

FILED NOV 18, 2015  
DOCUMENT NO. 07318-15  
FPSC - COMMISSION CLERK

State of Florida



## Public Service Commission

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**-M-E-M-O-R-A-N-D-U-M-**

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**DATE:** November 20, 2015

**TO:** Office of Commission Clerk (Stauffer)

**FROM:** Division of Accounting and Finance (Barrett, Bulecza-Banks, Lester) *MCB*  
Division of Economics (Draper) *ED*  
Division of Engineering (Matthews) *MD*  
Office of the General Counsel (Brownless, Janjic, Villafrate) *ALM*

**RE:** Docket No. 150001-EI – Fuel and purchased power cost recovery clause with generating performance incentive factor.

**AGENDA:** 12/03/15 – Regular Agenda – Post Hearing Decision – Participation is Limited to Commissioners and Staff

**COMMISSIONERS ASSIGNED:** All Commissioners

**PREHEARING OFFICER:** Graham

**CRITICAL DATES:** Decision must be rendered by 12/03/15 in order to implement new fuel factors with the first billing cycle in 2016.

**SPECIAL INSTRUCTIONS:** None

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## Case Background

As part of the continuing fuel and purchased power adjustment and generating performance incentive factor clause proceedings, an administrative hearing was held on November 2-3, 2015. At the hearing, certain stipulated issues for Tampa Electric Company (TECO), Gulf Power Company (Gulf), Florida Power & Light Company (FPL), Florida Public Utilities Company (FPUC), and Duke Energy Florida, LLC. (DEF) were approved by bench decision. Although the Commission approved some stipulated issues for each of these investor-owned utilities (IOUs), testimony and other evidence was presented at the November 2-3, 2015 hearing for Issues 1D, 1E, 2B, 3B, 3K, 5B, and 6B (hedging-related issues for the generating IOUs), and also for Issues 4A and 4B, which are company-specific issues for FPUC.<sup>1</sup> TECO, Gulf, FPL, FPUC, DEF, Florida Industrial Power Users Group (FIPUG), the Office of Public Counsel (OPC), and PCS Phosphate (PCS) filed briefs on November 13, 2015.<sup>2</sup>

The Commission has jurisdiction over this subject matter pursuant to the provisions of Chapter 366, Florida Statutes (F.S.), including Sections 366.04, 366.05, and 366.06, F.S.

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<sup>1</sup>Staff notes that Issues 8-12, 19, 21, and 23 remain open for FPUC and are addressed in this memorandum as “fall-out issues” associated with Issues 4A and 4B.

<sup>2</sup>The Florida Retail Federation (FRF) filed a notice of joinder in OPC’s brief on the same date.

## Discussion of Issues

**Issue 1D:** Is it in the consumers' best interest for the utilities to continue natural gas financial hedging activities?

**Recommendation:** Yes. Staff recommends that continuation of fuel price hedging activities is in the consumers' best interest. (Lester, Barrett)

### **Position of the Parties**

**FPL:** Yes. Utilities' natural gas financial hedging programs have worked exactly as intended by the Commission and the utilities to limit the volatility of fuel costs that FPL customers pay. The intervenors have failed to demonstrate that the program should be revised or discontinued.

**DEF:** As part of effective fuel cost management, DEF believes managing fuel price volatility risk over time for a portion of its projected fuel costs is a prudent risk management practice. However, this is a policy decision for the Commission to determine.

**FPUC:** No position.

**GULF:** Yes. Future market price risk and price volatility still exists for natural gas purchases. Changes in the natural gas market have occurred and will continue to occur in the future as gas producers and consumers adapt to both regulatory and market price pressures and uncertainty. Order No. PSC-08-0667-PAA-EI provides the utilities an appropriate fuel risk management tool for use in limiting future natural gas price volatility and should be continued going forward. Gulf has demonstrated that implementation of its risk management plan has accomplished the objective of the hedging order to limit price volatility.

**TECO:** Yes. These hedging programs have worked exactly as intended by the Commission and the utilities by eliminating the volatility of fuel costs that utility customers have to pay. The Intervenor has failed to demonstrate that these programs should be revised or discontinued. Future natural gas market price risk and price volatility remain for natural gas purchases. However, should the Commission conclude that the programs should cease, it should occur prospectively, with existing hedges remaining in place to their maturities. Any cessation should remain in place until such time as the Commission orders approval of new risk management plans.

**OPC:** No. The facts and evidence adduced at the fuel clause hearing unequivocally demonstrate that it is not in the best interest of the customers for the Companies to continue natural gas financial hedging activities. Hedging is a net cost unnecessarily added to the price of fuel. Any perceived benefits received from hedging are vastly outweighed by the billions of dollars in costs paid by customers for this temporary benefit.

**FIPUG:** No. Hedging should be discontinued.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No. PCS agrees with the Office of Public Counsel. For the facts and reasons described in the testimonies of OPC witnesses Noriega and Lawton and in OPC's basic position, it is not in the best interest of the customers for the Companies to continue natural gas financial hedging activities.

**Staff Analysis:** Staff will begin its analysis of this issue by providing a background on how the Commission's policy on hedging has developed, and key actions the Commission has taken regarding the hedging programs that Florida's four largest IOUs use today. Thereafter, staff's consideration of this issue will address the key arguments the witnesses addressed, followed by staff's analysis and conclusions.

## **Background**

Financial hedging is the use of swap contracts and options to fix the price at the time the hedge instrument is executed for fuel to be delivered at a future date. Physical hedging is the use of long-term fixed price contracts with suppliers to fix the price of fuel over a period. Hedging allows utilities to manage the risk of volatile swings in the price of fuel. Prior to 2001, IOUs had carried out a small number of financial hedging transactions. In response to significant fluctuations in the price of natural gas and fuel oil during 2000 and 2001, the Commission raised issues regarding the utilities' management of fuel price risk as part of the 2001 fuel clause proceeding. The specific issues raised involved the reasonableness of hedging as a tool to manage fuel price risk and the appropriate regulatory treatment of hedging gains and losses. These issues were spun off to Docket No. 011605-EI for further investigation.

At the hearing for Docket No. 011605-EI, parties reached a settlement of all issues. By Order No. PSC-02-1484-FOF-EI ("Hedging Order"),<sup>3</sup> the Commission approved the settlement of the issues. Specifically, the settlement provided a framework that incorporated hedging activities into fuel procurement activities. For natural gas, fuel oil, and purchased power, the settlement allowed Florida's generating IOUs to charge prudently incurred hedging gains and losses to the fuel clause. The Hedging Order specified that the Commission will review each IOU's hedging activities as part of the annual fuel proceeding.

The Hedging Order required utilities to file risk management plans as part of true-up filings. The intent of this requirement was to allow the Commission and parties to the fuel docket to monitor utility hedging activities. As part of the annual final true-up filings in the fuel docket, utilities were required to state the volumes of fuel hedged, the type of hedging instruments, the average length of the term of the hedge positions, and fees associated with hedging transactions.

Although the Hedging Order allowed utilities flexibility in the development of risk management plans, the order also set forth guidelines utilities were to follow. For example, the order required that risk management plans identify the objectives of the hedging programs and the minimum quantities to be hedged. The order also required that plans provide mechanisms and controls for the proper oversight within the utility of hedging activities, as well as include the method for assessing and monitoring fuel price risk.

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<sup>3</sup>Order No. PSC-02-1484-FOF-EI, issued October 30, 2002, in Docket No. 011605-EI, *In re: Review of investor-owned electric utilities' risk management policies and procedures*.

In tandem with Docket No. 011605-EI, staff conducted a review of Internal Controls of Florida's Investor-Owned Utilities for Fuel and Wholesale Energy Transactions. This study examined the practices, procedures, controls, and policies these companies followed when purchasing fossil fuels and wholesale energy. The study period looked at data from 1998 through 2001. The study concluded that Florida IOUs had engaged in physical hedging in fuel procurement but very limited financial hedging. At the time, the IOUs had not set up the proper controls to engage in extensive financial hedging. Also, for the period studied, TECO and Gulf had little exposure to the volatility of natural gas prices.

The next time the Commission reviewed its policy on hedging was at the 2007 fuel hearing. Parties raised questions regarding the period for which the Commission was determining the prudent costs of hedging activities. The Commission deferred its decision on the prudence of 2007 hedging activity costs to 2008 in order to allow for sufficient detail and review of the matter.

Following the 2007 fuel hearing, staff initiated two audits of the IOUs hedging programs. Staff conducted a management audit that reviewed IOUs hedging programs to assess the costs and benefits realized since the Hedging Order. Staff also reviewed the IOUs accounting treatment of 2007 hedging activities to determine compliance with risk management plans filed in 2006.

The management audit assessed the current and historical strategies of the fuel procurement hedging programs within each company at that time, evaluated hedging objectives set forth in each company's risk management plan, and quantified the net costs and benefits of each company's hedging program. Specifically, staff examined the structure and performance of hedging natural gas and fuel oil through the use of physical purchases and/or financial instruments for the years 2003 through 2007. Staff collected information from each company's policies and procedures, organizational charts, risk management plans, and historical hedging transactions, and provided an analysis for each company. In June 2008, Commission staff issued a report entitled Fuel Procurement Hedging Practices of Florida's Investor-Owned Electric Utilities.

In its 2008 report, staff found that each company shared a universal goal in purchasing financial hedges for its fuel procurement; that is, to reduce the impacts of the price extremes that can occur in the natural gas and fuel markets. In their hedging activities, the companies were not attempting to speculate on price movements in the market. Rather each was working to stabilize its annual fuel costs by initializing and settling financial hedging transactions through authorized financial counterparties. The volumes of gas and fuel oil hedged would be less than the total volumes expected to be purchased. Overall, staff believed that the use of financial hedges for fuel purchases provided a benefit to utility customers.

In response to the deferral of the determination of the prudent costs in the 2007 fuel hearing, on January 31, 2008, FPL filed a petition requesting that the Commission approve FPL's proposed volatility mitigation mechanism (VMM) as an alternative to FPL's hedging program. The VMM proposal involved FPL collecting under recoveries of fuel costs over two years instead of one year, as is the current practice. On March 11, 2008, staff held a workshop to get stakeholder input on this proposal. All parties to the 2002 settlement attended.

By Order No. PSC-08-0316-PAA-EI,<sup>4</sup> the Commission clarified the Hedging Order in several areas. IOUs were required to file a Hedging Information Report by August 15<sup>th</sup> of each year. The Commission also specified that it would make a determination of prudence of hedging results for the twelve month period ending July 31<sup>st</sup> of the current year. Staff held additional workshops on June 9, 2008 and June 24, 2008, regarding FPL's VMM petition and guidelines for hedging programs. FPL withdrew its VMM petition on August 5, 2008.

Following the workshops, the Commission established guidelines for risk management plans by Order No. PSC-08-0667-PAA-EI.<sup>5</sup> The Commission noted that its approval of the proposed guidelines demonstrates the Commission's support for hedging. The Commission also determined that utility hedging programs provide benefits to customers. The guidelines clarified the timing and content of regulatory filings for hedging activities, but allowed the IOUs flexibility in creating and implementing risk management plans. Each year in the fuel clause, staff auditors review utility hedging results for the twelve month period ending July 31 of the current year. In addition, each year the Commission approves the IOUs' risk management plans for hedging transactions the utility will enter the following year and beyond.

No other hedging-related orders have been issued to-date, although on various dates since the issuance of these three orders, staff has presented hedging-related information to the Commission at Internal Affairs meetings.

Since the 1990s, natural gas-fired generation has become a large part of the generation mix for Florida IOUs, and the increasing role for natural gas is expected to continue. Natural gas prices have been volatile over the years, with significant price spikes in 2000, 2003, 2005, and 2008. Since 2008, natural gas supply has increased significantly due to shale gas production.

### **Arguments**

In direct testimony, FPL witness Yupp stated the objective of FPL's fuel price hedging is to reduce price volatility. He stated FPL does not engage in speculation and that FPL carries out its program consistent with its approved risk management plan. (TR 377-378, 398-400) Witness Yupp noted that fuel price hedging is important for FPL and its customers because FPL projects that 72 percent of the electricity it produces in 2016 will be generated with natural gas. (TR 399, 410) He further noted that hedging is not intended to reduce fuel costs. Rather, hedging is a tool to reduce the volatility of fuel rates. (TR 400) Since FPL hedges only a portion of its projected natural gas consumption, customers can benefit from falling prices affecting the unhedged portion. (TR 400-401)

In direct testimony, DEF witness McCallister stated that DEF has a structured approach to hedging, and that there are two primary objectives that DEF's hedging program seeks to achieve:

- To reduce the impacts of fuel price volatility over time.
- To provide a greater degree of fuel price certainty to its customers.

