it had collected back to customers
3 over the next 18-20 years (FPL's estimated remaining life for plant) would have not
4 adequately addressed the severity of the inequity that FPL's situation presented. Indeed,
5 this severe imbalance existed, even after FPL had voluntarily sought and received
6 permission to credit (reduce) depreciation expense by a billion dollars so as to reduce the
7 excess level of depreciation reserve in the periods prior to the filing that initiated Docket
8 No. 080677-EI.

9
10 **Q. DID YOU TESTIFY REGARDING THE EXCESS DEPRECIATION RESERVE**
11 **ISSUE IN FPL'S LAST RATE PROCEEDING?**

12 A. Yes. I submitted testimony regarding the excess level of depreciation reserve in FPL's
13 last rate case. In that testimony I noted that not only did FPL admit to a material excess
14 depreciation reserve, but I also identified that the level of excess reserve was much
15 greater than indicated by FPL.

16
17 **Q. WHAT ACTION DID THE COMMISSION TAKE IN DOCKET NO. 080677-EI?**

18 A. Based in part on my testimony, the Commission determined that it was appropriate to:
19 (1) recognize that a \$1.2 billion excess depreciation reserve did exist, (2) that \$314
20 million of that amount should be used to immediately offset capital recovery schedules
21 that FPL had requested, and (3) that the remaining \$895 million of the \$1.2 billion
22 should be amortized over a four-year period. (See Order No. PSC-10-0153-FOF-EI,
23 pages 22 and 82). The amortization pattern of the \$895 million surplus reserve from
24 2010 through 2012 was later identified in the 2010 Rate Settlement associated with
25 FPL's last rate case. That settlement provided FPL flexibility in the timing of the

1 amortization during the 2010 through 2012 timeframe. (See Mr. Barrett's Direct
2 Testimony at page 25).

3
4 **Q. WHAT HAPPENS AS FPL IMPLEMENTS THE COMMISSION'S POLICY**
5 **DECISION IN DOCKET NO. 080677-EI?**

6 A. To explain this, I must begin with what usually happens when the utility records
7 depreciation expense. At the same time the utility records depreciation expense on its
8 books, it also records a corresponding amount in an account called the "depreciation
9 reserve," or the "accumulated provision for depreciation," which normally increases
10 over time as additional depreciation expense is recorded. The gross amount recorded for
11 the investment in plant remains constant on the books, but (for purposes of quantifying
12 the rate base used in the ratemaking formula) is offset by the depreciation reserve, which
13 represents the amount of capital recovery that has accumulated (and therefore the
14 portion of plant costs that have been recovered from customers) over time. When the
15 Commission requires a utility to amortize depreciation reserve surplus, this process is
16 reversed. The amount of the annual amortization of the surplus has the effect of
17 offsetting (reducing) the depreciation expense for that period, and the corresponding
18 reversing entry to the depreciation reserve has the effect of reducing the size of the
19 depreciation reserve. Since the depreciation reserve represents the amount by which the
20 gross investment in plant is reduced for rate base and ratemaking purposes, reducing the
21 reserve has the effect of increasing rate base (i.e., gross plant less depreciation reserve
22 equals net plant).

23
24 **Q. DOES THIS REVERSAL MEAN RATE BASE WILL BE HIGHER IN THE**
25 **FUTURE THAN WOULD HAVE BEEN THE CASE IF THE COMMISSION**

1 **HAD SPREAD THE CORRECTION OVER THE FULL REMAINING LIVES**
2 **INSTEAD OF FOUR YEARS?**

3 A. Yes, but not higher than rate base would have been had FPL been recovering the cost of
4 its plant over time at the appropriate rate in the first place. The current aspect of the
5 amortization correction simply reflects the fact that rate base had previously been
6 reduced on an accelerated basis, and that a continuation of “business as usual”
7 (correction over the full remaining life) would have overstated then current (2010) rates
8 and understated the cost responsibility of future customers whom the plant will continue
9 to serve. In other words, the accelerated action in the last rate case was necessary to
10 meaningfully address the prior violation of the “matching principle” and to bring rate
11 base more in line to where it should have been.

12
13 **Q. EARLIER, YOU SAID FPL PRESENTED A SEVERE OVERCOLLECTION**
14 **SITUATION DESPITE THE FACT IT HAD SOUGHT AND RECEIVED**
15 **PERMISSION TO REDUCE THE EXCESS DEPRECIATION RESERVE IN**
16 **PERIODS PRIOR TO DOCKET NO. 080677-EI. PLEASE ELABORATE.**

17 A. In the final order that it issued in Docket No. 080677-EI, the Commission recognized
18 that about \$300 million of FPL’s then current base rate case request was due to the \$125
19 million annual depreciation reserve credit due to the prior excess depreciation reserve
20 that was recorded in accordance with the 2005 FPL rate case settlement order. (See
21 Order No. PSC-10-0153-FOF-EI at page 83, footnote 28). In other words, by the end of
22 the 1990s, FPL was in a significant intergenerational inequity position as it related to its
23 depreciation reserve. FPL previously recognized the significant level of excess
24 depreciation reserves that had been amassed and agreed to amortize \$1 billion of the
25 excess prior to its last rate case. In the last rate case, the Commission determined it

1 should address the remaining intergenerational inequity in a more meaningful manner
2 than proposed by FPL. In that case the Commission ordered the amortization of excess
3 depreciation reserve over a four-year period (2010 – 2013), rather than over the
4 remaining life as proposed by FPL.

5
6 **Q. WAS THE COMMISSION FULLY COGNIZANT OF THE FACT THAT**
7 **AMORTIZATION OF EXCESS RESERVES WOULD RESULT IN HIGHER**
8 **REVENUE REQUIREMENTS IN FUTURE CASES?**

9 A. Yes. The Commission was well aware that FPL's rate base was low in relation to what
10 would have been the case had historical depreciation expense been collected ratably over
11 the current life expectations. In other words, the various amortizations of excess
12 reserves result in future rate base being more in line with where it should have been all
13 along. The Commission properly recognized that the resulting correction of future
14 depreciation expense due to excess depreciation reserve amortization is the only way to
15 meaningfully address the intergenerational inequity due to prior over collection of
16 depreciation expense, and move towards compliance with the matching principle. While
17 such actions may be viewed as resulting in higher future depreciation expense, the more
18 correct view of such actions is that it places future customers at the same approximate
19 level of depreciation expense that they would have experienced if historical depreciation
20 collection had been in line with current life estimates.

21
22 **Q. DID THE COMMISSION MAKE A MISTAKE WHEN IT ORDERED FPL TO**
23 **AMORTIZE A PORTION OF ITS DEPRECIATION RESERVE SURPLUS**
24 **OVER FOUR YEARS INSTEAD OF OVER THE REMAINING LIVES OF**
25 **PLANT?**

1 A. No. To the contrary, its decision was the appropriate means of addressing and
2 correcting a severe excess reserve imbalance that resulted in intergenerational inequity.

3

4 **Q. WHAT ABOUT THE STATEMENT THAT THE AMORTIZATION IS A**
5 **“DRIVER” OF FPL’S CURRENT RATE CASE PETITION?**

6 A. First, as I said earlier, the increase in rate base that is associated with the amortization is
7 part and parcel of the measure designed to apportion the cost of plant between past and
8 future customers equitably. That said, the amortization is not a “driver” of FPL’s effort
9 to increase base rates at this time.

10

11 **Q. ON WHAT DO YOU BASE THAT STATEMENT?**

12 A. My statement is based on the testimony of OPC witness Donna Ramas, who states that
13 when all of OPC’s adjustments are taken into account, FPL has not demonstrated the
14 need for a base rate increase. Notably, OPC’s adjustments do not disturb the
15 Commission ordered requirement that FPL amortize \$895 million of depreciation
16 reserve over four years. Therefore, it cannot accurately be said that the decision in
17 Docket No. 080677-EI to amortize a portion of depreciation reserve surplus is “driving”
18 an increase in base rates at this time.

19

20 **Q. WHAT ABOUT THE STATEMENT THAT THE DECISION WAS A**
21 **TEMPORARY MEANS OF DEFERRING AN INCREASE IN BASE RATES?**

22 A. First, this statement is a mischaracterization. The decision was a means of correcting a
23 severe imbalance and inequity, not a means of postponing an increase in rates. Indeed,
24 even FPL proposed correction of its excess reserve imbalance, but over a longer period
25 of time. Moreover, the decision led to an annual amortization of \$224 million, when

1 FPL had requested a total increase amounting to more than \$1.2 billion annually. Many
2 other factors—including very substantial adjustments—accounted for a far larger
3 portion of the adjustments that the Commission made to FPL’s request in Docket No.
4 080677-EI. In addition, as I have noted, OPC’s witnesses have demonstrated that no
5 increase in base rates is warranted at this time, despite the fact that the amortization has
6 led to a commensurate and expected increase in rate base. This proves that the question
7 of whether base rates should be increased is always a function of many variables, of
8 which the amortization of depreciation surplus is only one factor.

9
10 **SECTION IV: AMORTIZATION OF SURPLUS DEPRECIATION- 2013 TEST**
11 **YEAR**

12 **Q. WHAT LEVEL OF EXCESS RESERVE AMORTIZATION IS REFLECTED IN**
13 **THE 2013 TEST YEAR IN THIS PROCEEDING?**

14 A. The Company has relied on a combination of actual and forecasted amortizations of the
15 \$895 million surplus reserve for the period 2010 through 2012. The resulting impact of
16 these actual and forecasted amounts yields a claimed remaining \$191 million of
17 amortization, which the Company has included in its 2013 revenue requirement. (See
18 Mr. Barrett’s Direct Testimony at page 26).

19
20 **Q. PLEASE CLARIFY HOW FPL’S PROPOSED TEST YEAR \$191 MILLION**
21 **AMORTIZATION AND THE REFERENCED \$104 MILLION FIGURE**
22 **INTERRELATE.**

23 A. There are two separate revenue requirement components associated with the
24 amortization of the excess depreciation reserve: (1) the amortization itself, which
25 decreases revenue requirements, and (2) the higher rate base due to prior year

1 amortizations, which increases revenue requirements. FPL's claimed \$191 million
 2 remaining amount of excess depreciation reserve amortization reduces the requested
 3 revenue requirement in the 2013 test year. This remaining amount is the projected
 4 balance for the fourth year of the ordered four-year amortization of the \$895 million
 5 excess depreciation reserve. Alternatively, because FPL claims that \$704 million (\$895
 6 million - \$191 million) will have been amortized during the first three years (2010-2012)
 7 of the four-year amortization, the 2013 test year rate base will be higher than it would
 8 have been absent the amortization. Further, since the \$191 million proposed
 9 amortization in 2013 is lower than the average \$224 million amortization assumed in the
 10 last case (\$895 million / 4 years) revenue requirements will be higher. These two
 11 components, as presented by FPL, mathematically increase the 2013 revenue
 12 requirement by \$104 million. The following table identifies FPL claimed change in rate
 13 base.

<u>Year</u>	<u>Basis</u>	<u>Amount (millions)</u>	<u>Weight</u>	<u>Impact (millions)</u>	<u>Cumulative (millions)</u>	<u>Cumulative (w/o 2010 Rate Case)</u>
2010	Rate Case	(\$224)	50%	(\$112)	(\$112)	N/A
2010	Actual	\$4	100%	\$4	(\$108)	\$4
2011	Forecast	\$174	100%	\$174	\$66	\$178
2012	Forecast	\$526	100%	\$526	\$592	\$704
2013	Forecast	\$191	50%	\$95	\$687	\$799

15 (See Exhibit REB-8).

16
 17 **Q. HOW DOES THE ABOVE NOTED CHANGE IN RATE BASE AND THE**
 18 **CHANGE IN ANNUAL AMORTIZATION AMOUNT PRODUCE A \$104**
 19 **MILLION INCREASE IN 2013 REVENUE REQUIREMENTS?**

1 A. First, I wish to stress that this \$104 million amount is a point of information rather than
2 an important item that impacts revenue requirements. For reasons I will describe, the
3 important value in this portion of the case is the amount of depreciation reserve
4 amortization in the 2013 test year, which FPL claims to be \$191 million.

5
6 Also, I will note that an increase in revenue requirements associated with the
7 amortization does not mean that FPL's rates necessarily must increase by that amount—
8 *or by any amount*. In fact, as I have said, OPC's witnesses sponsor adjustments that
9 offset FPL's proposed increase completely. However, I will describe the math
10 underlying FPL's \$104 million number. As noted by Mr. Barrett at page 26 of his
11 Direct Testimony, there is a \$71 million revenue requirement impact associated with the
12 estimated higher rate base due to the amortization of all but the FPL-identified amount
13 of \$191 million of the excess reserve. The \$71 million revenue requirement impact is
14 based on the claimed \$799 million of actual and forecasted excess reserve amortization
15 during 2010 through 2013 less the \$112 million rate base level already reflected in
16 current rate. As noted in the table above, the cumulative net change in rate base between
17 the test years in the prior and current case is \$687 million. When FPL's requested 10.3%
18 pre-tax rate of return is applied to the net rate base increase of \$687 million (\$799
19 million - \$112 million) a \$71 million revenue requirement results. However, OPC's
20 witnesses are testifying that major adjustments to FPL's requested capital structure and
21 return on equity should be made. To the extent these adjustments are accepted in whole
22 or in part, they will reduce the \$71 million impact. Next, the difference between the
23 average expected \$224 million ($\$895 \text{ million} / 4 \text{ years}$) annual excess depreciation
24 reserve amortization and the 2013 remaining \$191 million ($\$895 \text{ million} - \704 million
25 through 2012) level projected by the Company further increases revenue requirements

1 by an additional \$33 million (\$224 million - \$191 million). (See Mr. Barrett's Direct
2 Testimony at pages 26-27). The combination of the \$71 million and \$33 million
3 amounts total \$104 million.

4
5 **Q. IS AN INCREASE IN THE CURRENT RATE PROCEEDING REVENUE**
6 **REQUIREMENTS RELATING TO PRIOR PERIOD EXCESS RESERVE**
7 **AMORTIZATION TO BE EXPECTED?**

8 A. Yes, as I explained earlier, the amortization of excess reserve does increase future
9 revenue requirements, all other things remaining equal. However, all things do not
10 remain equal. FPL has historically over collected depreciation expense based on current
11 life and net salvage estimates. In order to comply with the matching principle and
12 address the concept of intergenerational inequity that had occurred over time, the
13 Commission recognized the existence of a material excess depreciation reserve
14 imbalance in FPL's last rate case. (See Order No. PSC-10-0153-FOF-EI at page 83). In
15 ordering the amortization of the excess depreciation reserve over a four-year period, the
16 Commission noted that:

17 If the reserve surplus is reduced, the depreciation reserve will increase
18 [decrease], thereby, all things remaining equal, causing depreciation rates
19 and future revenue requirements to naturally increase. (See Order No.
20 PSC-10-0153-FOF-EI at page 83).

21
22 **Q. IS THERE ANYTHING SURPRISING ABOUT THE COMMISSION'S PRIOR**
23 **ACTION AS IT RELATES TO THE AMORTIZATION OF MATERIAL**
24 **EXCESS DEPRECIATION RESERVES?**

1 A. No. Indeed, all parties have previously agreed to excess depreciation reserve
2 amortizations, whether through settlement or by order of the Commission. FPL agreed
3 in two separate settlements to amortize \$1 billion of excess depreciation reserve between
4 2000 and 2009. While FPL disputed the legitimacy of continuation of the amortization
5 of excess depreciation reserve in its last case, the Commission found that such continued
6 action was appropriate. Therefore, I believe it is appropriate to reinforce the concept
7 adopted by the Commission in previous proceedings to eliminate material levels of
8 depreciation reserve imbalances over periods shorter than the remaining life of the assets
9 at issue, while always being cognizant of overall Company financial considerations.
10 This process simply attempts to place future customers in the position they should be in
11 based on current life and net salvage values.

12
13 **Q. IS IT POSSIBLE THAT A FURTHER AMORTIZATION OF EXCESS**
14 **RESERVE DEFICIENCY MAY BE WARRANTED IN FPL'S NEXT BASE**
15 **RATE CASE?**

16 A. Yes. As service lives lengthen, the amount of capital recovery that is needed to adhere
17 to the matching principle in a given year decreases. If depreciation rates remain
18 unchanged as the lives increase, the utility will overcollect depreciation expense. In
19 general, the life expectancy of utility property has increased over the past many decades.
20 It does not matter whether the increase in life expectancy is a function of better
21 operation and maintenance practices, better materials, better installation practices or for
22 that matter, more historic information upon which to draw better statistical results. It is
23 reasonable to expect that possible longer service lives will be proposed by the Company
24 and found appropriate by the Commission in FPL's next rate case. Indeed, in the last
25 proceeding, I recommended longer average service lives and less negative levels of net

1 salvage for many plant accounts. If those mortality characteristics continue to be
2 accurate, it would result in the quantification of even higher levels of surplus
3 depreciation reserves in FPL's next rate proceeding. In other words, the rapid
4 amortization of material depreciation reserve imbalances as historically practiced by the
5 Commission and specifically impacting FPL for more than a decade, is an appropriate
6 ratemaking mechanism to counter the impacts of material levels of intergenerational
7 inequities that may continue to exist in the future.

8
9 **SECTION V: TERMINATION OF AMORTIZATION OF SURPLUS**
10 **DEPRECIATION**

11 **Q. THE COMPANY INCLUDED \$191 MILLION OF DEPRECIATION RESERVE**
12 **AMORTIZATION IN TEST PERIOD REVENUE REQUIREMENTS IN THIS**
13 **CASE. HOW SHOULD THE SUBJECT OF DEPRECIATION RESERVE**
14 **SURPLUS BE TREATED AFTER THE 2013 TEST YEAR?**

15 A. The Commission ordered the amortization of \$895 million of excess depreciation
16 reserve to be completed over a four-year period. The four-year period ends in 2013.
17 FPL elected to present its best estimate of the remaining amortization due in 2013 at
18 \$191 million. The level of the 2013 remaining depreciation reserve amortization is a
19 direct function of the 2010 Rate Settlement Agreement. In this case, the Commission
20 will decide whether the \$191 million amount or some other amount is the appropriate
21 completion of the previously ordered \$895 million four-year amortization. It is my
22 strong opinion that no further amortization should be recognized beginning in 2014
23 without the benefit of a rate case review. In other words, all parties will have completed
24 their obligations under the Commission's order in FPL's last rate proceeding and the
25 2010 Rate Settlement Agreement by the end of the 2013 test year.

1

2 **Q. WHEN IS FPL'S NEXT DEPRECIATION STUDY SCHEDULED TO BE**
3 **COMPLETED?**

4 A. FPL states that its next depreciation study is scheduled for March 2013. Therefore, the
5 results of that study cannot be factored into the revenue requirements in this case.

6

7 **Q. IF THE AMORTIZATION OF EXCESS DEPRECIATION RESERVE IS TO BE**
8 **TERMINATED AS OF THE END OF 2013, WILL SUCH ACTION HAVE AN**
9 **IMPACT IN 2014?**

10 A. Yes. Whatever the necessary revenue requirements in 2014 might ultimately be, it
11 should not reflect an impact of a separate excess depreciation reserve amortization
12 unless such amortization is ordered by the Commission in a subsequent base rate case.
13 The culmination of the various impacts due to the Commission last rate case order and
14 the 2010 Rate Settlement Agreement should revert back to the normal overall interaction
15 of expenses, return and revenues for the Company. To the extent the Company, the
16 Commission, or an affected party determines that the interaction of all factors, including
17 the elimination of excess depreciation reserve amortization, result in the need for a rate
18 case (whether to increase or decrease rates) in 2014, that is a decision to be determined
19 at that time. Part of that determination undoubtedly will be the termination of the
20 amortization of excess depreciation reserve and the results of the depreciation study to
21 be completed next year.

22

23 **Q. IS THERE AN IDENTIFIABLE O&M EXPENSE THAT WILL HAVE AN**
24 **IMPACT ON 2014 AND 2015 REVENUE REQUIREMENTS THAT IS NOT**
25 **REFLECTED IN FPL'S 2013 REVENUE REQUIREMENTS?**

1 A. Yes. It is my understanding that FPL is in the process of converting to smart meters.
2 There are sizable O&M savings that will transpire subsequent to the meter change outs.
3 (See response to Staff's 4th ROG 146). If the \$191 million reserve amortization were to
4 be allowed to continue after 2013 without proper recognition of all other revenue
5 requirement changes in 2014 and thereafter in a subsequent base rate case, FPL would
6 be able to capture the O&M expense reductions associated with smart meters as
7 additional bottom line return while increasing rate base for the continued excess reserve
8 amortization. Such a process would unjustly enrich FPL's shareholders and
9 inappropriately punish customers.

10
11 This potential unjust rate treatment is demonstrated by the following illustrative
12 example. Assume that FPL would not need a base rate change in 2014 if there were to
13 be an incremental \$191 million of annual O&M savings due to smart meter installation
14 and the \$191 million annual excess reserve amortization was terminated. In other
15 words, revenue requirements would increase due to the termination of the reserves
16 amortization, but would be fully offset by the equal level of new O&M expense
17 reduction. Moreover, since the reserve amortization would be terminated, there would
18 be no rate base related increase on an annual basis. Alternatively, assume that FPL were
19 allowed to continue the reserve amortization in 2014, still realized the smart meter
20 related O&M expense savings and elected not to seek a base rate reduction. Under this
21 scenario, FPL would both increase rate base by \$191 million annually due to the
22 continued amortization as well as retain the \$191 million of O&M expense reduction
23 due to smart meter operations. The smart meter related O&M savings would become
24 additional return for the benefit of shareholders. In my opinion, the alternative does not
25 constitute appropriate ratemaking and should not be allowed.

1

2 **Q. IS IT NECESSARY FOR THE COMMISSION SPECIFICALLY TO ADDRESS**
3 **THE TERMINATION OF THE AMORTIZATION OF EXCESS RESERVE**
4 **ISSUE IN THIS CASE?**

5 A. Yes. It is necessary to address this issue now, so that no party can claim in a future rate
6 proceeding that it was always the intention to continue the recording of the \$191 million
7 of excess depreciation reserve amortization past the 2013 test year. Clear and certain
8 direction on this matter removes any ambiguity that any party can claim in a subsequent
9 rate proceeding. Any specific action regarding material reserve imbalances that may
10 exist in 2014 or thereafter should be determined based on the best available information
11 at that time. In my opinion, the termination of the excess depreciation reserve
12 amortization at the end of 2013 represents the most equitable position to be taken on this
13 matter, so that all parties may have certainty and make informed decisions based on
14 facts that are not in existence today. Indeed, the \$191 million amount proposed by the
15 Company is but an estimate, and for that matter any adjusted amount recommended by
16 any other party, including OPC, would still represent an amount which, as the Company
17 states, "no one can predict." (See Mr. Ousdahl's Direct Testimony at page 22, lines 19-
18 20). Future determination of depreciation reserve imbalances and the accelerated
19 treatment of any of such amounts should be determined in future rate proceedings based
20 on the facts as known at that time.

21

22 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

23 A. The Commission determined that FPL was in a material excess depreciation reserve
24 position in FPL's last rate proceeding. The Commission took corrective action to
25 eliminate such significant levels of intergenerational inequity through the amortization

1 of the excess depreciation reserve over a four-year period. The Commission took such
2 action in full recognition that such action would result in a higher level of rate base in
3 future rate proceedings, but at a level approximately equal to where it would have been,
4 had FPL's capital recovery been based on current life and net salvage expectations. This
5 situation is only logical and appropriate given that the Company had previously over
6 collected depreciation expense in relationship to current mortality characteristics for its
7 various plant accounts. In other words, if the Company is entitled to recover 100% of its
8 investment through depreciation and it over collects early in the life cycle of plant, then
9 the remaining life depreciation calculation as utilized by FPL and the Commission
10 requires a deceleration of depreciation recovery in the future. However, if material
11 excess levels of intergenerational inequity are eliminated through amortization periods
12 shorter than the remaining life of the investment at issue, then the actual depreciation
13 rates for each of the various plant accounts will have to increase to allow the Company
14 to recover the level of surplus depreciation it has amortized during prior periods. This is
15 the only way to reasonably balance the material overpayment of depreciation expense
16 associated with historical and current customers with the benefits that those customers
17 received and the benefits that future customers are expected to receive from the same
18 plant. The more rapid amortization of material depreciation reserve imbalances
19 represents an appropriate and desired compliance with the matching principle as
20 recognized by the Commission in its last order for FPL. (See order No. PSC-10-01153-
21 FOF-EI at page 82, footnote 25).

22
23 Simply put, necessary and appropriate actions were taken by the Commission in
24 amortizing the material excess depreciation reserve recognized in the last rate
25 proceeding. The revenue requirement in current and future rate proceedings will be

1 higher than they would be otherwise due to this corrective action, but at a level
2 approximately equal to where it should be based on current life and net salvage
3 expectations. Finally, the Commission should explicitly direct FPL to terminate the
4 amortization of depreciation reserve as of the end of 2013, which is the end of the four-
5 year period prescribed in FPL's last rate case order. Any future amortization of
6 depreciation reserve imbalances should be established after a thorough review and
7 analysis in a future rate case, including reliance on future depreciation studies. Such
8 determination is the only appropriate culmination of the Commission's order on this
9 matter as set in FPL's last rate case.

10

11 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

12 A. Yes, however to the extent I have not addressed an issue, method, practice, etc. proposed
13 by FPL, it should not be taken that I am in agreement with such issue, method, practice,
14 etc.

1 BY MR. MCGLOTHLIN:

2 Q And did you prepare an exhibit to your
3 testimony, Mr. Pous?

4 A An appendix.

5 Q Only an appendix? You're getting off light
6 in this case, aren't you?

7 A Very light.

8 Q Have you prepared a summary of your
9 testimony?

10 A Yes, I have.

11 Q Please summarize your testimony for the
12 Commissioners.

13 A Thank you.

14 FP&L claims that the 2010 decision of the
15 Commission to require FP&L to amortize 894 million of
16 depreciation reserve surplus over four years was a
17 temporary means of postponing a rate increase. This is
18 a mischaracterization of that important policy
19 decision. The decision was necessary to treat present
20 and future customers fairly.

21 The objective of depreciation is to recover
22 plant costs over the lives of the related assets so
23 that each generation of customers pays its fair share.
24 This is called the matching principle.

25 A utility recovers its investments in plant

1 through depreciation expense, which is built into base
2 rates. Depreciation studies are performed periodically
3 to measure whether the depreciation rates are
4 performing in a way that satisfies the matching
5 principle. If an imbalance, over-correction or
6 under-correction is detected, corrective action is
7 taken.

8 When a utility amortizes a depreciation
9 reserve surplus, the accounting entry is to reduce the
10 depreciation reserve that is an offset to the original
11 plant balance and so that the effect is to increase
12 rate base by the amount being amortized.

13 Similarly, correcting an under-recovery will
14 increase depreciation expense, add to the depreciation
15 reserve and reduce rate base. Usually it is sufficient
16 to roll the over or under-correction into the amount of
17 undepreciated plant cost to be collected in the future
18 and design new depreciation rates that will again
19 recover the investment over the remaining life of the
20 assets. An imbalance can be so severe that the usual
21 treatment is inadequate to achieve fairness.

22 In the last rate case, which was consolidated
23 with FP&L's concurrent depreciation study, the
24 Commission concluded that FP&L had a depreciation
25 reserve surplus of about \$1.2 billion. In other words,

1 in recovering cost of plant, FP&L was ahead of schedule
2 by 1.2 billion. This represented a severe inequity in
3 that past and then current customers had been burdened
4 with \$1.2 million more than their fair share and future
5 customers would benefit unfairly by paying 1.2 billion
6 less than their fair share.

7 To address this severe generation inequity in
8 a way that would be meaningful, the Commission required
9 FP&L to amortize 894 million of reserve surplus over
10 four years instead of the 18-year remaining life. The
11 amount of the amortization included in the test year in
12 the last case lowered FP&L's revenue requirements and
13 so appropriately benefited customers. But the purpose
14 was to address an inequity, not temporarily reduce
15 rates.

16 FP&L states that the decision had the effect
17 of increasing rate base in this case. But what FP&L
18 does not say is that rate base resulting at the end of
19 the four-year amortization period will be at the level
20 where it should have been if in the past FP&L had
21 applied depreciation rates that had been collected --
22 that would have collected the amount of expense
23 appropriate to satisfy the matching principle and to
24 achieve equity between generations of customers.

25 FP&L also claims that the 2010 reserve

1 surplus decision is a driver of its current rate case.
2 An increase in depreciation expense doesn't necessarily
3 mean a corresponding base rate increase. As the
4 Commission knows, a utility's revenue requirements are
5 a result of the interplay of many variables.

6 OPC's adjustments in this case do not disturb
7 the implementation of the four-year amortization
8 decision. Yet Donna Ramas' exhibits show that FP&L has
9 an overall revenue surplus, not a revenue deficiency.

10 Finally, as of the end of 2013, FP&L should
11 cease the booking of any excess reserve amortization
12 unless specifically ordered by the Commission to
13 implement new reserve amortizations. The prior
14 Commission order on reserve amortization was for the
15 period 2010 through 2013. In this case, FP&L proposes
16 to amortize 191 million in 2013.

17 OPC witnesses assert it should be that
18 \$40 million higher. Whatever the Commission determines
19 is the final amount for 2013, FP&L must cease the
20 booking of any reserve amortization beginning in 2014.

21 The usual relationship should govern until
22 the Commission reviews FP&L's next depreciation study
23 and reflects any changes in future base rates. That
24 concludes my statement.

25 MR. McGLOTHLIN: Mr. Pous is available for

1 cross-examination.

2 CHAIRMAN BRISE: Mr. Lavia.

3 MR. LAVIA: No questions, Mr. Chairman.

4 CHAIRMAN BRISE: Mr. Saporito.

5 MR. SAPORITO: No questions, Mr. Chairman.

6 CHAIRMAN BRISE: Mr. Wiseman.

7 MR. WISEMAN: No questions.

8 CHAIRMAN BRISE: Mr. Moyle.

9 MR. MOYLE: Just a couple.

10 CROSS-EXAMINATION

11 BY MR. MOYLE:

12 **Q In your opening statement, you had remarked**
13 **that at the last rate case the depreciation study was**
14 **consolidated with the rate case, correct?**

15 A Correct.

16 **Q And you would agree there's interplay between**
17 **depreciation and base rates, correct?**

18 A Absolutely.

19 **Q Okay. Do you believe as a matter of policy**
20 **that to the extent that depreciation studies can be**
21 **combined with rate cases, that that is a good thing --**

22 A I think it's --

23 **Q -- because of the interplay?**

24 A I think it is appropriate that they be
25 combined.

1 MR. MOYLE: That's all I have. Thank you.

2 CHAIRMAN BRISE: Thank you, Mr. Moyle.

3 Captain Miller.

4 CAPTAIN MILLER: No questions. Thank you.

5 CHAIRMAN BRISE: Mr. Butler.

6 MR. BUTLER: No questions for FPL.

7 CHAIRMAN BRISE: All right. Staff.

8 MS. BROWN: No questions.

9 CHAIRMAN BRISE: Commissioners.

10 (No response.)

11 CHAIRMAN BRISE: All right. Redirect.

12 MR. MCGLOTHLIN: I'm hard-pressed to find a
13 question. No redirect.

14 CHAIRMAN BRISE: All right. At this time,
15 we'll deal with exhibits.

16 MR. MCGLOTHLIN: OPC moves 254, which is the
17 appendix to Mr. Pous' testimony.

18 CHAIRMAN BRISE: Any objections to
19 Exhibit 254?

20 (No response.)

21 CHAIRMAN BRISE: All right. Seeing none, we
22 will move 254 into the record.

23 (Exhibit No. 254 received in evidence.)

24 CHAIRMAN BRISE: Thank you very much.

25 THE WITNESS: Thank you very much.

1 CHAIRMAN BRISE: And I believe you may be
2 excused.

3 Mr. McGlothlin.

4 MR. MCGLOTHLIN: We're going to change
5 counsel now. Could we have just one minute in
6 place for that, Mr. Chairman?

7 CHAIRMAN BRISE: Sure.

8 MR. MCGLOTHLIN: We're having a changing of
9 the guard here.

10 CHAIRMAN BRISE: Okay.

11 MS. CHRISTENSEN: Thank you. The witness
12 that OPC would like to call is Mr. David Vondle.

13 CHAIRMAN BRISE: All right.

14 MS. CHRISTENSEN: I think we're ready.

15 CHAIRMAN BRISE: Sure. Go right ahead.

16 Thereupon,

17 DAVID VONDLE

18 was called as a witness, having been first duly sworn,
19 was examined and testified as follows:

20 DIRECT EXAMINATION

21 BY MS. CHRISTENSEN:

22 **Q Can you please state your name and business**
23 **address for the record.**

24 A My name is David Vondle, 4926 Calle De Tierra
25 Northeast, Albuquerque, New Mexico.

1 **Q And did you cause to be filed prefiled direct**
2 **testimony consisting of 37 pages in this docket?**

3 A I did.

4 **Q And do you have any corrections to your**
5 **testimony?**

6 A I do not.

7 **Q You do or do not?**

8 A Do not.

9 **Q Okay. And if I were to ask you the same**
10 **questions today, would your answers be the same?**

11 A Yes.

12 MS. CHRISTENSEN: I would ask that the
13 testimony of Mr. Vondle be entered into the record
14 as though read.

15 CHAIRMAN BRISE: Okay. We will enter
16 Mr. Vondle's direct testimony into the record as
17 though read, seeing no objection.

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DIRECT TESTIMONY

Of

DAVID P. VONDLE, CMC

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

Docket No. 120015-EI

I. BACKGROUND

A. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is David P. Vondle. My business address is 4926 Calle de Tierra, NE, Albuquerque, NM 87111.

Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR POSITION?

A. I am President of Vondle & Associates, Inc.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE.

A. I received a Bachelor of Science degree in Industrial Management from the University of Akron and a Masters of Business Administration degree from Southern Methodist University. I have been a management consultant for over thirty years, working mostly in the public utility industry. I have been designated a Certified

1 Management Consultant (CMC) by the Institute of Management Consultants (IMC)
2 USA. IMC USA is the certifying body for the Certified Management Consultant™
3 (CMC®) designation. The CMC certification process confirms the CMC's education,
4 continuing professional development and commitment to the highest ethical
5 standards, and the IMC USA examiners rigorously assess the CMC's consulting
6 engagements and competence to apply the knowledge and skills defined in IMC
7 USA's Competency Framework and Certification Scheme for Certified Management
8 Consultants.

9 I started working in affiliate relationships and transactions in 1981 when I led
10 the Cross-Sectional Purchasing Study of Four Florida Telephone Companies for the
11 Florida Public Service Commission (FPSC or Commission). That study led to my
12 testifying in the AT&T anti-trust trial. I have continued to work on affiliate
13 relationships and transactions through management audits of affiliate relationships for
14 state regulatory commissions, assistance to utilities in complying with affiliate rules,
15 and litigation support and expert witness services for law firms, attorneys general and
16 public advocates in court and regulatory cases.

