BEFORE THE FLORIDA PUBLIC SERVICE COMMISSION

In re: Petition for expedited approval of an agreement to purchase the Tiger Bay cogeneration facility and terminate related purchased power contracts by Florida Power Corporation.

Docket No.: 970096-EQ

Filing Date: March 21, 1997

PREHEARING STATEMENT OF FLORIDA POWER CORPORATION

Florida Power Corporation ("FPC"), pursuant to Rule 25-22.038, Florida Administrative Code, hereby submits its Prehearing Statement.

A. WITNESSES

Witness	Subject Matter	Issues
Direct		
Robert D. Dolan	Description of the purchase transaction and its principal terms, the context giving rise to the transaction, and discussion of the expected benefits resulting from the purchase	1,2,3,4,5,6, 10,12,13,14, 15;19,23,24, 25 and 26
John Scardino, Jr.	Description of the proposed accounting and ratemaking treatment associated with the transaction	6,7,8,9,10, 11,12,13,16, 17,18,20,21, 22 and 23
Rebuttal		
Robert D. Dolan	Rebuttal of FIPUG witness Falkenberg; Rebuttal of Vastar witness Catasein	As above
John Scardino, Jr.	Rebuttal of FIPUG witness Falkenberg	As above

T#523028.1

C. EXHIBITS

Exhibits	Witness	Description
Direct		
_______ (RDD-1)	Robert D. Dolan	House Bill No. 338 "Ratepayer Protection Act"
_______ (RDD-2)	Robert D. Dolan	Excerpts from Relevant FERC Decisions
_______ (RDD-3)	Robert D. Dolan	Customer's QF Costs vs. Current Estimated Avoided Costs
_______ (RDD-4)	Robert D. Dolan	Savings Due to Purchase of Tiger Bay
_______ (RDD-5)	Robert D. Dolan	Impact of Tiger Bay Purchase on Customers
_______ (JS-1)	John Scardino, Jr.	Savings due to the Purchase of Tiger Bay Scenario #3 - Proposed Methodology for Cost Recovery
_______ (JS-2)	John Scardino, Jr.	Florida Power Corporation Fuel and Purchase Power Cost Recovery Clause Capacity-to-Energy Recovery Ratios for Tiger Bay Contract Versus Purchase
_______ (JS-3)	John Scardino, Jr.	Florida Power Corporation Estimated Allocation of Purchase Price of Tiger Bay Limited Partnership
_______ (JS-4)	John Scardino, Jr.	Florida Power Corporation Acquisition of Tiger Bay (In Thousands)
_______ (JS-5)	John Scardino, Jr.	Florida Power Corporation Proforma of Impact of Tiger Bay Transaction (In Thousands)

Rebuttal

None

C. STATEMENT OF BASIC POSITION

In its direct testimony, FPC has explained the unique circumstances giving rise to FPC's opportunity to terminate the Tiger Bay contracts and purchase the facility. FPC's testimony also clearly establishes that, absent this transaction, the collection of five Tiger Bay contracts will continue as one of the most expensive sources of capacity and energy serving FPC's ratepayers, to their substantial disadvantage. No party has introduced any evidence to suggest that the purchase of Tiger Bay will not, in total, produce substantial savings to ratepayers, or to contest FPC's assertion that the savings will begin to be realized within five years of the transaction's close. Indeed, even FIPUG acknowledges that a buyout is economical if "the cost of the buy out (and replacement power and energy) is lower in present value terms than the remaining contract prices." This is precisely the case with respect to this buyout, as demonstrated in FPC's direct testimony. Thus, it is uncontested that, in total, the ratepayers will pay considerably more if this purchase is rejected than if it is approved. Similarly uncontested is FPC's estimate that the total amount that ratepayers will save through this transaction is $1.9 to $2.4 billion, or $203 to $388 million on an NPV basis.

The only real challenge to this transaction from FIPUG relates to the timing and mechanisms by which FPC seeks authorization to recover the purchase costs. FPC has demonstrated that a five year recovery of the purchase cost through the Capacity Cost Recovery clause is appropriate, with FPC recovering the Vastar contract's natural gas fuel costs through the Fuel Adjustment Clause. The five year period strikes a reasonable balance between preserving the savings for ratepayers (which would be delayed through a longer recovery period), avoiding a short-term but substantial rate increase (which might be required with a shorter recovery period), and avoiding placing an unfair burden on FPC's shareholders by requiring them to support the buydown financing through a longer recovery period. The fairness of the five-year period is especially evident when one considers that FPC's shareholders will not recognize one penny of the savings achieved, and, indeed, will absorb significant additional operating and other costs over the foreseeable future. Moreover, giving FPC some flexibility in the manner in which it recovers these costs within the five year period, as FPC has requested, will help FPC further mitigate the ratepayer effects.