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<sup>4</sup>Order No. PSC-08-0316-PAA-EI, issued May 14, 2008, in Docket No. 080001-EI, *In re: Fuel and purchased power cost recovery clause with generating performance incentive factor.*

<sup>5</sup>Order No. PSC-08-0667-PAA-EI, issued October 8, 2008, in Docket No. 080001-EI, *In re: Fuel and purchased power cost recovery clause with generating performance incentive factor.*

(TR 465, 470, 477; EXH 116) The witness stated that DEF's hedging program targets purchasing a certain percentage of natural gas over time whether prices are high or low, which he believes is a prudent risk management practice. (TR 477, 1008, 1010; EXH 116; DEF BR 1) Additionally, the witness stated that DEF's program is executed in an environment of strong internal controls, in a non-speculative, structured manner. (TR 467, 477, 497) Furthermore, by following its Commission-approved Risk Management Plans in a non-speculative manner, DEF is not trying to "out-guess" the market in order to meet its objectives. (TR 467, 471-472; EXH 116) When cross-examined by the OPC, the witness acknowledged that the results of DEF's hedging activities for natural gas from 2002 through 2014 was a hedging loss of about \$1.2 billion, and further losses were projected for 2015. (TR 475, 499) Additionally, witness McCallister stated that by executing hedges on a regular, non-speculative manner, the company is executing hedges in different market environments over time as those markets change. (TR 478) In doing so, DEF is not estimating or forecasting whether hedging gains and losses will occur, according to witness McCallister. (TR 467; EXH 116) He acknowledged that DEF does not forecast the volatility of natural gas, and also that DEF's fuel mix is a consideration in setting fuel hedging target ranges, and noted DEF's projected fuel mix for 2016 is approximately 73 percent natural gas. (TR 476, 486, 492, 1008; EXH 116)

Witness McCallister stated that customer interests are very important in this process and that the Commission should be cognizant of this. (TR 507) He noted that the Commission's hedging program acts to serve customer interests, and not the interests of utilities. (TR 1009) He expressed ambivalence about continuing hedging if the Commission or its customers wanted to stop hedging. (TR 489-491, 1010; DEF BR 2) He cautioned, however, that without a hedging program, customers would have no protection against price swings, and could be subject to large under and over recoveries, or mid-course corrections. (TR 510)

Gulf witness Ball asserted that the objective of natural gas hedging is to "reduce the upside price risk to Gulf's customers in a volatile price market." (TR 653; Gulf BR 2, 4, 8) The witness elaborated as follows:

We do not look at gains and losses. We look at standard deviation of pricing, both hedged and unhedged, and we determine in each case that the volatility or the standard deviation of the hedged pricing for the year is lower than the standard deviation of the unhedged prices, thus basically making the case that we have reduced the volatility of pricing.

(TR 696)

He stated that Gulf's hedging program provides price stability to customers and is a protection against unanticipated dramatic price increases in the natural gas market. (TR 680; EXH 117; BR 2) Witness Ball acknowledged, however, that natural gas market conditions are far different in 2015 than in the era when hedging began. (TR 687) He also stated that weather events are "a significant driver of natural gas demand, and, as a result, natural gas prices." (TR 688; Gulf BR 5) Nonetheless, he states that Gulf has followed its Risk Management Plan for hedging, and over the long term, his Company anticipates less volatile future fuel costs because its hedging program has been utilized. (TR 669-670, 698; EXH 117; Gulf BR 3, 8) When asked about what



Gulf’s customers would face without hedging, witness Ball stated that customers would bear the full market prices with no measure of protection from price spikes, and possibly mid-course corrections due to swings in over and under recovery balances. (TR 707-708)

In direct testimony, witness Caldwell stated that TECO follows a non-speculative risk management strategy to reduce fuel price volatility and to maintain a reliable supply of fuel. TECO had hedging savings for 2014. Shale gas production increased supply and decreased prices after a sharp increase in early 2014. Fuel savings may or may not result from hedging activities. TECO’s hedging program follows a disciplined approach and does not attempt to out-guess the market. (TR 722-723, 752-754; EXH 118) Witness Caldwell noted that Florida IOUs have been employing a hedging strategy since 2002 when the Commission issued an order addressing fuel price hedging. In 2008, the Commission issued guidelines for hedging programs and found that these programs provide customer benefits by mitigating price volatility. (TR 756-759)

OPC witness Noriega testified as a fact witness for OPC, presenting testimony and exhibits that summarize the results of the hedging programs since 2002. (TR786, 790, 807; EXH 54, EXH 55) Based on the most current information available, the witness stated that natural gas hedging programs have lost approximately \$5.3 billion over the time period from 2002-2014, with additional losses projected for 2015.

**Table 1D-1  
 Results of Natural Gas Hedging<sup>6</sup>**

<b>Year</b>	<b>DUKE</b>	<b>GULF</b>	<b>TECO</b>	<b>FPL</b>	<b>TOTALS</b>
2002-2014	(\$1,267,848,634)	(\$127,278,227)	(\$381,417,733)	(\$3,516,671,769)	(\$5,293,216,363)
Est. 2015	<u>(\$215,000,000)</u>	<u>(\$44,000,000)</u>	<u>(\$40,000,000)</u>	<u>(\$490,000,000)</u>	<u>(\$789,000,000)</u>
<b>TOTAL</b>	<u><b>(\$1,482,848,634)</b></u>	<u><b>(\$171,278,227)</b></u>	<u><b>(\$421,417,733)</b></u>	<u><b>(\$4,006,671,769)</b></u>	<u><b>(\$6,082,216,363)</b></u>

Source: TR 416, 475, 686, 761; EXHs 54, 55, 105; OPC BR 32

OPC witness Lawton stated hedging programs have two types of costs: the costs of running the program (typically not large) and the opportunity costs and benefits of hedging depending on how the market prices settle compared to the hedged price. (TR 827) Using results provided by OPC witness Noriega, witness Lawton noted hedging opportunity costs, also described as hedging losses, during the period 2009 through 2014 have been large. (TR 823, 831) According to witness Lawton, customers are insulated from daily price swings in the price of natural gas because the fuel factors are set annually. The cumulative effect of price swings could result in a mid-course correction to fuel factors. (TR 828-829) Witness Lawton believed the hedging losses since 2008 should bring continuation of fuel price hedging in Florida into question and notes that losses have not offset gains. (TR 830) Witness Lawton stated that natural gas prices and price volatility have been declining. Price volatility can be measured by the standard deviation of daily, monthly, and annual prices. (TR 835)

<sup>6</sup>In its brief, OPC filed proposed findings of fact with regard to the natural gas hedging cumulative net losses and gains for each IOU for the years 2002-2014, natural gas hedging actual and projected net losses and gains for 2015, and the combined natural gas hedging historical and projected cumulative net losses and gains for the years 2002-2015. (OPC BR at 32) To the extent not reflected in this table, OPC’s proposed findings of fact are not adopted.

Witness Lawton stated that Florida IOUs hedge significant portions of their projected natural gas burn. (TR 835-836) He noted that the IOU's hedging programs are designed to reduce the variability or volatility of fuel prices and not necessarily fuel cost. (TR 837) Florida IOU hedging programs accomplish the goal of limiting price volatility. The IOUs hedge less than 100 percent of their projected gas burn. The programs are non-speculative and avoid market timing. Witness Lawton believes that Florida IOUs should reconsider their hedging programs in light of declining volatility, increased production and reserve levels, and forecasted lower prices. (TR 840-842)

Witness Lawton testified that natural gas price volatility has declined over the period 1997 through 2015. (TR 848-850) Looking at daily price movements, there are fewer days where the price change exceeds levels from \$0.25 to \$1.00. The size and frequency of price changes are lower, according to witness Lawton. (TR 853-855) However, he noted that historical price and volatility trends may not be a predictor of future trends. (TR 856)

Witness Lawton noted that natural gas reserves have increased. The Energy Information Administration (EIA) 2015 long term forecast presents increased supply and lower natural gas prices compared to the 2011 long-term forecast. (TR 858-859) Witness Lawton believes the forecasts of increased supply and slower growth in prices suggest declining price volatility. (TR 860-861)

The Commission reviewed hedging in a workshop in 2011, and no changes were made to hedging programs. (TR 862-863) Witness Lawton stated that several states have discontinued natural gas price hedging or do not allow hedging (TR 863-868) Noting EIA long-term forecasts regarding supply and price trends, he believes the natural gas markets have changed substantially and will experience lower price volatility. (TR 868)

Witness Lawton reviewed the VMM alternative to hedging that was presented by FPL in 2008. While he does not endorse the alternative, it does provide a longer period for recovering fuel cost under-recoveries. Witness Lawton concluded that natural gas markets have changed substantially since 2002 and recommended that financial hedging of natural gas prices be discontinued and that the Commission not approve the IOUs risk management plans. (TR 871-872)

In rebuttal to OPC witness Lawton, FPL witness Yupp stated that the primary purpose of hedging is to reduce price volatility. Rising prices will provide savings for customers and falling prices will incur costs. (TR 938-939) Hedging has significantly reduced the number of times FPL was outside of the 10 percent mid-course correction threshold, according to witness Yupp. (TR 940; EXH 106) Witness Yupp believed the success of FPL's hedging program should not be based on gains or losses as this would involve speculation about the direction of the market. Instead, hedging is about mitigating volatility. (TR 940-941) He noted that a hedging program should be well disciplined to avoid speculation. To discontinue the hedging program with the thought of starting it back up in the future would amount to "chasing the market." (TR 941-942)

Witness Yupp disagreed with witness Lawton's calculation of price volatility in natural gas markets from 1997 to 2015. He provided his version of the calculation and finds price volatility to be much higher, notably in 2014. (TR 943-944; EXH 57, EXH 107)

Witness Yupp agreed with witness Lawton regarding a general trend toward lower average annual volatility but he notes some large year to year swings. He noted that price volatility varies significantly year to year and cannot be reliably predicted. (TR 946-947). He further testified that volatility of natural gas prices is high relative to other traded commodities such as crude oil and relative to the volatility of the S&P 500. (TR 948-949; EXH 109)

Witness Yupp noted that prices cannot go below the variable cost of production for any extended period. He believed there are asymmetrical risks associated with price movement. Given the current relatively low natural gas prices, the direction of prices is more likely to move up than further down, making it an inappropriate time to discontinue hedging. (TR 947-949; EXH 108)

In his rebuttal testimony, DEF witness McCallister stated that DEF has no basis to disagree with OPC Lawton's belief that future natural gas prices will be stable with declining volatility, although he warned that Florida's pronounced reliance on natural gas to fuel generating plants will expose ratepayers to market swings that could be more impactful to customers if today's hedging programs are removed. (TR 1006, 1014-1016; EXH 116) He restated that DEF's projected fuel mix for 2016 is approximately 73 percent natural gas. (TR 1008) Witness McCallister added that the hedging programs are intended to serve consumer interests, and not those of the utilities that participate in the programs, and concluded by noting that he agreed with OPC witness Lawton that the Commission should periodically review its hedging policies. (TR 1006; EXH 116)

In rebuttal, Gulf's witness Ball asserted that OPC witness Lawton failed to discuss that a number of factors could impact natural gas supply and demand. (TR 1030; Gulf BR 2) He believes increased future demand in the market for natural gas could lead to increased volatility, and that existing or proposed environmental regulations could impact shale gas production, as well as decisions regarding generating mixes for utilities. (TR 1029-1030; Gulf BR 5) Although OPC presented evidence that lifetime hedging costs have outpaced hedging gains, witness Ball stated "historical data is not a reliable predictor of future events and, in this case, is not reliable evidence of the absence of future gas price volatility." (EXH 117; TR 1030) The witness believes that future price risk and price volatility still exist, and the company's risk strategy, as set forth in its Risk Management Plan is appropriate. (TR 1035; EXH 117; Gulf BR 8)

In rebuttal to OPC witness Lawton, TECO witness Caldwell opined that, if natural gas prices were rising and fuel price hedging programs were producing savings, the intervenors would not be challenging hedging. He noted that customers benefit from the decline in natural gas prices for the unhedged portions of gas consumption. (TR 1054) As part of reducing price volatility, hedging can result in lost opportunity costs when price declines below the hedged price. (TR 1055-1056)

Witness Caldwell also noted that the current abundance of shale gas may not continue to contribute to lower price trends. He reviewed the history of gas supply and prices and noted earlier periods – with offshore gas and with liquefied natural gas – when prices recovered after a period of adjustment. (TR 1056) The generation mix in Florida and nationally is moving toward more natural gas, with the replacement of coal-fired units and the aging nuclear fleet. According

to the witness, natural gas is essential during periods of high demand or supply constraint. (TR 1057)

Witness Caldwell noted that the standard deviation of market gas prices is significantly above that of hedged prices. This proves that hedging has reduced the customer's exposure to price volatility. (TR 1058) He further noted that the volatility in annual fuel cost recovery factors is reduced. According to witness Caldwell, a levelized fuel factor does not mitigate price volatility. He noted that the variance from forecasted fuel costs is reduced with hedging, thus reducing true-up amounts. (TR 1060)

### **Analysis**

This issue focuses on three, somewhat overlapping arguments: (1) the significant opportunity costs of hedging programs that IOUs incurred as part of fuel costs paid by customers; (2) whether the volatility of natural gas prices has declined to the point where hedging is no longer effective or necessary; and (3) whether conditions in the natural gas market are stable and eliminate the need for hedging.