17
18 **Q. HAVE YOU EVER PROVIDED EXPERT TESTIMONY BEFORE A**
19 **REGULATORY AGENCY OR BODY?**

20 **A.** Yes. I have testified on affiliate relationship and transaction topics several times in
21 U.S. and state district courts and before several state public utility commissions in
22 Alaska, California, Connecticut, Massachusetts, Maine, and New Mexico. I have also
23 testified on capital programs, staffing and costs. I have attached my résumé as
24 Exhibit DPV-1, which includes a list of my expert testimonies.

25 In 1981, I testified before the FPSC about a management consulting study I

1 led for the Commission regarding contributions-in-aid-of-construction for water and
2 wastewater utilities.

3

4 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS DOCKET?**

5 A. The purpose of my testimony in this docket is to review Florida Power & Light's
6 (FPL's) affiliate relationships and transactions in relation to the FPSC's rules and
7 precedents. I raise several concerns regarding FPL's current affiliate relationships
8 and transactions and propose alternative structures and methodologies. Lastly, based
9 on my findings, I make recommendations on adjustments to FPL's affiliate charges.

10

11 **B. REGULATORY STANDARD**

12 **Q. WHAT IS THE REGULATORY STANDARD FOR AFFILIATE**
13 **RELATIONSHIPS AND TRANSACTIONS IN FLORIDA?**

14 A. The foundation for Florida's regulatory standard for affiliate relationships and
15 transactions is Section 366.05(9), Florida Statutes, which stands for the
16 proposition that FPL's Florida ratepayers should not be used to subsidize
17 nonutility affiliate activities. Specifically, Section 366.05(9) states, in part, that
18 "[t]he commission may also require such reports or other data necessary to
19 **ensure that a utility's ratepayers do not subsidize nonutility activities.**"
20 (Emphasis added).

21 The Commission established the standard for evaluating affiliate
22 relationships and transactions in Rule 25-6.1351, F.A.C., Cost Allocation and
23 Affiliate Transactions, (affiliate transaction rule or Rule) which I have attached
24 as Exhibit DPV-2.

1 Q. CAN YOU SUMMARIZE THIS RULE?

2 A. Yes. The rule applies to transactions between a utility and its affiliates, and
3 also a utility's unregulated activities, with the intent that these affiliate and
4 nonregulated transactions and activities not be subsidized by utility ratepayers.
5 (Rule section 1) Some of the key points regarding the rule's applicability to
6 FPL in this case are:

- 7 • Substantially all entities under the NextEra Energy, Inc. (NEE) corporate
8 umbrella are, by rule definition, FPL affiliates. Rule section 2(a)
- 9 • FPL must charge affiliates the higher of fully allocated cost or market price,
10 and affiliates must charge FPL the lower of fully allocated cost or market
11 price for non-tariffed products and services under most circumstances
12 (asymmetrical cost allocation). Rule sections 3(b) and 3(c)
- 13 • FPL accounting records must show whether each transaction involves a
14 product or service that is regulated or nonregulated. Rule section 4(a)
- 15 • Direct costs shall be assigned to each non-tariffed service and product
16 provided by FPL. Rule section 4(b)

17 Q. IS THERE A RELEVANT COMMISSION ORDER AS WELL?

18 A. Yes. In Order No. PSC-01-1374-PAA-WS, issued June 27, 2001, in Dockets
19 Nos. 000737-WS and 010518-WS, the Commission stated:

20
21 By their very nature, related party transactions require closer scrutiny.
22 Although a transaction between related parties is not per se unreasonable, it is
23 the utility's burden to prove that its costs are reasonable. Florida Power Corp.
24 v. Cresse, 413 So. 2d 1187, 1191 (Fla. 1982). This burden is even greater when
25 the transaction is between related parties. In GTE Florida, Inc. v. Deason, 642
26 So. 2d 545 (Fla. 1994) (GTE), the Court established that the standard to use in
27 evaluating affiliate transactions is whether those transactions exceed the going
28 market rate or are otherwise inherently unfair.

1 Order No. PSC-01-1374-PAA-WS at p. 15.

2

3 **Q. HOW SHOULD THE REGULATORY STANDARD BE APPLIED FOR**
4 **AFFILIATE TRANSACTIONS?**

5 A. The utility bears the burden of proof to ensure that its transactions with
6 affiliates are fair, that they are priced appropriately at market price or fully
7 allocated cost, and that they do not disadvantage the ratepayer. In addition, the
8 utility must account for affiliate transactions in a detailed, prescribed manner
9 and allocate costs according to the rule. If the utility does not meet its burden
10 of proof or does not comply with the affiliate accounting and allocation rules,
11 the affiliate charge should not be allowed.

12

13 **C. IMPORTANCE OF AFFILIATE RELATIONSHIPS AND CHARGES**

14 **Q. CAN YOU EXPLAIN WHY AFFILIATE RELATIONSHIPS AND**
15 **CHARGES ARE IMPORTANT IN REGULATING PUBLIC**
16 **UTILITIES?**

17 A. Yes. Under traditional utility ratemaking, such as in this case, the utility's rates
18 are set based upon a determination of its revenue requirement. The higher the
19 allowed costs are, the higher its overall revenue requirement; and, hence, its
20 rates and future revenue. With affiliate relationships, there is an opportunity
21 for a company to allocate common or shared costs between a regulated utility,
22 which recovers its allowed costs in regulated rates, and unregulated affiliates
23 that have no limit on revenues and profits. Therefore, there is a strong financial

1 incentive for companies to allocate more costs to a regulated utility to increase
2 its revenue requirement and rates and to allocate fewer costs to unregulated
3 affiliates to increase their profits. Essentially, every extra dollar of common
4 cost that is allowed to be charged to a utility results in another dollar of revenue
5 to the utility; and, every dollar not charged to an unregulated affiliate results in
6 an additional dollar of profit to that affiliate.

7
8 **Q. WHAT ARE THE TOTAL COSTS THAT ARE SUBJECT TO**
9 **AFFILIATE TRANSACTIONS BETWEEN FPL AND ITS AFFILIATES,**
10 **AND WHAT IS THE POTENTIAL IMPACT OF SUBSIDIZATION BY**
11 **FPL'S CUSTOMERS?**

12 A. I have summarized FPL's projected 2013 affiliate transactions in Exhibit DPV-
13 3. Charges from FPL to affiliates are projected to be \$150.6 million and
14 charges from affiliates to FPL are projected to be \$22.2 million. In my
15 testimony, I will describe how FPL fails to ensure the reasonableness of these
16 amounts and actually uses methods that skew the costs in the direction of FPL
17 and its customers. For the reasons I will detail in my testimony, in light of the
18 lack of adequate support for the charges, I will recommend the Commission
19 disallow 20% of the total for ratemaking purposes. In addition, I will
20 recommend that the Commission open a separate docket for the purpose of
21 establishing procedures and mechanisms that will more closely govern FPL's
22 affiliate relationships and transactions in the future.

1 **D. OVERVIEW OF FPL'S AFFILIATE RELATIONSHIPS**

2 **Q. WHAT ARE FPL'S AFFILIATE RELATIONSHIPS?**

3 A. The FPL MFR Schedule C-30 projects eight FPL affiliate relationships in 2013
4 with:

- 5 • NextEra Energy, Inc. (its parent)
- 6 • NextEra Energy Resources, LLC (the principal unregulated NEE subsidiary)
- 7 • FPL Energy Services, Inc.
- 8 • FPL FiberNet, LLC (one of the other major nonregulated NEE subsidiaries)
- 9 • Palms Insurance Company
- 10 • Lone Star Transmission, LLC (the second other major nonregulated NEE
11 subsidiary)
- 12 • New Hampshire Transmission, LLC
- 13 • NextEra Energy Transmission, LLC

14 However, the FPL MFR Schedule C-30 is somewhat misleading in that,
15 according to the response to OPC Interrogatory No. 165, Attachment 1, there
16 are approximately 238 actual separate affiliate relationships that FPL has
17 chosen to roll-up into the eight reported in Schedule C-30. My reading of the
18 affiliate transaction rule is that FPL must comply with the rule for each
19 individual affiliate relationship -- all 238 that exist.

20

21 **Q. PLEASE DESCRIBE FPL'S CORPORATE STRUCTURE.**

22 A. According to NextEra Energy, Inc.'s (NEE's) and Florida Power & Light's
23 (FPL's) 2011 United States Securities and Exchange Commission Form 10-K,
24 FPL is a wholly owned subsidiary of NEE. NEE is one of the largest electric
25 power companies in North America with over 41,000 megawatts of generating

1 capacity in 24 states in the U.S. and three provinces in Canada, NEE employs
2 approximately 14,800 people. NEE's nonregulated operations are organized
3 under NextEra Energy Capital Holdings, Inc. (NEECH).

4 The principal nonregulated subsidiary under NEECH is NextEra Energy
5 Resources, LLC (NEER). NEER is one of the largest wholesale generators of
6 power in the U.S., with approximately 16,600 megawatts of generating
7 capacity. NEER also provides full energy and capacity requirements services,
8 owns a retail electricity provider serving customers in 13 states and the District
9 of Columbia, and engages in power and gas marketing and trading activities.

10 In addition to NEER, other subsidiaries are organized under NEECH,
11 including FPL FiberNet and Lone Star. FPL FiberNet delivers wholesale and
12 enterprise telecommunications services in Florida and certain parts of the South
13 Central U. S. Lone Star is a rate-regulated transmission provider in Texas. The
14 SEC requires large corporations like NEE to subdivide their operations into
15 "reportable segments." NEE's SEC reportable segments are FPL, NEER and
16 Corporate and Other. The Corporate and Other reportable segment is primarily
17 comprised of interest expense, the operating results of FPL FiberNet, Lone Star
18 and other business activities, as well as corporate interest income and expenses.

19
20 **Q. WHAT IS THE FINANCIAL SCALE OF NEE'S AND FPL'S**
21 **OPERATIONS?**

22 A. In 2011, NEE's operating revenues (including those of subsidiaries) were \$15.3
23 billion, its net income was \$1.9 billion and it had total assets of \$57.2 billion.
24 Of the totals, FPL was responsible for \$10.6 billion in operating revenue
25 (69%), \$1.1 billion in net income (56%), and \$31.8 billion in assets (56%).

1 FPL's \$654 million of 2011 income tax expense accounted for 124% of NEE's
2 2011 income tax expense of \$529 million, as the other two reportable segments,
3 NEER and Corporate and Other, had credits of \$24 million and \$101 million,
4 respectively. FPL's 2011 capital expenditures of \$3.5 billion were 53% of
5 NEE's \$6.6 billion total.

6
7 **Q. DOES FPL HAVE A TYPICAL AFFILIATE STRUCTURE?**

8 A. No. In my experience, utility companies of the scale of NEE and FPL typically
9 have utility operating companies in more than one state and are structured with
10 a separate service company that provides common and shared services to
11 multiple utility operating companies and unregulated companies. By having
12 only one utility operating company (FPL) serving only one state (Florida), NEE
13 has not had to form a service company. Instead, NEE uses FPL, in Witness
14 Ousdahl's term, as its "primary operating entity." That is, FPL combines the
15 functions of a utility operating company and a service company serving
16 unregulated affiliates. FPL provides common and shared services to itself, to
17 its parent and to unregulated affiliates that would typically be provided by a
18 service company in other companies of this scale.

19
20 **Q: PLEASE DESCRIBE HOW FPL ACCOUNTS FOR ITS AFFILIATE**
21 **CHARGES TO AND FROM ITS AFFILIATES.**

22 A. Witness Ousdahl, beginning on page 28 of her direct testimony, describes three
23 methods of charges to affiliates:

- 24 • Direct Charges – Costs of resources used exclusively to provide service for
25 the benefit of one company are directly charged to that company. Direct

1 charges are projected to be \$60.1 million or 40% of the \$150.6 million total
2 charges to affiliates in 2013.

- 3 • Service Fees – Service fees are charged monthly for many of the fleet
4 support operations. There are three current service fees: Nuclear (allocated
5 on number of generating units); Energy, Marketing and Trading (allocated
6 on time studies or specific analyses by function); and, Nuclear Information
7 Management (allocated on number of generating units). Service fees are
8 projected to be \$13.8 million or 9% of affiliate charges in 2013.
- 9 • Affiliate Management Fee (AMF) – for governance costs and general
10 corporate support services. AMF allocations for 2013 are projected to be
11 \$75.6 million, or 50% of affiliate charges.
 - 12 ○ Some are collected in cost pools and allocated on cost drivers, such
13 as number of employees, square feet, and work stations. These
14 charges are estimated by FPL to be 40% of the AMF charges, or
15 \$30.2 million in 2013.
 - 16 ○ Cost pools which do not have identified cost drivers are allocated
17 using FPL's general allocator, the Massachusetts Formula. These
18 charges are estimated by FPL to be 60% of the AMF charges, or
19 \$45.4 million in 2013.

20 In addition, MFR Schedule C-30 lists FPL charges to FPL FiberNet of \$1.2
21 million for pole attachments in 2013.

22 Based on my review, I have inferred that FPL's service fees allocation
23 are a general allocation methodology using the single factor general allocation
24 formula of the relative number of nuclear units. I further surmised that the

1 AMF allocations based on cost drivers and the pole attachment charges are
2 “rate” based allocation methodologies. I construed that the AMF allocations
3 using the Massachusetts Formula are a general allocation methodology.

4 MFR Schedule C-30 lists all charges to FPL from affiliates as direct
5 charges.

6 **II. CONCERNS WITH FPL’S CURRENT AFFILIATE TRANSACTION**

7 **METHODOLOGIES**

8 **A. AFFILIATE STRUCTURE**

9 **Q. DOES THE UNUSUAL NEE/FPL AFFILIATE STRUCTURE YOU**
10 **MENTIONED EARLIER CAUSE CHALLENGES IN DETERMINING**
11 **APPROPRIATE AFFILIATE CHARGES?**

12 **A.** Yes. Service companies have the benefit of being separate legal entities with
13 accounting structures designed to facilitate cost allocation from a central pool
14 to all of the benefitting entities. Common and shared costs are accumulated in
15 cost pools in the service company and then allocated based upon a preferred
16 allocation methodology hierarchy which will be discussed later in my
17 testimony. All service company costs are allocated among the family of
18 benefitting affiliates each year.

19
20 Typically, any employee who regularly serves more than one company
21 on a regular, material basis is a service company employee. As examples, the
22 generation or transmission expert who advises regulated and unregulated
23 operations would be a service company employee and the accountants who do

1 financial accounting for several affiliates would be service company
2 employees.

3 However, in FPL's case, because there is no service company, there is
4 an extra step which complicates accounting for and allocating common and
5 shared costs among the corporate family. In a service company, all costs are
6 allocated to the entities served by the service company. For FPL, costs must
7 first be segregated between its pure utility operating company costs and the
8 common or shared costs that should be allocated among FPL and its affiliates.
9 As mentioned above, NEE/FPL has a strong incentive to classify costs as
10 purely FPL utility operating costs that are not allocated to unregulated
11 affiliates.

12 An example of the complexity of FPL cost allocation is that several
13 executives have dual regulated and unregulated roles. According to the NEE
14 2011 10-K report, page 23, six of the 14 NEE executive officers also have a
15 second role as FPL officers. For example, the Executive Vice President of the
16 NEE Power Generation Division is also the Executive Vice President of the
17 FPL Power Generation Division. In addition, FPL's 2011 Diversification
18 Report lists non-regulated affiliate responsibilities for several of FPL's officers.

19
20 **Q. ARE THERE OTHER STRUCTURAL COMPLICATIONS?**

21 A. Yes. According to OPC Interrogatory No. 3, NEE, NEER and other affiliates
22 are now providing shared common services back to FPL that are typically in a
23 shared services company or, at least, were previously centralized in FPL.

1 These include aviation operations, nuclear, information management, legal, and
2 human resources services. Other affiliates that may be providing what are
3 normally shared common services to FPL include NextEra Energy
4 Infrastructure (transmission, finance, and regulatory affairs), FPL Energy
5 Services (customer service and energy marketing and trading), and Lone Star
6 Transmission (transmission and general counsel). These affiliates have an
7 incentive to charge a disproportionate amount of their costs to FPL.
8

9 **Q. IS THERE AN ALTERNATIVE TO THE FORMATION OF A SEPARATE**
10 **SERVICE COMPANY?**

11 A. Yes. With sophisticated accounting software systems, it is possible for a
12 regulated utility to create a “virtual service company” capable of accomplishing
13 many of the functions of a separate corporate entity. However, just doing this
14 within FPL would not address the common support services provided to FPL
15 by affiliates.
16

17 **Q. DOES FPL HAVE THE ABILITY TO IMPLEMENT VIRTUAL SERVICE**
18 **COMPANIES?**

19 A. Yes. According to FPL witness Ousdahl, FPL recently underwent a conversion
20 to a new accounting software program called SAP. It is my understanding that
21 the SAP system has the capability to allow FPL and the affiliates who charge
22 FPL to assign employees who work for multiple affiliates to a “virtual” service
23 company established as a division or department within the entity. While not

1 as attractive as establishing a real legal entity service company for all of NEE,
2 establishing virtual service companies within FPL and each affiliate charging
3 FPL would improve the transparency of affiliate transactions.
4

5 **B. COST ALLOCATION METHODOLOGIES – FPL TO AFFILIATES**

6 **Q. HOW ARE FPL'S COSTS ALLOCATED TO AFFILIATES?**

7 A. MFR Schedule C-30, as summarized in my Exhibit DPV-3, shows that the fully
8 allocated cost of affiliate charges of \$150.6 million in 2013 will be allocated to
9 affiliates by the following methods: 40% by direct charges; 9% by service fees;
10 1% by pole attachment charges to FPL FiberNet; and 50% by Affiliate
11 Management Fee (AMF). Direct charges include simple convenience payments
12 made on behalf of affiliates by FPL. FPL does not follow the normal practice
13 of reporting which charges are convenience payments and the portion of the
14 costs that is allocated by direct charges of FPL employee time.

15 FPL also has an unusual practice of combining charges made by rates
16 (per employee, per square foot, etc.) and by the Massachusetts Formula general
17 allocator under the AMF category. This disguises the amount allocated using
18 the general allocator. However, FPL estimates that 60% of the AMF, or about
19 \$45.4 million, is allocated with the Massachusetts Formula in 2013.
20

21 **Q. HOW ARE FULLY ALLOCATED COSTS DETERMINED?**

22 A. The cost accounting to determine the total cost for a cost pool for a product or
23 service is fairly straightforward. The direct costs are collected in each cost pool

1 and appropriate overheads are then applied to determine the total fully loaded
2 cost for a cost pool or direct charge for a particular product or service. The
3 challenge is to allocate those costs among FPL and the affiliates in an equitable
4 manner.

5

6 **Q. ARE THERE PREFERRED METHODS TO ALLOCATE COSTS?**

7 A. Yes. The basic principle is to attach cost to the cause of the cost as precisely as
8 possible. For utility and affiliate cost allocations, there is a generally accepted
9 hierarchy of preferred cost allocation methodologies. The hierarchy, from most
10 preferred to least preferred, is:

11 **Direct charges whenever possible.** That is, the cost, in the finest granularity
12 practical, is charged directly to the entity causing the cost. For example, if an
13 invoice from a third party vendor is paid by FPL on behalf of an affiliate (a
14 “convenience payment”), that full cost should be charged to the affiliate.
15 Likewise, if an FPL engineer works on a project for an affiliate, the fully
16 allocated cost of each hour spent on that project should be charged directly to
17 that affiliate.

18 **Charge rates linked to cost drivers applied to all allocation recipients**
19 **equally.** This technique is appropriate when the costs cannot be directly
20 assigned to a benefitting entity, but a pool of costs can be allocated on a simple
21 cost driver. This is appropriate for things like shared office space in which all
22 the fully allocated costs associated with having the office are accumulated in a
23 cost pool and then are allocated to the office tenants on an occupied square
24 footage basis.

1 **General allocator.** This is the least preferred allocation method and should be
2 used sparingly. This method only applies when neither direct charges nor
3 acceptable cost drivers can be identified. Costs that fall in this category are
4 allocated based upon one or more general allocation factors like sales, assets or
5 growth rates determined to be fair to all recipients. Because of the incentive to
6 overcharge regulated utilities and undercharge unregulated affiliates, great care
7 must be taken to select a general allocation formula that is clearly fair to the
8 utility.

9
10 **Q. DOES FPL USE THE PREFERRED HIERARCHY OF COST**
11 **ALLOCATION METHODOLOGIES?**

12 A. No. FPL under-utilizes positive time reporting for direct charges and cost
13 pools, and over-utilizes the general allocator. Also, the general allocator FPL
14 has chosen, the Massachusetts Formula, is inappropriate for a steady, regulated
15 utility with growing unregulated affiliates. Each of these deficiencies is
16 discussed below.

17
18 **C. POSITIVE TIME REPORTING**

19 **Q. WHAT IS POSITIVE TIME REPORTING?**

20 A. Positive time reporting charges each employee work hour to a specific client,
21 work order or activity. It is the standard way for private attorneys, public
22 accountants, consulting engineers, management consultants and other
23 professionals to charge their clients for hourly services. It is also the most
24 accurate way for FPL employees providing services to FPL and affiliates to
25 account for their time and allocate their costs.

1 **Q. WHAT IS THE ALTERNATIVE TO POSITIVE TIME REPORTING?**

2 A. Fixed time allocations with exception reporting is the principal alternative to
3 positive time reporting. With fixed time allocations, employees' time is
4 allocated among work orders or activities the same way each reporting period,
5 usually based on estimates or time studies of how time would be spent.

6 Exception reporting requires a fixed time allocation employee first to
7 identify that he or she is spending time differently than the fixed allocation and
8 then to take the initiative to report an exception in the time reporting system.
9 Fixed allocations are less accurate than real-time positive time reporting of how
10 time is actually spent. Exception reporting is highly suspect in its ability to
11 identify differences from the fixed allocation and to actually report the
12 exception in the time keeping system.

13

14 **Q. DOES FPL USE POSITIVE TIME REPORTING APPROPRIATELY?**

15 A. No. The response to OPC Interrogatory No. 8 says, "[f]ixed employees use
16 exception reporting and variable employees use positive time reporting." The
17 response to OPC Interrogatory No. 157 says, "[p]ositive time reporting is used
18 by either non-exempt or bargaining unit employees. Exception reporting is
19 used only by exempt employees." All of the professional services employees –
20 engineers, accountants, IT specialists, and so on – who are typically exempt
21 employees do not use the more accurate positive time reporting methodology.

22

23 **D. MASSACHUSETTS FORMULA**

24 **Q. WHAT IS THE MASSACHUSETTS FORMULA AND HOW IS IT**
25 **APPLIED?**

1 A. The Massachusetts Formula is a size driven allocation methodology. The
2 Massachusetts Formula is based on the relative amounts of the simple average
3 of property, plant, and equipment (assets); revenue; and, payroll among FPL
4 and its affiliates. Electric utilities are asset and employee intensive enterprises
5 with high revenues. The response to OPC production of documents (POD) No.
6 11 shows the calculations for the 2012 Massachusetts Formula allocations.
7 According to Exhibit KO-13, the Massachusetts Formula allocations of
8 approximately \$45.6 million for 2013 are 64% to FPL, 33.82% to NEER, and
9 only 2.18% to all other affiliates.

10

11 **Q. IS FPL'S MULTIFACTOR GENERAL ALLOCATION**
12 **METHODOLOGY APPROPRIATE?**

13 A. No, for two important reasons. First, as mentioned above, the preferred
14 methodologies of direct charges and rates are underutilized, making the
15 strongly less-preferred multi-factor allocation methodology over-used. This
16 over-use compounds the second problem, which is that the Massachusetts
17 Formula selected by FPL as its general allocator is biased in the direction of
18 overcharging FPL and undercharging unregulated affiliates.

19

20 **Q. WHAT IS WRONG ABOUT FPL'S USE OF THE MASSACHUSETTS**
21 **FORMULA FOR ITS GENERAL ALLOCATOR?**

22 A. A major failing of the Massachusetts Formula is that it gives no weight to
23 growth and change. In reality, the growth and change of developing
24 unregulated affiliates command proportionately more management attention
25 and services than a stable, steady regulated utility. FPL notes that its

1 percentage share of the Massachusetts Formula allocation decreases over time,
2 but only because of the faster growth rate of the unregulated affiliates. The
3 Massachusetts Formula does not account for the effort required to drive that
4 growth in the unregulated affiliates operating in the challenging competitive
5 arenas.

6 Newness and growth are important cost drivers and can be better
7 indicators of the level of management attention and staff services than absolute
8 size alone.

9

10 **Q. IS THERE AN ALTERNATIVE TO THE MASSACHUSETTS FORMULA**
11 **THAT, IN YOUR OPINION, WOULD MORE FAIRLY ALLOCATE**
12 **THE COSTS THAT ARE THE SUBJECT OF THE FORMULA?**

13 A. Yes. First, FPL should increase its use of direct charges and rates for cost
14 allocation, thereby reducing its reliance on the less preferred general allocator.
15 Second, after appropriate inquiry and investigation, the Commission should
16 require FPL to develop a new general allocation formula that gives proper
17 weight to the growth and change aspects of unregulated affiliates that consume
18 management attention and staff resources. The general allocation formula
19 should also deemphasize payroll as a factor as contract labor is a ready
20 substitute for employee payroll. The different mixes of employees and
21 contractors can distort the payroll factor among FPL and its affiliates.

22

23 **E. COST ALLOCATION METHODOLOGIES – AFFILIATES TO FPL**

24 **Q. ARE FPL'S AFFILIATES' PRICING AND COST ALLOCATION**
25 **METHODOLOGIES ADEQUATE?**

1 A. No. All of the affiliate charges to FPL are listed as direct charges in MFR
2 Schedule C-30. (The response to OPC Interrogatory No. 161 clarifies that
3 some affiliate charges to FPL are allocated, and are not direct charges.)
4 However, other than a line item cost comparison for FiberNet and AT&T, FPL
5 provided no support for being charged the lower of cost or market price by
6 affiliates. For charges based upon direct or allocated cost, none of the FPL
7 affiliates have cost allocation manuals that are designed to enable FPL to
8 comply with the Commission's affiliate transaction rule. FPL, as the regulated
9 entity, is responsible to assure that charges to it from affiliates comply with the
10 Florida Rule. Therefore, FPL should assure the methodologies employed by its
11 affiliates comply with the Rule. Further, FPL should audit the transactions to
12 assure that the affiliate methodologies are being applied properly.

13 FPL does not perform the accounting for the affiliates who charge FPL.
14 It has no oversight responsibility or authority to assure that the fully allocated
15 cost based charges to FPL are correctly calculated and are accurate. Further,
16 there have been no internal audits of affiliate charges to FPL in Witness
17 Ousdahl's memory according to an informal telephone interview. FPL has
18 provided no assurance that the 2013 affiliate charges to FPL of \$22.2 million
19 are correct and proper, other than that the affiliates comply with federal
20 financial accounting rules. However, it is possible to comply with federal
21 financial accounting rules and still overcharge FPL.

1 **III. GENERAL CONCERNS WITH FPL'S AFFILIATE RELATIONSHIPS AND**
2 **TRANSACTIONS**

3 **A. ASYMMETRICAL PRICING**

4 **Q. WHAT IS FPL'S RESPONSIBILITY REGARDING PRICING**
5 **CHARGES TO AND FROM AFFILIATES?**

6 A. The Florida affiliate transaction rule is clear that "asymmetrical" pricing is required
7 between FPL and its affiliates. That is, for charges from FPL to an affiliate, FPL
8 must charge the higher of market price or fully allocated cost. For charges from
9 affiliates to FPL, the affiliate must charge the lower of market price or fully allocated
10 cost. (This is called "asymmetrical" pricing because the benefit is always to FPL and
11 its ratepayers and not to the affiliate.) Because FPL is the regulated entity, it bears
12 the responsibility to assure that each charge meets this requirement. Therefore, FPL
13 must know what the market price and fully allocated cost are for each affiliate
14 transaction, both to and from FPL.

15
16 **Q. HOW CAN FPL MEET ITS RESPONSIBILITY TO KNOW THE**
17 **MARKET PRICE FOR EACH AFFILIATE TRANSACTION?**

18 A. Some market prices are relatively straightforward, in that FPL or the affiliate
19 could issue an RFP for the service or product and determine the market price
20 from responses from unaffiliated suppliers. In this case, FPL or the affiliate
21 must accept the best market-derived proposal if it is more advantageous than
22 the affiliate offering. Otherwise, bids will not be the vendors' best efforts or
23 they may not bid at all. This true market test is the strongly preferred method

1 for proving that FPL is paying the lower of cost or market when affiliate
2 products or services are an option.

3 It is more difficult to determine the market price for shared common
4 support services that do not easily lend themselves to competitive bidding. In
5 some cases, market studies may be able to determine comparable professional
6 fee rates for engineering, legal, accounting and similar professional services.
7 Then, FPL could compare its or its affiliates' fully allocated cost hourly rates to
8 the going market rates determined by the study. A similar approach could be
9 used for those costs charged by rates, such as, per square foot, per full-time
10 equivalent employee (FTE) or per workstation.

11
12 **Q. DID FPL AVAIL ITSELF OF EITHER OF THESE METHODS FOR**
13 **ADDRESSING MARKET PRICES FOR AFFILIATE COSTS?**

14 A. No. Interrogatories and requests for PODs on this topic produced only three
15 examples of any effort remotely related to addressing market prices for the
16 hundreds of affiliate transactions other than asset transfers. One was only a
17 sole source justification for a purchase by FPL from an affiliate for an
18 emergency generator installation that did not include any competitive pricing
19 information. The second was a simple line item comparison of FiberNet prices
20 to AT&T prices that included no explanation or analysis and no indication that
21 AT&T was bidding on an equal footing for FPL's business. The third is a
22 periodic (five-year interval) market study of office space rental costs that FPL
23 uses as a basis for the rent that FPL charges its affiliates for office space.

1 FPL offered no market price information for any of the other hundreds
2 of affiliate transactions for tens of millions of dollars of related costs that are
3 incurred each year. It is clear that FPL rarely makes any attempt to determine
4 the higher of market or cost for pricing services to affiliates and the lower of
5 market or cost for purchases from affiliates, other than for transfers of assets.

6
7 **Q. DOES FPL MEET ITS BURDEN FOR ASYMMETRICAL PRICING?**

8 A. No. FPL appears to make good faith efforts to do asymmetrical pricing for
9 asset transfers. However, it makes little or no effort to do asymmetrical pricing
10 for affiliate transactions for goods and services. As an example, the FPL Cost
11 Allocation Manual, Exhibit KO-9 page 3, discusses cost or market pricing for
12 transfers of assets, but does not require it for purchasing or selling goods and
13 services from and to affiliates.

14 Witness Ousdahl states in her testimony, page 27, lines 13-15, “[t] he
15 CAM largely follows the published guidelines recommended by the National
16 Association of Regulatory Utility Commissioners (“NARUC”).” However, the
17 NARUC Guidelines included in the FPL CAM state in Section D: “1.
18 Generally, the price for services, products and the use of assets provided by a
19 regulated entity to its non-regulated affiliates should be at the higher of fully
20 allocated costs or prevailing market prices.” And, “2. Generally, the price for
21 services, products and the use of assets provided by a non-regulated affiliate to
22 a regulated affiliate should be at the lower of fully allocated cost or prevailing
23 market prices.” (See, KO-9, p. 13 of 16) FPL adopts the NARUC Guidelines
24 for asymmetric pricing, and then fails to implement them for goods and
25 services transactions with affiliates.

1 Q. CAN YOU PROVIDE AN EXAMPLE OF A RELATIONSHIP IN
2 WHICH THE MARKET PRICE OF FPL SERVICES MIGHT BE
3 HIGHER THAN THE FULLY ALLOCATED COST?

4 A. Yes. The response to OPC Interrogatory No. 12, Attachment 1, lists extensive
5 services provided by FPL to FPL Energy Services (FPLES). These include call
6 center customer assistance, transferring new customer calls to FPLES, financial
7 hedge transactions, mark to market adjustments, and many others. This is a
8 prime example of NEE/FPL "leveraging" the FPL organization developed to
9 serve ratepayers in order to facilitate the development of an affiliated
10 enterprise. FPL's "leveraging" of its resources, and good will paid for by its
11 Florida ratepayers violates the intent of Section 366.05(9), Florida Statutes, and
12 the affiliate transaction rule that Florida ratepayers not subsidize FPL affiliate
13 nonutility activities. It is highly likely that the market value of these important
14 services is higher than the cost allocations assigned to FPLES. FPL does not
15 meet its burden to prove that the amounts it is charging FPLES are the higher
16 of cost or market price.

17

18 Q. CAN YOU PROVIDE AN EXAMPLE OF A PROBLEM WITH
19 AFFILIATES UNDER-COMPENSATING FPL FOR SERVICES?

20 A. Yes. The response to OPC Interrogatory No. 18, asking how affiliates pay for
21 the value of using FPL established contracts or relationships, says that, "[t]here
22 is no separate compensation provided to FPL by affiliates for having FPL
23 establish vendor contracts or relationships." In other words, FPL does the work
24 paid for by ratepayers to establish vendor relationships and contracts, and
25 affiliates can utilize those relationships and contracts for free, thereby causing

1 Florida ratepayers to subsidize the affiliates' nonutility activities. This is
2 another example of NEE "leveraging" the value of FPL for the benefit of its
3 unregulated subsidiaries. FPL should be compensated for the value of the
4 relationships and contracts utilized by affiliates.

5
6 **Q. WHAT IS FPL'S POSITION ON "LEVERAGING" THE FPL**
7 **ORGANIZATION FOR THE BENEFIT OF ITS UNREGULATED**
8 **AFFILIATES?**

9 A. Witness Ousdahl, in response to OPC Interrogatory No. 4, said, "[a]s affiliate
10 operations began, FPL leveraged its fleet and support organizations to serve the
11 enterprise . . ." My interpretation of this statement, based on the information
12 provided by FPL, is that FPL and NEE consciously decided to utilize the FPL
13 organizational assets paid for by Florida ratepayers to assist in the development
14 of its now substantial unregulated operations. NEE uses the resources and
15 capabilities assembled in FPL to serve Florida customers under regulated
16 tariffed rates to facilitate diversification into unregulated operations.

17 In my experience, new and growing unregulated enterprises normally
18 take more time and energy than a well-established, "going concern" regulated
19 utility. It is likely that a disproportionate share of FPL's time and energy has
20 been applied to these diversification efforts. As I will explain below, this raises
21 the concern that the developing enterprises do not pay their fair share of FPL's
22 costs. As explained above, NEE and FPL have a large incentive to undercharge
23 the diversified businesses that are being leveraged from the organizational
24 resources of FPL paid for by the Florida ratepayers. An example of this is
25 NEE's leveraging of the FPL Nuclear Division and the FPL Power Generation

1 Division to develop NEE's large scale unregulated generation portfolio in
2 NEER, as described in the response to OPC Interrogatory No. 5.

3

4 **Q. IS FPL'S "LEVERAGING" APPROPRIATE?**

5 A. Only if FPL's customers are properly compensated for the utilization of its
6 organizational resources paid for by Florida ratepayers at every step and in
7 every instance.