FIPUG's suggestion of a longer recovery period is a blatant attempt to impose a deal on FPC to which it has never agreed, and to which FPC would not agree because of the substantial additional burdens and risk it would impose on FPC's shareholders, and because the associated effects on FPC's credit ratings could ultimately work to the detriment of its ratepayers. The bottom line is that the cogeneration contracts and their associated costs have already been found prudent by this Commission. In turn, the burden of them currently falls, and will continue to fall, squarely on FPC's ratepayers. As a result, it is fair for those same ratepayers, rather than FPC's shareholders, to absorb the costs of this transaction, and to reap the associated benefits.

As to the mechanisms for recovery, FPC has demonstrated that recovery of the purchase price through the CCR and recovery of the gas contract costs through the FAC appropriately apportions those costs. The savings which this transaction will produce in the future are in capacity related costs; thus, it is appropriate to recover the purchase price through the CCR. While this will produce a slight shift in the ratio of capacity and energy related costs associated with the contract (because of the higher fuel costs that FPC must inherit as part of the deal permitting the much greater capacity savings), this shift is modest and consistent with Commission precedent. Moreover, the only logical means of avoiding such a shift in the ratio would be to permit FPC to recover a portion of the fuel related costs of the Facility through the CCR.

There is no reason for the Commission to delay approval based on the testimony put forward by Vastar Marketing. FPC has made clear that it intends to satisfy all material terms of the gas contract. Indeed, FPC's substitution as purchaser leaves Vastar in a better position than it previously enjoyed. After FPC assumes the contract obligations, Vastar will be able to look directly to FPC for payment and performance. Conversely, while contracting with Tiger Bay, Vastar's primary recourse and security was the revenue stream provided by FPC's payments under the contract. Vastar has intervened in the simple hope that, by disrupting and delaying the proceeding, it can negotiate concessions and terms to which it has no current contractual right. Obviously, any such concessions or terms will effectively come at the expense of FPC's ratepayers and should not be countenanced.

D. STATEMENT OF ISSUES AND POSITIONS

FPC believes that the issues can be broken down into five major categories as follows.

A. Benefits of Terminating the Tiger Bay Contracts and Purchasing the Facility:

Issues 1, 2, 3, 4, 6, 12 and 13, as set forth below.

B. Accounting Matters:

Issues 7, 8, 9, 10, and 11, as set forth below.

C. On-Going Fuel Cost Recovery:

Issues 5, 14, and 15, as set forth below.

D. Method for Recovery and Amortization of Purchase Price

Issues 16, 17, 18, 19, 20, 21, and 22, as set forth below.

E. Miscellaneous

Issues 23, 24, 25, and 26, as set forth below.

ISSUE 1: Has Florida Power Corporation provided adequate assurances regarding the operational reliability of the Tiger Bay facility?

FPC: Yes. FPC's and Tiger Bay's testimony establishes that the facility can be expected to be operationally reliable. It uses desirable technology, has had an excellent performance history, and fits well with the remainder of FPC's generating fleet, allowing FPC to draw on its already developed expertise to continue operating and even improve the facility's performance. In addition, FPC's answers to Staff's Interrogatory Numbers 27 through 31, 33 and 34 provide further support for FPC's position on this issue.

ISSUE 2: Has Florida Power Corporation provided adequate assurances regarding the financial viability of the Tiger Bay generating facility?

FPC: Yes. FPC has demonstrated that it has undertaken due diligence to evaluate the facility's viability and that such due diligence indicates the project is profitable and capable of satisfying the terms of the PPAs. Tiger Bay's testimony also supports this position. The facility's technical characteristics, ownership structure, revenue streams under the PPAs and the facility's financial obligations, including its gas contract, have been described. Based on those descriptions, there is no reason to believe the facility is not financially viable and no party has maintained to the contrary. FIPUG's expert has agreed that the facility should be able to meet its obligations.

ISSUE 3: Are Florida Power Corporation's projections of non-fuel operating expenses reasonable?