#### ***Opportunity Costs and Savings***

In their briefs, the intervenors argued that hedging should be discontinued due to the large cumulative net losses.<sup>7</sup> (OPC BR 3, 7-8; PCS BR 1, 4; FIPUG BR 4) In their brief, the IOUs state the purpose of hedging is to reduce price volatility, that gains and losses can occur, and that assessing the hedging programs based on gains and losses would encourage speculation. (FPL BR 8; Gulf BR 2-3; TECO BR 5)

The IOU witnesses acknowledged significant net cumulative hedging losses for natural gas. FPL had losses of \$3.5 billion for the period 2002 to 2014 for natural gas (\$3.162 billion when fuel oil hedging gains are included) and \$490 million for 2015. (TR 415-416) DEF incurred \$1.2 billion in losses for the period 2002 to 2014 and estimates \$196 million in losses for 2015. (TR 474-475) Gulf Power incurred \$127 million in losses from 2002 to 2014 and estimates \$44 million for 2015. (TR 686) Tampa Electric incurred losses of \$381 million for the period 2002 to 2014 and estimates \$40 million for 2015. (TR 761) FPL's recently approved Woodford project is estimated to experience hedging losses for 2015. (TR 423-24) OPC witness Lawton notes that prolonged periods of losses should signal a re-evaluation of hedging programs. (TR 830; also EXH 121)

There have been earlier periods before 2008 when gains offset losses. (TR 975-977; EXHs 55, 115, 116, 117, 118) Customers also benefit from falling prices for the unhedged portion of the gas supply portfolio. (TR 439-440, 768)

The IOU witnesses stated that the goal of their hedging program is to reduce volatility. (TR 938-939, 1008, 1028, 1055-1056, 1058-1059) Witness Yupp noted that gains and losses should not be used to judge the success of the program and that the Commission-approved hedging guidelines provide reasonable tradeoffs for mitigating volatility. (TR 442-443, 975)

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<sup>7</sup>The Florida Retail Federation filed a Notice of Joinder in the Citizens Post-Hearing Statement of Positions and Post-Hearing Brief.

Staff believes the level of opportunity savings and costs – hedging gains and losses – should not be a chief consideration in deciding whether to continue fuel price hedging. When gas prices are falling, losses will occur. Conversely, when gas prices are rising, gains will occur. The main objective of IOU hedging programs is to reduce the customer’s exposure to fuel price volatility, not to reduce fuel costs. Therefore, these programs should be well disciplined to accomplish this objective and to be non-speculative.

As emphasized by intervenors, the cumulative losses are currently large. These losses took place in an environment of steadily falling natural gas prices. Customers experienced the benefits of this downward trend in prices for the unhedged portions of the IOU natural gas purchases. Should natural gas prices trend or spike upward, hedging savings will occur but, overall, fuel costs will increase.

### ***Natural Gas Price Volatility***

OPC witness Lawton argued that price volatility has decreased, making hedging unnecessary. (TR 835, 848-850) The IOUs do not forecast price volatility. (TR 417, 476) While FPL witness Yupp does not agree that price volatility is trending downward, DEF witness McAllister agreed that prices are less volatile. (TR 417-418, 476) Gulf witness Ball stated that Gulf does not forecast price volatility and suggests such a forecast is not possible. He notes – with exceptions – that in recent history volatility is lower. (TR 688-689) Witness Caldwell agreed that fuel price volatility decreased during the period 1997 to 2015. (TR 763)

Witness Yupp disagreed that the volatility of natural gas prices is currently decreasing. (TR 417) He provided an exhibit showing that the volatility of natural gas prices varies considerably year to year. The trend line for this volatility shows a decline but there is very low correlation for the yearly data. The trend line in price volatility is not a good predictor of the next price volatility point. (TR 943-946, 953, 969-971; EXH 107, EXH 130)

Witness Yupp provided evidence that hedging has reduced the number of times FPL was outside of the 10 percent mid-course correction threshold. (TR 939-940, EXH 106) He acknowledges that both under-recoveries and over-recoveries of fuel costs occurred. (TR 962-963)

Witness Lawton acknowledged that current EIA forecasts for natural gas prices show a confidence interval ranging more toward higher prices than lower prices. (TR 888-890; EXH 126) Witnesses Ball affirmed this aspect of the forecast as well. (TR 1031)

In its brief, OPC argued that the annual fuel factor smoothes out price volatility and is a cost-free alternative to hedging. (OPC BR 11, see also PCS BR 4) Witness Lawton stated that the annual or level fuel factor shields customers from day-to-day changes in market prices. He acknowledges the cumulative effect of unexpected changes in market prices could lead to a mid-course correction to fuel factors. (TR 828-829) Witness McAllister agreed that the level fuel factor can reduce the customer’s exposure to price volatility within the year, assuming no mid-course correction. However, without hedging, the true-up amounts can be significant. (TR 509-510) Witness Caldwell testified that, while the annual fuel factor provides some smoothing over twelve months, it does not limit the potential for fuel costs to increase or decrease. Hedging can

limit potential changes in fuel costs and mitigates price and fuel factor volatility. (TR 1058-1060) Spreading an under-recovery over more time presents a risk of stacking under-recoveries if prices rise. (TR 1067-1068)

The level or annual factor has some smoothing effect within the year assuming no mid-course corrections. By providing certainty to a portion of expected gas consumption, hedging can reduce true-up amounts and mid-course corrections. Without hedging, large true-up amounts and deferrals could occur.

All witnesses generally agree that price volatility cannot be accurately and consistently forecasted. Staff concludes that price volatility varies up and down significantly and that it cannot be forecasted. Therefore, while natural gas prices have trended downward in the last few years, the level of price volatility is uncertain. Witness Yupp noted that a one cent change in natural gas prices translates to \$6 million for FPL. (TR 981-982) Further, the increased dependence on natural gas means customers would have significant exposure to the uncertainties of natural gas prices if hedging were discontinued.

The objective of the IOUs' hedging programs is to reduce the customers' exposure to price volatility. Staff concludes that, while natural gas prices have recently trended downward, the volatility of those prices can vary considerably and can have a significant effect on the IOUs' total fuel cost.

Currently, natural gas prices are low compared to prices since 2008. One could reasonably assume that prices are more likely to rise than to continue downward, and FPL witness Yupp provides calculations, reasons, and an opinion supporting this possibility. That prices may be approaching or going below the variable cost of production is a noteworthy consideration. However, staff believes the low prices and possible price direction should not be a chief consideration since it would involve some degree of speculation about the future direction of prices.

### ***Natural Gas Market Conditions***

Intertwined with price volatility are the supply and demand conditions of the natural gas market. All witnesses agreed that natural gas market conditions in 2015 are different from those of 2002. All witnesses agreed that the growth of shale gas production has increased the supply of natural gas. (TR 416-417, 475, 687, 958) Witness Caldwell notes that the natural gas market seems to move in cycles of significant production increases, due to new sources, followed by increases in demand (TR 762, 1056)

Natural gas prices are more volatile when weather events affect supply or demand. In January 2014, the polar vortex had a significant effect on natural gas prices. (TR 688, 848, 883) Weather events, such as very cold periods during the winter, can increase demand, prices, and volatility. (TR 883-884, 953) Additional pipelines under construction that connect the Marcellus Shale to northeastern states may diminish this effect. (TR 884)

Regarding shale gas production and the current abundant supply of natural gas, witness Yupp noted that the market price may be below the cost of production for many producers. The market

price cannot be below the cost of production for any extended period of time. He further noted that production costs vary among producers. (TR 421-422) Rig counts are down and this could impact gas supply but this may not be a complete indicator of future gas production. (TR 882; EXHs 81, 88, 96, 102) Witness Ball alluded to future events that could disrupt shale gas production. (TR 1029-1031) As noted above, witness Lawton testified to increases in gas reserves, suggesting an adequate supply for the future. (TR 857)

In its brief, OPC minimized the potential threats to shale gas production. (OPC BR 12) Witness Lawton opined that environmental concerns have largely been put to rest. He acknowledged that New York currently bans fracking. (TR 908-909) Staff notes there are specific risks associated with shale gas production. (TR 769, 1029; EXHs 81, 88, 96, 102) These risks include more Federal and State regulations for hydraulic fracturing, which is used for shale gas production.

Demand for natural gas, particularly for electric generation, is increasing. In Florida, natural gas represents a significant percentage of the fuel for generation and this dependence on natural gas is increasing. In 2016, DEF estimates 73 percent of its generation will be from natural gas. FPL estimates 72 percent. For Tampa Electric and Gulf, the figures are 52 percent and 44 percent, respectively. (TR 489, 677, 734, 772, 901, 981, 1008, 1057; EXHs 12-14, 24, 42, 47) In addition, natural gas will begin to be exported in late 2015 and a number of export terminals are under construction or are planned. (TR 383-384, 486-486; EXHs 81, 88, 96, 102)

### **Conclusion**

Staff believes the decision of whether to continue fuel price hedging rests with what one expects price volatility and natural gas market conditions to do in the future. Staff believes, while natural gas prices have trended down, price volatility is uncertain and cannot be reliably forecasted. What is known is that, without hedging, customers have very significant exposure to natural gas price volatility.

Regarding market conditions, the natural gas market is very dynamic. While prices have trended lower and gas supply is currently forecasted to be abundant, demand is increasing and is heavily influenced by weather and potentially uncertain supply conditions.

As such, staff believes that continuation of fuel price hedging activities is in the consumers' best interest.

**Issue 1E:** What changes, if any, should be made to the manner in which electric utilities conduct their natural gas financial hedging activities?

**Recommendation:** No changes are warranted at this time to the manner in which electric utilities conduct their natural gas financial hedging activities. (Barrett)

**Position of the Parties**

**FPL:** No changes should be made to the manner in which electric utilities currently conduct their natural gas financial hedging activities.

**DEF:** This is a policy decision for the Commission. If the Commission determines that hedging should be wound down and eliminated, reduced in scope, suspended, or replaced with something new, DEF will comply with the Commission's policy.

**FPUC:** No position.

**GULF:** None. As noted in response to Issue 1D, Gulf believes that it is appropriate to continue its financial hedging activities as an appropriate risk management tool. Gulf has demonstrated that implementation of its risk management plan has accomplished the objective of the hedging order to limit price volatility. No changes are necessary or appropriate at this time.

**TECO:** There should not be any changes to the manner in which electric utilities conduct their natural gas financial hedging. No such changes have been proposed in this proceeding. Moreover, the current natural gas financial hedging model was carefully constructed after due consideration of all relevant matters by the Commission and all affected persons. No changes are in order.

**OPC:** The natural gas financial hedging activities of the Companies should be discontinued. The facts and the evidence adduced at the fuel clause hearing unequivocally demonstrate that the Commission should deny the Companies' Risk Management Plans as they relate to natural gas financial hedging activities and the Commission should suspend and end the practice of natural gas financial hedging.

**FIPUG:** Hedging should be discontinued.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** PCS agrees with the Office of Public Counsel. For the reasons described in the testimonies of OPC witnesses Noriega and Lawton and in OPC's basic position, the Commission should deny the Company's risk management plans as it relates to natural gas financial hedging activities and should suspend and end the practice of natural gas financial hedging.

**Staff Analysis:** Staff notes this issue is essentially a fallout consideration of Issue 1D. In order to minimize duplicative arguments and for administrative efficiency, the argument for this issue will be brief.



## **Arguments**

As presented in Issue 1D, the parties that participate in hedging activities believe that hedging is in the public interest and should be continued. (FPL BR 2, 15; DEF BR 1; Gulf BR 3, 7; TECO BR 5) As a fallout to that decision, those parties answer to this issue reflects a position that no changes are needed to the manner in which electric utilities currently conduct their natural gas financial hedging activities.

FPL witness Yupp states that no changes are needed because his company's hedging program has "worked exactly as intended by the Commission and FPL to limit the volatility of fuel costs that FPL's customers pay." (TR 951; BR 6) Because the future is uncertain and volatility still exists, FPL's witness believes hedging should continue. (TR 978, 980) DEF's witness McCallister stated that DEF is open to continuing in the current recovery practices, or something new, but stated that the timing aspects of fuel cost recovery is something the Commission should be aware of. (TR 1022; FPL BR 2)

OPC's case advocated that hedging be eliminated prospectively, and the intervening parties by and large supported this position. (OPC BR 1; PCS BR 1; FIPUG BR 1) Staff believes that if OPC's basic position in Issue 1D to completely eliminate hedging on a prospective basis prevails, answering this issue is unnecessary.

## **Analysis**

Consistent with staff's recommendation in Issue 1D, staff believes natural gas hedging activities are in consumers' best interest, and should continue prospectively. Staff believes no changes are warranted at this time to the manner in which electric utilities conduct their natural gas financial hedging activities.

However, if the Commission wants to consider changes that could be made to the manner in which electric utilities conduct their natural gas financial hedging activities a subsequent proceeding can be scheduled. A few options that were identified are described below:

### ***Alternative Accounting Treatment of Hedging Gains/Costs***

At the present time, hedging gains/losses are recognized and reported at the time they occur. In practice, if the results of hedging activity for a given month resulted in a hedging gain, the amount of that gain is reflected as an offset to the fuel costs for that period. Conversely, if the results of hedging activity for a given month resulted in a hedging loss, the amount of that loss is reflected as an adder to the fuel costs for that period.

An alternative treatment of hedging gains/losses would be to defer the timely recovery (of a hedging gain or a hedging cost) to a future period. A future period could be defined as a month, a quarter of a year, or even a year or longer. An advantage for doing so would be that ratepayers would be somewhat shielded from volatile hedging results. A disadvantage would be that any deferral of costs might artificially create a lump sum swing in fuel costs if the deferral was for an extended period.