8

9 **Q. HAS FPL (AND HAVE THE FLORIDA RATEPAYERS) BEEN**
10 **PROPERLY COMPENSATED FOR THE UTILIZATION OF FPL**
11 **ORGANIZATIONAL RESOURCES IN THE DEVELOPMENT OF THE**
12 **UNREGULATED AFFILIATES?**

13 A. No. In my testimony, I will point out several instances of FPL (and the Florida
14 ratepayers) being inadequately compensated for the use of the FPL
15 organizational resources in developing and operating the unregulated affiliates.

16

17 **B. ECONOMIES OF SCALE**

18 **Q. WHAT IS FPL'S POSITION ON THE POSSIBLE BENEFIT OF**
19 **LEVERAGING FPL'S ORGANIZATIONAL RESOURCES TO**
20 **DEVELOP ITS UNREGULATED AFFILIATES?**

21 A. Witness Ousdahl discusses the leveraging of FPL's organizational resources for
22 the benefit of its unregulated affiliates. She states on pages 26 and 27 of her
23 direct testimony that, "[w]hile the activities embedded in FPL today continue to
24 be necessary to support the provision of electric service to FPL's Florida retail
25 customers; charging a portion of these support services to its affiliates has

1 allowed FPL to reduce its share of these necessary fixed costs for the benefit of
2 its retail customers and shareholders.” She adds, “Furthermore, by spreading
3 the fixed cost of the support activities over a broader base, the retail utility
4 customers’ cost responsibility is reduced below what they would otherwise
5 incur.” In other words, FPL should benefit from economies of scale of serving
6 the unregulated affiliates from the regulated utility.

7

8 **Q. DID YOU FIND EVIDENCE OF THESE ECONOMIES OF SCALE?**

9 A. No. On the contrary, I found evidence that the costs of the kind of support and
10 shared services normally provided by a service company to a utility like FPL
11 and the unregulated affiliates are projected to increase faster than inflation.
12 According to MFR Schedule C-33, over the 2009 to 2013 period,
13 Administration and General (A&G) Expenses increase from \$74.51 per
14 customer to \$93.84 per customer, an increase of 25.9%; and, Operations and
15 Maintenance (O&M) Expenses Less Fuel per KWH sold increases from
16 \$0.01422 to \$0.01829, an increase of 25.7%. However, over the same period,
17 the Consumer Price Index is only projected to increase from 214.5 to 233.8, an
18 increase of 9%.

19 A&G expenses per customer and non-fuel cost per KWH sold are the
20 type of expense rates that should benefit from the economies of scale Witness
21 Ousdahl is touting. Both FPL and its unregulated affiliates are expected to
22 grow over this period and should provide ever greater economies of scale. For
23 example, according to the NEE/FPL 2011 Form 10-K, FPL has estimated
24 planned capital expenditures of \$10.7 billion from 2012 through 2016 and
25 NEER and Corporate and Other has estimated planned capital expenditures of

1 \$6.6 billion. However, the FPL filing does not reflect corresponding
2 economies of scale happening.

3

4 **Q. WHY DO YOU THINK THE ECONOMIES OF SCALE ARE NOT**
5 **PROJECTED TO APPEAR?**

6 A. As I discuss throughout my testimony, FPL has several deficiencies in the way
7 it implements and oversees its affiliate relationships and transactions, such as
8 the lack of a service company as mentioned above. In my opinion, these
9 deficiencies are contributing to FPL and Florida ratepayers failing to benefit
10 from actual economies of scale that are and will be occurring.

11

12 **C. SOLE SOURCE AFFILIATE CONTRACTS**

13 **Q. HAS FPL AWARDED SOLE SOURCE CONTRACTS TO**
14 **AFFILIATES?**

15 A. Yes, almost all of FPL's contracts with affiliates are sole source contracts,
16 meaning it has not given the chance to win the business to unaffiliated
17 competitors. The response to OPC Interrogatory No. 25 says, "[s]chedule C-
18 31, Contracts with Affiliates, is apparently referencing page 455 of FPL's 2010
19 FERC Form 1. The majority of the contracts included on page 455 are
20 considered sole source arrangements." Also, in response to OPC POD No. 5,
21 FPL only provided partial documentation of two of nine new affiliate
22 contractual relationships. FPL did not adequately justify any of the nine
23 relationships.

24 The new or amended sole source contracts listed in Schedule C-31 are

1 for things like accounts receivable financing (\$900 million at one percent per
2 year), purchase of emergency generators (\$28 thousand), switchyard upgrades
3 (\$50 million), Future Enterprise Network Architecture (\$1.5 million), and
4 insurance (over \$9 million) that are easily and normally bid to unaffiliated
5 suppliers by other electric utilities.

6 **Q. IN YOUR OPINION, DOES FPL'S USE OF SOLE SOURCE**
7 **CONTRACTS COMPLY WITH THE COMMISSION'S AFFILIATE**
8 **TRANSACTION RULE?**

9 A. No, on two counts. First, Florida's asymmetrical pricing affiliate transaction
10 rule requires that FPL determine market prices so it can price goods or services
11 from affiliates at the lower of market price or fully allocated cost. A
12 competitive bidding process with full participation by non-affiliated suppliers is
13 the ideal way to establish market prices.

14 Second, a non-affiliated supplier may be able to offer FPL a more
15 advantageous relationship. FPL may be overpaying its affiliates or it may be
16 receiving less advantageous terms and conditions.

17
18 **D. SERVICE AGREEMENTS**

19 **Q. WHAT ARE SERVICE AGREEMENTS?**

20 A. Service agreements are contracts between a service provider and an affiliate. This is
21 a good management practice that spells out commitments and expectations on both
22 sides. For holding companies with service companies, there is typically a service
23 agreement between the service company and each affiliate served. Further, there is

1 typically a service agreement between a regulated utility and each affiliate that
2 provides it goods or services. Service agreements specify such things as the goods
3 and services to be provided, the service levels to be achieved, how the transactions
4 will be priced, standard terms and conditions, audit rights, and so on. It is best if the
5 agreements are signed by accountable executives on each side who are
6 organizationally unrelated, making the agreements as arms-length as possible.

7

8 **Q. DOES FPL UTILIZE SERVICE AGREEMENTS WITH ITS**
9 **AFFILIATES?**

10 A. Of the hundreds of affiliate relationships identified by FPL (rolled up into eight
11 categories) in its MFRs, FPL provided only two affiliate agreement-like documents.
12 The first is a Corporate Support Services Agreement between FPL and Lone Star
13 Transmission required by the Public Utility Commission of Texas (PUCT). The
14 second is a Master Service Agreement between FPL and FPL FiberNet. There are no
15 other service agreements.

16

17 **Q. IS IT GOOD PRACTICE TO REQUIRE SERVICE AGREEMENTS**
18 **BETWEEN AFFILIATES AS DOES THE PUBLIC UTILITY**
19 **COMMISSION OF TEXAS?**

20 A. Yes. In addition to being a good management practice, some states require
21 service agreements to be filed and approved by the regulatory commission. In
22 addition to Texas, I am also aware that Maine requires Commission approved
23 service agreements between regulated operating companies and their affiliates.
24 This is a good regulatory practice as well and assures the affiliate relationships
25 are structured to comply with affiliate rules and regulations. Service

1 agreements also provide a starting point for audits of affiliate relationships and
 2 transactions. In addition to making sure the affiliate relationship is structured
 3 correctly, it is also important to assure that it is being operated as designed. I
 4 recommend that the Commission investigate the desirability of requiring
 5 service agreements between FPL and its affiliates.

6
 7 **E. USE OF THE FPL NAME**

8 **Q. IS FPL COMPENSATED FOR THE USE OF ITS NAME BY**
 9 **UNREGULATED AFFILIATES?**

10 A. No. The FPL response to OPC Interrogatory No. 14 says, “[t]here is no
 11 separate compensation provided to FPL by affiliates for the use of the Florida
 12 Power & Light name.” This is contrary to the Florida requirement for FPL to
 13 charge affiliates the higher of market price or fully allocated cost for value
 14 received. In the case of using the FPL name, FPL charges affiliates nothing at
 15 all. However, the ratepayers have supported FPL in building its brand over
 16 many years. In my opinion, NEE likely chose to include FPL in the names of
 17 unregulated subsidiaries operating in Florida because of the positive
 18 connotation it would bring. FPL should be charging them the market value for
 19 the benefits provided by use of the FPL name.

20 This is another good example of NEE and FPL “leveraging” the value
 21 of FPL built by ratepayers, and FPL being inadequately compensated for the
 22 use of FPL assets, resources and intellectual property.

23
 24 **IV. FINDINGS, RECOMMENDATIONS, AND ADJUSTMENTS**

25 **Q. IN YOUR EXPERT OPINION, DID FPL MEET ITS BURDEN OF**

1 **PROOF REGARDING THE REASONABLENESS OF ITS PROPOSED**
2 **AFFILIATE CHARGES AND PAYMENTS?**

3 A. No. FPL did not adequately support the charges, either in its direct case or in
4 responses to interrogatories and POD requests. In my opinion, FPL's direct
5 case makes assertions without proof and its responses to the interrogatories and
6 POD requests that ask for specific support of its affiliate charges and payments
7 were inadequate. FPL did not comply with important aspects of the Florida
8 affiliate transaction rule nor the precedents emphasizing its burden to prove that
9 affiliate charges and costs are reasonable.

10 It is clear that NEE's strategy is to leverage the FPL ratepayer funded
11 resources to build its unregulated affiliates. It is also clear that FPL is not
12 adequately compensated for the use of its ratepayer funded resources by
13 affiliates. The claim that FPL somehow benefits from economies of scale by
14 serving unregulated affiliates from FPL funded resources is not supported by
15 the evidence.

16 FPL has organized its affiliate relationships and transactions in a
17 manner that makes the true nature of the relationships and transactions less than
18 transparent. However, it is clear that FPL does not meet the full letter or spirit
19 of the Florida affiliate transaction rule or the precedents which place the burden
20 of proof on FPL to establish the reasonableness of its affiliate transactions.
21 FPL has multiple deficiencies in its affiliate relationships and transactions.

1 Q. CAN YOU SUMMARIZE THE DEFICIENCIES YOU FOUND IN FPL'S
2 AFFILIATE RELATIONSHIPS AND TRANSACTIONS?

3 A. Yes, they are as follows:

- 4 1. There is no service company legal entity encompassing the common and
5 support services provided by both FPL and NEER. This makes determining the
6 appropriateness of affiliate transactions difficult.
- 7 2. Of its hundreds of affiliate relationships (which FPL rolls up into eight
8 categories), FPL has service agreement-like contracts for only two of them.
- 9 3. Asymmetric pricing is not used by FPL for all affiliate transactions for goods
10 and services as required by the affiliate transaction rule. Asymmetric pricing is
11 only adhered to for asset transfers.
- 12 4. The preferred allocation methodologies of direct charges and rates for affiliate
13 cost allocations are used too little, and the use of the less preferred general
14 allocator is used too much.
- 15 5. Positive time reporting for all service company type functions is underutilized,
16 making cost accounting less accurate.
- 17 6. The Massachusetts Formula general allocator overemphasizes size, specifically
18 the things that characterize electric utilities (assets, employees and revenue)
19 and underemphasizes growth and change, which typify the unregulated
20 affiliates. It also over-emphasizes payroll as a factor, which can be misleading
21 when an entity uses contractors instead of employees. The Massachusetts
22 Formula over-allocates costs to FPL and under-allocates costs to unregulated
23 affiliates.

- 1 7. FPL does not document the benefit of purchases of goods and services to FPL
2 ratepayers from affiliates and does not assure that affiliates' fully allocated cost
3 calculations are accurate.
- 4 8. The use of sole source contracts with affiliates is inappropriate, particularly
5 when the goods or services involved are readily available in the marketplace.
- 6 9. Affiliates do not pay for the value of using the FPL name.

7

8 **Q. WHAT SHOULD BE DONE IN THIS CASE ABOUT THE FPL**
9 **DEFICIENCIES IN AFFILIATE RELATIONSHIPS AND**
10 **TRANSACTIONS?**

- 11 A. Because of the manner in which FPL reports its affiliate relationships and
12 transactions, it is impossible to calculate the cost to ratepayers for each of the
13 nine deficiencies identified. However, it is substantial. The Commission
14 should require remedies of the deficiencies before the next rate case so that the
15 reasonable affiliate transactions can be clearly identified. This will allow the
16 Commission to assess FPL performance against the affiliate transaction rule
17 and precedents much more precisely going forward.

18 For this case, as a proxy for the substantial cost to ratepayers of the nine
19 identified deficiencies in FPL's affiliate relationships and transactions, I
20 recommend that the Commission increase the 2013 projected FPL affiliate
21 charges to affiliates by 20% and reduce the 2013 charges from affiliates to FPL
22 by 20%. Based upon my experience, 20% is an appropriate representation of
23 the order of magnitude of the ratepayer subsidization caused by the deficiencies

1 identified. This would increase the FPL charges to affiliates by \$30.1 million
2 from \$150.6 million to \$180.7 million, and would reduce the charges by
3 affiliates to FPL by \$4.4 million from \$22.2 million to \$17.8 million.
4 Therefore, I recommend that FPL test year operating and maintenance expenses
5 be decreased by \$34.5 million to reflect the impact of my adjustment.

6
7 **Q. DO YOU HAVE ANY ADDITIONAL RECOMMENDATIONS?**

8 A. Yes. Due to the large negative impact of the existing situation to Florida
9 ratepayers, the Commission should also open an investigation into FPL's
10 affiliate relationships and transactions to address the deficiencies I have
11 identified in my testimony.

12
13 **Q. WHAT WOULD THE INVESTIGATORY DOCKET THAT YOU**
14 **RECOMMEND ENCOMPASS?**

15 A. I would recommend that an investigatory docket encompass the following
16 areas, at a minimum:

17 *Virtual and/or Service Company* -- Ideally, NEE/FPL should establish a
18 service company legal entity encompassing FPL, NEER and other subsidiary
19 provided common and support services. Alternatively, the Commission could
20 require FPL to form virtual service companies within FPL and its affiliates
21 providing services to FPL utilizing available features in the SAP accounting
22 system. All employees who materially serve more than one company (at least
23 ten percent of their time to a second company) should be assigned to a service

1 company, real or virtual.

2 As discussed earlier, FPL recently underwent a transition to new
3 financial account software that would, in my opinion, make virtual service
4 companies a realistic possibility.

5 ***Service Agreements*** -- The investigatory proceeding should consider requiring
6 the use of service agreements between FPL and each of its affiliates.

7 ***Asymmetric Pricing*** -- The investigatory proceeding should include the manner
8 in which the Commission will require proof of asymmetric pricing for all FPL
9 affiliate transactions.

10 ***Allocation Methodologies*** -- The investigatory proceeding should include
11 methods by which the Commission may require FPL to substantially increase
12 the use of direct charges and rates for affiliate cost allocations and decrease the
13 use of a general allocator.

14 ***Positive Time Reporting*** -- The investigatory proceeding should consider
15 requiring FPL to develop and implement positive time reporting for all service
16 company professional services type functions.

17 ***General Allocator*** -- The Commission should include in its investigatory
18 docket a consideration of the deficiencies in using the Massachusetts Formula,
19 and require FPL to develop a general allocator that better reflects the
20 consumption of management attention and staff services by growing
21 unregulated affiliates. The general allocation formula should also deemphasize
22 payroll as a factor as contract labor is a ready substitute for employee payroll.
23 The mix of employees and contractors can distort the payroll factor among FPL

1 and its affiliates.

2 ***Benefits of Purchases from FPL Affiliates to Ratepayers*** -- The investigatory
3 proceeding should consider requiring FPL to document the benefit of purchases
4 of goods and services from affiliates to FPL ratepayers and assure that the
5 affiliates' fully allocated cost calculations are accurate.

6 ***Extent of FPL's Use of Sole Source Contracts in Lieu of Competitive Bidding***
7 -- The investigatory proceeding should investigate FPL's overuse of sole source
8 contracts with affiliates and consider requiring FPL to bid all existing affiliate
9 contracts to all qualified potential providers.

10 ***Compensation for Use of FPL Name*** -- As part of the investigatory proceeding
11 that I recommend, the Commission should require FPL to charter an
12 independent appraisal of the value of using the FPL name and require FPL to
13 charge all FPL named affiliates the appropriate royalty fees.

14

15 **Q. DOES THAT CONCLUDE YOUR TESTIMONY?**

16 **A. Yes.**

1 BY MS. CHRISTENSEN:

2 Q Mr. Vondle, did your prefiled testimony have
3 three exhibits labeled "DPV-1" through "DPV-3" attached
4 to it?

5 A Yes.

6 Q Do you have any corrections to those
7 exhibits?

8 A No.

9 Q I would ask you, Mr. Vondle, if you could
10 please summarize your testimony.

11 A The purpose of my testimony is to review
12 Florida Power & Light's affiliate relationships and
13 transactions in relation to the FPC's rules and
14 precedence.

15 The Commission established a standard for
16 evaluating affiliate relationships and transactions in
17 the cost allocation and affiliate transactions rule.
18 Three of the key points regarding this rule are, one:
19 Substantially all entities under the NextEra Energy
20 corporate umbrella are FPL affiliates; two, FPL must
21 charge affiliates the higher of fully allocated costs
22 or market price, and affiliates must charge FPL the
23 lower of fully allocated cost or market price. This is
24 known as asymmetric pricing. And three, it is FPL's
25 burden to prove no subsidization of nonutility

1 activities by the ratepayers. If the utility does not
2 meet its burden of proof or does not comply with the
3 affiliate accounting and allocation rules, the
4 affiliate charges should be disallowed.

5 There's a strong financial incentive for
6 companies to allocate more costs to a regulated utility
7 to increase its revenue requirement in rates and to
8 allocate fewer costs to unregulated affiliates to
9 increase their profits.

10 Essentially every dollar of common cost that
11 is allowed to be charged to a utility results in
12 another dollar of revenue to the utility. And every
13 dollar not charged to an unregulated affiliate results
14 in an additional dollar of profit to that affiliate.
15 Overcharging FPL and undercharging unregulated
16 subsidiaries would be a win/win for NextEra Energy.

17 In analyzing FPL's filing and responses to
18 interrogatories and requests for production of
19 documents, I found that FPL fails to ensure the
20 reasonableness of the affiliate transaction amounts and
21 has nine major deficiencies in its affiliate
22 relationships and transactions.

23 These are, one, there is no service company
24 legal entity encompassing the common and support
25 services provided by both FPL and NextEra Energy

1 resources. Of its hundreds -- number two, of its
2 hundreds of affiliate relationships, FPL has
3 service-agreement-like contracts with only two of them.
4 Three, asymmetric pricing is not used by FPL for all
5 affiliate transactions for goods and services as
6 required by the rule.

7 Four, the preferred allocation methodologies
8 of direct charges and rates for affiliate cost
9 allocations are used too little, and the use of the
10 less preferred general allocator is used too much.

11 Five, positive time reporting for all service
12 company type functions is under-utilized, making cost
13 accounting less accurate.

14 Six, the Massachusetts General Allocator
15 Formula over-emphasizes and under-emphasizes growth and
16 change. It also overemphasizes payroll as a factor in
17 the allocation formula, and as a result, the
18 Massachusetts formula over-allocates costs to FPL and
19 under-allocates costs to unregulated affiliates.

20 Seven, FPL does not document the benefit of
21 purchases of goods and services to FPL ratepayers and
22 does not ensure that the affiliate's fully allocated
23 costs to them are accurate.

24 Eight, the use of sole source contracts with
25 affiliates is inappropriate, particularly when the

1 goods or services involved are readily available in the
2 marketplace. Nine, affiliates do not pay for the value
3 of using the FPL name.

4 Because of the manner in which FPL has
5 conducted its affiliate relationships and transactions,
6 it is impossible to calculate the cost to ratepayers
7 for each of the nine deficiencies I have identified;
8 however, it is substantial.

9 For this case, as a proxy for the substantial
10 cost to ratepayers of the nine identified deficiencies,
11 I recommend that the Commission increase the 2013
12 projected FPL affiliate charges to affiliates by
13 20 percent and reduce the 2013 charges from affiliates
14 to FPL by 20 percent.

15 Based upon my experience, 20 percent is an
16 appropriate representation of the order of magnitude of
17 the ratepayers' subsidization caused by the
18 deficiencies identified. Therefore, I recommend that
19 the FPL test year operating and maintenance expenses be
20 decreased by 34.5 million.

21 I also recommend that the Commission open an
22 investigation into FPL's affiliate relationships and
23 transactions to address the deficiencies I have
24 identified in my testimony.

25 MS. CHRISTENSEN: We tender the witness for

1 cross.

2 CHAIRMAN BRISE: Mr. Lavia.

3 MR. LAVIA: No questions.

4 CHAIRMAN BRISE: Mr. Saporito.

5 MR. SAPORITO: No questions, Mr. Chairman.

6 CHAIRMAN BRISE: Mr. Wiseman.

7 MR. WISEMAN: No questions.

8 CHAIRMAN BRISE: Mr. Moyle.

9 MR. MOYLE: Just a couple.

10 CROSS-EXAMINATION

11 BY MR. MOYLE:

12 **Q You have a master's in business from Southern**
13 **Methodist University; is that right?**

14 A I do.

15 **Q Did they teach you in college the value of**
16 **advertising to get a brand identified?**

17 A Yes.

18 **Q Okay. And you're aware that FPL advertises,**
19 **correct?**

20 MR. BUTLER: I'm going to object to this. I
21 believe that it's friendly cross, which the
22 prehearing order, order establishing procedure,
23 does not permit.

24 CHAIRMAN BRISE: Mr. Moyle.

25 MR. MOYLE: I'll withdraw.

1 BY MR. MOYLE:

2 Q Let me ask you this question: You say in
3 your testimony about FPL is not being compensated by
4 its affiliates for the use of the FPL name, but I don't
5 see anywhere where you say that issue is worth dollar X
6 or dollar Y.

7 How would you suggest that that issue -- if
8 the Commission were to conclude that there is value
9 associated with the FPL's name, how would you suggest
10 as an expert that that issue be addressed?

11 MR. BUTLER: Again, I'm going to object.

12 This is friendly cross. Mr. Moyle is trying to
13 expand the scope of Mr. Vondle's direct testimony.
14 He's not crossing him at this point.

15 CHAIRMAN BRISE: Mr. Moyle.

16 MR. MOYLE: Well, I think I kind of am
17 because I'm trying to clarify with respect to, you
18 know, the affiliate compensations. He said
19 20 percent. But then he's also said that he
20 thinks there should be a separate docket to
21 examine affiliate transactions.

22 I'm trying to understand what the
23 recommendation is with respect to the use of the
24 FPL name, or if he doesn't have one, he doesn't
25 have one. I'm just trying to clarify that point.

1 And that's all I have.

2 CHAIRMAN BRISE: All right. Mary Anne.

3 MS. HELTON: It seems to me that Mr. Moyle
4 has raised a point where clarification would help
5 make the record clear, so I would recommend going
6 forward with his question.

7 CHAIRMAN BRISE: All right. I'll allow the
8 question.

9 THE WITNESS: To be clear for this case, I'm
10 recommending the 20 percent reduction in affiliate
11 charges for this particular case. I'm making
12 another recommendation for a docket to investigate
13 each of these nine deficiencies and perhaps a
14 larger scope, if you choose.

15 In that investigation, there would include
16 the engagement of an expert in branding,
17 advertising the value of the FPL name to conduct a
18 study and provide an expert opinion on what the
19 value of using the FPL name is to the nonregulated
20 subsidiaries that do use it.

21 BY MR. MOYLE:

22 **Q Okay. And then I guess, just so we're**
23 **completely clear, in this case you haven't said the**
24 **value of the use of the FPL name is worth \$100;**
25 **therefore, you know, there should be an adjustment**

1 based on that of 20 percent. There's no information
2 with respect to the value of the use of the FPL name in
3 your testimony; is that right?

4 A Yes.

5 Q Okay.

6 MR. MOYLE: That's all I have. Thank you.

7 CHAIRMAN BRISE: Captain Miller.

8 CAPTAIN MILLER: I have no questions.

9 CHAIRMAN BRISE: All right. Mr. Butler.

10 MR. BUTLER: Thank you, Mr. Chairman. And I
11 apologize to Mr. Moyle. I was going to ask that
12 question, as it turns out, so that's good.

13 CROSS-EXAMINATION

14 BY MR. BUTLER:

15 Q Mr. Vondle, good morning, still by a few
16 moments.

17 You're not an attorney, are you?

18 A No.

19 Q Okay. Have you conducted any investigation
20 into the regulatory history of the Florida Public
21 Service Commission Affiliate Transaction Rule?

22 A Into the history of it?

23 Q Yes, that's right.

24 A No.

25 Q Okay. Have you testified in Florida

1 previously on affiliate transaction issues?

2 A No.

3 Q All right. Where in the affiliate
4 transaction rule do you find a reference to the burden
5 of proof being on FPL for demonstrating the
6 reasonableness or prudence of affiliate transaction
7 costs?

8 A I believe it's in the Commission order, not
9 in the rule that I referred to on page 4.

10 Q Okay. You don't see anything in the rule to
11 that effect, do you?

12 A No.

13 Q Okay. In preparing your testimony in this
14 case, did you evaluate the affiliate transaction
15 processes of other holding companies in which there is
16 only one utility operating company that serves in a
17 single state similar to NextEra Energy?

18 A No.

19 Q Okay. In preparing your testimony, did you
20 review any Florida PSC audits of FPL affiliate
21 transactions?

22 A No.

23 Q On page 9, lines 7 to 18 of your direct
24 testimony, if you could turn there.

25 A Which line?

1 Q I'm sorry, it's page 9, lines 7 through 18.

2 A Okay.

3 Q A question about whether FPL has a typical
4 affiliate structure, and you answer no and then go on
5 to explain, correct?

6 A Yes.

7 Q But isn't it correct, Mr. Vondle, that you
8 conceded in your deposition that you didn't know what
9 is or isn't a typical structure for holding companies
10 such as NextEra Energy that have utility operations
11 only in a single state?

12 A Well, to be clear, I'm not sure there is a
13 standard or typical structure. My recommendation in
14 this particular case is that because of the scale of
15 NextEra Energy's nonregulated operations, that a
16 service company would be appropriate for this
17 particular situation.

18 Q Okay. Mr. Vondle, do you have a copy of your
19 deposition transcript available to you?

20 A I do.

21 Q Would you turn to page 36 of the transcript.
22 And there starting on line 15 I asked you, "But you're
23 not aware of what is or isn't typical for holding
24 companies in the circumstance of NEE and FPL with
25 operations in only a single state or the operations in

1 a single state?" And you answered: "No, I have not
2 done a survey of those types of companies."

3 Was that testimony accurate?

4 A Yes.

5 Q Okay. Have you performed any such survey
6 between the time of your deposition and today?

7 A No, I have not done a survey of that
8 particular topic.

9 Q Mr. Vondle, do you know how FPL selects the
10 appropriate cost allocation methodology that it uses in
11 its affiliate transactions?

12 A I know what they have testified they use. I
13 do not know how they selected the methodologies.

14 Q Okay. Big picture, does FPL use the three
15 types of allocation methods you identify on pages 15
16 and 16 of your testimony for its charging of affiliate
17 costs?

18 A Yes.

19 Q Okay. And to the extent you know, does FPL
20 follow the same hierarchy of preference among those
21 methods that you recommend?

22 A Yes. I did not personally audit their cost
23 accounting and cost allocation. But according to their
24 testimony, they follow the same general hierarchy.

25 Q Okay. I would like to ask you to turn to

1 page 20 of your testimony, lines 20 to 21. You have a
2 sentence there: "However, it is possible to comply
3 with federal financial accounting rules and still
4 overcharge FPL."

5 Do you see that?

6 A Yes.

7 Q Okay. Isn't it true that when you prepared
8 your testimony, you weren't aware of any specific
9 federal accounting rules with which FPL or its
10 affiliates could comply but still overcharge?

11 A Just the general financial accounting rules
12 that all public companies must comply with. I'm not a
13 financial accountant.

14 Q Okay. And you said at your deposition that
15 you weren't aware of any specific federal accounting
16 rules where this -- where you could follow them and
17 still overcharge FPL; is that correct?

18 A Yes.

19 Q Okay. I would like you to look up on
20 page 20, lines 6 through 8 of your testimony. You make
21 the point or the assertion that "None of the FPL
22 affiliates have Cost Allocation Manuals that are
23 designed to enable FPL to comply with the Commission's
24 affiliate transaction rule."

25 Do you see that?

1 A I'm sorry, I must have misheard the
2 reference.

3 **Q Page 20, lines 6 through 8, at least in my**
4 **copy.**

5 A Yes.

6 **Q The sentence that begins "For charges based**
7 **upon direct or allocated cost," et cetera. Do you see**
8 **that?**

9 A Yes.

10 **Q Okay.**

11 MR. BUTLER: Mr. Chairman, I would like to
12 distribute an exhibit at this time.

13 CHAIRMAN BRISE: Sure. That would be 575.

14 Any objections to this document?

15 (No response.)

16 (Exhibit No. 575 was marked for
17 identification.)

18 BY MR. BUTLER:

19 **Q Mr. Vondle, have you seen the document**
20 **that --**

21 CHAIRMAN BRISE: Ms. Christensen, do you have
22 an objection?

23 MS. CHRISTENSEN: I don't believe so. I'll
24 have to see how he's using them, assuming this is
25 the Cost Allocation Manual.

1 MR. BUTLER: It is the NEER policy on
2 transactions with affiliates and subsidiaries.

3 CHAIRMAN BRISE: Okay. You may proceed.

4 MR. MOYLE: Was this provided in an
5 interrogatory response or a production of
6 documents?

7 MR. BUTLER: It was. It was provided in
8 response to OPC's first set of production of
9 documents, document request number 6.

10 MR. MOYLE: Okay.

11 BY MR. BUTLER:

12 Q Have you seen this document before,
13 Mr. Vondle?

14 A I think so, but I think this is the one
15 Witness Ousdahl said was not a -- did not apply.

16 Q Well, let me ask you about it, Mr. Vondle.
17 Would you turn to the first page after the cover sheet,
18 which is identified at the bottom with a Bates No.
19 OPC-004710.

20 Do you see that?

21 A Yes.

22 Q Okay. I would like to focus your attention
23 on Section 2, "General," and I would like you to read
24 the first paragraph of that section.

25 A "Although FPL, Infrastructure, and NEER are

1 wholly-owned subsidiaries of NextEra Energy, Inc., FPL,
2 and certain Infrastructure subsidiaries such as Lone
3 Star Transmission, LLC, are regulated utilities which
4 have adopted rules concerning cost allocation and
5 affiliate transactions. The purpose of this rule
6 making is to establish cost allocation requirements to
7 ensure proper accounting for affiliate transactions in
8 nonregulated utility activities in order for these
9 transactions and activities to not be subsidized by
10 utility ratepayers."

11 **Q Would you agree that that stated purpose, in**
12 **fact, is to provide guidelines for N-E-E-R, NEER, to**
13 **comply with the Commission's affiliate transaction**
14 **rule?**

15 A Yes. I'm kind of confused by having this
16 document because we asked about it as being the -- when
17 we asked for copies of affiliates' Cost Allocation
18 Manuals, this was the only thing that came close to
19 that, and when we inquired about it, we were told that
20 it does not apply and it wasn't being put forward as an
21 affiliate Cost Allocation Manual.

22 **Q But would you agree on its face that it --**
23 **first of all, it is by NEER, which is -- would you**
24 **agree that is FPL's principal and regulated affiliate?**

25 A I believe NEECH would technically be the

1 principal unregulated affiliate. But, yeah, NEER is a
2 large, unregulated affiliate.

3 **Q As most of the unregulated affiliate**
4 **operations, actually, doesn't it, from your**
5 **understanding?**

6 A Yes.

7 **Q Okay.**

8 A NEECH does.

9 **Q All right. Would you agree that this**
10 **procedure is indeed directed at assuring that the**
11 **affiliate transactions between NEER and FPL are**
12 **conducted in a way that ensures that utility ratepayers**
13 **are not subsidizing them?**

14 A No. I would have to study this and ask
15 questions about it. This was presented earlier and we
16 asked about it and were told it wasn't relevant.

17 **Q All right. Thank you, Mr. Vondle. But you**
18 **have not studied it; is that correct?**

19 A I'm sorry?

20 **Q You have not studied it at this point,**
21 **correct?**

22 A We looked at it and were curious about it and
23 asked follow-up questions and were told it was not
24 relevant so I didn't continue with it.

25 **Q Okay.**

1 A And just for clarity, if it would have been
2 relevant, if we were told it was relevant and
3 applicable, I would have included it in my testimony as
4 an exception.

5 **Q Okay. Let me ask you some questions about**
6 **FPL Energy Services, FPLES.**

7 A Yes.

8 **Q Turn to page 24 of your testimony. Okay. On**
9 **lines 13 and 14, you make the statement that "It is**
10 **highly likely that the market value of these important**
11 **services is higher than the cost allocations assigned**
12 **to FPLES."**

13 **Do you see that?**

14 A Yes.

15 **Q Is it correct, Mr. Vondle, when you prepared**
16 **your testimony, you didn't have any documentation of**
17 **specific cost allocation or market values to support**
18 **that conclusion?**

19 A No. It actually would be FPL's burden to
20 provide the market values, and they weren't provided.

21 **Q But you didn't have any -- you didn't have**
22 **any information, anything you could point to at the**
23 **time of your deposition to support this conclusion, did**
24 **you?**

25 A In the absence of information from FPL, I

1 formed an opinion that --

2 MR. BUTLER: Mr. Chairman, I would ask that
3 the witness follow our convention of answering the
4 questions yes and no and then a brief explanation
5 if he feels the need.

6 CHAIRMAN BRISE: Yeah, I think that would be
7 important. Start with a yes or no and then you
8 can put in the qualifier.

9 THE WITNESS: Will do.

10 MS. CHRISTENSEN: Can we ask that Mr. Butler
11 repeat his question.

12 CHAIRMAN BRISE: Mr. Butler, if you would
13 repeat your question so that Mr. Vondle can answer
14 it again.

15 MR. BUTLER: Okay.

16 BY MR. BUTLER:

17 **Q At the time you prepared your testimony,**
18 **Mr. Vondle, isn't it correct that you didn't have any**
19 **specific documentation to support the conclusion that**
20 **is reflected on page 24, lines 13 and 14?**

21 A That is correct. We asked for that
22 information from FPL. It was not provided.

23 **Q Did you review this Commission's**
24 **investigation into FPL's transactions with FPLES?**

25 A No.

1 **Q Okay.**

2 MR. BUTLER: Mr. Chairman, I would like to
3 mark as the next exhibit a composite of the
4 materials relevant to that investigation.

5 CHAIRMAN BRISE: Sure. That would be 576.

6 Mr. Butler, just for planning purposes, do
7 you have a lot more with this witness or should we
8 recess and go for our lunch break and then return?

9 MR. BUTLER: I have more than a couple of
10 questions. I'm not sure that it would be a lot.
11 We could break at this point, if you would like,
12 or I could ask about this exhibit and then we
13 could break. That's certainly fine with me.