FPC: Yes. FPC's projected non-fuel operating expenses are reasonable. FPC has provided an estimate of these costs, and they are reflected in its computations of expected customer savings. The relatively modest amount of these expenses is explained by the facts that the facility has desirable technology, fits well with FPC's current generating fleet, and is located close to FPC's new Polk site, allowing for efficiencies between the two. Moreover, FPC will be absorbing all such costs in its base rates for the foreseeable future, minimizing the impact of any deviations in such projections.

ISSUE 4: Has Florida Power Corporation provided adequate assurances that sufficient natural gas pipeline capacity will be available to transport natural gas to the Tiger Bay facility?

FPC: Yes. The facility's performance to date indicates that the facility has sufficient gas transportation to ensure its operation at a very high level of reliability. Moreover, FPC will assume all obligations of the plant. Thus, it will inherit both the obligation to purchase transportation, and the right to claim such transportation, that the facility currently enjoys. Lenders have provided substantial financing for the facility, indicating that third parties also have confidence that the natural gas arrangements supporting the facility are sufficient to ensure its operation. Finally, FPC's new Polk plants will be served by natural gas, providing FPC additional flexibility in transporting gas to serve the Tiger Bay facility.

FPC's answers to Staff's Interrogatory Numbers 21 and 22 provide further support for FPC's position on this issue.

ISSUE 5: Is Florida Power Corporation's fuel price forecast reasonable?

FPC: Yes. FPC has used the same fuel forecast that it uses in connection with its regular business planning activities. FPC's answers to Staff's Interrogatory Number 25 provides further support for FPC's position on this issue.

ISSUE 6: Are Florida Power Corporation's financial assumptions reasonable?

FPC: Yes. FPC has used reasonable and conservative financial assumptions.

ISSUE 7: What is the appropriate annual accrual amount for the provision of final dismantlement of the Tiger Bay Facility?

FPC: The estimated catch-up fossil dismantlement accrual for 1995 and 1996 is $241,000 and $253,000 respectively. The estimated 1997 fossil dismantlement accrual for the Tiger Bay facility is $266,000. FPC's answers to Staff's Interrogatory Numbers 4 and 5 provide further support for FPC's answer on this issue.

ISSUE 8: What is the appropriate remaining life, net salvage, reserve and resultant depreciation rate for the Tiger Bay Facility?

FPC: Florida Power Corporation proposes an average service life of 20 years, an average remaining life of 18 years, net salvage rate of negative 10 percent, and a depreciation rate of 5.5%. FPC's answers to Staff's Interrogatory Numbers 1,2 and 3 provide further support for FPC's answer on this issue.

ISSUE 9: Are the purchase power agreement termination payments properly classified as an acquisition adjustment?

FPC: No. Upon subsequent review, Florida Power has determined that the proper FERC account is 182.3 "Other Regulatory Assets." FPC's answer to Staff's Interrogatory Number 14 provides further support for FPC's answer on this issue.

ISSUE 10: Is there an acquisition adjustment associated with the purchase of the plant facilities?

FPC: No. Florida Power is purchasing the plant facilities at the estimated net book value of $75.9 million based on our original cost analysis. FPC's answers to Staff's Interrogatory Numbers 2, 8, and 14 provide further support for FPC's answer on this issue.

ISSUE 11: Should FPC be required to perform an original cost study for the Tiger Bay generating plant to determine the appropriate amount of investment and reserve to include in Account 101?

FPC: No. However, in response to Staff's interrogatories, Florida Power voluntarily conducted an original cost analysis by obtaining an EPC (engineer, procure and construct) budget estimate for a similar type of facility from Black & Veatch and indexing these costs to the year of construction using an appropriate Handy-Whitman construction cost index. FPC's answer to Staff's

Interrogatory Number 8 provides further support for FPC's answer on this issue.

ISSUE 12:
FIPUG: Is Florida Power Corporation's proposal to purchase the Tiger Bay facility and terminate the related power purchase agreements prudent?

FPC: FPC's proposal is prudent, as it will provide substantial benefit to FPC's ratepayers as compared to maintaining the contract obligations as currently structured and approved. FPC notes that it does not believe this is a proper issue in the context of this proceeding. It attempts to apply issue analysis traditionally applied to the construction of new generation to a transaction that does not involve FPC constructing a new generation resource, but which rather is being undertaken to mitigate the costs to ratepayers of purchased power contracts that have already been found prudent by this Commission and the costs of which are therefore eligible for full cost recovery, even if uneconomic compared to current new generation.