Although no party advocated that an alternative accounting treatment of a hedging gains/costs was needed, staff notes that several witnesses referred to FPL's Volatility Mitigation Mechanism (VMM) proposal, which was only a mitigation proposal to spread hedging costs over a 2 year

period. FPL witness Yupp stated that FPL's VMM proposal was offered at a time when there was regulatory uncertainty around hedging, and was withdrawn when the hedging guidelines were developed. Additionally, the witness stated that VMM did not mitigate price spikes to consumers. (TR 989-990)

DEF witness McCallister stated that FPL's VMM was evaluated years ago, but offered that his company would have to study an alternative like that in order to offer a definitive opinion on it. (TR 1022) Witness Ball from Gulf echoed the same concern, acknowledging that a year over year under-recovery would be amplified, if an alternative accounting treatment required that a balance be carried over. (TR 1049) The "stacking effect" is a real consideration, according to TECO witness Caldwell, and for this reason, his company would not support an alternative accounting treatment that required a balance be carried over in this manner. (TR 1059) Witness McCallister stated that a deferred recovery only addresses the timing of the recovery, not volatility. (TR 1023).

### ***Impose Limits on the Upper Range of Hedging Volumes***

At the present time, the IOUs hedge natural gas according to the range of volumes set forth in their risk management plans. Generally, the upper and lower hedging limits are company-specific and confidential, and are expressed as a percentage of total natural gas burn.

The Commission could consider imposing a "not to exceed" threshold to limit the upper range of volume to be hedged. An advantage of doing this would be to limit hedging losses in periods when market prices were lower than hedged prices. However, the disadvantage for imposing an upper limit on hedged volumes would be that hedging gains would be limited in times when hedged prices would be lower than market prices.

### ***Implement a Sharing Mechanism***

At the present time, all hedging gains and costs are borne by customers. An advantage of implementing a sharing mechanism would be to limit hedging losses for customers in periods when market prices were lower than hedged prices. However, the disadvantage for imposing a sharing mechanism would be that participants might speculate on future prices as a means to mitigate to their shared exposure, which would be contrary to the principles and guidelines expressed in the 2002 and 2008 hedging orders.

At the hearing, hedging witnesses were asked their opinion of implementing a mechanism whereby gains and costs could be shared between the company and ratepayers. DEF witness McCallister stated that it might lead to speculation, and would not be something DEF would support. (TR 488) This thought was also expressed by TECO witness Caldwell while Gulf witness Ball opined that his company has no interest in such a proposal. (TR 1038, 1048, 1057)

### **Conclusion**

Staff believes no changes are warranted at this time to the manner in which electric utilities conduct their natural gas financial hedging activities.

**Issue 2B:** Should the Commission approve DEF's 2016 Risk Management Plan?

**Recommendation:** Yes. The Commission should approve DEF's 2016 Risk Management Plan. (Barrett, Lester)

**Position of the Parties**

**FPL:** No position.

**DEF:** Yes, unless the Commission concludes that it is in the best interests of customers for the hedging program to be wound down and eliminated, reduced in scope, suspended, or replaced with something new. If the Commission amends or modifies the parameters of the hedging program, DEF will amend its Risk Management Plan accordingly, and will not execute any hedges beyond those previously executed per approved risk management plans to comply with the Commission's direction.

**FPUC:** No position.

**GULF:** No position.

**TECO:** No position.

**OPC:** No. The Risk Management Plan should not be approved as filed inasmuch as it would authorize the company to continue the financial hedging of natural gas. Incorporate by reference OPC's arguments for Issues 1D & 1E.

**FIPUG:** Hedging should be discontinued.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No. PCS agrees with the Office of Public Counsel. The plan should not be approved as filed inasmuch as it would authorize the company to continue the financial hedging of natural gas.

**Staff Analysis:** Staff notes that there is considerable overlap between the arguments DEF presented in Issue 1D and the issue to consider the approval of DEF's Risk Management Plan for 2016 (Issue 2B). In order to minimize duplicative arguments and for administrative efficiency, the argument for this issue will be brief and concise.

**Arguments**

Witness McCallister stated the hedging activities set forth in DEF's Risk Management Plan are followed in a structured manner to reduce price risk. (TR 497) Although small changes are made from year to year, DEF's prescriptive, consistent approach will be followed in 2016. (TR 514)

As presented in Issue 1D, OPC witness Lawton stated that prospective hedging activities should cease, and the Risk Management Plans for 2016 should not be approved. (TR 822)

**Analysis**

Consistent with staff's recommendation in Issue 1D that the utilities should continue natural gas financial hedging activities, staff recommends that the Commission approve DEF's 2016 Risk Management Plan. Staff believes DEF's Risk Management Plan for 2016 provides the appropriate governance for a well-disciplined and prudently-managed utility hedging program, and is consistent with the Hedging Guidelines.

**Conclusion**

Staff recommends the Commission approve DEF's 2016 Risk Management Plan.

**Issue 3B:** Should the Commission approve FPL's 2016 Risk Management Plan?

**Recommendation:** Yes. Staff recommends that the Commission approve FPL's 2016 Risk Management Plan.

**Position of the Parties**

**FPL:** Yes. On August 5, 2008, FPL filed a petition in the fuel docket requesting approval of Hedging Order Clarification Guidelines (the "Hedging Guidelines"). The Hedging Guidelines were approved by the Commission. Section I of the Hedging Guidelines provides for investor-owned utilities such as FPL to file a risk management plan covering the activities to be undertaken during the following calendar year for hedges applicable to subsequent years, and for the Commission to review such plans for approval as part of the annual fuel adjustment proceeding. FPL's 2016 Risk Management Plan is consistent with the Hedging Guidelines and should be approved.

**DEF:** No position.

**FPUC:** No position.

**GULF:** No position.

**TECO:** No position.

**OPC:** No. The Risk Management Plan should not be approved as filed inasmuch as it would authorize the company to continue the financial hedging of natural gas. Incorporate by reference OPC's arguments for Issues 1D & 1E.

**FIPUG:** Hedging should be discontinued. Otherwise, adopt the position of OPC.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No position.

**Staff Analysis:** Staff notes that there is considerable overlap between the arguments FPL presented in Issue 1D and the issue to consider the approval of FPL's Risk Management Plan for 2016 (Issue 3B). In order to minimize duplicative arguments and for administrative efficiency, the argument for this issue will be concise.

**Arguments**

From a historical perspective, witness Yupp believes that FPL's Risk Management Plan has reduced fuel price volatility, which delivered fuel price certainty for FPL's customers. (TR 398) The witness asserted that the Risk Management Plan for 2016 carries this forward by expressing the parameters within which FPL intends to place hedges during 2016. (TR 401) The witness noted, however, that the 2016 Plan differs from earlier plans because of FPL's participation in the Woodford Gas Reserves Project. (TR 402) FPL's hedging program is consistent with the

guiding principles outlined in the Commission's hedging orders. (TR 399) FPL witness Yupp believes FPL's Risk Management Plan for 2016 should be approved.

As presented in Issue 1D, OPC witness Lawton stated that prospective hedging activities should cease, and the Risk Management Plans for 2016 should not be approved. (TR 822)

### **Analysis**

Consistent with staff's recommendation in Issue 1D that the utilities should continue natural gas financial hedging activities, staff recommends that the Commission approve FPL's 2016 Risk Management Plan. Staff believes FPL's Risk Management Plan for 2016 provides the appropriate governance for a well-disciplined and prudently-managed utility hedging program, and is consistent with the Hedging Guidelines.

### **Conclusion**

Staff recommends that the Commission approve FPL's 2016 Risk Management Plan.

**Issue 3K:** What costs are appropriate for FPL's Woodford natural gas exploration and production project for recovery through the Fuel Clause?

**Recommendation:** For the period January 2015 through December 2015, the appropriate actual/estimated costs FPL should recover through the Fuel Clause for the Woodford natural gas exploration and production project is \$24,611,461. For the period January 2016 through December 2016, the appropriate projected costs FPL should recover through the Fuel Clause for the Woodford natural gas exploration and production project is \$53,777,690. (Barrett)

**Position of the Parties**

**FPL:** The amount of total system recoverable expenses related to FPL's Woodford Project that FPL should be allowed to recover through the Fuel Clause for 2015 and 2016 are \$24,611,461 and \$53,777,690, respectively.

**DEF:** No position.

**FPUC:** No position.

**GULF:** No position.

**TECO:** No position.

**OPC:** FPL has the burden of proof to justify and support the recovery of costs and their proposal(s) seeking the Commission's adoption of policy statements (whether new or changed) or other affirmative relief sought, regardless of whether the Intervenor provide evidence to the contrary. Regardless of whether the Commission has previously approved a program or costs as meeting the Commission's requirements, the utilities must still meet their burden of demonstrating that the costs submitted for final recovery meet the statutory test(s) and are reasonable in amount and prudently incurred. The OPC takes no position on whether FPL has met its burden of proof on this issue.

**FIPUG:** None.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No position.

**Staff Analysis:**

**Argument**

FPL witness Keith sponsored an exhibit reporting the company's return on capital investment and depletion for FPL's Woodford natural gas exploration and production project (the Woodford Project). (TR 31; EXH 12) As shown in the exhibit, for the period January 2015 through December 2015, the appropriate actual costs through July and estimated costs for the remaining months totaled \$24,611,461, and for the period January 2016 through December 2016, the projected costs FPL should recover through the Fuel Clause for the Woodford natural gas exploration and production project is \$53,777,690. (EXH 12)

FPL witness Yupp testified that the projected expenses for 2016 total about \$500,000 for incremental O&M for accounting, technical services or business management functions. (TR 398) Witness Yupp stated that in 2015, the Woodford project was in the “startup phase,” and that production delays and a host of other issues emerged. (TR 424-425). The witness stated, however, that the most recent production figures and expense projections show higher production volumes than prior reports, and lower expenses, resulting in a delivered price of \$2.70 per mmBtu. (TR 425-426, 428) When cross examined, the witness acknowledged that low market prices contributed to overall hedging losses in 2015 for the Woodford Project. (TR 427) Witness Yupp testified that FPL earned a return on its Woodford Project investment, although he stated this project will benefit ratepayers by providing a long-term stable volume of gas at a fixed cost. (TR 425 448)

### **Analysis**

On June 25, 2014, FPL petitioned the Commission for a determination that it was prudent for FPL to acquire an interest in a natural gas reserve project (the Woodford Project) and that the revenue requirement associated with investing in and operating the gas reserve project was eligible for recovery through the Fuel Clause. In Order No. PSC-15-0038-FOF-EI<sup>8</sup> (Woodford Order), the Commission found that the Woodford Project was in the public interest and its costs were recoverable through the Fuel Clause. OPC and FIPUG have filed appeals of the Woodford Order with the Florida Supreme Court, which are pending as of the date of this memorandum<sup>9</sup>.

As summarized in the Woodford Order, the Woodford Project is a capital investment by which FPL invests directly in shale gas reserves in the Woodford Shale region of Oklahoma and ratepayers pay natural gas production costs rather than the market price on the physical gas produced.

Historically, production costs have been less volatile than market prices. We find the Woodford Project will act as a hedge that is designed to decouple costs from market prices.<sup>10</sup> The Woodford Project costs are based solely on the operations and maintenance costs, and on the investment that is required, and is essentially fixed. FPL purchases more natural gas than any other electric utility in the country. The reality is that in this state, and nationally, we continue to grow the need for natural gas to provide electricity as we move away from coal. Although the Woodford Project is relatively small and will have a small effect on FPL’s overall cost of natural gas and on price hedging, it will act as a long-term physical hedge (30 years or longer in duration) compared to financial hedges, which typically lock in prices for 12 – 24 months. Fuel and related costs that are subject to volatile changes are recoverable through the Fuel Clause.<sup>11</sup> We have allowed

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<sup>8</sup>Order No. PSC-15-0038-FOF-EI, issued January 12, 2015, in Docket No. 150001-EI, *In re: Fuel and purchased power cost recovery clause with generating performance incentive factor*.

<sup>9</sup>On March 30, 2015, the Florida Supreme Court consolidated OPC’s three appeals and the FIPUG appeal into a single case (Florida Supreme Court Case No. SC15-95).

<sup>10</sup>Customers currently bear certain drilling, production, and shale gas risks (earthquakes, environmental issues, etc.) as these factors are embedded in the market price of gas.

<sup>11</sup>Order No. 14546, issued July 8, 1985, in Docket No. 850001-EI-B, *In re: Cost recovery Methods for Fuel-Related Expenses*.



non-fuel items to be recovered through the Fuel Clause as long as they are projected to result in fuel savings.<sup>12</sup> FPL's natural gas price forecasts of October 2013 and July 2014 indicate that the Woodford Project will likely produce positive customer fuel savings over the life of the Project based on combinations of two factors: well productivity and natural gas market price. Under FPL's July 2014 natural gas price forecast, 6 of 9 sensitivities produce positive customer savings. ...

(Order No. PSC-15-0038-FOF-EI, pp. 4-5)

Staff acknowledges the Commission's approval of the Woodford Project is presently subject to certain appeals at the Florida Supreme Court. However, no motions to stay have been filed and the Woodford Order remains in full force and effect. Nonetheless, FPL has moved forward with its investment, and drilling and production activity began earlier this year. Therefore, staff recommends FPL is entitled to recover its Woodford Project costs through the Fuel Clause.