14 CHAIRMAN BRISE: Okay. So let's finish with
15 this exhibit and then we'll go ahead and move into
16 our break.

17 MR. BUTLER: That's fine.

18 CHAIRMAN BRISE: Any objections to this
19 document?

20 MS. CHRISTENSEN: I'm not sure that this
21 includes the full audit report, and I would ask
22 that the full audit report be included. This is
23 only excerpts from the audit that was done on FPL.

24 MR. BUTLER: Actually, it doesn't include any
25 of the audit report. I wouldn't object to

1 including the audit report if the Commission
2 parties would like to see it.

3 What's included here is FPL's response to the
4 audit report, and that is included in its complete
5 form, and then the Commission's order following
6 the audit and FPL's response.

7 CHAIRMAN BRISE: So your exhibit is primarily
8 the response from FPL?

9 MR. BUTLER: The response from FPL and the
10 Commission's order on the sort of closing the
11 investigation.

12 CHAIRMAN BRISE: Okay.

13 MS. CHRISTENSEN: And I would not have an
14 objection to necessarily including FPL's responses
15 if we, in fairness, include the audit report that
16 was produced by staff. And obviously no objection
17 to the order.

18 MR. BUTLER: We don't have any objection to
19 doing that. We don't have copies as we sit here,
20 but we can certainly provide it to the parties and
21 agree to including it as part of this exhibit.

22 CHAIRMAN BRISE: Okay. We'll do that.

23 (Exhibit No. 576 was marked for
24 identification.)

25 CHAIRMAN BRISE: You may proceed.

1 MR. BUTLER: Thank you.

2 BY MR. BUTLER:

3 Q Mr. Vondle, have you ever seen the letter
4 that is the first several pages of this exhibit dated
5 October 29 from FPL to the Commission Clerk responding
6 to the Commission staff's audit report in Docket
7 100077?

8 A I don't think so.

9 Q Okay. Have you ever seen the Order No. PSC
10 11-0378PAAEI that is the remaining pages of this
11 exhibit?

12 A I don't think so.

13 Q Okay. The letter is from 2010 and the order
14 is from 2011, correct?

15 A The letter is 2010, the order is dated 2011.

16 Q Okay. Mr. Vondle, doesn't it seem like for
17 somebody whose specific purpose in this proceeding is
18 to investigate FPL's affiliate transactions, it would
19 have been a good idea to look at an investigation that
20 was actually on that same subject of affiliate
21 transactions and concluded less than a year before the
22 Commission -- or before FPL filed its rate case?

23 A No. The company, FPL, has the burden to
24 prove its compliance with the affiliate rule, so I
25 looked at what the company provided to prove its

1 compliance with the affiliate rule.

2 I don't believe this was provided or I would
3 have looked at it if we thought it was relevant. So if
4 you think it's relevant, I think the company should
5 have provided it in meeting its burden.

6 **Q Wouldn't you think the Commission would**
7 **already be aware of it seeing as how they issued the**
8 **order?**

9 MS. CHRISTENSEN: Objection, it goes beyond
10 the -- it calls for speculation.

11 MR. BUTLER: I'll withdraw the question.

12 BY MR. BUTLER:

13 **Q Mr. Vondle, would you turn to -- let's see,**
14 **I'm sorry, the pages aren't numbered in this. It is**
15 **the Exhibit 1 attached to the letter, so it's, I think,**
16 **the sixth page in.**

17 A Yes.

18 **Q Do you see that?**

19 MS. CHRISTENSEN: Can you tell me exactly
20 which page you're on. I think there's page 4 of 5
21 on top of the FPL response. I just want to make
22 sure I'm on the right document, in the order.

23 MR. BUTLER: If you're on page 4 of 5 of the
24 letter, go one more page because 5 of 5 is the
25 conclusion of it. And then the page after that is

1 an attachment to an Exhibit 1, FPLES connect
2 services -- excuse me -- market price comparison.

3 Do you see that, Mr. Vondle?

4 THE WITNESS: I see that.

5 MR. BUTLER: Okay. And, Ms. Christensen, do
6 you see it?

7 MS. CHRISTENSEN: I see it. I'm not sure,
8 was that part of the original response?

9 MR. BUTLER: It is. It is the attachment
10 that is alluded to on page 5 of 5 of the letter.

11 MS. CHRISTENSEN: Okay.

12 BY MR. BUTLER:

13 **Q Mr. Vondle do you see the reference to FPL**
14 **having incurred a cost of generating a lead list for**
15 **customers to whom FPLES would offer its services of \$20**
16 **per thousand customers? And it's referenced in the**
17 **second paragraph of Exhibit 1.**

18 A Yes.

19 **Q Okay. And if you look in the third**
20 **paragraph, you'll see that it discusses the**
21 **compensation FPL received for providing that lead list.**

22 **And would you agree that this indicates the**
23 **price was approximately \$20 per thousand customers?**

24 **Or, I'm sorry, is \$120 per thousand customers?**

25 A This is the first time I've seen this. I can

1 confirm what the document says.

2 **Q Fair enough. You haven't seen it before, you**
3 **don't know whether -- you don't have any background on**
4 **the figures that are provided here, correct?**

5 A Correct. But this isn't --

6 **Q And you didn't consider this in the course of**
7 **reaching the conclusion that is stated on page 24 of**
8 **your testimony about the likelihood of the market value**
9 **of these important services being higher than the cost**
10 **allocations assigned to FPLES?**

11 A That's correct. But had FPL provided it in
12 support of the amounts being charged to FPLES, I
13 certainly would have considered it.

14 **Q Are you aware, Mr. Vondle, that you can find**
15 **this document by simply clicking on a link in Docket**
16 **No. 100077?**

17 A Am I aware that I could do that?

18 **Q That's correct.**

19 A I suppose so.

20 **Q Mr. Vondle, I would like you to turn to the**
21 **order that's attached as part of this exhibit.**

22 MR. MOYLE: Mr. Chairman, we've refrained
23 from objecting, but I think the witness has
24 testified he's never seen this document, you know,
25 before today. And so, you know, all of the

1 testimony about, well, it says this, it says
2 that -- I mean, if it's coming in the record, it
3 will be in the record.

4 I don't know that this is appropriate to
5 continue showing him a document he's already said
6 he has no familiarity with, he can't authenticate,
7 and ask a series of questions about it,
8 particularly at this hour.

9 MR. BUTLER: You know what, Mr. Moyle has
10 accurately summarized the state of Mr. Vondle's
11 knowledge of this and I will not ask further
12 questions about it.

13 CHAIRMAN BRISE: All right. As agreed to, we
14 are going to take our lunch break.

15 MR. HARRIS: Mr. Chairman, I'm sorry, Larry
16 Harris, we do have a number -- we have some
17 exhibits in the deposition of Mr. Vondle when we
18 get back. I understand there may be some
19 objections from the parties as to the
20 admissibility, but I'm not aware of who
21 specifically is objecting or why.

22 If I could ask that the parties stay after
23 you dismiss us and hand out the documents and
24 maybe have them look at it during lunch and before
25 we reconvene we could get together and maybe have

1 a chance to work through some of the objections.

2 CHAIRMAN BRISE: Sure.

3 MR. BUTLER: That's fine. I just -- I'm not
4 sure, Mr. Harris -- you understand we have more
5 questions to ask; you just want to take the lunch
6 break to work out the deposition issues?

7 MR. HARRIS: Yes.

8 MR. BUTLER: Okay. Thank you.

9 CHAIRMAN BRISE: We will reconvene at about
10 1:10, okay. Enjoy your lunch.

11 (Whereupon, a lunch recess was taken.)

12 CHAIRMAN BRISE: All right. We're going to
13 reconvene at this time.

14 Just for planning purposing, this evening we
15 plan to be out around six today. Tomorrow morning
16 we will convene about nine-thirty. And hopefully
17 we'll run tomorrow between six or seven.

18 Wednesday, if we need to run late, then we'll run
19 late on Wednesday. But hopefully we won't have to
20 run late, okay.

21 We were on cross-examination.

22 MR. BUTLER: Thank you, Mr. Chairman. A
23 couple of housekeeping things before I return to
24 that. First of all, staff has distributed the
25 audit report that is dated October 11, 2010 in

1 which we had agreed to include as part of
2 Exhibit 576.

3 CHAIRMAN BRISE: Okay.

4 MR. BUTLER: I think that the Commissioners
5 and all of the parties should have a copy of that
6 now.

7 CHAIRMAN BRISE: Yes.

8 MR. BUTLER: The other housekeeping item
9 actually relates back to Mr. O'Donnell's
10 testimony. And there was some concern about
11 legibility of some of the pages in Exhibit 574,
12 and we have distributed a revised copy of it that
13 hopefully the legibility will be sufficient in
14 that copy.

15 CHAIRMAN BRISE: All right. Thank you. Mine
16 is legible. I don't know if everyone else's is,
17 but mine seems to be.

18 MR. SAPORITO: Mr. Chairman, mine is legible,
19 it's just slightly different from the original
20 offering. I don't know whether that's material or
21 not, because I don't know if the witness testified
22 to these last two pages from my recollection, but
23 I'm sure the record will reflect it.

24 CHAIRMAN BRISE: All right. Thank you.

25 So that was 574.

1 MR. BUTLER: 574, yes. And then the --

2 CHAIRMAN BRISE: And then 576.

3 MR. BUTLER: 576, that's right, the addition
4 of the audit report to 576.

5 CHAIRMAN BRISE: Sure.

6 Ms. Christensen, I remember you had an
7 objection. Does this satisfy?

8 MS. CHRISTENSEN: I believe for that exhibit
9 would complete the full picture, and then I would
10 be satisfied, yes.

11 CHAIRMAN BRISE: All right. Thank you very
12 much.

13 All right. You may proceed, Mr. Butler.

14 MR. BUTLER: Thank you.

15 BY MR. BUTLER:

16 Q Good afternoon, Mr. Vondle.

17 A Good afternoon.

18 Q Just very briefly on 576, I just want to ask,
19 when you were engaged by the Office of Public Counsel
20 to valuate FPL's affiliate transactions, did you ask
21 Public Counsel to provide copies of materials that were
22 related to FPL's affiliate transactions that the
23 Florida Public Service Commission might have prepared
24 over, say, the last five years or anything like that?

25 A Yes.

1 Q And am I correct from your earlier testimony
2 that the materials with respect to the Docket 100077,
3 the investigation of the FPLES affiliate relations was
4 not provided to you at that time?

5 A I believe they mentioned it to me. I did not
6 review the report.

7 Q Okay. Mr. Vondle, would you turn to page 35
8 of your testimony.

9 A Yes.

10 Q In lines 17 and 18, you talk about the
11 establishment of a service company legal entity. You
12 say, "Ideally, NEE/FPL should establish a service
13 company legal entity encompassing FPL, NEER, and other
14 subsidiary provided common and support services,"
15 right?

16 A Yes.

17 Q Okay. Do all utility holding companies with
18 which you are familiar have service companies?

19 A No.

20 Q Okay. Have you done any analysis of the
21 incremental costs of organizing and operating a service
22 company for FPL/NEE?

23 A No.

24 Q Okay. Do you know whether the use of a
25 service company would make FPL's operations more

1 **efficient?**

2 A No, I'm not recommending the service company
3 to make them more efficient; I'm making the
4 recommendation that they be -- the common support
5 services be more transparent.

6 **Q Okay. But you don't know whether that**
7 **transparency would translate into any additional**
8 **efficiency for FPL or its affiliates?**

9 A It would be speculation. I would say in
10 general having costs more visible helps with the cost
11 control as well as cost accuracy.

12 **Q But you haven't done any evaluation to**
13 **determine whether there would be any efficiency gains**
14 **or how much, if there were any; is that correct?**

15 A That's correct.

16 **Q Okay.**

17 MR. BUTLER: I'd like to pass out an exhibit
18 at this point. It's direct testimony of
19 Mr. Vondle on behalf of Southwestern Public
20 Service Company from May of 2006.

21 CHAIRMAN BRISE: The exhibit number for
22 identification purposes is going to be 577.

23 MR. BUTLER: While it's being distributed, I
24 would note, Mr. Chairman, that this is an excerpt
25 from Mr. Vondle's testimony. We have a full copy

1 of the testimony. If any party is interested in
2 seeing that, we would be happy to provide it to
3 them.

4 CHAIRMAN BRISE: Okay. Any objections?

5 MS. CHRISTENSEN: I would have to see how the
6 testimony is planned on being used and whether or
7 not I feel a full copy of the testimony is
8 warranted.

9 CHAIRMAN BRISE: Okay. Thank you.

10 (Exhibit No. 577 was marked for
11 identification.)

12 CHAIRMAN BRISE: Mr. Butler, you may proceed.

13 MR. BUTLER: Thank you.

14 BY MR. BUTLER:

15 **Q Mr. Vondle, are you the individual who**
16 **submitted this testimony?**

17 A Yes.

18 **Q And it was submitted to the Public Utilities**
19 **Commission of Texas; is that right?**

20 A Yes.

21 **Q Okay. Would you please turn to page 9,**
22 **line 17.**

23 A Yes.

24 **Q Would you read the -- well, first of all,**
25 **read the question, then if you would, please, read the**

1 **first paragraph of the answer there into the record.**

2 A "Why is benchmarking relevant in this case?

3 "ANSWER: In this case" --

4 MS. CHRISTENSEN: Objection. I'm going to
5 ask the relevancy of this line of questioning to
6 this case.

7 MR. BUTLER: I'm going to ask Mr. Vondle --
8 you'll see if you read down in here that it talks
9 about the use of benchmarking as an indicator of
10 reasonableness of affiliate costs, and I'm going
11 to ask him about what work, if any, he has done in
12 benchmarking for FPL.

13 MS. CHRISTENSEN: I have no objection to him
14 asking whether or not he's conducted any
15 benchmarking with regards to FPL and whether or
16 not that was appropriate. But I think it's not
17 appropriate impeachment using the prior testimony
18 regarding benchmarking to ask him whether or not
19 he's done any benchmarking in this case.

20 MR. BUTLER: Mr. Vondle's prior testimony
21 indicates that he supported the use of
22 benchmarking. I think it's an appropriate
23 predicate for whether he has performed
24 benchmarking in this proceeding.

25 MS. CHRISTENSEN: He could have asked him

1 whether or not he feels benchmarking is
2 appropriate. I don't know the relevancy of this
3 testimony to establish whether or not he feels
4 benchmarking can be appropriate.

5 And specifically the question asked whether
6 or not benchmarking was relevant in the case in
7 Texas. So to the extent that we're talking about
8 the FPL case in Florida and Florida's rules, I'm
9 not sure whether or not Mr. Butler has established
10 the relevancy for a Florida proceeding.

11 BY MR. BUTLER:

12 **Q Mr. Vondle, can benchmarking be used as an**
13 **indicator of the reasonableness of affiliate costs and**
14 **as evidence of the quality and efficiency of a**
15 **utility's management?**

16 A Yes. These are -- the standards in Texas are
17 different than the standards in Florida.

18 **Q But would you agree that the benchmarking**
19 **would be relevant information in assessing the**
20 **effectiveness of affiliate transaction processes**
21 **regardless of the jurisdiction?**

22 A Yes. But the purpose of this testimony -- in
23 Texas they have a burden of proof to prove that the
24 affiliate costs are reasonable. And I forgot the
25 language of their rule, but they have -- it's not a

1 higher cost or market asymmetric pricing test; it's a
2 reasonableness test. So this testimony was in support
3 of their affirmative case that the affiliate costs were
4 reasonable.

5 **Q Do you consider it relevant to the Florida**
6 **Public Service Commission whether a utility's affiliate**
7 **transactions are reasonable?**

8 A It's important, but the Florida rule goes
9 farther. The Florida rule requires asymmetric pricing.

10 **Q Okay. But you agree that it would be**
11 **something that the Florida Public Service Commission**
12 **could reasonably consider -- pardon the double use of**
13 **reasonableness -- but it could appropriately consider**
14 **the reasonableness of affiliate transactions?**

15 A The Commission is welcome to consider
16 anything it wishes.

17 **Q Okay. Mr. Vondle, did you perform any**
18 **benchmarking analysis of FPL in aiding you evaluating**
19 **FPL's affiliate transactions?**

20 A No. In preparing the case, we looked for
21 benchmarking information from FPL.

22 **Q Have you reviewed the benchmarking analyses**
23 **prepared by FPL Witness Reed in this case?**

24 A No.

25 **Q Are you aware that that was filed as a part**

1 of FPL's original on -- or along with FPL's original
2 petition in March of this year?

3 A I did not review it.

4 Q Okay. So I think it would be fair to say you
5 don't know what that testimony shows about how FPL
6 benchmarks relative to other utilities, correct?

7 MS. CHRISTENSEN: Asked and answered.

8 MR. BUTLER: No, it wasn't. I asked him
9 whether he had reviewed. I'm asking to confirm
10 whether having not reviewed it on the -- he is not
11 in a position to know whether that benchmarking
12 shows that FPL's costs compare favorably to other
13 utilities.

14 MS. CHRISTENSEN: And I believe he answered
15 that he has not reviewed it. So any questioning
16 on the content of the testimony has already been
17 asked and answered.

18 MR. BUTLER: Mr. Chairman, it doesn't work
19 that way.

20 CHAIRMAN BRISE: I think I'll allow the
21 question.

22 THE WITNESS: Could you repeat the question.

23 BY MR. BUTLER:

24 Q Sure. I'm just confirming, Mr. Vondle,
25 having not reviewed Mr. Reed's testimony, is it correct

1 you don't know what that shows about how FPL's
2 operations compare to the utilities against which
3 Mr. Reed benchmarked them; is that correct?

4 A That's correct.

5 Q Okay. Have you reviewed the benchmarking
6 analyses prepared by FPL's Rebuttal Witness
7 Mr. Flaherty?

8 A Yes. He just arrived, yes.

9 Q Would you agree that those benchmarking
10 analyses show that FPL compares favorably to the
11 utilities in Mr. Flaherty's comparison group?

12 A No. I would have to know more about the
13 benchmarking.

14 Q Okay. So you've reviewed his exhibits; is
15 that correct?

16 A I did look at his exhibits.

17 Q Okay. Would you agree that on their face
18 they show that FPL compares favorably to the utilities
19 against which he compared them?

20 A He used A&G cost only in the ones that I
21 reviewed. He did not use a higher level cost to start
22 with. It would be something like nonfuel O&M expense.

23 The problem with just using A&G expenses is
24 each utility can choose to categorize costs as A&G or
25 customer service or transmission and distribution. And

1 just using A&G costs and presuming that there is
2 apples-and-apples comparison, it's -- unless he
3 normalized the data, which we don't know if he did, I
4 would say just using A&G costs by themselves is not
5 conclusive.

6 **Q And you mentioned nonfuel O&M expenses as**
7 **being something else that one might want to look at; is**
8 **that right?**

9 A Yes. Yeah, I would have been happier if he
10 had started there.

11 **Q Okay. Do you know whether that is a metric**
12 **that Mr. Reed benchmarks?**

13 A I do not know that.

14 **Q Okay. I would like to ask you a couple of**
15 **questions about the Massachusetts formula, Mr. Vondle.**

16 A Yes.

17 **Q Turn to page 16 of your testimony.**

18 A Yes.

19 **Q You say on lines 12 and 13 that FPL**
20 **over-utilizes the general allocator. By that you're**
21 **referring to the Massachusetts formula for FPL,**
22 **correct.**

23 A Yes.

24 **Q Okay. Would you agree, Mr. Vondle, subject**
25 **to, I guess, arithmetic check, that FPL allocates**

1 approximately 30 percent of its total affiliate cost
2 using the Massachusetts formula?

3 A I'll take your word for it.

4 Q Okay. Just so you know where I'm getting
5 this, if you want, you can look -- page 10 of your
6 testimony I'm taking -- 50 percent of the charges use
7 the AMF and then 60 percent of the AMF is Massachusetts
8 formula, which would be, you know, .5 times .6 or .3.

9 Would you agree?

10 A Right.

11 Q Do you have any studies or surveys indicating
12 that 30 percent use of the Massachusetts formula is
13 exceptionally high for utility operating companies such
14 as FPL?

15 A No.

16 Q I think you also criticize FPL for which
17 inputs are used in the general allocator, correct?

18 A Yes.

19 Q And one of the ones that you think should be
20 used, added or used instead, is a factor that reflects
21 growth; is that correct?

22 A Yes.

23 Q Have you performed any evaluation to
24 determine whether in the period, say, 2010 through
25 2013, FPL's nonregulated affiliates are growing

1 **quickly?**

2 A No.

3 **Q Have you performed any study or analysis to**
4 **determine what difference in the allocation would**
5 **result if FPL had used a growth factor?**

6 A No. It's a fairly complicated question, and
7 the recommendation is to do a fairly rigorous study of
8 alternative allocation factors and in consultation with
9 the Commission develop a new general allocator.

10 **Q Okay. Are you familiar with the United**
11 **States Supreme Court case of *Groesbeck v. Duluth***
12 ***Railroad*?**

13 A The Duluth Railroad?

14 **Q Yes. It was Justice Brandeis' decision.**

15 A You know, it rings a distant bell, but I
16 can't recall any specifics.

17 **Q Okay. All right.**

18 MR. BUTLER: To help ring the distant bell
19 louder, I'll hand out an additional exhibit,
20 please.

21 CHAIRMAN BRISE: Sure. For marking purposes,
22 this would be 578.

23 (Exhibit No. 578 was marked for
24 identification.)

25 MR. MOYLE: And while there's a lull, I mean,

1 obviously this witness isn't a lawyer so I assume
2 that we're not going to get his legal opinion, you
3 know, on the opinion. Again, I'm not sure what
4 the purpose of offering the Supreme Court case is.
5 Maybe that could be clarified.

6 CHAIRMAN BRISE: Okay.

7 MR. MOYLE: I think counsel has also said,
8 with respect to opinions, that we can cite them
9 and we don't need to necessarily introduce them as
10 well.

11 MR. BUTLER: I'm sorry, we have one more that
12 needs to be handed out. My apologies, I should
13 have had them done together.

14 Mr. Chairman, I would ask that what is being
15 handed out now, which is an excerpt from rebuttal
16 testimony of Mr. Vondle before the Public
17 Utilities Commission of Texas, also in the
18 Southeastern Public Service Company case, that is
19 really -- it makes reference to the case that I
20 handed out, so it probably makes sense just to
21 have those as a composite exhibit, that perhaps we
22 could designate that as 578.

23 CHAIRMAN BRISE: Okay.

24 BY MR. BUTLER:

25 **Q Mr. Vondle, do you have a copy of the excerpt**

1 from your rebuttal testimony that has been distributed
2 and marked as Exhibit 578?

3 A Yes.

4 Q Do you recall giving this testimony before
5 the Public Utilities Commission of Texas?

6 A Yes. But to be honest, I did not review it
7 for this case. I did look at my direct testimony, so
8 this is a little foggy.

9 Q Okay. Would you look on page 6, which is
10 the --

11 MR. MOYLE: I'm going to object on relevancy
12 grounds.

13 CHAIRMAN BRISE: Okay.

14 MR. BUTLER: I'm using it to refresh
15 Mr. Vondle's recollection regarding his citation
16 with approval of the Supreme Court case that I had
17 referred to a moment ago with him.

18 MR. MOYLE: But the mere fact that he cited a
19 Supreme Court case in a case in Texas doesn't
20 necessarily -- what relevancy does it have to
21 anything that's live in this case?

22 I mean, the Supreme Court case dealt with
23 transportation rates, and he cited it, and it's
24 just, not that I can see, relevant to anything
25 that is in dispute in this case right now.

1 MR. BUTLER: That proceeding was also about
2 affiliate transactions. Mr. Vondle was citing it
3 with approval for a proposition that I want to
4 refer him to. And it seems to me relevant that he
5 would have cited it with approval in another
6 proceeding before another Public Service
7 Commission dealing with the subject of affiliate
8 transactions.

9 CHAIRMAN BRISE: Ms. Christensen.

10 MS. CHRISTENSEN: I would also agree with
11 Mr. Moyle, that this does not appear to be
12 relevant to any issue in this case in that it
13 appears to be applying a PURA Statute section that
14 I think the witness was commenting on. So it may
15 be that this is specifically addressing an issue
16 that had to do with statutory construction before
17 a different tribunal.

18 MR. BUTLER: I have a pretty narrow question
19 that I want to ask Mr. Vondle about this and then
20 I'll be happy to move on.

21 CHAIRMAN BRISE: Mary Anne.

22 MR. BUTLER: Let me try the question and see
23 if it is objectionable, if I may, Your Honor.

24 CHAIRMAN BRISE: Okay.

25

1 BY MR. BUTLER:

2 Q Mr. Vondle, does the excerpt from your
3 rebuttal testimony, bottom of page 6, line -- or top of
4 page 7 -- refresh your recollection regarding the
5 Supreme Court case that I had handed out a moment ago?

6 A Yes.

7 MR. MOYLE: Same objection. I mean, I guess
8 I'll just make the point. But if he says to the
9 witness, you know, isn't it true that if a
10 witness, you know, recommends a methodology, he
11 should have details.

12 I mean, if he has something that is relevant
13 to this case and then the witness answers and he
14 can impeach him with this statement, that's fair
15 game. But to just, you know, say here's a Supreme
16 Court case and here's the testimony and kind of
17 try to shovel it in that way, I just think it's
18 improper, it's beyond -- you know, it's not
19 relevant to anything in this proceeding at this
20 point.

21 CHAIRMAN BRISE: Mary Anne.

22 MS. HELTON: I was actually going to say
23 about the same thing that Mr. Moyle just said. My
24 recollection of how you deal with impeaching a
25 witness is you ask him a question and if his

1 answer to the question is inconsistent with prior
2 statements, then you can bring forth the
3 information that would show the prior statements.
4 It seems to me that Mr. Butler's got it a little
5 bit backwards here.

6 CHAIRMAN BRISE: Okay.

7 MR. BUTLER: My apologies.

8 BY MR. BUTLER:

9 **Q Let me just ask you this question,**
10 **Mr. Vondle: Do you agree with Justice Brandeis'**
11 **statement that it is much easier to reject formulas**
12 **presented as being misleading than to find one**
13 **apparently adequate?**

14 A Yes.

15 **Q Okay.**

16 MR. BUTLER: Those are all my questions.

17 Thank you.

18 CHAIRMAN BRISE: Thank you.

19 Staff.

20 MR. HARRIS: Yes, Commissioner, I'm pleased
21 to report that the parties have graciously agreed
22 to stipulate to some exhibits that we passed out
23 and therefore staff will have no
24 cross-examination.

25 The documents are the deposition transcript

1 of Mr. Vondle, which I believe have been
2 previously marked in the comprehensive exhibit
3 list. That would be Exhibit No. 116 previously
4 marked.

5 CHAIRMAN BRISE: Okay.

6 (Exhibit No. 116 was marked for
7 identification.)

8 MR. HARRIS: And then the hearing exhibit --
9 that's the deposition transcript, and there's an
10 errata sheet that goes with that that we would ask
11 to be included with that. Then there's also,
12 according to the comprehensive exhibit list, three
13 discovery responses, and these are marked as
14 No. 102, 106, and 107.

15 CHAIRMAN BRISE: 102, 106, and 107?

16 MR. HARRIS: Yes.

17 MS. CHRISTENSEN: Can I ask for clarification
18 for which one is 102?

19 MR. HARRIS: According to the exhibit list,
20 102 is OPC's responses to FPL's fourth set of
21 interrogatories 69 through 73. 106 is OPC's
22 response to FPL's fourth request for production of
23 documents Nos. 12 through 17. And 107 is OPC's
24 responses to FPL's sixth request for production of
25 documents No. 24.

1 MS. CHRISTENSEN: Thank you.

2 (Exhibit Nos. 102, 106, and 107 were marked
3 for identification.)

4 MR. HARRIS: And with that, we have no cross.

5 CHAIRMAN BRISE: All right. Commissioners.
6 Commissioner Balbis.

7 COMMISSIONER BALBIS: Thank you, Mr. Chairman
8 I just have one question.

9 You mention in your testimony nine
10 deficiencies in FPL's affiliate relationships and
11 transactions, and because of those deficiencies
12 you recommend a 20 percent reduction in affiliate
13 costs. And in your testimony you said "Based on
14 my experience." If you can expand on that, on
15 where the 20 percent came from and what justifies
16 it.

17 THE WITNESS: It's an order-of-magnitude
18 estimate. And I have worked as an expert witness
19 on affiliate relationships and transactions
20 several times over my career, but more than that,
21 I've worked with individual utilities and with
22 other Regulatory Commissions doing management
23 audits of affiliate relationships and
24 transactions. It's been a big part of my
25 practice.

1 And it's based upon that cumulative
2 experience that the nine different deficiencies
3 that we found here are substantial, and I believe
4 would cause the affiliate charges to be
5 approximately 20 percent more or less, depending
6 on if you're going from FPL to an affiliate or
7 from an affiliate to FPL. So it's an
8 approximation of the order of magnitude of the
9 scale of the problems we found.

10 COMMISSIONER BALBIS: Okay. Thank you.
11 That's all I had.

12 CHAIRMAN BRISE: All right. At this time, we
13 will deal with exhibits for Mr. Vondle.

14 MS. CHRISTENSEN: I do have some redirect.

15 CHAIRMAN BRISE: I'm sorry. Redirect, I'm
16 sorry.

17 MS. CHRISTENSEN: Okay.

18 REDIRECT EXAMINATION

19 BY MS. CHRISTENSEN:

20 **Q Let me just follow-up on Commissioner Balbis'**
21 **question regarding the use of the 20 percent. Can you**
22 **explain why you had to use a 20 percent approximation**
23 **in lieu of an actual dollar amount adjustment?**

24 A Yes. One of the fundamental problems is the
25 lack of asymmetric pricing, sole source contracts with

1 affiliates. And to get the actual cost difference, the
2 company would have had to do RFPs to let these
3 contracts in the open market and gotten bids and
4 selected the most advantageous bid.

5 Since they didn't do that, there's no
6 comparison in the record for me to say, well, it was
7 100 -- well, they charged 100 and they could have
8 gotten 80 and so we should disallow the 20. We've got
9 the 100, we just don't have the 80. So all of this is
10 an approximation of the order of magnitude here of the
11 problem -- the many problems we have with affiliate
12 transactions.

13 **Q And, Mr. Vondle, can you do a retrospective**
14 **type of benchmarking or market analysis that you were**
15 **just describing?**

16 A You might be able to do something in a
17 retrospective market analysis basis, but FPL did not.
18 I think their burden was to bring to the case their
19 market studies, their proof that they were paying --
20 they were charging the higher marketer cost, and they
21 were paying, when they paid to an affiliate, the lower
22 of marketer cost. That's what we were looking for and
23 did not find.

24 **Q And I think Mr. Butler asked you about**
25 **whether or not you had done any benchmarking studies in**

1 **this case. Are you testifying on FPL's behalf**
2 **regarding the appropriateness of their affiliate**
3 **transactions?**

4 A Am I -- I'm sorry, can you --

5 **Q Are you testifying for FPL and providing**
6 **benchmarking studies on their behalf in this case?**

7 A No. We asked for all of the evidence they
8 had, and I don't think we got any benchmarking studies
9 in this latest rebuttal witness. We've got testimony
10 about benchmarking studies FPL has done, but I don't
11 think we've ever been provided the actual benchmarking
12 studies.

13 **Q Okay. I think you were also asked questions**
14 **by Mr. Butler about your recommendation that you have a**
15 **separate legal entity or at a minimum an individual**
16 **corporate division that holds employees that provide**
17 **affiliate type transactions.**

18 **Can you explain why you make that**
19 **recommendation?**

20 MR. BUTLER: Excuse me, I don't think that's
21 what I asked about. I simply asked him a question
22 about a service company.

23 BY MS. CHRISTENSEN:

24 **Q I'll narrow my question to can you explain**
25 **why you believe that it was appropriate to recommend**

1 that -- or it was part of your recommendation that you
2 thought a separate legal service company was
3 appropriate in this case.

4 A Well, the fundamental problem is the scale of
5 the nonregulated affiliates in the case of FPL and
6 NextEra Energy, NEER, and FPLES and all of the others,
7 Lone Star Transmission, are all large entities. And
8 that scale, I believe, demands more transparency in the
9 shared cost accounting and allocation.

10 And a well-established vehicle for that is a
11 legal entity service company where all employees that
12 serve FPL and at least one other nonregulated
13 subsidiary on a regular basis would be housed in the
14 service company, their costs would then be clearly
15 visible and then how they're allocated among the
16 affiliates in FPL would be also much more clear.

17 Q And I believe Mr. Butler also spoke with you
18 in your testimony regarding how you could be in
19 compliance -- or your testimony regarding how you could
20 be in compliance with federal financial rules and still
21 not be complying with the Florida affiliate
22 transactions rule.

23 Can you explain what you meant by that
24 testimony?

25 A Yes. When you get outside the regulatory

1 scheme, the question of pricing between affiliates is a
2 transfer pricing issue, and companies have latitude in
3 how to price goods and services from one subsidiary to
4 another subsidiary, and there's a fair amount of
5 latitude.

6 But in the regulatory environment here, there
7 is no latitude. The pricing is prescribed by the
8 affiliate transactions rule here as asymmetric, so it
9 has to be the higher of cost or market when they're
10 charging an affiliate. And under financial accounting,
11 they could charge incremental cost, they could charge
12 the lower of cost or market. They have a lot of
13 discretion in how transfer pricing is done. So they
14 could comply with financial accounting rules but be
15 out-of-compliance with the Commission rules.

16 **Q I think Mr. Butler also discussed with you a**
17 **document regarding affiliate transactions. Can you**
18 **explain how you obtained your understanding of the**
19 **availability of affiliate Cost Allocation Manuals?**

20 A Yes. After we reviewed the official
21 responses to interrogatories and the production of
22 documents, and we reviewed the initial filing. We had
23 a number of questions about the affiliate relationships
24 and transactions, and FPL was kind enough to offer an
25 informal conversation with Witness Ousdahl, and we had

1 a teleconference to discuss many of the questions we
2 had about the material that had been provided.

3 One of the items that was provided seemed to
4 be a Cost-Allocation-Manual-related kind of document
5 from NEER and so we asked about that. And that's when
6 Witness Ousdahl told us that it was not relevant in
7 response to that particular question. And we
8 clarified, I believe with Witness Ousdahl, that none of
9 the nonregulated affiliates had Cost Allocation Manuals
10 that would be compliant with the Florida rule.

11 **Q And then I think, finally, referring you to**
12 **page 4 of your testimony, I think Mr. Butler had asked**
13 **you where in the rule that you showed the burden of**
14 **proof, and I think you referred to an order.**

15 **Can you tell us what the order says regarding**
16 **the burden of proof?**

17 A Yes. It's a 2001 order. It says, "By their
18 very nature, related-party transactions require closer
19 scrutiny. Although a transaction between related
20 parties is not per se unreasonable, it is the utility's
21 burden to prove that its costs are reasonable. *Florida*
22 *Power Corp vs. Cresse*. This burden is even greater
23 when the transaction is between related parties. In
24 *GTE Florida vs. Deason*, the Court established that the
25 standard to use in evaluating affiliate transactions is

1 whether those transactions exceed the going market rate
2 or are otherwise inherently unfair."