ISSUE 13: Should the Commission approve the purchase agreement for Florida Power Corporation to purchase the Tiger Bay facility and terminate the related power purchase agreements?

FPC: Yes. The agreement will provide ratepayers substantial savings over time compared to the costs those ratepayers would incur under the current purchase power agreements. Thus, this transaction is a reasonable way in which to mitigate the effects of the high cost purchase power agreements previously entered into by FPC with Commission approval. The associated cost recovery terms in the acquisition agreement, providing that the Commission must approve a five year recovery period in order for the deal to close, are reasonably balanced to avoid undue short-term impact on ratepayers while ensuring the maximum possible total benefit to ratepayers without placing an unfair burden on FPC's shareholders.

In light of FPC's commitment to assume the gas contract obligations under Tiger Bay's current supply contract, the transaction will have no meaningful effect on Vastar Gas Marketing and therefore there is no reason to delay approval. Such delay can only work to the detriment of FPC's ratepayers by providing Vastar leverage by which it can threaten to disrupt the entire transaction and thereby demand concessions and accommodations to which it has no legal entitlement.

ISSUE 14: Should the Commission approve recovery of the fuel costs associated with the Vastar natural gas supply contract through the Fuel and Purchased Power Cost Recovery Clause?

FPC: Yes. FPC's willingness to undertake this transaction depends on it receiving advance approval to recover the Vastar fuel costs it would assume under the transaction. Tiger Bay is only willing to undertake the transaction if FPC assumes Tiger Bay's gas obligations, thus relieving it of "take" obligations that for which it would have no use without a facility to burn the gas. Thus, FPC's assumption of the Tiger Bay's gas obligations is essential to the transaction. The Fuel and Purchased Power Recovery Clause is the appropriate recovery mechanism as recovery in this manner is consistent with Commission precedent. It distributes the fuel costs and capacity costs associated with this transaction in a manner that, to the greatest degree possible while remaining consistent with Commission precedent, maintains the ratio of fuel costs and capacity costs that would be experienced if the contracts were not terminated and the contract costs instead continued to be passed through to ratepayers. FPC's answer to Staff's Interrogatory Number 24 provides further support for FPC's answer on this issue.

ISSUE 15: Should the Commission approve recovery of the natural gas transportation costs associated with the Tiger Bay Facility through the Fuel and Purchased Power Cost Recovery Clause?

FPC: Yes. FPC's willingness to undertake this transaction depends on it receiving advance approval to recover the fuel transportation costs it would assume under the transaction. Tiger Bay is only willing to undertake the transaction if FPC assumes Tiger Bay's gas obligations, thus relieving it of "take" obligations for which it would have no use without a facility to burn the gas. Thus, FPC's assumption of the Tiger Bay's gas obligations is essential to the transaction. The Fuel and Purchased Power Recovery Clause is the appropriate recovery mechanism as recovery in this manner is consistent with Commission precedent. It distributes the fuel costs and capacity costs associated with this transaction in a manner that, to the greatest degree possible while remaining consistent with Commission precedent, maintains the ratio of fuel costs and capacity costs that would be experienced if the contracts were not terminated and the contract costs instead continued to be passed through to ratepayers.

ISSUE 16: What is the appropriate method for recovering the cost of the Tiger Bay generating facility?

FPC: As an integrated transaction, all costs should be recovered using the same method. Because the benefits to be achieved are 100% capacity related, the appropriate method of recovery is through the Capacity Cost Recovery Clause.

ISSUE 17: What is the appropriate method for recovering the cost of the power purchase agreements?

FPC: As an integrated transaction, all costs should be recovered using the same method. Because the benefits to be achieved are 100% capacity related, the appropriate method of recovery is through the Capacity Cost Recovery Clause.

ISSUE 18: What is the appropriate method of recovering the cost of the Materials and Supply Inventory?

FPC: As an integrated transaction, all costs should be recovered using the same method. Because the benefits to be achieved are 100% capacity related, the appropriate method of recovery is through the Capacity Cost Recovery Clause. FPC's answer to Staff's Interrogatory Number 24 provides further support for FPC's answer on this issue.

ISSUE 19: Should the revenue from the steam sales agreement be credited through the Fuel and Purchased Power Recovery Clause?

FPC: Yes. FPC accounts for steam sales revenues from its existing University of Florida cogeneration plant through use of a credit to the Fuel Adjustment Clause. The same procedure should be used here. FPC's answer to Staff's Interrogatory Number 35 provides further support for FPC's answer on this issue.