### **Conclusion**

Staff recommends that for the period January 2015 through December 2015, the appropriate actual/estimated costs FPL should recover through the Fuel Clause for the Woodford natural gas exploration and production project is \$24,611,461. For the period January 2016 through December 2016, the appropriate projected costs FPL should recover through the Fuel Clause for the Woodford natural gas exploration and production project is \$53,777,690.

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<sup>12</sup>Order Nos. PSC-97-0359-FOF-EI, issued March 31, 1997, in Docket 970001-EI, *In re: Fuel and purchased power cost recovery clause and generating performance incentive factor* (FPL investment in rail cars) and PSC-01-2516-FOF-EI, issued December 26, 2001, in Docket 010001-EI, *In re: Fuel and purchased power cost recovery clause and generating performance incentive factor* (Incremental Power Plant Security Costs).

**Issue 4A:** Should FPUC be permitted to recover the cost (depreciation expense, taxes, and return on investment) of building an interconnection between FPL's substation and FPUC's Northeast Division through the fuel recovery clause?

**Recommendation:** No. (Brownless)

**Position of the Parties**

**FPL:** No position.

**DEF:** No position.

**FPUC:** Yes. The project costs constitute unanticipated fuel-related costs not included in the computation of base rates for the Company. The project itself is designed to lower the delivered price of purchased power to the Company, which will produce savings for FPUC's customers.

**GULF:** No position.

**TECO:** No position.

**OPC:** No. Transmission costs are traditionally and historically recovered through base rates, not the fuel clause, and are not fossil fuel-related costs. Therefore, FPUC's request for fuel clause recovery violates the Company's base rate case Settlement. Further, FPUC's argument that the transmission costs should be recovered as 2016 fuel costs should be rejected since any potential "fuel savings" cannot occur in 2016 because the current PPA does not expire until 2017 and this plant will not go into service until the end of 2017. The \$107,333 revenue requirement impact should be removed from the 2016 projected fuel factor calculation.

**FIPUG:** No. Such costs should be recovered in base rates, not through the fuel clause. Furthermore, any lobbying-type expenses should not be recovered.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No. The Florida Public Utilities Company's proposal to recover the costs of an interconnection project through the fuel recovery clause would be an inappropriate use of the fuel recovery clause and should be denied.

**Staff Analysis:**

**Background**

FPUC has requested that it be allowed to recover \$107,333 in 2016, the depreciation expense, taxes other than income taxes and a return on investment associated with the \$3.5 million dollar cost of rerouting FPUC's 138 KV transmission line to parallel an existing FPL 230 KV line and upgrading FPL's substation to accommodate this interconnection. (TR 571, 594-596, 626; EXH 34) At this time, FPUC's 138 KV transmission is directly connected to the JEA 138 KV transmission network. (TR 594) If construction is started in 2016, the completion date is expected during the latter half of 2017. (TR 595) FPUC has estimated that savings will result from this interconnection for essentially two reasons: 1) improved system reliability on FPUC's

transmission system; and 2) the ability to purchase power from other wholesale providers without incurring additional transmission wheeling costs which should result in lower purchased power costs. (TR 595-597) FPL will be constructing the transmission line with the costs to be reimbursed by FPUC. (TR 633)

FPUC does not generate any electricity but is solely dependent on wholesale purchase power agreements to meet its capacity and energy needs. (TR 567, 600) At this time, FPUC has wholesale power purchase agreements with JEA which service its Northeastern Division (Amelia Island) and Gulf Power Company (Gulf Power) which service its Northwestern Division (Marianna). (TR 603) Both of these wholesale purchased power contracts include payments for JEA's and Gulf Power's transmission rate base costs to provide power to FPUC. (TR 577, 615-616) However, FPUC does not currently recover any of its own transmission rate base costs through the fuel clause. (TR 616) FPUC's current contract with JEA is set to expire in December 31, 2017, the same time that FPUC's interconnection with FPL is expected to be completed. (TR 600) FPUC is required to purchase all of its wholesale purchased power from JEA during the term of the current contract. (TR 604-5) Thus, the projected \$2.3 million in savings for future purchased power costs associated with the FPL interconnection can't materialize until after January 1, 2018. (TR 600, 605)

FPUC Witness Cutshaw testified that FPUC intends to issue an RFP soliciting capacity and energy for delivery at the beginning of 2018. (TR 624) Thus, while FPUC anticipates that as a result of its RFP it will be able to contract for wholesale capacity and energy at significantly lower rates once the interconnection is completed, no contracts have yet been signed and FPUC "cannot specifically define what those savings will be..." (TR 596)

When asked by several parties if FPUC would go forward with the interconnection if recovery was not allowed through the fuel clause, both Witnesses Young and Cutshaw stated that they simply didn't know. (TR 563, 572, 612-3, 633-4)

### **Parties' Arguments**

The Commission's basic guidelines for recovery of costs through the fuel adjustment clause are found in Order No. 14546.<sup>13</sup> Since the issuance of Order No. 14546 in 1985, the Commission has issued 19 orders interpreting and applying these two principles to various proposed rate base capital costs for which recovery through the fuel clause was requested.<sup>14</sup> FPUC's brief focuses

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<sup>13</sup>Order No. 14546, issued on July 8, 1985, in Docket No. 850001-EI,-B, *In re: Cost Recovery Methods for Fuel-Related Expenses*.

<sup>14</sup>Order No. PSC-11-0080-PAA-EI, issued on January 31, 2011, in Docket No. 100404-EI, *In re: Petition by Florida Power & Light Company to recover Scherer Unit 4 Turbine Upgrade costs through environmental cost recovery clause or fuel cost recovery clause* (This order includes a list of all orders between 1985 and 2005); Order No. PSC-12-0498-PAA-EI, issued on September 27, 2012, in Docket No. 120153-EI, *In re: Petition to recover capital costs of Polk Fuel Cost Reduction Project through the Fuel Cost Recovery Clause, by Tampa Electric Company*; Order No. PSC-13-0505-PAA-EI, issued on October 28, 2013, in Docket No. 130198-EI, *In re: Petition for prudence determination regarding new pipeline system by Florida Power & Light Company*; Order No. PSC-14-0309-PAA-EI, issued on June 12, 2014, in Docket No. 140032-EI, *In re: Petition to recover capital costs of Big Bend fuel cost reduction project through the fuel cost recovery clause, by Tampa Electric Company*; Order No. PSC-15-0038-FOF-EI, issued on January 12, 2015, in Docket No. 150001-EI, *In re: Fuel purchased power cost recovery clause with generating performance incentive factor*.

on why its proposed transmission project qualifies for recovery through the fuel adjustment clause (FPUC BR at 5-12).

However, OPC, FRF, FIPUG, and PCS all take the position that the rate case stipulation and settlement agreement entered into between OPC and FPUC on August 29, 2014 and approved by this Commission in Order No. PSC-14-0517-S-EI, issued on September 29, 2014, (Order No. PSC-14-0517)<sup>15</sup> prohibits the recovery of costs associated with the FPL interconnection through the fuel clause. (OPC BR 15-18; FIPUG BR 10; PCS BR 7-9)

Section I, Term, of the settlement agreement prohibits FPUC from increasing its base rates during the minimum term of the agreement, or until after December 31, 2016. The settlement agreement also states in Section VI, Other Cost Recovery, as follows:

Nothing in this agreement shall preclude the Company from requesting the Commission to approve the recovery of costs that are: (a) of a type which traditionally and historically would be, have been, or are presently recovered through cost recovery clauses or surcharges or (b) incremental costs not currently recovered in base rates which the Legislature or Commission determines are clause recoverable subsequent to the approval of this settlement. Except as provided in this Agreement, it is the intent of the Parties in this Paragraph VI that FPUC not be allowed to recover through cost recovery clauses increases in the magnitude of costs, incurred after implementation of the new base rates, of types or categories (including but not limited to, for example, investment in and maintenance of transmission assets) that have been traditionally and historically recovered through FPUC's base rates.

[Emphasis added.]

### **Analysis**

The analysis of this issue has two parts. First, are the costs of this rate base transmission project appropriately recovered through the fuel clause? And, second, if so, is this transmission project reasonably expected to result in reductions to the purchased power costs of FPUC? Unless the first question is answered in the affirmative, the second question need not be addressed. Staff agrees with the intervenors that the rate case stipulation and settlement agreement entered into between OPC and FPUC on August 29, 2014 and approved by this Commission in Order No. PSC-14-0517-S-EI, issued on September 29, 2014, (Order No. PSC-14-0517)<sup>16</sup> prohibits the recovery of costs associated with the FPL interconnection through the fuel clause.

FPUC's arguments for allowing recovery for the FPL interconnection costs through the fuel adjustment clause essentially are three: 1) unlike other investor-owned utilities (IOUs), FPUC's transmission costs have traditionally and historically been recovered through the fuel clause; 2) the FPL interconnection is more than a transmission asset, it is the means by which FPUC can lower its wholesale purchased power costs; and 3) absent recovery through the fuel clause, FPUC might not be able to construct the interconnection with FPL and thereby get the benefit of

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<sup>15</sup>Order No. PSC-14-0517-S-EI, issued on September 29, 2014, in Docket No. 140025-EI, *In re: Application for rate increase by Florida Public Utilities Company*.

<sup>16</sup>Order No. PSC-14-0517-S-EI, issued on September 29, 2014, in Docket No. 140025-EI, *In re: Application for rate increase by Florida Public Utilities Company*.

lower fuel costs at the expiration of its current power purchase agreement with JEA in December 2017. Staff does not find these arguments persuasive.

First, the only transmission costs that FPUC has historically recovered through the fuel clause are those of JEA and Gulf Power embedded in its current wholesale power purchase agreements with both parties. (TR 577, 615-616) None of FPUC's own transmission costs have ever been recovered through the fuel clause. (TR 616) Nor have any other IOU transmission costs been "historically" or "traditionally" recovered through the fuel clause. (TR 616) It should also be noted here that one of the benefits of the FPL interconnection testified to by witness Cutshaw is that the interconnection will significantly improve the reliability of service to Amelia Island. (TR 595-597, 600) However, capital improvements to enhance service reliability have neither "historically" nor "traditionally" been recovered through the fuel clause.

Second, FPUC failed to make the case that if recovery of the cost of the FPL interconnection through the fuel clause is disallowed, this project which FPUC believes to be valuable, would not be built or would be delayed and the benefits associated with lower costs postponed for its ratepayers. Nor did FPUC prove that completion of this transmission project is the only means by which its ratepayers could receive potential lower purchased power costs at the expiration of its contract with JEA. (TR 635) FRF, FIPUG, OPC and Commissioners all questioned FPUC's witnesses on these points. Both Witnesses Young and Cutshaw testified that FPUC would evaluate "other options" to recover the cost of the interconnection, e.g., a rate case or limited proceeding. (TR 563, 572, 613, 634, 614-616, 619-621)

Section VIII, Earnings, of the settlement agreement, states that if FPUC's earned ROE falls below 9.25 percent during the minimum term of the agreement, FPUC is permitted to file a petition for a rate increase under Sections 366.06 or 366.07, F.S., or a limited proceeding under Section 366.076, F.S. As reported in FPUC's most recent earnings surveillance report filed on September 15, 2015, FPUC's reported achieved ROE for the period ended June 30, 2015, was 4.79 percent. (EXH 124, Schedule 1) At this time FPUC is earning below 9.25 percent, the low point of the range. Thus, despite the base rate freeze currently in place as a result of the settlement, FPUC has met the settlement's conditions to release that freeze and is entitled to file for a rate base increase should recovery through the fuel clause be denied. In order to meet an in-service date for the transmission line of January 2018, a rate case filing in 2017 with rates effective the first of billing cycle of 2018 is required. (TR 614-615) Further, filing a rate case, which would involve other issues beyond the proposed FPL interconnection project, could result in a base rate increase for customers. (TR 636-637) Given these facts, staff believes that FPUC does have the option of filing for a base rate increase under the settlement agreement to recover the costs of the FPL interconnection.

Finally, FPUC has argued that the FPL interconnection is not prohibited by the settlement agreement because it will allow FPUC to reduce the price of its wholesale purchased power. For FPUC reducing the price of purchased power is the equivalent of reducing the price of fossil fuels for the other IOUs. (FPUC BR 10) FPUC argues that Order No. 14546<sup>17</sup> applies to purchased power as well as fossil fuels and should be used here to allow recovery of the FPL

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<sup>17</sup>Order No. 14546, issued on July 8, 1985, in Docket No. 850001-EI-B, *In re: Cost Recovery Methods for Fuel-Related Expenses*.

interconnection costs. (FPUC BR 10-12) FPUC dismisses the plain language of Section VI of the settlement agreement which does not allow recovery of “investment in and maintenance of transmission assets that have been traditionally and historically recovered through FPUC’s base rates” on two rationales. First, Exhibit A to the settlement agreement entitled “Planned Capital Improvements” covering the period 2016-2019 does not list the FPL interconnection project. (FPUC BR 19) Second, the prohibition against recovery of transmission projects in the settlement agreement applies only to “investment in, or maintenance of, existing transmission.” (FPUC BR 19-20)

Staff agrees with FPUC that if the provisions of Order No. 14546 are not applied to purchased power, there is very little guidance as to what is recoverable in terms of purchased power through the fuel clause. (FPUC BR 10) Certainly, this is the first instance in which FPUC, the only non-generating electric utility in the state, has requested recovery of a transmission asset through the fuel clause. However, staff does not agree that the explicit terms of the settlement agreement should be dismissed summarily.