3 **Q Thank you.**

4 MS. CHRISTENSEN: I have no further redirect.

5 CHAIRMAN BRISE: Thank you, Ms. Christensen.

6 At this time, we will deal with exhibits.

7 MS. CHRISTENSEN: Office of Public Counsel
8 would move in Mr. Vondle's exhibits, and I believe
9 those are marked as 255, 256, and 257 on the
10 composite hearing exhibit list.

11 CHAIRMAN BRISE: Okay. 255, 256, and 257.

12 MS. CHRISTENSEN: Correct.

13 CHAIRMAN BRISE: Okay. Any objections to
14 those?

15 (No response.)

16 CHAIRMAN BRISE: Seeing none, we will move
17 those into the record.

18 (Exhibit Nos. 255, 256, and 257 received in
19 evidence.)

20 MR. BUTLER: FPL would move Exhibits 575,
21 576, and 577. We will withdraw 578. We don't
22 have a need for that one.

23 CHAIRMAN BRISE: Okay. So we will move into
24 the record 575, 576, and 577.

25 Any objections?

1 MS. CHRISTENSEN: Office of Public Counsel
2 has objections, not to 576, which is, I think, the
3 completed packet regarding the audit responses and
4 order on that.

5 However, we do have objections to 575, which
6 is purportedly a discovery response regarding
7 transactions that I believe it was clear
8 Mr. Vondle stated that he had not reviewed, has no
9 knowledge of, and therefore has not authenticated
10 this document. There is no authentication to move
11 that into the record.

12 And I believe he further clarified that he
13 did not do any further follow-up discovery based
14 upon representations of Ms. Ousdahl, the FPL
15 witness.

16 As to 577, I believe the witness agreed with
17 the direct question; therefore, it is unnecessary
18 to put in the testimony of an unrelated docket
19 that has -- from Texas that doesn't have anything
20 to do with this. I believe Mr. Butler finally had
21 asked him the question and he agreed with it, and
22 therefore this would be improper to move in. It's
23 not proper impeachment. So those are our
24 objections to those two documents.

25 CHAIRMAN BRISE: Okay. Mr. Moyle -- I mean,

1 Mr. Butler.

2 MR. BUTLER: On 575, this is the response to
3 Public Counsel. We provided this document to the
4 Office of Public Counsel. There's obviously been
5 a fair amount of testimony about it.

6 I think Mr. Vondle says he recognizes it and
7 was, you know, aware of it. Simply he recalls
8 there being a discussion of it with Ms. Ousdahl,
9 you know, subsequently.

10 I think that there's substantial indication
11 that, one, it's part of the discovery that was
12 provided in this proceeding. You know, he's aware
13 of it, he's familiar with it. It provides context
14 for a lot of the discussion that was had regarding
15 that topic, and I think it would be appropriate
16 for it to be part of the record that you can, you
17 know, take for whatever weight you choose to give
18 it.

19 MR. SAPORITO: Mr. Chairman, it's my
20 recollection with respect to 575 -- I would object
21 to this exhibit on similar grounds to OPC. This
22 witness did not in any way, shape, or form
23 recognize or validate this document in his
24 testimony today. It's not been validated.

25 MS. CHRISTENSEN: And I would disagree.

1 Mr. Vondle did not testify that he recognized the
2 document. Yeah, it was provided as part of
3 discovery responses, but a lot of documents were
4 provided as part of discovery responses. That's
5 not a sufficient foundation for admitting a
6 document.

7 I think that you have to have some personal
8 knowledge or some sort of foundation laid by the
9 witness on which you're trying to get it entered
10 in through and therefore I think it's reasonable
11 to exclude this document.

12 MR. BUTLER: Well, Mr. Chairman, unless I
13 mistook the redirect examination, Ms. Christensen
14 was asking Mr. Vondle about this particular
15 document and his awareness of it and his
16 discussion of it with Ms. Ousdahl. So I'm kind of
17 hard-pressed to understand how we would be now
18 contending that he isn't familiar with it.

19 MS. CHRISTENSEN: I think that may be part of
20 the confusion. I think what we had discussed was
21 whether or not -- as part of the original
22 production of document requests, we asked for all
23 Cost Allocation Manuals. They produced a document
24 that was similar to this, but not this particular
25 document, which is what was discussed with

1 Ms. Ousdahl. And when a follow-up question was
2 asked about whether or not there were any further
3 Cost Allocation Manuals, she indicated that none
4 existed.

5 That's why this document being produced at
6 this time is problematic. I mean, I realize it
7 was produced as further revised discovery
8 responses at some later date, but that may be
9 causing some of the confusion that we're having
10 here today.

11 CHAIRMAN BRISE: All right. Mary Anne.

12 MR. BUTLER: Mr. Chairman, one thing just
13 before Ms. Helton speaks. I just want to clear
14 the record. This document, the NEER Procedure 5.5
15 that's identified as Exhibit 575, was provided in
16 discovery to the Office of Public Counsel. They
17 had access to it.

18 Now, what they choose to do with it or not do
19 with it is a different matter. But I just want
20 the record to be clear this is not something that
21 has been sprung on them today, you know, and not
22 previously available to them.

23 CHAIRMAN BRISE: Mary Anne.

24 MS. HELTON: Mr. Chairman, I think there has
25 been a lot of discussion about this particular

1 exhibit on the record and whether or not Florida
2 Power & Light provided it to OPC in a timely
3 manner, and in my mind, I think it will make the
4 record clear to have it included. And then if
5 necessary, OPC can argue that they didn't provide
6 it, Florida Power & Light can argue that they did
7 provide it timely, and staff can hopefully sort it
8 out for you all so that you can use that as a
9 basis for your decision.

10 MR. SAPORITO: Mr. Chairman, just real
11 quickly. It's not a matter of timeliness of when
12 the document was received or provided; it's a
13 matter of relevancy. This witness did not
14 validate this document in any way, shape, or form.
15 It's not relevant to this proceeding.

16 CHAIRMAN BRISE: Thank you, Mr. Saporito.

17 We will move 575 into the record.

18 (Exhibit Nos. 575 and 576 received in
19 evidence.)

20 MR. BUTLER: Thank you, Mr. Chairman. And on
21 577, we will withdraw our request for admission of
22 that one. The topic was adequately addressed with
23 the witness, we don't need the testimony from the
24 PUCT.

25 CHAIRMAN BRISE: All right. So 577 will be

1 withdrawn.

2 I have a 578 here. Was that withdrawn as
3 well?

4 MR. BUTLER: Yes. I'm sorry if I didn't
5 mention that. Yes, we will withdraw 578 for the
6 same reason, that we covered the topic adequately
7 with the witness.

8 CHAIRMAN BRISE: Okay. And staff.

9 MR. HARRIS: Staff would move 102, 106, 107,
10 and 116 with the errata sheet.

11 CHAIRMAN BRISE: All right. Are there any
12 objections to 102, 106, 107, and 116?

13 Mrs. Christensen.

14 MS. CHRISTENSEN: No objection.

15 CHAIRMAN BRISE: All right. Seeing no
16 objections, we will move 102, 106, 107, and 116
17 into the record.

18 (Exhibit Nos. 102, 106, 107, and 116 received
19 in evidence.)

20 CHAIRMAN BRISE: All right. At this time,
21 since we're done with exhibits for Mr. Vondle, do
22 we seek to get Mr. Vondle excused?

23 MS. CHRISTENSEN: Yes, I would ask that
24 Mr. Vondle be excused from the proceeding.

25 CHAIRMAN BRISE: All right. At this time, we

1 will excuse Mr. Vondle from the proceedings.

2 Thank you very much.

3 THE WITNESS: Thank you.

4 MR. REHWINKEL: Thank you, Mr. Chairman. The
5 Citizens of Florida call Helmuth Schultz, III.

6 Thereupon,

7 HELMUTH SCHULTZ, III

8 was called as a witness, having been first duly sworn,
9 was examined and testified as follows:

10 DIRECT EXAMINATION

11 BY MR. REHWINKEL:

12 **Q Mr. Schultz, could you state your name for**
13 **the record, please.**

14 A My name is Helmuth Schultz, III.

15 **Q And were you previously sworn as a witness**
16 **today?**

17 A Yes, I was.

18 **Q Mr. Schultz, on whose behalf are you**
19 **testifying today?**

20 A I am testifying on behalf of the Citizens of
21 the State of Florida.

22 **Q Did you cause to be filed 51 pages of**
23 **prefiled testimony in this docket?**

24 A I did.

25 **Q Do you have any changes or corrections to**

1 **make to that testimony?**

2 A I have some minor changes, yes, sir.

3 **Q Could you give those -- read those into the**
4 **record, please.**

5 A On page 28, line 12, there's a number that
6 says 1.604 million; it should read 1.601 million. On
7 page 30, line 2, there's a percentage of 13.94 percent;
8 that should be 12.94.

9 **Q I'll ask you about your exhibits after that.**

10 A Okay.

11 **Q Okay. Are those all the changes or**
12 **corrections you have to your direct testimony?**

13 A Yes.

14 **Q Okay. If I asked you the questions contained**
15 **in your testimony with those two corrections, would the**
16 **answers in your prefiled testimony be the same?**

17 A Yes, they would.

18 MR. REHWINKEL: Mr. Chairman, I ask that the
19 prefiled direct testimony of Helmuth Schultz, III
20 be inserted into the record as though read.

21 CHAIRMAN BRISE: All right. We will enter
22 Mr. Schultz's testimony into the record as though
23 read, seeing no objections.

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DIRECT TESTIMONY

OF

Helmuth Schultz III

On Behalf of the Office of Public Counsel

Before the

Florida Public Service Commission

Docket No. 120015-EI

I. STATEMENT OF QUALIFICATIONS

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Helmuth W. Schultz III. My business address is 15728 Farmington Road, Livonia, Michigan 48154.

Q. BY WHOM ARE YOU EMPLOYED?

A. I am a Senior Regulatory Analyst with Larkin & Associates, P.L.L.C.

Q. PLEASE DESCRIBE THE FIRM LARKIN & ASSOCITES, P.L.L.C.

A. Larkin & Associates, P.L.L.C., performs independent regulatory consulting primarily for public service/utility commission staffs and consumer interest groups (public counsels, public advocates, consumer counsels, attorney generals, etc.). Larkin & Associates, P.L.L.C., has extensive experience in the utility regulatory field as expert witnesses in over 600 regulatory proceedings, including water and sewer, gas, electric and telephone utilities.

1 Q. HAVE YOU PREPARED AN EXHIBIT WHICH DESCRIBES YOUR
2 EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE?

3 A. Yes. Attached as Exhibit No.__(HWS-1), is a summary of my background,
4 experience and qualifications.

5

6 Q. BY WHOM WERE YOU RETAINED, AND WHAT IS THE PURPOSE OF
7 YOUR TESTIMONY?

8 A. Larkin & Associates, P.L.L.C., was retained by the Florida Office of Public Counsel
9 (OPC) to review the rate increase requested by Florida Power & Light Company (the
10 Company or FPL). Accordingly, I am appearing on behalf of the citizens of Florida
11 (“Citizens”) who are customers of FPL.

12

13 **II. BACKGROUND**

14 Q. PLEASE BRIEFLY DESCRIBE THE ISSUES YOU WILL BE ADDRESSING
15 IN THIS PROCEEDING.

16 A. I am addressing the appropriateness of the Company’s recovery on payroll, incentive
17 compensation, benefits other than pensions and post-retirement benefits (OPEB),
18 payroll taxes, tree trimming, pole inspections, the recovery of Directors and Officers
19 Liability (DOL) Insurance and uncollectible expense. I will also be addressing the
20 level of the depreciation reserve surplus available in 2013 based on recommendations
21 regarding costs estimates in 2012 that are considered excessive and impact the
22 amount the Company projected to be utilized in 2012. I am also addressing the rate
23 base impact from the change in the depreciation reserve surplus and some
24 recommendations to working capital. Finally, I will address the Company’s request

1 regarding the continuation of the automatic storm recovery mechanism contained in
2 the 2010 settlement arguments among parties that the Commission approved in Order
3 No PSC-11-0089-S-EI.

4
5 **III. PAYROLL**

6 **Q. WERE THERE ANY ISSUES IDENTIFIED DURING YOUR REVIEW THAT**
7 **IMPACTED YOUR RECOMMENDATIONS REGARDING THE AMOUNT**
8 **OF PAYROLL INCLUDED IN FPL'S 2013 PROJECTED TEST YEAR?**

9 A. Yes. I determined that documentation supporting the amount of payroll included in
10 O&M expense was inconsistent and insufficient. Later in my testimony I will provide
11 the basis for my concerns and express my reservations related to the payroll O&M
12 factor.

13
14 **Q. IN YOUR REVIEW OF THE FILING, DID YOU IDENTIFY ANY**
15 **CONCERNS RELATED TO THE LEVEL OF PAYROLL REQUESTED BY**
16 **FPL IN THE TEST YEAR?**

17 A. Yes. In my review I became concerned that the projected employee complement is
18 excessive. The Company's request is based on an average of 10,312 employees in
19 2012 and 10,147 employees in 2013. As shown on Schedule C-35, the average
20 number of employees in 2011 was 9,971. This historical information initiated my
21 concern and prompted a more in-depth review of the reasonableness of the
22 Company's request.

1 **Q. WHAT OTHER INFORMATION DID YOU REVIEW THAT CONFIRMED**
2 **YOUR CONCERN WAS JUSTIFIED?**

3 A. The Company response to OPC Interrogatory No. 33, as amended, indicated that, as
4 of April 2012, the employee count was 9,932. My further review of that response and
5 the amended response to OPC Interrogatory No. 34 suggested that the request was
6 excessive, not only because of the increase over current levels, but also because the
7 request is based on a combination of actual filled positions and authorized positions
8 that historically FPL has not filled. As shown on Exhibit No. HWS-2, Page 2 of 3,
9 the Company has a long history of not filling the number of its authorized positions.
10 Specifically of concern is that more recently the variance between authorized and
11 filled positions has increased. Based on the information included in the filing and the
12 responses to discovery, I believe the Company has significantly overstated the
13 projected number of employees in its rate request.

14

15 **Q. DID THE COMPANY ADDRESS THE NEED FOR EMPLOYEES IN ITS**
16 **REQUEST?**

17 A. Yes. In her direct testimony on pages 7-11, Company Witness Slattery stated that the
18 industry continues to face a severe shortage of skilled workers. She adds this is due
19 to an aging workforce, skill gaps in the talent pool, and emerging technologies, with
20 special emphasis on the nuclear employees. She then refers to some statistics
21 indicating that 40% of the workforce will be eligible to retire within five years, and
22 the number of nuclear employees within different age groups is shifting to where a
23 greater percentage of the employee complement consists of older employees.

1 Q. DOES THE COMPANY'S EXPLANATION JUSTIFY THE INCREASE IN
2 EMPLOYEES THAT IT IS REQUESTING?

3 A. No. The Company presented a very similar argument in Docket No. 080677-EI,
4 which time has refuted.

5

6 Q. PLEASE ELABORATE.

7 A. As shown on Exhibit No. HWS-2, Page 2 of 3, the number of actual employees at
8 FPL has actually declined from an average of 10,711 in 2008 to 9,921 as of May
9 2012. The current request is troubling, since the Company in Docket No. 080677-EI
10 requested 11,111 employees. According to the direct testimony and rebuttal
11 testimony of Company Witness Slattery in that last rate case, complements of 11,111
12 in 2010 and 11,157 in 2011 were required because of the increased number of
13 employees eligible for retirement and the challenges to utilities with nuclear
14 operations. Specifically, Ms. Slattery stated at page 6 of her rebuttal, "The staffing-
15 level forecasts are management's reasonable estimate of what is required to do the
16 work based on optimal staffing levels." This assumption of what is reasonable is
17 important, because it provides a contrast between how the Company approaches a
18 rate request and how the Company actually operates. The fact is that the projected
19 11,111 positions claimed to be *required* for 2010 in the last rate case significantly
20 exceeded the 10,195 actual average employment level for 2010. The projected
21 11,157 positions claimed to be *required* for 2011 in the last rate case significantly
22 exceeded the 9,961 actual average employment level for 2011. With a variance of
23 916 positions in 2010 and 1,196 positions in 2011, any request for a significant
24 increase by FPL should be viewed with skepticism. It should be noted that my

1 analysis that compares actual employees to the authorized number reflects a
2 significantly lower authorized level for 2010 and 2011 than what the Company stated
3 it had a need for in Docket No. 080677-EI. Based on those differences, the Company
4 apparently revised its estimate of needed positions subsequent to the Commission's
5 decision in Docket No. 080677-EI. It is worth further noting that in its direct
6 testimony and petition for increase in this case, FPL does not claim that it
7 implemented austerity measures affecting employee levels after the last rate case
8 decision and stipulation that impacted service levels. To the contrary, FPL witnesses
9 brag about high service levels and FPL even requests a 25 basis point ROE adder as a
10 reward.

11
12 **Q. DID THE COMMISSION ALLOW THE COMPANY THE REQUESTED**
13 **11,111 POSITIONS IN DOCKET NO. 080677-EI?**

14 A. No. In Order No. PSC-10-0153-FOF-EI, the Commission indicated that the history
15 of variances suggests that the Company's forecast for 2010 did not take into account
16 unfilled positions. The Commission then elected to apply the 2007 variance of 2.48%
17 in determining a disallowance to payroll expense. The order does not specifically
18 identify the number of allowed positions; however, if one reduces the 11,111
19 positions by 2.48% (or 276 positions), the result is an allowance of 10,835 positions
20 for 2010. The Company never achieved an employee count of 10,835 during any
21 month in the period from January 2009 through May 2012. As indicated earlier, the
22 average actual employee count for 2010 was 10,195 positions and for 2011 it was
23 9,961 positions. Based on the variance between the number of positions allowed in
24 rates and the number actually employed, the Company cannot argue that the positions

1 were not filled on account of the Commission disallowing a number of the positions it
2 requested in Docket No. 080677-EI.

3

4 **Q. WHAT ADJUSTMENT ARE YOU PROPOSING TO THE COMPANY'S**
5 **REQUEST?**

6 A. As shown on Exhibit No. HWS-2, Page 1 of 3, using the 3.76% average variance for
7 the five months ended May 2012, I am recommending that the number of positions in
8 the 2013 test year be reduced from 10,147 to 9,766. That reduction in employees
9 reduces total payroll, excluding incentive compensation, by \$34.866 million. That
10 equates to a reduction in payroll expense of \$24.968 million (\$24.578 million
11 jurisdictional).

12

13 **Q. WHY DID YOU EXCLUDE INCENTIVE COMPENSATION?**

14 A. Because the Company made an adjustment for executive incentive compensation, I
15 will address incentive compensation separately. I am proposing an additional
16 adjustment for employee incentive compensation. Including incentive compensation
17 in the above payroll adjustment could result in a double counting of the dollars being
18 adjusted.

19

20 **Q. BASED ON YOUR RECOMMENDATION OF ALLOWING 9,766**
21 **EMPLOYEES IN THE TEST YEAR, YOU ARE RECOMMENDING AN**
22 **EMPLOYEE COMPLEMENT THAT IS LOWER THAN THE CURRENT**
23 **MAY 2012 LEVEL OF 9,921. WHY SHOULD THE COMMISSION REDUCE**

1 **THE EMPLOYEE COMPLEMENT TO A LEVEL BELOW WHAT IS**
2 **CURRENTLY EMPLOYED?**

3 A. FPL's request for authorized positions assumed 10,348 positions in May 2012 and an
4 average of 10,147 in the projected test year 2013. That is a difference of 201
5 positions, based on the number of FPL's authorized positions. My recommendation
6 to reduce the projected 2013 authorized number of 10,147 by 381 positions may
7 appear high in comparison. However, when you consider that the actual complement
8 as of May 2012 is 9,921 and my recommendation is to allow 9,766, my
9 recommendation is only a reduction of 155 positions. I am actually making a
10 conservative adjustment.

11
12 **Q. WOULD YOU EXPLAIN WHY YOU BELIEVE THAT COMPARISON IS**
13 **PROPER?**

14 A. FPL and I disagree as to what will occur with respect to the number of employees.
15 The Company's request is based on a projection built on a projection, while my
16 analysis and recommendation is based on actual data as it relates to the Company's
17 less than accurate historical forecasts. The key starting point is May 2012. The
18 Company estimated that as of May 2012, there would be 10,348 employees. It
19 further assumed that, from May 2012 through the projected 2013 test year, the
20 employee complement would be reduced by 201 positions (10,348 – 10,147),
21 reflecting an average test year complement of 10,147 employees. My
22 recommendation begins with the actual employee complement of 9,921 as of May
23 2012 and essentially eliminates FPL's May 2012 guesstimate from the equation. I

1 then determined that the need in the projected 2013 test year is 9,766. My
2 recommendation is for a reduction of 155 positions (9,921 – 9,766) to the employee
3 complement for the same time frame that the Company assumes a reduction of 201
4 positions.

5
6 **Q. ARE YOU AWARE OF WHY THE COMPANY WOULD FORECAST A**
7 **REDUCTION IN THE EMPLOYEE COMPLEMENT DURING 2012 AND**
8 **INTO 2013?**

9 A. Based on the response to OPC Interrogatory No. 48, some of the reduction was due to
10 the Company factoring in a reduction of approximately 206 positions associated with
11 the Smart Meter deployment during 2012 and 2013. That would account for a large
12 portion of the Company's decline of 352 positions between January 2012 (10,404)
13 and December 2013 (10,052).

14
15 **Q. DID YOUR REVIEW OF THE COMPANY'S PAYROLL REQUEST**
16 **INCLUDED IN THE CURRENT FILING LEAD TO ANY OTHER**
17 **CONCERNS?**

18 A. Yes. The purpose of my review was to determine how FPL developed the payroll
19 amount included in O&M expense, evaluate whether the development of the
20 employee complement was reasonable and whether a proper amount was charged to
21 O&M expense. In addition to my concern with the excessive estimated employee
22 complement, I identified a concern related to the appropriate O&M payroll factor.
23 Even though I am not proposing an adjustment, I do believe that the Commission

1 should be aware of the problems and/or uncertainties that I encountered as part of my
2 review.

3

4 **Q. IF YOU ARE NOT PROPOSING AN ADJUSTMENT RELATED TO THE**
5 **O&M PAYROLL FACTOR, THEN WHY ARE YOU ASKING THE**
6 **COMMISSION TO RECOGNIZE THE PROBLEMS YOU ENCOUNTERED**
7 **WITH THE COMPANY'S PAYROLL DOCUMENTATION?**

8 A. First, the Company's filing should be supported by documents that readily identify
9 what is actually included in the filing. A document that is labeled as payroll should
10 consist of payroll not a combination of payroll and loaders. The fact that one
11 response stated that O&M was 80% of total payroll and a second response indicates
12 O&M is 70.6% of total payroll indicates there are uncertainties about the reliability of
13 information being provided to other parties that are evaluating the filing. The second
14 reason that I am asking the Commission to recognize issues that have been
15 encountered is that I am proposing an adjustment to the employee complement, and
16 that adjustment is based on total payroll that will ultimately be adjusted to reflect an
17 amount that is included in FPL's O&M expense requested in the 2013 test year.
18 Because a question may arise as to whether a reasonable O&M factor has been
19 applied to the total payroll adjustment, the Commission should be aware of the
20 discrepancies in information supplied by the Company.

21

22 **Q. PLEASE ELABORATE ON THE METHOD OF REVIEW AND ANALYSIS**
23 **YOU UNDERTOOK AND THE ISSUES THAT YOU IDENTIFIED.**

1 A. According to the Company's Schedule C-35, in 2012 there is an estimated average
2 employee complement of 10,312 and a total payroll of \$1,075,925,000. For 2013, the
3 projected test year, there is an estimated average employee complement of 10,147 and
4 a total payroll of \$1,048,734,000. To verify the dollars and employee numbers, I
5 reviewed the Company's workpapers provided in the response to OPC Production of
6 Documents, POD No. 12. During this review, I identified 4 specific files that my
7 experience and the Company's response to discovery led me to believe would provide
8 verification of the Company's Schedule C-35. First, I noted an Excel document
9 (MFR C-35_05_Payroll 2012 and 2013) that listed the total payroll for 2012 and 2013
10 to be \$1,075,924,714 and \$1,048,734,277, respectively. This verified the total dollar
11 information on Company Schedule C-35. A second document (MFR C-35_04_FPL
12 AVG Headcount_ 2012) identified an average employee complement of 10,312 and
13 10,147 for 2012 and 2013, respectively. This verified the "Average Employees" for
14 the respective years on Company Schedule C-35.

15

16 **Q. YOU INDICATED THAT THERE WERE FOUR SPECIFIC DOCUMENTS**
17 **THAT YOU RELIED UPON. IF YOU VERIFIED THE TOTAL PAYROLL**
18 **AND THE AVERAGE NUMBER OF EMPLOYEES FOR THE RESPECTIVE**
19 **YEARS WITH THESE TWO DOCUMENTS, WHAT OTHER**
20 **INFORMATION WAS REQUIRED FOR YOUR REVIEW?**

21 A. The Company's request is based on the total payroll; however, the cost of service
22 includes only the portion of total payroll being charged to O&M. Therefore, further
23 review was required to determine the amount charged to O&M.

24

1 **Q. WHAT AMOUNT OF PAYROLL DID THE WORKPAPERS INDICATE WAS**
2 **CHARGED TO O&M?**

3 A. A third document (Allocation of FERC Payroll to COSSIDs.xlsx) indicated that FPL
4 charged \$836,441,007 and \$847,283,848 to O&M expense in 2012 and 2013,
5 respectively. Because the amounts indicated a higher than normal percentage of total
6 payroll being charged to O&M, I elected to verify that the amounts represented as
7 O&M payroll were in fact charged to O&M in the filing. I performed this verification
8 process by testing some of the expense accounts to a fourth workpaper (Compound
9 Allocator Calculations-Test 2013.xlsx). This document provided a breakdown of
10 costs by account between "labor" and "other". The labor dollars matched the
11 amounts tested on the third document (Allocation of FERC Payroll to COSSIDs.xlsx)
12 and the total matched the amount of expense in the respective accounts on MFR
13 Schedule C-4, which in turn ties into the Company's MFR Schedule C-1. Based on
14 that testing, I concluded that I had a document that did in fact reflect the O&M
15 payroll included in the Company's rate filing.

16

17 **Q. YOU INDICATED THAT YOU HAD A CONCERN REGARDING THE**
18 **PERCENTAGE OF PAYROLL THAT APPEARED TO BE CHARGED TO**
19 **O&M. WHY DID YOU HAVE THAT CONCERN?**

20 A. As shown on Exhibit No. __ (HWS-2), Page 3 of 3, I have summarized the expense,
21 capital and other payroll for the years 2006 through 2011 and for 2012 year-to-date.
22 For the years 2007-2011, the five year average of payroll that was charged to O&M
23 expense is 75.18% and the 2012 year to date is 73.68%. The workpaper (Allocation
24 of FERC Payroll to COSSIDs.xlsx) that shows \$836,441,007 and \$847,283,848 being

1 charged to O&M expense in 2012 and 2013, respectively, reflects that the O&M
2 payroll in 2012 and 2013 represents 77.7% and 80.8%, respectively, of total payroll.
3 That is a concern because that represents a significant increase over the historical
4 trend discussed earlier, especially with the significant amount of capital work FPL
5 has proposed in the filing. My subsequent review determined that the document was
6 not just payroll, as indicated, but that it also included benefits. I concluded this
7 because the “payroll” document included \$81,919,357 charged to Account 926
8 (Employee Pensions & Benefits) in 2012 and \$96,280,274 charged to Account 926 in
9 2013. Based on my experience and the documentation provided by FPL, I concluded
10 that these benefit dollars are not payroll dollars. Subsequent information provided by
11 FPL in informal discovery confirmed my conclusion. FPL responded to seven of nine
12 questions on June 22, 2012. The Company’s response of most concern was that “The
13 workpapers correctly reflect that approximately 80% of FPL’s payroll is allocated to
14 O&M.” On June 25, 2012, the Company responded to a remaining question
15 regarding the O&M expense factor. The response provided an O&M amount of
16 \$740,842,090 (70.6% of total payroll). This confirmed I was correct when I
17 concluded that the O&M payroll amount in the Company’s payroll workpapers was
18 not 100% payroll dollars. In fact, the response indicates the \$847,283,848 figure
19 includes “Loaders” which generally is indicative of employee benefit costs.

20
21 **Q. ARE YOU CONVINCED THAT THE O&M FACTOR FOR 2013 IS 70.6%?**

22 A. No. There still remain too many variances in the Company’s discovery responses for
23 me to firmly conclude that the 70.6% is accurate. However, by removing the
24 \$96,280,274 shown on the Company workpaper as being charged to Account 926 in

1 2013, I calculated an O&M factor of 71.61%. This calculation is shown on Exhibit
2 No. HWS-2, Page 3 of 3, Line 14. The comparable percentages eliminated the need
3 for adjusting payroll because of what appeared to be the Company's use of an
4 excessive expense factor in the test year. However, I recommend that the
5 Commission be very cautious in relying on the level of FPL's documentation in
6 making decisions related to payroll.

7
8 **IV. INCENTIVE COMPENSATION**

9 **Q. HAVE YOU ANALYZED THE COMPANY'S INCENTIVE COMPENSATION**
10 **IN THIS CASE?**

11 A. Yes. I analyzed FPL's testimony on this issue, its incentive plans, the Commission's
12 Order for FPL's last rate case in Docket No. 080677-EI, and the responses to
13 discovery regarding payroll and incentive compensation. In this case, Company
14 Witness Slattery stated on page 14 of her direct testimony that "FPL has excluded
15 from its expense request the portions of executive and non-executive incentive
16 compensation that were excluded from the 2010 rate order, Order No. PSC-10-0153-
17 FOF." She explained that this adjustment was made in an effort to narrow the items
18 at issue in this rate case. Subsequent to the filing of testimony in this proceeding,
19 FPL filed a "Notice of Identified Adjustments" that indicated the Company had
20 inadvertently omitted from the initial filing the removal of \$.7 million associated with
21 the non-executive performance share portion of the incentive compensation
22 adjustment.

1 **Q. HAS THE COMPANY ADJUSTMENT TO REMOVE THE INCENTIVE**
2 **COMPENSATION BASED ON THE ORDER IN DOCKET NO. 086077-EI**
3 **NARROWED THE ISSUES IN THIS RATE CASE?**

4 A. To some degree, it has. However, I am still recommending an adjustment be made
5 for incentive compensation. As shown on Exhibit No. HWS-3, I am recommending
6 that the Company's 2013 O&M expense be reduced by \$22.726 million (\$22.371
7 million jurisdictional).

8

9 **Q. DID YOU REVIEW THE ADJUSTMENT MADE BY THE COMPANY?**

10 A. Yes. FPL, in determining the revenue requirement for 2012 and for the projected test
11 year 2013, removed \$36.176 million and \$28.459 million, respectively, on a
12 jurisdictional basis for executive incentive compensation. As noted above, the
13 Company has acknowledged that the adjustment was understated by \$.7 million for
14 the non-executive incentive compensation portion.

15

16 **Q. DID YOU VERIFY THE AMOUNTS TO BE ACCURATE?**

17 A. I am questioning the amounts based on my review of the work papers provided in
18 response to OPC POD No. 12 and responses to discovery. For example, the response
19 to OPC POD No. 12 indicated that the 2012 and 2013 executive incentive
20 compensation is \$42.900 million and \$44.745 million, respectively. In addition, there
21 is \$12.211 million and \$12.575 million of executive performance incentive
22 compensation in 2012 and 2013, respectively. As noted above, the respective
23 adjustments made by FPL to executive incentive compensation for 2012 and for the
24 projected 2013 test year were to remove \$36.176 million and \$28.459 million,

1 respectively. I have concerns that in 2012, the adjustment to O&M made by the
2 Company is \$36.176 million out of a total of \$55.111 million (approximately 65.6%),
3 however in the 2013 test year only \$28.459 million out of a total of \$57.320 million
4 (approximately 49.6%) is removed. The difference is significant, and I have concerns
5 whether the amount of executive incentive compensation removed from the
6 respective projected 2012 and 2013 O&M expense is correct.

7
8 I also reviewed the differences in the non-executive incentive compensation amounts.
9 The response to OPC POD No. 12 indicated the employee incentive compensation is
10 \$60.045 million and \$63.471 million for 2012 and 2013, respectively. In response to
11 FIPUG Interrogatory No. 8, the Company indicated the non-executive pay for
12 performance is \$60.8 million and \$59.0 million for 2012 and 2013, respectively. In
13 response to OPC Interrogatory No. 236, the Company indicated the forecasted non-
14 executive/non-bargaining incentive compensation for 2012 and 2013 is \$59 million
15 and \$53.7 million, respectively. There is some apparent uncertainty within the
16 Company as to the actual amount of employee incentive compensation that is
17 included in the filing.

18
19 **Q. DID YOU TRY AND RECONCILE THE DIFFERENCES?**

20 A. Yes. Upon noting some significant differences, OPC tried to schedule a meeting with
21 Company personnel to discuss the incentive differences, as well the payroll questions
22 discussed elsewhere in my testimony. After some delays, FPL said that due to the
23 complexity of the questions, it would provide written responses. When the responses
24 were provided, the answer to the question on the disparity between the two

1 adjustments was delayed until a formal response to SFHHA's Interrogatory No. 262
2 was to be provided. However, FPL indicated that the response to SFHHA's
3 Interrogatory No. 262 would not address fully OPC's request and that a written
4 response would be provided specific to OPC's request. The actual response to OPC's
5 informal request was provided on June 26, 2012. It suggests that, similar to the initial
6 \$.7 million error already identified for 2013, a second error exists for 2013 and that
7 there was a comparable adjustment in 2012 of \$7.904 million. I interpret the response
8 to indicate that the 2012 executive incentive compensation amount was not the
9 \$42.900 million as originally identified, but instead it was approximately \$57.7
10 million. That would explain the disparity with the executive incentive adjustments;
11 however, it raises a further concern as to how much reliance can be placed on the
12 amounts reflected in the filing.

13
14 **Q. EARLIER YOU NOTED THAT THE NON-EXECUTIVE INCENTIVE**
15 **COMPENSATION MISSED BY THE COMPANY IN ITS INCENTIVE**
16 **COMPENSATION ADJUSTMENT WAS \$.7 MILLION. WHY IS THAT**
17 **ADJUSTMENT SO SMALL IN COMPARISON TO THE APPROXIMATELY**
18 **\$60 MILLION YOU IDENTIFIED FOR 2012 AND FOR 2013 FOR NON-**
19 **EXEXECUTIVE INCENTIVE COMPENSATION?**

20 **A.** FPL volunteered to make the same adjustment that was made by the Commission in
21 Docket No. 080677-EI. The adjustment made in the 2010 rate order, Order No. PSC-
22 10-0153-FOF, and the adjustment made by the Company in the current filing, after
23 including the omission, appears to be consistent in the mechanics of the
24 Commission's determination. The problem, in my opinion, is that based upon my

1 review of testimony and the Commission's prior decision, I believe there was an
2 inadvertent oversight in the Commission's order regarding what should have been
3 included as part of the adjustment in that proceeding. The OPC witness' testimony
4 on that issue was entitled "Non-Executive Incentive Compensation" and the questions
5 discussed issues related to "Non-Executive Incentive Compensation" however; the
6 testimony dealt only with the non-executive long term incentive compensation. This
7 was a different plan than the more costly, general non-executive type compensation
8 plan. The Commission order also refers repeatedly to non-executive incentive
9 compensation, which suggests the Commission was also under the impression that the
10 OPC witness' recommended adjustment was similar to the executive incentive
11 compensation cost adjustment recommendation that consisted of both cash-based
12 incentives as well as stock-based incentives. Therefore, in my opinion, the non-
13 executive compensation adjustment in Docket No. 080677-EI inadvertently omitted
14 the cash-based portion of the non-executive incentive compensation when the
15 decision was made as to what should be adjusted. That is why a significant difference
16 exists when compared to the mechanics of the overall executive incentive
17 compensation adjustment. The difference on a total Company basis in Docket No.
18 080677-EI amounted to approximately \$52.966 million. The questionable amount of
19 non-executive incentive compensation in this docket, according to the response to
20 SFHHA Interrogatory No. 262, is \$59.873 million. This incentive compensation
21 includes \$53.667 million of cash incentives and \$6.205 million of Performance Dollar
22 Incentive Program costs.