ISSUE 20: What is the appropriate amortization period for recovering the cost of the Tiger Bay generating facility?

FPC: Since the costs of the Tiger Bay generating facility is part of a single integrated transaction undertaken for the benefit of the customer, the Company should be allowed to recover the costs over 5 years. A five year recovery period represents a reasonable balancing of the timing of costs versus the recognition of benefits resulting from this transaction (which would be delayed through a longer recovery period), avoids a short-term but substantial rate increase (which might be required with a shorter recovery period), and avoids placing an unfair burden on FPC's shareholders by requiring them to support the buydown financing through a longer recovery period. The fairness of the five-year period is especially evident when one considers that FPC's shareholders will not recognize one penny of the savings achieved, and, indeed, will absorb significant additional operating and other costs over the foreseeable future.

ISSUE 21: What is the appropriate amortization period for recovering the cost of terminating the power purchase agreement?

FPC: Since the costs of terminating the power purchase agreements are part of a single integrated transaction undertaken for the benefit of the customer, the Company should be allowed to recover the costs over 5 years. As noted in response to Issue 21 above, a five year recovery period represents a reasonable balancing of the timing of costs versus the recognition of the benefits resulting form this transaction.

ISSUE 22:
FPC: Should Florida Power be granted the latitude to manage the collection of the purchase price over the amortization period?

FPC: Yes. This latitude may take the form of a non-levelized recovery of the purchase cost using a "constant purchasing power" methodology similar to that authorized by the Commission for fossil plant dismantlement cost recovery, and/or deferring the commencement of the five-year recovery period to April or October 1998. The sole purpose of this latitude would be to stabilize the total rate charged to customers to the extent that recovery of the Tiger Bay purchase cost may interact with other changes in Florida Power rates.

ISSUE 23:
FIPUG: Will the contract buyout and plant purchase cause rate shock?

FPC FPC does not believe that this is a proper issue in the context of this proceeding. However, assuming this is a proper issue, FPC believes that if the costs of the buyout are recovered as Florida Power has proposed no so-called "rate shock" will occur. The five year recovery period FPC has proposed fairly spreads the cost of the transaction to minimize the rate effects while also maintaining a reasonable balancing of the timing of costs versus the recognition of the benefits resulting from this transaction. Moreover, granting FPC latitude in the precise timing of the recovery would further permit FPC to stabilize the total rate charged to customers to the extent that recovery of the Tiger Bay purchase cost may interact with other changes in Florida Power rates.

ISSUE 24:
FIPUG: Will the proposal impact economic development within Florida Power Corporation's service territory?

FPC: FPC does not believe that this is a proper issue in the context of this proceeding. However, assuming this is a proper issue, FPC believes that this transaction will benefit economic development in its service territory by leading to overall savings to ratepayers compared to what they would pay if the contracts were maintained.

ISSUE 25:
FIPUG: What impact will this proposal have on competition in the electric industry?

FPC: FPC does not believe that this is a proper issue in the context of this proceeding. However, assuming this is a proper issue, the effects of this transaction are likely to be procompetitive by producing lower rates for ratepayers, which is the ultimate goal of competition.

ISSUE 26:
VASTAR: Whether it is premature for the Florida Public Service Commission (the "Commission") to consider the Petition filed by Florida Power Corporation ("FPC") until Tiger Bay Limited Partnership ("TBLP") has obtained VGM's consents as required by the terms of TBLP's Gas Sales and Purchase Contract with VGM (the "Gas Sales Contract")?

FPC: FPC does not believe that this is a proper issue in the context of this proceeding. However, assuming this is a proper issue, there is no reason for the Commission to defer consideration of this transaction while awaiting Vastar's consent. Such an approach would threaten to destroy the transaction to the detriment of FPC's ratepayers and would allow Vastar to hold the transaction hostage, in an attempt to extract undeserved benefits at the expense of FPC's ratepayers.

ISSUE 27: Should this docket be closed?

FPC: Yes.

E. STIPULATED ISSUES

None at this time.

F. PENDING MOTIONS

Vastar's motion to intervene.

FPC's several motions seeking confidential treatment of certain documents.

G. REQUIREMENTS THAT CANNOT BE COMPLIED WITH

None.

H. OTHER MATTERS

None.

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CERTIFICATE OF SERVICE
Docket No.: 970096-EQ

I HEREBY CERTIFY that a true and correct copy of the foregoing has been communicated via fax and sent by regular U.S. mail to the following individuals on March 13, 1997:

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