The settlement agreement does not state that the prohibition against recovery of transmission costs through the fuel clause is limited to the projects listed on Exhibit A. In its joint motion with OPC for approval of stipulation and settlement, FPUC stated that “FPUC will use all reasonable infrastructure projects, consistent with those outlined in demonstrative Exhibit A, attached to the Agreement, in order to maintain the reliability of its electrical system.” (Motion at 6) The joint motion also reiterates that “The Company may continue to seek recovery of costs through recovery clauses, but cannot seek recovery of costs that the Company has traditionally and historically recovered through base rates.” (Motion at 7) Given the language in its motion, the fact that the FPL interconnection was not included on Exhibit A does not support the conclusion that its costs are exempt from the settlement agreement’s specific prohibition against the recovery of transmission costs through the fuel clause. Nor does the motion’s or the settlement agreement’s prohibition against recovery through the fuel clause contain any language limiting prohibited transmission projects to existing projects. FPUC has cited no specific provision of the settlement agreement to support this contention nor is there any testimony or record evidence to support it.

Witness Cutshaw agreed that transmission rate base costs were normally recovered through base rates and that the proposed FPL interconnection was part of a transmission asset. (TR 616, 621) While there may be potential savings associated with the project, the plain language of the settlement agreement prohibiting recovery of the capital costs of transmission projects does not support recovery of these costs through the fuel adjustment clause.

### **Conclusion**

For the reasons stated above, staff recommends that FPUC should not be allowed to recover the cost (depreciation expense, taxes, and return on investment) of building an interconnection between FPL’s substation and FPUC’s Northeast Division through the fuel recovery clause.

**Issue 4B:** Should FPUC's request to recover consulting and legal fees through the fuel clause be approved?

**Recommendation:** Yes. FPUC should continue to be allowed recovery of its consulting and legal costs associated with the review and analysis of FPUC's existing purchase power agreements and costs associated with evaluating future fuel cost saving applications through the fuel cost recovery clause. However, the true-up amount, estimated/actual costs, and projected costs should be reduced to remove consulting costs associated with the preparation of Commission filings. Within 20 days of the Commission vote, FPUC should file revised true-up and projections schedules that reflect the removal of the costs associated with the preparation of Commission filings. (Bulecza-Banks, Barrett)

**Position of the Parties**

**FPL:** No position.

**DEF:** No position.

**FPUC:** Yes. These costs are not being recovered in the Company's base rates, tend to fluctuate significantly from year to year, and are directly related to projects that will inure to the benefit of FPUC's ratepayers. Moreover, FPUC has historically recovered similar legal and consulting expenses through the fuel clause.

**GULF:** No position.

**TECO:** No position.

**OPC:** No. The requested consulting and legal fees are not fossil fuel-related costs recoverable through the fuel clause. FPUC's request to recover these costs in the fuel clause violates the Company's rate case Settlement pursuant to Order PSC-14- 0517-S-EI. Further, consulting and legal costs related to generation opportunities and fuel procurement administration costs, pursuant to Order No. 14546, are more appropriately recovered through base rates. Moreover, FPUC's argument that its consulting and legal fees for generation opportunities may produce fuel savings and, as such, should be recovered as 2016 fuel costs, should be rejected, as no "fuel savings" will occur in 2016.

**FIPUG:** No. Such costs should be recovered in base rates, not through the fuel clause. Furthermore, any lobbying-type expenses should not be recovered.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No position.

**Staff Analysis:**

**Background**

As part of its filed petition, testimony, and supporting schedules, FPUC included actual and estimated consulting and legal fees in its fuel costs for 2014, 2015, and 2016. (TR 520, EXHs 32, 33, 34) Actual costs included in its 2014 true-up calculation are \$122,933. FPUC included \$111,135 in its 2015 estimated/actual costs, and \$387,000 its 2016 projected costs.

The OPC, FRF, and FIPUG oppose the inclusion of legal and consulting fees in FPUC's true-up expenses for 2014, its actual/estimated fuel costs for 2015, and costs included in FPUC's calculation of its 2016 projected fuel costs. The other investor-owned utilities and PCS have taken no position on this issue.

**Parties' Arguments**

**FPUC**

FPUC believes that costs incurred and projected to be incurred for contracted consultants and legal services are directly fuel-related and will ultimately produce fuel savings that will flow to FPUC's customers through the fuel adjustment clause, and thus, are appropriate for recovery through the fuel cost recovery clause. (TR 520-523, 531-532, 589, and 591-592; BR 5) FPUC argued that the Commission has clearly stated that the purpose of the clause proceedings is to provide for recovery of volatile costs that tend to fluctuate between rate case proceedings, which if incorporated in based rates, would unduly penalize the utility or its customers.<sup>18</sup> (BR 6)

FPUC pointed out that no party filed testimony in the proceeding in opposition to FPUC's requested legal and consulting fees, and the only evidence in the record is that provided through the testimony of FPUC witnesses Young and Cutshaw. (BR 6)

In support of its request, FPUC witness Young argued that the consultants hired by FPUC engaged in activities related to the negotiation of a new power purchased contract with Eight Flags Energy, modification of FPUC's existing agreement with Rayonier Performance Fibers, and analysis of FPUC's current power purchase agreement to determine opportunities to produce fuel cost reductions. (TR 521; BR 13) Witness Cutshaw emphasized that the costs being requested are not associated with administrative functions associated with fuel procurement, nor associated with the Company's internal staff responsible for fuel procurement. (TR 530 and 539)

FPUC witness Young opined that that the costs FPUC is seeking to recover are similar to costs the Commission has traditionally and historically allowed recovery through the fuel clause. (TR 523; BR 14 and 20-21, EXH 89, pg. 242) In addition, witness Young pointed out that the costs requested have not been included in FPUC's base rates as these costs are volatile and fluctuate between rate case proceeding (TR 529-530, 539-540; BR 5, 6, and 21, EXH 89, pgs. 210-212)

FPUC argued that it has met its burden of proof by demonstrating that the legal and consulting fees it proposes for recovery through the fuel clause are (1) prudent expenses associated with

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<sup>18</sup>Order No. PSC-05-0748-FOF-EI, issued July 14, 2005, in Docket No. 041272-EI, at p.37, *In Re: Petition for approval of storm cost recovery clause for recovery of extraordinary expenditures related to Hurricanes Charley, Frances, Jeanne, and Ivan, by Progress Energy Florida, Inc.*



retaining outside expertise that the Company does not otherwise have in-house (TR 538 and 540); (2) work for which these consultants were retained are associated with projects that are either currently producing fuel savings or are reasonably expected to produce savings for the Company and its customers (TR 539); and (3) expenses of a type that the Commission has traditionally allowed FPUC to recover through the fuel adjustment clause. (TR 523, BR 13 and 22)

***OPC and FRF (FRF filed a Joinder in the Citizens' post-hearing statement of positions and post-hearing brief)***

The OPC argues that not only does the Settlement Agreement it entered into with FPUC last year preclude FPUC from seeking recovery in the fuel clause of its legal and consulting fees, but Fuel clause Order No. 14546 also prohibits FPUC recovery of such costs.

In Order No. PSC-14-0517-S-EI, issued September 29, 2014, the Commission approved a Settlement Agreement (Settlement) between the OPC and FPUC. Paragraph VI of the Settlement, states:

Nothing in this agreement shall preclude the Company from requesting the Commission to approve the recovery of costs that are (a) of a type which traditionally and historically would be, have been, or are presently recovered through cost recovery clauses or surcharges, or (b) incremental costs not currently recovered in base rates which the Legislature or Commission determines are clause recoverable subsequent to the approval of this settlement. Except as provided in this Agreement, it is the intent of the Parties in this Paragraph VI that FPUC not be allowed to recover through cost recovery clauses increases in the magnitude of costs, incurred after implementation of the new base rates, or types or categories (including but not limited to, for example, investment in and maintenance of transmission assets) that have been traditionally and historically recovered through FPUC's base rates.

OPC opines that the Settlement language clearly bars FPUC from even seeking recovery in the fuel clause for cost of types or categories that have been traditionally and historically recover through FPUC's base rates. In addition, OPC argues that the same base rate freeze anti-circumvention provision also prohibits FPUC from recovering the costs through cost recovery clauses.

OPC argues that the Commission has historically and traditionally treated allowed recovery of prudent consulting and legal generation-related costs through base rates and as FPUC does not have its own recovery history of these types of costs, they should be recovered in the same manner as have been historically and traditionally treated for other regulated electric companies. OPC accepts that FPUC was allowed recovery, on a limited basis, of its legal and consulting fees associated with purchased power agreements, but asserts that generic legal and consulting activities have not been specifically identified and allowed to be recovered through the fuel clause.

In addition, OPC argues that Fuel Clause Order No. 14546 sets forth a policy whereby costs permitted for recovery through the fuel clause must produce fuel savings. OPC asserts that the Company is simply speculating that the consulting and legal activities will result in fuel savings. While OPC acknowledges that FPUC witness Young confirmed that some of the consultant and legal activities “produced” savings, he could not identify any specific “fuel savings.” (TR 576) OPC also maintains that FPUC conceded that the outside consulting and legal fees are fuel procurement and administration charges or costs that Order No. 14546 specifically precludes from recovery through the fuel clause

In conclusion, OPC argues that the FPUC’s request is an attempt to circumvent the Settlement which specifically precludes FPUC from seeking recovery of costs historically and traditionally recovered through base rates. Further, OPC argues that the requested consultant and legal costs do not qualify for fuel clause recovery pursuant to Order No. 14546

### **FIPUG**

FIPUG did not address this issue in its brief other than to provide its statement of its position: No. Such costs should be recovered in base rates, not through the fuel clause. Furthermore, any lobbying-type expenses should not be recovered.

### **Analysis**

#### **Commission Order No. 14546**

Commission Order No. 14546, issued July 8, 1985, acknowledged the type of costs that would be permitted for recovery through the fuel cost recovery clause.<sup>19</sup> The order resulted from an agreement reached between staff, the Office of Public Counsel, Florida Power & Light, Florida Power Corporation (now Duke Energy Florida (DEF)), Gulf Power Company, and Tampa Electric Company. The Florida Industrial Power Users Group (FIPUG) was informed of the stipulation but it took no position.

As part of the stipulation, the two policies agreed to by the parties which they believed reflected the Commission’s practical application of fuel adjustment clauses included:

- 1) When similar circumstances exist, the Commission should attempt to treat, for cost recovery purposes, specific types of fossil-fuel related expenses in a uniform manner among the various electric utilities. At times, however, it may be appropriate to treat similar types of expenses in dissimilar ways.
- 2) Prudently incurred fossil fuel-related expenses which are subject to volatile changes should be recovered through an electric utility’s fuel adjustment clause...

In addition, the parties recommended to the Commission that the policy be flexible so that costs normally recovered through base rates, could be recovered through the fuel adjustment clause where the utility took advantage of a cost-effective transaction and those costs were not recognized or anticipated in the level of costs used to establish the utility’s base rates. As stated

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<sup>19</sup>Order No. 14546, issued on July 8, 1985, in Docket No. 850001-EI, *In re: Cost Recovery Methods for Fuel-Related Expenses*.

in the order, “The Commission shall rule on the appropriate method of cost recovery based upon the merits of each individual case.”

Since its issuance 30 years ago, the types of costs allowed recovery through the fuel clause has evolved to include prudent, non-fossil fuel-related costs. Examples of costs that have been permitted recovery through the fuel clause that are not fossil-fuel related include nuclear fuel disposal costs,<sup>20</sup> incremental power plant security cost,<sup>21</sup> capital and operating and maintenance costs for Nuclear Regulatory Commission compliance with post Fukushima standards.<sup>22</sup> The recovery of such costs was not contemplated at the time the Order was issued in 1985.

With respect to fuel-savings, Order No. 14546 set forth a policy whereby recovery of fossil fuel-related costs normally recovered through base rates but which were not recognized or anticipated in the cost levels used to determine current base rates and which, if expended, will result in fuel savings to customers would be made on a case by case basis. The Order did not require that the fuel savings occur concurrently with the costs incurred.

Order No. 14546, which was the result of a Commission-approved settlement of the parties to the fuel adjustment clause proceedings, was intended to identify costs that were appropriate for cost recovery, yet recognized that the Commission had the ultimate authority to rule on the method of cost recovery.

#### ***Prior Cost Recovery of Legal and Consulting Fees***

In Docket Nos. 060001-EI; 070001-EI, 080001-EI, 090001-EI, 10001-EI, 110001-EI, 120001-EI, 130001-EI, and 140001-EI, FPUC included legal and consulting fees associated with fuel-related work in its true-up filings which the Commission approved. In response to staff discovery, FPUC states that the legal and consulting fees included in its actual and projected costs are beyond the scope of normal, day-to-day fuel procurement administration functions. (EXH 89, p. 241)

The Commission has historically permitted FPUC to recover costs associated with legal and consulting fees related to purchase power agreement review and analysis. (TR 530) In Docket No. 120001-EI, FPUC was specifically granted recovery of the legal and consulting fees associated with an amendment to its Purchased Power Agreement for the Northwest Division. (EXH 89, p. 242)

As a small, non-generating investor-owned electric utility, FPUC has historically used consultants to perform a variety of activities in efforts to bring savings to its customers via lower fuel rates. (TR 520-523, 529-532, 538-539). In approving consulting costs paid by FPUC to

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<sup>20</sup>Order No. PSC-01-2516-FOF-EI, issued December 26, 2001, in Docket No. 010001-EI, *In re: Fuel and purchased power cost recovery clause and generating performance incentive factor*.