1 **Q. DOES ORDER NO. PSC-10-0153-FOF FACTOR INTO YOUR**
2 **RECOMMENDATION IN THIS CASE?**

3 A. Partially. The Commission decided that 100% of executive incentive compensation
4 should be excluded from rates and “that 50 percent of the *non-executive incentive*
5 *compensation*” shall be excluded from O&M expense as unreasonable. The
6 justification for disallowing 50% (instead of the 100% disallowed for executives) was
7 that the Commission was “hesitant to conclude that one hundred percent of the non-
8 executive incentive compensation benefited only shareholders.” In my opinion, the
9 Commission was right, provided the goals are set at a level that creates a true
10 incentive to enhance performance. The adjustment I am proposing is consistent with
11 the Commission’s Order in Docket No. 080677-EI. The only difference between that
12 case and this case is that I have identified the portion of non-executive incentive
13 compensation that was not addressed in Docket No. 080677-EI.

14
15 **Q. DO YOU BELIEVE THAT ALLOWING SOME INCENTIVE**
16 **COMPENSATION IS REASONABLE?**

17 A. Yes, if certain requirements are established and met. For example, in the Progress
18 Energy Florida (PEF) rate case (Docket No. 090079-EI), I recommended full
19 disallowance, based on the fact that the plans were not designed to provide a
20 quantifiable and/or tangible benefit to rate payers. Basically, the incentive plan was
21 focused on paying added compensation for goals that were shareholder-oriented. The
22 Commission agreed with my recommendation and disallowed the entire amount
23 requested. Had the employee plan been designed in a manner that would have, in
24 fact, enhanced performance that benefited ratepayers, I would have recommended a

1 50/50 split. A properly designed employee incentive compensation plan will provide
2 enhanced performance that benefits shareholders and ratepayers equally. The cost of
3 such a plan then should be shared equally by shareholders and ratepayers. More
4 scrutiny has to be placed on executive compensation, because executives are already
5 highly compensated and the goals that are included in the executive plan are more
6 focused on shareholder returns than customers. In addition, the main purpose for an
7 incentive plan for executives is to provide a means of deducting, for tax purposes,
8 compensation that may not be deductible if paid strictly as base pay. More
9 compensation is at issue; therefore, the bar has to be set higher for any executive
10 compensation to be included in rates.

11
12 **Q. DID YOU REVIEW THE GOALS FOR THE FPL INCENTIVE**
13 **COMPENSATION PLAN?**

14 A. I did. The plan I found is borderline with regard to performance goals. During some
15 years when the goal(s) were not achieved, the goal was lowered. And, in some years
16 when a goal was achieved, the new goal was not always set at the past year's
17 achievement level. FPL has indicated that this could occur due to timing, since the
18 subsequent year's plan is established prior to completion of the current year.

19
20 **Q. WOULD YOU EXPLAIN HOW YOUR RECOMMENDATION FOR**
21 **SHARING THE NON-EXECUTIVE INCENTIVE COMPENSATION**
22 **DIFFERS FROM THE COMMISSION'S DETERMINATION IN ORDER NO.**
23 **PSC-10-0153-EI-FOF?**

1 A. The decision, as I interpret it, focused on the sharing of benefits. The Commission
 2 stated it was hesitant to conclude that the plan benefitted only shareholders. That, in
 3 my opinion, means it was evaluating the flow of benefits when the decision was made
 4 to share the cost of non-executive incentive compensation equally. As I discussed
 5 earlier, for that sharing to take place, the evidence must establish that the goals used
 6 to determine whether payment will be made must be set at a level that creates a true
 7 incentive to perform at a higher level than previously achieved. As I noted earlier,
 8 PEF's failure to set true incentive goals was the basis for my recommending a total
 9 disallowance.

10

11 **Q. IS IT POSSIBLE THAT, BECAUSE SOME OR ALL OF INCENTIVE**
 12 **COMPENSATION IS DISALLOWED FOR RATEMAKING PURPOSES,**
 13 **COMPANIES WILL SIMPLY ELIMINATE THE PLAN AND INCREASE**
 14 **BASE PAY TO ACCOUNT FOR THE DIFFERENCE?**

15 A. It is possible. The real question is whether it is probable that this change could take
 16 place. In my three decades of analyzing rate cases, this has been a fairly common
 17 response by companies. I have never seen it happen. In fact, Company Witness
 18 Slattery was asked this very question in the rebuttal phase of Docket No. 080677-EI¹:

19 Q. Would FPL need to reconsider restructuring its total compensation
 20 package *if any* incentive compensation expenses were excluded?

21 A. Yes. FPL would need to consider reallocating total compensation
 22 and benefits so as to reduce performance-based compensation
 23 programs while raising base salaries and/or other traditional fixed-
 24 cost programs. This would raise costs to customers in the long run.
 25 Doing so would also negatively affect the Company's performance
 26 and impede the ability to compete in attracting and retaining the

¹ Docket No. 080677-EI, REBUTTAL TESTIMONY & EXHIBIT OF: KATHLEEN SLATTERY; Page 21; filed August 6, 2009.

1 talent needed to deliver on commitments to customers. Penalizing
2 utilities that shift from traditional fixed-cost programs to more
3 flexible, performance-based programs would encourage inefficient
4 program design that would negatively affect performance and harm
5 customers.

6 Almost two and one-half years have passed since the decision in Docket No. 080677-
7 EI, and FPL still has an incentive compensation plan. Not only does FPL have an
8 incentive compensation plan, it has proposed to remove 100% of the executive
9 incentive plan and 50% of the Long Term non-executive incentive compensation plan
10 from the rate request to comply with the terms of the last order.

11
12 **Q. IS THERE MERIT TO THE ARGUMENT THAT PENALIZING UTILITIES**
13 **THAT SHIFT FROM TRADITIONAL FIXED-COST PROGRAMS TO MORE**
14 **FLEXIBLE PERFORMANCE-BASED PROGRAMS WOULD NEGATIVELY**
15 **AFFECT PERFORMANCE AND HARM CUSTOMERS?**

16 **A.** No. The first problem with that argument is that at this time, I am not aware of any
17 utility that does not have some form of incentive compensation plan. When I have
18 asked in the past about the implementation of the incentive plan, I have not found a
19 utility that actually shifted from the fixed-cost plan to a flexible performance-based
20 plan. I have uniformly found that no reduction in base pay occurred. That means the
21 introduction of incentive compensation was, in effect, just another form of
22 compensation offered to employees, in addition to the employees base pay. The
23 second problem is that companies will typically argue that without this plan they will
24 not be competitive and will not be able to attract and retain competent employees. In
25 my experience, I have not observed any utility eliminate its incentive compensation
26 plan. Therefore, I believe this claim has no merit. Finally, companies will argue the

1 compensation is reasonable and should be allowed based on compensation studies.

2 The compensation studies used by companies to justify the employee compensation
3 are focused on total compensation. These studies may justify the total compensation
4 paid to employees; however, to date I have not seen a study that makes a comparison
5 of the various jurisdiction-specific allowance levels for incentive compensation as
6 such is included in total compensation. Basically, the studies may provide some basis
7 for paying employees, but the studies do not make any determination as to what is
8 reasonable with regard to incentive compensation for purposes of establishing rates.

9 If one were to make a comparison of PEF's incentive compensation expense and that
10 of FPL's, one might conclude that the compensation of each of the companies was
11 reasonable. However, based on the last rate case decisions for PEF and FPL, FPL's
12 incentive compensation could be considered excessive, since more of the costs for
13 incentive compensation were allowed in FPL's rates than in PEF's. The other
14 problem with the penalty argument made by companies is that for it to be a
15 meaningful one there would have to be a pending proposal that the plan be
16 eliminated. My recommendation is not to eliminate the plan, but to limit the amount
17 to be included in rates. The issue is whether the cost of a well-conceived plan should
18 be shared by both of the benefactors of improved performance from an incentive
19 program or whether only one benefactor should pay for it. The benefits from a well-
20 conceived plan will inure to both shareholders and ratepayers, and the cost to achieve
21 the benefits that are beyond normal expectations should be shared equally.

1 **Q. IF A PLAN IS PROPERLY DEVELOPED AND ADMINISTERED, IS THERE**
2 **ANY DISPUTING THE SHARING OF THE COSTS AND BENEFITS**
3 **BETWEEN RATEPAYERS AND SHAREHOLDERS?**

4 A. No. As long as the plan is properly developed and administered with true incentive
5 type goals that focus on providing financial benefits as well as enhanced customer
6 service and reliability, the sharing of costs is appropriate. In fact, when rebutting a
7 focus on financial factors in Docket No. 080677, FPL Witness Slattery acknowledged
8 that the plan provides benefit to both shareholders and ratepayers. Ms. Slattery stated
9 that shareholders benefit from increased efficiency and productivity. Under these
10 circumstances, customers will indirectly benefit from such improvements. There
11 appears to be agreement that both may benefit if the plan is properly developed and
12 administered. That being the case, it would only be appropriate that the extra cost as
13 well as the extra benefit of the plan be shared equally.

14

15 **V. EMPLOYEE BENEFITS**

16 **Q. ARE YOU MAKING ANY RECOMMENDATION WITH RESPECT TO**
17 **EMPLOYEE BENEFITS?**

18 A. I am recommending that employee benefit expense (excluding pensions and OPEB
19 expense 2013) be reduced by \$14.992 million (\$14.771 million jurisdictional). This
20 calculation is shown on Exhibit HWS-4, Page 1. My recommendation includes
21 separate adjustments for the Company's excessive request for employees and the
22 Company's use of an excessive O&M expense factor. I have not recommended an
23 adjustment to the escalation of costs at this time; however, I am questioning the

1 escalation of benefits, excluding pensions and OPEB, on a per employee basis in
2 2012 and in the 2013 projected test year.

3
4 **Q. WHY ARE YOU QUESTIONING THE ESCALATION?**

5 A. The per employee cost for benefits, excluding pension and OPEB costs, increased
6 13.5% in 2012 and 8.6% in 2013. The increases in general appear to be high. What
7 makes the increase more of a concern is the fact that the 2011 comparable cost per
8 employee of \$12,655 was less than the 2010 cost per employee of \$13,387, which
9 was also less than the 2009 cost per employee of \$14,490. The sudden large increase
10 in cost per employee after years of declining costs raises doubts in the ratemaking
11 context and calls into question FPL's justification of these costs. This is consistent
12 with an overall problem with the reliability of the Company's estimates for the
13 various benefits. In Docket No. 080677-EI, FPL Witness Slattery stated that the
14 benefit cost would be \$198.355 million and \$231.752 million in 2010 and 2011,
15 respectively. Company Schedule C-35 shows the 2010 and 2011 actual costs to be
16 \$173.893 million and \$168.017 million, respectively. The differences are significant
17 in every cost category.

18
19 **Q. HAVE YOU MADE AN ADJUSTMENT SIMILAR TO YOUR PAYROLL**
20 **ADJUSTMENT, WHERE YOU REDUCED THE BENEFITS ON A PER**
21 **EMPLOYEE BASIS?**

22 A. Yes. The adjustment for excess employees is shown on Exhibit No. HWS-4, Page 1
23 of 2. I am recommending a reduction to Account 926 of \$4.886 million (\$4.814
24 million on a jurisdictional basis) for the benefit costs associated with the 381 unfilled

1 positions that I have recommended be disallowed from the Company's projected
2 employee complement, as discussed earlier.

3
4 **Q. WOULD YOU EXPLAIN WHY YOU CONSIDER THE COMPANY'S O&M**
5 **FACTOR FOR EMPLOYEE BENEFITS TO BE CONSIDERED EXCESSIVE?**

6 A. Yes. Exhibit No. HWS-4, Page 2 of 2 is a two-part analysis of historical and
7 projected benefits costs. The analysis on lines 1 through 18 compares the historical
8 benefits costs and distribution of benefit costs to the 2012 and 2013 costs reflected in
9 the Company's filing. The second analysis is a simple comparison of expenses using
10 different documents to verify the validity of the first analysis, and to display how the
11 amount of expense for Pensions and Benefits charged to Account 926 has varied from
12 2007 through the projected 2013. The analysis indicates that historically FPL has
13 expensed approximately 75% of benefit costs, and the current level of expense for the
14 first three months of 2012 is approximately 75%. Based on FPL's workpapers for
15 benefits and its Schedules C-4 and C-35, the 2012 and 2013 expense factors are
16 80.69% and 82.1%, respectively. I regard the projected costs and expense allocation
17 as excessive, given the historical trend and the level of construction projected by the
18 Company.

19
20 **Q. ARE YOU RECOMMENDING AN ADJUSTMENT BE MADE TO ACCOUNT**
21 **FOR THE EXCESSIVE ALLOCATION TO O&M EXPENSE?**

22 A. Yes. My adjustment is shown on Exhibit No. HWS-4, Page 1 of 2, on Lines 11
23 through 13. To avoid a possible double count I first reduced the \$130.029 million of
24 original requested benefit expense, excluding pensions and OPEB costs, by the

1 \$4.886 million associated with the excess employee request. I then multiplied the
2 adjusted remaining total benefit cost of \$152.431 million by the 2012 year-to-date
3 expense factor of 75.47% to determine a more reasonable and consistent expense
4 level of \$115.037 million. The recommended reduction to expense of \$10.106
5 million (\$9.957 million jurisdictional) is simply the difference between the adjusted
6 expense of \$125.143 million (based on 82.1% expense factor) and the \$115.037
7 million (based on the 75.47% actual 2012 expense factor). I believe this adjustment
8 addresses my concern with FPL's excessive allocation to O&M expense. It minimizes
9 the potential for over charging ratepayers for benefits due to excessive estimates, as
10 was done in Docket No. 080677-EI.

11
12 **Q. DOES THE ADJUSTMENT ALLEVIATE YOUR CONCERNS ENTIRELY?**

13 A. No. The benefits adjustment was made excluding pensions and OPEB costs, mainly
14 because those cost estimates are based on actuarial assumptions and calculations. I
15 note that in Docket No. 080677-EI, the Company estimated the 2011 pension credit to
16 be \$37.715 million; however, the actual credit was \$53.858 million. That would
17 mean the pension expense was overstated by \$16.143 million. The OPEB costs for
18 2010 and 2011 were similarly overstated. Consequently, I believe my recommended
19 adjustment is very conservative.

20
21 **VI. PAYROLL TAX EXPENSE**

22 **Q. ARE YOU RECOMMENDING AN ADJUSTMENT TO PAYROLL TAX**
23 **EXPENSE?**

1 A. Yes. Payroll taxes must be reduced to reflect the impact of any payroll adjustment.
2 Since payroll is the direct driver impacting payroll tax expense, any reduction to
3 payroll must flow through to payroll tax expense. Thus, I am recommending a
4 reduction of \$1.601 million (\$1.577 million jurisdictional) to payroll taxes to
5 correspond with my other payroll adjustments.
6

7 **Q. HOW DID YOU DETERMINE YOUR PAYROLL TAX ADJUSTMENT?**

8 A. Based on the Company's projected expense as shown on Schedule C-4 and the
9 projected payroll expense reflected on Schedule C-4, I calculated an effective payroll
10 tax rate. The effective tax rate as calculated on Exhibit HWS-5 is 6.41%. I then
11 applied that effective tax rate to my recommended adjustment to payroll expense of
12 \$24.968 million. The result is a payroll tax adjustment of \$1.604 million.
13

14 **VII. VEGETATION MANAGEMENT/HARDENING PLAN**

15 **Q. ARE YOU RECOMMENDING THAT THE 2013 PROJECTED TEST YEAR**
16 **VEGETATION MANAGEMENT/HARDENING PLAN COST BE REDUCED?**

17 A. Yes. In reviewing the Company response to Staff Interrogatory No. 235, I noted that
18 several reliability related expenses historically were below budget during the period
19 2008 through 2010. Based on my analysis, it is appropriate to make an adjustment to
20 reflect the expected and normal level of vegetation management/hardening expense.
21

22 **Q. WHAT ADJUSTMENT ARE YOU PROPOSING TO THE COMPANY'S**
23 **"PROJECTED COSTS?"**

1 A. As shown on Exhibit No. HWS-6, I am recommending a reduction of \$9.240 million
2 (\$9.236 million jurisdictional) to the Company's latest estimate for 2013. The
3 adjustment was determined by multiplying FPL's request of \$71,400,621 by the
4 budget-to-actual variance of 87.06% for the years 2008 through 2010. I then
5 subtracted the result from the amount requested.

6

7 **Q. WHY DID YOU REFER TO THE COMPANY REQUESTED AMOUNT AS A**
8 **"LATEST ESTIMATE"?**

9 A. In response to OPC Interrogatory No. 134, FPL indicated that the costs for vegetation
10 management and the hardening plan were \$76,142,406. FPL subsequently provided a
11 revision to its response to OPC Interrogatory No. 134 and reduced the amount to
12 \$71,400,621. The approximate \$4.7 million reduction was re-categorized by FPL to
13 pole inspections.

14

15 **Q. IS IT REASONABLE TO ASSUME THAT THE AMOUNT TO BE**
16 **EXPENDED IN 2013 WILL BE LESS THAN WHAT THE COMPANY**
17 **ACTUALLY EXPENDED IN 2011?**

18 A. Yes. In fact, the Company-proposed spending for 2012 is less than the actual amount
19 expended in 2011, even though more total miles are projected to be cut. Spending for
20 vegetation management can vary from year to year, depending on the condition of the
21 planned area for trimming, contractual pricing, and the actual miles trimmed. The
22 level of costs for 2013 is an estimate, because it is not known what the actual cost will
23 ultimately be. The difference between my recommendation and FPL's request is that
24 I applied a known and measurable factor to the estimate. That known and measurable

1 factor is that during the years 2008 through 2010, the Company actually spent
2 13.94% less on vegetation management and hardening than it originally estimated.
3

4 **VIII. POLE INSPECTIONS**

5 **Q. ARE YOU RECOMMENDING THAT THE 2013 PROJECTED TEST YEAR**
6 **POLE INSPECTION COSTS BE REDUCED FOR THE SAME REASON**
7 **THAT YOU RECOMMENDED THE VEGETATION MANAGEMENT/**
8 **HARDENING PLAN COST BE REDUCED?**

9 A. Yes. In my review of the Company response to Staff Interrogatory No. 235, I noted
10 that actual pole inspections expenses were below budget during the period 2008
11 through 2010.
12

13 **Q. WHAT ADJUSTMENT ARE YOU PROPOSING TO THE COMPANY'S**
14 **PROJECTED POLE INSPECTION EXPENSE?**

15 A. As shown on Exhibit No. HWS-7, I am recommending a reduction of \$2.734 million
16 (\$2.733 million jurisdictional) to FPL's latest estimate for 2013. I calculated the
17 adjustment by multiplying the Company request of \$14,014,888 by the budget-to-
18 actual variance of 80.49% for the years 2008 through 2010 and subtracting the result
19 from the amount requested.
20

21 **Q. IS IT SIMILARLY REASONABLE TO ASSUME THAT THE AMOUNT TO**
22 **BE EXPENDED IN 2013 WILL BE LESS THAN WHAT THE COMPANY**
23 **ACTUALLY EXPENDED IN 2011?**

1 A. Yes. Exhibit No. HWS-7 shows that the cost-per-pole fluctuated from 2007 through
2 2011, with 2011 being an extraordinarily high year. FPL estimated the cost for 2012
3 and 2013 at different rates, and at a rate lower than 2011. The Company-proposed
4 spending levels for both 2012 and 2013 are less than the actual amount expended in
5 2011. FPL's request for 2013 is simply an estimate. As with the vegetation
6 management estimate, the only difference between my recommendation and FPL's
7 request is my application of a known and measurable factor to the estimate. That
8 known and measurable factor is that during the years 2008 through 2010, the
9 Company actually spent 19.51% less than it originally estimated for pole inspections.

10

11 **IX. DIRECTORS AND OFFICERS LIABILITY INSURANCE**

12

13 **Q. ARE YOU RECOMMENDING AN ADJUSTMENT TO THE COST OF
14 DIRECTORS AND OFFICERS LIABILITY INSURANCE?**

15

16 A. Yes. The cost associated with acquiring Directors and Officers liability insurance
17 (DOL), while considered to be a necessary business expense by many, is in reality a
18 necessary business expense designed to protect shareholders from their past
19 decisions. DOL insurance protects shareholders from the decisions they made when
20 they hired the Company's Board of Directors and the Board of Directors in turn hired
21 the officers of the Company. The question is whether this cost that FPL has elected
22 to incur is for the benefit of shareholders and/or ratepayers, and who should be
23 responsible for the costs associated with acquiring this coverage. I am
recommending, even though shareholders are the primary beneficiary, that this
business expense be shared equally between shareholders and rate payers.

1 **Q. WHAT ADJUSTMENT ARE YOU RECOMMENDING?**

2 A. According to the response to OPC Interrogatory No. 60, FPL has included \$2,781,173
3 of expense in account 925 for DOL insurance (DOL). As shown on Exhibit HWS-8,
4 I am recommending a reduction to Account 925 of \$1.391 million (\$1.369 million
5 jurisdictional).

6
7 **Q. HAVE YOU ADDRESSED THIS ISSUE IN PREVIOUS RATE CASES IN**
8 **FLORIDA?**

9 A. Yes. I recently addressed this issue in Gulf Power Company Docket No. 110138-EI.
10 In that case, the Commission determined that the cost for DOL insurance should be
11 shared equally between shareholders and ratepayers. Prior to the Gulf Power
12 proceeding, the Commission addressed the subject on three other occasions. In the
13 Peoples Gas Company case and the Tampa Electric case², the Commission allowed
14 100% of the cost to be included in customer's rates. In those cases, the Commission
15 viewed the cost as a legitimate business expense. However, in the PEF case (Docket
16 No. 090079-EI³), the most recent of the other three, the Commission observed that
17 other jurisdictions make an adjustment for DOL insurance and that it has disallowed
18 DOL insurance in wastewater cases. The Commission in that case allowed PEF to
19 place one half the cost of DOL insurance in test year expenses.

² See Order No. PSC-09-0411-FOF-GU, page 38, issued June 9, 2009, in Docket No. O80318-GU, In re: Petition for rate increase by Peoples Gas System; and Order No. PSC-09-0283-FOF-EI, issued April 30, 2009 in Docket No. 080317-EI, In re: Petition for rate increase by Tampa Electric Company.

³ See Order No. PSC-10-0131-FOF-EI, issued March 5, 2010, in Docket No. 090079-EI, In re: Petition for increase in rates by Progress Energy Florida, Inc.

1 **Q. ARE THE GULF AND PEF DECISIONS WHY YOU ARE RECOMMENDING**
2 **AN ADJUSTMENT FOR THE COST ASSOCIATED WITH DIRECTORS**
3 **AND OFFICERS LIABILITY INSURANCE IN THIS CASE?**

4 A. To a great extent I would say yes, because I believe that the Commission recognizes
5 that, while this is a legitimate business expense, the expense is unique in that it is
6 designed primarily to protect shareholders from their past decisions.

7
8 **Q. WHAT WOULD YOUR RECOMMENDATION BE IF THE COSTS HAD**
9 **NOT BEEN DISALLOWED IN THE GULF AND PEF DOCKETS?**

10 A. Even if the costs had not been disallowed, I would continue to recommend to the
11 Commission that there be an equal sharing, because the cost associated with DOL
12 insurance benefits shareholders first and foremost. This is not an unregulated entity.
13 Certain criteria exist for recovery of costs, such as prudence and benefit. In
14 ratemaking, a prudent cost should follow the benefit. However, the reason for
15 incurring that prudent cost is often to protect shareholders from directors' and
16 officers' imprudent decision making. The benefit of this insurance clearly inures
17 primarily to shareholders; some of whom generally are the parties initiating any suit
18 against the directors and officers. The Commission's decisions on this question in
19 the Gulf Power and PEF rate case dockets were fair, and those decisions should be
20 followed in this Docket.

21

22 **X. UNCOLLECTIBLES EXPENSE**

23 **Q. ARE YOU RECOMMENDING A REVISION TO THE COMPANY'S**
24 **UNCOLLECTIBLE FACTOR OF .166%?**

1 A. No. As my schedule indicates, the uncollectible expense declined in 2010 and 2011.
2 The uncollectible rate of actual net write-offs has been declining since 2009. In
3 reviewing FPL's calculation of the uncollectible factor for this case I found it to be
4 reasonable, given the change in the economy and because 2011 was
5 uncharacteristically low. However, I am recommending that the amount included in
6 expense be reduced by \$1.76 million. The adjustment is calculated on Exhibit HWS-
7 9.

8

9 **Q. IF YOU CONSIDER THE UNCOLLECTIBLE RATE TO BE REASONABLE,**
10 **THEN WHY ARE YOU CHALLENGING THE EXPENSE THAT THE**
11 **COMPANY IS REQUESTING?**

12 A. The expense included in the Company's request is based on an uncollectible factor. It
13 is then increased by an estimated adjustment to the reserve for uncollectibles. It is the
14 estimated adjustment to the reserve with which I disagree. The uncollectible expense
15 in rates should be representative of the net write-offs expected, similar to the
16 uncollectible factor used in the revenue expansion factor.

17

18 **XI. DEPRECIATION RESERVE SURPLUS**

19 **Q. ARE YOU RECOMMENDING AN ADJUSTMENT TO THE DEPRECIATION**
20 **RESERVE SURPLUS INCLUDED IN THE COMPANY'S 2013 PROJECTED**
21 **TEST YEAR?**

22 A. Yes. The amount included in 2013 is an estimate based on the projected cost of
23 service for 2012. FPL estimated that \$525.529 million of the ordered \$894 million
24 reserve surplus amortization (credit) would be utilized in 2012. The key word is

1 estimated. The amount for 2012 is not known and measurable, and is subject to
2 change based on changes in facts and/or assumptions that were employed in the
3 forecasting of rate base, revenue and expenses for 2012. To simply assume the
4 Company is correct could result in rates being set for 2013 with no means for
5 accounting for the 2012 estimate being inaccurate. In my opinion, the Company has
6 overestimated the depreciation reserve surplus amortization requirement for 2012 by
7 overstating expenses. One fact that leads to my reservations about the accuracy of the
8 2012 estimates is that the Company estimated a need for \$139 million in 2010, yet it
9 actually utilized only \$3.847 million. FPL's estimate was off by more than 97%. In
10 2011 the Company estimated it would use \$267 million, but the actual amount
11 required was only \$186.964 million. That is a variance of 30%. Thus, if the estimate
12 for 2012 is off by 30%, the Company would have an additional \$157.7 million
13 available in 2013.

14
15 **Q. ARE THERE SOME SPECIFIC COSTS THAT YOU BELIEVE WOULD**
16 **IMPACT THE AMOUNT OF THE DEPRECIATION RESERVE SURPLUS**
17 **THAT WOULD BE REQUIRED IN 2012?**

18 A. Yes. As discussed in detail, FPL has overestimated payroll and, because it assumed
19 an even higher employee complement in 2012 than in the 2013 projected test year,
20 the amount of payroll to be adjusted is even greater than what was recommended for
21 2013. Similarly, there are other estimated costs such as tree trimming, pole
22 inspections, and uncollectible expense that are overstated, as well as employee
23 benefits and payroll taxes.

1 **Q. HAVE YOU CALCULATED ADJUSTMENTS TO THE 2012 PROJECTED**
2 **COSTS THAT WOULD RESULT IN AN INCREASED AMOUNT OF**
3 **DEPRECIATION RESERVE SURPLUS AVAILABLE TO OFFSET COSTS IN**
4 **2013?**

5 A. Yes. As shown on Exhibit No. HWS-10, I have made a comparison of the costs
6 based on actual requirements and estimated requirements as proposed by the
7 Company. I then adjusted the 2012 requirement for payroll, benefits, tree trimming
8 and pole inspections based on similar adjustments proposed by me to the 2013
9 projected test year. Based on the adjustments identified to date, the depreciation
10 reserve surplus applied as a reduction to cost of service in 2013 should be increased
11 by \$40.55 million from \$190.918 million to \$231.468 million.

12

13 **Q. THE SUM OF YOUR ADJUSTMENTS IS \$53.808 MILLION. WHY IS YOUR**
14 **ADJUSTMENT FOR ONLY \$40.55 MILLION?**

15 A. FPL's \$190.918 million figure was based on an estimated reserve surplus requirement
16 of \$174 million for 2011, and the actual in 2011 was \$187 million. Because of the
17 use of that estimate, the \$190.918 was overstated by \$13.258 million. The \$53.808
18 million less the \$13.258 results in a difference of \$40.550 million.

19

20 **Q. PLEASE EXPLAIN YOUR 2012 EMPLOYEE ADJUSTMENT FOR**
21 **PAYROLL.**

22 A. As shown on Exhibit No. HWS-10, Page 2, I reduced 2012 payroll expense by
23 \$27.517 million on a jurisdictional basis. I calculated the adjustment the same way I
24 did for the 2013 projected test year, except that I used the 2012 Company estimated

1 costs and employee counts. Also, since I have not adjusted the employee incentive
2 compensation for 2012, I did not remove that cost from the payroll dollars used to
3 calculate the average cost per employee.

4
5 **Q. WHY DIDN'T YOU MAKE AN ADJUSTMENT TO REMOVE HALF OF THE**
6 **EMPLOYEE INCENTIVE COMPENSATION, SIMILAR TO YOUR**
7 **RECOMMENDATION FOR 2013?**

8 A. Rates are being established for 2013, not 2012. My recommendation to remove half
9 of the employee incentive compensation in 2013 is based on what I believe the
10 Commission intended to do in Docket No. 080677-EI and what I have described as
11 proper rate making treatment for incentive compensation costs. I cannot make the
12 same adjustment in 2012 because rates for 2012 are based on the decision in Docket
13 No. 080677-EI, and that specific employee incentive compensation was not adjusted
14 in that order.

15
16 **Q. WHAT ADJUSTMENT ARE YOU PROPOSING TO THE COMPANY 2012**
17 **ESTIMATED COSTS FOR EMPLOYEE BENEFITS?**

18 A. On Exhibit No. HWS-10, Page 3, I calculated an adjustment of \$11.941 million
19 (\$11.763 million jurisdictional). Consistent with the methodology used to adjust the
20 2013 employee benefits excluding pension and OPEB costs, I removed the cost
21 associated with the excess employees. I then removed the cost differential between
22 FPL's use of an 80.69% expense factor and my use of the 2012 actual to date expense
23 factor of 75.47%.

24

1 **Q. WHY ARE YOU ADJUSTING THE VEGETATION MANAGEMENT/
2 HARDENING EXPENSE FOR 2012?**

3 A. The Company estimate in 2012 is just an estimate. Based on the historical trend I
4 reviewed, FPL has been consistently high with its estimates when a comparison to
5 actual is made. Therefore, I calculated a reduction to Vegetation
6 Management/Hardening expense of \$7.929 million (\$7.925 million jurisdictional) by
7 applying the historical variance rate to FPL's estimate. This calculation is shown on
8 Exhibit No. HWS-10, Page 5.

9

10 **Q. ARE YOU RECOMMENDING A SIMILAR ADJUSTMENT TO POLE
11 INSPECTION EXPENSE?**

12 A. Yes. On Exhibit No. HWS-10, Page 6, I calculated a \$2.842 million (\$2.840 million
13 jurisdictional) reduction to the Company's 2012 estimated expense of \$14.566
14 million. Consistent with the recommendation for 2013 I applied the historical
15 variance rate to FPL's estimate to determine my recommended expense level.

16

17 **Q. WHAT ADJUSTMENT IS RECOMMENDED FOR UNCOLLECTIBLE
18 EXPENSE FOR 2012?**

19 A. The uncollectible expense should be reduced by \$1.997 million. The adjustment is
20 shown on Exhibit HWS-9. I am making this recommendation because the Company
21 expense includes an amount for increasing the reserve. As discussed earlier, I do not
22 believe that that amount is appropriate in rates.

1 **Q. DOES YOUR RECOMMENDED ADJUSTMENT TO THE DERPRECIATION**
2 **RESERVE SURPLUS IMPACT RATE BASE?**

3 A. Yes. I have recommended the reserve balance as of 2012 be increased by \$40.550
4 million. The adjustment to the unamortized reserve is a reduction to rate base of
5 \$20.275 million or one-half of the additional credit not required in 2012.

6

7 **XII. WORKING CAPITAL**

8 **Q. WHAT AMOUNT OF JURISDICTIONAL WORKING CAPITAL HAS FPL**
9 **REQUESTED IN THIS RATE FILING?**

10 A. The Company's initial net jurisdictional working capital request is \$1,217,209,000,
11 which is shown on MFR B-17. The Commission's decision in Docket No. 080677-EI
12 authorized a working capital amount of \$112,121,000. The Company's current
13 requested working capital amount in this docket is nearly 10 times the amount that
14 was allowed in the last rate case.

15

16 **Q. DID THE COMPANY INDICATE IN DISCOVERY THAT THERE WOULD**
17 **BE SOME ADJUSTMENTS TO THIS AMOUNT?**

18 A. Yes, the Company indicated there was at least one error which would have a minor
19 effect on the original cash working capital request of \$1.2 billion. The Company is
20 proposing to adjust Account 228.3 – Accumulated Provision – Pension and Deferred
21 Benefits, which would increase jurisdictional working capital by approximately \$6
22 million. Incorporating the Company's adjustment when setting rates would not
23 significantly change the Company's already substantial request of \$1.2 billion for

1 working capital, which is significantly higher than what was requested and approved
2 in its last rate case.