<sup>21</sup>The Commission moved recovery of incremental security costs from the Fuel Clause to the capacity cost recovery clause so that the security costs were be allocated on a demand basis, in the same manner as “ordinary” security costs. See Order No. PSC-01-2516-FOF-EI, issued December 26, 2001, in Docket No. 010001-EI, *In re: Fuel and purchased power cost recovery clause and generating performance incentive factor*.

<sup>22</sup>Order No. PSC-13-0665-FOF-EI, issued December 18, 2013, *In re: Fuel and purchased power cost recovery clause and generating performance incentive factor*.

Christensen and Associates, the Commission distinguished FPUC from the other electric IOUs, finding that given FPUC's small size, it does not have the resources internally to prepare an RFP and evaluate responses.<sup>23</sup> The Commission also found that the costs associated with this type of activity are not included in base rates.<sup>24</sup>

Currently, the consulting and legal fees FPUC is requesting are not being recovered in base rates. In response to staff discovery, FPUC stated that the legal and consulting fees were not anticipated in the Company's last rate case, as these types of costs fluctuate significantly from year to year. (EXH 89, p. 210) Thus, FPUC did not include any costs associated with these activities in their base rate increase request. (EXH 89, p. 211)

### ***Fuel Savings and Customer Benefit***

As stated by witness Young, FPUC has been aggressively seeking opportunities to reduce fuel costs to its consumers. (TR 538) To properly and thoroughly explore fuel-saving opportunities, FPUC engages legal and consulting assistance as it lacks in-house expertise. (TR 538) Witness Young testified that the costs that FPUC is requesting to be recovered through the fuel cost recovery clause are associated with legal and consulting fees incurred in the development and enactment of projects designed to reduce fuel rates to FPUC's customers, costs associated with the development and negotiations of power supply contracts, and costs to consultants engaged in performing due diligence in review and analysis of the Renewable Energy Agreement between FPUC and Rayonier. (TR 531)

In response to staff discovery, FPUC was asked whether the costs it projects to incur in 2016 for contracted consultants and legal services will result in fuel savings to its customers. FPUC responded, "Yes, that is FPUC's goal and expectation." (EXH 89, p. 217) FPUC further states in its response that during 2016, FPUC will begin discussions with various purchased power providers in preparation for the 2017 expiration of its NE Florida wholesale power contract with JEA. Currently FPUC is reliant upon JEA for all its power needs in its NE division and is prohibited from taking power from another wholesale power provider. (EXH 90, p. 257) FPUC asserts that there will be a need for an abundance of research, analysis, and negotiation to ensure that every detail is reviewed so that FPUC obtains the best overall price for its wholesale power needs. (EXH 89, p. 217).

### **Conclusion**

Previous Commission decisions have approved recovery of FPUC's consultant and legal fees associated with evaluating power purchase agreements, and costs that were beyond the scope of the day-to-day procurement administrative functions. In 2005, the Commission specifically recognized that due to FPUC's small size and lack of internal resources to craft a request for proposal and evaluate responses, it was appropriate to allow recovery of the consultant and legal fees associated with such activities.

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<sup>23</sup> Order No. PSC-05-1252-FOF-EI, issued December 23, 2005, in Docket No. 050001-EI, In re: *Fuel and purchased power cost recovery clause with generating performance incentive factor*.

<sup>24</sup> Ibid.

Staff believes there is no compelling reason to deviate from past Commission decisions. FPUC is still a small, non-generating electric utility that lacks the in-house expertise to find and evaluate potential opportunities for fuel savings and craft and evaluate requests for proposals for generation needs. FPUC did not include such costs in its last rate case as it believes the costs are volatile and as such, are more appropriately included for recovery in the fuel clause. At the time of its last rate case, similar costs were being recovered through the fuel clause. If recovery of these costs through the fuel clause is denied, these prudent costs would have to be absorbed by FPUC. Based on FPUC's most recently filed surveillance report, it achieved a return on equity of 4.79 percent while its approved return on equity is 10.25 percent, with a range of 9.25 to 11.25 percent.

Staff further believes that allowing recovery of FPUC's legal and consulting fees complies with Commission Order No. 14546. While the Order references fossil fuel-related expenses, the Order repeatedly provides the Commission the flexibility to determine the appropriate method of cost recovery of expenses that were not recognized or anticipated in the cost levels used to determine base rates and if expended, will result in fuel savings. The costs FPUC is requesting for recovery through the fuel clause are not related to FPUC's internal staff for fuel and purchased power procurement and administration. (TR 539) Not only has FPUC been previously allowed recovery of these types of legal and consulting fees, the types of costs that have been approved for recovery through the fuel cost recovery clause has evolved over time. Order No. 14546 was issued over 30 years ago, and while the basis for enactment of the policies reflected in the order is still valid, changes in the utility industry and the need to respond to such changes requires flexibility. Order No. 14546 repeatedly provides the Commission flexibility to address costs and transactions that were not recognized nor anticipated in the level of costs used to establish the utility's base rates. Costs that have been handled on a case-by-case basis in the fuel recovery clause include plant conversions costs, pipeline lateral costs, plant modification costs, and rail car costs. Recovery of these costs through the fuel cost recovery clause was based on estimated fuel savings. Similarly, FPUC projects that the opportunities being evaluated by its contracted consultants and legal professionals will also result in fuel savings. (EXH 89, pp. 217 and 219)

In conclusion, staff recommends that FPUC's consulting and legal fees associated with the development and enactment of projects designed to reduce fuel rates to FPUC's customers, costs associated with the development and negotiations of power supply contracts, and costs to consultants engaged in performing due diligence in review and analysis of the Renewable Energy Agreement between FPUC and Rayonier be recovered through the fuel cost recovery clause. Further, as acknowledged by Witness Young at the hearing, costs associated with a consultant who prepared Commission filings for the consolidation of FPUC's fuel divisions should be removed from its requested costs included in its true-up and projected filings. (TR 559).

**Issue 5B:** Should the Commission approve Gulf's 2016 Risk Management Plan?

**Recommendation:** Yes. Staff recommends that the Commission approve Gulf's 2016 Risk Management Plan. (Barrett, Lester)

**Position of the Parties**

**FPL:** No position.

**DEF:** No position.

**FPUC:** No position.

**GULF:** Yes. Gulf's 2016 Risk Management Plan for Fuel Procurement is a reasonable and prudent implementation of the Commission's hedging order and should be approved. Gulf believes that continued compliance with the "Hedging Order" provides an appropriate fuel risk management tool for utilities to utilize to limit natural gas price volatility.

**TECO:** No position.

**OPC:** No. The Risk Management Plan should not be approved as filed inasmuch as it would authorize the company to continue the financial hedging of natural gas. Incorporate by reference OPC's arguments for Issues ID & IE.

**FIPUG:** Hedging should be discontinued.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No position.

**Staff Analysis:** Staff notes that there is considerable overlap between the arguments Gulf presented in Issue 1D and the issue to consider the approval of Gulf's Risk Management Plan for 2016 (Issue 5B). In order to minimize duplicative arguments and for administrative efficiency, the argument for this issue will be brief and concise.

**Arguments**

Gulf witness Ball stated the company's Risk Management Plan has reduced fuel price volatility, which delivered fuel price stability for Gulf's rate paying customers. (TR 653, 1035) No major changes are present in Gulf's 2016 plan, according to the witness. (TR 678) In its 2016 Risk Management Plan, natural gas prices will be hedged financially using instruments that conform to the Commission's guidelines for hedging activity, and coal supply and transportation will be hedged physically using term agreements. (TR 679) Witness Ball believes Gulf's Risk Management Plan for 2016 should be approved because it presents a reasonable and appropriate strategy for protecting customers from fuel price volatility. (TR 679, 1035)

As presented in Issue 1D, OPC witness Lawton stated that prospective hedging activities should cease, and the Risk Management Plans for 2016 should not be approved. (TR 822)

**Analysis**

Consistent with staff's recommendation in Issue 1D that the utilities should continue natural gas financial hedging activities, staff recommends the Commission approve Gulf's 2016 Risk Management Plan. Staff believes Gulf's Risk Management Plan for 2016 provides the appropriate governance for a well-disciplined and prudently-managed utility hedging program, and is consistent with the Hedging Guidelines.

**Conclusion**

Staff recommends the Commission approve Gulf's 2016 Risk Management Plan.

**Issue 6B:** Should the Commission approve TECO's 2016 Risk Management Plan?

**Recommendation:** Yes. Staff recommends that the Commission approve TECO's 2016 Risk Management Plan. (Barrett, Lester)

**Position of the Parties**

**FPL:** No position.

**DEF:** No position.

**FPUC:** No position.

**GULF:** No position.

**TECO:** Yes. Tampa Electric's 2016 Risk Management Plan provides prudent nonspeculative guidelines for mitigating price volatility while ensuring supply reliability. This Plan like the ones that preceded it, has been prepared in accordance with the Commission's Hedging Order and subsequent orders refining hedging guidelines.

**OPC:** No. The Risk Management Plan should not be approved as filed inasmuch as it would authorize the company to continue the financial hedging of natural gas. Incorporate by reference OPC's arguments for Issues ID & IE.

**FIPUG:** Hedging should be discontinued.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** No position.

**Staff Analysis:** Staff notes that there is considerable overlap between the arguments TECO presented in Issue 1D and the issue to consider the approval of TECO's Risk Management Plan for 2016 (Issue 6B). In order to minimize duplicative arguments and for administrative efficiency, the argument for this issue will be brief and concise.

**Arguments**

TECO witness Caldwell stated the company's Risk Management Plan for 2016 describes the company's strategies to mitigate fuel price volatility using a disciplined, non-speculative approach that includes financial hedges for natural gas. He stated these financial hedges are entered solely for the benefit of customers. (TR 760) Witness Caldwell asserted

Using a disciplined, methodical, consistent natural gas financial hedging program ensures that a portion of projected natural gas needs are being hedged frequently, but never all at once. This provides known future pricing that is a blend of future prices acquired over a period of time. (TR 1058)

As presented in Issue 1D, OPC witness Lawton stated that prospective hedging activities should cease, and the Risk Management Plans for 2016 should not be approved. (TR 822)



**Analysis**

Consistent with staff's recommendation in Issue 1D that the utilities should continue natural gas financial hedging activities, staff recommends the Commission approve TECO's 2016 Risk Management Plan. Staff believes TECO's Risk Management Plan for 2016 provides the appropriate governance for a well-disciplined and prudently-managed utility hedging program, and is consistent with the Hedging Guidelines.

**Conclusion**

Staff recommends the Commission approve TECO's 2016 Risk Management Plan.

**Issue 9:** What are the appropriate final fuel adjustment true-up amounts for the period January 2014 through December 2014?

**Recommendation:** The appropriate final fuel adjustment true-up amount for the period January 2014 through December 2014 is an under-recovery of \$1,474,307. (Barrett)

**Position of the Parties**

**FPUC:** \$1,474,307 (Under-recovery)

**OPC:** The utilities have the burden of proof to justify and support the recovery of costs and their proposal(s) seeking the Commission's adoption of policy statements (whether new or changed) or other affirmative relief sought, regardless of whether the Intervenors provide evidence to the contrary. Regardless of whether the Commission has previously approved a program or costs as meeting the Commission's requirements, the utilities must still meet their burden of demonstrating that the costs submitted for final recovery meet the statutory test(s) and are reasonable in amount and prudently incurred. The OPC takes no position on whether the utilities have met their burden of proof on this issue.

**FIPUG:** FIPUG takes no position on this issue other than that the respective utilities must meet their burden of proof at the hearing in this matter, pursuant to applicable law, to demonstrate entitlement to the monies and other relief that the utilities request in this proceeding.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** PCS agrees with the Office of Public Counsel.

**Staff Analysis:** Witness Young acknowledged that FPUC has removed certain expenses<sup>25</sup> from its request for cost recovery of the final true-up amounts for the period January 2014 through December 2014. (TR 569; EXH 123) The expenses were for work performed to restructure FPUC's Fuel schedules (A-Schedules and E-Schedules), when the respective divisions were consolidated. (TR 558; EXH 89) The appropriate final fuel adjustment true-up amount for the period January 2014 through December 2014 is properly reflected in the brief FPUC filed on November 13, 2015. (FPUC BR 2, 22)

Staff recommends that the appropriate final fuel adjustment true-up amounts for the period January 2014 through December 2014 is an under-recovery of \$1,474,307.

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<sup>25</sup>Staff notes that the expense amount at issue is identified in Confidential Exhibit No. 123, but was subsequently disclosed in the FPUC brief on page 22 as \$2,046.

**Issue 10:** What are the appropriate fuel adjustment actual/estimated true-up amounts for the period January 2015 through December 2015?