3
4 Other Regulatory Liabilities

5 **Q. DOES THERE APPEAR TO BE A PRIMARY SOURCE FOR THIS**
6 **SIGNIFICANT INCREASE IN WORKING CAPITAL?**

7 A. Yes. On a jurisdictional basis, FPL has projected a beginning credit balance for
8 Account 254 – Other Regulatory Liabilities of \$2,058,556,000, which is reflected as a
9 reduction to working capital. In its MFRs, the Company made debit Adjustment No.
10 33 to reduce the liability by \$2,816,670,000 related to the Asset Retirement
11 Obligation ("ARO") and debit Adjustment No. 36 of \$271,004,000 for Nuclear Cost
12 Recovery, on a Florida jurisdictional basis, which brings the projected ending balance
13 of this account to \$1,029,118. Since the amounts of the adjustments were greater
14 than the beginning credit balance in the account, FPL created a debit balance for this
15 liability account, which has the effect of changing the account from a reduction in
16 working capital of approximately \$2 billion to an increase in working capital of
17 \$1,029,118,000. However, the \$2,816,670,000 pro forma adjustment to remove the
18 ARO liability exceeded the existing 13-month average liability balance in the account
19 (\$1,625,431,000) by \$1,191,239,000 as shown in the Company's response to OPC
20 Interrogatory 252. This adjustment alone accounts for the significant increase in the
21 Company's working capital request.

1 **Q. WHAT IS AN ARO?**

2 A. An ARO is a company's recognition of a liability for certain obligations associated
3 with the retirement of long-lived assets.
4

5 **Q. DO COMMISSION RULES CONTAIN SPECIFIC REQUIREMENTS**
6 **REGARDING AROs?**

7 A. Yes. Section 25-14.014, Florida Administrative Code, entitled Accounting for Asset
8 Retirement Obligations, states that under Statement of Financial Accounting
9 Standards (SFAS) 143 (Accounting Standards Codification 410), the implementation
10 of the accounting for AROs shall be revenue neutral in the rate making process.
11

12 **Q. WAS THE COMPANY ASKED TO EXPLAIN WHY THIS ADJUSTMENT**
13 **WHICH CREATED A DEBIT BALANCE IN THE WORKING CAPITAL**
14 **WAS APPROPRIATE?**

15 A. Yes. In OPC Interrogatory 252 the Company was asked "If any of those adjusted
16 balances results in a debit (or a negative balance for a liability) please explain why a
17 negative liability amount should be included as a working capital addition." The
18 Company's response stated:

19 The Commission has consistently approved FPL's use of a balance
20 sheet approach in determining the amount of working capital to include
21 in rate base. See Order No. 10306 in Docket No. 810002-EU; Order
22 No. 11437 in Docket No. 820097-EU; Order No. 13537 in Docket No.
23 830465-EI; and Order No. PSC-10-01530-FOF-EI in Docket No.
24 080677-EI. The balance sheet approach defines working capital as
25 current assets and deferred debits that are utility related and do not
26 already earn a return, less current liabilities, deferred credits and
27 operating reserves that are utility related and upon which the Company
28 does not already pay a return. Except for net overrecoveries associated
29 with FPL's cost recovery clauses, Account 254 - Other Regulatory

1 Liabilities represents current liabilities that do not already pay a return.
2 The Commission has required that FPL include net clause
3 overrecoveries in working capital consistent with Commission policy,
4 which was confirmed on page 95 of FPL's last base rate order (Order
5 No. PSC-10-01530-FOR-EI in Docket No. 080677-EI). Accordingly,
6 the balance in Account 254 is eligible for inclusion in the working
7 capital calculation as reflected on MFR-B-2.

8 As can be seen, the Company's response did not explain why this increase in working
9 capital would be appropriate for ratemaking. There is no indication that the resulting
10 debit balance in Account 254 was the result of an overrecovery and the debit balance
11 is not a current liability or a deferred credit.

12
13 **Q. HOW DOES THE LIABILITY ACCOUNT HAVE A DEBIT BALANCE?**

14 A. The Company debited Account 254 for \$2,816,670,000 related to the ARO and
15 \$271,004,000 for Nuclear Cost Recovery. The response to OPC Interrogatory No.
16 252 shows a credit balance of \$1,625,431,000 related to the ARO and \$271,004,000
17 for Nuclear Cost Recovery. There is no problem with the Nuclear Cost Recovery
18 adjustment because it results in a zero balance. However, I am questioning how one
19 can debit Account 254 for \$2,816,670,000 related to the ARO when the account has a
20 credit balance of only \$1,625,431,000. The Company needs to explain how this
21 adjustment can be considered appropriate.

22
23 **Q. WERE THERE OTHER ADJUSTMENTS TO THE COMPANY'S RATE**
24 **BASE WHICH MAY HAVE THE EFFECT OF OFFSETTING THIS**
25 **INCREASE IN WORKING CAPITAL?**

26 A. There appear to be; however, it is not clear that the result is revenue neutral, as
27 required by the Florida Administrative Code. Adjustment No. 1-ARO to plant in

1 service and Adjustments 12 and 13 to the accumulated depreciation and
 2 amortization, ARO-Decommissioning and ARO-Other, when totaled together equal
 3 the ARO adjustment made to working capital. However, there is no clear explanation
 4 of what this working capital balance represents and how it relates to other
 5 adjustments that the Company has made to Accumulated Depreciation and
 6 Amortization related to the ARO. For instance, the Company's Adjustment No. 11
 7 for \$3,078,681,000 increases the depreciation reserve associated with the provision
 8 for decommissioning costs. An illustration of the ARO adjustments is shown below,
 9 (all amounts are on a total company basis):

Commission Adj. No.	Description	Total Company Amount
1	Asset Retirement Obligation	\$ (8,562)
	Asset Retirement Obligation-	
12	Decommissioning	\$ (2,808,939)
13	Asset Retirement Obligation-Other	\$ (42,650)
33	Asset Retirement Obligation	\$ 2,860,151
		<u>\$ -</u>
11	11 Accum Prov Decommissioning Costs	\$ 3,078,681

12
 13 As can be seen above, Adjustment No. 11 decreases the depreciation reserve, which
 14 increases rate base. Therefore, the net effect of all the above adjustments is to,
 15 increase rate base, which suggests that the ARO related adjustments are not revenue
 16 neutral.

17
 18 **Q. DOES THE FACT THAT THE OTHER ADJUSTMENTS APPEAR TO**
 19 **OFFSET THE ACCOUNT 254 ARO ADJUSTMENT RESOLVE THE**

1 **CONCERN WITH THE MISMATCHING DEBIT AND CREDIT POSTED TO**
2 **ACCOUNT 254?**

3 A. No. The Company still needs to explain why there is a difference.

4
5 **Q. ARE YOU RECOMMENDING AN ADJUSTMENT AT THIS TIME?**

6 A. No, I am not. The Company's has not clearly presented an affirmative explanation
7 whether these adjustments related to the ARO are revenue neutral as required by the
8 Commission's rule. The Commission should require the Company to explain why the
9 adjustments for decommissioning and ARO were made, what they represent, how
10 they relate to one another, what the net effect on the Company's rate base is and why
11 ratepayers should pay a rate of return related to the net balance of these adjustments.

12
13 Other Accounts Receivable

14 **Q. HAS FPL PROVIDED A DETAILED ANALYSIS OF OTHER ACCOUNTS**
15 **RECEIVABLE - ACCOUNT 143 WHICH WOULD JUSTIFY THE**
16 **INCLUSION OF THIS PROJECTED BALANCE IN WORKING CAPITAL?**

17 A. No. The Company stated that it projects Account 143 – Other Accounts Receivable
18 based on the total balance, but does not project individual accounts receivable.
19 Therefore, it is not possible to analyze what the Company has included in this account
20 for working capital purposes for the projected test year.

21
22 **Q. DID THE COMPANY PROVIDE AN EXPLANATION OF EACH OF THE**
23 **BALANCES AND WHY EACH SHOULD BE INCLUDED IN WORKING**
24 **CAPITAL?**

1 A. No, it did not. The Company was asked to provide the detailed balances and a
2 description of what relationship each respective account had to service provided to
3 ratepayers in the test year ended December 31, 2013. The Company's response
4 provided detailed balances for 2011 on a 13-month average basis; however, there was
5 no explanation of how each of these balances relates to providing services to retail
6 ratepayers and why each individual balance should be included in working capital for
7 2013.

8
9 I have reviewed the account titles of each of these 2011 balances and have listed the
10 13-month averages for those accounts that do not have a title indicating that they
11 relate to providing current service to ratepayers, or those titles that indicate they are
12 unrelated to providing current customer service. Since the total 2011 balance is
13 greater than the amount the Company included in the 2013 test year, I identified the
14 balances of the accounts (lacking support for their inclusion in working capital) as a
15 percentage of the total 13-month average balance for 2011. That percentage is
16 65.10%. Applying this percentage to the 2013 test year balance of Other Accounts
17 Receivable balance, results in a reduction of \$90,116,880 on a total company basis
18 and \$88,680,327 on a jurisdictional basis. I have included my analysis of this
19 account information as Exhibit No. HWS-11.

20 FPL has failed to justify the balance and the explanation is not sufficient. The
21 balances I have identified should remain excluded from Account 143 – Other
22 Accounts Receivable.

1 Other Regulatory Assets

2 **Q. WAS THE COMPANY ASKED TO PROVIDE A BREAKDOWN AND**
3 **EXPLANATION OF PROJECTED BALANCES WHICH IT HAS INCLUDED**
4 **IN WORKING CAPITAL IN THE 2013 TEST YEAR FOR OTHER**
5 **REGULATORY ASSETS?**

6 A. Yes.

7
8 **Q. DID THE COMPANY PROVIDE A JUSTIFICATION FOR THE**
9 **PROJECTED BALANCES IT HAS INCLUDED IN OTHER REGULATORY**
10 **ASSETS?**

11 A. No. The Company's response to OPC Interrogatory 249 merely states that the
12 Commission allows the Company to follow the balance sheet approach, but it does
13 not discuss each balance in Account 182.3 – Other Regulatory Assets and why those
14 balances should be included for working capital purposes.

15
16 **Q. WHAT ADJUSTMENT ARE YOU RECOMMENDING?**

17 A. Since the Company has provided no support for these amounts, I am removing from
18 the total those account balances which do not have descriptions which indicate they
19 should be included for working capital purposes. If the Company can provide
20 appropriate explanations and documentation then I will revise my adjustment
21 accordingly. The following jurisdictional balances are those I have excluded from
22 working capital and are shown in the table below:

1	Other Regulatory Assets – Other	\$214,014,000
2	Other Regulatory Assets – Under Recovered Conservation Costs	\$ 461,000
3	Other Regulatory Assets – Under Recovered ECRC Costs	\$ 596,000
4	Other Regulatory Assets – Convertible ITC Depreciation Loss	<u>\$ 51,779,000</u>
5		
6	Total -	<u>\$266,850,000</u>
7		

8 These balances should be removed unless the Company can provide an appropriate
9 and full explanation of how they provide benefit to ratepayers and why they should be
10 included in working capital. My adjustment reduces Other Regulatory Assets by
11 \$271,365,000 and (\$266,850,000 jurisdictional).

12

13 Miscellaneous Deferred Debits

14 **Q. DID YOU ALSO REQUEST THAT THE COMPANY PROVIDE A LIST OF**
15 **MISCELLANEOUS DEFERRED DEBITS - ACCOUNT 186 AND ALSO TO**
16 **STATE WHY EACH BALANCE WAS INCLUDED IN PROJECTED**
17 **WORKING CAPITAL FOR RATE MAKING PURPOSES?**

18 A. Yes, OPC Interrogatory No. 251 requested this information.

19

20 **Q. DID THE COMPANY’S RESPONSE PROVIDE ALL OF THE REQUESTED**
21 **INFORMATION?**

22 A. No. The Company was asked to provide explanations of why each balance was
23 included in working capital. Again, the Company’s response was simply that the
24 Commission had authorized the use of the balance sheet method for calculating
25 working capital, but did not discuss the individual balances. This response is
26 inadequate. There are certain balances that do not appear to relate to provision of
27 current service to ratepayers. Furthermore, the Company’s response did not contain a

1 detailed analysis by subaccount for the test year working capital request. The
 2 response provided 13-month averages by subaccount for the years 2008 through 2011
 3 and the 13-month period through March 2012. Many of these subaccounts contained
 4 vague descriptions which do not identify them as costs necessary for providing utility
 5 service. I based this judgment on reviewing the account titles of each of the balances
 6 and identifying those that do not have a title or other description indicating that they
 7 relate to providing current service to ratepayers, as well as those titles that indicate
 8 they are unrelated to providing current customer service. The items were removed as
 9 shown below.

10
 11 **Q. WHAT ADJUSTMENT ARE YOU RECOMMENDING RELATED TO**
 12 **MISCELLANEOUS DEFERRED DEBITS?**

13 **A.** Below I have listed the following account titles and March 2012 13-month average
 14 balances which do not meet FPL's burden of proof:

15		
16	Miscellaneous Deferred Debits	\$1,417,111
17	Miscellaneous Deferred Debits-FIN48 L/T Int Rec	\$1,620,056
18	Miscellaneous Deferred Debits – LT Receivables	\$ 477,991
19	Miscellaneous Deferred Debits – GO Grain	\$ 59,089
20	Miscellaneous Deferred Debits – Contract Services	\$ 195,663
21	Miscellaneous Deferred Debits – Mitigation Banking CR Sales	\$ 77,665
22	Miscellaneous Deferred Debits – Mitigation Banking CR Sale-Phase II	<u>\$ 48,596</u>
23		
24	Total -	<u>\$3,896,171</u>
25		
26		

27 My adjustment reduces Miscellaneous Deferred Debits by \$3,896,171 (\$3,836,435
 28 jurisdictional).

29

1 **Q. WHY ARE YOU REMOVING THE MISCELLANEOUS DEFERRED DEBIT**
2 **BALANCES FROM THE MARCH 2012 13-MONTH AVERAGE?**

3 A. Since the company did not provide a comparative analysis for the test year balance, it
4 is reasonable to assume that similar items and amounts are included in the test year as
5 those I have identified above and have removed as a surrogate. FPL has failed to
6 justify the balance and the explanation is not sufficient. The balances I have identified
7 and removed should be excluded from test year working capital.

8

9 Deferred Rate Case Expense

10 **Q. SHOULD ANY OTHER ADJUSTMENTS BE MADE TO THE COMPANY'S**
11 **PROJECTED WORKING CAPITAL?**

12 A. Yes. OPC consultant Ms. Ramas is addressing the deferred rate case expense
13 component of working capital in her direct testimony.

14

15 **Q. HAVE YOU PREPARED A SUMMARY OF YOUR ADJUSTMENTS TO**
16 **WORKING CAPITAL?**

17 A. Yes, I have summarized my adjustments to working capital in the chart below:

Working Capital	Total Company	Florida Juris.	Juris. Factor
Other regulatory Assets			
Other reg. assets-other	\$ 217,480,000	\$ 214,014,000	0.984059
Other reg. assets-under recovered conservation costs	\$ 461,000	\$ 461,000	1.000000
Other reg. assets-under recovered ECRC costs	\$ 596,000	\$ 596,000	1.000000
Other reg. assets - convertible ITC Deprec. Loss	\$ 52,828,000	\$ 51,779,000	0.980140
Total regulatory assets	\$ 271,365,000	\$ 266,850,000	
Misc deferred debits	\$ 3,896,171	\$ 3,836,435	0.984668
Other Accounts Receivable	\$ 90,116,880	\$ 88,680,327	0.984059
Total reduction to working capital	\$ 365,378,051	\$ 359,366,762	

1

2

3 **XIII. STORM RECOVERY MECHANISM**

4 **Q. HAVE YOU REVIEWED THE TESTIMONY OF COMPANY WITNESS**
5 **DEWHURST REGARDING STORM COST RECOVERY?**

6 A. Yes, and I agree that FPL should not be seeking an accrual in this proceeding to
7 increase its storm reserve. Based on the response to OPC Interrogatory 229, FPL's
8 storm reserve is in excess of \$200 million. FPL Witness Dewhurst stated in his pre-
9 filed testimony that "FPL can expect to incur, on average, about \$150 million per year
10 in restoration costs." Reviewing the charges from 2008 through March 2012, the
11 Company has recorded a net of \$38.3 million that was offset by \$24.9 million of
12 earnings. On average, FPL has recorded less than \$10 million a year since the end of
13 2007. Based on my analysis, the reserve appears sufficient at this time.

14

15 **Q. IS THERE AN ISSUE WITH STORM RECOVERY IN THIS CASE?**

16 A. Yes. The Company is requesting that it be allowed to continue to recover storm costs
17 under the framework prescribed by the 2010 Rate Settlement (Settlement). Under

1 paragraph 3 of the Settlement, FPL could implement, on an interim basis without
2 Commission action, a monthly surcharge to recover current storm costs. The OPC is
3 of the opinion that, with the expiration of the settlement agreement, storm cost
4 recovery should follow past Commission practice for addressing the adequacy of
5 FPL's storm reserve and the recovery of storm costs. As noted in FPL Witness
6 Dewhurst's testimony, the Commission's past practice allows utilities to seek
7 recovery of costs that go beyond the storm reserve. That practice is sufficient to
8 protect FPL if a storm of that magnitude were to occur. Putting aside any issue of the
9 Commission's authority to approve on an automatic storm-related adjustment in the
10 absence of a stipulation of parties, to allow the automatic surcharge practice to
11 continue essentially would negate the need for a reserve that is intended to cover
12 storms that are not as financially severe as those that occurred in the 2004/2005
13 timeframe. The reserve is available to cover the costs of major storms and the
14 provision for recovery of storms that would exceed the reserve is a sufficient
15 mechanism to protect FPL if significant damage were to occur. The automatic
16 recovery mechanism that Mr. Dewhurst is requesting was one feature of a
17 multifaceted negotiation and settlement agreement. In addition to my reasons for
18 opposing it, I have been informed by OPC counsel that OPC does not consent to the
19 unilateral effort of FPL, who was one of several parties to the settlement, to seek to
20 continue this feature of the agreement beyond the expiration date.

21

22 **Q. DOES THAT CONCLUDE YOUR TESTIMONY?**

23 **A.** Yes it does.

1 BY MR. REHWINKEL:

2 Q Mr. Schultz, did you also cause to be
3 prepared 11 exhibits identified in the comprehensive
4 exhibit list as 258 through 268?

5 A I did.

6 Q Do you have any changes or corrections to
7 make to those exhibits?

8 A Yes. On Exhibit HWS-3, lines 1 and 2 have a
9 reference of "A." That, in fact, should be a "B."
10 Line 7 has a reference of "B," that should be "A." And
11 then when you go down to the source, it refers to -- or
12 reference A is company schedule C-35; it should be
13 company schedule C-1.

14 Q Do you have any other changes to your
15 schedules?

16 A That's all the changes I'm aware of.

17 Q Okay. With the changes to your exhibits, are
18 they true and correct to the best of your knowledge?

19 A Yes.

20 Q Okay. Mr. Schultz, do you have a five minute
21 or less summary of your testimony to give?

22 A I do.

23 Q Could you please give that now.

24 A Good afternoon, Commissioners. My testimony
25 addresses the appropriateness of the company's request

1 for payroll, incentive compensation, related taxes and
2 benefits, vegetation management, pole inspections, DOL
3 insurance, and uncollectibles. In addition, I address
4 the reasonableness of the depreciation reserve surplus,
5 amortization, and working capital that.

6 The company in this case, as in Docket
7 08677-EI, projected an excess of staffing level. The
8 Commission Docket 08677-EI found the request excessive
9 and reduced the company's request. However, that
10 reduced level was still higher than FPL actually
11 staffed since those rates went into effect. In fact,
12 the company, after that case, lowered the budget
13 numbers for 2010 and 2011 and still the actual results
14 were lower than the revised budget.

15 Following a method of adjustment similar to
16 that used by the Commission in Docket 08677-EI, I am
17 recommending rates be set assuming a staffing of 387
18 positions lower than FPL claims in 2013. I am also
19 recommending that nonexecutive incentive compensation
20 be reduced to a 50/50 sharing, similar to the
21 adjustment made by the Commission in Docket 08677-EI to
22 the nonexecutive stock-based performance pay.

23 My recommendation also factors in the
24 Commission precedent that incentive compensation is
25 designed to improve performance beneficial to both

1 ratepayers and shareholders and therefore the costs
2 associated with those benefits should also be shared.

3 The Commission referenced sharing of the cost
4 and benefits in that docket. This is not a
5 recommendation to eliminate incentive pay but instead
6 to have the proper sharing of the cost.

7 FPL, like many utilities, argues the
8 compensation should be allowed because salaries are
9 reasonable when compared to others. What is ignored is
10 that we are discussing utility compensation to be
11 included in rates, and those studies do not reflect any
12 adjustments made to other companies for disallowances
13 or sharing of incentive compensation. My
14 recommendation to adjust benefits and payroll taxes is
15 a follow-through adjustment to my staffing
16 recommendation except benefits are adjusted further for
17 what I believe is a reasonable O&M factor.

18 Vegetation management cost and pole
19 inspections in the current filing are projected using
20 the company budget process. Historically, the actual
21 costs have been less than budget; therefore, I am
22 recommending that the company projections be reduced
23 based upon the historical variance to better reflect
24 the true cost of the two programs.

25 My recommendation to reduce DOL insurance by

1 50 percent is consistent with the most recent Progress
2 Energy's decision and the even more recent Gulf Power
3 decision. My adjustment to uncollectibles expense
4 simply removes the reserve component included in the
5 company calculation of uncollectibles because it is an
6 amount for adjusting the reserve that is not typically
7 allowed for rate-making purposes.

8 The surplus depreciation reserve amortization
9 in 2012 and remaining for 2013 is based on an estimated
10 cost of service for 2012 that includes, at minimum,
11 excessive payroll benefits, vegetation management
12 costs, pole inspection costs, and uncollectibles. I am
13 recommending an unamortized portion to be applied to
14 2013 to be increased to account for the excess costs in
15 2012.

16 I have also recommended the reduction to
17 working capital because the company has failed to
18 provide sufficient justification, including certain
19 asset accounts. Simply stating they are utility
20 related is not sufficient.

21 The company's request for continuation of the
22 automatic storm recovery mechanism should not be
23 allowed. Mr. Dewhurst indicated that 150 million of
24 damage per year could be expected. The reserve is in
25 excess of 200 million. And the net costs recorded

1 since 2008 was 38 million, and that was almost totally
2 offset by earnings and credits. Thank you.

3 MR. REHWINKEL: Mr. Chairman, Mr. Schultz is
4 available for cross-examination.

5 CHAIRMAN BRISE: Thank you.
6 Mr. Lavia.

7 MR. LAVIA: No questions, Mr. Chairman.

8 CHAIRMAN BRISE: Mr. Saporito.

9 MR. SAPORITO: No questions, Mr. Chairman.

10 CHAIRMAN BRISE: Mr. Wiseman.

11 MR. WISEMAN: No questions.

12 CHAIRMAN BRISE: Mr. Moyle.

13 MR. MOYLE: I have just a couple.

14 CROSS-EXAMINATION

15 BY MR. MOYLE:

16 **Q You're providing testimony in part on**
17 **incentive compensation; is that right?**

18 A Yes, sir.

19 **Q As part of getting ready for your testimony,**
20 **did you ask to see the metrics or criteria by which the**
21 **incentive compensation is measured?**

22 A I did. And I think I alluded to them in
23 testimony as being borderline.

24 **Q I'm sorry?**

25 A I did review them, and I referred to them in

1 testimony --

2 Q Okay.

3 A -- in my testimony as being borderline.

4 Q Okay. And did any of those metrics include
5 financial measurements such as return on equity or
6 earnings per share, if you recall?

7 A The ones in the -- the ones that I identified
8 in the employees were not the ones specific to what you
9 just identified, but they do have to do with financial
10 as they have budget results as a measurement, capital
11 budget results, O&M budget results. Those are
12 financial measurements.

13 Q Okay. So it may not be specific to ROE or
14 earnings per share, but with respect to budget numbers,
15 I guess your testimony is it translates over into
16 financial measures; is that right?

17 A That is correct.

18 Q Okay. And your testimony, I understand
19 you're saying there should be a split, a 50/50 split
20 between shareholders and ratepayers. Is there any
21 magic to the 50/50 or could it be some other split?

22 MR. RUBIN: Mr. Chairman, I object. This is
23 friendly cross and it's gone on for a little while
24 and it's continuing to go further down that road.

25 MR. MOYLE: That's my last question. I was

1 wondering whether his 50/50 has to be 50/50 or is
2 there the ability for the Trier of Fact to make a
3 judgment that, well, maybe if it's not 50/50, it
4 should be some other split. That's the question.

5 CHAIRMAN BRISE: I'll allow the question.

6 THE WITNESS: There's no magic formula. The
7 50/50 is basically something that's been accepted
8 in different jurisdictions as -- because the
9 incentive comp provides benefits that are supposed
10 to be over and above from performance from the
11 employees, that that sharing is appropriate
12 because then ratepayers and shareholders can share
13 in the benefits and the cost. I've made
14 recommendations both, you know, for greater ones
15 in different cases but, you know, that's the
16 premise for the 50/50 really.

17 BY MR. MOYLE:

18 **Q Okay. And I guess that would just depend on**
19 **the facts of the particular case, correct?**

20 A That is correct. As my testimony states in
21 Progress Energy, I recommended 100 percent
22 disallowance.

23 **Q Okay. Thank you.**

24 MR. MOYLE: That's all I have.

25 CHAIRMAN BRISE: All right. Captain Miller.

1 CAPTAIN MILLER: I have no questions. Thank
2 you.

3 CHAIRMAN BRISE: Okay. FPL.

4 MR. RUBIN: Thank you, Mr. Chairman.

5 CROSS EXAMINATION

6 BY MR. RUBIN:

7 **Q Good afternoon, Mr. Schultz.**

8 A Good afternoon.

9 **Q My name is Ken Rubin, I represent FPL. I**
10 **don't think we met before.**

11 A No, sir, not that I'm aware of.

12 **Q Mr. Schultz, at page 2, line 9 of your**
13 **testimony, you say that you were retained, quote, to**
14 **review -- and that's your word -- to review the rate**
15 **increase requested by Florida Power & Light Company,**
16 **correct?**

17 A What line is that, sir?

18 **Q Page 2, line 9.**

19 A Yes, I see that. Yes.

20 **Q Now, would you agree with me, sir, that the**
21 **word "review" implies sort of an unbiased, analytical**
22 **approach to an issue?**

23 A I would agree with that.

24 **Q Okay. In this particular case, review was**
25 **really only the first half of your assignment; wouldn't**

1 you agree? In other words, your assignment also
2 concluded with an obligation or a request to criticize
3 or find fault with FPL's rate request, correct?

4 MR. REHWINKEL: I'm going to object to the
5 form of the question as it assumes facts not in
6 evidence.

7 MR. RUBIN: All right. I can ask the
8 question a different way.

9 CHAIRMAN BRISE: Sure, if you could restate
10 the question.

11 BY MR. RUBIN:

12 Q Mr. Schultz, were you asked to pick apart,
13 find fault with, criticize any aspect of FPL's rate
14 request?

15 A I don't recall anybody specifically directing
16 me to do that. With respect to the review, my position
17 is I take a look at a review. If the documents
18 indicate that something should be adjusted, I will
19 recommend an adjustment based upon that review.

20 Q Okay. Would you agree with me, sir, that in
21 51 pages of your prefiled testimony addressing your
22 review of this rate request, you did not have one
23 positive thing to say about FPL?

24 A I'm not going to agree with that.

25 Q Can you find for me where you said something

1 **positive about FPL?**

2 A Yes. I think the fact that I indicated that
3 their incentive comp was borderline suggests some
4 positive factor. I mean, it's not uncommon for
5 utilities to have incentive compensation plans that are
6 set at such a level that the company will always be
7 paying out an incentive, and that they don't have goals
8 that really increase the incentive to perform even at a
9 higher level than they previously have performed. So
10 that, I think, is on a positive level.

11 And if it's something that is not -- when it
12 comes to a hearing, I don't think that the -- it's my
13 experience that I'm not supposed to sit there and say,
14 yes, you did a good job at this expense, you did a good
15 job at that expense, because that would only expand the
16 record beyond what I think everybody would like to see
17 it.

18 **Q So you would agree then, I think, based upon**
19 **your last statement, that it's not your job to say you**
20 **did a good job here, you did a good job there, your job**
21 **is to find fault with what FPL did?**

22 A It's to find fault with specific areas, if I
23 can find fault.

24 **Q Okay. Your company, Larkin & Associates,**
25 **according to the resume that you've attached, has**

1 appeared as expert witnesses in over 600 regulatory
2 proceedings, correct?

3 A Yes, sir.

4 Q And by my count, your personal, partial list
5 of your utility cases -- this is you personally --
6 attached to your prefiled testimony lists approximately
7 138 cases. Does that sound about right?

8 A I've never counted them.

9 Q Okay. I did.
10 What period of time does that list cover,
11 sir?

12 A My first case I participated in was in 1976.

13 Q Okay. You've testified all around the
14 country?

15 A I've testified in different jurisdictions
16 around the country, not the entire country.

17 Q Okay. And those are reflected on your
18 resume?

19 A To the best of my knowledge.

20 Q Okay. In those cases, have you primarily
21 been retained to review -- again, your words -- the
22 operations of electric utilities?

23 A Electric, gas, water, sewer, telephone.

24 Q All right. Mr. Schultz, based upon your
25 review of all of the materials that you reviewed in

1 **this case, would you agree that FPL is a well-managed**
2 **and well-run company?**

3 A I didn't perform a management audit so I
4 can't attest to the overall management philosophy and
5 all of the practices that were done. I had a limited
6 focus as to what costs I was looking at.

7 **Q Well, if my list is accurate, your limited**
8 **focus involved criticism or finding fault with FPL on**
9 **the following subjects: Payroll and staffing, correct?**

10 A That's correct.

11 **Q Incentive compensation?**

12 A That's correct.

13 **Q Employee benefits?**

14 A That's correct.

15 **Q Payroll tax expense?**

16 A That's correct.

17 **Q Vegetation management?**

18 A That's correct.

19 **Q FPL storm hardening plan?**

20 A That's correct.

21 **Q Pole inspections?**

22 A That's correct.

23 **Q Directors and officers liability insurance?**

24 A That's correct.

25 **Q Uncollectible expense?**

1 A That's correct.

2 **Q Depreciation reserve surplus?**

3 A That's correct.

4 **Q Working capital?**

5 A That's correct.

6 **Q And storm reserve mechanism?**

7 A That's correct.

8 **Q So it sounds like you've looked at and**
9 **offered opinions on a wide variety of subjects relative**
10 **to FPL's operations; is that fair?**

11 A A few of them. I mean, there is -- I'll
12 even -- if you want to throw in another one, I looked
13 at injuries and damages and I didn't adjust that.

14 **Q Okay. So even having looked at all of those**
15 **various areas, the 12 that I mentioned, and the**
16 **injuries and damages reserve, you still don't believe**
17 **you've seen enough to be able to agree that FPL is a**
18 **well-managed and well-run company?**

19 A On an overall basis, I can't make an
20 evaluation on specific areas. If you want me to
21 address them, I can address them.

22 For instance, payroll, the company says in
23 their testimony and rebuttal testimony how they put
24 this robust budget process into place and how they
25 developed their payroll. And in doing so, they have

1 historically under-budgeted for staffing -- they have
2 over-budgeted staffing levels and had actuals that were
3 what I would consider fairly significant when you look
4 at the total cost.

5 In response to that, they tell me, well, you
6 got to look at overtime, you didn't look at the
7 overtime and weigh that in to how it is and how our
8 overtime has been over-budget on a regular basis.

9 Well, if a company is historically year after
10 year after year having a default on one where they're
11 over-budgeting and one where they're under-budgeting,
12 you would think that they would try to improve the
13 process by following what they actually do in the
14 practice of supplying energy to their customers.

15 **Q And I'm going to ask you about those things**
16 **in just a few minutes. I will get to that.**

17 **You, though, sir, by education and training**
18 **are an accountant, correct?**

19 A That's correct.

20 **Q Okay. And you've worked for the firm Larkin**
21 **& Associates since you graduated from Ferris State**
22 **College back in 1975?**

23 A That is correct.

24 **Q Okay. You've never worked for a utility?**

25 A No, sir.

1 **Q** You filed your direct testimony in this case
2 on July 2, 2012, correct?

3 A Yes, sir.

4 **Q** All right. Have you reviewed that testimony
5 before you came here today?

6 A Yes, sir.

7 **Q** All right. I assume you've also reviewed
8 FPL's rebuttal testimony that was filed July 31st of
9 2012?

10 A I reviewed the witnesses that addressed areas
11 that I addressed.

12 **Q** Let me go through and see if you've reviewed
13 these folks' testimony: Kathleen Slattery?

14 A Most definitely.

15 **Q** Okay. Mr. Hardy, George Keith Hardy?

16 A Yes, sir.

17 **Q** Terry Deason?

18 A Yes, sir.

19 **Q** Bob Barrett?

20 A Some of it.

21 **Q** Okay. Moray Dewhurst?

22 A Some of it.

23 **Q** And Kim Ousdahl?

24 A Some of it.

25 **Q** Okay. I assume you've also reviewed the

1 prefiled testimony of -- and attached exhibits -- of
2 Staff Witness Kathy Welch?

3 A No, I did not.

4 Q Okay. How about the audit report attached to
5 Ms. Welch's testimony, have you seen that?

6 A No, I did not.

7 Q All right. Have you reviewed the deposition
8 of Ms. Welch?

9 A No.

10 Q Your deposition was given July 24th of 2012.
11 Have you reviewed that transcript?

12 A Yes, I did.

13 Q All right. Let's talk about the payroll and
14 staffing issues since you do -- I think you devote
15 about half of your testimony to that, so I want to
16 spend some time on that.

17 In your deposition when you were asked
18 whether you have expertise in employee compensation
19 matters, you responded with this answer -- and it's on
20 page 38 if you want to look at it, lines 1 through 3 --
21 and I quote -- "Well, I consider myself pretty
22 knowledgeable. I have been doing this in excess of 30
23 years. And that is usually an area that I address."

24 Does that sound to be your answer?

25 A Yes, sir.

1 **Q Okay. That's the basis of your information**
2 **about the compensation systems, the fact that you've**
3 **been doing it for 30 years?**

4 MR. REHWINKEL: I'm going to object to the
5 form of the question. I think it, again, assumes
6 facts not in evidence?

7 CHAIRMAN BRISE: If you could restate the
8 question.

9 MR. REHWINKLE: He asked if he was an expert,
10 not what he looked at.

11 MR. MOYLE: Additionally, to the extent that
12 he's questioning his expert credentials, you know,
13 I think that we had a prehearing order on that,
14 they have to challenge somebody as an expert in
15 advance, and I'm not sure that they've done that
16 with respect to this witness and his expertise on
17 salary information.

18 MR. RUBIN: And, Mr. Chairman, that's not my
19 intention. This goes to weight and credibility.
20 I'm not challenging in the sense of a voir dire.

21 BY MR. RUBIN:

22 **Q Let me ask you a different question, sir. Do**
23 **you have any formal education or specialized training**
24 **in the development and analysis of employee**
25 **compensation systems?**

1 A No.

2 **Q Have you ever developed or implemented a**
3 **total compensation and benefits program that is**
4 **designed to attract and retain qualified electric**
5 **utility employees?**

6 A No.

7 **Q Have you ever developed or implemented an**
8 **incentive program designed to attract and retain**
9 **qualified electric utility employees?**

10 A No. But in all of those cases, I've reviewed
11 various incentive programs from utility to utility. As
12 far as compensation is concerned, I've analyzed -- I
13 can't even give you a guess how many compensation
14 studies by the various compensation companies that are
15 considered professionals in this field that evaluate
16 compensation. I've got a lot of familiarity with that
17 that I've developed over the 30-plus years that I've
18 been looking at compensation studies.

19 **Q All right, sir. Have you ever had to hire**
20 **and retain a staff in excess of 10,000 employees with**
21 **positions as diverse as those employed by FPL, from**
22 **engineers to linemen, nuclear operators, customer**
23 **service representative, all of the kind of employees**
24 **that are needed to run a utility the size of FPL?**

25 A No, sir.

1 Q All right. And have you ever designed or
2 implemented any programs, including benefits programs,
3 that are designed to maintain the positive morale and
4 the kind of work ethic that's needed to run a company
5 like FPL at the high levels?

6 A No, sir.

7 Q All right. Have you ever faced the daily
8 challenges of an electric utility that serves nearly
9 4.6 million customers, covers 28,000 square miles, and
10 serves customers in 35 counties?

11 A No, sir.

12 Q Have you ever performed any analyses that go
13 to the development and continuous modification of
14 benefit plans, including health insurance, pension
15 benefits, 401-K programs, disability programs, wellness
16 programs, and all of the other elements of employee
17 benefits?

18 A No, sir.

19 Q And particularly in today's competitive
20 market for qualified utility workers, are you actively
21 engaged in hiring or retaining that type of employee
22 for any clients of yours?

23 A I don't have any utility clients, so no, sir.

24 Q Okay. You yourself have never conducted any
25 compensation studies or surveys or performed any

1 **benchmarking; is that true?**

2 A I have not performed any studies or surveys.
3 I'm not clear, if you want to clarify what you mean by
4 "benchmarking."

5 **Q Benchmarking against others in the industry**
6 **to determine whether the -- I guess if you don't have**
7 **any utility clients, you wouldn't be involved in that**
8 **sort of thing. I was trying to get to whether you had**
9 **benchmarked for a utility to determine whether they**
10 **were being competitive in the market with other**
11 **utilities.**

12 A Well, that's why I was trying to get some
13 clarification.

14 **Q Yes, sir.**

15 A I mean, because what I do do when I have
16 looked at these compensation studies over the years is
17 I make a comparison of what the company's compensation
18 level is to what the studies reflect. I've looked at
19 that on specific studies within companies where the
20 company has done studies that reflect what their
21 compensation is and show on an employee-by-employee
22 basis what the studies say a comparable compensation is
23 for that position. So to the extent of doing any
24 analysis of any kind of benchmarking, I've done that.

25 **Q Okay. In reading through your testimony, it**

1 appears that you don't really have any quarrel with
2 FPL's total rewards approach, and I don't see where
3 you've actually criticized FPL's employee pay levels or
4 performance-based variable compensation plan design.

5 Is that a fair statement?

6 A That's a fair statement.

7 Q Okay. And in your work, you've seen other
8 utilities that have average compensation at levels --
9 at FPL levels, correct?

10 A Yes, sir, there is compensation. But as I
11 note in my testimony, this gets to be a very fine area
12 to be looking at because of the fact that those
13 compensation studies do not factor in what the rate
14 decisions in other jurisdictions have made and how that
15 has impacted the salary that's being reflected in those
16 studies.

17 Q Okay. And you agree, sir, that a properly
18 designed employee compensation plan will provide
19 enhanced performance that benefits customers but you
20 also feel that it benefits shareholders?

21 A I would agree.

22 Q Okay. So the issue is not whether FPL has a
23 well-conceived plan; it's basically who should pay for
24 it when we're talking about nonexecutive incentive
25 compensation?

1 A With the caveat -- I agree with that
2 statement with the caveat that I said that FPL's
3 incentive comp goals are borderline. And by that I can
4 identify the fact that some years they did increase the
5 goals, but in other years, even though they achieved a
6 certain level, the goals were below those levels, so it
7 just depended on which year you're looking at.

8 **Q Okay. You don't know of any utility that**
9 **does not have some form of incentive compensation plan,**
10 **correct?**

11 A I cannot think of an independent operating
12 utility.

13 **Q Okay. So by virtue of your suggestion that**
14 **50 percent of the costs of this nonexecutive incentive**
15 **compensation plan be borne by customers and the other**
16 **half by shareholders, you are implicitly agreeing that**
17 **the plan benefits customers, correct?**

18 A That is the premise for a 50/50 split.

19 **Q Okay.**

20 A They each receive a 50 percent benefit and
21 they each should share in the cost 50/50, yes, sir.

22 **Q Okay. Do you understand that FPL's**
23 **nonexecutive incentive comp plan is based upon meeting**
24 **goals that are focused on customer benefits, customer**
25 **service, and performance metrics, not on the financial**

1 **returns of the company?**

2 A Well, as I indicated to Mr. Moyle, that's not
3 exactly the way I see it because I also identified that
4 there were budget goals. And budget goals to me, and I
5 think anybody that does numbers in the accounting world
6 or elsewhere, are financial related.

7 Q Okay. I think you answered this question for
8 Mr. Moyle, but I want to make sure we're clear on the
9 record. Am I correct that you did not perform any kind
10 of statistical or empirical analysis to come up with
11 your suggestion of a 50/50 split on the nonexecutive
12 incentive compensation?

13 A That is correct.

14 Q Okay. Do you agree with the statement, sir,
15 that a fundamental, tentative, sound regulatory policy
16 is to provide recovery of all reasonable and necessary
17 costs incurred to provide service to customers?

18 A As long as they're prudently incurred and
19 they provide benefits to the customers.

20 Q Okay. And in this particular case, you've
21 presented no evidence, no market data, no studies, no
22 empirical data that the total compensation paid to FPL
23 employees, including the performance-based variable
24 compensation, is unnecessary or unreasonable or
25 imprudent, correct?

1 A I'm not going to totally agree with that.

2 **Q Okay.**

3 A I mean, I identified in my testimony that if
4 you compared Florida Power & Light to Progress Energy
5 and the fact that Florida Power & Light included 100
6 percent of their incentive compensation in that number
7 and Progress Energy had to exclude that because it was
8 disallowed in rates, that would suggest that -- that
9 would be to me that there is evidence that their rates
10 could be excessive.

11 **Q Are you familiar with what this Commission**
12 **has recently done on that issue in the Gulf case?**

13 A I did look at the Gulf case.

14 **Q And what was the Commission's decision in**
15 **that case?**

16 A They removed some of the employees' incentive
17 compensation.

18 **Q In this particular case, sir, you have**
19 **presented no analysis of the employment market to**
20 **determine what amount of compensation is reasonable or**
21 **necessary to attract and retain the diverse and**
22 **specialized workforce that FPL employs, correct?**

23 A That's correct.

24 **Q Okay. You have never done any study to**
25 **support your supposition that if FPL reduced its**

1 nonexecutive comp by 50 percent and did not increase
2 base or other compensation by a like amount, that they
3 would still be able to attract and retain workers,
4 correct?

5 A I did not do a study. And in reference to
6 that, that question was asked in deposition, and I
7 believe I indicated then, and I continue to believe,
8 that FP&L, if in the unlikely event decided to
9 eliminate that 50 percent from payment to the
10 employees, that they would still be able to attract and
11 retain employees.

12 Q Okay. But you've never seen any studies that
13 support that supposition or idea of yours, have you?

14 A I've never seen no study to support that.
15 But I've never seen any study to support the company's
16 suggestion that the opposite would occur.

17 Q So you have one opinion, the company has a
18 different?

19 A That's a fair statement.

20 Q Okay. Let me go back to the 50/50 split for
21 just a moment. Would it be your view that a capital
22 investment that improved a utility's productivity
23 should be shared 50/50 between customers and
24 shareholders?

25 A The investment itself?

1 **Q Yes, sir.**

2 A Or the goal?

3 **Q Yes, sir, the capital investment.**

4 A The capital investment is traditionally -- if
5 it's a prudent investment -- is deemed to be something
6 that's recoverable in rates.

7 **Q But it benefits both customers and**
8 **shareholders?**

9 A It does benefit both customers and
10 shareholders.

11 **Q Okay. You mentioned it earlier, and I said I**
12 **would come back to this, and I wanted to do that now.**
13 **From a budgeting perspective, you would agree that you**
14 **have based your entire analysis of the historical**
15 **staffing levels, I think what you may have termed**
16 **"headcount," rather than looking at specific workload**
17 **trends and requirements, correct?**

18 A That's correct. I rely on what the
19 historical trend has reflected. And I'll even refer to
20 your co-counsel's suggestion earlier today that those
21 who fail to recognize history will repeat it.

22 And if that be the case in this filing where
23 the company continues to recommend a high level of
24 budget which will never be attained, then ratepayers
25 are going to continue to pay for bodies that don't

1 exist.

2 **Q Okay. You've assumed that the payroll**
3 **budget -- well, tell me if this is correct -- that**
4 **you've assumed that the payroll budget is simply a**
5 **function of staffing levels?**

6 A It's not a function of staffing levels alone.
7 And I thought it was very interesting how Ms. Slattery
8 made that comparison in her rebuttal testimony because
9 in her rebuttal testimony, she elected to take only the
10 base and overtime and stick it in the testimony and
11 say, here is a comparison, here is what really happens.
12 That ignores other compensation like incentive comp was
13 not included in there, other pay was not included in
14 there.

15 I mean, it seems to be, you know, if you're
16 going to take the position that you have to look at the
17 whole thing, you have to look at the whole thing. You
18 can't just take the position that she did, in my
19 opinion, and take selective components that look
20 favorable.

21 **Q Okay. Well, you just mentioned**
22 **Ms. Slattery's rebuttal. You're referring to her**
23 **rebuttal testimony, I assume?**

24 A That's correct.

25 **Q All right. Do you know the variance between**

1 the projected and actual payroll costs as opposed to
2 headcount during the past ten years?

3 A That was not in her rebuttal testimony.

4 Q Okay.

5 A Her variances that she referred to was a
6 combination of base and overtime.

7 Q Okay. And what was the ten-year variance
8 that she identified in that testimony?

9 A I can look it up. I don't recall off the top
10 of my head.

11 Q Well, subject to check, an average variance
12 of less than one-third of 1 percent, does that sound
13 about right?

14 A That's possible. I'll take it subject to
15 check.

16 Q Okay. In your analysis, sir, have you
17 considered the need to sometimes rely on these less --
18 what we would call less efficient staffing models, the
19 overtime, the temporary labor, that sort of thing?

20 A Could you repeat that? I'm just not
21 following your question, I'm sorry.

22 Q Okay. In your analysis that you did
23 regarding the payroll and the requested modifications,
24 have you considered the need for a company like FPL to
25 sometimes rely on less efficient staffing models, for

1 **example, overtime, for example, hiring temporary labor**
2 **if there's no available employees to hire?**

3 A Well, I think this kind of goes back to what
4 I was saying earlier. I mean, if you historically are
5 projecting a staffing level that well exceeds what you
6 actually can fill, then maybe that's how you should do
7 your budgeting, you should budget for what you actually
8 believe you can fill and budget your overtime
9 accordingly.

10 And when it comes down to it, I actually
11 think that the company took that into consideration as
12 part of the filing because what they budgeted for
13 overtime in 2012, was comparable to what they've
14 actually been incurring. It's at a level that's very
15 comparable to that.

16 And in 2013, granted, they had a reduction in
17 the overtime budget. But that reduction also factors
18 into consideration that FP&L has recognized that
19 they're going to have a downsizing in employees, so
20 they have made a reduction to their overtime consistent
21 with their projected move in staffing, so they have a
22 direct correlation between staffing and overtime.

23 **Q And in your suggested reduction of 381**
24 **employees, sir, have you identified the types of**
25 **positions or the types of personnel that you believe**

1 are not appropriately being hired or retained by FPL?

2 A No, I have not.

3 Q Okay.

4 A That's a company decision, and how that will
5 happen -- and that's basically what's going to happen
6 when the actual results come through.

7 Q Okay. On your Exhibit HWS-2, page 2, you
8 have ten years of data there, if I remember correctly,
9 comparing total employees to authorized employee
10 numbers, correct?

11 A That's correct.

12 Q All right. And when you did your calculation
13 to come up with your variance of 3.76 percent, how much
14 of that data did you use?

15 A What variance did you refer to?

16 Q I thought in your testimony, sir, you've come
17 up with a proposed variance for headcount of
18 3.76 percent?

19 A All right. I'm sorry, I thought you said
20 3.61.

21 Q Okay. I'm sorry. Perhaps I did, I
22 apologize. But what data did you use? Did you use all
23 ten years of data that are shown on HWS-2 for that
24 calculation?

25 A No. What I did was I selected the five

1 months of 2012 that I had at the time because that was
2 the most current. It gave me the best reflection of
3 what happened. And I also thought that it played a
4 factor into being consistent with what the Commission
5 decided to do in the last decision where it was
6 recommended that a -- I believe it was a four or
7 five-year average was recommended by the OPC, and the
8 Commission decided to take a select point in time --
9 period of time -- and I believe it was the year 2007 --
10 and used that variance as it. So I was trying to be
11 more consistent with the company's -- or the
12 Commission's decision in the last docket.

13 **Q So just so we're clear on the record, you had**
14 **ten years of data available, but you choose to use just**
15 **the first five months of 2012 to come up with your**
16 **variance, correct?**

17 A Right. The other was informative. I think
18 it's very informative. And I will not deny in any way
19 that typically I would use an average. I mean, I think
20 if you're taking an average maybe for the last three
21 years, I believe that the average was actually -- would
22 be comparable to that.

23 It's 3.64 percent for 2009 through 2011 that
24 would reflect the years that have basically occurred
25 since the late rate decision when the last actual

1 information was available.

2 **Q And if you took the last ten years, which is**
3 **the data that you compiled on this chart which, I**
4 **presume, then you felt was somewhat important to put on**
5 **your chart, the number would be significantly lower,**
6 **would it not?**

7 A I would say it would be lower. I know a
8 five-year average is probably around 3 -- about
9 3.1 percent, something in that area. It depends. But
10 it also -- you know, there are some other peculiarities
11 that are going forward in this filing because the
12 company has projected a downsizing of staff.

13 And if you look at the movement over those
14 years, those years I would have a little trouble
15 utilizing because the temporary staff in those years
16 was significantly less.

17 **Q Okay. So basically it all depends on what**
18 **dataset you select, and the numbers will change**
19 **depending on how many years you choose, correct?**

20 A That's correct.

21 **Q Okay. Let's turn to the directors and**
22 **officers liability insurance for just a minute. And**
23 **just for our discussion, if I refer to it as D&O**
24 **coverage, you'll know what I'm referring to?**

25 A Most definitely.

1 **Q All right, sir. You understand that by law**
2 **companies like FPL are required to have officers and**
3 **directors, correct?**

4 A Yes, they are.

5 **Q Okay. And you agree that D&O insurance is a**
6 **legitimate business expense which benefits customers by**
7 **virtue of the fact that you again suggest a recovery of**
8 **a 50/50 split here like you did before on the incentive**
9 **compensation?**

10 A That is correct.

11 **Q Okay. However, you believe that shareholders**
12 **are the primary beneficiary of that expense, correct?**

13 A I firmly believe that, yes, sir. I've
14 analyzed directors and officers liability insurance for
15 years. And in doing so, it's usually you find that the
16 person that's suing the company is a shareholder.

17 **Q Okay. You don't think that FPL should do**
18 **away with D&O insurance, correct?**

19 A That's their choice. You know, it's their
20 choice. It's probably not a wise move, especially if
21 they don't have the confidence in their employees to
22 suggest that they won't get sued.

23 **Q Okay. And let me take that to the next step.**
24 **You have no opinion as to whether FPL or its parent**
25 **would be able to attract the type of top quality**

1 outside directors it has if it did not provide them
2 with D&O coverage, correct? You have no opinion on
3 that?

4 A I'm not sure that they wouldn't be able to
5 attract them, but I think that's assuming facts that
6 don't exist and probably would never, ever exist. I
7 mean, I don't know of a company that would say, okay,
8 we're not going to have D&O insurance, would you become
9 our officer and director.

10 Q So you have no evidence to support it one way
11 or the other?

12 A That's correct.

13 Q Okay. Describe for me the analysis or the
14 empirical data that you used or reviewed to arrive at
15 this 50/50 split.

16 A Basically it was just more on the fact that
17 who benefits from this. While I firmly believe that
18 shareholders are the major beneficiary, I think it's
19 fair to split it 50/50 at a minimum. And that has been
20 what various Commissions have concluded.

21 So that's -- you know, given the fact that
22 that's something that has been concluded here in the
23 state of Florida, I relied on the last couple of
24 decisions that made that conclusion and made that
25 recommendation consistent within.

1 Q Okay. Let me move to another area of
2 vegetation management. Sir, have you ever designed,
3 modified, or managed, or staffed a program to trim more
4 than 36,000 miles of overhead wire?

5 A No, sir.

6 Q Or for that matter, any vegetation management
7 program to trim any overhead wire?

8 A No, sir.

9 Q All right. But you are familiar from this
10 case with the fact, and maybe from prior cases, that
11 FPL's service territory requires the company to trim
12 throughout that large 28,000 square mile service
13 territory, correct?

14 A Yes, sir.

15 Q And you are familiar with the Commission's
16 requirements that FPL trim its feeders on a three-year
17 cycle and its laterals on a six-year cycle, correct?

18 A Yes, sir.

19 Q You understand that this is a continuous
20 program and process, it varies from day to day, it
21 varies depending upon the geographic location, growth
22 rates of various types of vegetation, access issues,
23 weather, all kinds of things, correct?

24 A There's a ton of variables.

25 Q Okay.

1 A I've walked the lines, I've seen it. I've
2 talked to the guys that cut the trees. I'm very
3 familiar with what's required for vegetation
4 management.

5 **Q Okay, sir. And you don't take issue with**
6 **this Commissions rules on vegetation management, the**
7 **three-year cycle, the six-year cycle, that's not part**
8 **of what you've done here, correct?**

9 A I am not taking exception with that, no, sir.

10 **Q Okay. On your exhibit HWS-6 on line 8, you**
11 **set forth the cycle over which both laterals and**
12 **feeders are to be trimmed, correct?**

13 A Yes, sir.

14 **Q All right. So if I read your exhibit**
15 **correctly, you agree that all 22,700 miles of FPL**
16 **laterals are on schedule to be cut every -- in a**
17 **six-year period of time, once in a six-year period of**
18 **time, correct?**

19 A Based upon the ups and downs and based upon
20 the representations by the company in response to data
21 requests, yes, they are on schedule to complete a
22 six-year cycle. That has yet to be completed.

23 **Q Right. And you have no reason to doubt that?**
24 **In other words, you haven't gone out and looked at the**
25 **lines and said, wow, they said they were on schedule**

1 but they're really behind? You don't have anything
2 like that, do you?

3 A No, sir.

4 Q All right. So with the lateral cycle that's
5 been approved by the Commission, FPL should trim on
6 average approximately 3,800 miles of laterals each
7 year, correct?

8 A I wouldn't go as high as 3,800.

9 Q How about 3,783? I was just trying to round
10 it. I just took 22,700 divided by six. I'm a lawyer
11 though, so I could have got it wrong.

12 A Yeah. I mean, just eyeballing it, I think
13 it's more around 3,500 or 3,583, maybe, I don't know,
14 something in that area. I don't know specifically, I
15 didn't calculate it.

16 Q Okay.

17 A As you see though, that's not what's been
18 done from the time that this new six-year lateral
19 system went into effect.

20 Q Yes, sir. But do you know where FPL was in
21 terms of the trimming schedule prior to the
22 commencement of the six-year program?

23 A No, I do not.

24 Q Okay. And you do agree that the schedule
25 that FPL is on now will allow it to comply with the

1 Commission's order to complete the trimming that's
2 required within the six years?

3 A That's my understanding, yes, sir.

4 Q All right. And in terms of the feeder miles,
5 that's the three-year cycle, correct, also reflected on
6 your exhibit?

7 A That's correct.

8 Q All right. And do you understand that FPL is
9 scheduled to trim 4,800 miles of feeders in 2013?

10 A That's correct.

11 Q Okay. You don't take any issue with that
12 projection, do you?

13 A It's a little more than a third, but it's
14 what happens -- that's not unusual.

15 Q Okay.

16 A In fact, in 2010, which would have been
17 approximately a period in time when they would have
18 been completing the first three-year cycle.

19 Q They actually trimmed more feeder miles,
20 correct?

21 A They trimmed 5,222.

22 Q Right.

23 A So it just depends on what happened in
24 previous years.

25 Q Right. All right. It's what we were talking

1 about, the variables, sometimes weather prevents
2 things, sometimes situations you have to -- you get a
3 little behind, you have to catch up, you get a little
4 ahead and then you fall behind, correct?

5 A There's all variables, yes, sir. I mean,
6 including budgets. A lot of times companies will look
7 at a budget and say, we need to save some money this
8 year so maybe we'll cut back on our trimming. That's
9 usually one of the ones that companies will cut back on
10 when money gets tight.

11 Q You don't have anything to suggest in this
12 particular case that that's what FPL has done, do you?

13 A I haven't seen anything, no. I'm just -- you
14 asked for some variables.

15 Q Yes, sir.

16 A You identified some. I just threw in another
17 one that I've found very common.

18 Q Okay. But not one that applies in this case?

19 A I can't say it does or doesn't. I just
20 didn't notice that it did.

21 Q All right. In terms of the analysis that
22 you've done here, it sounds like you don't disagree
23 that FPL should be trimming the laterals and the
24 feeders; you simply disagree with the per-mile cost
25 that it would require to do that, correct?

1 A No. What I'm disagreeing with is the total
2 cost not on a per-mile basis or whatever. I'm just
3 saying historically the company has budgeted X, they
4 spent less than that budget. And if we ignore that,
5 then you're going to have too much money in rates
6 because that's something that's historically happened.
7 And, again, as your co-counsel indicated, those who
8 ignore history are doomed to repeat it.

9 **Q Do you know what the per mile cost of**
10 **trimming has been over the last three years?**

11 A It's in our response, I believe. There is --
12 well, actually, I have that calculated there. That's
13 the farthest column on my schedule.

14 **Q Right. Go ahead. Do you have that number**
15 **there?**

16 A Oh, I didn't know if you wanted me to
17 elaborate on it. You asked me if I knew it and I said,
18 yes, it's on my schedule.

19 **Q I'm sorry. And what is that number, sir?**

20 A Well, in 2007 it was approximately \$10,000 a
21 mile; 2008 it's \$10,000 a mile; 2009 it's \$9,000 a
22 mile; and in 2010, thereafter, it was around 8,000.
23 Now, this is give or take because this is rounded just
24 to the thousands. Some of those could be 8,101, one
25 could be, you know, 8,400, and as such.

1 And this is just -- actually, I will say,
2 since you're looking for me to say something -- the
3 fact that -- on a positive note, the decreasing cost
4 per mile is a positive note for FP&L because I've seen
5 where it goes up and down because of, as you indicated
6 earlier, the variabilities that are there. There is
7 always room for improvement on the cost for doing tree
8 trimming.

9 **Q Well, thank you, Mr. Schultz. An hour in and**
10 **we got that positive comment, and I appreciate that.**
11 **Thank you, sir.**

12 **Pole inspections, I'm going to take just a**
13 **couple of minutes on pole inspections. The same kind**
14 **of predicate questions, sir, you've never designed,**
15 **modified, managed your staff to program, to inspect a**
16 **pole population of more than a million poles, correct?**

17 **A That's correct.**

18 **Q Or for that matter, any other pole**
19 **population?**

20 **A That's correct.**

21 **Q Okay. And in this particular case, you**
22 **understand that FPL is on an eight-year cycle for**
23 **inspection of its 1.1 million distribution poles,**
24 **correct?**

25 **A Yes, sir.**

1 **Q** All right. You understand that this program
2 was approved by the Commission back in 2006?

3 A Yes, sir.

4 **Q** And you don't take issue with the schedule or
5 the Commission's rule on pole inspections, correct?

6 A No, sir.

7 **Q** All right. And you understand that of that
8 1.1 million poles, 800,000 have been inspected,
9 repaired, or replaced in accordance with the
10 Commission's approved plan to date, correct?

11 A I'm not sure where you're getting 800,000
12 from. That's not the same as the numbers that I'm
13 showing.

14 **Q** What are your numbers?

15 A Well, I have 702 of actual pole inspections.

16 **Q** And that's through what date?

17 A 2011.

18 **Q** Okay. All right. Do you understand that FPL
19 remains on schedule to complete it's first eight-year
20 cycle in 2013?

21 A In 2013?

22 **Q** Yes, sir.

23 A That would be ahead of schedule, unless my
24 line numbering is wrong. If it's implemented in 2007,
25 that's only seven years.

1 **Q Okay. So you understand that the pole**
2 **inspection program will be completed when; 2014?**

3 A I would assume if it was implemented at the
4 beginning of 2007, yes, sir.

5 **Q Okay. Once again, you don't take issue with**
6 **the need to inspect, repair, or replace the poles; you**
7 **just think it should cost less?**

8 A I just think that, again, the budget number
9 has been X, the company has been under-budget, and I
10 just keep saying, you can't ignore the realities that
11 have occurred.

12 **Q Okay.**

13 A And the company should be complimented from
14 being able -- to be able to reduce the cost of
15 inspections. But the fact remains actuals below
16 budget, and I don't think you can ignore that.

17 **Q Okay. Let me just turn to one last area, the**
18 **working capital area. You agree, sir, that regulatory**
19 **assets should be included as a component of working**
20 **capital under the balance sheet approach, correct?**

21 A If they all are in fact regulatory assets,
22 yes.

23 **Q Okay. And you also agree that miscellaneous**
24 **deferred debits should be included as a component of**
25 **working capital under the balance sheet approach?**

1 A If they are found to be ratepayer related,
2 yes.

3 **Q In your testimony, you recommended various**
4 **adjustments to FPL's 2013 working capital, correct?**

5 A That's correct.

6 **Q You claimed that there was no clear**
7 **explanation of what the working capital balance**
8 **represented or how it related to company adjustments,**
9 **correct?**

10 A That's correct.

11 **Q All right. And so you recommended an**
12 **adjustment to remove regulatory assets from the test**
13 **year working capital because -- and I quote -- these**
14 **balances should be removed unless the company can**
15 **provide an appropriate and full explanation of how they**
16 **provide benefit to ratepayers and why they should be**
17 **included in working capital?**

18 A Yes, sir.

19 **Q All right. Now, did you say at the beginning**
20 **that you have not yet reviewed Kim Ousdahl's rebuttal**
21 **testimony or that you have?**

22 A I reviewed parts of it where she addressed
23 areas.

24 **Q Okay. So would you agree that Witness**
25 **Ousdahl's rebuttal testimony, specifically at pages 8**

1 to 13, provide an appropriate and full explanation of
2 how they provide benefit to ratepayers and why they
3 should be included in working capital?

4 A No, I wouldn't.

5 MR. WISEMAN: Your Honor, if I could inquire
6 what portion of the witness's testimony this area
7 of cross-examination relates to. If you could
8 clarify that, that would be helpful to understand
9 where we're going.

10 MR. RUBIN: Sure. To his section entitled
11 "Working Capital," which begins at page 39 of this
12 witness's prefiled testimony.

13 MR. WISEMAN: All right. Thank you.

14 MR. RUBIN: You're welcome.

15 MR. REHWINKLE: Mr. Rubin, can I just ask you
16 to tell me again what portion of Ms. Ousdahl's
17 testimony you reference?

18 MR. RUBIN: Sure, pages 8 through 13 of the
19 rebuttal testimony.

20 MR. REHWINKEL: Thank you.

21 MR. RUBIN: You're welcome.

22 BY MR. RUBIN:

23 Q Have you had a chance to review that or at
24 least to find it, if you need to?

25 A Well, I haven't reviewed all those -- I don't

1 have all of those pages. I have reviewed it.

2 **Q Okay.**

3 A And I can address some of it.

4 **Q Okay. But you don't believe that she**
5 **provided a sufficient explanation to respond to your**
6 **concerns?**

7 A No. In fact, one of the lines was, well, the
8 staff audited all of these numbers for one of the
9 groups of counts. And my first inclined -- you know,
10 says, well, the staff audited it, you know, there's
11 some credibility to the fact that the staff audited.
12 However, one, it doesn't tell me what's in those
13 accounts as we originally asked for. Two, just because
14 something's audited does not mean that everything that
15 is in those accounts has been evaluated and determined
16 to be reasonable. And then, three, one of those
17 accounts listed specifically says, "SAP other accounts
18 receivable non-FP&L retiree medical benefits."

19 Now if it's non-FP&L retiree benefits, I
20 would have to wonder how that can be a cost that should
21 be included in rate base for ratepayers to pay. I
22 mean, it doesn't sound like, to me, it's a rate-making
23 item that belongs there.

24 And then there were some costs where she
25 addressed -- get into another group, she addressed some

1 others, but she also indicated that a couple of the
2 costs that were in the other regulatory assets based
3 upon past Commissions shouldn't be included in there,
4 but yet they're still there.

5 **Q So are you finding fault with staff's audit**
6 **then in this case?**

7 A No, I didn't say that.

8 **Q Okay. You haven't seen the audit?**

9 A What I'm saying is the caveat that the
10 company says I don't have to explain any of these
11 numbers or anything that's in those accounts because
12 the staff audited it to me isn't sufficient because of
13 the fact, as I indicated, an audit doesn't check every
14 single dollar that's in there. And I indicated one
15 specific account that to me clearly says it's not FP&L
16 related, yet it's in there.

17 **Q Okay. Did you say at the beginning, sir, of**
18 **your testimony that you had not yet seen the staff's**
19 **audit report?**

20 A That's correct.

21 **Q Okay. So if I tell you that staff's audit**
22 **verified that the accounts were utility related and**
23 **included appropriately in working capital and concluded**
24 **with no exceptions to the working capital issues you**
25 **have raised, you would have no reason to dispute that,**

1 **would you?**

2 A As I indicated, you know, that's exactly what
3 Ms. Ousdahl said. And I pointed out specifically an
4 account that by its label suggests otherwise.

5 **Q All right.**

6 A So it raises some question.

7 **Q Thank you, sir.**

8 CHAIRMAN BRISE: All right. Staff.

9 MR. YOUNG: Mr. Chairman, in lieu of staff's
10 cross, the parties have graciously agreed that
11 what is identified as Hearing Exhibit No. 117 can
12 be moved into the record. This includes the
13 amended errata sheet --

14 CHAIRMAN BRISE: Okay. 117.

15 (Exhibit No. 117 was marked for
16 identification.)

17 MR. REHWINKLE: Mr. Young, if I could --
18 Mr. Chairman, if I could just inquire.

19 MR. YOUNG: -- with one correction.

20 MR. REHWINKEL: I think Mr. Young mentioned
21 an amended errata sheet. And that would cover the
22 one word to be inserted on line 8, page 17.

23 MR. YOUNG: Yes.

24 MR. REHWINKEL: Okay. Which would put a
25 "not" between the "should" and the "be." Thank

1 you.

2 MR. YOUNG: With that, Mr. Chairman, staff
3 has no questions.

4 CHAIRMAN BRISE: Okay. Commissions.
5 Commissioner Balbis.

6 COMMISSIONER BALBIS: Thank you,
7 Mr. Chairman. I have one or two questions for
8 this witness concerning your Exhibit HWS-2, page 2
9 of 3.

10 THE WITNESS: Yes, sir.

11 COMMISSIONER BALBIS: I just want to make
12 sure that I understand this correctly. And it
13 seems pretty self-explanatory, but I think it's
14 important.

15 So that column "Authorized," those are the
16 authorized staffing levels by this Commission
17 or --

18 THE WITNESS: No. That's what the company
19 was authorizing to be included in their budget.

20 COMMISSIONER BALBIS: Okay. And then the
21 total is how many were actually in -- how many of
22 those positions were filled?

23 THE WITNESS: That's correct.

24 COMMISSIONER BALBIS: And the percentage
25 variance obviously is the difference between those

1 two?

2 THE WITNESS: That's correct.

3 COMMISSIONER BALBIS: And in this filing, FPL
4 is requesting how many employees?

5 THE WITNESS: In 2013, they requested 10,147.

6 COMMISSIONER BALBIS: And the revenue
7 requirements associated with the 10,147 assumes
8 that 100 percent of those will be filled?

9 THE WITNESS: Yes, sir.

10 COMMISSIONER BALBIS: Are they including in
11 the O&M expense, expenses for temporary employees?

12 THE WITNESS: Included in that would -- I
13 would have to say, yes, it includes the temporary
14 because their authorized number of positions is a
15 total that reflects would be temporary as well as
16 full-time people.

17 And there's actually a shift. If you note
18 like January, February, March, the significant
19 increase in temporary compared to the previous
20 years. The company did provides updates for June
21 and July. And that number of temporaries has
22 jumped significantly, while there were reductions
23 in the other levels, so it's kind of a shifting of
24 people.

25 So, you know, it shows that, you know, they

1 have to be factoring in temporaries when they make
2 their estimates. And if they aren't classifying
3 them, so to speak, as temporaries, then they
4 recognize them as full-time equivalents
5 essentially.

6 COMMISSIONER BALBIS: Okay. So in addition
7 to the 10,147 employees, temporary labor, is FPL
8 asking for revenues associated with overtime as
9 well?

10 THE WITNESS: My understanding in looking at
11 the work papers of the company, the temporaries
12 are included in the 10,147.

13 COMMISSIONER BALBIS: Okay. But I'm talking
14 about a separate expense for overtime, is that
15 included in the O&M expenses?

16 THE WITNESS: They have -- yes, they have
17 budgeted overtime expenses, as I indicated in
18 response to FP&L's questions. There's a -- I
19 think it's a hundred and -- I have the number --
20 it's 123, I think, million or something like that
21 that's budgeted for 2012.

22 And then in 2013, it dropped down to 80 --
23 about 83 million is what they had. But that's
24 included in their expenses that they're asking
25 for.

1 COMMISSIONER BALBIS: Okay. And then I know
2 some utilities, in order to account for turnover
3 or pay reduction where you hire someone in at a
4 lower level of the position that's -- with the
5 employee that used to hold that position. Is
6 there a similar credit to the O&M expense that's
7 included in their filing such as pay reduction and
8 turnover where it's a credit that accounts for
9 turnover you normally see?

10 THE WITNESS: I did not see that in reviewing
11 work papers. I didn't see any kind of variance
12 factor being applied.

13 COMMISSIONER BALBIS: All right. Thank you.
14 That's all I had.

15 CHAIRMAN BRISE: All right. Redirect.

16 (Whereupon proceedings continued in
17 Volume 20.)

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CERTIFICATE OF REPORTER

STATE OF FLORIDA)
COUNTY OF LEON)

I, MICHELLE SUBIA, Registered Professional Reporter, certify that the foregoing proceedings were taken before me at the time and place therein designated; that my shorthand notes were thereafter translated under my supervision; and the foregoing pages, numbered 2486 through 2737, are a true and correct record of the aforesaid proceedings.

I further certify that I am not a relative, employee, attorney or counsel of any of the parties, nor am I a relative or employee of any of the parties' attorney or counsel connected with the action, nor am I financially interested in the action.

DATED this 30th day of August, 2012.



MICHELLE SUBIA
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EXPIRES JUNE 7, 2014