**Recommendation:** The appropriate fuel adjustment actual/estimated true-up amounts for the period January 2015 through December 2015 is an under-recovery of \$107,841. (Barrett)

**Position of the Parties**

**FPUC:** \$107,841 (Under-recovery)

**OPC:** The utilities have the burden of proof to justify and support the recovery of costs and their proposal(s) seeking the Commission's adoption of policy statements (whether new or changed) or other affirmative relief sought, regardless of whether the Intervenors provide evidence to the contrary. Regardless of whether the Commission has previously approved a program or costs as meeting the Commission's requirements, the utilities must still meet their burden of demonstrating that the costs submitted for final recovery meet the statutory test(s) and are reasonable in amount and prudently incurred. The OPC takes no position on whether the utilities have met their burden of proof on this issue.

**FIPUG:** FIPUG takes no position on this issue other than that the respective utilities must meet their burden of proof at the hearing in this matter, pursuant to applicable law, to demonstrate entitlement to the monies and other relief that the utilities request in this proceeding.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** PCS agrees with the Office of Public Counsel.

**Staff Analysis:** Witness Young acknowledged that FPUC has removed certain expenses<sup>26</sup> from its request for cost recovery of the final true-up amounts for the period January 2015 through December 2015. (TR 569; EXH 89) The expenses were for work performed to restructure FPUC's Fuel schedules (A-Schedules and E-Schedules), when the respective divisions were consolidated. (TR 558; EXH 89) The appropriate fuel adjustment actual/estimated true-up amounts for the period January 2015 through December 2015 is properly reflected in the brief FPUC filed on November 13, 2015. (FPUC BR 2, 22)

Staff recommends that the appropriate fuel adjustment actual/estimated true-up amounts for the period January 2015 through December 2015 is an under-recovery of \$107,841.

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<sup>26</sup>Staff notes that the expense amount at issue is identified in Confidential Exhibit No. 89, but was subsequently disclosed in the FPUC brief on page 22 as \$4,532.

**Issue 11:** What are the appropriate total fuel adjustment true-up amounts to be collected/refunded from January 2016 to December 2016?

**Recommendation:** The appropriate total fuel adjustment true-up amounts to be collected/refunded from January 2016 through December 2016 is an under-recovery of \$1,582,148. (Barrett)

**Position of the Parties**

**FPUC:** \$1,582,148 (Under-recovery)

**OPC:** The utilities have the burden of proof to justify and support the recovery of costs and their proposal(s) seeking the Commission's adoption of policy statements (whether new or changed) or other affirmative relief sought, regardless of whether the Intervenors provide evidence to the contrary. Regardless of whether the Commission has previously approved a program or costs as meeting the Commission's requirements, the utilities must still meet their burden of demonstrating that the costs submitted for final recovery meet the statutory test(s) and are reasonable in amount and prudently incurred. The OPC takes no position on whether the utilities have met their burden of proof on this issue.

**FIPUG:** FIPUG takes no position on this issue other than that the respective utilities must meet their burden of proof at the hearing in this matter, pursuant to applicable law, to demonstrate entitlement to the monies and other relief that the utilities request in this proceeding.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** PCS agrees with the Office of Public Counsel.

**Staff Analysis:** Witness Young acknowledged that FPUC has removed certain expenses<sup>27</sup> from its request for cost recovery of 2014 and 2015 true-up amounts. (TR 569; EXHs 89, 123) The sum of the expense amounts referenced in Issues 9 and 10 is properly reflected in the brief FPUC filed on November 13, 2015. (FPUC BR 2, 22)

Staff recommends that the appropriate total fuel adjustment true-up amounts to be collected/refunded from January 2016 through December 2016 are an under-recovery of \$1,582,148.

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<sup>27</sup>The expense amount for this issue is the sum of the confidential values referenced in Issues 9 and 10, which are identified in Confidential Exhibit No. 89 and 123, but was subsequently disclosed in the FPUC brief on page 22 as \$6,578.

**Issue 12:** What are the appropriate projected total fuel and purchased power cost recovery amounts for the period January 2016 through December 2016?

**Recommendation:** The appropriate projected total fuel and purchased power cost recovery amounts for the period January 2016 through December 2016 is \$67,381,664. (Barrett)

**Position of the Parties**

**FPUC:** The appropriate projected total fuel and purchased power cost recovery amounts for the period January 2016 through December 2016 is \$67,488,997.

**OPC:** The utilities have the burden of proof to justify and support the recovery of costs and their proposal(s) seeking the Commission's adoption of policy statements (whether new or changed) or other affirmative relief sought, regardless of whether the Intervenors provide evidence to the contrary. Regardless of whether the Commission has previously approved a program or costs as meeting the Commission's requirements, the utilities must still meet their burden of demonstrating that the costs submitted for final recovery meet the statutory test(s) and are reasonable in amount and prudently incurred. The OPC takes no position on whether the utilities have met their burden of proof on this issue.

**FIPUG:** FIPUG takes no position on this issue other than that the respective utilities must meet their burden of proof at the hearing in this matter, pursuant to applicable law, to demonstrate entitlement to the monies and other relief that the utilities request in this proceeding.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** PCS agrees with the Office of Public Counsel.

**Staff Analysis:** Consistent with the recommendation for Issue 4A, the appropriate projected total fuel and purchased power cost recovery amounts for the period January 2016 through December 2016 should not include any costs associated with FPUC's interconnection line project with FPL.

Staff recommends that the appropriate projected total fuel and purchased power cost recovery amounts for the period January 2016 through December 2016 is \$67,381,664.

**Issue 19:** What are the appropriate projected net fuel and purchased power cost recovery and Generating Performance Incentive amounts to be included in the recovery factor for the period January 2016 through December 2016?

**Recommendation:** The appropriate projected net fuel and purchased power cost recovery and Generating Performance Incentive amount to be included in the recovery factor for the period January 2016 through December 2016 is 68,863,812. (Barrett)

**Position of the Parties**

**FPUC:** The appropriate projected amount to be included in the recovery factor for the period January 2016 through December 2016 is \$68,971,145, which includes prior period true-ups.

**OPC:** The utilities have the burden of proof to justify and support the recovery of costs and their proposal(s) seeking the Commission's adoption of policy statements (whether new or changed) or other affirmative relief sought, regardless of whether the Intervenors provide evidence to the contrary. Regardless of whether the Commission has previously approved a program or costs as meeting the Commission's requirements, the utilities must still meet their burden of demonstrating that the costs submitted for final recovery meet the statutory test(s) and are reasonable in amount and prudently incurred. The OPC takes no position on whether the utilities have met their burden of proof on this issue.

**FIPUG:** FIPUG takes no position on this issue other than that the respective utilities must meet their burden of proof at the hearing in this matter, pursuant to applicable law, to demonstrate entitlement to the monies and other relief that the utilities request in this proceeding.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** PCS agrees with the Office of Public Counsel.

**Staff Analysis:** Consistent with the recommendation for Issue 4A, the appropriate net fuel and purchased power cost recovery and Generating Performance Incentive amount to be included in the recovery factor for the period January 2016 through December 2016 should not include any costs associated with FPUC's interconnection line project with FPL. Witness Young acknowledged that FPUC has removed certain expenses<sup>28</sup> from its request for cost recovery of 2014 and 2015 true-up amounts. (TR 569; EXHs, 89, 123) The sum of the expense amounts referenced in Issues 9 and 10 is also properly reflected in this issue. (FPUC BR 2)

Staff recommends that the appropriate projected net fuel and purchased power cost recovery and Generating Performance Incentive amounts to be included in the recovery factor for the period January 2016 through December 2016 is \$68,863,812.

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<sup>28</sup>Issue 19 is a summary of the expense amounts from Issues 11 and 12. The Issue 11 expense amount is the sum of confidential amounts referenced in Issues 9 and 10, which are identified in Confidential Exhibit Nos. 89 and 123.

**Issue 21:** What is the appropriate levelized fuel cost recovery factor for the period January 2016 through December 2016?

**Recommendation:** The appropriate levelized fuel cost recovery factor for the period January 2016 through December 2016 is 6.675 cents per kilowatt hour. (Barrett)

**Position of the Parties**

**FPUC:** The appropriate factor is 6.692¢ per kWh.

**OPC:** The utilities have the burden of proof to justify and support the recovery of costs and their proposal(s) seeking the Commission's adoption of policy statements (whether new or changed) or other affirmative relief sought, regardless of whether the Intervenors provide evidence to the contrary. Regardless of whether the Commission has previously approved a program or costs as meeting the Commission's requirements, the utilities must still meet their burden of demonstrating that the costs submitted for final recovery meet the statutory test(s) and are reasonable in amount and prudently incurred. The OPC takes no position on whether the utilities have met their burden of proof on this issue.

**FIPUG:** FIPUG takes no position on this issue other than that the respective utilities must meet their burden of proof at the hearing in this matter, pursuant to applicable law, to demonstrate entitlement to the monies and other relief that the utilities request in this proceeding.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** PCS agrees with the Office of Public Counsel.

**Staff Analysis:** Based on adjustments made in Issue 19, staff recommends that the appropriate levelized fuel cost recovery factor for the period January 2016 through December 2016 is 6.675 cents per kilowatt hour.

**Issue 23:** What are the appropriate fuel cost recovery factors for each rate class/delivery voltage level class adjusted for line losses?

**Recommendation:** The appropriate fuel cost recovery factors for each rate class/delivery voltage level class adjusted for line losses are shown below in Tables 23-1 and 23-2. (Draper, Barrett, Lester)

**Position of the Parties**

**FPUC:** The appropriate levelized fuel adjustment and purchased power cost recovery factors for the period January 2016 through December 2016 are as follows:

<i>Rate Schedule</i>	<i>Adjustment</i>
RS	\$0.10619
GS	\$0.10169
GSD	\$0.09709
GSLD	\$0.09407
LS	\$0.07211
Step rate for RS	
RS Sales	\$0.10619
RS with less than 1,000 kWh/month	\$0.10188
RS with more than 1,000 kWh/month	\$0.11438

The appropriate adjusted Time of Use (TOU) and Interruptible rates for the Northwest Division are:

*Time of Use/Interruptible*

Rate Schedule	Adjustment On Peak	Adjustment Off Peak
RS	\$0.18588	\$0.06288
GS	\$0.14169	\$0.05169
GSD	\$0.13709	\$0.06459
GSLD	\$0.15407	\$0.06407
Interruptible	\$0.07907	\$0.09404

**OPC:** No position.

**FIPUG:** No position.

**FRF:** Adopts the position of OPC.

**PCS Phosphate:** The loss of DEF's nuclear generation and reductions in its coal-fired generation will lead to a shrinking differential between peak and off-peak fuel rates that is inconsistent with the core statutory objectives set forth in FEECA, Section 366.81, F.S. The Commission should direct DEF to address this concern in its next fuel filing.



**Staff Analysis:** In its brief PCS provided a position for Issue 23 with regard to DEF, not FPUC. PCS does not purchase any power from FPUC and did not take a position with regard to FPUC in its prehearing statement filed on October 9, 2015. Further, the fuel cost recovery factors for each rate class/delivery voltage level class for FPL, DEF, TECO and Gulf were part of the stipulations contained in the Notice of Stipulations filed on October 31, 2015, approved by the Commission by bench decision at the beginning of the final hearing on November 2, 2015. (Prehearing TR 11-13) PCS made no objection to the motion to approve the stipulation on Issue 23 with regard to DEF at that time. Since Issue 23 has been stipulated with regard to DEF, staff considers DEF's fuel cost recovery factors to be a moot issue.

For FPUC, staff recommends that the appropriate fuel cost recovery factors for each rate class/delivery voltage level class adjusted for line losses are shown in Tables 23-1 and 23-2. These factors reflect staff's recommendations for Issues 4A and 4B.

**Table 23-1  
 2016 Fuel Cost Recovery Factors for FPUC**

<b>Rate Schedule</b>	<b>Levelized Adjustment</b>
RS	\$0.10602
GS	\$0.10152
GSD	\$0.09692
GSLD	\$0.09390
LS	\$0.07194
<b>Step rate for RS</b>	
RS Sales	\$0.10602
RS with less than 1,000 kWh/month	\$0.10171
RS with more than 1,000 kWh/month	\$0.11421

Consistent with the fuel projections for the 2016 period, the appropriate adjusted Time of Use (TOU) and Interruptible rates for the Northwest Division for 2016 period are shown in Table 23-2 below.

**Table 23-2  
 2016 Fuel Cost Recovery Factors for FPUC**

<b>Rate Schedule for Time of Use/Interruptible</b>	<b>Levelized Adjustment On Peak</b>	<b>Levelized Adjustment Off Peak</b>
RS	\$0.18571	\$0.06271
GS	\$0.14152	\$0.05152
GSD	\$0.13692	\$0.06442
GSLD	\$0.15390	\$0.06390
Interruptible	\$0.07890	\$0.09390

**Issue 37:** Should this docket be closed?

**Recommendation:** No. The Fuel and Purchased Power Cost Recovery Clause is an on-going docket and should remain open. (Brownless)

**Staff Analysis:** On October 30, 2015, a Notice Of Stipulations was filed acknowledging that stipulations were entered between the parties to this docket, subject to Commission approval. This issue (Issue 37) was among several issues identified in that document. On November 2, 2015, the Commission approved the stipulations identified in the Notice of Stipulation. (TR 11-13)

The Fuel and Purchased Power Cost Recovery Clause is an on-going docket and should remain open.